Choosing Your Companies

Suggested Time

50 minutes

Background

A stock's price not only reflects a company's current value -- it also reflects the investor's expectations of future growth and earnings. It is an indication of what investors believe a company is worth.

There are two general schools of stock analysis: Technical and Fundamental. Technical Analysis seeks to identify the patterns in a stock's price changes by examining charts of its past performance. Fundamental Analysis also looks at a stock's price changes but includes a lot of additional factors that may or may not make that stock a good investment.

For example, market forces such as supply and demand impact share prices. If more people want to buy a stock (demand) than sell it (supply), then the price goes up. Conversely, if more people wanted to sell a stock than buy it, supply exceeds demand and the price falls.

News events working in conjunction with public opinion also cause stock prices to rise and dip. Reports on internal corporate activity, industry trends, and national/international events (e.g. political, social and scientific news) are interpreted as either "good" or "bad" news by the public, who in turn determine whether a company is a good investment or not.

Fundamental data such as P/E ratios and projected earnings help investors place a value on a stock. Public companies must report their earnings four times a year (once each quarter). "Wall Street" carefully watches earnings results. Analysts base their opinions about future value of a company on its earnings projections. If a company's results are better than analysts expected, the stock price rises. If a company's results are worse than expected the stock price falls.

Investors have developed literally hundreds of variables, ratios and indicators to predict stock price changes. The main forms of stock analysis are: fundamental, technical and quantitative. Each approach involves following various market indicators to decide whether to buy, sell, or hold a stock.

Vocabulary

Earnings: Whatever profits or net income remains after subtracting the company's expenses from its revenue (also called a company's profit).

Fundamental Analysis: A primary method for analyzing a stock's potential return. It involves assessing a corporation's financial history and current standing, including earnings, sales, and management, as well as the strength of the corporation's products or services in the marketplace.

Inflation: An increase in the general level of prices of goods and services.

Market Capitalization: A measure of the value of a company, calculated by multiplying the number of outstanding shares by the current price per share. For example, a company with 100 million shares of stock outstanding and a current market value of $25 a share has a market capitalization of $2.5 billion.

P/E Ratio: A company's closing price divided by its latest annual earnings per share. The Price / Earnings is the relationship between a company's earnings and its share price. It is calculated by dividing the current price per share by the earnings per share.

Quantitative Analysis: Analysis focused on a corporation's financial data including looking at profit-and-loss statements, sales and earnings histories and the statistical state of the economy.

Technical Analysis: Tracking price movements and trading volumes in various securities to identify patterns in the price behavior of particular stocks, mutual funds, commodities, or options in specific market sectors or in the overall financial markets.

Performance Objectives

Students will be able to:

- Discuss the various ways stock prices are influenced.
- Interpret charts and graphs to better understand the growth and change in stock prices.
- Analyze and interpret market indices, which influence change in the price of stock.

Materials

Challenge 1: Comparing Stock Quotes
Challenge 2: What is a Good Company?

Procedure

Group your students into their SMG teams and engage them in Challenge 1: Comparing Stock Quotes. Encourage your students to consider the volume (number of shares traded) and numbers of Shares Outside (number of shares available to publically trade). If a stock has a high volume does it mean its price is unstable? Or the company is unstable? If the company has a lot of shares outstanding does that mean it is harder for its management to make decisions that could potentially earn money for the company? Using only the information presented in the Challenge ask each team to choose the company they believe is a good investment. They should provide three reasons for their decision that can be supported by facts.

Afterwards, ask the students to view the historical quotes for both companies from 2012 to present. How would they describe the performance of each company? Do the price histories of the stocks make a difference in how they feel about the companies as good investment? Why? Why not?

After some discussion, proceed to Challenge 2:What is a Good Company?

