chapter 7

Finance Business Activities

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Case STUDY

The New York Stock Exchange

More than 2 billion shares of stock are traded (bought and sold) through the New York Stock Exchange (NYSE) on a typical business day. Often called the "Big Board," the NYSE is one of the oldest and largest stock markets in the world.

The New York Stock Exchange started in 1792 through the efforts of 24 brokers and merchants. Five securities were traded when the NYSE started. Three were government bonds and the other two were bank stocks. Today, nearly 2,700 companies are regularly on the exchange, including most of the largest U.S. corporations as well as many foreign companies.

In recent years a combination of three institutions created the NYSE Group. This merger of the New York Stock Exchange, Archipelago, and the Pacific Exchange created the largest-ever securities exchange.

The NYSE Group has a global emphasis. Over 450 companies from nearly 50 countries make up the NYSE non-U.S. directory. More recently, the NYSE had plans to purchase Euronext. This Europe-based stock exchange was created by a merger of the Paris, Brussels, and Amsterdam exchanges.

The members of the New York Stock Exchange are registered brokers and dealers. They are approved to initiate transactions on the trading floor or through the online facilities of the NYSE. A *floor broker* will usually execute the buy or sell order. Also involved in the transaction process is the *specialist*. This *market maker* creates an efficient buying and selling environment for a given stock. The main activities of the specialist are

- To create a fair and orderly trading environment by setting the day's opening price and reporting bid and offer prices during the trading day
- To be the contact point to bring together brokers with buy and sell orders
- To carry out orders as required by the floor brokers. This activity may require specialists to buy or sell from their own inventory of the stock

Traditionally a system of open outcry was used on the trading floor. Today this process is being replaced by electronic exchanges. In an effort to maintain its market leadership, the NYSE operates both a floor auction exchange as well as a system to facilitate online trades.

Think Critically

1. What activities of the New York Stock Exchange might affect your life?
2. Go to the web site of the New York Stock Exchange to obtain information about current developments of this organization.

7.1 Financing Choices

Goals
- Explain short-term financing alternatives.
- Compare debt and equity financing.

Terms
- line of credit
- promissory note
- commercial paper
- leasing

Short-Term Financing Activities

While companies hope to avoid borrowing, various types of debt are necessary for most businesses. To finance current business activities, a number of short-term borrowing sources are available.

BUYING ON ACCOUNT

Companies often buy on credit. An organization's suppliers and vendors provide companies with needed items. *Accounts payable* refer to amounts owed to creditors for goods and services. These short-term, unsecured debts allow a company to finance daily business activities. Accounts payable are current liabilities generally due within 12 months from the transaction date, with most requiring payment in 30 to 90 days. This borrowing is considered unsecured since the loans are not backed by specific collateral.

Businesses with seasonal sales may cover their expenses with loans or lines of credit.

BANK LOANS AND NOTES

Most businesses borrow money at one time or another. Bank loans may be used for financing inventory, equipment, and other organizational needs. These installment loans are obtained from a commercial bank or other similar financial institution.

Bank installment loans are usually considered medium-term debt, since they are likely to be for more than a year but less than four years. The loan may be secured (with collateral) or unsecured (no collateral).

A **line of credit** is an agreement that allows a company to obtain additional loans without a new loan application. A preapproved limit is established. The business may then borrow additional amounts, often called *advances,* as long as the total does not exceed the established credit limit. A line of credit is especially useful when a company has irregular sales. These loans help the business cover its expenses in times of lower income.

Another common type of loan is a **promissory note**, which is a signed, written promise to borrow money between a borrower and a lender. The terms and conditions of the loan agreement are stated in the promissory note, including the amount of the loan, the interest rate, the payment schedule, late fees, and the financial institution where the loan is to be repaid.

COMMERCIAL PAPER

Companies often need funds for short periods of time. **Commercial paper** refers to unsecured, short-term debt instruments issued by corporations. These loans have maturities ranging from 2 to 270 days.

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What are the main types of short-term financing used by companies?

Long-Term Financing Choices

Companies face daily decisions about financing long-term business activities. Their choices are focused on debt, equity, and leasing.

USING DEBT AND EQUITY

Should a company use bonds or stock for updating equipment or expanding its global activities? This question is an ongoing issue for business organizations.

Debt Financing The use of accounts payable, loans, notes, and bonds are examples of debt financing. The use of long-term debt financing is common among companies and other types of organizations. The main benefits of debt include

- Use of someone else's money
- Expected return for investors is lower with debt than with equity
- Interest payments on debt reduce a company's taxes

In contrast to these advantages, the major drawback of debt—the risk of bankruptcy—must also be considered.

Equity Financing Instead of debt, companies may seek additional investors for the company. A smaller company might offer partial ownership to investors, while a larger corporation might sell stock. Common positive aspects of equity include

- No increased bankruptcy risk; equity contributions are not required to be repaid
- Potential participation by additional owners
- Increased future potential for borrowing

The major negative aspect of equity is that the increased number of shares can result in reduced control by existing owners.

teamwork

In your team, describe several situations in which an organization might lease an item rather than buy it.

LEASING

Instead of buying an item, companies may decide to rent. **Leasing** is a legal agreement to use property that belongs to another person. This type of contract may be used for real estate, equipment, or other assets. For a specified time of use, a lease payment, sometimes called rent, must be made to the owner of the property. The owner of the property is called the *lessor,* while the user who rents the item is the *lessee*. When a company is deciding whether to buy or lease, the following factors are considered.

- Are funds available to buy the item?
- What is the length of the useful life of the asset?
- How would the company's taxes be affected?
- What is the expected value of the asset after its useful life?

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How does leasing differ from other financing activities?

technology topics

Online Investment Activities

Many brokers operate online services that allow investors to access account information and buy and sell securities. By investing online, you can become your own financial planner. These transactions are usually less expensive and more convenient than using a financial planner or traditional stockbroker.

There are disadvantages to investing online. Inexperience in making investment trading decisions can result in a large financial loss. Many online investors buy or sell stocks too quickly because making trades is only a click away.

Before doing business with an e-broker, be sure to investigate the reputation of the company. Talk with others about their experiences with the company. Determine if the online broker has local offices or customer service that will allow you to resolve difficulties easily. Finally, use a variety of sources to obtain advice about the investments you are considering.

Most online brokers allow you to buy and sell a variety of investment products. These include stocks, bonds, mutual funds, T-bills, exchange-trade funds, and stock options. The commission fee charged by e-brokers can range from $4.95 to nearly $30.

In addition, various banking services will likely be available through your online broker. Checking accounts, savings accounts, ATM access, and retirement accounts are commonly offered.

Think Critically

1. When might you consider using an online broker for your investments?
2. Go to the web site of an online broker. What services are provided? What fees are associated with these services?

7.1 Lesson Assessment

UNDERSTAND CONCEPTS

Determine the best answer for each of the following questions.

1. Which of the following is *not* considered to be short-term credit?
   a. line of credit
   b. promissory note
   c. mortgage
   d. commercial paper
2. A common advantage of equity is
   a. interest payments are tax deductible
   b. no increased risk of bankruptcy
   c. a lower required cost of capital by investors
   d. use of someone else's money
3. An agreement that allows a company to obtain additional loans, up to a set amount, without a new loan application is called ____?____.
   a. line of credit
   b. commercial paper
   c. accounts payable
   d. promissory note
4. **True or False?** Commercial paper is usually backed by collateral.
5. **True or False?** Leasing is considered to be renting.

MAKE ACADEMIC CONNECTIONS

6. **Consumer Finance** Obtain information on home equity loans. What are the benefits and drawbacks of this type of consumer credit?
7. **Research** Conduct research about commercial paper. How is this type of business credit used? What are current interest rates for commercial paper for various companies?
8. **Law** Talk to someone who leases an item, such as an apartment or automobile. Obtain information about the legal protection available to the lessor and lessee.
9. **Communication** Interview a local business owner about the types of credit used to finance various business activities.

7.2 Debt Financing: Bonds

Goals
- Describe the main types of government and corporate bonds.
- Explain activities associated with issuing bonds.

Terms
- mortgage bond
- debenture bond
- investment banker
- coupon rate
- bond rating

Types of Bonds

To raise money for current operations or future expansion, most governments and corporations sell bonds. A *bond* is a certificate representing a promise to pay a definite amount of money at a stated interest rate on a specified *maturity date* (due date). Bonds are similar to promissory notes issued by individual borrowers.

When you buy a bond, you are lending money to the organization issuing the bond. You become a *creditor* of the organization.

GOVERNMENT BONDS

Borrowing is a major source of funds for most government agencies. Federal, state, and local governments issue a variety of bonds.

U.S. Savings Bonds One of the safest investments for people with small amounts to invest is U.S. government savings bonds. Series EE savings bonds, which come in denominations from $50 to $10,000, pay interest through a process called discounting.


STOCKBYTE

States may issue municipal bonds for such projects as toll roads.

A Series EE bond is bought at half its face value. A $50 bond costs $25 and, at the end of its full term, pays at least $50. The difference between the purchase price and the redemption (payoff) value is the interest earned. The interest earned is determined by the length of time the bond is held. The time it takes for a savings bond to mature will vary depending on the current interest rate being paid.

One other type of savings bond is the I bond. These investments pay an interest rate that is lower than the rate of other savings bonds, but they pay a variable rate that increases with inflation.

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Treasury Direct is a web site run by the U.S. Department of the Treasury that provides information on government securities. Access thomsonedu.com/school/busfinance and click on the link for Chapter 7. Use the Research Center to find out information on Series EE Savings Bonds.

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Federal Government Bonds The federal government also borrows. The U.S. Treasury issues three major types of debt securities. The difference among them is the length of time to maturity.

1. **Treasury Bills** T-bills are short-term borrowing, with maturities from 91 days to one year.
2. **Treasury Notes** T-notes have maturities from one to ten years.
3. **Treasury Bonds** T-bonds are long-term borrowing, with maturities ranging from 10 to 30 years.

Debt securities are also issued by other federal agencies. These include the Federal National Mortgage Association (often called Fannie Mae), the Federal Housing Administration (FHA), the Government National Mortgage Association (Ginnie Mae), and the Federal Loan Mortgage Corporation (Freddie Mac). Bonds issued by these agencies pay a slightly higher interest rate than Treasury Department securities.

State and Local Government Bonds States, cities, counties, school districts, and other taxing entities borrow to fund various projects. Bonds issued by local and state governments are called *municipal bonds,* or munis.

Two types of municipal bonds exist. A *general obligation bond* is backed by the full faith, credit, and taxing power of the government issuing the bond. A *revenue bond* is repaid with the income from the project that the bond was issued to finance, such as a toll bridge or stadium.

Municipal bonds have an advantage over bonds issued by companies. Often, interest earned on municipal bonds is exempt from federal and most state income taxes. A tax-exempt investment results in a higher return. Consider these two situations.

- Investment A, a corporate bond paying $100 in interest that is taxable, results in the investor keeping less than $100, since taxes must be paid on the interest earned.
- Investment B, a municipal bond paying $100 in interest that is not taxed, resulting in a higher return since the investor keeps the entire $100.

This higher rate of return, often referred to as the *taxable equivalent yield,* would be the comparable rate of return had the interest been subject to income taxes.

Foreign governments issue bonds to finance infrastructure improvements such as roads.

Foreign Government Bonds To finance roads, schools, and military equipment for their nations, foreign governments also issue bonds. These debts are a direct obligation of a foreign government. Foreign governments may issue two types of bonds.

1. **External bonds** These bonds are intended for investors in another country. Interest and principal are paid in the currency of the country in which investors live. External bonds of countries intended for purchase by investors in the U.S. are called *dollar bonds*.
2. **Internal bonds** These bonds are aimed at investors in the country issuing the bond and are payable in the native currency. Foreign government bonds that are payable in several currencies are known as *multiple currency bonds*.

The value of foreign government bonds is based on the same factors as other bonds, including the economic and political stability of the government issuing the bonds. Investors in these bonds commonly face additional risk, such as varied exchange rates, currency instability, and changes in administrations.

CORPORATE BONDS

Investing in bonds is quite different from investing in stock. When you invest in stock, you are an owner of the company. When you buy a bond, you are lending money to the company. Bonds issued by corporations are called *corporate bonds*.

Mortgage Bonds One type of corporate bond is a **mortgage bond.** This type of debt is secured by a specific asset or property. The collateral for a mortgage bond may be equipment, a building, or land. For lenders, a mortgage bond is safer than other types of bonds since a pledge of an asset in the event of default reduces the risk.

Debenture Bonds A corporate bond without collateral is a **debenture bond.** This is an unsecured debt bond whose holder has the claim of a general creditor on all assets of the issuer not pledged specifically to secure other debt.

Other Features of Corporate Bonds A *callable bond* allows the company to pay off the debt before the maturity date at a specified price. A

teamwork

In your team, prepare a list of business situations for which a company may decide to issue bonds.

convertible bond can be exchanged for common stock in the same company. This conversion of a bond to stock will occur according to terms set forth in advance. The agreement will list the set number of shares that will be issued for each bond.

GLOBAL COMPANY BONDS

Companies based in other countries also issue bonds. A corporation may issue debt securities in more than one region at a time. For example, a European company may issue bonds for sale in both its home region and in Japan. These bonds will most likely be issued both in the currency of the home country (euro) and the other country (yen). Global bonds are usually issued by businesses with an international reputation and high credit rating.

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How do mortgage bonds differ from debenture bonds?

Issuing Bonds

Every bond has a *face value,* also called the *maturity value* or *par value,* that indicates the amount being borrowed. Most corporate bonds issued in the United States have a face value of $1,000. Around the world, bonds may be issued with different face values. In the United Kingdom, bonds traditionally are issued for 100 pounds sterling. In Brazil, the standard amount is 1,000 reals, while in South Africa it is 100 rand.

The *maturity date* is the date when the bond, which is a loan, must be repaid. Corporate bonds in the U.S. may be issued for any time period, but they are most often issued for 5, 10, or 20 years.

INVESTMENT BANKERS

An **investment banker** is an individual or company that assists companies with issuing new securities. When raising large amounts of capital, several investment banking companies may work together to sell the new bonds.

Advice to Company One of the significant roles of the investment banker is to guide the company when it issues bonds. Investment bankers will evaluate the company's capital structure (use of debt and equity) to determine if issuing bonds is appropriate and will help to determine the amount of additional debt that might be sold.

Underwriting Process Another task of the investment banker when issuing bonds is underwriting. Underwriting involves setting the price, selling the new bonds, and taking on the risk in this process.

Underwriters make their income from the price difference, or *spread,* between the amount paid to the company issuing the bonds and what investors pay for the bonds. Potential buyers of newly issued bonds include banks, investment companies, pension funds, and individuals. Should the investment bankers not be able to find enough buyers, they hold some bonds themselves. Later, they hope to sell the securities to various investors.

INTEREST RATES

Interest is paid periodically (usually twice a year) to bondholders based on the bond's face value and its stated interest rate. Then, on the bond's maturity date, the face value is repaid to the investor.

Coupon Rate The **coupon rate** is the stated annual interest rate for a bond. The annual interest is based on the face value of the bond. For example, an 8 percent, $1,000 bond would have annual interest of $80. This amount is paid to the holder of the bond each year until maturity. The total interest for a year is usually made in two semiannual payments, every six months.

The coupon rate is based on current market interest rates for bonds with comparable risk. This rate is determined during the underwriting process. The monetary policy of the Federal Reserve has a major effect on interest rates. When money is *tight,* interest rates tend to move upward. In contrast, an environment of *loose* money results in lower rates.

Current Yield The actual rate of return for investors will often vary from the coupon rate. As interest rates change, the rate of return required by investors may increase or decrease. The current yield of a bond is the relationship between the amount of interest and the cost of the bond. As interest rates increase, bond values decline, so the current yield is higher.

$$\textbf{Current Yield (\%)} = \frac{\textbf{Interest Amount}}{\textbf{Cost of Bond}}$$

$$\text{Current Yield (\%)} = \frac{\$80}{\$940} = 0.085 = 8.5 \text{ percent}$$

In this situation, the cost (market value) of the bond declined from $1,000 to $940 due to higher interest rates. This lower bond value, in relation to the fixed interest payment ($80), results in a higher yield for the investor.

DIGITAL VISION

A successful and competent management team positively affects the bond rating of a company.

Basis Points Bond yield is also reported in terms of *basis points,* which divides 1 percent into hundreds. A basis point is 1/100 of a percentage point. For example, 40 basis points is 0.4 percent. When a bond yield goes from 5.07 percent to 5.32 percent, this change will be reported as an increase of 25 basis points. If a rate changes 50 basis points, it represents a change of one half of 1 percent.

BOND RATINGS

All companies do not pay the same coupon rates. Their coupon rates are affected by the current market level of interest rates and the financial stability of the company. A **bond rating** is a measure of the quality and safety of a company's debt. This evaluation is an indicator of how likely it is that a business will be able to make the interest and maturity value payments on the bonds it issues.

Bond ratings evaluate the possibility of default by a bond issuer. As shown in Figure 7-1, these ratings range from AAA (highly unlikely to default) to D (in default). Two commonly used bond rating companies are Standard & Poor's and Moody's Investors Service.

FIGURE 7-1

Bond Ratings

Quality	Moody's	S&P	Description
High-grade	AAA AA	AAA AA	These ratings are assigned companies judged to be of high quality by all standards; almost no chance of default.
Medium-grade	A BAA	A BBB	Bonds from companies that have many favorable factors with very little chance of default.
Speculative	BA B	BB B	Bonds judged to be somewhat uncertain and a fairly high risk.
Default	CAA CA C	CCC CC C D	Bonds from companies that are of poor standing with extremely poor prospects for making payments to investors; company may have filed for bankruptcy.

Bond ratings are commonly affected by

- The earning power of the company
- Other debts the company currently owes
- The past success and future potential of company management

Bond ratings affect the interest rate a company must offer on its bonds. Lower bond ratings require a high rate to attract investors to the higher risk bond.

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What is the purpose of the underwriting process?

7.2 Lesson Assessment

UNDERSTAND CONCEPTS

Determine the best answer for each of the following questions.

1. The federal government debt security with the longest maturity is the
   a. treasury bill
   b. treasury note
   c. treasury bond
   d. municipal bond
2. A bond selling for $1,000 and earning interest of $45 would have a current yield of ____?____ percent.
   a. 10
   b. 45
   c. 4.5
   d. 40.5
3. A ____?____ bond allows investors to exchange the bond for common stock in the same company.
   a. debenture
   b. convertible
   c. mortgage
   d. callable
4. **True or False?** A mortgage bond is considered a secured loan.
5. **True or False?** The bond rating of a corporate bond is based on the earning power of the issuing company.

MAKE ACADEMIC CONNECTIONS

6. **Economics** Research the rates for Treasury bills, Treasury notes, and Treasury bonds for the past five years. What factors affect changes in these rates?
7. **Global Business** Conduct Internet and library research on bonds issued by foreign countries and corporate bonds from around the world. Prepare a short written summary of your findings.
8. **Research** Identify an investment banking company. Conduct research to obtain information about the activities of this organization.
9. **Visual Art** Create a poster or computer presentation to communicate the factors that affect the bond rating of a company.

7.3 Equity Financing: Stock

Goals

- Describe the types of capital stock sold by corporations.
- Explain the process for issuing stock.

Terms

- common stock
- dividend
- preferred stock
- initial public offering (IPO)
- primary market
- secondary market

Types of Stock

To raise funds for current expansion, future growth, and other company goals, a company may wish to take on additional owners who will provide more equity. A company that sells stock for the first time or sells additional shares is using equity financing.

COMMON STOCK

The most frequently used type of corporate ownership gives participants voting rights and an opportunity to share in profits. **Common stock** is an equity security representing ownership in a corporation with voting rights. Common stock has no stated dividend rate. As part owners of the corporation, common stockholders are invited to the annual meeting of the corporation. They are entitled to one vote per share of common stock owned.

DIGITAL VISION

Common stockholders can attend the annual meeting of the corporation.

teamwork

In your team, prepare a list of advantages and disadvantages of (a) a company regularly paying dividends, and (b) a company not paying dividends.

When sharing in profits, stockholders receive a **dividend**, which is a portion of company profits. Common stockholders receive dividends only after preferred stockholders have been paid their dividends. If the profits of a company are large, the common stockholders may receive additional dividends. For example, suppose that a company has issued $100,000 worth of common stock and $100,000 worth of preferred stock with a stated dividend rate of 6 percent. If the company earns a profit of $20,000 and pays all the profit out as dividends, preferred stockholders would be paid $6,000 in dividends ($100,000 × 0.06). The remainder, or $14,000 ($20,000 − $6,000), would be available to pay dividends to the common stockholders. The common stockholders would earn a return of 14 percent.

Investors who purchase common stock in a corporation

- Have voting rights to elect the company's board of directors at the annual stockholders' meeting
- Are not guaranteed dividends, but may receive higher dividends during the company's prosperous periods
- Are paid after bondholders, other creditors, and preferred stockholders if a company fails or liquidates

PREFERRED STOCK

Preferred stock is the second main class of stock issued by corporations. This security has priority over common stock in the payment of dividends. A preferred stockholder, for example, is paid first if profits are used for any dividends.

The dividends paid to preferred stockholders are usually stated as a dollar amount or as a percentage of the par value. The *par value* of a stock is the minimum price for which a share can be issued. A company sets the par value when the corporation is created. The par value usually has no relationship to the market value of a stock.

Preferred stock has characteristics of both debt and equity. Investors receive a set dividend, similar to bond interest payments, but preferred stock represents ownership.

Stockholders receive dividends, a share in company profits.

For investors, owning preferred stock is less risky than common stock. If liquidation would occur, preferred shareholders are paid before common stockholders. Preferred stockholders generally have no voting rights within the corporation.

Two other characteristics of preferred stock sometimes exist. *Cumulative preferred stock* requires that missed (unpaid) dividends due to low earnings will build up until paid to preferred stockholders. *Convertible preferred stock* allows an exchange into common shares. The conversion process is similar to that of convertible bonds.

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What are the main differences between common and preferred stock?

Issuing Stock

When a corporation decides to issue stock for the first time or to issue additional shares of stock, various actions are required.

INITIAL PUBLIC OFFERING

When a company offers stock to outside investors for the first time, it is termed an **initial public offering (IPO).** *Public offering* may refer to the issuing of additional shares of stock by a company.

The IPO for a company is also called "going public." The organization goes from being a *privately held* corporation to one that is *publicly held*. After this process, its shares are sold on a stock exchange. As shown in Figure 7-2, four steps are involved when issuing stock.

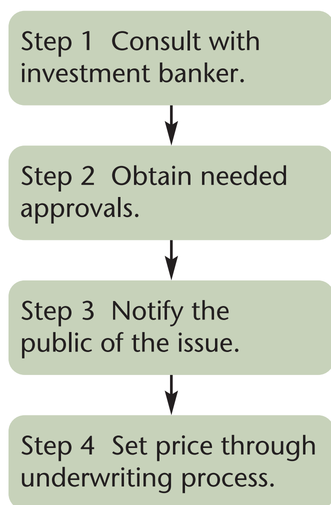


FIGURE 7-2 Initial Public Offering (IPO) Process

1. **Consult with investment banker.** The process starts with contacting an investment banking company. These firms provide advice about issuing stock and will assist with legal approval from the Securities and Exchange Commission (SEC). Investment bankers will develop a marketing and advertising plan to promote the stock issue. They will also obtain potential customers. Finally,

f.y.i.

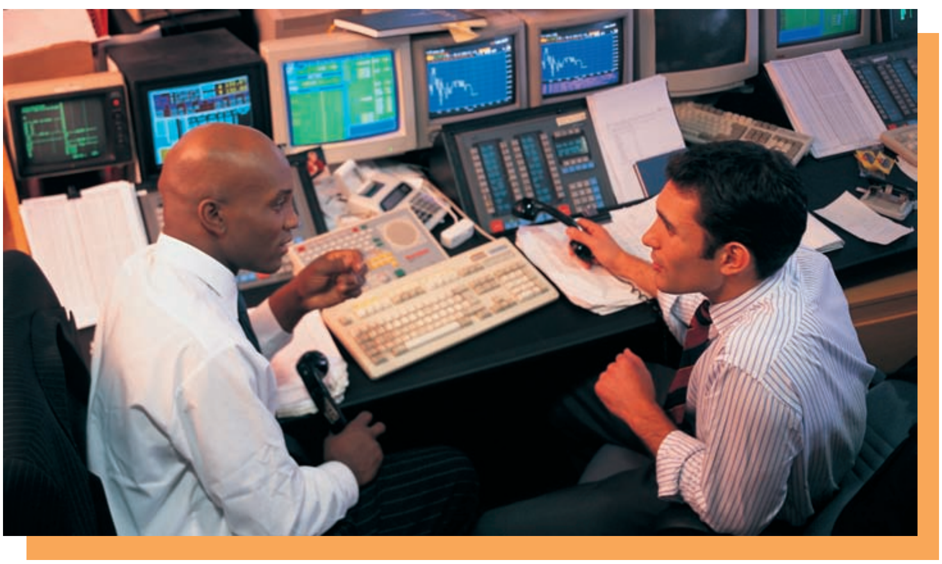
IPOs can be risky, especially if a buyout firm takes the company public. Of the 32 IPOs in early 2006 involving a buyout firm, only 11 had a positive return for investors.

investment bankers act as agents to distribute very large blocks of stocks and bonds.

2. **Obtain needed approvals.** This step involves two groups. First, a majority of current owners of the company must agree to "go public." Then, the SEC must approve the process. This federal agency assures that the stock offering is legitimate. The public must be protected from any deceptive practices or potential investment fraud.
3. **Notify the public of the issue.** Full disclosure of the upcoming stock issue is another requirement. Through news releases and ads in financial publications, the company communicates with the general public about the shares that will be available. A *prospectus* is prepared and distributed. This document presents the legal and financial information about the company issuing the stock.
4. **Set price through underwriting process.** The underwriters in the investment banking company evaluate various company and market factors to develop a price range for the stock. Then, an *issue price* (also called the *subscription price*) is set. Some questions the investment banking company might consider in setting the price include
   - Has the company been profitable over a period of years?
   - Have the company's managers made good business decisions?
   - Does the company have growth potential in coming years?
   - Does the company have an unusually large amount of debt?
   - How does the company compare with others in its industry?

The IPO process is often called the **primary market**, where newly issued securities are sold by investment bankers. After the initial selling, all later buying and selling of those securities occurs in the secondary market.

A **secondary market** is the location where securities are traded after they are initially offered in the primary market. The majority of security transactions occur in the secondary market. The New York Stock Exchange,



DIGITAL VISION

Stock brokers trade securities on the secondary market.

other stock exchanges, the NASDAQ, and bond markets are examples of secondary markets.

checkpoint

What factors affect the issue value of a stock?

a question of ethics

Investment Fraud

Each year, investors lose more than $1.2 billion to various scams. Especially vulnerable are elderly consumers, who may not completely understand the opportunities they are offered. And, after being scammed, older consumers may be too embarrassed to report their losses to government authorities.

Some of the most common tactics used to attract people to deceptive investment schemes include

- Developing trust, in which con artists create a friendly connection by telling you about their family and asking about yours.
- Offering an impossibly attractive investment opportunity, for example, land that is cheap compared to other real estate or guaranteed returns of over 50 percent.
- Establishing credibility. The scam artist might imply that the investment is safe because it is advertised in *The Wall Street Journal* or mention that the company is "licensed" with the state.
- Creating social pressure by implying that many other people have made this investment. They may even mention names of people the investor knows.
- Generating fear to close the deal, since "you wouldn't want to miss this opportunity."
- Implying limited availability, such as "these are the last two rare coins available."

To avoid becoming a victim of investment fraud, use these guidelines.

1. Investigate before signing and paying any money. Contact federal and state agencies about any complaints against the company. Also, talk with family members and friends about the investment.
2. Avoid "you must sign up today" opportunities. Take your time to determine if the investment is legitimate and appropriate for your situation.
3. Research the company and type of investment. Understand the costs and potential risks.
4. Most important, remember that deals that seem "too good to be true"…usually are!

Think Critically

1. Why do so many people each year get cheated with phony investments?
2. Conduct an Internet search to obtain additional information about various investment frauds. Prepare a summary of your findings.

7.3 Lesson Assessment

UNDERSTAND CONCEPTS

Determine the best answer for each of the following questions.

1. Common stockholders have the right to
   a. vote for members of the board of directors
   b. receive a set amount of dividends
   c. receive payment before preferred stockholders
   d. convert their stock into other types of securities
2. When a company first issues shares of stock, it is referred to as the ____?____ market.
   a. stock
   b. bond
   c. primary
   d. secondary
3. An initial public offering refers to ____?____.
   a. issuing foreign bonds
   b. selling stock without using an investment banker
   c. doubling the number of shares of stock
   d. a company going public
4. **True or False?** Most preferred stockholders select preferred stock so they will be able to vote for corporate officers.
5. **True or False?** On a daily basis, most investors buy and sell shares of stock through the primary market.

MAKE ACADEMIC CONNECTIONS

6. **Research** Obtain additional information about issuing preferred stock. Locate the current market value of preferred stock for a company.
7. **Visual Art** Research a company that recently had a new stock issue. Prepare a visual presentation of the steps of the initial public offering (IPO) process using specific information and visuals for the situation you researched.
8. **Law** Conduct an Internet search or library research about the role of the Securities and Exchange Commission (SEC) in the initial public offering process. Prepare a brief summary of your findings.
9. **Global Business** Identify a multinational company that sells stock both in its home country and in the U.S. What are the benefits of this action?

7.4 Stock and Bond Markets

Goals

- Identify the activities involved with stock market transactions.
- Explain the purpose of a mutual fund.
- Describe the factors that affect bonds values.

Terms

- stockbroker
- stock exchange
- market value
- stock split
- selling short
- mutual fund
- capital gain
- yield to maturity (YTM)

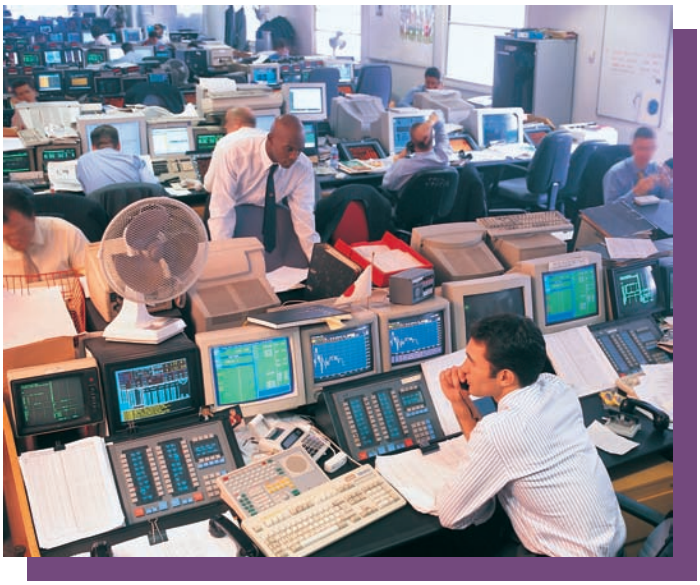
Stock Market Transactions

Each day, hundreds of millions of shares of stock are bought and sold in the secondary market. These shares were previously issued by companies in the primary market, and now they are bought and sold among various investors.

TYPES OF STOCKBROKERS

A **stockbroker** is a licensed specialist in the buying and selling of stocks and bonds. Brokers serve as an intermediary between the issuer of securities (bonds and stock) and potential customers (investors). Through brokers, stockholders state the price at which they are willing to sell their shares. Interested buyers tell brokers what they would be willing to pay for those shares. The brokers then work out a price that is acceptable to both buyers and sellers. For their services, brokers charge a fee called a *commission*.

Two types of brokers are common. A *full-service broker* provides information about securities you may want to buy. Full-service brokers work for brokerage houses with large research staffs. In contrast, a *discount broker* places orders and offers limited research and other services. Discount brokers charge lower commissions than full-service brokers. Investors who do their own research can save money by using a discount broker. Today, both full-service and discount brokers can be reached online handling trades through their web sites.



DIGITAL VISION

Stockbrokers are specialists in the buying and selling of stock.

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The cost of an online stock trade can range from $5 to $30. The service provided also varies. Investors must decide how much they are willing to pay for assistance and information.

STOCK EXCHANGES

Brokers work through **stock exchanges**, which are businesses where securities are bought and sold. The best known stock exchange is the New York Stock Exchange in New York City. The American Stock Exchange is also in New York City. Regional stock exchanges operate in Boston, Chicago, Philadelphia, and San Francisco. More than 150 stock exchanges are in operation around the world.

In the past, stocks of smaller companies were not traded on a stock exchange. The *over-the-counter (OTC)* market is a network where securities transactions occur using telephones and computers rather than on the floor of an exchange. The OTC market in the U.S. is the NASDAQ, which stands for the National Association of Securities Dealers Automated Quotations. Today, the NASDAQ includes many large companies.

CHANGING STOCK VALUES

The **market value** of a stock is the price at which a share of stock can be bought and sold in the stock market. This current value of a share can change rapidly. If the business is doing well, the market value is likely to go up. If the business has a poor record, the market value usually goes down. The market value may be affected by current economic conditions as well as national and global politics.

The prices at which stocks are being bought and sold are available through stock market listings in newspapers and online. Examine Figure 7-3, which gives an explanation of the stock market listing.

FIGURE 7-3

Stock Market Listing Explanation

STOCK MARKET QUOTATIONS

1	2	3	4	5	6	7	8	9	10	11	12
52-Week					Yld.		Vol.				Net
Hi	Lo	Stock	Sym.	Div.	%	PE	100s	Hi	Lo	Close	Chg.
74.93	56.72	Deere	DE	1.12	1.6	15	21823	70.14	67.38	68.01	−0.42
95.64	64.84	FedExCp	FDX	0.28	0.3	27	14555	94.54	91.78	93.74	+1.22
45	35	Kellogg	K	1.01	2.3	21	6791	44.82	43.67	44.74	−0.24
20.50	15.94	Mattel	MAT	0.40	2.1	16	21682	19.23	17.77	18.80	−0.15
42.95	31.25	Reebok	RBK	0.30	0.8	14	4501	40.47	37.82	39.22	+0.12

1 – Highest price paid for stock during past 52 weeks
2 – Lowest price paid for stock during the past 52 weeks
3 – Abbreviated company name
4 – Symbol used to report company
5 – Current dividend per share (in dollars)
6 – Dividend yield based on current selling price
7 – Price-earning ratio
8 – Number of shares traded, expressed in hundreds, on the trading day
9 – Highest price for a share on the trading day
10 – Lowest price for a share on the trading day
11 – Closing price for the day
12 – Change in closing price compared to previous trading day

Stock Market Indexes Another measurement of investment values is a *stock index*. These indicators of stock values are commonly reported on television, radio, and in newspapers. The Dow Jones Industrial Average (DJIA) includes 30 of the largest U.S. companies. Another commonly reported stock index is the Standard & Poor's (S&P) 500, which is based on stock values of 500 major companies.

Stock Split When the value of a share of stock gets fairly high, many companies decide to lower the price to increase market activity. A **stock split** is the proportional division of a number of stock shares into a larger number. With this action, a lower share value occurs, but there is no change in the proportion of each stockholder's ownership. For example, with a 2-for-1 stock split, the number of shares you own doubles, but the total market value is unchanged. Instead of one share of stock valued at $100, you would have two shares valued at $50 each.

This increase in the number of shares does not change the company's total market value or each shareholder's share of ownership. If you own 20,000 shares, representing 5 percent of the company, you would now have 40,000 shares which would still represent 5 percent ownership. The company hopes that the lower share price resulting from a stock split will create increased interest and market demand for the stock. A stock split can result in strong gains if the price increases to the previous level, since each investor now has more shares.

Selling Short If an investor believes the price of a stock will fall, a method exists to make money. **Selling short** involves selling a stock not actually owned when a lower price is expected. Then, the investor must buy the stock back at the market price to replace the "borrowed" shares.

For example, an investor may decide to "sell short" 1,000 shares of a company's stock on April 20 for $10 a share. Then, on May 1, if the stock is selling at $9 a share, the investor can "replace" the borrowed shares at a lower price. By selling short, this investor made a profit of $1,000, less commission and any other fees.

In this process, investors who sell short hope to buy the needed replacement shares at a lower price. This activity can be quite risky. If the stock increases in value, a loss will occur when the replacement shares must be bought at a higher price.

Consumer spending habits affect stock prices.

teamwork

Discuss various business and economic trends. Prepare a list of stocks which your group believes would be good investments. Explain what factors influenced the selection of these companies.

STOCK SELECTION ACTIONS

As a person decides which stocks to purchase, an investment analysis process can be helpful.

Investment Analysis Process Buying stocks can consist of a process with the following steps.

1. Observe and analyze economic and social trends.
2. Determine industries that will be affected.
3. Identify companies in those industries.
4. Decide whether to buy, sell, or hold the stock of those companies.

By observing various economic and social trends in the U.S. and around the world, you can determine what types of companies could benefit from those trends.

Economic Factors Various economic conditions can affect stock prices, including the following factors.

- **Inflation** Higher prices can result in lower spending by consumers, reducing company profits
- **Interest Rates** As the cost of money changes, company profits can increase or decline
- **Consumer Spending** Profits of companies that sell products and services to households are directly affected by consumer buying habits
- **Employment** As people obtain or lose jobs, the amount of money they have for spending will affect company profits

Industry Trends Societal changes and other factors can have a positive or negative influence on various types of companies. For example, as people live longer, increased health care is required. Companies involved in health care products may be a wise investment. Other industries that investors might analyze and consider for stock purchases include automotive, construction, consumer products, financial services, retailing, technology, and utilities.

Market Trends The overall direction of stock market prices is also a factor to consider. A *bull market* refers to a period of rising stock values. During this time, investors tend to have a positive attitude about the stock market and the economy. In contrast, a *bear market* is a period of declining stock market prices, in which investor attitudes are generally negative.

Dividend Yield Additional information about a company may also be considered. The *yield* of a stock is an important factor if your goal is to earn a good return from your investment.

For example, suppose that a company is paying a quarterly dividend of \$0.60 a share. The total dividend for the year would be \$2.40, and if the stock is selling for \$40 a share, the current yield (return) would be calculated as follows.

$$\textbf{Dividend Yield} = \frac{\textbf{Dividend per share}}{\textbf{Market price per share}}$$

$$\frac{\$2.40}{\$40} = 0.06 \text{ or } 6 \text{ percent}$$

Price-Earnings Ratio The price of a stock should also be considered. Many investors look at the stock's *price-earnings (P/E)* ratio, which is the relationship between a stock's selling price and its earnings per share. The P/E gives you an indication of whether the stock is priced high or low in relation to its earnings per share.

Stock Information Sources When selecting stocks, learn something about the company. Several information sources are available, such as *Moody's Handbook of Common Stocks, Value Line,* and *Standard & Poor's Encyclopedia of Stocks*. These publications provide data about net worth, debt, sales revenue, profits, dividend history, and the future prospects of companies. Many web sites are also available to provide valuable information on companies.

The U.S. Securities and Exchange Commission, which oversees the financial markets, requires all companies that issue publicly traded securities to file detailed reports electronically. Those reports can be accessed online.

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What factors are commonly considered when evaluating a company's stock?

finance around the world

Stock Exchanges around the World

Locations of stock exchanges range from Johannesburg to Hong Kong and from Madrid to Lima. More than 150 exist in countries around the world. Each of these organizations serves local companies with trading facilities for buying and selling stocks, bonds, and other securities.

The Prague Stock Exchange started in 1993, the year Czechoslovakia divided into two separate countries—the Czech Republic and Slovakia. As the countries moved from a centrally planned economy under communist rule to a free-market economy, citizens were allowed to invest in stocks.

As the capital of the Czech Republic, Prague is the center of the country's business activities. When it started, the Prague Stock Exchange handled transactions for only seven companies. Today, this exchange has expanded its business to include many more companies. Many of the previously government-controlled businesses are now privately owned. Some of the most popular stocks are companies in the hotel and glass manufacturing industries.

While many local stock exchanges exist, the influence of regional markets is expanding. Euronext was formed in 2000 through a merger of the Paris, Brussels, and Amsterdam stock exchanges. This organization regularly trades stocks of more than 1,250 companies. More recently, Euronext has been acquired by the New York Stock Exchange.

Think Critically

1. How might the activities of stock exchanges in different countries differ from each other?
2. Conduct an Internet search to locate the web site for a stock exchange in another region of the world.

Mutual Funds

Instead of buying individual bonds and stock, many people buy shares in an *investment company*. A **mutual fund** is an investment fund set up and managed by companies that receive money from many investors. Then, the company buys and sells a wide variety of stocks or bonds. Mutual funds allow investors to spread their risk among many investments.

TYPES OF MUTUAL FUNDS

Over 17,000 different mutual funds are available to investors. These funds have many different objectives. For instance, some emphasize investing in growth stocks, some emphasize stocks that pay high dividends, and some emphasize international stocks. Some of the main types of mutual funds include

- Aggressive growth stock funds, which seek quick growth but also have higher risk
- Income funds that specialize in stocks that pay regular dividends
- International funds that invest in stock of companies from around the world
- Sector funds, which include stocks of companies in the same industry, such as health care, energy, or telecommunications
- Bond funds, which specialize in corporate bonds
- Balanced funds that invest in both stock and bonds

When selecting a mutual fund in which to invest, investors should match their personal investment goals to the type of mutual fund.

The London Stock Exchange is one of many in cities around the world.

MUTUAL FUND VALUES

Mutual fund investors own shares of the mutual fund. The value of each share is based on the total value of all investments made by the mutual fund company. For example, if the investments were worth $400,000 and 80,000 shares existed, each share would be worth $5.

$400,000 ÷ 80,000 = $5

This amount is called the *net asset value (NAV)* of a mutual fund.

A part of the dividends and interest received from the fund's investments is used to pay operating expenses of the fund. The major portion of earnings is distributed to the mutual fund shareholders or reinvested in the fund.

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What are the advantages of investing in mutual funds?

Changing Bond Values

Bonds are bought and sold in the bond market. The market value of a bond varies based on changing interest rates and the credit rating of the borrowing organization.

REPORTING BOND PRICES

Bond values are reported, like stocks, in daily newspapers and online. Corporate bond prices are stated in 100s, with the bonds sold in $1,000 denominations (ten times the reported amount).

The price of bonds is affected by changing interest rates.

For example, a bond reported at 100 is selling at its face value of $1000. A bond selling at 105 has a current market value of $1,050. At 100, the bond is being sold at *par*. At 105, it is being sold at a *premium*. Below 100, the bond is being sold at a *discount*.

The price investors are willing to pay for a bond depends upon the *stated interest rate*. If interest rates on similar bonds are higher than the bond's stated rate, investors will want to buy the bond for less than its face value. On the other hand, if the bond's stated interest rate is higher than interest rates on similar bonds, the seller of the bond will want to receive more than its face value.

As shown in Figure 7-4, changing interest rates affect the price of the bond. Since the interest payment is set when the bond is issued, the current yield will be affected by the amount a person pays for the bond.

FIGURE 7-4

Changing Bond Values and the Current Yield

Situation	Bond Sold at	Market Value	Reported at	Interest Payment	Current Yield
Bond issued	par	$1,000	100	$100	10% $100 ÷ $1,000
Higher interest rates	discount	$ 900	90	$100	11.1% $100 ÷ $900
Lower interest rates	premium	$1,100	110	$100	9.1% $100 ÷ $1,100

CAPITAL GAINS

When a person holds a bond until maturity, a **capital gain** may occur. A capital gain is the increase in the value between the purchase price and the maturity value. When a bond is bought at a discount such as $900 and held until maturity, the investor has a $100 capital gain, in addition to the interest payments on the bond.

A *capital loss* can also result. If a bond is bought at a premium, such as $1,100, at maturity the bondholder only receives $1,000. Why would a person do this? The investor has paid for the right to receive the annual interest payments on the bond until the maturity date.

The current yield is the rate of return based on interest earned. Capital gains and losses affect the **yield to maturity (YTM)** of a bond. The yield to maturity is the annual rate of return an investor would receive when a bond is held until maturity. YTM takes into account the price discount below or the premium above the face value of the bond.

As you might expect, the YTM is more than the current yield when the bond is selling at a discount. This rate is less than the current yield when the bond is selling at a premium.

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What factors affect bond prices?

7.4 Lesson Assessment

UNDERSTAND CONCEPTS

Determine the best answer for each of the following questions.

1. When a company changes the number of shares of stock to bring the current market price down, this is called
   a. selling short
   b. an initial public offering
   c. a stock split
   d. a mutual fund
2. An investment that allows a person to own a variety of companies is called
   a. a corporate bond
   b. preferred stock
   c. a mutual fund
   d. a municipal bond
3. **True or False?** Only discount brokers allow investors to buy and sell stocks online.
4. **True or False?** As interest rates rise, bond prices tend to rise.

MAKE ACADEMIC CONNECTIONS

5. **Technology** Visit the web site of a stock brokerage company. What services are offered to investors? How might you use this site to select stocks in which to invest?
6. **Data Analysis** Using Figure 7-3, answer the following questions:
   a. What is the amount of the most recent dividend for Federal Express?
   b. What is the yield for Kellogg's stock?
   c. What is the lowest price that Mattel stock sold for over the past year?
   d. What was the closing price of Reebok stock on the previous trading day?
7. **Visual Art** Prepare a poster, computer presentation, or other visual to communicate the main types of mutual funds in which a person can invest.
8. **Research** Using online sources or the financial section of the newspaper, obtain current information about the trend on bond values. What factors have affected bond prices?

Chapter 7 Assessment

Summary

7.1 FINANCING CHOICES

1. The main short-term financing methods used by businesses include buying on account (accounts payable), bank loan, line of credit, promissory note, and commercial paper.
2. Debt (borrowing), equity (selling stock), and leasing (renting) are methods used by organizations to finance business activities.

7.2 DEBT FINANCING: BONDS

3. Bonds are issued by the federal government, state and local governments, foreign governments, and companies.
4. The process for issuing bonds involves the use of an investment banker, who provides advice to the company and helps set the price of the bonds. Rates on new bonds will be affected by current interest rates and the bond rating of the company.

7.3 EQUITY FINANCING: STOCK

5. The two main types of stock issued by corporations are common and preferred.
6. An initial public offering (IPO) is the process of offering stock to outside investors for the first time. When this occurs, a company that was privately owned becomes a public company.

7.4 STOCK AND BOND MARKETS

7. A stockbroker is a licensed specialist in the buying and selling of stocks and bonds. Brokers work through stock exchanges, which are businesses that accommodate the buying and selling of securities. The main factors that affect stock prices are economic conditions, industry trends, and market trends.
8. A mutual fund is an investment fund set up and managed by companies that receive money from many investors. The money from investors is used to buy and sell a wide variety of stocks or bonds. Mutual funds allow investors to spread their risk among many investments. Many different types of mutual funds exist to meet different investment objectives.
9. Bond prices are affected by interest rates. Higher rates will result in a bond being sold at a discount. When rates decline, bonds are sold at a premium. A capital gain is the increase in value between the purchase price and the maturity value on a bond or other investment.

Develop Your Business Language

Match the terms listed with the definitions. Some terms will not be used.

1. Price at which a share of stock can be bought and sold in the stock market
2. Security that has priority over common stock in the payment of dividends
3. Unsecured, short-term debt instruments issued by corporations
4. Stated annual interest rate for a bond
5. Corporate bond without collateral
6. Type of debt secured by a specific asset or property
7. Selling a stock not actually owned when a lower price is expected
8. An equity security representing ownership in a company with voting rights
9. When a company offers stock to outside investors for the first time.
10. Increase in the value between the purchase price and the maturity value
11. Measure of the quality and safety of a company's debt
12. Legal agreement to use property that belongs to another person
13. Business organization where securities are bought and sold
14. A licensed specialist in the buying and selling of stocks and bonds
15. Portion of company profits
16. Proportional division of a number of stock shares into a larger number
17. An individual or company that assists with the issuing of new securities

a. bond rating
b. capital gain
c. commercial paper
d. common stock
e. coupon rate
f. debenture bond
g. dividend
h. initial public offering (IPO)
i. investment banker
j. leasing
k. line of credit
l. market value
m. mortgage bond
n. mutual fund
o. preferred stock
p. primary market
q. promissory note
r. secondary market
s. selling short
t. stock exchange
u. stock split
v. stockbroker
w. yield to maturity (YTM)

Review Concepts

18. A federal government debt security that pays a variable rate that increases with consumer prices is ____?____.
    a. T-bill
    b. T-note
    c. T-bond
    d. I-bond
19. A person interested in current income would select a mutual fund emphasizing
    a. technology stocks
    b. dividends
    c. long-term growth
    d. foreign government bonds
20. The yield to maturity of a bond would be highest when the bond is
    a. sold at a discount
    b. sold at a premium
    c. sold at par
    d. tax deductible

Think Critically

21. What actions might a small company take when needing to borrow funds?
22. What benefits and drawbacks are associated with leasing?
23. What actions can be taken by a company to improve its bond rating?
24. Describe the role of an investment banker when a company is involved in mergers and acquisitions.
25. How can a stock split affect the long-term profits of an investor?
26. What are the economic benefits of capital gains earned by investors?

Business Financial Calculations

27. For each of the following situations, calculate the annual yield.
    a. stock that cost $56 and earned a dividend of $4.20
    b. bond costing $1,000 with annual interest of $106
    c. land purchased for $10,000 and sold a year later for $11,600
28. A bond with a yield of 6.72 percent has dropped 30 basis points. What is the new yield?
29. You call your broker to sell short, asking to sell 100 shares at $42. Within three days, the stock drops to $39 a share and you obtain the required shares. What is the amount of your capital gain in this situation?
30. You own 40,000 shares of stock of a company, representing 6 percent ownership. The company plans a 3-for-2 stock split. After the split,
    a. how many shares would you own?
    b. what percentage of the company would you own?
31. Based on Figure 7-3, answer the following questions.
    a. The number of shares traded on Federal Express stock increased by 10 percent the next trading day. How many shares were traded the next day?
    b. What was the closing price of Deere stock on the previous trading day?
    c. Based on the closing price for Mattel, if the company paid an annual dividend of $1.26, what would be the yield?
32. What would be the market value (in dollars) for a corporate bond selling at 97? What would be the market value of a bond selling at 106?

Analyze Cases

Use the case from the beginning of the chapter, The New York Stock Exchange, to answer the following questions.

33. What activities does the NYSE provide to assist businesses?
34. How do expanded global business activities affect the NYSE?
35. Describe positive and negative aspects of stock exchange mergers for companies and investors.
36. How might technology affect future NYSE activities?
37. What aspect of the NYSE activities poses the greatest challenge for its future? What actions would you suggest to address this concern?

Portfolio Activity

COLLECT an item that reflects the financing alternatives used by various organizations—debt, equity, leasing. This example could be an advertisement, newspaper or magazine article, a web site, photo, or an actual item.

CREATE a visual, such as a table or diagram, to summarize the benefits and drawbacks of the financing methods commonly used by businesses and other organizations. Use photos, ads, actual items, and drawings to illustrate the advantages and disadvantages of debt, equity, and leasing.

CONNECT your visual to other aspects of our economy and society or relate it to an idea you have learned in another class. Make the connection by preparing a brief written summary comparing debt, equity, and leasing.

Stock Market Activity

Issuing stock is a major financing activity of most companies. Organizations may also use debt and leasing. These financing alternatives affect both the company's current business activities and its long-term potential.

Use online and library resources to research the company you have been studying (or select a different company).

1. Compare the use of debt and equity by the company. Use the company's annual report as well as other research sources.
2. Determine if the company has recently issued additional stock or bonds. If so, what was the planned use of these funds?
3. Describe situations in which the company might use leasing.
4. Analyze your findings to determine the effect of these financing decisions on the value of the company's stock. At this point, would you buy, sell, or hold the stock of this company as an investment for your current or future personal financial situation? Explain your reasons.

Planning a Career in Stock Brokerage

When a company needs to raise funds through issuing stocks or bonds, an investment banker will be involved. Investment banking firms help companies and governments issue securities, help investors purchase securities, manage financial assets, trade securities, and provide financial advice.

Expanded public offerings by foreign companies and privatization of firms previously owned by foreign governments will likely increase international investment banking needs.

Stockbrokers work with customers when buying or selling stocks, bonds, mutual funds, and other investment products.

Employment Outlook

- Opportunities for investment and financial services sales agents are expected to grow about 10 percent over the next eight years. Most of these jobs are in securities, commodity contracts, and other financial investment activities.
- Other opportunities exist with banks, credit unions, and other financial institutions. Many people in this field are self-employed.
- Turnover is often high for beginning sales agents who have not yet established a strong base of clients. Opportunities for entry-level positions are very competitive.

Job Titles

- Investment banker
- Stockbroker
- Account executive
- Registered representative
- Brokerage sales manager
- Stock analyst
- Economist
- Security sales agent
- Commodity sales agent

Needed Skills

- A college degree with knowledge of finance, accounting, and economics is a basic requirement
- Sales and interpersonal skills are vital when working with clients
- Research ability and computer competency to keep informed on economic and industry trends
- Knowledge of laws related to securities and financial markets
- Securities and commodities sales agents must pass licensing exams, such as the Series 7 and the Series 63 licenses

What's It Like to Work in Stock Brokerage?

"How might the merger affect the company's stock price?" "Will the company's dividends continue for the next few years?"

These are some of the questions you might address as a stockbroker. Your ability to attract new clients and serve existing ones is a key to success. You will likely work long hours. Your income may be based all or partially on commission.

As you prepare a sales strategy for your clients, you must assess their current financial situation and future needs. Developing a plan to meet clients' investment goals will be the major focus of your work.

What about you? What elements of being a stockbroker might interest you? What additional information would you like to have about this career?

MULTIMEDIA PRESENTATION EVENT

Participants in this event are challenged to use presentation technologies and software to prepare and deliver their message. Most consumers understand the need to invest for their financial future, but do not have a thorough understanding of the investment options. You are to create a multimedia presentation that teaches people about investment options. The presentation should explain stocks, corporate bonds, government bonds, and real estate as investment options. Each type of investment should be carefully defined in the presentation. Definitions should be in terms the average consumer understands. The presentation should also emphasize strengths and weaknesses for each type of investment.

Presentations can be created by 1 to 3 members, and may be submitted using only a CD or DVD. Presentations must be at least two (2) and no more than four (4) minutes in length. They must address the assigned topic, be well organized, and contain substantiated statements.

The oral presentation is an explanation of the multimedia presentation. The oral presentation should explain the development and design process, the use and implementation of innovative technology, the use and development of media elements, and copyright issues with pictures, music, and other features. The individual or team has nine (9) minutes to give the multimedia presentation. Setup time is included in the total presentation time. A timekeeper will stand at eight (8) minutes. Five (5) points will be deducted for any presentation over 9 minutes in length. Following the oral presentation, the judge may conduct a three-minute question-and-answer period during which the presenters should be prepared to defend all aspects of their multimedia presentation.

Performance Indicators Evaluated

- Explain the development of the topic in the presentation.
- Explain the development and design process.
- Demonstrate the use and implementation of innovative technology.
- Compare customer service offerings.
- Explain the use and development of graphics, video, and audio.
- Organize an effective oral presentation.
- Deliver an effective oral presentation that indicates self-confidence.

Go to the FBLA web site for more detailed information.

Think Critically

1. Why is a multimedia presentation a good way to explain different investment options?
2. Why should this presentation compare and contrast investments according to strengths and weaknesses?
3. What is the disadvantage of a presentation that uses too much text?
4. How does the way presenters dress affect the impact of a presentation?

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