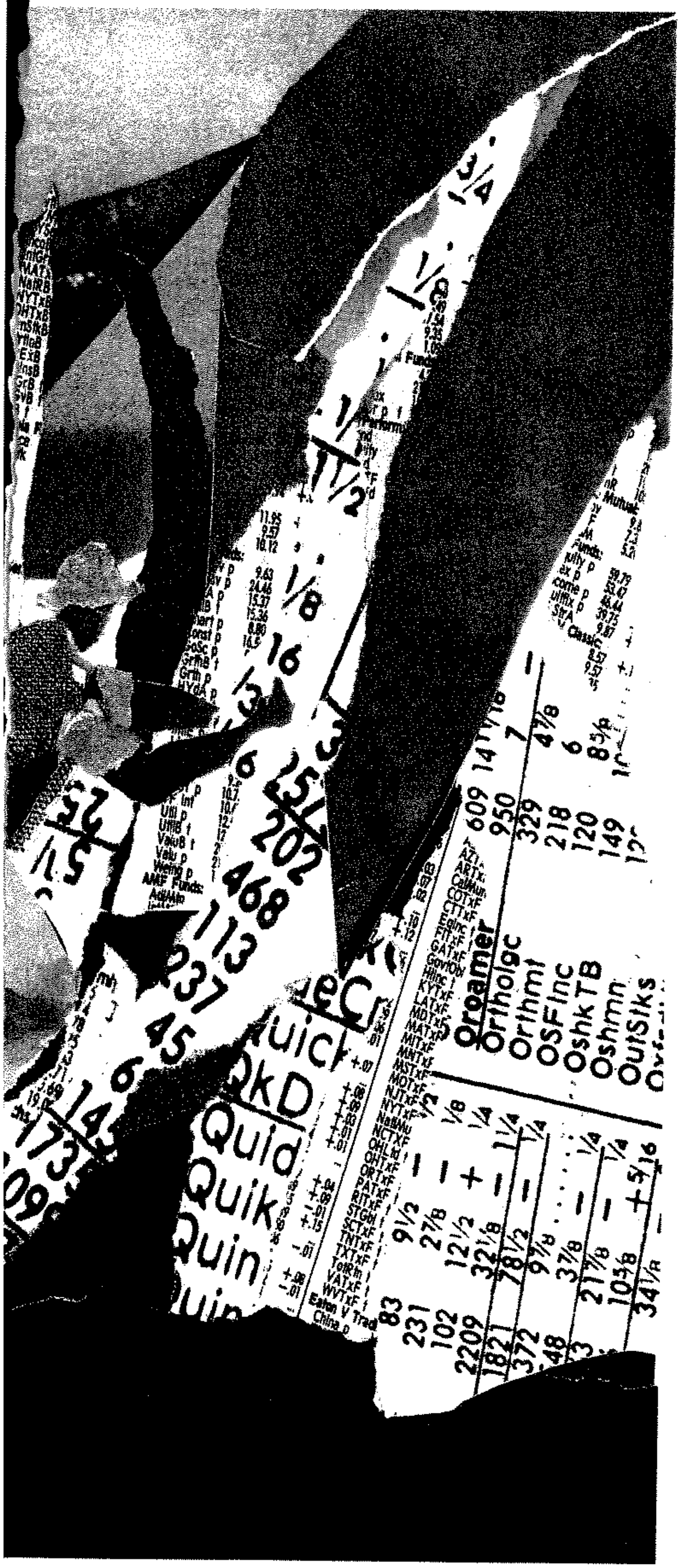


VALUE

HUNTING

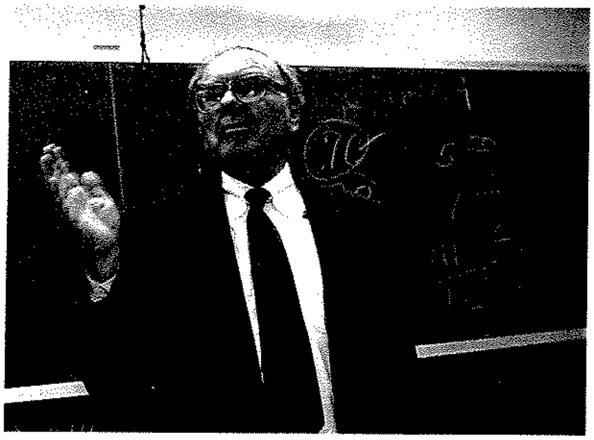
COLUMBIA STUDENTS BET ON UGLY DUCKLINGS

Students at Columbia Business School are learning about the increasingly popular investment strategy of "value investing" from masters of the discipline. Developed by Benjamin Graham and David Dodd in 1934, value investing is the art of finding stocks priced far below their true worth in the market.

Last fall, throngs of would-be investment titans rushed to take "The Fundamentals of Investing: Approaches to Value," an advanced seminar co-taught by Bruce Greenwald, Robert Heilbrunn Professor of Asset Management and Finance, and Roger Murray, S. Sloan Colt Professor Emeritus of Banking and International Finance. The class was in such high demand that 400 students vied for 75 spaces that were selected by lottery.

BY BEVERLY NORMAN-COOPER (MBA '94)

Those lucky enough to snag one of the prized seats spent the first four weeks tackling the basics of value investing: accounting, balance sheet analysis and how to value an asset. The final project for the course? Uncover an unloved and undervalued stock.



Warren Buffett (MS '51), chairman and CEO, Berkshire Hathaway, teaching at Columbia Business School.

Budding money mavens didn't have to rely on academic textbooks to understand how value investors generate market-beating returns. Instead, they listened to firsthand accounts from eight of value investing's most celebrated disciples. Guest lecturers included market wizards Warren Buffett (MS '51), chairman and CEO, Berkshire Hathaway; Chuck Royce (MBA '63), president, The Royce Funds; Mario Gabelli (MBA '67), chairman, Gabelli Funds, Inc.; and Robert Bruce (MBA '70), managing partner of Alpine Capital, a private partnership.

"It could only take place at Columbia Business School. Classroom speakers such as Buffett, Royce and Price are making the course a showpiece the world over."

—Professor Meyer Feldberg (MBA '65)
Dean, Columbia Business School

Also part of the star-studded line-up were bargain hunters Michael Price of Mutual Series Fund, Inc.; Walter Schloss, who heads Walter & Edwin Schloss Associates; Seth Klarman of The Baupost Group; and Boston University economist-cum-investor Andrew Weiss. The course, which is offered for the second time this semester, was masterminded by Greenwald and Murray, who was one of the inventors of the Individual Retirement Account.

It's only natural, says Dean Meyer Feldberg, that Columbia lead the charge to put value investing back at the top of the finance curriculum. "The course builds on a long and glorious tradition, beginning with Graham and Dodd," he says. "It could only take place at Columbia Business School. Classroom speakers such as Buffett, Royce and Price are making the course a showpiece the world over."

These words are music to Mario Gabelli's ears. He runs a successful multibillion dollar empire in private accounts, mutual funds and hedge funds. Two years ago, he financed a series of lectures by Roger Murray and hosted about 250 business people. Greenwald attended one of the seminars, hooked up with Murray, and the two began to design the value investing seminar for the School. "I guess I can claim an assist," says Gabelli.

"We wanted to teach students financial management principles that applied to the real world," says Greenwald, "and we wanted to use real world practitioners who had a demonstrable success rate over a period of time. We compiled a list of people we wanted to speak. Nobody we asked turned us down."

SAVVY INVESTORS LOOK FOR WALLFLOWER SECURITIES

Columbia Business School is uniquely qualified to teach the investment course, says Greenwald, because it has an "historical connection" to value investing. To understand why this is no idle boast, a little history comes in handy.

In 1934, the late Benjamin Graham and David L. Dodd — both Columbia Business School professors — set out the precepts of value investing in their classic primer *Security Analysis*. Now in its fifth edition, the book is still considered adillac of investment guides by e patient flock who follow the Graham and Dodd model.

No doubt, the book's slightly ponderous prose can be daunting. But strip away the technical jargon and it comes down to this: forget about trying to predict the gyrations of the stock market. Instead, savvy investors should ferret out ugly duckling companies destined to become swans — companies with rising cash flow, hidden assets or a stock price hammered by a temporary earnings hiccup. Once they find these wallflower securities, they should hold them until their intrinsic value is recognized by the market.

Graham became enshrined in the annals of business lore in 1948 when his Wall Street investment firm bet a quarter of its capital on a little-known outfit called Government Employees Insurance Company. GEICO's shares surged a stratospheric 1,645 percent over the next eight years. The iconoclastic professor-investor later published *The Intelligent Investor,* a far less technical version of the earlier investment book.

When Graham retired from academe in 1956, he tapped banker and stock analyst Roger Murray to be his successor. (Graham died in 1976; David Dodd, who, along with Graham, wrote the classic text on security analysis, died in 1988.)

THE GURU OF VALUE INVESTING TAKES LONG VIEW

Money magazine once called Murray one of the "grand old men of value investing." As a long-time follower of the Graham and Dodd

Roger Murray and Robert Heilbrunn

model, Murray, 82, considers these words a compliment.

"Through the years, we've been through every conceivable kind of market," he says. "Yet, value investing remains a fruitful, useful and productive discipline."

Murray should know. After graduating from Yale in 1932, he joined Bankers Trust, where he managed money and analyzed stock for 24 years. In his 20 years at Columbia Business School, Murray preached the gospel of security analysis to famed investor Mario Gabelli and hundreds of other Wall Street investment moguls.

Murray can also claim credit for helping create the Individual Retirement Account. Hoping to spur saving by people who didn't have a pension plan, he proposed the IRA concept to Congress in 1971, three years before it became law.

In 1987, he scored another big hit as the co-author of the fifth edition of the Graham and Dodd work. "In the book, we said that stocks were grossly overvalued," he says. "The book came out in the fall of 1987; the stock market correction happened in October 1987. Do I think value investing will last as a discipline? Sure. It will hold in the future just as it held in the first edition of the book in 1934."

INVESTMENT TIPS AND OTHER WORDS OF WISDOM FROM TOP MONEY MAVENS

Warren Buffett (MS '51), Chairman and CEO, Berkshire Hathaway

"Take one industry at a time and develop some expertise on [it]."

Walter Schloss, President, Walter & Edwin Schloss Associates

"Do what's comfortable for you. If you feel you're competent in one area, concentrate in that area."

Seth Klarman, President, The Baupost Group

"Only join an organization you'll feel proud to work for. If you're involved with good people, people who are honest and who treat you well, you'll do fine. But if you're involved with people who don't care about you, you'll be sure to fail."

Mario Gabelli (MBA '67) Chairman, Gabelli Funds, Inc.

"I hire people who are Ph.D.s — poor, hungry and driven."

Chuck Royce (MBA '63) President, The Royce Funds

"A successful value investor has to have integrity, patience and discipline. If you have all these, then the investment business can be the most dynamic business on the face of the earth."

Michael Price President, Mutual Series Fund, Inc.

"I'd rather have a hungry 'C' student than an 'A' student who is arrogant."

Andrew Weiss Professor of Economics, Boston University

"Value investing is just standard economics. Think logically about what you're doing. Think about it without emotion. And think about what makes sense."

Robert Bruce (MBA '70) Managing Partner, Alpine Capital

"Early on, you should try to work with the most remarkable person you can find, even if the pay isn't as great. You can always make money, but you can't always find someone you can learn from."

ROBERT HEILBRUNN: A VALUE INVESTING ORIGINAL

Robert Heilbrunn readily admits that he was your typical teenager. So, when his father first mentioned Ben Graham, Heilbrunn, 17 and on break from the New York Military Academy, paid scant attention. "My father casually mentioned that he had met a sharp young stockbroker," says the Brooklyn-born value investor, who is now 85. "He was quite impressed with Ben and felt that one day Ben would be quite rich. But at that age, I had lots of other things on my mind and really didn't listen very well."

Robert Heilbrunn (center) celebrates his 85th birthday with Dean Meyer Feldberg (MBA '65) and students from "The Fundamentals of Investing: Approaches to Value" seminar.

Jump ahead several decades. In 1988, in honor of Robert Heilbrunn on his 80th birthday, the Heilbrunn family makes a gift of $1.5 million to Columbia Business School to finance the Robert Heilbrunn Professorship of Asset Management and Finance. In 1993, on the occasion of his 85th birthday, Heilbrunn gives another $1 million to the School for fellowships and scholarships for students interested in the field of security analysis pioneered by Graham.

What explains the epiphany? "In 1929, just a week before the great stock market crash, my father died," Heilbrunn explains. "Suddenly, I had to pay more attention." Just 21 years old, he knew nothing about business, having completed only one year of undergraduate studies.

Taking over the reins of his father's struggling leather business, he was forced to liquidate it over the next two years. He also assumed responsibility for the family's modest portfolio. "I didn't know anything about stocks and a lot of brokers were coming to see me," he recalls.

He remembered his father's remarks about Graham and talked Graham into managing the small portfolio. Says Heilbrunn: "When I first telephoned him, he was unfriendly. I believe he thought I was going to ask him for a loan. But he agreed to manage the portfolio and charged me $25 a month. This was less than a dollar a day. It just goes to show you how bad things were."

Later, when Graham began teaching about security analysis at Columbia Business School, Heilbrunn enrolled in the class. He also worked for Graham, doing special research. The two became close friends as well as business associates. "He was at our wedding in 1934. He was a brilliant man," Heilbrunn recalls.

Heilbrunn seems pleased about the renaissance of interest in value investing. "The long-term method of investing is still the best," he says. "I think people are better off buying good stocks and staying with them."

He also has kudos for Bruce Greenwald, the Robert Heilbrunn Professor of Asset Management and Finance, who teaches the value investing class. "I'm quite impressed with Greenwald," Heilbrunn says. "The program he developed has generated a great deal of interest."

Heilbrunn is optimistic about the future of value investing. "Value investing is a wonderful field to be in," he says. "The opportunity for making money in this business is probably greater than in any other business. My family and I gave the money because we felt we owed it to the School, to Ben Graham and to the future. I hope that 50 years from now, some of the students will become very successful and establish more fellowships so we can keep the value investing legacy alive."

During the 1970s and 1980s, the Graham and Dodd tradition began to fall from favor. Enter value investor Robert Heilbrunn, whose family has generously supported the Business School since 1988. "I want to see a renaissance of interest in the subject," admits the 85-year-old investor.

THE LECTURERS: RICH, FAMOUS — AND NERVOUS

Without a doubt, one of the most famous value investors à la Ben Graham is Buffett, who got an A+ from Graham at the School in 1951 and later wrangled a job at Graham's firm. In 1965, Buffett bought Berkshire Hathaway, a sleepy New Bedford, MA, textile manufacturer with $10 million in assets. The company's stock was a steal at $12 a share, especially since its book value topped $19 a share. Following the Graham and Dodd approach, Buffett transformed this old-line company into a diversified holding company and financial juggernaut.

Today, Berkshire Hathaway is the highest-priced stock on the New York Stock Exchange. Buffett's share of that empire — which includes holdings in Coca-Cola, Salomon Brothers and American Express — has jumped to a value of $8.3 billion. Last year, *Forbes* ranked Buffett the richest man in America.

Instead of admission tickets, students in Greenwald's seminar course donned specially printed T-shirts to get into the packed — and restricted — Buffett lecture last semester. Students who weren't enrolled in the class had to watch the proceedings from a television monitor in another room. Says student James Considine (MBA '94): "The highlight of the course was seeing Warren Buffett sitting on the edge of the table drinking Coke and making offhanded remarks about investing. It was phenomenal. Sure, I could have read these things in a textbook, but it wouldn't have had the same effect."

While the value investor was cool and collected, small-stock maven Royce — who admits that he became a convert to value investing after "losing money and having terrible things happen to a few stocks" — says he was "scared to death" to lecture. "It was a little unnerving standing in front of the students, who all seemed incredibly bright. Plus, I had never been very quantitative and I was concerned that I'd make an idiot of myself." Lecturer Robert Bruce notes: "I was impressed that the group was alert and challenging. What I really liked was the fact that the students were skeptical, and they didn't just accept what was being said without questioning it."

Weiss, an old hand at talking before a roomful of students, says he never sweated it. "As a professor, I know that people remember about 20 minutes worth of material. So I tried to stick with the things I know: how to find investment opportunities in places like Japan and Germany." While Weiss was unconcerned about how his talk would go over, his 14-year-old daughter was a bit ruffled. "She said to me, 'Why are you giving that lecture? You'll be giving away all your secrets.'"

VALUE INVESTING REDUX

Bruce Greenwald's brainstorm came in the back seat of a cab. "I read Ben Graham and became interested in value investing," says Greenwald. "Then I went to a series of lectures that Roger Murray gave and Mario Gabelli sponsored. On the way back to campus, it occurred to me: Murray was the repository of all this knowledge. He was the last of a rare breed — an outstanding academic and a great investor."

Greenwald convinced Murray to team-teach the value investing course. And the rest, as they say, is history.

Greenwald — former associate professor at Harvard Business School, research economist at Bell Laboratories and staff economist to the Brady Commission, which was formed in the wake of the 1987 stock market crash — became a full professor of finance and economics at the School in 1991. In 1992, he was appointed the Robert Heilbrunn Professor of Asset Management and Finance. Earlier, as a visiting professor, he taught finance and economics in the MBA program and corporate finance to senior financial managers in the executive program.

A 1967 graduate of M.I.T. with a BS in electrical engineering, he also holds a master's degree in that field from Princeton, where he simultaneously received the MPA in public and international affairs. His Ph.D. in economics is from M.I.T.

Greenwald says it's good to see value investing back in the finance mainstream. "It's always a good time to teach a course like this," he says. "It's appropriate to the 1970s, the 1980s and the 1990s."

A FEW SURPRISES

While the basic tenets of value investing may seem like common sense, value hunters still face a daunting task. The blunt fact is that value investors must be able to weather the sort of heart-stopping volatility that might give vapors to someone with a flimsier constitution. Given this fact, Chris Shirley (MBA '94) says he was a bit surprised at how simple the lecturers made it all appear. "They made it seem like there was nothing to it," he says. Adds classmate Fong-Keon Chee (MBA '94): "The concepts are easy enough to understand. But there are only a few people who seem to be able to apply the concepts consistently."

REDISCOVERING BENJAMIN GRAHAM

When Janet Lowe began digging for information for her book on Benjamin Graham, she unexpectedly struck paydirt. Buried deep in a file cabinet in Warren Buffett's Omaha office were reams of paper detailing the close friendship between Graham and Buffett.

"There was correspondence, class notes and transcripts of hearings of Graham's congressional testimony on various investment subjects," says Lowe. Her book, *Benjamin Graham on Value Investing: Lessons from the Dean of Wall Street*, is scheduled to hit bookstores in September. Had Graham lived, he would have celebrated his 100th birthday in May.

A former San Diego financial reporter and editor, Lowe didn't stumble onto Graham's work until long after she had graduated from business school. "I was writing a story about a couple of con artists who swindled investors while claiming to be 'Graham and Dodd' investors," she says. "Suddenly, I became interested."

Lowe spent hours talking with the School's staff and faculty and interviewed dozens of alumni and Graham and Dodd aficionados, including Heilbrunn, Schloss and Gabelli. "Columbia Business School plays a prominent role in the book," she says.

The book explores Graham's early years, his rocky and tempestuous marriages and his strained relations with his children. It also traces his meteoric rise as the guru of value investing. Scattered throughout are Graham's own insights on security analysis.

While researching the book, Lowe says she made two surprising discoveries. "It seems that Graham had an incredibly open mind. He always entertained the possibility that there was a better way of doing things," she says. "He was also a very ethical man. He showed that you can be ethical and still make money."

What does she think will be Graham's legacy? "He laid the foundation for the future Buffetts. Graham's work is like wine. The longer it ages, the more people will be able to appreciate it."

Gina Violante (MBA '94) says her biggest concern going into the course was that all the lecturers would be singing the same tune. "But they didn't," she says. "It was a good mix. They all had their own approaches and their own philosophies." She especially recalls the lecture by Walter Schloss, whom Greenwald describes as "probably the most long-lived, successful value investor in the United States today."

In addition to preaching about value investing, Schloss and Buffett both stressed ethics. "I started my discussion with ethics because I think it is important," Schloss says. "I think that every investor should have high ethical standards." Buffett also devoted the first portion of his speech to ethics, telling students that integrity is a quality they should value highly.

For some students, the interest in value investing has already yielded results. Gabelli currently has five Columbia Business School students on his payroll. George White (MBA '95) and Christa Wagner (MBA '95) both log in about 25 hours a week as research analysts — and they haven't even gotten their sheepskin or taken the course.

White's grandfather began teaching him about value investing when he was just 11. He met Gabelli through his former boss, the owner of a Southeastern investment firm. "I came to Columbia because my boss wanted me to have the influence of Benjamin Graham and Warren Buffett and Mario Gabelli."

Wagner met Gabelli at alumni day last year, and nailed down a job. "In most other firms, I would be working as someone's assistant," she admits. "Here, I have major responsibilities, and I work directly with Mario." Both White and Wagner plan to take the value investing class this fall.

As more value converts jump into the fray and computers allow investors to screen entire libraries of balance sheets in a flash, bargains in the true Graham and Dodd mode will be tougher to come by. Still, says Baupost's Klarman, true believers won't be swayed. "There will always be a place for value investors," he says. "Most investors either believe in it, or they don't. Once you believe in it, you're stuck."

Murray says he's glad to see value investing back in Columbia Business School's finance curriculum. "It's hard to see when there will be a time when the discipline won't be useful. As long as we have unpredictable capital markets, we'll always need to study something that's fruitful, useful and productive," he says.

Students concede it might be tough to surpass the success of superstars like Buffett or Gabelli. Still, they say the class is one of the best at the School. "The course got me interested in the concept of being a professional investor, something I'd never thought about before," says Considine. Adds Shirley, "It was a great class. It's one of the great things about Columbia. I enjoyed telling my friends at other schools just what they were missing."

FOURTH ANNUAL GRAHAM AND DODD BREAKFAST FEATURES KEYNOTE SPEAKER LEWIS SANDERS

Columbia Business School's fourth annual Graham and Dodd breakfast was held in New York City on July 26, 1994. Keynote speaker Lewis A. Sanders (right), chairman of Sanford C. Bernstein & Co., shown here with Robert Heilbrunn Professor of Asset Management and Finance Bruce Greenwald, spoke on value investing in the global marketplace. The annual breakfast has consistently attracted top speakers, including Michael Steinhardt of Steinhardt Partners, Seth Klarman of The Baupost Group and Robert Bruce of Alpine Capital. The breakfast is one of the most popular components of the Graham and Dodd program and allows a continuing dialogue among hundreds from the academic and business communities.