THINK CRITICALLY

Handwrite your responses in the space below; 2 sentences each.

1. What factors are commonly considered when evaluating a company's stock?

2. What are the advantages of investing in mutual funds?

3. What factors affect bond prices?

4. When a company changes the number of shares of stock to bring the current market price down, this is called _____
   a. selling short
   b. an initial public offering
   c. a stock split
   d. a mutual fund

5. An investment that allows a person to own a variety of companies is called _____
   a. a corporate bond
   b. preferred stock
   c. a mutual fund
   d. a municipal bond

6. True or False? _____Only discount brokers allow investors to buy and sell stocks online.

7. True or False? _____As interest rates rise, bond prices tend to rise.

8. A person interested in current income would select a mutual fund emphasizing _____
   a. technology stocks
   b. dividends
   c. long-term growth
   d. foreign government bonds

9. The yield to maturity of a bond would be highest when the bond is _____
   a. sold at a discount
   b. sold at a premium
   c. sold at par
   d. tax deductible

TEAMWORK

Discuss in pairs or small groups and then write your conclusions below.

10. Discuss various business and economic trends. Prepare a list of stocks which your group believes would be good investments. Explain what factors influenced the selection of these companies.

Mr. Market

by Ben Graham

Imagine you are partners in a private business with a man named Mr. Market. Each day, he comes to your office or home and offers to buy your interest in the company or sell you his [the choice is yours]. The catch is, Mr. Market is an emotional wreck. At times, he suffers from excessive highs and at others, suicidal lows. When he is on one of his manic highs, his offering price for the business is high as well, because everything in his world at the time is cheery. His outlook for the company is wonderful, so he is only willing to sell you his stake in the company at a premium. At other times, his mood goes south and all he sees is a dismal future for the company. In fact, he is so concerned, he is willing to sell you his part of the company for far less than it is worth. All the while, the underlying value of the company may not have changed - just Mr. Market's mood.

The best part of this entire arrangement: you are free to ignore him if you don't like his price. The next day, he'll show up at your door with a new one. For your interest, the more manic-depressive he is, the more opportunity you will have to take advantage of him [don't worry, he doesn't have feelings or mind being taken advantage of.] As long as you have a strong conviction of what the company is really worth, you will be able to look at Mr. Market's offers and reject or accept them... the choice is yours.

This is exactly how the intelligent investor should look at the stock market - each security that is traded is merely a part of a business. Each morning, when you open up the newspaper, go online, or turn on CNBC, you can find Mr. Market's prices. It is your choice whether or not to act on them and buy or sell. If you find a company that he is offering for less than it is worth, take advantage of him and load up on it. Surely enough, as long as the company is fundamentally sound, one day he will come back under the sway of a manic high and offer to buy the same company from you for a much higher price.

By thinking of stock prices in this way - as mere quotes from an emotionally unstable business partner - you are free from the emotional attachment most investors feel toward rising and falling stock prices. Before long, when you are looking to buy stock you will welcome falling prices. The only time you want to invite high stock prices is when you are eager to sell your securities for some reason. Thankfully, in most cases, you are free to wait out Mr. Market's emotional roller coaster until he offers a price that you consider equal to or higher than intrinsic value. This is perhaps your greatest advantage in your investments.

Questions for Discussion *(use space provided; 2 sentences each)*

1. Who is “Mr. Market”? Explain.

2. What is the purpose of using Mr. Market when thinking about investing?

3. What’s your opinion? Is the “Mr. Market” metaphor helpful? Explain.

Debt, Equity, and Retained Earnings

REVIEW PACKET

1. **Sources of Capital.** There are three main sources of capital for any business. List what they are; provide a definition of each in your own words; and then give the advantages and disadvantages of each.

Source of Capital	Definition	Advantages & Disadvantages
A.		ADV 1
		ADV 2
		DIS 1
		DIS 2
B.		ADV 1
		ADV2
		DIS 1
		DIS 2
C. Retained Earnings		ADV 1
		DIS 1

2. **Where on the Balance Sheet?** Using the balance sheet shown to the right, answer the questions below.

   A. What types of **short-term debt** financing has this company used?

   B. What types of **long-term debt** financing has this company used?

   C. What are the **payments** called that this company will have to make on their debt?

   D. What other types of financing has this company used to grow? (Hint: there are 3 additional types of financing used other than debt)

BALANCE SHEET
(dollars in thousands)

ASSETS	
Current Assets	
Cash and Cash Equivalents	5,000
Accounts Receivable	4,000
Inventory	7,000
Other Current Assets	1,000
Total Current Assets	**17,000**
Property, Plant, and Equip.	22,500
Other Assets	500
Total Assets	**40,000**
LIABILITIES	
Current Liabilities	
Accounts Payable	4,000
Bank Line of Credit	1,000
Commercial Paper	2,000
Total Current Liabilities	**7,000**
Mortgage Bonds	10,000
Debenture Bonds	1,500
Total Liabilities	**18,500**
STOCKHOLDERS' EQUITY	
Preferred Stock	1,500
Common Stock	14,000
Retained Earnings	6,000
Total Stockholders' Equity	**21,500**

3. **Case Studies.** For each of the case studies below, imagine that you are an investment banker advising the companies. Indicate which source of capital would be most appropriate and explain why you feel this is so. Be specific with your reasons!

   Less Is Moe, Inc., would like to expand soon. The plan is to build another plant in a nearby city. Less Is Moe's financial position is excellent. While it is highly profitable, it does not have enough profit available for capital investment. It has little debt. Its tax liabilities are very high. The company does not want to give up any additional control.

   Moe's Mulching, Inc., is in a strong financial position. Summer is coming – a time when Moe's business makes most of its money. Moe would like to buy another truck and hire a few more workers. He just needs some money for a few months for operating costs-working capital. The company will earn more than enough in the summer to pay it back.

   Moe Money, No Problems, Inc., was originally a family-run business; it went public several years ago. At the time, Moe's family wanted to open operations in several cities. Now they have many locations throughout the Midwest. Those expansions were funded by corporate bonds. The family still owns 70 percent of the stock. Although the company has not shown a profit for the last two quarters, its financial condition is not critical; but more debt could strain the already strained cash flow. Moe's family would prefer to maintain their image of a growing, prosperous firm. They need money for modernization of their kitchens to meet environmental protection laws and to become more efficient.