Wanna stock a share in the Big Apple?

Some of you might be wondering why you should care about the stock market. Maybe you think you are too young to be investing, or can't see how the market relates to your every day life. The fact is, even if you don't have money in the stock market, or are still in school, the stock market affects you. It affects everything you do, from going to the mall, to buying that new outfit you have always wanted. After all, Calvin Klein has to have money to make those outfits!

How did it start?

As you are reading this article, billions of dollars are being traded on the New York Stock Exchange, with thousands of companies being traded, and millions of people being affected. If we were to trace the origins of the New York Stock Exchange to its very beginning, we would find that the exchange started out on a dirt path in front of the Trinity Church in East Manhattan over 200 years ago. At that time, there was no paper money changing hands, or even the idea of stocks. Rather, businessmen traded silver for papers saying they owned shares in cargo that was coming in on ships every day. The trade flourished.

Wall Street was becoming a major venue for these transactions, and in 1792, 24 men signed an agreement that created the New York Stock Exchange (NYSE). The men agreed to sell shares, or individual equal portions of companies, between themselves and charge other people commissions, or fees, to buy and sell these shares for them. They found a home at 40 Wall Street in New York City. As their business grew, they later moved into what is currently the New York Stock Exchange Building.

The 1900s witnessed the Industrial Revolution, and along with it a boom on Wall Street. Everybody wanted a piece of the action, and Wall Street grew. The New York Stock Exchange was not the only way to buy stocks at that time. Many stocks that were deemed unworthy of the NYSE were traded outside on the sidewalk. This so-called "curb trading," became the American Stock Exchange (AMEX).

Today, the New York Stock Exchange and American Stock Exchange have been joined by the NASDAQ, and hundreds of local and international stock exchanges, which all play a part in the national and global economy.

How it works

Let's say you hear a tip that McDonalds is coming out with a brand new product that is expected to double the company's business. You think to yourself, "Darn, I wish I owned that company." Well, you can. McDonalds, along with thousands of other companies, lets the public buy part of its company. It does this through selling shares. A share is simply a piece of paper that says you own part of a particular company. This part is usually extremely small, perhaps thousandths of a percent of the total company, but, hey, it's a beginning. You decide you want to buy part of McDonalds. You run home and count up all of the money you have been saving, and find out you have $250. You are obviously not going to be able to buy the whole company.

So you've got the money, you know what stock you want to buy, now what? Do you go to the grocery store and ask for a dozen shares of McDonalds? Not exactly, but close. You don't go to a grocery store, but rather you call a broker. A brokerage house is like a supermarket for stocks. You can call up any broker and say, "Charles, I've got $250 and want to buy as many shares of McDonalds as I can."

Charles in return tells you, "Let's see, a share of McDonalds costs $20 (not the actual price), and I am going to charge you $50 for my services, so you can buy 10 shares of McDonalds." You then give Charles the money and you get the stock. (Brokers usually don't give you the paper stock certificates, but simply transfer ownership over to you.) Voilà, you have just bought stock in a company!

Sounds simple enough, right? Actually, it is not that simple if you look at it from the broker's point of view. When you told the broker you wanted those 10 shares of McDonalds, he did not magically buy them for you, or already own them. Rather, he sent a message to another person working down on the floor of the New York Stock Exchange (or any other stock exchange). He tells this person to buy these stocks for you. This person is called a "floor broker."

The floor broker then goes to the part of the stock exchange that is allotted to this particular stock. Here there are companies that specialize in this stock. This means that they will usually, if not always, buy and sell shares from people at the normal price. The floor broker then buys you 10 shares from one of these people, reports his trade through the hundreds of computers on the floor, and reports to his colleagues back at the brokerage house that he bought the stock. The broker keeps a record that you own that stock, rather than sending you the actual paper stock certificates. If you ever want to sell them, your broker will sell them, deduct his commission, and then give you the money.

Got all that? Well, in case you didn't, here it is again in a simplified example. When you want a stock, you call a broker. The broker calls a person on the floor (usually an employee of the broker). This person runs to the space that is allotted to this stock. He then buys the amount of stock from the specialists, or companies, that are there to sell and buy on a regular basis. He then tells the firm he bought it, and there you have your stock.

Rules

We have now learned how to hand over money to brokers in exchange for stocks, but what is to stop them from cheating you, or from running off to Mexico with your hard earned $250 that was supposed to go to McDonalds? To keep brokers honest, governments have created many regulatory commissions and organizations.

The purpose of these governmental agencies is to regulate the securities industry (stock markets). All companies must follow rules about what they can do with their stock, how they can advertise, and much more.

Most of the rules placed on companies are to prevent the owners and employees from using “insider” information. Insider information is information that a person obtains about a company that is not available to the general public, and that can be used to their advantage while buying stocks. For example, lets say you are the CEO of company XYZ, and company ABC is now in negotiations with you to merge the two firms and create a much larger company called GHI Inc. Usually mergers cause stock prices to increase, so if you, knowing that a merger is going to take place, go out and buy a large amount of stock from both company ABC and XYZ, you are using insider information, and by doing so are breaking the law.

As an investor, you are also prohibited from buying stocks if you have information about a company that no one else knows. The heaviest burden of rules and regulations is applied to brokers. Most of these rules are there to protect you, the investor. An example of one of these rules is that when a floor broker goes to buy a stock on your behalf, he must buy from the lowest bidder; and when he is selling, he must sell to the highest bidder. This seems like common sense, but in fact it is not. Floor brokers could easily sell your stock at a very low price to another broker, in exchange for them selling you a different stock cheap, or to give another customer a better price. This would not be fair to you, as you would essentially be sacrificed to get another investor a better price.

Crashes

You were right to follow your hunch with McDonalds. Your $250 has skyrocketed into $1000 over a few years. You’ve been checking the stock price recently but today when you open up the newspaper, the headline reads “CRASH!” You read on and discover that the stock market has dropped 500 points, not to mention the fact that McDonalds’ stock value has been slashed in half. You can’t believe it - years of work, all gone, in one day.

Sounds frustrating, but if you had invested in the stock market during the late 1980s, 1987 to be exact, you would have experienced this scenario as a painful reality. On October 19, 1987, the stock market plunged 508 points, or 22 percent of the total market value. It was the worst crash since 1927, which signaled the Great Depression. What brought about this crash? Why was there such a large drop in such a short period of time?

One major reason for the crash was fear. Fear of a correction. Fear of a drop. Fear of being too late to get out…

What are stocks?

Stocks, or shares, are certificates that show you own a small fraction of a corporation. When you buy a share, you are paying for a small percentage of everything a company owns, including its buildings, chairs, computers, etc. When you own stock, you are referred to as a shareholder or a stockholder. In essence, **stocks are a representation of the amount of a company that you own**.

The benefit of owning stock in a corporation is that whenever the corporation profits, you profit as well. For example, if you buy shares in Coca-Cola and the corporation comes out with a new drink that everyone buys in massive quantities, then the company will profit tremendously, and so will you. A stock also gives you the right to make decisions that may influence the company. Each share of a company that you own represents a little bit of voting power; so the more shares you own, the more decision-making power you have.

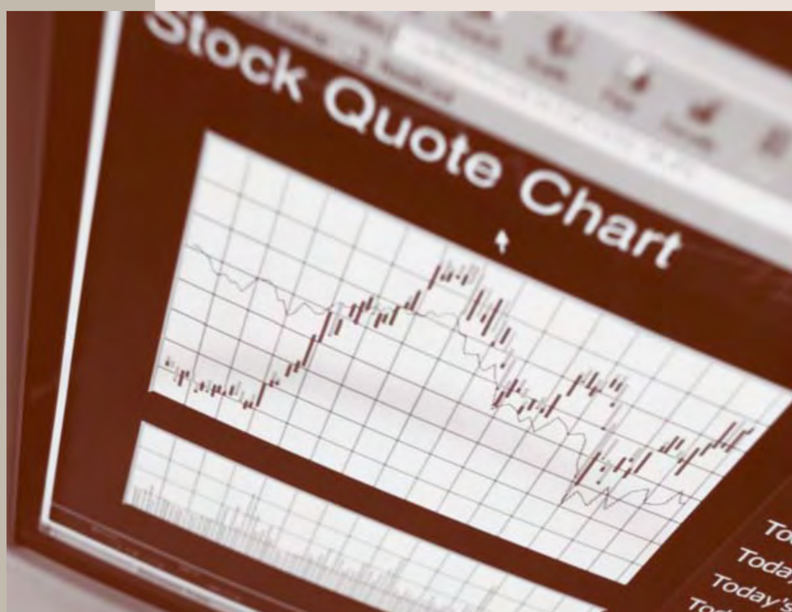
There are four levels of stock available for purchase. The lowest level is a **penny stock**. Penny stocks are shares of small companies that have almost no chance of making it big, and they are usually of no value. These stocks could be a local chain of stores, or a company that is seen as not providing a desirable service or commodity.

Stock tricks

Listed below are three "tricks" that experienced investors use to turn a profit. Like the rest of the stock market, these tricks are very risky, and you should know what you are doing before attempting any of these tricks. They include selling short, buying on margin, and buying warrants.

The first trick is short selling. Basically, short selling is selling a stock before you actually buy it. To sell short, you must first "borrow" stocks from a broker. Then, sell them immediately on the market. Keep the money that you made from selling the stocks, then wait and hope that the price of the stock drops. If the price of the stock does drop, you can buy back the original stocks and give them back to your broker. If all goes well, you will have made a tidy profit, since you sold the stocks for more than you bought them. Unfortunately, selling short does not always end well…

Buying on margin is another trick, which basically means buying stocks on borrowed money. The first step is to set up a margin account, which has a minimum balance of $2000. Once you have a margin account, you can borrow up to 50 percent of the cost of the stocks you want. By borrowing 50 percent of the cost, you are controlling twice as must value as you paid for. This will enable you to make more profit with less money. For example, if you invest $500, and the broker lends you $500, then you have $1000 to work with. You then buy 100 shares at $10 a share. If the price of the stock increases to $15, and you sell at that price, then you have $1500. You then repay the broker the $500 loan, plus interest, and pocket the roughly $1000, doubling your initial investment of $500. If you had only invested $500 of your own money, you would have only been able to buy 50 shares. Then, after selling them for $15, you would have made $750, which is only $250 more than your initial investment. The risky part about buying on margin is that any losses are also much greater. Had you bought 100 shares on margin at $10, and the price dropped to $5, you would have lost all $500, since you have to pay the broker back his $500. If you had invested only your $500 and bought 50 shares at $10, and the price dropped to $5, then you only would have lost $250.



Buying warrants is a less risky trick. A warrant is a certificate conferring on the holder limited or perpetual rights to buy common stock or other securities, or to subscribe to a new issue. The warrant gives you the right to buy stocks at a certain price. For example, if you buy a warrant to buy a stock at $5 per share for a $1 fee per share, and the stock ends up being issued at $10 a share, then you can sell the shares for a profit of $4 per share, since you paid only $6 total.

Moving up one level brings us to **growth stocks**. Growth stocks are shares of new companies that have a large potential for success, but which are not stable.

Secondary issues are well-established businesses that are almost guaranteed to continue growing in strength. They are a good investment since the profit can be great, but finding the companies can be hard.

The highest level of stocks you can buy is **blue chip stock**. Shares in older and more established companies are usually called blue chip, such as those of International Business Machines (IBM), AT&T and Coca-Cola. These blue chip stocks are the safest investment you can make, but they also take a lot longer to turn a profit.

If you want to profit from buying stocks, you must decide on a successful company to invest your money in. There are many things about a company to base your decision on. By analyzing all of the aspects you have a better chance of predicting whether or not the stock will rise in value. Below are some questions to keep in mind:

How much profit has the company made recently? If a company has not generated a lot of profit recently, chances are it may never profit, and is therefore not a good investment. If a company has generated a lot of profit recently, then it may be a good investment, since the profit margin may continue to grow.

Is the product or service provided popular and in demand? If a company offers an undesirable product, then the company may fail, since no one will buy their product. If the company fails, investors will suffer heavy financial losses. You want to invest in a company with a service or product that is in high demand. If a company invents a new kind of food, and everyone wants it, then there is an opportunity to made tremendous profit, since the company will make a lot of profit.

Is there a high level of close competition? If a company is the only company to offer a specific product, then everyone has to buy from that company, meaning the company will grow larger and generate exceptional profit. For example, if there was a company called Sneakies, and it was the only company to produce sneakers, then everyone would be forced to buy from them, which would result in huge profits for Sneakies. In real life however, there are big time competitors for this product, such as Nike and Reebok. Therefore, Sneakies would not make a lot of profit, and neither would you.