

# FN312 Investment Lecture 2

## How Securities are Traded

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# Outline

- **How firms issue securities**
  - Primary vs. secondary market
  - Privately held vs. publicly traded companies
  - Initial public offerings
- **Market transactions**
  - Short selling and buying on margin
- *Rise of electronic trading and globalization of stock markets\**
- *Market regulation\**

**Reading:**  
Chapter 3

# How Firms Issue Securities

# How Firms Issue Securities

- *Primary Market*

- Market for newly-issued securities
- Firms issue new securities through underwriter to public

- *Secondary Market*

- Investors trade previously issued securities among themselves



## Issue Outstanding : 2.1 Long-term Corporate Bond

Export to Excel

ThaiBMA Symbol	Local Issue Rating		International Issue Rating				Coupon Type	Coupon Rate (%)	Issue Date	Maturity Date	TTM (Yrs.)	Outstar Value (TH
	TRIS	Fitch (Thaila...	Moody's	S&P	Fitch Ratings	R&I						
A201A							Fixed Coupon	5.250000	31-Jan-2017	31-Jan-2020	0.42	
A204A							Fixed Coupon	5.950000	05-Apr-2017	05-Apr-2020	0.60	
A200A							Fixed Coupon	5.400000	05-Oct-2016	01-Oct-2020	1.09	
A214A							Fixed Coupon	5.950000	31-Oct-2017	30-Apr-2021	1.67	
A214B							Fixed Coupon	5.950000	31-Oct-2017	30-Apr-2021	1.67	
A210A							Fixed Coupon	6.050000	19-Oct-2018	19-Oct-2021	2.14	
A210B							Fixed Coupon	6.750000	01-Apr-2019	08-Oct-2021	2.11	
A222A							Fixed Coupon	6.050000	22-Nov-2018	22-Feb-2022	2.49	
ABPSPV204A	A-						Fixed Coupon	2.680000	21-Apr-2017	21-Apr-2020	0.65	
ABPSPV214A	A-						Fixed Coupon	3.000000	21-Apr-2017	21-Apr-2021	1.65	

1 2 3 4 5 ... 10 items per page

1 - 10 of 1629 items

# How Firms Issue Securities

- Privately Held Firms
  - Up to 499 shareholders
  - Raise funds through *private placement*
  - Lower liquidity of shares
  - Fewer obligations to release financial statements

# How Firms Issue Securities

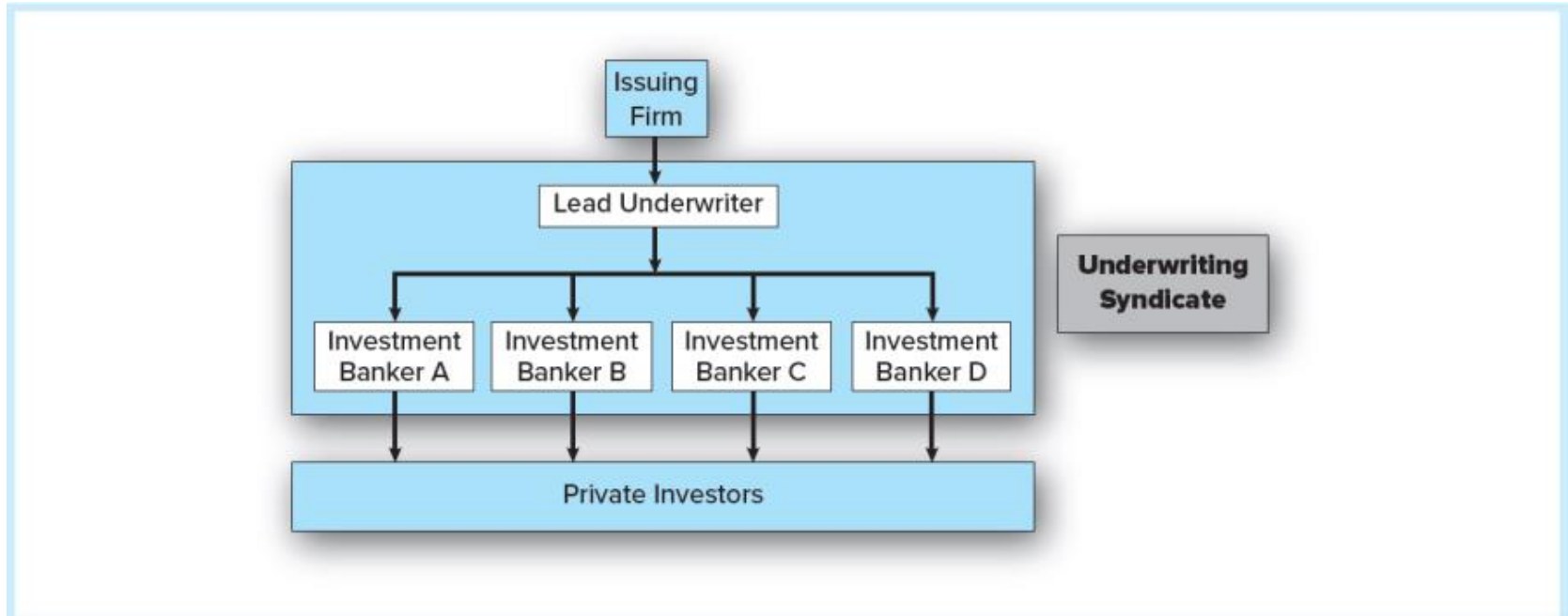
- Publicly Traded Companies
  - Public offerings are marketed by *underwriters*
    - *Initial Public Offering:*  
.....
    - *Seasoned equity offering:*  
.....
- Registration must be filed with the SEC

# How Firms Issue Securities

- Shelf Registration

- *SEC Rule 415*: Allows firms to register securities and gradually sell them to the public for two years
- Shares can be sold on short notice and in small amounts without incurring high floatation costs

# Relationship Among a Firm Issuing Securities, the Underwriters, and the Public



**Figure 3.1** Relationships among a firm issuing securities, the underwriters, and the public

**A214B : AMORTIZED DEBENTURES OF AREEYA PROPERTY PUBLIC COMPANY LIMITED NO. 3/2560 SERIES 2 DUE B.E.**

Symbol	A214B	Registration Date	31 October 2017			
Issuer	<a href="#">AREEYA PROPERTY PUBLIC COMPANY LIMITED</a>	Name (Thai)	หุ้นกู้ชนิดทยอยชำระคืนเงินต้นของบริษัท อารีญา พรอพเพอร์ตี้ จำกัด (มหาชน) ครั้งที่ 3/2560 ชุดที่ 2 ครบกำหนดไถ่ถอนปี พ.ศ. 2564			
ISIN Code (Local)	TH0770A31401	Put/ Call Option	-			
ISIN Code (Foreign)		Collateral	-			
Bond Type	[ Senior ][ Unsecured ][ Amortizing Issue ]	Payment Frequency	Quarterly			
Initial Par	THB 1,000.0000	Calculation Method	Actual/365			
Current Par	THB 850.0000	Issue Term (Year)	3.5 Yrs.			
Issue Size	THB 208.10 mln.	Issue Date	31 October 2017			
Outstanding Size	THB 176.88 mln.	Maturity Date	30 April 2021			
Distribution	Private Placement to 13 types of institutional investors plus high net worth investors	Prospectus	<a href="#">↓</a> <a href="#">🔍</a>			
Issue Rating	Rating Agency		Issue Rating		Rating Date	
Issuer Rating	Issuer Name	Rating Agency		Issuer Rating	Rating Date	
	A	Local	TRIS	BB	9 Jan 2019	
Guarantor Rating	Guarantor Name		Rating Agency		Guarantor Rating	
Coupon Payment	Reference			Max.	Min.	To
	Fixed: 5.950000%					31 Oct 2017 30 Apr 2021
Amortized Schedule	Coupon Date		Principal Amount			
	31-Oct-2018		150.000000			
	31-Oct-2019		150.000000			
	31-Oct-2020		150.000000			
	30-Apr-2021		550.000000			
Registrar	CIMB THAI BANK PUBLIC COMPANY LIMITED		Debenture Holder Representatives		-	
Lead Underwriter(s)	CAPITAL NOMURA SECURITIES PUBLIC COMPANY LIMITED		Financial Advisor(s)		-	


**ThaiBMA**

# How Firms Issue Securities

- Initial Public Offerings

- Road shows to publicize new offering
- Bookbuilding to determine demand
- Degree of investor interest provides valuable pricing information
- Underwriter bears price risk:
  - IPOs are commonly underpriced compared to the price they could be marketed
    - Example: : Groupon
  - Some IPOs are well overpriced
    - Example: Facebook
  - Others cannot even fully be sold

# How Securities are Traded

## Types of Markets

- Direct search: Buyers and sellers seek each other
- Brokered markets: Brokers search out buyers and sellers
- Dealer markets: Dealers have inventories of assets from which they buy and sell
- Auction markets: Traders converge at one place to trade

# Bid and Asked Prices

## Bid Price

- Bids are offers to buy
- In dealer markets, the bid price is the price at which the dealer is willing to buy
- Investors “sell to the bid”

## Ask Price

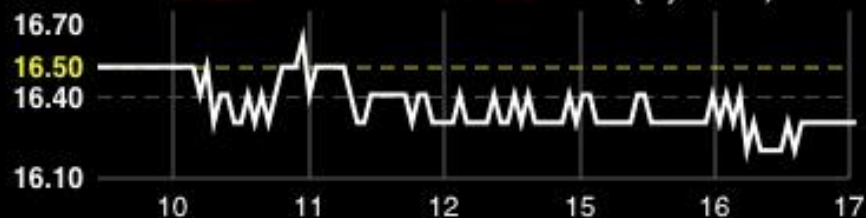
- Asked prices are sell offers
- In dealer markets, the asked price is the price at which the dealer is willing to sell
- Investors must pay the asked price to buy the security

**Bid-asked spread is the profit for making a market in a security**

Pruksa Real Estate Public

**PS** **16.30** **-0.20**  
**-1.21%**

Prev C 16.50 Avg 16.37 Close 16.30  
High 16.60 Ceil 21.10 Vol 5,786,900  
Low 16.20 Floor 11.50 Val (K) 94,705



Vol	Bid	Offer	Vol
321,400	16.20	16.30	194,400
597,000	16.10	16.40	148,600
781,300	16.00	16.50	646,700
176,200	15.90	16.60	172,400
75,600	15.80	16.70	742,600

Time	Side	Volume	Price	Change
16:27:01	B	1,300	16.30	-0.20
16:28:12	S	1,000	16.20	-0.30
16:28:12	B	100	16.30	-0.20
16:28:24	S	20,200	16.20	-0.30
16:29:39	B	3,000	16.30	-0.20
16:29:44	S	11,900	16.20	-0.30
16:29:47	B	2,900	16.30	-0.20
16:29:48	B	200	16.30	-0.20
16:29:52	B	200	16.30	-0.20
16:37:22	B	442,900	16.30	-0.20

# Market transactions

# Trading Costs

- ***Brokerage Commission***: Fee paid to broker for making the transaction
  - Explicit cost of trading
  - Full service vs. discount brokerage
  
- ***Spread***: Difference between the bid and asked prices
  - Implicit cost of trading

# Buying on Margin

- Borrowing part of the total purchase price of a position using a loan from a broker
- Investor contributes the remaining portion
- Margin refers to the percentage or amount contributed by the investor
- You profit when the stock rises

# Buying on Margin

- Initial margin is set by the Fed
  - Currently 50%
- Maintenance margin
  - Minimum equity that must be kept in the margin account
  - Margin call if value of securities falls too much

# Margin Trading: Initial Conditions

Share price \$100

Initial Margin: 60%

Maintenance Margin: 40%

Shares Purchased: 100

Initial Position

# Margin Trading: Margin Call

Stock price falls to \$70 per share

## New Position

Stock \$.....	Borrowed	\$4,000
	Equity	\$.....

Margin% = ...

# Margin Trading: Maintenance Margin

How far can the stock price fall before a margin call? Let maintenance margin = 30%

Solve to find:

$$P = \$...$$

# Short Sales

- *Purpose*

- To profit from a decline in the price of a stock or security

- *Mechanics*

- Borrow stock through a dealer
- Sell it and deposit proceeds and margin in an account
- Closing out the position: Buy the stock and return to the party from which it was borrowed

# Short Sale Mechanics

Purchase of Stock		
Time	Action	Cash Flow*
0	Buy share	– Initial price
1	Receive dividend, sell share	Ending price + Dividend
Profit = (Ending price + Dividend) – Initial price		
Short Sale of Stock		
Time	Action	Cash Flow*
0	Borrow share; sell it	+ Initial price
1	Repay dividend and buy share to replace the share originally borrowed	– (Ending price + Dividend)
Profit = Initial price – (Ending price + Dividend)		

**Table 3.2**

Cash flows from purchasing versus short-selling shares of stock

\*A negative cash flow implies a cash *outflow*.

# Short Sale: Initial Conditions

Dot Bomb	1000 Shares	
	Initial Margin	50%
	Maintenance Margin	30%
	Initial Price	\$100

Sale Proceeds                      \$100,000

Margin & Equity                      \$50,000

Stock Owed                              1000 shares

# Short Sale:

Dot Bomb falls to \$70 per share

Assets

Liabilities

Equity

= \$ ....

Profit = ?

# Short Sale: Margin Call

How much can the stock price rise before a margin call?

\* Initial margin plus sale proceeds

# Regulation of Securities Markets

- Major regulations:
  - Securities Act of 1933
  - Securities Exchange Act of 1934
  - Securities Investor Protection Act of 1970
- Self-Regulation
  - Financial Industry Regulatory Authority
  - CFA Institute standards of professional conduct
- Sarbanes-Oxley Act

# Insider Trading

- Officers, directors, major stockholders must report all transactions in firm's stock
- Insiders *do* exploit their knowledge
  - Jaffe study:
    - Inside buyers > Inside sellers = Stock does well
    - Inside sellers > Inside buyers = Stock does poorly

Question?