

What Causes Stock Prices to Change?

Suggested Grade & Mastery Level

Middle School – all levels

Suggested Time

50 minutes

Teacher Background

The following lesson discusses influences that effect stock prices. We can consider the stock market a living entity because of its volatility—and stock’s ability to change price minute to minute. A number of factors may determine this change. Market forces such as supply and demand at times determine share prices. If more people want to buy a stock (demand) than sell it (supply), then the price goes up. Conversely, if more people wanted to sell a stock than buy it, supply exceeds demand and the price falls.

Many factors determine what makes people favor a particular stock and dislike another. Fundamental data such as P/E ratios and projected earnings help investors place a value on a stock. News events, positive or negative, can also influence the price of a stock. There are always varying opinions on what is good or bad for a company, so news alone is seldom the sole determining factor of price, but it can influence its change. News that moves a stock’s price may be a result of internal corporate activity, industry trends or information based upon national or international occurrences including political, social or even scientific events.

A stock’s price change indicates what investors believe a company is worth. The price of a stock not only reflects a company’s current value—it also reflects the future growth and earnings that investors expect. The most important factor that affects the value of a company is its earnings. Public companies must report their earnings four times a year (once each quarter). “Wall Street” carefully watches earnings results. Analysts base their opinions about future value of a company on its earnings projections. If a company’s results are better than analysts expected, the stock price rises. If a company’s results are worse than expected the stock price falls.

Earnings are just one way to change investors’ opinion of a stock and ultimately, its price. Investors have developed literally hundreds of variables, ratios and indicators that help predict or determine stock price changes. Forecasting prices consistently is almost impossible.

The main forms of stock analysis are fundamental, technical and quantitative. Each approach involves following various market indicators to decide whether to buy, sell, or hold. This lesson, however, will touch on the analysis of outside influences (i.e., current events). It is a broader and more basic approach to understanding the influences of the market.

Vocabulary

Earnings: Whatever profits or net income remains after subtracting the company’s expenses from its revenue (also called a company’s profit).

Fundamental Analysis: A primary method for analyzing a stock’s potential return. It involves assessing a corporation’s financial history and current standing, including earnings, sales, and management, as well as the strength of the corporation’s products or services in the marketplace.

Inflation: An increase in the general level of prices of goods and services.

Market Capitalization: A measure of the value of a company, calculated by multiplying the number of outstanding shares by the current price per share. For example, a company with 100 million shares of stock outstanding and a current market value of \$25 a share has a market capitalization of \$2.5 billion.

P/E Ratio: A company's closing price divided by its latest annual earnings per share. The Price / Earnings is the relationship between a company's earnings and its share price. It is calculated by dividing the current price per share by the earnings per share.

Quantitative Analysis: Analysis focused on a corporation's financial data including looking at profit-and-loss statements, sales and earnings histories and the statistical state of the economy.

Technical Analysis: Tracking price movements and trading volumes in various securities to identify patterns in the price behavior of particular stocks, mutual funds, commodities, or options in specific market sectors or in the overall financial markets.

Performance Objectives

Students will be able to:

- Discuss the various ways stock prices are influenced.
- Interpret charts and graphs to better understand the growth and change in stock prices.
- Analyze and interpret market indices, which influence change in the price of stock.

Subject Areas

Economics, Mathematics, English Language Arts, Technology/Research, Business, Social Studies

Materials

- Internet access and/or Newspapers for current events (teacher may ask students to bring in copies of newspapers from the last few days)
- **Activity Sheet 1 – The Ripple Effect (3 copies per team)**
- **Activity Sheet 2 – Influences on the Market**

Springboard Activity

List the following pairs:

- I-Pod vs. I- Phone
- Video tapes vs. Digital recordings
- Digital cameras vs. Film Cameras
- Slide projector vs. SmartBoard

ASK

- In your SMG team, discuss which product in each pair you believe is the better investment.

Discuss the answers, noting that new products reduce the demand for old products, which affects the value of the companies that make both products.

Procedure

Explain: Share prices fluctuate for many different reasons. In addition to new products replacing old ones, what are some other reasons that you can think of for a company's stock to rise or fall?

Elicit various reasons and list these reasons.

Explain that today we will focus on the impact of current events on stock prices.

Distribute and have students discuss **Activity Sheet 2**, which contains four different scenarios.

ASK

- Which of the four companies' stock would you purchase? Why?

Novice and Apprentice Levels:

Have students review their portfolios in their SMG groups. Have each student choose one company for follow-up research. Track possible influences on the price changes that have occurred within the last two weeks.

Master and Grand Master Levels:

Have students download a quarterly report for one of the companies in their portfolio, (<http://www.tva.gov/finance/reports/pdf/3rdq05.pdf>) and create a PowerPoint presentation reviewing the reasons the company's shares were up or down. Have students write their predictions about the future of the company. Have students make these presentations in class and discussed their conclusions.

Assessment

Distribute **Activity Sheet 2: The Ripple Effect**. Use this sheet in conjunction with the instruction below.

Novice and Apprentice Levels:

Distribute newspapers or ask the class to go to a news website on line. Have each SMG group select one current event story they believe will influence the stock prices of a company.

Have each group present its headline and its determination of the event's impact on the stock price of that company.

Master and Grand Master Levels:

Distribute newspapers or ask the class to go to a news website on line. Have each SMG group select one current event story it believes will influence stock prices.

Have each group present its headlines and determination of the event's impact on stock prices by:

- Identifying the industry effected
- Listing three to five stocks from that industry
- Explaining how the current event will influence stock prices for those companies and in that industry

Application

Novice and Apprentice Levels:

Stocks are easily influenced by world events. Have students select a stock in their portfolio that is most likely to be influenced by the news. Have students explain how current events may increase or decrease the value of that stock.

Master and Grand Master Levels:

Have students download a recent quarterly report for the most successful stock in their portfolio. (<http://www.tva.gov/finance/reports/pdf/3rdq05.pdf>) Have them use the report together with current events to create a presentation that convinces their team members to either sell or purchase more of the stock.

Enrichment Activities

Have students create a quarterly report on a stock that the SMG group has chosen and present it to the class. They may use a downloaded version of a quarterly report as a model for creating their own report. (<http://www.tva.gov/finance/reports/pdf/3rdq05.pdf>).

Have students present their reports as PowerPoint presentations or with charts and graphs. Students should make the document come alive and be graded on their creativity in dispersing the information. Presentation rubrics are available in the Assessment section of the SMG Teacher Support Center.