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This is Dr. Bob Nolley, with a look at what goes on in the security markets. Now that we have examined the financial instruments themselves, let's see how they are traded. When companies issue shares of stock, it is most often done through an initial public offering-- an IPO.

When they do this for the first time, a privately-held company becomes a public company. They do this to raise funds for growth. When the company issues shares through its IPO, it doesn't pay the public investors back. The shares then get traded freely in the open market.

Executing an IPO does have the advantage of raising new capital, but there are disadvantages as well. Among those are the direct costs associated with an IPO. There is also information that needs to be disclosed.

Companies going through an IPO do this with the help of an investment banking firm, which is the underwriter. They help assess the market with the correct price for the issuance and navigate the initial sale.

The other disadvantage is, of course, the information needs to be disclosed. This could be useful to other competitors in that industry. The information that's being published is done so in the prospectus.

The second type of market is the secondary market. This market is not the issuance of new securities by an organization, but it's an exchange among investors in the marketplace. This is where individuals such as you and I execute trades. Because of the number of participants in the market is so great, it stays very liquid.

The third type of transaction is private placement. This is the initial funding of a block of securities that are not so publicly offered but rather privately to a specific group of investors.

The fourth type of transaction to be aware of is stock repurchases. This is also called a share buyback. This occurs when a company buys back its own stock. Companies may take on the strategy that it feels that if its stock is undervalued in the market to the point that is of value to distribute cash for the shares to the current stockholders.

Two things happen with the shares. They can either retire them or they can hold them as what is called treasury stock. Treasury stock is available for reissue.

It is also important that we look at the type of organization that the markets are themselves. There are three types of these. And the first is the auction market. In an auction market, buyers and sellers come together directly and buy and sell securities. Orders are centralized in the market. So the highest bidder and the lowest sellers can be connected.

An example of this is the New York Stock Exchange. On the floor of the New York Stock Exchange, traders physically gather around the specialist, who is the auctioneer, bringing buyers and sellers together.

The second type of market is a broker market. Broker markets are used only for securities that have no public market. Because there is no public market, there is a need for a middleman to take on the role of the broker. This broker provides information about the buyers and sellers and earns a commission for doing this. Municipal bonds are often treated in this way.

The third type of market is the dealer market. This market focuses on dealers who provide a service of continually bidding for securities that investors want to sell and buyers want to buy. NASDAQ and OTC markets are examples of this. So are foreign exchange markets. The dealers earn the commission by collecting a spread on the difference between the price bid and the price offered.

Now let's review the concepts from the lesson. Securities are traded in the primary and secondary markets. The primary market is where we find initial public offerings where companies issue new securities and raise capital. The secondary market is where investors and speculators exchange ownership of securities.

There are also private placements where securities are issued to a small group of investors. Companies can also repurchase their own stock to retire the shares or hold as treasury stock.

There are three main types of market organizations. The first is the auction market, such as the New York Stock Exchange, where buyers and sellers physically get together in an open auction. Broker markets are used for securities that have no public market and need a middleman to act as a broker. Dealer markets are quote-driven for the sake of continuously bidding for securities they want to buy and sell. Examples of this are NASDAQ and the OTC.

This is Dr. Bob Nolley. And I'll see you in the next lesson.

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