

Learning outcomes: Lesson 8

Making informed decisions about investments

Students

Learn how to manage their share investments.

Identify where to access the information needed to make wise decisions when investing.

How to interpret data relevant to investing.

Understand the terminology and strategies used by investors.

Lesson 8 allows students to build their capacity in managing share investments to ensure success. Students learn to understand the important terminology and strategies used in investing, as well as how to read and understand data relevant to investment, all essential skills in being a successful investor.

General capabilities related to this lesson

- Literacy
- Numeracy
- Information and Communication Technology (ICT) Capability

Terminology (skill directives)

Calculate: Ascertain/determine from given facts, figures or information.

Explain: Relate cause and effect; make the relationships between things evident; provide why and/or how.

Identify: Recognise and name; establish or indicate who or what someone or something is.

Justify: Support an argument or conclusion.

Links to curriculum

Australian Curriculum

Subject: Economics and Business

- Year 7
- Year 8
- Year 9
- Year 10

NSW

Subject: Commerce

- Core 1: Consumer and Financial Decisions
- Core 2: Economic and Business Environment
- Option 1: Our Economy
- Option 2: Investing

Solutions

Activity 1

Scenario

- Domino's Pizza (DMP) with a range of \$73.50
- \$42.15
- \$0.36
- Fortescue (FMG) at 2,695,436 shares traded
- The high dividend yield of 5.88 % for Fortescue (FMG) indicates that this may be a good company to invest in for a retiree as it offers a potentially solid level of income for the amount invested.
- 8.83
- The lowest share price in the year proceeding 23 December 2022 is \$31.67
 - The highest share price in the year proceeding 23 December 2022 is \$39.63

Activity 3

Statement	True	False
a Fundamental Analysis must be used in conjunction with other strategies to make it effective.	<input type="checkbox"/>	<input checked="" type="checkbox"/>
b A high P/E ratio may indicate that a share may be too expensive relative to the potential earnings through dividends.	<input checked="" type="checkbox"/>	<input type="checkbox"/>
c Technical Analysis uses charts to track patterns to assist in predicting trends to identify the best time to buy and sell shares.	<input checked="" type="checkbox"/>	<input type="checkbox"/>
d Dividend yields are the best way to track the value of shares over the long term as they indicate ongoing high levels of profits.	<input type="checkbox"/>	<input checked="" type="checkbox"/>
e Shares that are fully franked are more attractive to investors because they then pay less income tax on them.	<input checked="" type="checkbox"/>	<input type="checkbox"/>
f Shares that are fully franked are more attractive to investors because they then pay less income tax on them.	<input type="checkbox"/>	<input checked="" type="checkbox"/>
g An overvalued share may be a reflection of a company's future potential.	<input checked="" type="checkbox"/>	<input type="checkbox"/>

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Glossary

Bull or Bear Markets: A bull market is a rising market as a “bull” tosses market prices up. A bear market is a falling market as a “bear” claws market prices down.

Franking Credits: Also known as imputation credits, many companies in Australia pay tax to the Australian Taxation Office (ATO) on their profits. This tax paid is often made available as a deductible benefit to shareholders as a franking credit, possibly reducing the tax investors need to pay on dividend income.

Company Tax: Taxes paid by companies on profits made, directly to the Federal government. Currently companies in Australia are taxed between 25% to 30% on profits, depending on the size of the company.

Capital Gains Tax: Is the tax paid on the increased value of an asset by an investor at the point in which they sell their asset. For example, if a person purchases \$1000 worth of shares and sells them in a year for \$1500, they may need to pay tax on the \$500 increase in value in the asset.

Clearing House Electronic: Sub-register System (CHES) A computer system used by the ASX to manage share transaction settlement and record shareholdings. Investors are given a Holding Identification Number (HIN) to easily identify their shares and to view all their shareholdings in one place.

Investing for Growth: Buying shares at a low price and selling at a high price, achieving capital growth.

Investing for Income: Investing in companies that pay high dividends.

Fundamental Analysis: This approach analyses the fundamentals of a company, the broader economy, industry sector, the management of the company, and the company’s

competitors. Fundamental analysis involves an in-depth analysis of the company, including the company’s profits, dividends, its assets, and management. (Refer to Lesson 3 for information on influences relevant to fundamental analysis).

Technical Analysis: Technical analysis (also known as charting) involves looking at past movements in share price and the volume of shares traded in a particular company to identify any patterns that can be used to predict future performance. It can be used to complement fundamental analysis in the determination of the best time to buy and sell shares. This approach to investing, looks at patterns and market trends to signal the best time to buy or sell a stock.

Dividend Per Share (DPS): This indicates the dividend paid, expressed in cents per share. The last dividend in the company’s financial year is classified as final and all others are classified as interim. The DPS is calculated by adding any interim dividends and final dividend payments. If a company increases its dividend substantially the stock will have greater appeal to investors who are looking to earn income from their investments.

Dividend Yield: This measures the return on money invested. It is calculated through the formula:

$$\frac{\text{Dividend per share} \times 100}{\text{Share price}} = \text{Dividend Yield}$$

It is used to compare the income generated from dividends compared to other investments. Investors should consider that this ratio will change depending on the dividend paid by a company year-to-year and may be difficult to predict.

Earnings Per Share (EPS): Earnings per share are calculated by dividing the net

profit of the company by the total number of shares issued. A history of the EPS paid by a particular company shows the growth in earnings from one year to the next and the relative size of earnings to dividends.

Price Earnings Ratio (P/E ratio): This ratio is commonly used to ascertain a stock’s relative value, to ascertain if it is overpriced. It is calculated by dividing the current share price by the earnings per share (EPS). For example, for a company that has earnings of 20 cents per share when the share price is \$2.00:

$$\text{P/E ratio} = \frac{\$2.00}{20 \text{ cents}} = 10.0 \text{ times}$$

A high P/E ratio indicates the company’s share price is high relative to its earnings. This may be because investors have confidence in the future growth of the company. It may also indicate that a company is too expensive. P/E ratios tend to be higher when the economy is booming. P/E ratio comparisons between companies have more relevance when in the same industry i.e. comparing the P/E ratios of NAB with the Commonwealth Bank.

Net Tangible Assets (NTA): NTA gives an indication of what each share in a company is worth if all the assets were liquidated (sold) and all debts were paid and the proceeds were distributed to ordinary shareholders on a per share basis. NTA is frequently referred to as the asset backing per share. Investors sometimes use the NTA to assess the desirability of a share. If the NTA figure is higher than the share price, it may mean that the company is undervalued. This may make it more likely to be involved in a corporate take-over. If the NTA is less than the share price then the market may be overvaluing the company or it may be a reflection of the company’s future potential.