Risks Involved in Investing into Stocks- a case study of 3 Stocks

Introduction

World Economy is going through tough times owing to economic crisis emerging in most of the developed countries of the world. Since 2007, the overall state of the economy is not healthy and as such many sectors and markets of the economy are suffering from low demand and depressed activity. From housing markets to banks and stock exchanges, almost every sector of the economy is suffering from adverse economic situation.

Such an economic environment, therefore, suggests that the overall risks of making investment either into the stocks or other forms of investment may be higher. Since stocks are considered as most volatile and risky investments, therefore, to make an investment into any stock requires considerable analysis and exploration of different factors which may have a direct or indirect impact on the stock prices.

Since 2007, overall activity in the stock markets has been depressed due to different factors and currently the markets are suffering due to sovereign debt crisis in EU zone. (Elliott). Despite such economic uncertainty and decline in economic activity, there are sectors which are booming and can provide one of the most lucrative investment avenues to the investors. Stocks like Facebook, semi-conductor industry stocks, as well as 3M are some of the stocks which can provide real benefits to the investors at every level. It is also, however, important to note that the personal risk and return preferences are always individual and remain as an individual decision.

This paper will discuss the risks involved in the stocks such as Facebook, NXP and 3M, as well as will explore as to how the risks may emerge and how investors can actually invest into such stocks.

Stocks Investment

Before discussing the different stocks, it is important to provide a general introduction to the stock investment and how they can be approached from the investment point of view.

Historically, the returns on the stocks, as well as bonds remained volatile; however, stocks have returned more over the period of time. It is also critical to note that the bonds are considered as safer investments because they hold the preference over the stocks and the bondholders are paid fixed interest income over the period of bond maturity. It becomes the obligation of the bond issuers to pay regular interest over the period of the bond and return the principal at the end. However, this is not the case with the stocks and the shareholders are not paid any principal at the end neither they are guaranteed that they will be paid regular dividends. These characteristics of the stocks, therefore, make them risky and investors can only invest into them if they believe and understand the overall risks involved. It is critical to note that stockholders, however, are given the ownership into the firms and they can also participate into the overall decision making for the firm (Siegel).

The value, return and risks on the stocks, therefore, are relatively unique and different and need expertise and certain degree of business acumen to decide as to whether to invest or not.

Facebook Shares

World is experiencing a new internet boom and internet websites are becoming one of the hottest investment avenues for the investors. Different types of websites and services such as Facebook, Google, Zynga have been able to attract huge attention of the investors due to the sheer potential of growth involved in them.

Recently Zynga, one of the leading makers of social games, launched its IPO and was successfully oversubscribed by the investors in the global markets (Raice and Randall). Such receptivity towards these types of stocks, therefore, suggests that the investors are ready to understand the risks involved into dot com companies and are also willing to assume them.

Facebook Inc. is the leading social networking site with millions of active users who use Facebook every day. What is important to note, that the overall user base of the site is global and as such it has global exposure. The overall revenue model of the firm is based upon running the advertisements and earning from them. Though Facebook is still a privately owned firm with little or no actual figures being released for the revenue earned but the unofficial estimates value the firm to the tune of $100 billion.

Facebook is in the process of launching its initial public offering and plan to raise approximately $10 Billion through this IPO (MacMillan and Womack). This is also considered as the largest and the biggest IPO in the history and this investment is considered as one of the lucrative investments to look for.

It is, however, critical to understand that history suggests that investing into internet or dot com companies may not be a wise option. During 1990's the overall value of the stocks pertaining to internet and technology companies soared to really high levels as investors were hoping for achieving capital gains. As a result of this drive, not only the venture capitalist thrived but on the back of that activity, stock prices of the internet related firms increased too (Gjerstad and Smith).

The bubble burst owing to many reasons including the Federal investigation against Microsoft. As a result of this, NASDAQ, which was already dominated by the technology related firms sharply declined and investors of such firms lost value. In the aftermath of the bubble bursting, many firms either merged with the larger firms or simply vanished.

The overall historical factors, therefore, indicate that the technology related firms may have unique risks and investing into such firms may not be without significant risks. Investors, consequently, need to make sure that they understand the risks well and before investing into such firms must individually determine their level of risk tolerance.

Facebook Inc, on the whole may offer a better opportunity for the investors with a lot of potential for the investors, however, the overall risks may be higher.

Semi-conductor Industry

Bazzell (2012) discussed about the potential available in the semi-conductor industry and for NXP stocks in special. This article outlines as to how the semi-conductor industry is actually contributing towards the growth of the smartphone industry.

The recent growth of smartphones has increased the demand for the micro-chips used in such phones and makers or such micro-chips are considered as one of the key investments to be made. Micro-chips are considered as essential for increasing the efficiency and speed of the smartphones. They do not only increase the efficiency and speed of the smartphones, but also allow smartphones to perform relatively complex tasks which are normally performed by Personal Computers.

What makes NXP, a Dutch company superior than others is the fact that its technology can allow smartphones to process cash and credit payments. NXP, therefore, is the leading firms in providing cash and credit payments processing through smartphones and is considered as the world leader. This technology actually makes smartphones as the electronic cash wallets thus increasing their overall utility for the consumers. Over the period of time, the value of NXP has increased and the stocks have outperformed the market. Its value has increased by more than 130% which is considered as the highest price increase in the technology industry.

This growth potential of the firm, therefore, can serve as one of the key parameters for the investors to consider investing into the firm. Since there are millions of smartphones in use and their number is increasing, thus, a shift towards this technology can really help not only the end users but also the firms offering cash processing through smartphones a real chance to capture this market.

What is also critical to understand, that there are already other large firms for example, Google which are also making plans to invest into this market. Considering the overall size and brand acceptability of firms like Google, therefore, can prove a significant challenge and strong competition for firms like NXP. If the larger firms are able to dominate the market, it is quite possible that the smaller firms may not be able to sustain in the market and resultantly may witness significant decline in their performance and value.

Investors, therefore, have to ensure that they understand the risks of investing into an industry which is fast changing. The inability of the firms to keep track of the technological changes, thus, can really sustain. This invariably, however, depends upon the ability of the firms to raise extra capital to sustain them. Investors, therefore, should be considerate of the risks involved in investing into such firms.

3M Shares

3M is an industrial conglomerate and is also manages one of the largest portfolio of brands in the world. This industrial conglomerate is one of the oldest businesses and is the maker of famous Post-It notes.

The recent performance of the firm suggests that the overall earnings of the firm increased by 3.1% suggesting that the firm is being able to recover from the current economic crisis. The overall performance of the firm has not been good in recent times due to the economic slump in major economies of the world since 2007 (HARLIN).

The firm's performance further deteriorated due to Tsunami in Japan and large scale flooding in countries like Thailand. What is critical, however, the firm has been able to make a recovery despite such economic crisis and is now considered as a bargain purchase for the investors. This is also due to the fact that the US economy is making a recovery, thus, giving 3M a much needed boost to make progress.

Though the firm is in the maturity stage, however, its overall range of portfolio of products, therefore, can be one of the key features allowing investors to bank on the firm. Due to overall diversity of the product range, 3M covers almost all markets and is deeply penetrated into the consumer segments of the market.

Conclusion

Investing into stocks is considered as one of the risky investments because of the overall risk characteristics of the stocks. Shareholders tend to assume larger risk because they are not guaranteed to be paid in case the firm goes into liquidity. However, stocks are also one of the best investments and offer the highest returns as compared to other investments such as bonds and T-Bills.

This paper has discussed three important stocks i.e. Facebook, NXP and 3M and provided a comprehensive view of the different characteristics of such stocks. Further, it has also been discussed as to how these stocks may be lucrative options for the investors while at the same time discussing the different risks which shareholders may have to assume if they invest into such shared.

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