

MASTER SHEET.

• Learn Types of Preferred Stock.

• Conversion Ratio : $\frac{\text{Par Value}}{\text{Conv. Price}}$ $\xrightarrow{\text{Ex.}}$ $\frac{\$100}{\$10}$ \rightarrow 10 Shares Common stock.

Day 1.

SIE Intro

In Office 9:00 - 5:00 every day.

Exam on Feb. 19th. (18 - 19)

14 Business Days to work on exam.

Jan 29 - Feb 17.

Instructor Hotline: M-F 9:00 - 5:00 **(800) 782-3926**

Instructors@stcusa.com

Day #2. Ch.1: Overview of Market Participants & Market Structure.

1. Types of issuers.
2. How Firms function.
3. Types of Investors.
4. Primary & Secondary Markets
5. Clearing & Settlement.

Process matching investors that have money and issuers that need money.

I. ISSUERS

Legal entities that raise capital by issuing securities, including...

- Corporations
- U.S. Treasury
- State and Local Government.
- Banks.
- Foreign Governments.

I. I.
These issuers can issue securities such as...

- Equity - Used by corporations (stocks)
 - Represents ownership.
- Debt (i.e. notes and bonds)
 - Represents an issuer's promise to pay.

Debt Securities.

Corps. and government borrowers raise funds through the issuance of publicly traded loans referred to as bonds, notes, or debt instruments.

Bond: Security that represents the amount of indebtedness (Principal) that the issuer owes to the investor.

Investors that buy bonds are considered creditors of the issuer and essentially lend their funds to the issuer for a specified period (until maturity).

The issuer is to repay the principal balance of the bond at a future date.

With interest usually.

If the issuer misses an interest or principal payment, it is considered to be in default.

Equity Securities.

- Raise capital through stocks (equity)
- If investor purchases a stock, she has an ownership interest in the underlying business.
- If said company is profitable, they may be entitled to a portion of the profits (through dividends)

Financial Firms bridge issuers and investors.



MAINLY: Connect issuers and investors

Firms

Broker-Dealer.

Broker

Agency
Broker
Commission

- Firm acts as a Conduit/agent.
- Finds another party willing to take the other side of the trade.
- Collects commission for the service.
- No risk to the firm.

Dealer.

Principal
Dealer
Mark%

- Firm acts as a principal.
- Firm takes to the other side of the trade.
- Entitled to mark up/markdown
- Inventory / Risk

MARKET MAKER AND ITS QUOTE

Market Maker: Broker-Dealer that chooses to display quotes to buy or sell a specific amt. of securities @ specific prices.

- Quotes are firm for at least 100 shares.

Bid Ask
17.05 17.15
Spread: .10

Bid : Clients selling (liquidation) price. Price @ which MM will buy.

Ask (Offer) : Clients purchase price. Price @ which MM will sell.

More...

Broker.

- Any person that engages in the business of effecting agency transactions in securities for the accounts of OTHERS.

Dealer.

- Any person that buys and sells securities for its own account
- Firms acting as dealers engage in principal transactions in which they buy securities directly from their clients and hold them in inventory. Or they sell securities to clients from their inventory.
- Dealers can markup or markdown.

MM Quote.

Bid	Ask	Size
17.05	17.08	1000 X 2000

Wants to buy 1000 @ 17.05 and Sell 2000 @ 17.08

Broker - Dealer Departments.

· Investment Banking (IB): Area that works directly with the issuers to arrange and structure their securities offerings. For example, this department may advise an issuer that intends to raise funds through an issuance of stocks, bonds, or both.

· IB's are the underwriters of securities.

· IB may also assist companies that seek to merge w/ or acquire other companies (M&A) or those that need to restructure due to a bankruptcy.

· Research: Analysts in a firm's Research department study both the markets and individual issuers in order to make recommendations. (Typically Buy/Sell/Hold)

· Sales: Financial Professionals who work in the Sales area typically market individual stocks or bonds, but also packaged products (e.g. mutual funds) to both retail investors and institutions. Historically, Sales personnel have been referred to as stock or bond brokers.

· Will be referred to as registered representatives (RR's) or investment adviser representatives (IAR's)

· Trading: Trading professionals handle the execution of trades for both the firm's clients and the firm's own (proprietary) account. The trades may occur either in electronic marketplaces (NASDAQ) or hybrid marketplaces (NYSE).

· Operations: Ensures all paperwork, funds, and securities transfers that are associated with a trade (or processing) are handled efficiently and according to specific industry standards.

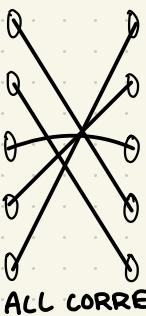
Investment Adviser (IA) and Municipal Advisor (MA)

- Investment Adviser (IA)
 - Is a firm that charges customers a fee for managing their securities portfolios.
 - The fee is based on the assets under management. (AUM)
 - An IA is considered a large or institutional customer of a broker-dealer.
- Municipal Advisor (MA)
 - An MA is a person or firm who advises municipalities on bond offerings and must be registered w/ the SEC
 - An MA typically advises issuers (e.g. State, county, city) regarding the structure and timing of a new offering.

Checkpoint: MATCH TERMS

Broker-Dealer: Commission
IA's: Charge a fee. (% of AUM)

Broker



Represents Ownership

Debt

Maintains an inventory of securities

Investment Adviser

Charges a fee.

Market Maker

Receives a commission

Equity

Issuer borrows money.

Institutional and Retail Investors

• Institutional Investors.

• Investors are typically defined based on the amount of assets that they have invested.

• Customers w/ a large amount of assets are referred to as 'institutional investors', such as Banks.

• Insurance Companies

• Investment Companies

• Corporations, partnerships, individual investors w/ a certain amount of money invested.

MORE ON IA'S.

SEC (Securities & Exchange Commission)

IA-AUM $< \$100\text{ mil.}$ must register w/states in which it conducts business.

IA-AUM $\$100_m \rightarrow \110_m , may register w/SEC or the States

IA-AUM $> \$110_m$, MUST register w/SEC.

MA's

Financial Advisors

3rd Party Marketers

Placement Agents

Solicitors

Finders

Swap Advisors

Types of Investors.

Retail:

- Buy stocks/bonds from broker dealers directly.
- Regular Individuals
- IRA, Retirement, Custodial acct.

Accredited:

- Sophisticated.
- Assumes greater risk.
 - Financial Institutions (Banks)
 - Private Business Company
 - Directors, Exec Officers
 - Individuals who have attained certification (CFP, Series 7, etc.)
- \$1mil net worth (no house)
200K/year (book expenses)
for Past 2 years.

Institutional:

- Large entities that pool their money to purchase securities.
- Banks, insurance company, pension plan, hedge fund.
- FINRA Defn. Includes an account of an individual or other entity w/ total assets of $\geq \$50,000,000$

Qualified Institutional Buyers (QIBS) (Entity / Not Human)

Three-Part Test

1. Eligible...

- Insurance Company
- Small Business development Companies
- Registered investment companies.
- Registered investment advisers.
- Private and public pension plans.
- Certain bank trust funds.

2. Buyer must be purchasing for its own account or for the account of another QIB

3. Buyer must own and invest at least 100 million of securities of issuers that are not affiliated w/the buyer

Primary Market: Where Shares originate. (New Issue Market)

Secondary Market: Shares between investors, buying and selling.

Exchange Market: Centralized venue. Auctioneer controls trading in a given stock Designated Market Maker(DMM)

NASDAQ: equity dealer-to-dealer market

- Securities Dealer

- Provides quotes on securities

Dealer-to-Dealer: Stocks that are unqualified for physical OR electronic exchange are considered OTC and are referred to as OTC Equities.

OTC markets trades occur in non-physical dealer-to-dealer markets.

OTC Markets Group.

DARK POOL: HF traders and Institutional Investors trade directly.

OTCQX: Highest tier

OTCQB: Entrepreneurial and development stage U.S and international companies.

OTCID: Serves companies that report baseline info.

Pink Limited: For Securities w/ minimal to no issuer involvement. Low disclosure.

NON-EQUITIES: Corporate, municipal, US Gov. bonds don't have organized exchanges.

Most are traded in OTC market.

3rd Market: Electronic, Internet based. OTC ^{OR} away from traditional exchanges.

4th Market: Institution to institution trading. No public market or exchanges.

Activity Page 6:

1. 1 million, 200K

2. individual, 100 million.

3.

4.

5.

6. NASDAQ

7. Market Makers, Traders.

8. Fourth Market.

Chapter 2

FINRA Rules:

- Conduct
- Uniform Practice Code
- Code of Procedure
- Code of Arbitration

Blue Sky Rules: INTRASTATE Laws. (SINGLE STATE) Established by each individual state.

MSRB: does not enforce its own rules.

IS an SRO

Establishes rules

Requires firms to register to trade municipality securities.

Securities that are specifically identified as belonging to a customer (registered) are not covered since they are able to be returned to the customer without limit. However securities held in street name (name of broker-dealer) are subject to the coverage limits of SIPC.

Written Supervisory Procedures (WSP) Manual: details the rules and identifies the person(s) responsible for enforcing these rules.

Pennystocks do not exist on national securities exchanges. (NYSE, NASDAQ)

MARGIN Requirements: Securities Exchange Act of 1934

Securities Act (1933) New Issue disclosure. (Primary Market)

Investment Company Act (1940): Regulates mutual funds and investment companies.

Investment Advisors Act (1940): Regulates investment advisers (ABC)

Telephone Consumer Protection Act: Calls allowed from 8:00 AM - 9:00 PM. (Customer's time zone)

WRAP Account: IA charges fee that covers.

- Investment Advice
- Portfolio Mgmt.
- Transaction Costs.
- Custody and Admin expenses.

Advisory Services & Transaction Costs.

S.Act 1933 Primary Market.

Primary Market.

Fair and Fair Disclosure.

"New Issue" Market.

Prospectus Delivery (info about the company).

Securities Exchange Act (1934) Secondary Market.

- Trading market.

- Registration of firms and personnel.

- Margin/Insider trading/on-going reporting for issuers.

Investment Company Act (1940) and IA Act (1940)

ICA '40: Covers mutual funds and other packaged products.

IA '40:

SIPA ↔ FDIC for Broker-Dealers

SIPA: Protects separate customers (not accounts)

if BD bankruptcy occurs.

Coverage:

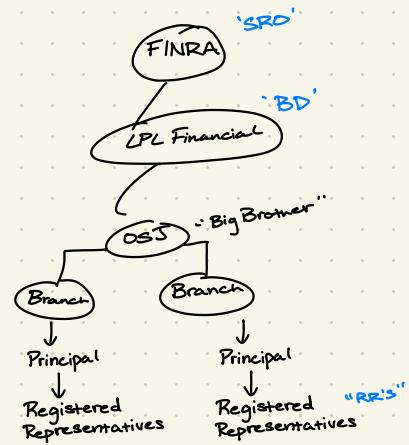
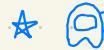
- Cash and Street name Securities \$500K

- Will only cover CASH up to: \$250K

- If limits are exceeded customer becomes a General Creditor

FRAUD is not covered.

Review SIPA Coverage Scenarios



SIPC

DoJ → Criminal Cases.
SEC → Civil Enforcement.

Covers: ≤ 500K (Securities)

≤ 250K (Cash)

- If a customer exceeds SIPC limits
 - The customer is a general creditor for the excess amount.

Violate federal Securities law → Department of Justice (DoJ)

Violate MSRB → FINRA/SEC enforces

SIPC Covers: Brokerage

IRA

Custodian for Minors Acc.

Short Seller → Profit ↑ if Price ↓

SIPC doesn't cover stocks held by customer in his name.

Broker-Dealer when opening account for customer.

- Provide SIPC web address.
- Provide written notification that he may obtain info abt. SIPC by contacting the insurer.
- Advise the customer on how he may obtain the SIPC brochure.

SEC

Insider Trading Profit → \$2 million → Can sue for \$6 million.

Chapter 3

Company Owned by Shareholder(s)
Need to raise Capital to fund Operations.

Capital → Money.

Borrow Money

Debt Financing

Bonds

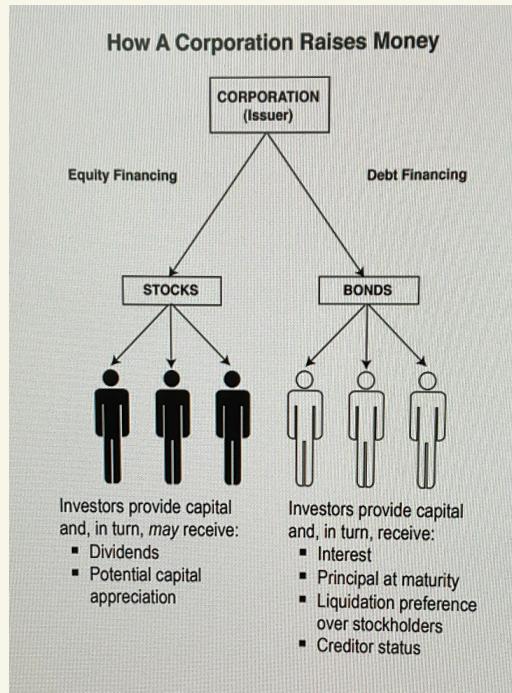
Sell Ownership.

Equity Financing

Stock

Issuer Sells bonds (debt) is borrowing money from investors who buy the bonds.

Bonds: Company borrows money, bondholders collect interest.



Cyclical Stock: Performance rises and falls w/economy. "Big Ticket" items.

$$1000 \text{ shares} @ 6\% \text{ dividend} \rightarrow 100 \times 6\% \rightarrow *1000 \rightarrow \text{Quarterly} \rightarrow \div 4 = \$1500/q$$

An issuer may buy back stock @ no higher than the higher of

- Last independent bid
- or
- Last independent transaction price.

Pre-Emptive rights allow stockholders to purchase the Common Stock of the same company.

Growth Stock: Company focused on expanding business.

- Company reinvests earnings.
- Doesn't pay dividends.

Preferred Stock Owners do not receive rights offering.

Authorized Shares: Amt of shares a company is permitted to use.

Investor Owns 500 shares of 3% convertible preferred stock. Conversion price is \$20 Assume Par Value is \$100 for Preferred Stock.

$$\text{Conversion Ratio} = \frac{\text{Par Value of preferred}}{\text{Conversion Price}} \rightarrow \frac{\$100}{\$20} \rightarrow 5 \text{ shares COMMON STOCK}$$

$$\text{Pref. Stock} * 5 = 2500$$

$$500 \text{ shares} * \$100 = \$50,000$$

$$\$50,000 \div \$20 = \$2500$$

Conversion is NOT taxable.

Cumulative Stock:

- All unpaid dividends accumulate
- Arrears must be paid in full before any common stock dividend can be paid.

$$71 \times \$100 \text{ (Pref. Stock)}$$

$$= .07 \times 100 = \$7/\text{share/year}$$

$$\begin{aligned} \$3 & 2024 \leftarrow \$4 \text{ Shortage} \\ \$3 & 2025 \leftarrow \$2 \text{ Shortage} \\ \$13 & 2026 \leftarrow \$7 + \$6 \end{aligned}$$

Warrant Intrinsic Value: stock price - warrant price
 $\$56 - \$50 = \$6$

Warrants only concern is common stock.

Lock-Up Agreement: Restricts insiders from selling their shares for a set period. Usually 90-180 days.

Corp. authorized to issue 30 million shares. Has 28 million shares. Has 4 million shares of treasury stock and stock price of \$18, what is their market capitalization?

Formula: Outstanding Shares \times Stock Price

Issued-Treasury. Authorized shares not included.
 $= 28 - 4$
 $= 24 \text{ mil} \rightarrow 24 \text{ mil} \times 18$

Convertible Preferred Stock may increase the most if the value of the company's common stock appreciates.
Convert \rightarrow Climb.

Rule 144: Applies to restricted and controlled stocks.

Can Sell for 6 mos.

CPL Bonus
Stock.

"Good Performance"

Rule 144: Gives rules for Selling stocks.

Form 144 Filled Out: You have 90 days.

- Can Sell 1/4 of Shares Outstanding.
- Avg. trading Volume OF 4 weeks.

1 4 4
↑ ↑ ↑
I. 4 4 quarters
W. 1 quarter
S. 90 days.

Ex. Question: Shares Outstanding: 5,600,000

Avg. Volume

5,600,000	x 1/4	Wk. 1 45,000	Avg. Formula
5,600,000 x .01	= 140,000	Wk. 2 50,000	
		Wk. 3 60,000	
		Wk. 4 45,000	
		Wk. 5 50,000	

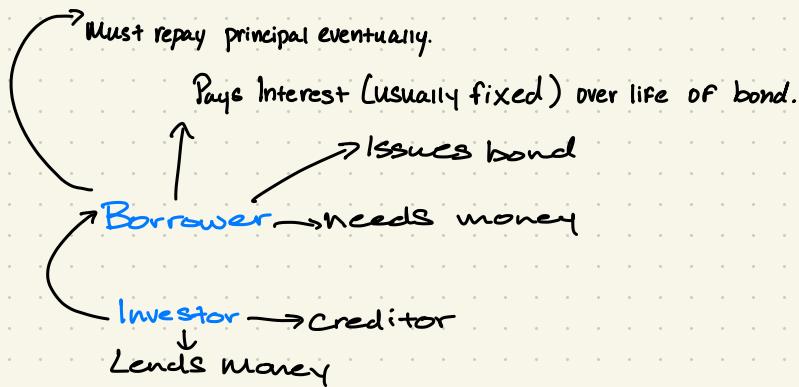
$\frac{200,000}{4} = 50,000$

Take the higher amt..

56,000 Shares.

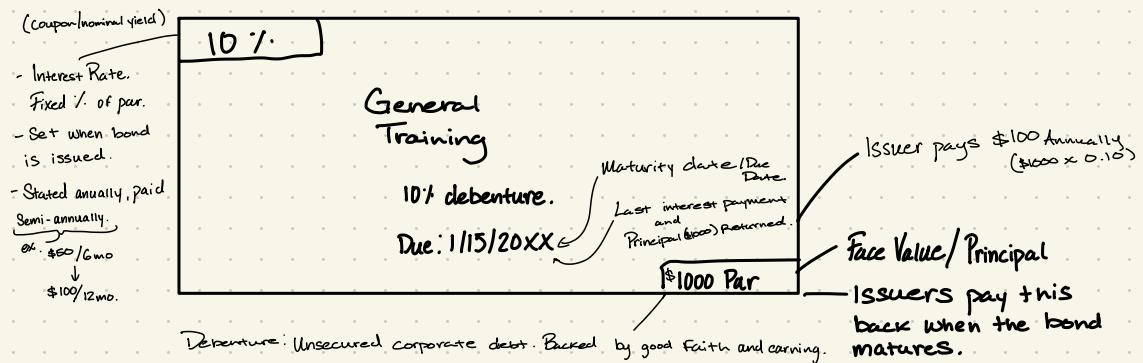
Chapter 4: Debt Instruments.

Bonds: A loan or debt obligation of an issuer (borrower)



Benefit: Consistent interest payment.

- Eventually receive principal (Par Value back)



Lower Coupon Rate: Short maturity bond.

Coupons Review.

Short Coupon:

- Occurs @ issuance
- Covers a partial interest period.
- Results in smaller 1st interest payment.
- 1st Coupon Period < 6 mo. \rightarrow Short Coupon.
 $> 6 \text{ mo} \rightarrow$ Long Coupon

Variable Coupon: Similar to Floating. Rate adjusts over time.

Floating Coupon: Rate changes based on an index.

Coupon = Interest Rate

= Annual Percentage of Par Value

- Determines interest payment, not market price.
- Coupons do NOT Change, yields Change.

Coupon: Fixed rate stated on bond.

Price: What investors pay.

Yield: Investors return.

Term and Serial Maturity

- Loan Repayment Structure.
- Both types are issued on the same day.
- Term Maturity: Entire bond offering matures on the same date.

- Serial Maturity: The bond offering matures over several years. (i.e. Series of Maturity dates.)
 - Level Debt Service: Serial maturities are structured so that principal and interest payments represent approx. equal annual payments over the life of the offering.

Serial Bond : 2014 | 2020 | 2021 | 2022 | 2023
Serial Bond : 10M + 10M + 10M + 10M + 10M.

Serial Bond. 

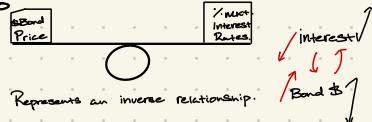
Par Value may differ from price.

Bond Selling less than par value. **Discount**

Bond Selling more than par value. **Premium**

Bonds fluctuate due to

- Interest Rates
- Credit Risks



ADR'S American Depository Receipts.

- Priced in U.S.D
- Pay dividends in USD (may be taxable)
- Remain subject to currency risk.

Sponsored

- Issued in co-op w/
the foreign company.
- May trade on U.S. exchanges
NASDAQ or NYSE

Unsponsored.

- Issued w/o involvement
of the foreign company.
- Generally trade in OTC market
(OTCBB or OTC Pink Market)

Learn types of preferred stock

Non-Cumulative

Cumulative

Callable

Participating

Convertible

Credit Risk.

- Recognition that an issuer may default and may not be able to pay back interest and principal to bond holders.
 - High Credit Risk \rightarrow High Interest Rate.
 - US Gov. issued securities have the lowest credit risk.
 - C.Risk is harder to evaluate when the bonds are issued by a corporation/municipality.
- A bonds Credit rating helps gauge risk.

Bond Pricing & Coupon Rates.

A bond w price of...

- 100 is selling @ 100% of its par value, \$1000.
- 90 is selling @ 90% (discount) par value, \$900.
- 110 is selling @ 110% (premium) par value, \$1100

(30 Day Month, 360 day year)

For Corporate and Municipal Bonds, a bonds price may also be expressed in terms of points.

- ea. point = 1% of bonds par value or \$10
- Corporate and municipal bonds trade in increments of $\frac{1}{32}$ of a point (\$1.25)
- Convert fractions \rightarrow decimal. $\frac{1}{8} \rightarrow .125, \frac{2}{8} \rightarrow .250, \frac{3}{8} \rightarrow .375 \dots$

Bond Quoted @ 93 $\frac{5}{8}$ \rightarrow 93.625 of par or \$936.25

◦ Government Bonds Such as T-Notes, T-Bonds, and Agency Securities trade in $\frac{1}{32}$ of a point.

Quotation	%	.xx	\$
1000	87.24	87 $\frac{24}{32}$	\$877.50
10000	106.04	106 $\frac{4}{32}$	\$10612.50

Bond Yields

Review This. 1/30/26

Nominal Yield. (NY) ($NY * PAR = \text{Annual Interest}$)

- Coupon Rate.
- Fixed.

Current Yield (CY)

- Annual interest divided by the current market price.

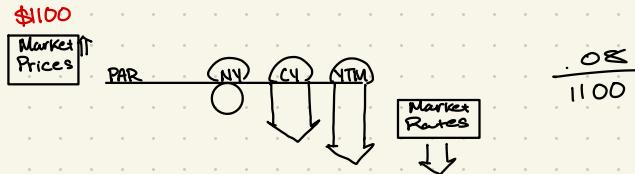
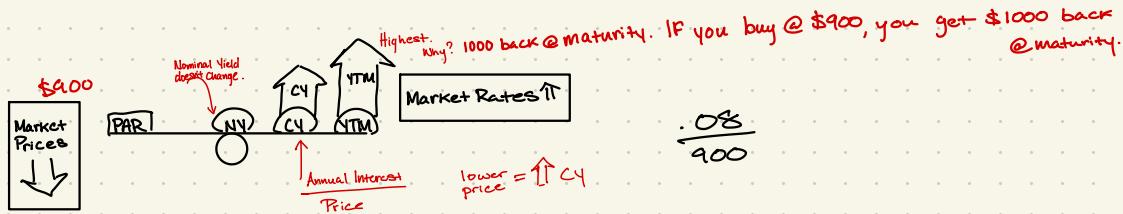
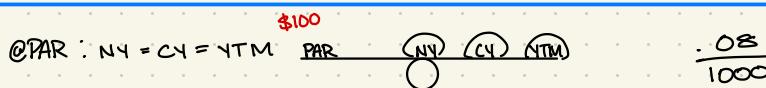
Yield-to-Maturity (YTM) \longleftrightarrow A Bonds Basis

- Same as basis and yield
- Includes reinvestment of annual interest and the gain or loss over the life of the bond.
- Measured to the bonds maturity.

$$1.00\% = 100 \text{ Basis Points}$$

$$.01\% = 1 \text{ Basis Point}$$

8.1 APR ↗



Retiring Debt prior to Maturity

- When a debt reaches maturity date, the holder redeems it to the issuer and receives the bond par value plus the last interest payment.
- Issuer Obligation to bondholder ends and the debt is retired.

- Some bonds redeemed before maturity.

↳ Call Provision: Issuer-Controlled. Rates fall, issuer calls.

◦ Features Disclosed:

- In-Whole: May call all outstanding bonds.
- Partial: may call a portion of the issue.

Put Provision: Bond holder Controlled. Rates Rise → Bondholder puts.

Quiz.

Balloon Maturity: Small early maturities. Big maturity @ end.

Bond w/Put Feature → More expensive

Bond Yield / Bond Price → Inverse Relationship.

\$1000 Municipal Bond priced 99 5/8 → 99.625. Callable @ 102 and putable @ 93

Company offering \$750 million of 8% bonds @ 99.25% of par value. Investor who buys the bonds will receive yearly interest of: 1st. Annual Interest = Rate × Par = $.08 \times 1000 = \$80$. Interest Payment doesn't change

Convertible @ \$25/per. Trading @ 1100 underlying stock trading @ 28.

$$\frac{1000}{25} = 40$$

$$40 \times \$28 = 1120$$

◦ \$20 per. Trading @ 960 Underlying Stock @ $\frac{\$}{15}$

$$\frac{1000}{20} = 50$$

$$50 \times \frac{\$}{15} = \frac{\$}{750}$$

Cancel 50 shares for a total of

Finish last 20 min of Ch.4 ON-Demand.

When a Corp is liquidated. Investors are paid in this order.

1. Secured Bondholders
2. Unsecured Bondholders.
3. Preferred Stockholders.
4. Common Stockholders.

ARS's can't be sold back to the issuer.

Issuers select an underwriter by evaluating bids that are submitted, using a Competitive Sale.

USGov bonds are taxed federally, but exempt from state.

Secured Debt.

- Mortgage Bond
- Collateral Trust Bond.
- Equipment Trust Certificate.

Income bonds do not accrue interest.

T-Bills. Short-Term, Zero Coupon Security. Quoted on discount yield.

Mortgage-Backed Security Risk is: Prepayment Risk.

Housing Revenue Bonds are issued by: State Housing Agencies

Review Last 10 mins Ch.5 ON-Demand.

T-Bills, Notes, Bonds (Treasury)

T Bonds/Notes: Interest bearing Securities.

- Have attributes of traditional fixed-income investments.
- Pay Semi-Annually.

SIE On-Demand Learning Guide

Comparing T-Bills, T-Notes, and T-Bonds

	T-Bills	T-Notes	T-Bonds
Maturities	Up to 1 year	2-10 years	Greater than 10 years
Denominations	All in \$100 multiples		
Forms of Issuance	Book entry No phys. Cert. ON Record own bonds/bills.		
Interest	<ul style="list-style-type: none">Discount securitiesTrades flat	<ul style="list-style-type: none">Stated annually, paid semi-annuallyAccrued Interest: Actual/365	
How They are Initially Sold	Weekly auction	Periodic auction	

1/32 Point Increments

Bid	Ask
2.94%	2.90%

↑
Buy
@ 2.94%:
discount
lower price

↑
Higher Price
Lower discount.

TIPS) Protects investors from inflation.

High inflation: Bad for Bonds.

T-Strips: Created in Secondary Market.

- Non interest bearing.

Gov. Sells Treasuries through auction.

Bid

100m @ 4.5% Coupon.

✓

20m non-competitive

✓

40m @ 4.9%

✓

40m @ 5.0%

✓

30m @ 5.1% NOT filled X

Highest Bid is 5%, all bidders get a 5% yield. Auction Clears @ 5%.

Activity.

Activity

Read each characteristic and then circle which type (or types) of treasury debt to which it applies.

MORE THAN 10-YEAR MATURITY

T-Bills T-Notes T-Bonds

INTEREST IS FEDERALLY TAXABLE

T-Bills T-Notes T-Bonds

SOLD AT WEEKLY AUCTION

T-Bills T-Notes T-Bonds

DISCOUNTED SECURITY

T-Bills T-Notes T-Bonds

2 – 10-YEAR MATURITY

T-Bills T-Notes T-Bonds

BOOK-ENTRY ISSUANCE

T-Bills T-Notes T-Bonds

INTEREST PAID SEMI-ANNUALLY

T-Bills T-Notes T-Bonds

Question

Which of these statements are TRUE with regards to Treasury auctions? Circle all that apply.

- I. Non-competitive bids are filled first.
- II. Competitive bids determine price.
- III. Non-competitive bids submit quantity and price/yield. ← NON-COMP → ONLY Quantity
- IV. The lowest accepted price/highest yield clears the auction.

↑
SAME

Government Agencies

Farming Loans (FFCB): Provide loans to farmers.

Mortgage Backed Securities: **GNMA** ← NOT Subject to Credit Risk.
FNMA
FHLMC

Municipal Bonds. and Their Issuers.

- ① States and Political Subdivisions
 - Cities
 - Counties
 - School Districts
- ② Public Agencies and Authorities
 - Transit.
 - Housing Authorities
 - Water, Sewer, electric systems.

- ③ Territories
 - Puerto Rico
 - Guam
 - U.S. V. Islands

General Obligation (GO)

- ①
 - General Purpose
- Paid by
 - Taxes
 - Issuers full faith & credit.

State Level

- Sales Tax
- Income Tax

Local Level

- Ad Valorem (Property Tax)
 - Assessed Value
 - Millage Rate = tax bill (1 mill = .001)
 - Parking/License Fees.

Revenue Bonds.

- Fund project.
- Paid by
 - Revenue from a project.

Typical Projects

- Toll
- Bridge
- Stadium
- Airport

Considered:

- Self-Supporting Debt.

Types of Revenue Bonds

Type	Source for Paying Debt Service
Transportation Revenue	Use tolls and user fees
Special Tax	Excise taxes on purchases, such as gasoline, tobacco, and liquor
Special Assessment	Assessments on the benefiting properties; used for sidewalks, sewers, etc.
Double Barreled	Two sources - project revenue and tax dollars (from GO bonds)
Moral Obligation	If project revenue is insufficient, the state legislature is morally (but not legally) obligated for the shortfall
Private Activity	A bond in which more than 10% of the proceeds will benefit a private entity (e.g., a sports team)
Industrial Development Bond (IDB)	Issued by a municipality and secured by a lease agreement with a corporate user of the facility

Municipal Notes (Tax-Free Anticipation Notes): Short term issues, normally issued to assist in financing a project or to assist a municipality in managing its cash flow.

- Tax Anticipation Notes **TAN'S**
- Revenue Anticipation Notes **RAN'S**
- Bond Anticipation Notes **BAN'S**
- Grant Anticipation Notes **GAN'S**

Ratings for Municipal Notes

	S&P	Moody's
Investment Grade	SP 1+ SP 1 SP 2	MIG 1 MIG 2 MIG 3
Speculative Grade	SP 3	SG

Practice Exam

- Debenture.

- Unsecured debt instrument.

- Preemptive Rights

- Stockholder maintain proportionate interest in Corp.

- Zero Coupon Bond.

- Investor gets 1 payment.
- No interest payment.

Dividend Dates.

1 Declaration: Dividend announced.

2 Payment Date: Dividend distributed.

3 Record Date: Date on which person must own the stock to receive dividend. (Owner of record)
Set by Corp. Buyer receives dividend if the transaction settles on or before record date.

4 Ex-Dividend Date.

- The same day as record date.
- Stocks sells w/o dividend. (Reduced Price)
- Regular-Way Settlement is assumed.

SIE On-Demand Learning Gu

Dividend Dates

MAY						
Sun.	Mon.	Tues.	Wed.	Thurs.	Fri.	Sat.
1	2	3	4	5	6	7
8	9	10	11	12	13	14

Record and
Ex-Dividend

Trade Date	Settlement	Entitled to Dividend?
May 10	11th	Buyer
May 11	12th	Buyer
May 12	13th	Seller
May 12 (cash)	12th	Buyer

↓
Same
Day
Settlement.

Activity

Scenario: A corporation has declared a cash dividend on June 1, payable on July 25 to stockholders of record on Thursday, July 12. Which of these states is/are TRUE? Circle all that apply.

- The stock trades ex-dividend on Thursday, July 12.
- The seller is entitled to the dividend on a trade executed on Wednesday, July 11.
- If securities are not delivered by July 12, a due bill must accompany the delivery.
- A cash trade can be done as late as July 25 in order for the buyer to receive the dividend.

Stock Dividends

Additional Shares instead of Cash.

SIE On-Demand Learning Guide

Stock Dividends

The Impact of Stock Dividends	If a company chooses to pay a dividend to its shareholders in the form of additional shares of stock, there is: <ul style="list-style-type: none">No economic gain or loss for holdersNo change to issuer's capitalizationNo change to holder's percentage of equity ownership
The Tax Treatment of Stock Dividends	<ul style="list-style-type: none">Additional shares received are generally not taxed as incomeInvestor's total basis is unchanged, but basis per share is adjusted

Example – Stock Dividend

Investor owns 100 shares of XYZ at \$60 per share.
XYZ Company declares a 10% stock dividend.



Value doesn't Change. # of Shares Change.

Current Yield for Equities (Dividend Yield)

Stock (\$40/share), Quarterly Dividend (\$0.30)

BASED
ANNUALLY

$$\text{Current Yield} = \frac{4 \times .30}{\$40} = \frac{1.20}{40} = \$3.00$$

Read each statement and determine whether it is TRUE or FALSE.

A STOCK DIVIDEND CHANGES THE OVERALL VALUE OF THE PORTFOLIO
THE COST BASIS OF SHARES IS REDUCED AFTER A STOCK DIVIDEND
A STOCK DIVIDEND IS TAXABLE IN THE YEAR IT'S PAID
IF A CASH DIVIDEND REMAINS THE SAME, THE CURRENT YIELD ON THE STOCK WILL INCREASE AFTER A STOCK DIVIDEND IS PAID

FALSE
TRUE
FALSE
TRUE

NO TAX on Stock dividend.

MORE because more Shares.

Bond Investments.

Nominal and Current Yield.
 (nv) (cy)

$$\text{Current Yield} = \frac{\text{Annual Interest} (\$)}{\text{Current Market Price.}}$$

NY

- Coupon ; Fixed

CY

- Annual interest payments
- Based on market price. NOT purchase price.

Current Yield Calculations

$$\frac{\text{Annual Interest}}{\text{Current Market Price}}$$

Nominal Yield	Bond Price	Calculation	Current Yield	
8%	\$1,000	$\frac{\$80}{\$1000}$	8%	Par
9%	\$1,125	$\frac{\$90}{\$1125}$	8%	Prem.
6 1/2% (6.5)	\$812.50	$\frac{\$65.00}{\$812.50}$	8%	Discount.

Yield - To - Maturity (Basis)

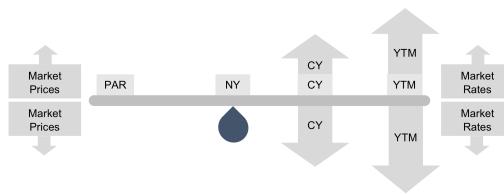
- Yield of a bond.

1 Basis Point = .01 %.

100 Basis Points = 1.0 %.

"4.60% vs 4.75%"

"18 Basis Points Higher"



Activity

Read each statement and fill in the blanks.

- A bond's nominal yield is also referred to as its Coupon rate.
- To calculate a bond's current yield, an investor must use its annual interest payment.
- To calculate a bond's current yield, the market price of the bond is used, not the investor's purchase price.
- A bond's yield-to-maturity is also referred to as its Basis or Yield.
- 1.20% is equal to 120 basis points.
- If interest rates are increasing, bond yields are higher and bond prices are lower.

For Callable Bonds always quote the lower of YTC or YTM. Yield-To-Worst.

When bonds are callable @ par use

Selling @ discount : YTM

Selling @ Premium : YTC

Yield to Call (YTC)

An investors yield if a bond is called at par.

Cost Basis and Capital Events.

Cost Basis: Price of Ownership.

Total amt. paid to acquire a security.

Capital Gains.

Result of sale or redemption of an asset if proceeds exceed the basis.

Short Term: < 1 year or less

Taxed @ Ordinary Rates.

Long Term: > 1 year

Taxed @ $\leq 20\%$

Capital Losses.

Result of sale of an asset if the proceeds are less than the basis

Total Return: Applies to all stock and bond investments by including

All cash flows from interest and dividends

plus any appreciation in value.

or minus any depreciation.

Total Return Formula:
$$\frac{(\text{End Value} - \text{Beginning Value}) + \text{Investment Income}}{\text{Beginning Value}}$$

Total Return Example

An investor purchased ABC preferred stock two years ago for \$25 per share. Over this time, she has received \$5 in dividends and the stock is currently trading for \$30 per share. What is the investor's total return on her investment?

$$\text{Total Return} = \frac{(\text{End Value} - \text{Beginning Value}) + \text{Investment Income}}{\text{Beginning Value}}$$

$$\frac{(30-25)+5}{25} = \frac{10}{25} \rightarrow \frac{2}{5} \rightarrow .40 \rightarrow 40\% \quad \text{Total Return}$$

Other Returns

Real Return: Rate of Return - Inflation.
(inflation adjusted)

Risk-Adjusted Return: Rate of Return - Risk Free Return.

Risk-Free Return: Rate of Return generally found on U.S. Treasury Bill.

Question

Scenario: A security has a 6% rate of return, when the inflation rate is 1.5%, and T-bills are yielding 2%.

What is the real return?

What is risk-adjusted return?

$$\text{Real Return} = 6.0\% - 1.5\% = 4.5\%$$

$$\text{Risk-Adjusted Return} = 6.0\% - 2.0\% = 4\%$$

Averages & Indexes

investment returns are often compared against a benchmark of a group of securities.

Narrow-Based indexes focus on market segments, while broad-based indexes attempt to include the entire market, such as...

- S&P 500 Index (NYSE stocks mainly)

- 400 Industrial
- 20 Transportation
- 40 Utility.
- 40 Financial.

- Dow Jones Composite - Broken down into three averages

- Dow Jones Industrial - 30 Stocks (most widely quoted)
- Dow Jones Transportation - 20 Stocks
- Dow Jones Utility - 15 Stocks

Other Averages and Indexes

Equity Indexes:

- Wilshire Associates Equity Index - Largest index; 5,000 stocks
- Russell 2000 - Focuses on small capitalized stocks
- Nasdaq Composite Index - Based on all Nasdaq listed securities
- Nasdaq 100 - The 100 largest companies listed on Nasdaq

The largest index is the Wilshire Associates Equity Index, while one of the smallest is the Dow Jones Industrial Average

Bond Indexes

- Barclay's Capital and other B/Ds have created indexes based on existing bonds in the market

Tracking Performance:

- An investor must track how his investments are performing relative to a benchmark or index (e.g., if his investment is up 5%, but the S&P 500 is up 10%)

Cn6 Quiz.

Buys 1000 Share (\$15/ea)

Paid: \$.30 Annually

After 1yr. \$18/ea

Orig.
Investment: 15,000

Cap. Gain: \$3 (15000) = \$3000

Dividend Income: \$.30(1000) = \$300

Total Gain = \$3300

$$\frac{3300}{15000}$$

Orig. \$100 ↓
\$43 ↓
\$93

3.80
93

Divid. \$4 ↓
\$3.80.

400 Shares of Stock @ \$25/each
Commission = \$220

$$\begin{array}{r} 400 \\ \times 25 \\ \hline 10000 \\ + 220 \\ \hline 10220 \end{array}$$

Packaged Products. Ch. 7.

Investment Advisor: IAA 1940. (Fund Manager)

- Gets paid a mgmt. fee.
- Paid based on AUM.

Underwriter: Sponsor / Wholesaler / Distributor

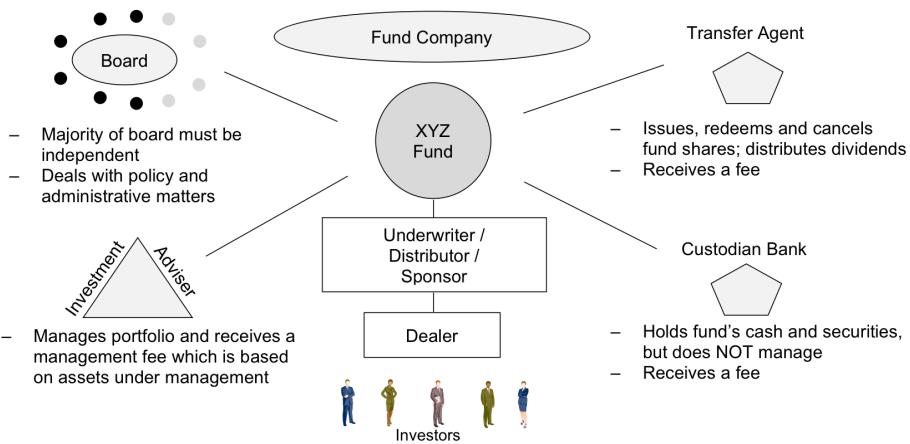
- Appointed by the board.
- Receives portion of sale.

Transfer Agent: Cancel, issue, etc.

Match each entity to the appropriate description.

TRANSFER AGENT	Determines investments to meet the fund's objectives
BOARD OF DIRECTORS	Sets the fund's objectives and deals with administrative matters
CUSTODIAN BANK	Issues, redeems, and cancels the fund's shares
UNDERWRITER	Responsible for the safekeeping of the fund's assets
INVESTMENT ADVISER	Receives a portion of the sales charge for selling shares to the public

Mutual Fund Structure



Liquidity: Mutual Fund redemption must be paid within 7 calendar days.

Prospectus Delivered @ or prior to the solicitation to sell the mutual fund shares.

UIT: Unit Investment Trust: Hold securities portfolios which are not actively managed, but remain fixed for the life of the trust.

Dollar Cost Averaging (DCA): Buying more when prices drop, less when they rise. (Same amt. regularly)

Investment Company that diversifies portfolio among different investment classes based on computer modeling techniques and forecasts of changes in the economy: Asset allocation fund.

Custodian Bank: Safekeeping of mutual fund assets.

Rights of Accumulation (RoA): Right to add up all purchases made from same family of funds.

Sector Fund: Specific industry. High growth potential.

Switching: Exchange shares of one MF for shares of another MF within the same family. No new sales charge.

Contingent Deferred Sales Charge (CDSC): Sales charge paid when MF's redeemed (Benefits Investor)

Redemption Fee: Charged @ time of redemption.

Domestic Aggressive Growth Fund: No exchange rate risk.

Closed-End Compared to Open-End

Closed-End (Publicly Traded)	Open-End (Mutual Fund)
Typically a one-time issuance of common shares <ul style="list-style-type: none">▪ Could issue preferred stock or bonds	Continually issue new shares <ul style="list-style-type: none">▪ Common shares▪ Sold by prospectus
Shares may trade at a discount or premium to NAV with commission or mark-up added (supply and demand)	Shares are sold at the NAV + sales charge (if any)
Sponsor does not stand ready to redeem shares	Sponsor stands ready to redeem shares at the next calculated NAV (forward pricing)
Shares trade in the secondary market	Shares remain in the primary market
Shares may be sold short	Shares cannot be sold short

12b-1 Fees

An annual fee levied against the fund's assets

- Allows distribution costs to be borne by the fund, rather than from front-end charges

Used to finance promotion, advertising, commissions

- Includes continuing commissions or "trailers"
- If a written contract exists, it may be paid to RRs who are still employed with a firm or to retiring RRs based on existing assets

No-Load Funds

For a fund to be described as a no-load, it must have:

- | | | |
|-------------------------------------|---|---|
| 1. No front-end sales charge (load) | 2. No deferred sales charge (back-end load) | 3. No 12b-1 fee that exceeds .25% of the fund's average net assets per year |
|-------------------------------------|---|---|

A no-load fund may have a redemption fee
(since the fee is not considered a sales charge)

SIE On-Demand Learning Guide

Fees and Charges

Ongoing fees are NOT sales charges

- These fees may be based on a percentage of assets under management or on amounts redeemed early from a fund

Management (Advisory) Fee	<ul style="list-style-type: none">Paid to the investment advisorAsset-based; not tied to profits or lossesTypically the largest of the fees
Administrative Fee	<ul style="list-style-type: none">Custodian bank paymentsTransfer agent costs
Redemption Fee	<ul style="list-style-type: none">Does not go to underwriter or dealerRemains behind in the fund, benefitting other owners

MF: Primary Market.

Closed End Fund: Secondary.

Ch. 7 Quiz.

Closed End Fund

- Shares trade on an exchange.
- Investors buy/sell shares in the open market.
- Only full shares may be purchased or sold.

12b-1 Fees: Distribution and marketing expenses.

Net Asset Value: synonymous w/the bid price or redemption (liquidation price)

Trustee manages DTD business activities of a Unit investment trust.

Expense Ratio: Determine the amt. that a fund charges its share holders each year for operating the fund.

An investor in a mutual fund **owns shares which represent an interest in the portfolio.**

Ex. NAV: \$13.20

POP: \$13.75

Sales Charge: \$0.55

NYSE: Close @ 4:00 p.m.

$$\frac{.55}{13.20}$$

Class A Shares: Front End.

Value Funds: Mutual funds that invest in stocks of companies that have good fundamentals, but are in sectors that are currently out of favor w/the market.

Index Fund: Low Portfolio turnover, few taxable events.

Activity

Read each description and indicate the type of investment company.

PORTFOLIO IS SUPERVISED, NOT MANAGED

SHARES MAY TRADE AT A PRICE LESS THAN THE NAV

A FIXED AMOUNT IS PAID AT A SPECIFIC DATE

SHARES ALWAYS REMAIN IN THE PRIMARY MARKET

UIT
Closed End Fund
Face Amount Certificate
Open End Fund

discounts
premiums

Chapter 8

Types of Annuities

Annuities are products that are sponsored by insurance companies in which investment income grows tax-deferred; they may be fixed or variable

	Fixed	Variable
Investment risk:	Insurance Company	Annuity.
Is it a security?	NO	Yes
Account:	General	Separate
Portfolio:	Safe, secure, predictable investments	Sub accounts that meet investor objectives.
Inflation hedge:	Poor	Superior.

An **annuity** is an insurance contract where you pay a lump sum or premiums in exchange for guaranteed, regular income (immediately or in the future)

No reduced tax rates for SCAFFABLE.

- Tax Free
- OR Taxable.
- That's it.

Question

As it relates to the accumulation phase of an annuity, which of these statements is/are TRUE?

Circle all that apply.

- Accumulation units are purchased after-tax and grow tax-deferred.
- Withdrawals are first considered a part of cost basis and not taxable.
- Death benefits are the greater of cost basis or the current value.
- Death benefits above cost basis are tax-free.

Payments.

- Straight life annuity
 - Annuitant gets payments for life.
 - Highest payout, high risk.
- Life Annuity w/ Period Certain.
 - Payments to annuitant for life or to beneficiary (in case of annuitant's death) for specified min. # of years.
- Joint and Last Survivor Annuity.
 - Payment as long as annuitant is alive
- Unit Refund Life Annuity
 - Annuitant receives amt. \geq Original investment.
 - @ death, any remaining is paid to a beneficiary.

Local Government Investment Pool (LGIP): Allow investments by State, County, and City ONLY.