

# REWARDS MARKET GUIDES

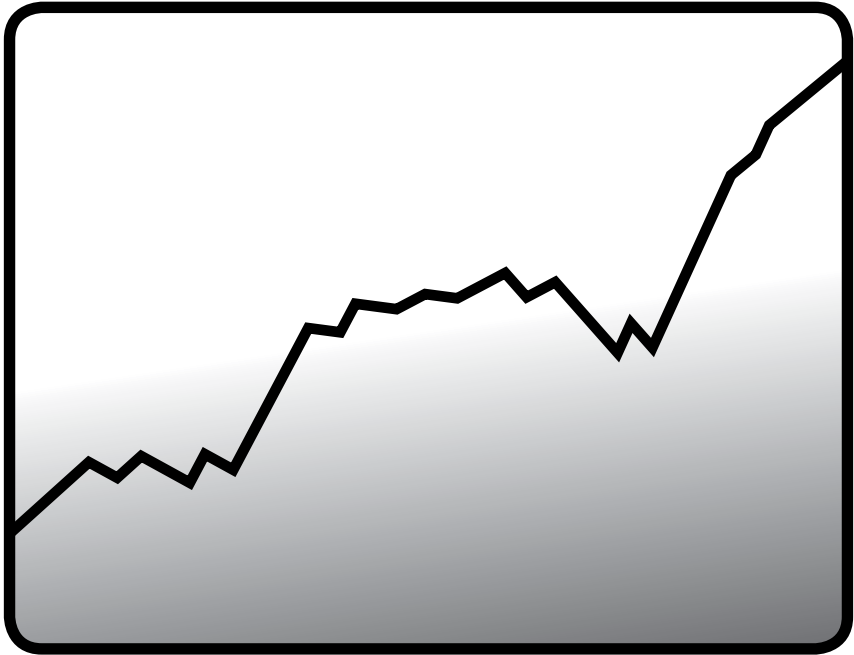


## Part I

### An Introduction To The Stock Market

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## **An Introduction To The Stock Market**

You may be surprised to find that the market is not as difficult to understand as you think. By the time you finish reading this guide, you should have all the basic knowledge you'll need to understand what the stock market is and the basics of how it works. The trick is to learn about the market in small steps, which is exactly what this guide presents to the member.

In the back of this guide you will find a very handy Glossary of commonly used terms in the Stock Market and trading of stocks/shares.

# **The Stock Market: The Biggest Auction in the World**

Think of the stock market as a huge auction or swap meet (some might call it a flea market) where people buy and sell pieces of paper called stock. On one side, you have the owners of corporations who are looking for a convenient way to raise money so that they can hire more employees, build more factories or offices, and upgrade their equipment. The way they raise money is by issuing shares of stock in their corporation. On the other side, you have people like you and me who buy shares of stock in these corporations. The place where we all meet, the buyers and sellers, is the stock market.

## **What Is a Share of Stock?**

We're not talking about livestock! Actually, the word stock originally did come from the word livestock. Instead of trading cows and sheep, however, we trade pieces of paper that represent ownership—shares—in a corporation. You may also hear people refer to stocks as equities or securities. Most people just call them stocks, which means supply. (After all, the entire stock market is based on the economic theory of supply and demand.)

When you buy shares of stock in a corporation, you are commonly referred to as an investor or a shareholder. When you own a share of stock, you are sharing in the success of the business, and you actually become a part owner of the corporation. When you buy a stock, you get one vote for each share of stock you own. The more shares you own, therefore, the more of the corporation you control. Most shareholders own a tiny sliver of the corporation, with little control over how the corporation is run and no ability to boss anyone in the corporation around. You'd have to own millions of shares of stock to become a primary owner of a corporation whose stock is publicly traded.

In summary, a corporation issues shares of stock so that it can attract money. Investors are willing to buy stock in a corporation in order to receive the opportunity to sell the stock at a higher price. If the corporation does well, the stock you own will probably go up in price, and you'll make money. If the corporation does poorly, the stock you own will probably go down in price, and you'll lose money (if you decide to sell it at that point).

## Stock Certificates

Stock certificates are written proof that you have invested in the corporation. (Some people don't realize that you invest in companies, not stocks.) Although some people ask for the stock certificates so that they can keep them in a safe place, most people let a brokerage firm hold their stock certificates. It is a lot easier that way. To be technical, there are actually two kinds of stock, common and preferred. In this guide, we will always be talking about common stock, because that is the only type that most corporations issue to investors. Remember, not all companies issue stock. A company has to be what is called a corporation, a legally defined term. Most of the large companies you have heard of are corporations, and, yes, their stocks are all traded in the stock market. I'm talking about corporations like Microsoft, IBM, Disney, General Motors, General Electric, and McDonald's.

## You Buy Stocks for One Reason

**MONEY!** The stock market is all about making money. Quite simply, if you buy stock in a corporation that is doing well and making profits, then the stock you own *should* go up in price. (By the way, the profits you make from a stock are called *capital gains*, which are the difference between what you paid for a stock and what you sold it for. If you lose money, it is called a *capital loss*.)

You make money in the stock market by buying a stock at one price and selling it at a higher price. It's that simple. There is no guarantee that you'll make money. Even the stocks of good corporations sometimes go down. If you buy stocks in corporations that do well, you should be rewarded with a higher stock price. It doesn't always work out that way, but that is the risk you take when you participate in the market.

## **New York: Where Stock Investing Became Popular**

Before there was a place called the stock market, buyers and sellers had to meet in the street. Sometime around 1790, they met every weekday under a buttonwood tree in New York. It just happened that the name of the street where all this took place was Wall Street. (For history buffs, the buttonwood tree was at 68 Wall Street.)

A lot of people heard what was happening on Wall Street and wanted a piece of the action. On some days, as many as 100 shares of stock were exchanged! (In case you don't think that's funny, in today's market, billions of shares of stock are exchanged every day.)

It got so crowded in the early days that 24 brokers and merchants who controlled the trading activities decided to organise what they were doing. For a fixed commission, they agreed to buy and sell shares of stock in corporations to the public. They gave themselves a quarter for each share of stock they traded (today we would call them stockbrokers). The Buttonwood Agreement, as it was called, was signed in 1792. This was the humble beginning of the New York Stock Exchange (NYSE).

It wasn't long before the brokers and merchants moved their offices to a Wall Street coffee shop. Eventually, they moved indoors permanently to the New York Stock Exchange Building on Wall Street. *(Keep in mind that a stock exchange is simply a place where people go to buy and sell stocks.*

*It provides an organized marketplace for stocks, just as a supermarket provides a marketplace for food.)*

Even after 200 years, the name Wall Street is a symbol for the U.S. stock exchanges and the financial institutions that do business with them, no matter what their physical location. If you go to New York, you'll see that Wall Street is just a narrow street in the financial district of Lower Manhattan. Therefore, the stock market, or Wall Street, is really just a convenient way of talking about anyone or anything connected to the financial markets.

## **Major Stock Exchanges**

After the NYSE was formed, there were also brokers trading stocks who weren't considered good enough for the New York Stock Exchange. Traders who couldn't make it on the NYSE traded on the street curb, which is why they were called "curbside traders". Eventually, these traders moved indoors and established what later became the American Stock Exchange (AMEX was purchased by NYSE in 2008).

In the US, there is also a second major stock exchange, the National Association of Securities Dealers Automated Quotation System (NASDAQ), which was created in 1971. This was the first electronic stock exchange; it was hooked together by a network of computers. (Yes, they did have computers back then.)

Competition is good for the stock market. It forces the stock exchanges to fill your orders faster and more cheaply. After all, they want your business. There are stock exchanges in nearly every country in the world, although the U.S. market is the largest. Other countries with stock exchanges include England, Germany, Switzerland, France, Holland, Russia, Japan, China, Sweden, Italy, Brazil, Mexico, Canada, and Australia, to name only a few. See the next page for the top Stock Exchanges in the world.

# **Top World Stock Exchanges 2010**

(in order of Market Capitalization)

1. NYSE (US)
2. NASDAQ (US)
3. Tokyo Stock Exchange (Japan)
4. London Stock Exchange (UK)
5. Shanghai Stock Exchange (China)
6. Hong Kong Stock Exchange (HK)
7. Toronto Stock Exchange (Canada)
8. Bombay Stock Exchange (India)
9. National Stock Exchange of India (India)
10. BM&F Bovespa (Brazil)
11. Australian Securities Exchange (Australia)
12. Deutsche Börse (Germany)
13. Shenzhen Stock Exchange (China)
14. SIX Swiss Exchange (Switzerland)
15. BME Spanish Exchanges (Spain)
16. Korea Exchange (S. Korea)
17. MICEX (Russia)
18. JSE Limited (South Africa)

# **Joining a Stock Exchange**

It's not easy for a corporation to be listed on, or join, a stock exchange because each exchange has many rules and regulations. It can take years for a corporation to meet all the requirements and join the exchange. The stock exchanges list corporations that fit the goals and philosophy of the particular exchange.

For example, the companies that are listed on the NYSE are some of the best-known and biggest corporations in the United States; blue-chip corporations like Wal-Mart, Procter & Gamble, Johnson & Johnson, and Coca-Cola. The NASDAQ, on the other hand, contains many technology corporations like Cisco Systems, Intel, and Sun Microsystems. In addition, stocks that are traded "over the counter" (OTC) are located on the NASDAQ.

## **Corporations: Convincing People to Buy Their Stock**

Once a corporation goes public and allows its stock to be traded, the trick is to convince investors that the corporation will be profitable. Corporations do everything in their power to attract money from investors. Bigger corporations spread the word through print and television advertising. Smaller corporations might rely on word of mouth, e-mail, or press releases. The more people there are who believe in a corporation, the more people there will be who will buy its stock, and the more money the people on Wall Street will make.

# Glossary of Market Terms

## **Advanced Computerized Execution System (ACES)**

This is the service offered by NASDAQ to broker-dealers to automatically perform internal transactions and process the records appropriately.

## **After Hours Trading**

Trading on normal currencies after normal trading hours.

## **Arbitrage**

This is transacting to profit between two or more markets by taking advantage of the difference in prices in the similar markets.

## **Ask**

This is the price which a trader can buy a currency offered for sale.

## **Attain ECN (ATTN)**

This is a broker-dealer that specializes on direct access electronic trading.

## **Auction Market**

This is the market where buyers and sellers compete to buy and sell currencies respectively.

## **Back testing**

This means analyzing the history of the investment opportunity provided and comparing with the present trends to see how successful (if successful) the investment would be.

## **Bear Market**

This is the period when the declines in prices of individual securities or assets have fallen for a long time.

## **Best Ask**

This is the lowest price of a security or asset which a seller can accept at a particular time.

## **Best Bid**

This is the highest price of a security or asset which a buyer can give at a particular time.

## **Beta**

This term is used to note how volatile or how risky an investment on a security might be when compared to the overall market.

## **Bid**

This is the price one is offering on stocks or commodities.

## **Big Board**

This is the major indigenous stock exchange company in the US, responsible for overseeing the activities in the stock exchange operations.

## **Block Trade**

This is the transaction of a very large amount of shares (typically 10,000 or more) worth at least \$200,000.

## **Blue Chip**

These are stocks that are seen as less volatile. Their investments are considered to be more profitable.

## **Book Value**

This is the value of a company if assets and common stock equity are added together and all liabilities are subtracted. There is little correlation between the book value and the market value. Book value is used in such fundamental analysis measurements as Price to Book ratio.

## **Broker / Dealer**

This is an individual or a company that trades on securities. The individual or company can also perform the actions of a broker or a dealer.

## **BRUT ECN**

An Electronic Communications Network owned by Brut.

## **Bull market**

This is a market where prices of securities have risen for a long time without returning to the normal prices.

## **Circuit Breakers**

This refers to the procedures/measures that are employed to halt trading on all US stock markets for a particular period of time.

## **Close Position**

This means buying back a stock to prevent a reversal of price trend which may have been observed in the stock market.

## **Consolidated Quote System (CQS)**

This is the service delivered by NASDAQ informing its subscribers on quotations of stocks traded on the regional stock exchanges in the US.

## **Common Stock**

This is the security owned by investors to seal their participation in owning a company.

## **Crossed Market**

This is the case when the bid price of an asset or stock is greater than the ask price.

## **CUSIP**

Committee on Uniform Security Identification Procedures.

## **Day Order**

An order, if not transacted on the day it was placed would get expired.

## **Day Trading**

This refers to the transactions that are made and within the same trading day before close of trade for the day.

## **Depth of Market**

This is the amount of assets or commodities that can be transacted without a large difference in price change at the end of trading.

## **Derivative**

This is an asset/commodity that gets its value from another asset/commodity.

## **Diversification**

This is the method of spreading investments within a portfolio to reduce the risk of losing within a portfolio.

## **Dividend**

This refers to the profits issued by companies to their share holders.

## **Dollar Cost Averaging**

This means buying stocks bit by bit over a long period of time.

## **Downtick**

This is normally experienced when a current transaction price falls below the initial transaction price.

## **Dow Jones Industrial Average**

This is a compilation of the 30 most traded blue chip stocks. This list is the most widely used for analyzing stock market indexes.

## **Dow Theory**

This theory states that the market appreciates if one of its averages goes above a previous important high.

## **ECN**

It is designed to facilitate trading of stocks and currencies.

## **Fill or Kill (FOK)**

This is an order made on a large amount of stocks. It is either that the transaction to be made will be made completely or it will not be made at all.

## **Firm Quote**

This is a non negotiable price of a security made by a market maker on not more than 100 shares.

## **Floor**

This is the medium whereby bids and offers are made by traders.

## **Floor Trader**

This is a registered competitive trader who understands the rules of a stock/commodities exchange for his own account.

## **Front Running**

This happens when a broker trades based on the information obtained from the analyst department before the clients (of the broker) receives the information.

## **Fundamental Analysis**

This means understanding the overall state of a business company. Factors that may be looked into are earnings and productions made by the company.

## **Gap**

This simply refers to the break between prices.

## **Good-'Til-Cancelled Order (GTC)**

This is an order to invest in a security which does not close until the conditions/ requirements for executing the order are met.

## **Hedging**

This is the method of buying or selling the same amount of securities, almost at the same time, in two different markets.

## **Imbalance of Orders**

This is used to describe the event when buy orders exceed sell orders.

## **Initial Public Offering (IPO)**

This is the first sales of stock by a private company that want to become publicly owned, so that they can expand.

## **Inside Market**

This is the market maker spread. It shows the highest bid quoted and the lowest price offered.

## **Instinet ECN (INCA)**

This is the first medium brokerages had to display bid and ask prices for most stocks in North America.

## **Joint Account**

This is any an account that is operated by more than one person.

## **Level I**

This is beginner trader who does not trade with real money.

## **Level II**

This is an advanced beginner. He trades with real money but at a minimum risk.

## **Level III**

This is a competent trader. He can trade on a more professional level.

## **Limit Order**

A price set by an individual to buy or sell a stock. Above or below this price, the trader is neither willing to buy nor sell securities or stocks.

## **Liquidity**

This is the ability of a trader to convert his assets to cash in a fast way.

## **Margin**

This is a collateral willing to be issued by a trader to a broker when he wants to borrow funds.

## **Margin Account**

This is the account a trader must own in order to qualify for borrowing funds.

## **Margin Call**

This is the call made by a broker to his clients when he observes that the securities bought from the borrowed funds have decreased in value. This call is normally made to tell the trader to add more money to his account.

## **Market Capitalization**

A company's market capitalization, also known as its market cap, is calculated by taking the number of outstanding shares of stock multiplied by the current price per share.

## **Market Maker**

This is a broker-dealer firm that facilitates the trade of a particular security by dealing on a large amount of them.

## **Market Order**

This is also called unrestricted order. It is the order that guarantees the execution of a trade.

## **Market Timing**

This is the process of predicting future price movements of stocks or securities.

## **Momentum Investing**

This means buying stocks that have been profitable around 3-12 months ago and selling off stocks that have not been profitable around the same time period (3-12 months ago).

## **NASDAQ**

This is the largest electronic screen based securities trading market in the US which originally stood for "National Association of Securities Dealers Automated Quotations".

## **New York Stock Exchange (NYSE)**

This is the largest equities-based exchange in the world.

## **Odd Lot**

This refers to stock that is less than 100.

## **Odd Lot Theory**

This states that if odd lot investors are selling, it is likely that buying such stocks at that time will be a profitable venture.

## **OptiMark**

This is a company that owns patents and intellectual properties and also has its own securities exchanges.

## **Overbought**

This means that the price of an asset has risen to a very high value within a short period of time.

## **Oversold**

This means that the price of an asset has fallen to a very high value within a short period of time

## **P/E Ratio**

This widely used analysis tool of Price to Earnings ratio measures how you pay for each dollar of corporate earnings. For example, if you have \$30 stocks that report a profit of \$2 per share, your P/E ratio is 15; \$30 per share divided by \$2 earnings per share equals 15. In this ratio the lower the P/E ratio, the better.

## **Paper Trading**

This is the practice made by potential investors when they start learning how to trade stocks.

## **Pink Sheets**

This is another way of referring to over the counter trading.

## **Preferred Stock**

These are stocks owned by those higher than the ordinary share holders of a company.

## **Program Trading**

This is the method used to take advantage of arbitrage possibilities. It occurs automatically when created.

## **Qualitative Analysis**

This means understanding the qualities of a company.

## **Quantitative Analysis**

This means measuring the strength of financial instruments and institutions.

## **Random Walk Theory**

This states that the prices of stocks in the market cannot be predicted.

## **Regulation T**

This is the regulation done by a Federal Reserve Board to control customer cash accounts and the issuance of credit to customers by brokers to purchase securities.

## **Round Lot**

This is 100 shares of stock.

## **SEC Fee**

This is an additional fee implemented by the Securities Exchange Act of 1934 for stock traders. They are paid into the brokers' account from where the sum is collected and remitted to the US treasury.

## **SEC Order Handling Rules**

This consists of the limit order display rule and the quote rule.

## **Sell-side**

This refers to a firm that sells securities and offers investment services.

## **Settlement Date**

This is an agreed date between the buyer and the seller when transactions must be made complete by effecting payments for securities bought.

## **Sharpe Ratio**

This is the value of the excess return per unit of risk in any trade or investment.

## **Short Sale**

This means selling borrowed stocks from a broker to take advantage of the falling prices of the stocks in the market.

## **Short Squeeze**

This is an upward price of stocks caused by lack of supply and over demand of stocks in the market.

## **Specialist**

This is a person who tries to narrow the gap that may be experienced when the market maker is not available.

## **Spiders (SPDR)**

SPDR means Standard and Poor's Depository and Receipt. They are traded under the symbol SPY just like other American stock exchanges.

## **Spread**

This is the difference in value between the bid and the ask price of a commodity/stock.

## **Stock**

This is the smallest measurable unit of ownership in a company. Shares fall into either the common or preferred categories; companies issue shares of stock in order to raise capital without borrowing money. Investing terms – These words and phrases reflect stock market terms for various stock market strategies. These stock market terms are used to describe specific conditions or analysis.

## **Stock Symbol**

This refers to letters used to represent stocks for trading purposes. The numbers of the letters vary among different stock exchanges. These letters are used for security purposes.

## **SuperDot**

This is an electronic system used on the New York Stock Exchange to place orders of listed stocks.

## **Systematic Risk**

This is the risk possessed on an individual which cannot be reduced by diversification.

## **Technical Analysis**

This means understanding the price movement of securities in the market.

## **Trading Halt**

This refers to the period when trading is stopped. Its normal duration is around 30 minutes.

## **Trin**

This is a tool used to indicate the presence of volume in the market.

## **Triple Witching Hour**

This is the final trading hours on the third Fridays of March, June, September and December.

## **Uptick**

This is the case when the current transaction price is above the initial transaction price.

## **Volatility**

This is the measure of the daily changes in the price of securities.

## **Volume**

This is the number of shares that are available to be traded in the market at a particular period and time.

## **Wash Sale Rule**

It states that an investor should not claim a capital loss for tax purposes as long as the capital was repurchased within 30 days.

## **Yield**

This is the percentage of a dividend paid against the stock price. For example, if you receive a \$3 dividend on a \$30 per share stock, your yield is 10%.

## **Zero-Sum Game**

This is the case when someone only gains when another investor losses.