



FIN 366: INVESTMENTS

CRITICAL THINKING & CONCEPTUAL QUESTIONS

Chapter 3:

1. What is the difference between the primary market and the secondary market?
2. A firm's share price rises. Does this directly affect the profitability of the firm?
3. What are the two ways in which firms generally raise capital for investing in projects? When it comes to the cashflows of the firm, what are each of these sources of funds entitled to?
4. When a firm issues shares through an IPO, it is raising money by selling ownership interest in the firm. Why, then, might the firm want the share price to rise?
5. Do public or private firms have more *liquid* ownership interest? What does having more liquid ownership interest mean? Why might that be desirable?
6. Why does the SEC require shareholder meetings and annual filing of reports and financial statements?
7. Why might a roadshow be important for underwriters and firms seeking to raise money by going public?
8. How do SPACs take firms public?
9. How can buying on margin offer upside potential when investing in stocks? How can it amplify risks?
10. What are the *initial* and *maintenance margins*? What might cause the initial margin to fall to a point where a *margin call* occurs?
11. Describe the mechanism for how you can *short sell* shares if you don't own them. What does *covering the short position* mean?
12. Why does the value of your liability when buying on margin remain a constant dollar amount while the value of your liability when short selling fluctuates?
13. Without margin requirements, how could your losses from a short sale be theoretically unlimited?

14. In which of the three markets that we discussed are the following transactions likely to have occurred (traditionally)?
 - a. A dealer views bid and ask prices for shares of BLK, and trades from their own inventory by selling shares at the bid to another dealer.
 - b. A large institutional client submits a market 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 DKNG, and this order is automatically matched to a sell order.
15. You'd like to purchase 10 shares of stock in DLTR. You place an order on your brokerage account app. How might your order be satisfied?
16. 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?
17. Your employer tells you they need the last 10 years of a firm's official financial statements. What government agency website would you visit to retrieve this?
18. Where would you go if you'd like more information on the work history, licensing, and disciplinary information of a broker?

