Activity 10.1
Save, Lend, Buy, Sell Cards

Directions to the teacher: Duplicate this sheet as necessary and cut cards from it in sufficient quantity to provide each student with one card.

You have saved $10,000. You are willing to lend the money if the borrower will pay interest.	You want to borrow $17,000 to buy a new car. You are willing to pay interest on the loan.
You have saved $3,000. You are willing to lend the money if the borrower will pay interest.	You want to sell MSTrans Incorporated stock to expand your business.
You have saved $20,000. You want to buy stock in Aerostar Corporation.	You need money to send your daughter to college. You are willing to sell your Burger Barn stock.
You have saved $14,000. You are willing to lend the money if the borrower will pay interest.	You want to borrow $5,000 to go on vacation. You are willing to pay interest on the loan.
You have saved $6,000 and want to buy StarPics stock.	You want to build a factory. You want to sell DelMouse corporate bonds to raise the money to build the factory.
You have saved $15,000. You want to buy Automotors corporate bonds.	You are the state government. You want to borrow $500,000 to repair roads. You want to sell bonds to do this.
You have saved $50,000. You want to buy NewsAmerica stock.	You want to borrow $10,000 to put an addition on your home. You are willing to pay interest on the loan.
You have saved $7,000. You are willing to lend the money if the borrower will pay interest.	You want to borrow $800 to buy a new refrigerator. You are willing to pay interest on the loan.
You want to sell your Electroworks stock and use the money to make a down payment on a house.	You want to buy 500 shares of Medicine Makers stock.
You have saved $20,000 and you want to buy LV Power and Light corporate bonds.	You want to sell your shares of Invest Up stock.
You have saved $2,000. You are willing to lend the money if the borrower will pay interest.	You want to borrow $15,000 to buy parts for your small computer company. You are willing to pay interest on the loan.

ACTIVITY 10.2
APPLE'S MISSING BILLIONAIRE

Many people know the story of how Steve Jobs and Steve Wozniak started Apple Computer in a California garage and later transformed it into the world's largest technology company. But few people know about Apple's missing billionaire, Ronald Wayne. Understanding the story requires knowing something about the three basic forms of business organization: *sole proprietorship, partnership,* and *corporation.*

If you have ever been paid to cut a lawn or look after children for a neighbor, you have been a sole proprietor: the only owner of a business, who receives all the profits and bears all the losses. When Steve Jobs did electronics work on the side as a young free-lancer, he was a sole proprietor.

In the early years, however, Jobs did little without his friend Wozniak, who actually invented the Apple I computer. Jobs got a local computer store to agree to buy 50 of the computers at $500 each—but neither he nor Wozniak had enough money to buy necessary parts for assembly. With the computer store's 50-computer order in hand, Jobs persuaded a supplier to provide the parts on 30 days' credit. Jobs and Wozniak built and delivered the computers, collected payment from the computer store, and turned around to pay the parts supplier on time. To continue financing their company, they sold personal possessions such as a prized Volkswagen bus.

Jobs and Wozniak soon learned that makeshift financing would not be sufficient to fuel Apple's growth. That's where the missing billionaire came in. Jobs and Wozniak called on their older friend, Ronald Wayne, for help. Wayne drew up a contract that officially made Apple a partnership, a business owned and managed by two or more individuals. (In a partnership the owners receive all the profits and bear all the losses.) The original contract gave Jobs 45 percent, Wozniak 45 percent, and Wayne 10 percent of the new company.

In a partnership, typically, all partners are responsible for the partnership's debts. Only two weeks after joining the partnership, Wayne got nervous because Jobs had borrowed $15,000 for materials on a new computer contract. (Jobs's borrowing inspired the card in Activity 10.1 that says "You want to borrow $15,000 to buy parts for your small computer company.") Wayne feared that he had more to lose because he had invested more personal money than the youthful Jobs and Wozniak. "I was getting too old, and those two were whirlwinds," Wayne later told an interviewer. (Source: Nick Allen, "U.S. Pensioner Gave Up £15bn Slice of Apple," *The Telegraph*, April 23, 2010, available online: http://www.telegraph.co.uk/technology/apple/7624539/US-pensioner-Ronald-Wayne-gave-up-15bn-slice-of-Apple.html.)

That is why Ronald Wayne gave up 10 percent of Apple Computer. He received payment in full for $1,500 later, when a check arrived in the mail.

Apple periodically struggled with finding enough funding. Keep in mind that in the early years, no one knew Apple would later succeed as it did. Some of its funding came from *venture capitalists,* investors who make money available for innovative projects. Venture capitalists face high probabilities of losses but also the possibility of large returns.

In 1980, Apple made an initial public offering of stock, offering its shares for general sale for the first time. The IPO set Apple's total value at $1.8 billion. After expenses, the proceeds of the IPO went to fund Apple's expansion. At this point it became a fully public corporation. Today anyone can buy Apple stock.

When Apple issues new stock as it did in 1980, it is engaging in *equity financing*. People who buy the stock get ownership shares or equity in the corporation. When Apple borrows money instead of issuing stock, it is engaged in *debt financing*. Debt and equity create different risks for the firm. Firms that use debt financing have to pay back the money on time or face severe consequences. Equity financing requires no fixed repayment—the firm can return large sums to stockholders if it is doing well, or it can return little or nothing if it is not doing well. But in using equity financing, a firm is selling off pieces of itself, whereas debt financing leaves ownership intact. Firms use a mix of debt and equity financing to get the funds used for their operations and growth.

In Figure 1 you will see numbered statements that apply to partnerships, proprietorships, and corporations. Be prepared to say which numbered statement applies to the listed statements (A. through F.) about Apple's financial history.

Figure 1: Advantages and Drawbacks of Different Organizational Forms

Sole proprietorship advantages	1. Easy to start up and shut down 2. Proprietor has control over profits and operations 3. Pride of being the only owner 4. Lower taxes (no corporate income taxes)
Sole proprietorship disadvantages	5. Personal responsibility for the business's debts (unlimited liability) 6. Difficulty in raising funds 7. Responsibility for all losses 8. Management's human resources limited to one person
Partnership advantages	9. Easier to raise funds than fund raising in a sole proprietorship 10. Management's human resources go beyond one person 11. Pride of being (with partners) the owners 12. Lower taxes (no corporate income taxes)
Partnership disadvantages	13. Profits are split among partners, rather than going solely to proprietor 14. Conflicts between partners possible 15. Possible instability when a partner leaves 16. Personal responsibility for the business's debts (unlimited liability)
Corporation advantages	17. Transferability of shares to anyone who wants to own stock 18. Unlimited life, even after death of founders 19. Liability of shareholders is limited to their investment
Corporation disadvantages	20. Costly to start up and shut down 21. Higher taxes (subject to corporate income taxes) 22. Separation of ownership (shareholders) from control (executives)

A. In the early years when Steve Jobs worked by himself, he knew he was good at marketing, but he missed the technical skills of his friend Steve Wozniak.

B. Worried about his responsibility for Apple's debts, Ronald Wayne left the young company after only two weeks.

C. The death of Steve Jobs in 2011 was difficult for Apple, but the corporation continued operations without interruption.

D. Apple shareholders have worried about executives' determination to spend whatever money it takes to defeat the rival smartphone operating system, Android, fearing the impact on profits and the value of their investment.

E. When Steve Jobs and Steve Wozniak were running Apple in the early days, they had disputes about required components for new designs.

F. It was easy for Steve Wozniak to get paid as a free-lancer for occasional technology jobs in California in the 1970s.

Activity 10.3
What It Means to "Go Public"

It is a big day in the life of an enterprise when it "goes public"—that is, it has an Initial Public Offering (IPO) of its stock. Until it is big enough to go public, it typically has to patch together whatever financing it can. Even if it has good products and a bright future, it may be limited in its ability to raise money to support its growth.

The simplest form of business organization, the sole proprietorship, is often quite limited in the funds it can raise. Bank loans and the owner's savings are possibilities. As soon as a proprietorship gives someone a piece of the enterprise in return for financing, it has turned into something different, typically a partnership. Funding for partnerships is limited to the partners' resources and what they can borrow. A growing enterprise may also attract the attention of investors called *venture capitalists* who specialize in identifying promising startups and providing funding in return for a share of the new enterprise. Because venture capitalists are working with risky startups, they require a high rate of return on successful projects to offset the losses that naturally occur some of the time. For venture capitalists, an IPO often represents a payday—a time when they can cash in their share of a new enterprise by selling their shares on the now-available open market.

When the enterprise goes public, it issues shares of stock that give each shareholder a piece of the company. The shareholders in turn provide funding that goes to the enterprise. Going public gives an enterprise access to the global markets. The amount of funds potentially available will be limited only by the quality of the firm's products and plans.

In our economy, IPOs are arranged by the set of institutions called the *primary market*. The primary market consists of those offering stock, those buying it, and the brokerages that bring buyers and sellers together. In the primary market, firms give up some control and they receive funding. They also take on substantial new requirements to report on their activities and finances to regulatory agencies. Reporting requirements are much stricter for public enterprises.

Once stock has been issued, the new shareholders may trade or sell their shares. For example, an investor who initially bought Apple shares in an IPO might convert those shares to cash by selling them on a stock exchange. This transaction is part of the *secondary market,* in which existing shares of stock are bought and sold. There are two important things to know about the secondary market:

1. Almost all of the stock market news you hear daily is about the secondary market. This includes all of the reporting about stock prices that went up and down on major stock exchanges. It also includes all of the reporting on stock market indicators.
2. Companies do not receive any funding when their stock trades on the secondary markets. Think about it: If Pat one day buys 100 shares of Apple stock from Terry, the money goes to Terry—not Apple. Years ago, when the shares were first issued, the money did go to Apple. But every time the shares have been traded on a stock exchange since then, money and shares changed hands without the money going to Apple.

Questions for Discussion

Classify each of the following situations as being part of the primary market or the secondary market:

A. A college endowment fund buys 40,000 shares of IBM stock on the New York Stock Exchange.

B. An excited reporter says, "Intel Corp. shares skyrocketed in trading today, with investors pushing the share price sharply higher."

C. Facebook, formerly a secretive and closely held enterprise, found that it would have to disclose financial data it had kept hidden before its widely celebrated Initial Public Offering.

D. A teacher leading a class in a stock market competition says, "Participants may choose any stock traded on the major exchanges."

E. The evening business news report says, "Venture capitalists found that a big gamble paid off today, walking away with a small fortune when the long-shot technology company GACC went public."