



The Long Position – Buy Low, Sell High

Buying stocks on a Long Position is the action of purchasing shares of stock(s) anticipating the stock's value will rise over time.

For example: Gary decides to purchase 100 shares of stock in Nike, Incorporated. Gary has decided to invest in this company after thorough research. His research indicated that Nike is a company with annual income growth, good management and excellent products.

Therefore, Gary buys 100 shares at today's closing price of \$82.00 a share.

$100 \times \$82.00 = \$8,200.00$ (the initial investment, not including the broker's fee)

One year later the price of the Nike stock is \$87.00 a share, an increase of \$5.00 per share from Gary's initial investment. The value of Gary's investment would now be as follows:

$100 \times \$87.00 = \$8,700.00$ (a gain of \$500.00, not including the broker's fee if he decides to sell)

The Short Position – Sell High, Buy Low

The Short Position is a technique used when an investor anticipates that the value of a stock will decrease in the short term, perhaps in the next few days or weeks. In a short sell transaction the investor borrows the shares of stock from the investment firm to sell to another investor. Investment firms normally have a large inventory of stocks on hand or can borrow stock from another firm to loan to the investor. Of course, the investor must eventually return the stock they borrow. The intent is to borrow the stock for sale at a high price, then buy them back later at a lower price to and return them to the stockbroker.

For example: Jill decides to short sell 100 shares of Ford Motor Company because she has heard rumors of a massive recall of their minivans. Jill thinks the value of Ford's stock will decrease in the next few weeks because of the high costs of the recall and the negative publicity.

Therefore, Jill borrows 100 shares of Ford stock from her broker and sells it to another investor for today's closing price of \$34.00. This action is referred to as short selling.

Two weeks later after notices of the recall have been publicized and other investors have reacted negatively by selling their Ford stock the price has fallen to \$28.00 a share. Jill decides to purchase 100 shares of Ford stock now to replace what she has borrowed from her broker. Jill's action of buying the stock is referred to as a short cover.

Here is what has taken place:

Jill sold 100 shares at \$34.00: $100 \times \$34.00 = \$3,400.00$ (Short Selling)

Jill then bought 100 shares at \$28.00: $100 \times \$28.00 = 2,800.00$ (Short Cover)

The transaction cost here \$2,800.00 (not including the broker's fee) but she gained \$3,400.00 from the sale. Overall, Jill made a profit of \$600.00. $\$3,400.00 - 2,800.00 = \600.00 (not including the broker's fee).

Although the idea is complex, all you need to understand is that you make money if the stock price goes down and lose money if the price goes up. A short position on a stock is a method of short term investing that is not common among the average investor.