TRANSCRIPT

Trading basics part 3: How to trade

Presenters: Nicholas Delisse and Matt Davison

Nicholas Delisse: Hello again and welcome back, everyone, to part three of our four part series on how to trade. We have a lot of really exciting information planned for everyone today and, of course, will be talking about trade tickets and different order types. Really building on what we talked about in part one and part two, addressing on how to implement that and actually get it into a trade. Now, with that said, we're going to break everything down into looking at what your balances are on Fidelity.com. We're going to talk about what those balances might mean. We are going to hit on what it means to trade on margin and the difference between using margin, using cash, and even borrowing on margin, because there is a difference between trading on margin and borrowing on margin. We'll even screenshare a little bit and address how to actually place a trade. We'll show you different parts of the website to get a quote and what a lot of that quote information means and finding out your order status. So, a lot of this on the backend of the presentation will be screenshare where we'll step you through on how you actually implement this particular process. With that said, Matt, why don't you take us through what it means to trade on margin?

Matt Davison: Sure. Yeah, absolutely. So that's the place that we're going to kick off the presentation today. The concept of margin, what it is, what it might be useful for as well as some considerations that we need to take into account about how it can be a little bit more risky than a regular cash trading account. So, first thing -- what is margin? Margin is a way to borrow against the value of the securities that you already own. In effect, it's a loan that the broker's extending to you in order for you to be able to leverage your account. So what does this mean? Well, it means that you could take the money that we're loaning as the broker, you could use it to buy more securities, you could make a large purchase or potentially even use it as a bridge loan if you needed some sort of short term liquidity. Maybe that's to purchase something outside of stocks -- it could be something in your everyday life. However, the vast majority of people are going to use this in order to leverage their account in order to buy more securities. The other thing that is important to note about margin is that it does allow you to also trade a little bit more rapidly due to not having to worry about things such as settlement time. So, day traders for example, there are some requirements such as having 25,000 dollars in the account. There are certain rules that go along with day trading. However, it is important to note that just because you're using margin on your account doesn't actually mean you have to borrow anything. So, very important to distinguish the different uses of margin. However, there's also some things that we need to be aware of when it comes to margin. The first thing would be obviously the amplified losses. So the reason that we would leverage our account would be to buy more securities. Obviously if these go in our favor this going to be beneficial. We're going to make more money. We do have to take into account things like the interest that we're going to incur from making the loan or borrowing from the broker. However, generally speaking if we have the positions on our account on margin go in our favor, we're going to have the ability to have better returns. However, this cuts both ways and the same that way that we could have more returns if things go in our favor, it can also amplify our losses if those securities start to depreciate against us. So we need to be very cognizant of that fact just because we're borrowing money doesn't mean that we're inoculating ourself from potentially amplified losses. So, be very aware of that. The second part would be margin calls and or liquidation of the security. So what do we mean by that? Well, if you are borrowing money to buy more securities, if we do have those securities go against us this could put us in what's called a margin call. What this means is basically the equity in the account is too low. So, the amount we own versus what the amount we owe is -- it's out of order. It's too low. Therefore, this could potentially lead to either the broker or you yourself having to go in there and liquidate a security even if it's not exactly the time that you want to liquidate and the reason for this -- the rules state that within a certain amount of time these margin calls do have to be met. Typically that's going to be as soon as possible. As stated before, losses greater than the original investment amount are possible, so it is potentially a thing where if you go in and you start the account with a certain amount -- whether that be 10,000, 50,000, 100,000 -- that if you extremely leverage your account you could have a situation where possibly you actually lose more money than you initially put in. Doesn't happen often but it is certainly something that has happened -- probably will happen again unfortunately to somebody out there. You have to be very aware of that when you're managing the account -- make sure that this situation is not something that's going to happen to you. And then the other thing -- and it's very prescient right now due to the fact that interest rates were just raised by the Fed last week -- the interest rates may rise. What this means for us in a margin account is the fact that the increasing cost of a loan may occur. So the interest that we're having to pay in order to borrow money from the broker, that could go up and therefore we're going to have pay more margin interest, thus potentially reducing our profits if we have them, amplifying our losses even more if the positions are going against us. So, hopefully that was helpful in considering some of the risks that are associated with margin as well as the general uses why somebody might be interested in margin to begin with. With that being said, Nick, why don't you take us through here -- I know you wanted to look at the bid-ask spread for securities and talk about what defines a quote when we're looking at a security out there in the open marketplace.

Nicholas Delisse: Absolutely, Matt. Now, with the bid and ask spread, this is in essence defining what prices you're paying for securities. The bid is the highest price out there that somebody is willing to pay you for a stock. It's what they're bidding for that particular security. The ask is the lowest price out in the market that somebody is asking for their stocks that they're willing to sell you. And this is what can be referred to as the national best bid, best offer, or the highest bid in the lowest offer out there. Now, one of the easiest ways to remember what you're going to be trading at is to take a look at the two and look at well, which one of these is the worst price? Which one would I rather not be trading in? Well, if you look at the bid you see the bid is lower than the ask. Well, that's the one you're going to be selling to because you'd rather sell the higher one so naturally you're going to be selling at the lower one. The ask, of course, ask is going to be higher which we're going to be buying from. Now, the spread between the bid and the ask -- this is what market maker is going to make. And the more active a market is the tighter that bid and ask spread might be. So it might be a penny wide, it might be five cents wide, it might be 10 cents wide. The more active the market is the tighter that particular spread is, because what a market maker is going to do is, of course, you're going to buy for the bid, sell at the ask, make that particular difference. And that's for providing liquidity to the broader market. Now, you can always go in and you can be the asking price yourself if you wanted to sell it at the asking price. You can be the bid yourself if you want to buy and we'll talk about those particular order types -- those limit orders -- a little bit later on in the particular -- in our presentation. The last price, of course, that's the last price the security traded at which may be different than the bid or the ask. For a very a actively traded security, frequently the last price is close to the bid or the ask where somebody sold it to the bid. And the last price is the bid -- somebody bought it from the offer or ask, so the last price is the ask or it could've changed where maybe the last price is a penny or two higher or lower than the bid and ask might be. Now, the net asset value is a little bit different than the bid or the ask. The asset value applies to baskets of securities such as mutual funds, such as exchange traded products, exchange traded funds. This is the total value of all the assets that is being held by the mutual fund. With this, mutual funds are typically traded at the net asset value. You're buying it at the net asset value. There might also be a public offering price -- a POP -- which might be a little bit different. There might be a little bit of a premium the net asset value that you're purchasing to find out if it is a loaded fund. But when you're then going to sell it, you're typically then selling the fund at the net asset value with a mutual fund. Now, an exchange traded fund will also have a net asset value of what its underlying assets are worth, but it might be trading at a premium or a discount than the net asset value. And this is something we talked about in previous sessions because an exchanged traded fund will trade continuously throughout the day. It will have its own bid, its own offer, and a last trading price which, again, could be different from that net asset value. Now, on the next slide we'll talk about some of those differences that I was just mentioning. Mutual funds, of course, will show that prior day's net asset value with the value of the total value of the mutual fund's assets divided by the number of shares giving you that value per share. And it'll show you what that was the prior day. And if we're placing a trade for a mutual fund that will go through the next available net asset value which, in the middle of the day we don't know what the fund is going to close at. And actually, typically with mutual funds you get the four o'clock closing price, four o'clock Eastern Time closing price of the fund, but you might not know that until 6 or 7 p.m. later that night. You'll get a notification saying, "Well, your trade went through, this is how many shares you bought or sold from the mutual fund," if you, of course, place it on a dollar amount. Now, stocks, again, they're different. They're trading continuously throughout the day, bought at the ask, sold at the bid. You see the last price with that. Exchange traded funds, exchange traded products, just like I mentioned -- buy it from ask, sell it to the bid. You know what these are -- what these are -- they're being displayed in the market. Again, they do have a net asset value that's calculated but it doesn't trade at the net asset value like a mutual fund does. And you can actually look up to see -- for the exchange traded fund -- what its premium might be. That trading at 100 dollars and 10 cents and net asset value is 100 dollars and five cents. It might be trading at that premium or it could be exaggerated where the net asset value is 103 dollars and the exchange traded fund could be trading at 97 dollars. It could be trading at a significant discount versus a slight discount or slight premium. The better a exchange traded fund is at tracking a particular index, typically the smaller that premium or discount is going to be. Now, with that said, what can be important when we're addressing an ask price -- we're addressing a bid price is well, how are you actually going to place your order? And that gets into the different order types that we have. With that though, Matt, why don't you introduce to everyone the common order types that traders will use to place their trades?

Matt Davison: Yeah, absolutely. So there's a number of different order types that do exist out there. We're going to focus on the primary two that are on the simplified trading ticket on Fidelity.com, which we're about to show here in just a couple of moments. So, the first one is a market order. What a market order does is it's an instruction to buy or sell at the next available price. So, this can only be placed between 9:30 and 4:00 -- I say that -- we can place it outside of those hours, it can only be executed between 9:30 and four o'clock. The reason why is because it has to go to a market maker or an exchange where the order will be executed. So when you're selecting your time in force it has to be a day order. For the market order we know that we're going to get an execution if placed or it's within that time frame of 9:30 a.m. to four o'clock. The main thing to consider here is we will not know exactly what price we're going to get. We have an idea -- that's what Nick just showed us on the last screen. We have a bid price, we have an ask price -- it should be somewhere around the current market -- but we don't know exactly what it will be. If we're putting it in as a buy we expect it to be somewhere around the ask. If we're putting it in as a sell we expect it to put somewhere around the bid for the execution. Now, one other thing to keep in mind here, we note that this is generally very prompt for liquid securities, however if something is not liquid this is an order type that we might want to reconsider for two main reasons. First of all, the spread may be wide. The bid and the ask may be far apart and the last trade may not necessarily represent what you're going to get as your price. So, that's the first thing. The second thing is that it may take a little bit longer for something that's really a liquid for its to execute with the market order. Therefore we have this other type of order which is going to be a limit order and the main difference here is that we're actually going to specify the price for which we're willing to execute our trade at. So, if we're putting in a buy order and we select the limit price for the buy. What that's doing is we're saying we're only willing to buy the security if we're going to get this price or lower. Conversely, if we're putting a sell limit in, what that's telling us is we're only willing to sell the security if we can get this price as our limit or higher. Another main difference between a limit and a market order -- we don't have to put this in for just today. You'll notice that at the bottom here we have 180 calendar days, also known as a good-til-canceled order and the advantage of this -- especially if we're putting the limit somewhat reasonably far away from where the current market price is -- there's a good chance it's not going to execute immediately that day. Well, instead of having to go in there and replace the limit every single day, you can utilize this good-til-canceled order which leaves it in the system for that 180 days or obviously until it executes. Limit orders -- they can be filled in whole or in part. So what this means if -- let's say we put the order the sale of security 10 dollars away from where the current market value is for that security. Well, if it ever gets up to our price it may hit that but it may not be able to execute all of our shares. It may only be able to execute a partial amount of those shares. So, it is possible that you get a partial execution in which case if you're using that good-til-canceled order, it'll still leave that remaining part of the order open until the 180 days go by or, of course, until the rest of it executes. The other main factor to consider here execution is not going to be guaranteed if it's a limit order. And this makes sense if we start to think about it rationally. If we're putting in a price and the price isn't exactly where the market is right now, it's always possible that the market never actually gets to our price, thus meaning we never get an execution -- we don't either enter or exit the position. So, have to be aware of that. That is one of the advantages of the market. We know we're going to get an execution but we're not sure exactly what the price is going to be. With the limit order we know exactly what the price will be or better but it doesn't guarantee that it will actually ever occur. So, those are the two main order types. There's a handful more out there that are a little bit more advanced. We'll show you where you can maybe get that information when we do the demonstration here in just a moment. But just for simplicity's sake, we're going to leave it at those two order types for this presentation. And Nick, I know you wanted to share a story with everybody about the order types so I'll turn it back over to you here.

Nicholas Delisse: With these two order types I always think back when I was studying for the Series 7 exam years and years and years ago. We had a moderator that was trying to help us with the differences between market order and limit order and what they'd mentioned is to picture a market order. You're coming to a market. Think of it as like a farmer's market -- one of those markets you just see a whole bunch of people gathered around somebody that's selling something. And you come up and say, "Hey, I don't care what you're selling those things for -- just -- I want to buy some. Just sell it to me. We'll figure out the price later." That's a market order. And maybe the price is here, maybe it's up here, maybe it's down here. Market order -- you're just going to go in, you're going to buy or you're going to sell, you're going to get the trade done but you don't know what price you're going to get the trade at. A limit order, though, is the flip side. You're coming up and you're staying back a little bit and you're going, "Well, I'm interested in buying some but I'm only going to buy some if I can do it at my price." So you're going to be guaranteed your particular price that if they're willing to sell it to you at your price, they'll sell it to you. But if they're wanting to sell at a higher price, you might buy. It's no different than coming up and telling someone, "Well, will you take this amount for it?" And they can say, "Sure, I'll go ahead and sell it to you at that price." Or they go, "No, I'm sorry. I've got to sell it at this price or better." So, a limit order, again, you're guaranteed your price. You're only going to trade at your price or better but you might not be guaranteed the execution. So you have to think about well, what's more important to you? Getting the trade done or getting your price? And different traders have different priorities in this. When somebody's trying to get out of a trade because the market is moving against them, maybe it's more important that they get out right then than they get a particular price. I've seen traders that have tried to specify and say, "Hey, I really want to get out but only if I can get out at this price," and the market's going boom, boom, boom, boom. It's continuing to drop and it never came up to their price. They never got out. So, what's more important, getting your price or getting out -- getting your order filled? That's an easy, easy way to think about those particular differences between those orders. And these are basic, foundational orders that all those other complex orders are based on, so it's important to understand these two orders first. Now, with that said, why don't we go ahead and jump over into the screenshare and take a look at some of these concepts we've been talking about -- the way they look on the Fidelity.com/webpage.

Matt Davison: Yeah absolutely, Nick. And the natural place to start here, I think, is to look at the balances screen, kind of go through that, show you some important considerations for both the margin and the cash side of an account. So the way that we're getting here when you log in to your Fidelity.com screen it should automatically take you to this page. If you ever navigate away from this and you're wondering how do I get back here -- accounts and trade, portfolio, and that'll launch this page right here that we're seeing. So, in order to take a look at our balances and see where we stand in our account, we're going to come right here to this tab that says balances by clicking on this tab.

It's going to load our page and for this particular test account that we have here it is in fact the margin account. So, if you don't have margin on your account just keep in mind you're not going to see some of these fields that we're listing here this morning. So first of all, we can see our total account balance. We're going to have a current tab and then it'll also tell us the change for the day. Some other important things especially for the margin account -- you see the available without margin impact. So this is what we have left before we start running an actual margin debit. We have the non-margin buying power which is securities that are not eligible for margin. So, we could -- in this particular case we see 8,822 dollars and eight cents and we're seeing that's for options, mutual funds. Important to note they're not marginable for the first 30 days because technically they're new issues, and then also penny stocks, and then what do we see here? Well, we see the actual margin buying power. This is where we would be going in there and using additional borrowed money in order to purchase more securities. So, those are the big three right there. We also have available to withdraw amounts. You can see there's a cash only figure, there's also what we can borrow with our own cash plus the additional margin. One other thing to note here if you're ever not exactly sure what it is that these definitions are representing, if you click that eye with the circle around it, it'll define the terms for you. So, it'll define what it actually is, how frequently it's updated. You can see most of these are going to be intradays so that if you actually place a transaction or we have fluctuation in the market then we'll see that update on the actual screen right here. So, we have all of those things and then one other thing that we should note here if we're looking for our margin status. So if whether or not we're in a call or something along those lines, we can go to the current status for our margin equity, house surplus, SMA, exchange surplus, and we can monitor where our margin account stands as well as if we're running some kind of margin credit or debit we can see that here. If we're running a margin debit -- what that means is we're actually borrowing money from the broker. Keep in mind sometimes there's a lag between where the margin debit is created and the cash that is actually going to go over and cover that on the margin side of the account. I know that gets a little bit nuanced -- don't want to confuse everybody this morning but certainly something to take into account and help us monitor our positions. Some other things that we can notice here -- if we're looking at our cash account this is mainly what we're going to be using. So, we have the cash buying power and then we also have settled cash and that's important to note for our trading rules to avoid things like good faith violations, free rides, etcetera. And then finally on the balances we have the margin interests and what this would represent -- if we were actually running a margin debit balance -- meaning we're actually borrowing money from the broker, we would see the daily amount that we're being charged on the account, the accrued month to date interest that we have, and then also what the margin rate is. It's currently saying zero because we're not actually borrowing anything but if we were to start you would see this percent update to the appropriate level that you'd be borrowing at. So those are the balances. I know that's a lot of information there but hopefully that was helpful and getting you started onto where you can actually view where you are in terms of your -- either cash or margin account. With that being said, Nick, I know you wanted to take us through placing an actual trade here on Fidelity.com, so I'll turn it back over to you.

Nicholas Delisse: Absolutely, and one last thing I want to underline on the balances page for those traders that maybe have margin on your account but don't want to borrow on margin because there's a difference between trading in margin and borrowing on margin. That field that says available without margin impact -- that is the important field that if you're buying securities and you're staying underneath that available without margin impact. This account could purchase 6,050 dollars' worth of stock, mutual funds options, whatever, and as long as it stays below that this won't actually incur a margin debit balance. So that's important to know that's different from non-margin buying power, which is addressing buying a non-marginal security -- potentially still using your debit balance. If you stay below that it's not going to impact your margin. That's just something that's important to keep in mind and be thinking about. Now with that said, we're going to go ahead and shift our screen back over. We're back at that default landing page that Matt was showing us by going to accounts and trades and then portfolio. Let's say that we would like to pull a quote for a particular security. If you already have the position in your account you can simply go to positions and this is going to display all the particular positions you have in your account. We do have, for example, shares of Bank of America which is stock in this account, and it'll show you that last price, today's gain and loss information, of course the current value or quantity and then cost basis information here. As I clicked on this you'll see this tile down here -- we'll actually see the quote information. We see the bid and ask along with size -- what this size is how many shares are available at these particular prices. So, with this ask at 44 and 10 cents, size of 36 means you could buy 3,600 shares -- 36 round lots at those particular prices. So, it's just representing if you're looking to buy a lot of shares, how much might be available at those particular prices. We then, of course, have that last trade, 44 and 9 and about a half cents. It's between the bid and ask at this particular time. It'll even show you the change -- how much change from yesterday's last trade with that same information. Now, if you wanted to place a trade, these green bars are where you'll place the trade. If we wanted to buy more shares we could simply click on buy. If we wanted to sell the shares we had we could click on sell. And from our positions page if we click on buy, this actually pulls up a floating trade ticket with all this information in these drop down boxes. Now, let's say you were wanting to look at a security that we don't happen to own in our account. Maybe we want to take a look at Apple, both the largest company in the NASDAQ and the largest company in the S&P 500. Well, we could come here to the very top right hand corner says search or get a quote and type, "AAPL," because we know that's what Apple is. Click on here and this will pull up this particular quote information for us. This is our stock research page showing us that detailed quote information for Apple. We still see that last trade, how much it is up, and that bid and ask right here at the very top with Apple trading at 168 and 54 cents is that highest bid price -- the highest price someone is willing to pay for shares -- 168.55 cents is the lowest ask price -- the lowest price someone is willing to sell their shares for you. And, of course, see 168.55 which happens to be that ask price. Now, this was current as of when we pulled that quote up. But as we know, the stock trades continuously throughout the day. So, if we hit this refresh button we see the time right here. We refresh we'll see that time has changed. It's advanced now 30, 45 seconds. We're now seeing this bid and ask has changed so it might change between when you pull this up and when you actually want to place the trade. From here, of course, if we want to buy shares we could simply click buy. This'll pull up this stock trade ticket again for us. We can also come up here to accounts and trade and trade and this will also pull up a trade ticket where maybe we already know what we want to trade. Maybe you want to trade Microsoft. We'll simply come here and type, "MSFT," for Microsoft. Or we can even start typing MICRO for Microsoft for Microsoft and it'll pull this up and it'll look up that particular symbol for us. From here getting a real time quote. We can always come up here, hit the refresh button and refresh this. Now everything from here is a dropdown order ticket and this views are going to be the same field on that popup ticket that we saw before. Our action -- we're going to want to buy or do we want to sell? And actually if we click on that trade, buy, and sell buttons – well, it prefills buy for us. We do need to tell it the quantity, maybe we only want to buy one share. We're going to buy one share at market, it's going to go through at the next stable market price which is currently about 304 dollars and 10 cents. Maybe we want to specify a limit order where we only want to pay 300 dollars or less. Our order won't go through unless this price is met. Now, naturally you can leave it as good for the day where it's just good until the end of today or we can make it good until canceled -- good for the next 180 days like Matt mentioned. If we're, of course, placing this trade after hours -- let's say it's five o'clock p.m. Eastern Time -- market closes at four. If we make this a day order this order won't be good until the next trading day when the market opens at 9:30 the next trading day. If that happens to be Monday because it's a weekend or if it happens to be Wednesday because it's a Tuesday, go to the next trading day. Now, this is of course our standard ticket. We can of course go to our simplified ticket which changes the dropdowns for more toggle boxes. So with these toggle boxes we go can go buy as opposed to having that dropdown. We can also trade dollars instead of shares if we want to. Maybe you want to purchase only 200 dollars' worth of Microsoft -- roughly two thirds of a share. We can actually purchase fractional shares with this ticket as well. We would do this at market or limit prices with this particular ticket. We'd simply then fill out the rest of the ticket, hit preview, and then of course place our order to get the order placed. With that, this really addresses all the different ways you can place trades. There's so many, many, many additional ways that you could do this whether it's with stocks, whether it's with options or additional order tickets. If you want to learn more about the order ticket I do strongly encourage you to take a look at some of our group coaching sessions that we have that we offer through the Trading Strategy Desk. We'll actually spend an hour just on order tickets -- addressing some of those more complex order tickets. Additionally, if you want to learn about some of those others that we showed up on that dropdown, stop orders, trailing stop orders and such, we also have classes that are just on those -- just on risk management using stop orders. Now, lastly what I want to wrap things up with is let's say you placed an order and you want to see if your order was filled or not. Well, if you come back to this accounts and trade and then portfolio -- or accounts and trade and then account positions -- that will bring you back to this particular page. Now the portfolio drops you on the summary tab, the positions drop you on this positions tab. But if you come over here to activity and orders, once you've placed an order it will show right here. Now, naturally we never hit preview and place the order with the demonstration so the order isn't in the system, but if you'd actually placed an order it'll be right here. If you happened to place an order the prior day and it filled the prior day it will show under history. You'll see your previous history right there. But if you placed an order a week ago, two weeks ago as a good-til-cancelled order and it still hasn't filled yet, it will still show right here. With that, any last thoughts you have, Matt, before we wrap up?

Matt Davison: No, not really. I think this was a helpful session. It shows you how you can start to use the balances tab. You showed how to place a trade in Fidelity.com. There's other ways to place a trade, as Nick said, so if you're looking to further develop that education about how to use our platform, definitely check out some of the videos we have in our learning center, and maybe Nick we can just show where to access the learning center just briefly here so that people if they want to learn a little bit more they have a launch point. So, if you click on news and research, go down to the learning center.

It’s the second from the bottom. And once you get there -- first of all, we’ll have on the left hand side all these different things so investment products, investing and trading, advanced trading strategies, a number of different things as well as the strategy desk coaching sessions that’s what we actually work with. So, if you’re looking to further that education this is a great resource to kind of help you get started. So that’s my final thought. Certainly appreciate everybody joining us to watch this video and looking forward to seeing you in video four.

Nicholas Delisse: Thanks for joining us everyone, we’ll see you back for session four.

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Margin trading entails greater risk, including, but not limited to, risk of loss and incurrence of margin interest debt, and is not suitable for all investors. Please assess your financial circumstances and risk tolerance before trading on margin. If the market value of the securities in your margin account declines, you may be required to deposit more money or securities in order to maintain your line of credit. If you are unable to do so, Fidelity may be required to sell all or a portion of your pledged assets. Margin credit is extended by National Financial Services, Member NYSE, SIPC.

Stop loss orders do not guarantee the execution price you will receive and have additional risks that may be compounded in periods of market volatility. Stop loss orders could be triggered by price swings and could result in an execution well below your trigger price.

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