# FIN 366: INVESTMENTS
# MARKETS
# CRITICAL THINKING & CONCEPTUAL QUESTIONS

1. What are the two ways in which firms generally raise capital for investing in projects? When it comes to the cashflows or ownership of the firm, what are each of these sources of funds entitled to?
2. Firm managers may be concerned with increasing the size of their department and their power within the firm (known as *empire building*) rather than working to increase the value of the firm overall. What is this an example of, and how might owners of the firm combat this problem?
3. Given a firm's share price doesn't directly affect the profitability of the firm, why might the firm and managers care about the stock price?
4. Do public or private firms have more liquid ownership interest? What does it mean for ownership interest to be liquid, and why might this be desirable?
5. What is the commonly known way in which firms compensate employees and managers of a firm with ownership interest, and how might this address the agency problem?
6. Is the creation and issuance of new shares in a seasoned equity offering a *primary market* or *secondary market* transaction?
7. You are the founder of a public firm. You own 10 million shares of the firm's common stock trading on exchanges (out of 50 million total shares outstanding), but you decide to sell 500,000 of your shares for cash. Is this a *primary* or *secondary* market transaction?
8. A SPAC itself must first go public and be listed on an exchange before finding a private company target. Why doesn't the private company just go public directly?
9. In which of the three markets/exchanges/networks that we discussed are the following transactions likely to have occurred (traditionally)?
    a. A dealer views bid and ask prices for shares of DKNG, and trades from their own inventory, selling shares at their own ask and another dealer's bid
    b. A large institutional client submits an order to their broker to purchase 50,000 shares of RCL. Their broker seeks out a specialist who matches their buy order with another party's sell order.
    c. A broker submits an order for a purchase to buy 80,000 shares of BLK, and this order is automatically matched to a sell order.
10. You'd like to purchase 10 shares of stock in DLTR. You place an order on your brokerage app. In what ways might your order be satisfied? What methods are more likely given you are only transacting 10 shares?
11. What is PFOF and why is it controversial?
12. What is the ask price for a security? The bid price? Why do these differ, and do we expect they will be the same for all investors at a point in time for a given stock?

13. What is the bid-ask spread and how does it represent a trading cost for an investor? How is it a source of profit to the dealer?
14. Where does one find firm filings submitted to the SEC? Why are they valuable for investors?
15. In which of the SEC filings that we've discussed would you find the following items? (Some may appear on multiple filings).
    a. Microsoft announces earnings per share (EPS) last quarter was $8.05.
    b. Mark Zuckerberg discloses that he has sold 10,000 shares of Facebook.
    c. Adobe Inc.'s financial statements (income statement, balance sheet, cash flow), in a filing submitted to the SEC annually.
    d. A firm announces it is filing for bankruptcy.
    e. Google announces the items on the firm's ballot at the annual meeting and provides recommendations for how shareholders should vote.
    f. Following the fiscal quarter, Visa files an abbreviated filing that includes firm financial statements.
16. CHALLENGE **Dark pools** are private trading systems where large traders can submit orders to buy or sell significant amounts of stocks without disclosing to the general public the size and scope of their orders. In conventional exchanges, orders are visible. Why would an investor want to use a **dark pool**? What are some advantages of having your order secret? What might be some disadvantages of the existence of dark pools (think about *efficiency*)?
17. CHALLENGE Comment on the **dilutive** effects of a seasoned equity offering. For example, if you own one share out of a firm's 100 shares just prior to the firm issuing 100 new shares to raise additional capital, what does it mean for you as an owner of the firm?
18. CHALLENGE If a firm's stock has a "wide" bid-ask spread, do we consider the stock to be more or less liquid than if the firm had a "narrow" bid-ask spread?
19. CHALLENGE **High frequency traders (HFTs)** use algorithms to rapidly make trades in stocks and securities in fractions of a second – at speeds no human can compete with. For example, **HFT** algorithms might identify a stock trading for $0.01 more in one market than in another, and rapidly buy up the shares in the cheaper market to immediately sell the shares on the more market where the price is higher. Why is this practice controversial? In what ways might it be a *good* thing?
20. CHALLENGE **Shelf registration** allows a firm to issues shares gradually over a period of three years rather than all at once through an IPO. How might a firm use this to take advantage of favorable market conditions?