Guide to getting started with stock trading

A beginner's guide to building a stock portfolio.

Qtrade Direct Investing

Write Your Own Future

Contents

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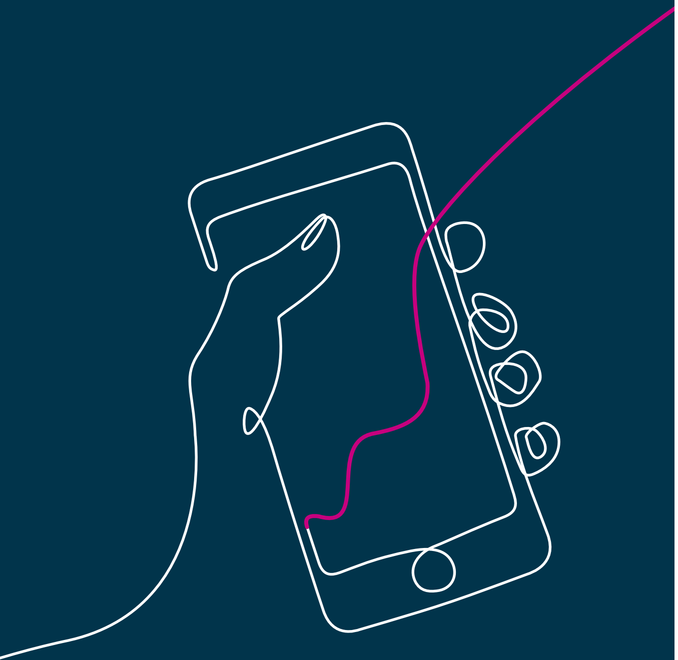

If growth is your long-term investing objective, you'll likely want to allocate a portion of your portfolio to stocks (also called shares).

Introduction

What do most successful investors have in common? They invest in the stock market. And for good reason—over the long term, stocks have outperformed other asset classes, including cash and bonds.

If you own shares of an equity mutual fund or exchange-traded fund, have an employer pension plan, or contribute to the Canada Pension Plan (CPP), then you are invested in the stock market, if only indirectly.

Managing your own portfolio of individual stocks is different, though. Instead of letting a professional investment manager choose stocks on your behalf, you're opting to research, buy and sell stocks on your own. Your goal is to choose specific stocks that you think will outperform the rest, without taking on more risk than is appropriate for you.

And there certainly is room to outperform. In 2020, the S&P 500—an American stock market index based on the performance of 500 large companies—posted a return of 18%. The challenge for stock pickers is to uncover those companies whose shares will excel in the future—and that's where some know-how and the right tools come in handy.

Stocks vs bonds: returns over 25 years—1993 to 2017

5.48%	9.69%
Bonds	**Stocks**

In this comparison, bond returns are represented by the Barclays U.S. Aggregate Total Return Bond Index. Stock returns are represented by the S&P 500 Total Return index (including dividends). Time period: January 1, 1993 through the end of 2017. Source: Bloomberg

What are stocks?

Companies sell stocks in order to raise money to fund growth and expansion. (Companies can also raise funds by issuing debt.) The portion of the company's balance sheet that is funded by shareholders is called shareholders' equity.

In exchange for providing the money, you, the shareholder, receive an ownership stake in the company, which includes a claim to future earnings.

The first time a company issues shares to investors is called an Initial Public Offering, or IPO. After that initial sale to the public, the shares can easily be traded—bought and sold— among investors. Stock exchanges and brokerages exist to facilitate those transactions and maintain an efficient, fast, accurate and cost-effective market for stocks and related securities. Your brokerage will keep electronic records of the stocks you own.

The price investors are willing to pay for a stock is based partly on the current value of the company's assets. But largely, the stock price reflects investors' opinion of the company's future growth and earnings potential. The more optimistic ("bullish") investors feel about a company's potential to grow its earnings, the more they are willing to pay for a share of those future earnings. But when investors feel pessimistic ("bearish") about a company's prospects, the stock price falls.

If you invest in a company's shares, you hope the company is successful and profitable, so that you'll receive a return on your investment. You can get a return in two ways:

- If the company grows its earnings and profits, shareholders may be willing to pay more for its shares. If you sell your shares for more than you paid for them, you'll realize a capital gain.
- The company may also distribute a portion of its profits to shareholders in the form of dividends.

Of course, like all investments, stocks entail risk. If the company's earnings or profits decline, its share price can fall below the price you paid. Then if you sell, you'll realize a loss.

Stocks

Stocks (also called shares or equities) represent an ownership position in a publically traded corporation

Details

- Canadian stocks that trade on the Toronto Stockl Exchange (TSX), TSX Venture Exchange (TSXV) and Canadian Stock Exchange (CSE)
- U.S. and foreign stocks that trade on the New York Stock Exchange (NYSE) and Nasdaq
- Over the counter (OTC) stocks
- New issues—including IPOs (intitial public offerings) as well as secondary or treasury offerings
- Rights and Warrants

Advantages

- Allows diversification across industry sectors and geography
- Accommodates strategies based on growth, or value, or on generating income from dividends
- You can borrow (trade on margin) to buy stocks trading for $3 or more on major stock exchanges

For a full list of all the investment options available at Qtrade Direct Investing, please visit us here https://www.qtrade.ca/en/investor/education/investing-articles/new-to-investing/investment-choices-explained.html

Types of stocks: common and preferred

There are two main kinds of stocks, which are quite different:

Common

These are what most people mean when they talk about stocks and stock prices. As an owner of common stock, you have the right to vote on certain company decisions, and to attend annual general meetings. Dividend payments are not guaranteed, but you may receive them if the company chooses to pay them. In the event of bankruptcy, common stock holders are last in line to claim the company's assets. (Bond holders are first in line, followed by preferred shareholders.)

Preferred

A hybrid security with characteristics of both a stock and a bond. Like a bond, preferred shares have a par value and pay a fixed dividend, typically every quarter. Like a stock, preferred shares represent an ownership stake, albeit without voting rights, and can increase or decrease in value. The shares are "preferred" since dividends must be paid on them before being paid on common shares, and also because in the event of bankruptcy, preferred shares rank ahead of common shares in claiming the liquidation proceeds.

Companies can add various features to their preferred shares. For example, the shares can be redeemable, meaning the company can buy them from investors at a preset price plus any dividends due. They can also be convertible, which allows investors to convert the preferred shares into a fixed number of common shares at a set price.

Categories of stocks: growth, value, income

Companies earn money differently. Some are fast growing, while others take a slow and steady approach. Investors divide stocks into three basic categories:

Growth stocks

Companies that are growing faster than the overall market and have substantial growth prospects in the foreseeable future. Generally, they don't pay dividends in order to channel earnings towards expansion (think about those up-and-coming technology companies).

Value stocks

Companies that seem undervalued and relatively cheap, given their solid fundamentals (for example, sales, earnings, dividends). Value investors look for underdogs and invest before others move in and drive up the stock price. Warren Buffet is a famous value investor.

Income stocks

Companies that have a track record of paying a regular dividend. Think about those slow and steady companies with solid cash flow—like a utility (people need to keep the lights on). When interest rates are low, dividend-issuing stocks are popular because their yields are typically higher than those of guaranteed instruments such as GICs. However, the value of income stocks can decline when interest rates rise.

Did you know?
If you own an equity mutual fund or exchange-traded fund, if you have an employer pension plan, or if you contribute to the Canada Pension Plan (CPP), then you are invested in the stock market.

Did you know?
A stock's price reflects investors' opinion of the company's future growth and earnings potential.

How many stocks should you hold?

Diversification

One key goal for any portfolio is diversification: you want to invest in a number of different assets, so that you achieve growth potential while controlling risk. In the context of stock investing, that means building a portfolio with several companies operating in different sectors, industries and markets. That way, a downturn in one industry or region won't torpedo your entire portfolio.

Number of stocks

The minimum number of stocks required for proper diversification is a subject of debate, with most experts recommending between 10 to 30.

Time

One related consideration is your available time. The more stocks you own, the more homework will be required to monitor the companies' performance and to remain aware of developments that can impact the companies and their sectors.

Start slowly

One option is to start slowly: buy shares of a small handful of companies, and supplement them with one or more exchange-traded funds or mutual funds for greater diversification. As you grow more comfortable and confident with stock investing, you can add shares of additional companies.

Four places to look for ideas

There are thousands of companies listing their shares on stock exchanges around the world.The question is, how can you narrow the playing field and identify the ones best suited for you?

Building a stock portfolio starts with ideas. Here are a few places to start hunting:

Economics and politics

Economic and political trends can have a powerful influence on a company's performance. Every country's economy moves through different cycles, from expansion and growth to contraction and recession. Some companies do better at different stages of that cycle. At the same time, major opportunities or challenges for companies can result from government decisions around taxation, interest rates, privatization, minimum wage laws, and so on.

Demographic and social themes and trends

From the rise of China as a major global economy to the wave of retiring and aging baby boomers in Western countries, big- picture themes are creating new markets and new demand for goods and services. In energy, healthcare, technology, and other areas, there are major shifts that could drive growth for companies that provide solutions.

Company announcement and industry trends

Financial results, mergers and product launches—these kind of company announcements can drive share prices in the short term and sometimes over the longer term as well. Bad news can push prices down as investors shed their shares, but good news can boost a company's stock price. As a stock investor, you'll want to keep tabs on the financial media and watch for developments in the industries and sectors that interest you. You may even want to directly monitor specific companies in order to get news as soon as it's released.

Analyst picks

Financial analysts continuously update their lists of stars and dogs—stocks they think are a good buy and others they recommend selling. Their reports provide specific insights and opinions into what companies are doing right, what they're doing wrong, and how that may or may not translate into gains and losses. Analysts aren't always right, but over time you may find some you trust more than others.

Evaluating companies

When it comes to analyzing stocks, there are two main approaches: **fundamental analysis** and **technical analysis**.

Fundamental analysis focuses on concrete information about a company's financial health and productivity. Investors study fundamental data in order to ascertain a company's intrinsic value. If you decide that a company's stock is priced below its intrinsic value, you have an attractive investment.

Technical analysis attempts to identify trends in the direction of a stock's price by focusing on pure market forces like price and volume. Investors who study technical data look for buy and sell signals in the data patterns.

Which approach is better is continuously debated. Many investors start with fundamental analysis before exploring the theory and practice of technical analysis.

10 key financial indicators explained

There are a number of fundamental indicators that give you a sense of whether a company's financial structure is sustainable and how well it's performing relative to industry peers.

To get you started, here are 10 key metrics for evaluating stocks.

Indicator		The calculation	What it indicates
1	**Earnings per share (EPS)**	Yearly profit / number of shares on the market	Profitability
2	**Price to earnings (P/E) ratio**	Price per share / earnings per share	Amount investors are willing to pay per $1 of earnings. The higher the ratio, the greater investors' expectations for earnings and profit growth.
3	**Price/earnings to growth (PEG) ratio**	P/E ratio / growth rate of earnings	Whether you're paying a discount or a premium for growth. A PEG less than 1 is usually preferred, because it indicates an undervalued stock.
4	**Price to book (P/B) ratio**	Price per share / Book value per share Book value = total assets minus total liabilities (there are other variations of this calculation)	How much shareholders are willing to pay for each dollar of a company's net assets. A value of less than 1 is usually preferred, because it indicates an undervalued stock.
5	**Debt-to-equity ratio**	Total liabilities / shareholders' equity	How leveraged a company is; how much debt it has relative to equity.
6	**Free cash flow (FCF)**	Operating cash flow - capital expenditures	How much cash a company generates after putting money into capital expenditures such as buildings or equipment. The more the better, and improving cash flow is a good sign.
7	**Return on equity (ROE)**	Net income / shareholders' equity	How efficient a company is at generating profits from money invested in the company.
8	**Return on assets (ROA)**	Net income / total assets	How well a company is doing at generating profits from its assets. The higher the better.
9	**Dividend payout ratio**	Annual dividends per share / earnings per share	Percentage of net income given to shareholders in the form of dividends. Important for income-oriented investors.
10	**Profit margin**	Net profits / sales	Profitability. How much a company earns from every dollar of revenue. Higher is better. Higher earnings with the same or lower profit margin indicates challenges controlling costs.

There are different key financial indicators for different industries and company types. For example, if you're evaluating a growing technology company, you might consider sales growth and EPS growth along with its P/E ratio. For a consumer products company, significant metrics include ROE and ROA. And keep in mind that typical values for specific indicators vary by industry, so it can be misleading to compare ratios of companies in different industries.

Placing trades

You've picked your stocks and you're ready to go—it's time to place your trades. In order to place buy order (or a sell order), here's what you need to know:

Whether you are trading on the Canadian or U.S. markets: The stock you want could trade on a Canadian stock exchange, on a U.S. stock exchange, or on stock exchanges in both countries.

The ticker symbol: Every stock has a short symbol to identify it on a stock exchange. (For example, Apple is AAPL, McDonalds is MCD, Procter & Gamble is PG.)

The currency it trades in: If you buy or sell a U.S.-dollar-denominated stock in your Canadian dollar trading account, your returns may be affected by the difference between the U.S. and Canadian dollars. It's called currency risk, and it can work for or against you depending on changes in the exchange rate.

The share price: Knowing the current share price, you can calculate how many shares you want to buy with the money you have available to invest.

Order type: When you place a straightforward "**market order**," it will be filled at the prevailing market price at the time the order is filled—with no limits placed on it from you. That means if there are big swings in the price of the stock, you could end up buying or selling for more or less than you expected.

A **limit order** gives you an added element of control—you can set the top price you're willing to pay to buy a stock, or the minimum price you will accept to sell a stock. Your trade will only be executed at that price or better.

Other order types can reduce (but not eliminate) the risk of losing money on stocks you own. A **stop market** order is an order to sell, but only if the market price drops below a certain level (the "stop price"). If the stock does in fact trade below that price, the stop market order becomes a market order, potentially allowing you to avoid further losses. Note, however, that in a volatile market your sale price could be well below the stop price.

A variation is a **stop limit order**, where you set a stop price and a limit price. If the stop price is reached, the order becomes a limit order, to be filled only at the limit price or better. Note that in a volatile market, the market price may fall below your limit price before the trade can be filled.

Did you know?
In exchange for your money, you, the shareholder, receive an ownership stake in the company, which includes a claim to future earnings.

Top tools for managing your stock portfolio

Qtrade Direct Investing™ provides a variety of powerful tools and resources for managing your stocks.

- Get real-time **quotes** on companies' stocks.
- Use **screeners** to quickly filter thousands of stocks and find the ones that suit your portfolio. Use prebuilt screens such as undervalued stocks or high dividend yield stocks or choose your own criteria.
- For any listed company, get complete **fundamental performance data**, so you can evaluate it and compare it to its peer group.
- **Technical analysis:** search and filter potential investments, and evaluate entry and exit points based on bullish or bearish indicators.
- Read **analyst recommendations** covering Canadian and U.S. stocks, including top picks for growth, value and income stocks.
- Scan the daily **Dow Jones Morning Briefing** or **Desjardins Morning Pulse** to gather stock trading ideas, along with market, business and economic news.
- Set up **watchlists** to keep a close eye on specific stocks.
- Set **alerts** to be notified when market events or stock price changes occur.
- Compare the performance of your portfolio against benchmarks and switch easily among multiple views including '**Valuation View**' and '**Performance View**.'
- **Account history** shows you all transactions on your account since inception including buys, sells, transfers, deposits, stock splits, and dividends.

Portfolio Analytics tools

Whatever your level of investment experience, build, evaluate and test your portfolio. Qtrade's Portfolio Analytics tools feature the industry's most advanced risk analysis and portfolio-building technology.

Portfolio Creator™ generates a tailored portfolio of exchange-traded funds (ETFs_ following a quick questionnaire on your investment preferences.

Portfolio Score™ lets you compare your portfolio's performance against domestic and global benchmarks. It grades your portfolio across five dimensions (e.g., downside protection, performance, diversification, income, and fees).

Portfolio Simulator™ allows you to create test portfolios in a simulator mode. You can easily add or remove securities in your portfolio to see how different holdings can affect your exposure to risks like inflation, U.S. currency and interest rate.

Qtrade Direct Investing: Write your own future

You've got goals. For your future. For your family's future. Pursue them with the confidence that comes from expanded investor knowledge and expert insights. And from tools that help guide your investment decisions.

With Qtrade Direct Investing, you'll have the confidence to buy and sell stocks, bonds, ETFs, and mutual funds - with low trading fees.

Execute with ease on an award-winning trading platform. Qtrade has consistently been ranked among the top online investing platforms in Canada.

Realize opportunity with industry-leading tools. Whatever your level of investment experience, build, evaluate and test your portfolio with calculators, and tools like Portfolio Creator™, Portfolio Score™ and Portfolio Simulator™, which feature the industry's most advanced risk analysis and portfolio-building technology.

Move forward with Canada's best online trading support. You can count on Qtrade. Friendly and responsive client service. Online self-help. How-to videos. An extensive library of articles and learning resources. And more.

How to open a Qtrade Direct Investing account

There are three steps to get your account up and running, so you can start investing:

1 **Complete our online application** from your desktop or mobile device.

2 **Fund your account** using an Electronic Funds Transfer or bill payment from your banking account; or by transferring assets from another investment account.

3 **Start investing!** www.qtrade.ca/apply

You can move money into your brokerage account from your banking account via electronic funds transfer, or by using your credit union's or bank's bill payment functionality.

Transferring other investments to your new online account

It's easy to move your investments from another brokerage to your new online investing account. At Qtrade, you can complete a Transfer form as part of your new account application, then print it and send it in along with your application. If you transfer $15,000 or more from another brokerage to Qtrade Direct Investing, we will reimburse up to $150 of your transfer-out fees.

The sooner you start, the more time you will have to reach your investment goals. Open an account at www.qtrade.ca/apply.

Not quite with us yet?

Before you commit to a trading account, you can still get a closer look at how Qtrade helps you invest with confidence. Take us for a spin with a trial account and check out the features that our community of Qtraders enjoys.

Sign up for a free 30-day trial account and see where investing confidence comes from.

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