

The Stock Exchange Corner

More Frequently Asked Questions

by George Edwards

Last week we gave you another set of Frequently Asked Questions (FAQs). This week we give you a final instalment of FAQs and answers which can also be viewed on our website: www.gasci.com for those with access to the internet.

Frequently Asked Questions (FAQs) - continued

How are stocks and shares valued?

Common stocks represent a share in the ownership of a company and their value mainly depends on the level of profits. Bonds represent debts owing by a company and their value mainly depends upon financial strength.

Bonds – which are documents acknowledging a debt by the issuer of the bonds to the holders of the bonds - are valued by reference to the rate of interest paid to the holders of the bonds. The Government can raise money at the lowest rate of interest; publicly owned bodies may have to pay a little more and private borrowers have to pay more again, depending on their creditworthiness and the size and liquidity of the issue. In other markets good quality corporate bonds can have an interest rate about one percent more than a government bond (meaning that if the Government is borrowing at 5%, a good corporate issuer may borrow at 6%)

Shares – which represent part ownership of a company – are usually valued partly by reference to the dividend they pay (which is comparable with the interest received on a bond) and partly by reference to the profits earned by the company and available to pay dividends or to be reinvested by the company in fixed or working capital.

For both bonds and shares, the income is measured by the “yield” and for shares the profit is measured by reference to the “price earnings ratio”.

Other measures that affect valuation of shares are “cash flow” and “asset value”

What makes the price of common stocks and bonds go up and down?

The stock market rises and falls with investor confidence.

What are the benefits of owning stocks?

It gives the investor an opportunity to participate in the success of a company through increasing dividends or increasing asset value.

What risks are involved in owning common stocks?

The risk that the companies who have issued the stocks are unsuccessful or, ultimately, insolvent, in which case the value of the common stock may be nil, In addition the price of common stocks is relatively volatile, moving up and down with the market.

What makes the price of bonds go up and down?

Bond prices rise and fall with interest rates, partly on changes in inflation expectations and partly on the supply and demand for credit.

What are the benefits of owning bonds?

A relatively secure and predictable monetary return in the form of interest and/or repayment at a premium over the cost of purchase. The price of bonds is relatively more stable than of common stocks.

What risks are involved in owning bonds?

Default in the payment of interest and/or the repayment of capital.

What are the risks of investing on the stock market?

The price of stocks and shares can go down as well as up.

Who can use the market?

Only brokers and dealers who are both registered with the GSC and who are members of GASCI are permitted to trade directly on the stock market, but anyone may place an order with a broker dealer to buy or sell stocks and shares.

How can you buy or sell securities on the Exchange?

Go to a registered broker, licensed by GASCI.

What does a limited service broker do?

A limited service broker executes transactions on behalf of investors, but does not provide advice or other ancillary services.

What does a broker/dealer do?

A broker dealer carries on business both as an agent for his customers and as a principal for his own account.

How are securities paid-for on the Exchange?

The buyer of a security pays his broker who pays the seller's broker who pays the seller; at the same time, the seller passes evidence of ownership to his broker who passes it to the buyer's broker who passes it to the buyer. It is good practice for payment of money to be matched by transfer of ownership at each stage.

When does trading take place on the Exchange?

Initially once a week during a short trading session; in the future it will be continuous between brokers' offices

At present, trading takes place on Mondays at 10.00 a.m. or on Wednesdays when Monday is a public holiday.

What about private deals outside the market?

Private deals are permitted but they are subject to stamp duty which makes them more expensive than trading on the Exchange.

Next week: Glossary of Terms used in the industry

N.B. – More information may be accessed on our website: www.gasci.com