

Assignment 5

1. Which type of stock could help you obtain your investment and financial goals? Justify your choice?

As a risk-averse investor who still wants to make apparent profits, I would diversify my portfolio and would invest in many types of stock from various sectors of an economy. I would invest in growth stocks to increase expected returns of the portfolio in terms of capital gains, while also invest in blue-chip and income stocks to diversify risk probability and to gain from dividend payments. I would be investing in stocks from different sectors to reduce the market risks. If one of the sectors faces some difficulties, the expected returns of my portfolio would not be affected by large.

2. Explain the relationship between earnings and a stock's market value.

The relationship between earning and a stock market value is one of the fundamental analysis on how the stock is valued. However, high earnings do not guarantee high market value, but it is still a major factor to consider when evaluating the stock's price. The direct relationship between a stock's price and its earning is Price-per-earning ratio, or P/E. It determines an amount an investor must invest to get a dollar/unit of that company's earnings.

3. What is the difference between the primary market and the secondary market?

Primary market is where a company issues their new stocks and bonds for the first time. These issues are in the form of an initial public offering (IPO). Buyers from the market are mostly large institutional investors who have abilities to buy large amount of securities at once.

Secondary market is where securities are traded after a company has sold all their securities on the primary market. Any investors can trade in this market.

4. Calculating Total Return. Tammy Jackson purchased 100 shares of All-American Manufacturing Company stock at \$31.50 a share. One year later, she sold the stock for \$38 a share. She paid her broker a \$28 commission when she purchased the stock and a \$42 commission when she sold it. During the 12 months that she owned the stock, she received \$160 in dividends. Calculate Ms. Jackson's total return on this investment.

Cost when purchased		Return when sold	
100 shares @ \$31.50	- \$3,150	100 shares @ \$38	- \$3,800
Plus, commission	+28	Minus, commission	-42
<u>Total investment</u>	<u>\$3,178</u>	<u>Total return</u>	<u>\$3,758</u>

Transaction Summary

Total return	\$3,758
Minus total investment	<u>-3,178</u>
Profit from stock sale	\$580
Plus dividends	<u>+160</u>
Total return of the transaction	\$740