Stock Trading
Presented by:
Ahmet Tezel
Rajneesh Sharma
Karen Hogan

Instructions for Registering

- Go to [www.marketwatch.com/game](http://www.marketwatch.com/game)
- Click on the orange button that says “Join Now”
- Click on the link “Get your membership now”
- Fill out the registration form and submit it
- In order to confirm your email address, you will need to go to your email account and open the email from Dow Jones. Click on the link in the email to confirm your email address
- You will be taken to the login page. Enter your email address as the username and the password you chose during registration
- You are now at MarketWatch’s home page and have finished registering your account
Trading Game

- After registering
  - Join the trading game: sjufac2013
  - The password is hawkfac2013

Common Stock

- What is common stock?
- **Residual Owners**: stockholders of a firm are the owners, who are entitled to dividend income and a prorated share of the firm’s earnings only after all the firm’s other obligations have been met
  - Stocks allow investors to tailor investments to meet individual needs and preferences
  - Stocks may provide a steady stream of current income through dividends
  - Stocks may increase in value over time through capital gains
Long and Short Positions

- **Long Purchase**
  - Investor buys and holds securities
  - Security – a tradable asset of any kind
  - **Buy low and sell high**
  - Make money when prices go up

- **Short Selling**
  - Investor sells securities they don’t own by borrowing securities from broker
  - Broker lends securities owned by other investors
  - **Sell high and buy low**
  - Investors make money when stock prices go down

General Market Conditions

- **Bull Market**
  - Rising prices
  - Investor/consumer optimism
  - Economic growth and recovery
  - Government stimulus

- **Bear Market**
  - Falling prices
  - Investor/consumer pessimism
  - Economic slowdown
  - Government restraint
Trading Tip 1: Trading on News

- These trades are based on the news
- You have to trade like a headline chaser
- Find two firms which are in the news
- If the news is good, buy the stock, if the news is bad, short sell the stock
- You can find tickers for firms on finance.yahoo.com

Finance News Websites

- http://www.google.com/finance
- http://money.cnn.com/
- http://www.morningstar.com/
- http://www.zacks.com/
Quotes

- **Bid Price**
  - A stock may have many buyers at different prices
  - The bid price is the highest price offered by the buyers to purchase a given security

- **Ask Price**
  - A stock may have many sellers at different prices
  - The lowest price at which a seller is willing to sell a given security

Basic Types of Orders

- **Market Orders**
  - Orders to buy or sell stock at current ask price when order is placed
  - Fastest way to fill order

- **Limit Orders**
  - You set the price limit at which you are willing to buy or sell your stock
  - If price limits are not met, order is not filled
Trading Tip 2: Trading in What You Know

- These trades are based on Peter Lynch's investment principle “Invest in what you know”
- Pick two products that you like or dislike. Which firms make these products?
- If the product is good, buy the stock; if the product is bad, short sell the stock.

---

1-Year Returns of Familiar Stocks

<table>
<thead>
<tr>
<th>Name</th>
<th>Ticker</th>
<th>Price 3/8/2012</th>
<th>Price 3/8/2013</th>
<th>1-yr Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nike Inc.</td>
<td>NKE</td>
<td>53.95</td>
<td>54.69</td>
<td>1.37%</td>
</tr>
<tr>
<td>McDonald's Corp</td>
<td>MCD</td>
<td>96.96</td>
<td>98.71</td>
<td>1.80%</td>
</tr>
<tr>
<td>Wal-Mart Stores</td>
<td>WMT</td>
<td>59.77</td>
<td>73.03</td>
<td>22.19%</td>
</tr>
<tr>
<td>Green Mountain Coffee</td>
<td>GMCR</td>
<td>62.40</td>
<td>52.87</td>
<td>-15.27%</td>
</tr>
<tr>
<td>Starbucks</td>
<td>SBUX</td>
<td>50.37</td>
<td>58.67</td>
<td>16.48%</td>
</tr>
<tr>
<td>Macy's</td>
<td>M</td>
<td>39.30</td>
<td>41.67</td>
<td>6.03%</td>
</tr>
<tr>
<td>Mastercard</td>
<td>MA</td>
<td>417.26</td>
<td>529.23</td>
<td>26.83%</td>
</tr>
<tr>
<td>Apple</td>
<td>AAPL</td>
<td>541.99</td>
<td>431.72</td>
<td>-20.35%</td>
</tr>
<tr>
<td>Exxon Mobil</td>
<td>XOM</td>
<td>84.83</td>
<td>88.97</td>
<td>4.88%</td>
</tr>
<tr>
<td>Johnson &amp; Johnson</td>
<td>JNJ</td>
<td>64.85</td>
<td>78.19</td>
<td>20.57%</td>
</tr>
<tr>
<td>S&amp;P 500 Index</td>
<td>^SP500</td>
<td>1365.92</td>
<td>1551.18</td>
<td>13.56%</td>
</tr>
</tbody>
</table>
Know how to place and confirm orders
Verify stock ticker symbols
Use limit orders
Check orders before submitting—you pay for typos
Don’t get carried away
  ◦ Follow a strategy
  ◦ Don’t churn
  ◦ Avoid or limit margin orders
Open accounts with two brokers
After completion double-check orders after for accuracy

Quotation from Yahoo

International Business Machines Corporation (IBM) - NYSE

211.30 \downarrow 1.06 (0.50\%) 10:56AM EDT - Nasdaq Real Time Price

<table>
<thead>
<tr>
<th>Prev Close</th>
<th>Open</th>
<th>Bid</th>
<th>Ask</th>
<th>1y Target Est</th>
<th>Beta</th>
<th>Next Earnings Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>212.36</td>
<td>210.96</td>
<td>211.22</td>
<td>211.27</td>
<td>225.70</td>
<td>0.61</td>
<td>16-Apr-13</td>
</tr>
</tbody>
</table>

Day’s Range: 210.10 - 211.44
52wk Range: 181.85 - 215.90
Volume: 955,923
Avg Vol (3m): 3,820,010
Market Cap: 235.44B
P/E (ttm): 14.68
EPS (ttm): 14.37
Div & Yield: 3.40 (1.60\%)
Using Behavioral Finance to Improve Investment Results

- Don’t hesitate to sell a losing stock
- Don’t chase performance
- Be humble and open-minded
- Review the performance of your investment on a periodic basis
- Don’t trade too much
Trading Tip 3: Trading Using Charts

- These trades are based on charts (technical analysis)
- Pick two stocks
- Look at their charts on stockcharts.com or finance.yahoo.com
- If you think the pattern suggests upward movement, buy the stock
- If the pattern suggests downward movement, sell the stock

Charting Tools Websites

- Plot the performance of stocks over a specified time period
- Examples:
  - Barchart.com
  - BigCharts.com
  - Stockcharts.com
**Types of Stock**

- **Blue Chip Stocks**: financially strong, high-quality stocks with a long and stable record of earnings and dividends
  - Companies are leaders in their industries
  - Relatively lower risk due to financial stability of company
  - Popular with investing public looking for steady growth potential, perhaps dividend income
  - Provides shelter during unsettled markets
  - Examples: AT&T, Chevron, Johnson & Johnson, McDonald’s, Pfizer
Types of Stock (cont)

- **Income Stocks**: stocks with a long and sustained record of paying higher-than-average dividends
  - Good for investors looking for relatively safe and high level of current income
  - Dividends tend to increase over time (unlike interest payments on bonds)
  - Some companies pay high dividends because they offer limited growth potential
  - More subject to interest rate risk
  - Examples: Duke Energy, Conagra Foods, Sara Lee, Altria Group

Types of Stock (cont)

- **Growth Stocks**: stocks that experience high rates of growth in operations and earnings
  - Have sustained rate of growth in earnings above general market
  - Investors expect higher price appreciation due to increasing earnings
  - Riskier investment because price may fall if earnings growth cannot be maintained
  - May include blue chip stocks as well as speculative stocks
  - Typically pay little or no dividends
  - Examples: Netflix, eBay, Berkshire Hathaway, Starbucks
Types of Stock (cont)

- **Tech Stocks**: stocks representing the technology sector of the market
  - Range from speculative stocks of small companies that have never shown a profit to blue chip stocks of large companies that are growth-oriented
  - Potential for attractive returns
  - Considerable risk and volatility
  - Difficult to put value on due to erratic or no earnings
  - Examples: Microsoft, Cisco Systems, Yahoo!, NVIDIA, SanDisk, Electronic Arts

Types of Stock (cont)

- **Speculative Stocks**: stocks that offer potential for substantial price appreciation, usually due to some special situation such as a new product
  - Companies lack sustained track record of business and financial success
  - Earnings may be uncertain or highly unstable
  - Potential for substantial price appreciation
  - Stock price subject to wide swings up and down in value
  - Examples: Facebook, Sirius XM Radio, Dreamworks Animation, Liberty Media, NitroMed, Under Armour
Types of Stock (cont)

- **Cyclical Stocks**: stocks whose earnings and overall market performance are closely linked to the general state of the economy
  - Stock price tends to move up and down with the business cycle
  - Tend to do well when economy is growing, especially in early stages of economic recovery
  - Tend to do poorly in slowing economy
  - Best for investors willing to move in and out of market as economy changes
  - Examples: Alcoa, Caterpillar, Genuine Parts, Lennar, Brunswick, Timken

Types of Stock (cont)

- **Defensive Stocks**: stocks that tend to hold their value, and even do well, when the economy starts to falter
  - Stock price remains stable or increases when general economy is slowing
  - Products are staples that people use in good times and bad times, such as electricity, beverages, foods and drugs
  - Gold stocks are a form of defensive stock
  - Best for aggressive investors looking for “parking place” during slow economy
  - Examples: Walmart, Checkpoint Systems, WD-40
Types of Stock (cont)

- *One Up on Wall Street* by Peter Lynch
  - The Slow Growers
  - The Stalwarts
  - The Fast Growers
  - The Cyclicals
  - Turnarounds
  - The Asset Plays

Types of Stock (cont)

- Market Capitalization
  - U.S. stock market segments based on stock market capitalization:
    - Small–Cap Stocks: less than $2 billion
    - Mid–Cap Stocks: $2 billion to $10 billion
    - Large–Cap Stocks: more than $10 billion
Investment Strategies

The Passive Strategy
- No over–under valuation, no market timing, minimize costs
- Buy–and–Hold
  - Investors buy high-quality stocks and hold them for extended time periods
  - Goal may be current income and/or capital gains
  - Investors often add to existing stocks over time
  - Very conservative approach; value-oriented
- Index Funds
  - Efficient markets, cost efficient, tax advantage

Investment Strategies (cont)

The Active Strategy
- Security selection
- EPS Critical
- Growth and Value stocks
- Sector rotation
  - Industry momentum
- Market timing
  - Risky. Missing 16 days in 100 years you miss 2/3 of the cumulative returns
Investment Strategies (cont)

- *Accounting for Value* by Stephen Penman
  - One does not buy a stock, one buys a business
  - When buying a business, know the business
  - Price is what you pay, value is what you get
  - Part of the risk in investing is the risk of paying too much
  - Understand what you know and don’t mix what you know with speculation
  - Beware of paying too much for growth
  - Return to fundamentals; prices gravitate to fundamentals (but that can take some time)

Investment Strategies (cont)

- *Expectation Investing* by A. Rappaport & M.J. Mauboussin
  - Investing is a game against other investors
  - Try to understand the forecast that explains the market’s valuation, in order to accept it or reject its asking price
  - Any disagreement is likely to lie in the growth forecast
  - Does the growth forecast look about right?
Investment Strategies (cont)

- **Price/Earnings (P/E) Approach**
  - Future price is based upon the appropriate P/E ratio and forecasted EPS
  - Simple to use and easy to understand
  - Widely used in stock valuation

  \[
  \text{Stock price} = \text{EPS} \times \text{P/E ratio}
  \]

- **Margin Trading**
  - Uses borrowed funds to purchase securities
  - Your currently owned securities used as collateral for margin loan from broker
  - Margin requirements set by Federal Reserve Board
    - Determines the minimum amount of equity required
    - On $5,000 purchase with 50% margin requirement, investor puts up $2,500 and broker will lend remaining $2,500
Margin Trading (cont)

- Advantages
  - Allows use of financial leverage
  - Magnifies profits

- Disadvantages
  - Magnifies losses
  - Interest expense on margin loan
  - Margin calls