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Curso de inglés económico, de finanzas y tributos

Module 7

Companies & Financial Markets

1. What's a company?

Every business begins with a person who has an idea about how to earn money and the drive to follow through on the idea and to create a business organization.

A **business organization** is an enterprise that produces goods or provides services. Most of the goods and services available in a market economy come from business organizations.

The purpose of most business organizations is to earn a profit. They achieve this purpose by producing the goods and services that best meet consumers' wants and needs.

In the course of meeting consumers' demand, business organizations provide jobs and income that can be used for spending and saving.

Business organizations also pay taxes that help finance government services.

Company (BrE)	Business organization (AmE)

2. Founding a Company

When people found or start, they draw up two documents: the **Memorandum of Association** (**U.S. Certificate of Incorporation**) and the **Articles of Association** (**U.S. Bylaws**).

The **Memorandum** sets out the company's objects (purposes), where the company has its registered office (where to send official documents), and the authorized share capital (the maximum share capital it can have).

The **Articles** set out the relationship between the company and its shareholders, and between them and the company's directors. It specifies the rights and duties of shareholders and directors as well.

3. Types of Business in the U.K. and the U.S.A.

There are different kinds of companies in the U.K. and the U.S.A.

The simplest form of business is the **sole proprietorship** (US) or **sole trader** (UK), an enterprise owned and operated by a single person. It also has unlimited liability for debts.

If several individuals wish to go into business together, they can form a **partnership**. Partners generally contribute equal capital, have equal authority in management and share profits and losses. However, a partnership is not a legal entity separate from its owners; like sole traders, partners have unlimited liability.

Consequently the majority of businesses are **limited companies** (US **Corporations**), in which investors are only liable for the amount of capital they have invested. The liability is limited to the value of their share capital (a shareholder's contribution to the company). These companies are legal entities, they have separate legal existence from their owners, the shareholders. Management is carried out by qualified managers and senior managers, known as directors.

Most of smaller businesses are **private limited companies** which are not allowed to sell their stocks and shares on an open market. They usually have 'Limited' or Ltd at the end of their name. Their owners can only raise capital from friends, banks and other venture capital institutions.

In the UK, private companies who make an Initial Public Offering become **public limited companies**. This means that they have their shares publicly traded on the London Stock Exchange (a market where anyone can buy stocks and shares). They have plc at the end of their name. These companies are also called **quoted companies**. They are required to produce a half-yearly interim report informing shareholders about the company's progress.

In the USA, the equivalent of a public limited company is one registered by the Securities Exchange Commission (SEC), known as **listed corporations**.

Listed Corporations in the USA are supervised by the SEC, an U.S. independent agency of the federal government. It holds primary responsibility for enforcing the federal securities laws, proposing securities rules, and regulating the securities industry, the nation's stock and options exchanges, and other activities and organizations. These corporations must prepare quarterly reports including the following information:

- the sales revenue or turnover (the money received by the Company in that period from selling goods or services),
- the gross profit (turnover less cost of sales) and
- net profit (gross profit less administrative expenses and tax).

In the U.S.A., we can also find a type of business known as **Limited Liability Company (LLC)** is a corporate structure in which its members cannot be held personally liable for the company's debts or liabilities. They are essentially hybrid entities that combine the characteristics of a corporation and a partnership or sole proprietorship. It is much easier to set up than a corporation and it is designed to separate the business assets of the company from the personal assets of the owner, which has the effect of insulating the owners from the LLC's debts and liabilities. However, it has to be dissolved upon the death or bankruptcy of a member, unlike a corporation, which can exist in perpetuity.

There follows a chart with functional equivalents of business organizations in Argentina, the UK and the USA.

British Law	American Law	Argentine Law
Sole Trader	Sole Proprietorship	Unipersonal
Partnership	Partnership	Sociedad Colectiva
Limited Liability Company	Limited Liability Company	Sociedad de Responsabilidad Limitada
Public Limited Company	Corporation	Sociedad Anónima

4. Initial Public Offering. Primary and Secondary Markets

There is a moment that successful companies decide to go public, which means changing from a private company to a public one, by selling shares to outside investors for the first time.

To do so, they need to follow certain steps:

1. Get advice from an investment bank about how many shares to offer and at what price.
2. Get independent accountants to produce a **due diligence report**, a detailed examination of a company and its financial situation.
3. Prepare a **prospectus**, a document inviting the public to buy shares, stating the terms of sale and giving information about the financial position of the company.

4. The company makes an **Initial Public Offering or flotation**, an offer of a company's shares to investors (financial institutions and the general public).
5. An investment bank **underwrites** the stock issue, which means that it guarantees to buy the shares if there are not enough other buyers.

When a company first issues stock, it is sold to investment bankers in the **primary market**. However, most stock is then resold to investors through a stock exchange, a **secondary market** where securities (negotiable financial instruments which represent some type of financial value, e.g. stocks and bonds) are bought and sold.

Most people buy stocks as a financial investment, with the expectation that the stock price will rise and that they can resell the stock for a profit. Gains made from the sale of securities are called **capital gains**.

Major stock exchanges such as N York and London have a lot of requirements about publishing financial information for shareholders. This the reason why most companies use **over-the-counter (OTC) markets**, such as NASDAQ in NY and the Alternative Investment Market (AIM) in London which have fewer regulations.

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5. Stocks & Shares. New Shares Issue

Stockholder or shareholders own part of a company, called "shares". They hold certificates of such stocks and shares which represent said ownership.

In Britain, **stock** is also used to refer to all kinds of **securities,** including government bonds.

The word **equity or equities** is also used to describe stocks and shares. These are **listed** or **quoted** on stock markets/stock exchanges.

There are essentially two types of stock—common stock and preferred stock.

Common stock is share of ownership in a corporation, giving holders voting rights and a share of profits.

Preferred stock is share of ownership in a corporation giving holders a share of profits (paid before common stockholders) but no voting rights.

Most people who buy stock choose to buy common stock. Notice that both types of stock give a share of ownership in the corporation that entitles a shareholder to receive dividends. The difference is that holders of preferred stock receive guaranteed dividends and will be paid before common stockholders if the company is liquidated. As a tradeoff for this preference, holders of preferred stock generally have no voting rights in the corporation, and their dividends do not increase if the company's stock increases in value. Each holder of common stock generally gets one vote per share owned to elect the board of directors, which makes important decisions about how the company conducts business.

Companies that require further capital can issue **new shares**. If these are offered to existing shareholders first this is known as a **rights issue**, as the current shareholders have the first right to buy them. Companies can also choose to capitalize part of their profit or retained earnings. This means turning their profits into capital by issuing new shares to existing shareholders instead of paying them a dividend. There are various names for this process: **scrip issue, capitalization issue and bonus issue**.

Companies with surplus cash can also choose to buy back some of their shares on the secondary market. These are then called **own shares** (in the UK) or **treasury stock** (in the US).

There are different categories of stocks and shares:

Blue chips are stocks in large companies with reputation for quality, reliability and profitability. More than two thirds of these stocks are owned by institutional investors such as insurance companies and pension funds.

Growth Stocks are stocks expected to regularly rise in value. Most technology companies, with innovative products, are growth stocks, but there are exceptions. Some growth companies are simply very well-run entities with good business models that have capitalized on the demand for their products.

Income stocks are those which have a history of paying consistently high dividends.

Defensive stocks provide a regular dividend and stable earnings, but their value is not expected to rise.

Value stocks are stocks that investors believe are currently trading for less than they are worth, when compared with the companies' assets.

Car manufacturers, for example, are not defensive stocks (people buy cars when things are going well, but postpone car purchases when times are tougher). By contrast, companies in the utilities sector are defensive stocks. Utilities are essential and cannot be put off. Even in times of economic hardship, people need to keep their families warm (using natural gas, in most cases) and light their houses (using electricity).