FINANCIAL LITERACY I

Investing in the Stock Market

2014 C.A.S.H. Program

INVESTING

For the purposes of simplicity we will only discuss one aspect of Investing and that is Stock Market Investing. There are other forms of Investing including Bond Investing, Real Estate Investing, Mutual Funds Investing, etc. We will only teach the student about investing in the Stock Market. To help the students understand this, we will primarily use the Virtual Stock Exchange Competition throughout the course of the program.

DEFINITION: Stock Market – Is the public or private market for the trading of company stock at an agreed price. These are called "securities" and are listed on a stock exchange as well as those only traded privately. The person buying "shares" of a company's stock become part owner with their purchase.

KEY POINTS OF DISCUSSION:

The U.S. stock market has been the most profitable investment compared with any other type of investment in the last 80 years.

There are 3 major market indices in the U.S. You will typically see media outlets including print, television and online report the results of these three each business day they are open for business.

(1) NYSE (New York Stock Exchange) is the most well known and largest U.S. market exchange. It is also called **DJIA (Dow Jones Industrial Average)** or "**The Dow**". It s located on Wall Street and some of the country's largest companies list their stocks on it (currently over 2000 companies trade here). The NYSE is typically known as the **"large-cap"** exchange. This means companies with market capitalization in excess of $5 billion. This is the index that most profoundly drives the U.S. as well as the world economy on a daily basis and its rise and fall is closely monitored all over the world for a sign into the health of the U.S. economy.

DEFINITION: Market Capitalization – Is a measure of corporate economic

size. It is equal to the company's stock share price multiplied by the total number of shares outstanding. This represents the overall value of the company.

The chart below represents a historical perspective of how the Dow has grown over the last 100+ years.

Note the significant downward dip after 1930—that was the Great Depression, and it is easy to see how a prolonged recession impacted the stock market for a number of years.

Also note the significant expansion during the 1990s. That was the "tech boom", which lasted until about 2001.
The following chart shows the Dow's performance since 2000. Today's recession is evident by the severe drop-off in performance about September of 2008, when Lehman Bros. failed.

What the Dow really is an index of "Averages". It is comprised of 30 companies who represent some of the most important industries in the U.S. economy. The science behind the number is a computed average of the stock prices of those 30 companies which represent various sectors of business. The sum of ALL the stock prices of the 30 companies is only part of the equation. Throughout history, companies as well as whole industries have been added to or removed from the Dow based upon business trends and/ or companies changing over time.

The 30 companies that make up the Dow as of January 2014 are:

Company	Symbol	Industry	Date Added

3M	MMM	Diversified Industrials		1976
American Express	AXP	Consumer Finance		1982
AT&T	T	Telecommunications	1999	
Boeing	BA	Aerospace & Defense	1987	
Caterpillar	CAT	Constructions & Mining Equip.		1991
Chevron	CVX	Oil & Gas		2008
Cisco Systems	CSCO	Computer Communications	2009	
Coca Cola	KO	Beverages: Non-Alcoholic		1987
DuPont	DD	Commodity Chemicals		1935
Exxon-Mobil	XOM	Oil & Gas	1928	
General Electric	GE	Conglomerate		1907
Goldman Sachs	GS	Investment Banks		2014
Home Depot	HD	Home Improvement Retailers	1999	
Intel	INTC	Semiconductors	1999	
IBM	IBM	Computer Services	1979	
Johnson & Johnson	JNJ	Pharmaceuticals	1997	
JP Morgan Chase	JPM	Banking		1991
McDonalds	MCD	Restaurants & Bars	1985	
Merck	MRK	Pharmaceuticals	1979	
Microsoft	MSFT	Computer Software		1999
Nike	NKE	Apparel/Footwear	2014	
Pfizer	PFE	Pharmaceuticals	2004	
Procter and Gamble	PG	Non-durable Household Products	1932	
Travelers Companies	TRV	Property/Casualty Insurance	2009	
United Technologies	UTX	Aerospace	1939	
United Healthcare	UNH	Healthcare		2013
Verizon	VZ	Telecommunications		2004
Visa	V	Financial Services	2014	
Wal-Mart	WMT	Broadline Retailers		1997
Walt Disney	DIS	Broadcasting & Entertainment	1991	

DEFINITION: Capital Gains – Are profits that results from investments into a capital asset such as stocks, bonds, or real estate, which exceeds the purchase price. It is the difference between a higher selling price and a lower purchasing price, resulting in a financial gain for the seller.

(2) The 2nd largest U.S. market exchange where stocks are traded is the **NASDAQ (National Association of Securities Dealers Automated Quotation System)**. It is one of the newest markets and is the largest electronic screen-based equity securities trading market in the U.S. It only began in 1971. It is known as the market for "small-cap" companies—market capitalization of $150-$500 million. This is the stock exchange that has become known for listing high tech, aggressive growth type of companies such as Cisco and Sun Microsystems. Currently over 3,000 companies trade on NASDAQ.

Some of the most well known companies listed on NASDAQ include:

Google (GOOG)
Yahoo (YHOO)
Intel (INTC) – also listed as a component of the Dow, but traded on NASDAQ
Microsoft (MSFT) – also listed as a component of Dow, but traded on NASDAQ
Sun Microsystems (JAVA)
Oracle (ORCL)
Blackberry (BBRY)
Apple (AAPL)
Sandisk (SNDK)
PF Chang's (PFCB)
Cheesecake Factory (CAKE)

Although not all of the companies listed on the NASDAQ are tech stocks, as evidenced by the two restaurants listed above, but it has commonly become known as the tech index.

The chart below shows the historical performance of the NASDAQ. Notice that it is on a different scale compared to the Dow. NASDAQ's all-time high close was only 5,048, on March 10, 2000. What the significance of this? This was the height of the "Tech boom". Also notice the significant hit NASDAQ took after the terrorist attacks of 9/11.

(3) The 3rd major U.S. market index is the **S&P 500 (Standard & Poors 500)**. It was first published in 1957. Stocks are NOT traded on this index as they are with the NYSE and NASDAQ. They are simply listed here. The S&P 500 is truly an index at its truest definition. It comprises the 500 largest cap common stock American companies by market capitalization. It is the second most followed index after the Dow. It is considered a bellwether for the American economy. Mutual funds, pension funds and other investment vehicles all try to mimic the performance of the S&P 500. Many companies and industries compare their own performance to that of the S&P. If you are

doing better than the S&P 500, it means that you are doing better than the 500 largest companies in America, relatively speaking.

The charts below shows the historical performance of the S&P 500. Notice that this index is calculated and appears on a much different scale compared to the Dow or NASDAQ.

There are obviously other important Financial Markets that we will not review due to either their complexity or having little time to get the general concepts across to the students. Some of these include:

AMEX (American Stock Exchange) – mid-market companies
The Bond Market (including the US Savings Bonds)
Chicago Board of Trade, market for futures contracts on commodities such as grains
Global Stock Markets (such as Nikkei in Japan; London Stock Exchange)
Emerging Markets (investing in developing countries such as India or Mexico)

DEFINITION: Bull Market – Tends to be associated with increasing investor confidence, motivating investors to "buy" in anticipation of future price increases and future capital gains.

DEFINITION: Bear Market – Is a steady drop in the stock market over a

period of time. It is described as being accompanied by widespread pessimism. Investors anticipating further losses are motivated to "sell", with negative sentiment feeding on itself in a vicious circle.

Three Key Moments defining a Bear Market in the last 25 years:
Black Monday – October 19, 1987, the largest one day % decline in US stock history
Dot com Bubble Bursting – October 2002 as a result of many tech companies failing
Sub-Prime Mortgage Crisis – October 2007 – 2008, causing the recent recession

INVESTMENT STRATEGIES

Before one invests in ANYTHING, whether its stocks or bonds or commodities or whatever, they should have a specific strategy of what they are looking to accomplish at "that" particular time as well as for the future. Because simply put, investing is done for the LONG-TERM, and should not be done as a "get-rich-quick-scheme". Throughout history, we have seen continuous evidence of those types of investments causing people to lose their entire life savings. Young adults should be especially mindful of this history and avoid these faults. The following represent some of the sound behaviors and habits wise investors make to secure their money for the very long-term.

The basic premise behind stock market investing is "**Buy Low/Sell High**". You want to buy a stock when the price is low and if you do sell, do so when the stock price is very high so that you profit from your investment.

Another strategy to employ is to **balance Risk vs. Reward** investing. The stock market can be highly profitable compared to other types of investments (this is the reward portion); but with this reward there is also a lot of volatility in the stock market, meaning that it can come down just as fast as it went up (this is the risk). Unlike your checking account, which is federally insured, the stock market is almost a total gamble—in particular if you don't have a sound strategy. You need to take several things into consideration such as your age; when you want to retire; how much you will need to retire; your level of risk tolerance, etc.

DEFINITION: Risk Aversion (or Tolerance) – A concept that measures the reluctance of a person to accept a bargain with an uncertain payoff rather than another bargain with a more certain, possible lower, expected payoff. A person who is 'risk-averse' might put their money in the bank with a low but guaranteed interest rate of say 1%; whereas a person willing to take more risk might invest in the stock market (i.e., risk-seeking or risk-loving type of person).

RESEARCH! RESEARCH! RESEARCH! This may actually be the most important (by far) thing an investor can do before making ANY decisions about what to do with their money. The phrase "a fool and his money are soon parted" is never truer than when someone invests their money without doing research into what they are getting into first. This is why MILLIONS of people lost everything they had in Ponzi schemes with Bernie Madoff and Danny Pang, to name just a few.

For starters, you should always investigate the past performance of companies that you want to invest in. And you want to ask yourself SEVERAL questions.
Are they a stable company? Is their industry stable right now?
Have they had major innovations?
Do they have a strong management team?
What are they best known for? Is it good or bad?
Are the under any legal or regulatory investigation?
What are the analysts who monitor them saying about them?
Are they a leader in their industry or are they just sitting on the sidelines?
What do the numbers look like?
How do their customers feel about them?
Are they global in presence?
Are they known for good products and/or services?
Have they been in the news recently? Good, bad or indifferent?

In addition, understand how significant changes in the economy or the industry or the company or single events can have an impact on their stock price. If there is a major oil spill in the Gulf of Mexico, what impact will this have on Exxon Mobil's stock? If Congress steps up and implements laws that provide more consumer protection from credit card companies, how will this impact the banking industry? If we are going more toward a "greener" environment, what impact will this have on the automobile industry? **THESE ARE JUST A FEW OF THE THINGS YOU SHOULD BE ASKING YOURSELF!**

Determine an investment objective and stick to it (within reason, that is – don't stay on a ship that is obviously going to sink); be prepared to revise it just as quickly. This is simply managing your Investment strategy to maximize your objectives. As young adults, you have a minimum of 40-50 years to make investment decisions. Therefore your decisions are going to be somewhat different than those of the generation before you who might only have 20 years or less left in their working lives and thus have to think about their money differently than you.

Almost every single American company operates within industries under one of the following 9 major sectors. Having a "diversified portfolio" is important, but regardless

you should **know your industries and sectors.**

THE 9 MAJOR U.S. BUSINESS SECTORS (with example industries within each)

Basic Materials (Aluminum, Paper, Steel, Oil & Gas, Chemical)
Conglomerates (Diversified Consumer, Commercial, Government Products)
Consumer Goods (Food, Automobiles, Household)
Financial (Retail Banking, Investments, Insurance, Real Estate)
Healthcare (Pharmaceuticals, Medical Services, Biotechnology)
Industrial Goods (Aerospace, Construction, Defense, Textiles, Waste Mngmt.)
Services (Broadcasting, Airline, Lodging, Shipping, Professional Services, Retail)
Technology (Computer Software, Wireless, Telecom, ISP, Semi-conductor)
Utilities (Electricity, Water, Natural Gas, Diversified Utilities)

Determine the types of stocks you want to invest in, as there are several groups of stocks. This depends highly on your level of risk-tolerance as mentioned previously and on things such as historical company performance, news updates, cyclical and non-cyclical trends, among other thins. Here are some examples of how companies stocks are classified.

Blue Chips: the highest quality of all common stocks, traditional stocks, including companies like Coca-Cola or GE or IBM

Growth Stocks: companies that increase their value by growing their earnings, typically smaller companies in rapidly growing industries such as Bio-tech companies or even a Google or Apple.

Value Stocks: companies that focus on hold their value, mostly mature or defensive stocks that are in slow growing phases (i.e., UTC, Alcoa, 3M)

Cyclical Stocks: companies whose earnings fluctuate with business cycles, such as automotive companies like Ford or GM, their stocks depend on the cycles of new car purchases; or John Deere, which depends on the season their equipment is needed.

Income Stocks: These stocks pay a substantial or above-average dividend to investors

DEFINITION: Dividend – A payment made by a corporation to its shareholders. When a publicly traded corporation makes a profit, that money can be put to two uses a) re-invest in the business or paid to shareholders as dividends. Most dividends are paid on a quarterly basis and

are based on the number of shares one owns, along with the previously set price that the company's board has agreed to pay.

Penny Stocks: These are highly speculative stocks, or in other words, have a share price of less than $1. Companies with stock prices in or around this territory are subjects for bankruptcy and/or completely going out of business, if not simply having their stock "de-listed" from the exchange it is traded on. Citigroup was in this territory early in the year

Don't be afraid to **get advice from experts**. In fact, it is strongly encouraged. Just make sure they are reputable and that they have **YOUR** end-goals in mind, not their own or how much money they can make off of you. Use their advice and expertise in combination with all of the previous 6 investment strategies.

ADDITIONAL RESOURCES FOR STUDENTS

OFFLINE
The Wall Street Journal
The Financial Times
Fortune Magazine
Money Magazine
Black Enterprise Magazine
Forbes Magazine
Barron's
ONLINE
HYPERLINK "http://www.bigcharts.com" http://www.bigcharts.com
http://www.marketwatch.com
HYPERLINK "http://finance.yahoo.com" http://finance.yahoo.com
HYPERLINK "http://www.cnnfi.com" http://money.cnn.com/
HYPERLINK "http://www.nasdaq.com" http://www.nasdaq.com
HYPERLINK "http://www.nyse.com" http://www.nyse.com
http://www.fortune.com

PAGE

PAGE 2

PAGE

PAGE 11