Different Kinds of Stocks

Size, Style, Sector & Risk for Beginners

Where Are We in the Course?

So far, we have learned:

- What a stock is, and how prices move.
- How to read charts (OHLC, candles, volume).
- Basic indicators (moving averages, RSI, etc.).

Now we ask a new question:

- Are all stocks "the same kind" of thing?
- Or are there different **species** of stocks?

In this lesson we will:

- Classify stocks by **size**, **style**, **sector**, etc.
- Tell stories about how they behave.
- Connect each type to **what kind of risk-taker** it suits.

Size Matters: Market Capitalization

One simple way to classify a stock is by how **big** the company is in the market.

The basic idea is **market capitalization** (market cap):

$$\text{Market cap} = \text{share price} \times \text{number of shares}.$$

Think of market cap as:

- "How big is this company in the stock market world?"
- Not the same as number of employees or physical size, but a good proxy for its **financial weight**.

Large-cap, Mid-cap, Small-cap

In practice, stocks are grouped into buckets (rough ranges, differ by country):

- **Large-cap:** very big companies (large market cap; giants everyone knows).
- **Mid-cap:** medium-sized companies.
- **Small-cap:** smaller, often younger or more niche companies.

Story:

- Large-caps are like **big cruise ships**: slow to turn, usually more stable.
- Small-caps are like **speedboats**: can move fast, but can also flip quickly.

How Size Affects Behaviour

	Large-cap	Mid-cap	Small-cap
Size	Very big	Medium	Smaller
Price wiggles (volatility)	Usually smaller (smoother)	Medium	Often large (bumpier)
Liquidity[1] (ease to trade)	High (easy to buy/sell)	Medium	Often lower (harder to trade size)
Info / coverage	Many analysts	Some coverage	Often less coverage

In charts:

- Small-caps often jump around more from day to day.
- Large-caps often have **smoother** moves.

We can measure "wiggliness" later using the standard deviation of returns, but for now we use the visual and intuitive idea: more jumpy $\Rightarrow$ more risky.

[1] Liquidity means how easily and quickly you can buy or sell a stock at or near the current market price, without moving the price too much.

Which Sizes Fit Which Risk Takers?

Think of three types of beginners:

1. **Very cautious**
   - Does not like big ups and downs.
   - Sleeps better when things move slowly.
   - More comfortable with **large-cap** and some safer mid-cap stocks.
2. **Moderate risk-taker**
   - Okay with some bumps for higher potential return.
   - Might mix large-cap and mid-cap, and a bit of small-cap.
3. **Aggressive risk-taker**
   - Chases higher growth even if the ride is scary.
   - More willing to hold **small-caps**, including volatile ones.

Style: Growth, Value, and Income

Size is not the only story. Two companies can be the same size, but **behave very differently**.

A common way to classify them is by **style**:

- **Growth** stocks.
- **Value** stocks.
- **Income / dividend** stocks.

These styles describe the kind of **story** behind the stock: fast-growing, underpriced, or paying out cash.

Growth Stocks: The Fast Runners

Growth stocks are companies expected to grow earnings and sales quickly.

Typical features:

- Revenues and profits are growing fast (or expected to).
- Often **reinvest** most of their profit back into the business.
- Price often looks **expensive** compared to current earnings (high P/E).

Story:

- Like a young athlete who runs faster each year.
- People pay a lot for the ticket (the stock) because they expect a big future.
- If growth slows or disappoints, the stock can drop sharply.

Value Stocks: The Underpriced Shop

Value stocks are companies that look “cheap” compared to their fundamentals.

Typical features:

- Lower ratios like price/earnings (P/E) or price/book.
- The market may be pessimistic or ignoring them.

Story:

- Imagine a good shop that is not very fashionable.
- The sign is old, the website looks ugly, but the business is okay.
- A value investor says: “This shop is **worth more** than the current price suggests.”

Income Stocks: The Cash-Flow Friends

Income or **dividend** stocks regularly pay out part of their profits to shareholders as **dividends**[2].

Simple total return idea over some period:

$$\text{Total return} \approx \frac{P_{\text{end}} - P_{\text{start}}}{P_{\text{start}}} + \frac{\text{dividends received}}{P_{\text{start}}}.$$

Story:

- These are like **rental properties**: you care about both the price of the house and the rent.
- Beginners who like regular income often feel more comfortable with such stocks.

[2]Dividends are payments that a company chooses to distribute to its shareholders, usually in cash (sometimes in extra shares), as a share of its profits. They are not guaranteed and are decided by the company's board.

Which Styles Fit Which Risk Takers?

Very cautious beginners:

- Prefer **income** and some **value** stocks.
- They like steady businesses and dividends.

Moderate risk-takers:

- Mix of **value**, **income**, and some **growth**.
- Okay with some price swings if story makes sense.

Aggressive risk-takers:

- More willing to hold **high-growth** stocks, even if prices jump up and down.
- May care less about dividends now, more about big future upside.

Penny Stocks: Tiny and Tense

Penny stocks are very low-priced shares (for example, a few dollars or less than a few dollars).

Story:

- They look cheap: "only 2 dollars, I can buy so many!".
- But price is just a number; what matters is the **business**.
- A move from 2 to 3 is **+50%**, but at the same time the company might still be very fragile.

Nature:

- Often small or micro-cap, low liquidity.
- Prone to big swings and sometimes manipulation.
- **Not** a good first choice for beginners.

Cyclical vs Defensive Stocks

Another lens: how does the business behave when the **economy** changes?

Cyclical stocks:

- Do well in good times, poorly in recessions.
- Examples: car makers, airlines, luxury goods, many banks.

Defensive (non-cyclical) stocks:

- Sell things people need even in bad times.
- Examples: basic food, utilities, medicine.

In a crisis (like Covid or a banking shock), cyclicals often fall more, defensives often fall less.

Which Suits Which Risk Profile?

For more cautious beginners:

- More comfortable with **defensive** sectors (staples, utilities, some healthcare).

For moderate beginners:

- Mix of defensive and some **cyclical** names.
- Accept that in recessions, cyclicals will hurt more.

For aggressive beginners:

- More open to cyclical sectors that can swing strongly (banks, airlines, discretionary consumption).
- Must be emotionally ready for deeper drawdowns.

Sectors: Different Parts of the Economy

Stocks are also grouped by **sector** or **industry**, for example:

- Technology
- Financials (banks, insurance)
- Healthcare
- Consumer staples (everyday goods)
- Consumer discretionary (nice-to-have goods)
- Energy, Industrials, Utilities, Real estate, ...

Each sector:

- Reacts differently to interest rates, inflation, and growth.
- Has its own typical risk level (e.g., utilities vs airlines).

Later, we can compare sector ETFs and see which sectors are calmer and which are wilder.

Summary: Matching Stock Types to Risk Takers

Risk profile	Often prefers
Very cautious beginners	Large-cap, defensive sectors, income/dividend stocks, some value stocks. Very little or no small-caps, no penny stocks.
Moderate risk-takers	Mix of large- and mid-cap, some small-cap. Combination of value, dividend, and selected growth stocks; mix of defensive and some cyclical sectors.
Aggressive beginners	More small-caps and high-growth names. More cyclical sectors. May experiment with some speculative and emerging market stocks, understanding that drawdowns can be large.

There is no single “correct” mix. The key is to match the **type of stock** to:

- Your **risk tolerance** (how much pain you can handle).
- Your **time horizon** (how long you can stay invested).

Next Steps

In the next lessons we can:

- Take real examples of each type of stock.
- Plot their price, volatility, and drawdowns.
- See how they behaved in different global events (Covid, rate hikes, banking stress).

For now, remember:

- Not all stocks are the same animal.
- Know what kind of animal you are riding before you get on.