

BARBADOS STOCK EXCHANGE INC.

SHARES 101

▼ A guide for new investors

► Introduction

Trading in shares has become an integral part of people's lives. However, the complex world of shares, bonds and mutual funds can be intimidating for many who still do not know what they are, where to purchase them and what they can offer to enhance investment opportunities. The purchase of shares is available to anyone who is eighteen years and older, not risk averse and who is looking for long-term opportunities to achieve their financial goals.

► Differences Between Stocks And Shares

None. There are always questions being asked about the differences between stocks and shares. The bottom line is that stocks and shares are the same thing, with any minor distinctions between them usually being overlooked. Discussions about the two terminologies have more to do with the syntax than with financial or legal accuracy. For example, "stock" is a general term used to describe the shares of any company and "shares" refers to a specific stock of a particular company. So, if investors say they own stock, they are generally referring to their overall ownership in one or more companies. If investors say they own shares - the question then becomes - shares in what company?

► What Is A Stock?

Corporations can raise capital through the issue and sale of shares. You become a shareholder in the company when you purchase shares and may have voting rights depending on the type of shares you purchase. A shareholder is an owner in the company and has a claim to part of the company's assets and earnings. You are also entitled to receive a dividend payment when the company has performed well, you are however not responsible for the company's liabilities (debt).

► Five Things To Know About Shares

- Shares represent part ownership in a limited liability company.
- Shares are your best shot for getting a return over and above the pace of inflation.
- Shares that perform strong in one year may decrease in another.
- A share value is dependent on the earnings a company makes.
- Shares are considered to be long-term investments.



► **What Is A Stock Market?**

The stock market can be described as a market place which brings together people who want to “sell shares” with those who want to “buy shares”. A number of shareholders trade in this market place and it is seen as one of the most important sources in which an investor can create wealth.

► **The Role Of The Stock Exchange**

The Stock Exchange facilitates trading in those companies listed on its board. It maintains records of the orders entered by each stockbroker and ensures that all orders are queued based on price and time entered.

To help in compliance with trading and settlement rules, intermediaries or brokers are given access to the stock exchange so that they can represent buyers and sellers and execute the trades. Anyone trading in or advising you on securities must be a registered broker with the Barbados Stock Exchange Inc. (BSE) and the Securities Commission of Barbados (SC).

► **Making A Start**

ABC Ltd wishes to raise \$900 in cash. They offer 100 shares for sale at \$9 per share via the capital market. You have heard about the share offer and decided that you would like to purchase some of the shares but you don't have a clue on how to go about making the purchase. After raising this capital through an Initial Public Offering (IPO) the company will approach the stock exchange to list on the board of the exchange. By listing on the board of the exchange the company provides an avenue by which the shareholders who participated in the IPO can trade their shares.

► **Where To Go And Who To Speak To**

Your first step is to choose an investment broker or stockbroker. To be a registered broker in Barbados the company must first be a member of the Barbados

Stock Exchange. A complete list of the registered stockbrokers may be found on our website www.bse.com.bb.

A **stockbroker** or **broker** is the direct link between you the investor and the company, ABC Ltd, whose shares have been listed on the stock exchange. The stockbroker provides investment advice and will help you decide if the purchase of shares is the kind of investment you want. When choosing a stockbroker you need to have confidence in, and be comfortable with both the stockbroker and the company who will handle your investment.

Stockbrokers charge a fee called commission, each time you buy and sell a stock. The commission charged is agreed upon between you and the stockbroker. Commissions are used to pay the broker's salary and for the services the company provides.

It is advisable to have a written understanding between yourself and the stockbroker.

► **Some Simple Questions You Might Ask In Your Investigation For A Stockbroker:**

- Is the firm in the market for new clients such as you, with your expected account size and your general investment objectives?
- Does the firm have any special expertise in the types of investment that might be of interest to you?
- What services does it provide to clients like you?
- Is the firm a member of a contingency fund designed to protect clients in case of insolvency? If so, what coverage does the fund provide?

► **Purchasing Of Shares Or Stocks**

Now that you are settled with your choice of stockbroker, you must open an account. He or she will then further advise you on the fundamentals of making a purchase of shares.

Financing your purchase depends on how much money you want to invest and the returns you wish to receive. Your choice of funding can include extra funds set aside, bonus cheque, income tax refund or even a bank loan.

When you make your actual purchase, you pay your broker for the value of the stock plus a commission fee, the Barbados Stock Exchange Transaction Fee

of 0.25% on either side of the transaction. This simply means that the investor selling the shares pays 0.25% and the investor purchasing the shares pays 0.25% in transaction fee to the BSE. The BSE fees are paid to the broker on behalf of the BSE.

Therefore, if you wish to purchase 40 of the 100 shares issued at \$9 per share, you will pay \$360 for the 40 shares plus the broker's commission and the BSE's fees.

► **Quick Tips For Buying Shares Or Stocks**

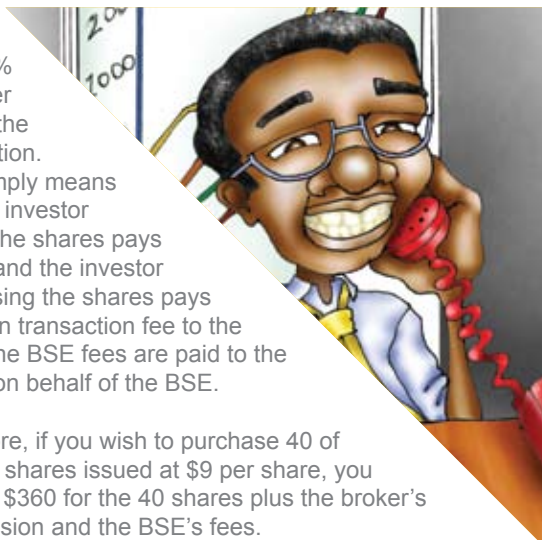
- Know the risk – the price of a stock can change and if the price falls after you buy it, you could earn less than you previously anticipated.
- Always purchase or sell your shares through a registered broker of the BSE – beware of the get rich quick schemes from someone stating they have a “great deal”. Genuine stockbrokers or financial advisers never work that way.
- Don't be quick to say that an investment in stock is not working for you. You never lose money on a stock until you sell it, as the price for that stock can rise in the long run.

► **Deciding On The Type Of Shares You Wish To Purchase**

A company can offer you the option of purchasing different types of shares. These include common or ordinary shares and preferred shares or stock. Your adviser can play a critical role in recommending to you the type of shares that are suitable for your financial goals.

► **Ordinary Shares Or Common Stock**

The purchase of ordinary shares or common stock gives you part ownership of the company, grants you a relative entitlement to dividends derived through surplus profits on a yearly basis, voting power over how the company will be run and a return on the liquidation of assets that may occur when winding up.



However, in the event that the company makes no profit the ordinary shareholder would not be paid a dividend for that period. In addition, if the company declares bankruptcy the ordinary shareholder could lose their investments as other creditors will be paid ahead of them.

► **Preferred Shares Or Stock**

Shareholders of preferred shares or preferred stock have priority over common shareholders in the distribution of dividends and assets and the right to buy more stock before it is placed on the open market. Each share of preferred stock is normally paid a guaranteed, relatively high dividend. In the event of bankruptcy, preferred stockholders have first dibs before common shareholders of the company's assets.

Preferred shares can be an attractive investment for investors who are somewhat more risk averse and desire a more stable investment. Preferred shares have characteristics similar to both equity and debt. As equity, the shares receive a dividend only if the corporation declares a dividend, and in liquidation the shares wait in line until all debt holders have been paid. Like debt, preferred shares pay a fixed return, and they have a liquidation preference over ordinary shares. Preferred shares can be issued in a variety of ways.

► **Advantages Of Investing In Shares**

- You can start off by buying a small amount of shares and build it up over time to increase your portfolio of investment.
- The income you earn from current shares can be used to purchase additional shares.
- You can sell off some of your shares to gain access to additional funds if needed.
- Shares can often be used as collateral for borrowing, which can include borrowing for additional share investment.

► **Steps To Making The Purchase**

Before you make your final decision be sure to ask any questions and get clarity on all information provided up to this point.

To place an order you have to tell your broker:

What type of shares you wish to buy –

There may be different types of shares issued by the same company. The broker will confirm the actual share you requested before making the investment on your behalf.

How many shares you wish to buy – In Barbados there is no minimum amounts of shares that you have to purchase but because there are costs involved (broker's commission and BSE fees) in making purchases it would make sense not to purchase less than a \$100 each time you wish to execute a trade.

The price you wish to pay for the shares – There may be a maximum price per share you are willing to pay. Your broker will not buy the share if on the day of trading the price is over your maximum limit, unless advised.

How long you want your order to stand – When you buy shares, you can advise your broker on how long you will wait for the shares to fall within your maximum price range. For example, you may ask the broker to let the order stand for 5 days, if the shares cannot be bought at the end of that period at the price you want, your order will expire.

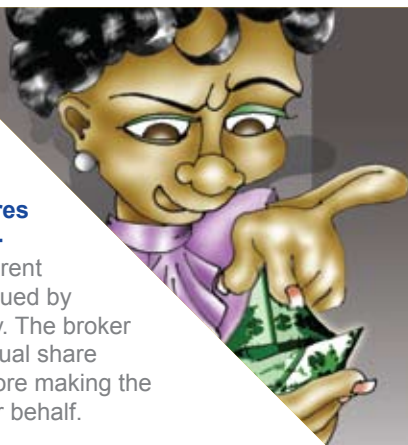
After the expiration date you will have to put in a new order if you still want to buy shares in that company. You can also instruct your broker to leave your trade in the market until it has been satisfied.

▶ Trading Days And Times

Trading on the Barbados Stock Exchange (BSE) takes place Monday to Friday from 10.00am to 1:00pm.

▶ Deposit Funds

Based on the amount of money you wish to invest be sure to have enough to cover the purchase. These funds may be deposited in your account at the brokerage company.



► Place Your Order

Orders can be made over the telephone, in person or via email. Once the order is filled, your stockbroker will send you information pertaining to:

- How many shares were purchased
- The price that was paid for the shares
- The commission and fee that were charged for buying the shares.

► Paying For Your Share Purchase

Money will be deducted from the cash portion of your account to cover the purchase of the shares.

► Record Of The Transaction

When full payment is made, ownership of the stock is transferred from the seller to you, the buyer. You will be sent a record (a statement) showing the amount of shares you bought, the price per share and the total price you paid. Keep the records and statements you receive in a safe place for easy reference.

► Settlement Cycle

A trade transaction requires a buyer and a seller. The buyer has to pay for the stock purchased and the seller has to deliver the stock sold. This process usually involves two brokers, one on behalf of the seller, the other on behalf of the buyer. Once the trade has been consummated, the share certificates must be exchanged for payment and change in the ownership of the shares must be recorded in the Issuer's Share Register. The timeframe for recoding these changes is currently T+3, and is called the "Settlement Cycle".

Effective January 1, 2006 the settlement cycle was guaranteed at T+3, as there will be a rolling/continuous settlement cycle for all trades. That is three (3) business days after the trade date.

► Making Money Through An Investment Of Shares Or Stocks

• Dividend Payments

As a shareholder in a company that issued shares you are entitled to receive money referred to as

dividends. A dividend is a portion of the company's earnings that is paid out to shareholders on a quarterly or annual basis.

The dividends paid to preferred shares are deducted as an expense because they are required payments, unlike the common stock dividend which is just a divided-up part of the profits. Therefore, if you own preferred shares, you will receive your dividends before payment is made to the common stock shareholders.

If the company is not able to pay a dividend for the current financial year the common stock shareholder would receive nothing for that financial year. On the other hand preferred shareholders will still receive the accumulated amount when the company is profitable again.

- **Sale of Shares and Stocks**

Another way of earning money from the stock market is by selling your shares at a higher price than you paid for them. If you have a large amount of shares and you are looking for quick cash you might ask your broker to sell off some of the shares for you to raise the necessary revenue.

- ▶ **Taxation And Your Stock Earnings**

The purchase of shares is tax free, however when you earn income from the stock investment, which is 'non-sheltered', you have to pay taxes on your earnings. As with everything else taxes can really impact on what you make when you invest.

In Barbados, a tax incentive is given when investing in new shares up to a limit of \$10,000. This must be in the form of an Initial Public Offering (IPO) or Secondary Offering such as a rights issue.

There is no capital gains tax in Barbados, so when you sell your shares any gains on your investment is not taxed when you liquidate your investment.

- ▶ **The Real Return On Stocks After All Costs**



Investing in shares or stocks is a good way to achieve your financial goals, however you need to understand the real cost for, and the real return of your share investment. You need to include all of the fees, charges and penalties you pay when you buy and sell shares. Also include the taxes due on your earnings.

To calculate your total return on an unsheltered stock investment you can

* **Calculate what it cost to buy and sell**

Commission fees + any additional brokers fees
+ interest on loan (if you borrow to invest) + BSE
Transaction Fee = total investment cost

* **Calculate your total return**

Your gross proceeds – your total investment cost –
your total tax = your total return.

► **Stock Terminology**

As you become more involved in the stock market you find a number of terminologies being used to describe the market and the activities involved within it.

• **Annual General Meeting**

The annual general meeting or AGM is a meeting of the shareholders which must be held every calendar year to enable them to review the records of the company, elect directors and vote on any referendum.

• **Bear**

An investor who believes that a particular security or market is headed downward. Bears attempt to profit from a decline in prices. Bears are generally pessimistic about the state of a given market.

• **Bond**

A bond is a debt investment with which the investor loans money to an entity (company or government) that borrows the funds for a defined period of time at a specified interest rate.

• **Bull**

An investor who thinks the market, a specific security or an industry will rise.



- **Capital Market**

The capital market (securities markets) is the market for securities, where companies and the government can raise long-term funds. The capital market includes the stock market and the bond market.

- **Contract Note**

A contract note is sent to a buyer or seller confirming the transaction and showing details as to price, brokerage and any other charges involved.

- **Deer Market**

A flat market. Neither a bull nor bear market, a deer market is characterized by low activity, with timid investors waiting for a sign of which way the market is going to end up moving. The term is used to illustrate when investors who are unable or unwilling to move due to uncertainty, like deer, freeze when “caught in the headlights” of a vehicle.

- **Dividend Declaration**

The dividend declaration gives the date the directors of the company fixed the dividend, the amount to be paid for the final dividend along with the date on which the dividend is to be paid.

- **Earnings Per Share (EPS)**

The portion of a company’s profit allocated to each outstanding share of common stock. EPS serves as an indicator of a company’s profitability.

Calculated as:

$$= \frac{\text{Net Income} - \text{Dividends on Preferred Stock}}{\text{Average Outstanding Shares}}$$

In the EPS calculation, it is more accurate to use a weighted-average number of shares outstanding over the reporting term, because the number of shares outstanding can change over time. However, data sources sometimes simplify the calculation by using the number of shares outstanding at the end of the period.

Diluted EPS expands on the basic EPS by including the shares of convertibles or warrants outstanding in the outstanding shares number.

- **Float**

The total number of shares publicly owned and available for trading. The float is calculated by subtracting restricted shares from outstanding shares.

Also known as “free float”.

- **Limit**

An order to a broker which places a limit on either the highest price that may be paid or the lowest price that may be accepted.

- **Market Capitalisation**

Market capitalisation or market cap refers to the aggregate value of a company’s outstanding common shares. Market capitalisation in essence, reflects the total value of a company’s equity currently available on the market. It is the number of common shares multiplied by the current price of those shares.

- **Market Index**

An index is a way of measuring how a market is doing and where it is going. The plural of index is indices. Therefore, if you hear the index went up, it mean that most of those stocks rose in price on that day, or a few heavily weighted stocks rose significantly. An index can help you see how well a stock is doing compared to other similar stock trading on the exchange.

- **Offer**

The offer or ask is the price at which someone is prepared to sell shares.

- **Odd-lot Market**

The odd-lot market is the amount of a security that is less than the normal unit of trading for that particular security. For stocks, any transaction less than 1000 shares is usually considered to be an odd lot.

- **Price/Earnings Ratio (P/E)**

A valuation ratio of a company’s current share price

compared to its per-share earnings.

Calculated as:

$$= \frac{\text{Market Value per Share}}{\text{Earnings per Shares (EPS)}}$$

For example, if a company is currently trading at \$4.60 a share and earnings over the last 12 months were \$0.18 per share, the P/E ratio for the stock would be 25.55 (\$4.60/\$0.18).

EPS is usually from the last four quarters (trailing P/E), but sometimes it can be taken from the estimates of earnings expected in the next four quarters (projected or forward P/E). A third variation uses the sum of the last two actual quarters and the estimates of the next two quarters.

Also sometimes known as “price multiple”.

- **Primary Market**

The primary market is that part of the capital markets that deals with the issuance of new securities.

- **Prospectus**

The prospectus is a document provided to investors purchasing securities in the primary market. It contains full, true and plain disclosure of all material facts relating to the securities being offered.

- **Right**

A current shareholder can be granted the privilege of buying new shares in the same company, usually below the prevailing market price.

- **Yield**

In general, yield is the annual rate of return for any investment and is expressed as a percentage.

The yield is the dividend divided by the closing price of the stock.

With stocks, yield can refer to the rate of income generated from a stock in the form of regular dividends. This is often represented in percentage form, calculated as the annual dividend payments divided by the stock’s current share price.

For example, $\$0.18/\$4.60 = 3.91\%$. This is the measure of the return on an investment and is shown as a percentage.

With bonds, yield is the effective rate of interest paid on a bond, calculated by the coupon rate divided by the bond's market price:

$$\text{Bond Yield} = \frac{\text{Coupon Rate}}{\text{Current Market Price of Bond}}$$

► Test Your Knowledge

Test yourself by ticking the correct answers to the following:

1. If you buy a company's sharestock:

- a. You own a part of the company, and have a claim on its assets and earnings
- b. You have lent money to the company
- c. You are liable for the company's debt
- d. The company will return your original investment to you with interest.

2. Barbados' laws protect investors by requiring companies to:

- a. Show profits before they can sell sharestock
- b. Give investors important information
- c. Pay dividends
- d. Repay investors who have lost money

3. You invest in stock by:

- a. Depositing money in a savings account
- b. Buying shares of stock
- c. Asking your employer to buy some for you
- d. None of the above

4. To create a well-balanced stock portfolio intended for long-term growth, you should include:

- a. Stocks from several different industries
- b. Mostly big, financially strong companies with above-average earnings growth
- c. Stocks you can hold for a long time
- d. All of the above

5. If you place a limit order to buy a particular stock, what exactly do you want?

- a. To buy a limited number of shares
- b. To buy at a particular price, if the stock dips down to that price, your order will be filled
- c. To hold shares of the stock for a limited amount of time, then sell
- d. To buy shares at any price

Correct Answers

1 – a • 2 – b • 3 – b • 4 – d • 5 – b

This document is intended for general information only. It is intended to help first-time investors to better understand the stock market processes.



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