



Brainy's Articles on Share Trading

Understanding share prices

Article No:
ST-2500
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31 Jan 2009

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Introduction

This article in Brainy's series on Share Trading (number ST-2500) provides information to help understand share prices, and what factors influence prices, and how to determine the "right price" for a specific share.

What events influence share prices?

Let's firstly have a look at the events that influence share prices, and what you might call the "right price" for a company's shares. The various influencing factors include:

- general news
- company news
- company announcements to the market (via the ASX)
- company results during the official reporting season (twice each year ~Feb, ~Aug)
- company earnings revisions (upward, and downwards), which can occur at any time during the year
- goodwill revaluation and impairment (write downs on forecast worsening conditions, as in a bear market)
- weather conditions (or adverse weather conditions)
- the economy, and whether it is good or bad
- government legislation which might affect the company
- disasters
- financial analysts' and brokers' analysis and ratings and recommendations
- stock rotation (where investors jump out of one stock and into another for a variety of reasons)
- sector rotation (where investors bail out of one market sector and hop into another, perhaps due to changes in the economy)
- index rebalancing (quarterly by Standards & Poors).

All of the above situations can have an impact on a company's share price. Some of these situations might result in a change in "mood" (or sentiment) of the market. And the resulting change can be overdone.

What is the right share price for a company?

- (a) It is possible to calculate a theoretical value for a company's share price (based on fundamentals). And many people do this.
- (b) But, what will it be worth in 6 months? or 12 months? How should you calculate the future value? Financial analysts do this using various assumptions. The assumptions might be to do with the weather, or the economy, or an estimate of the future price of crude oil or a base metal (for example). Over time, the assumptions might be proven to be correct, or they might be incorrect.
- (c) But as time goes by, this theoretical value will change based on various "news" and "events".
- (d) But at the end of the day, the market might disagree! That is, a company's shares are worth exactly what the market will pay for them. The theoretical price almost does not matter a hoot. If no one is prepared to pay the theoretical price, then it can't be the right price.

Share price behaviour can be strange?

Share prices can often change, but in a strange or unexpected way. Here are a couple of examples:

- (a) Why does the share price sometimes fall when there is good news?

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