WHAT ARE SHARES (ALSO REFERRED TO AS EQUITIES)?

Entrepreneurs need money to start a company and enable it grow. They can invest their own money or obtain a loan from a bank. But entrepreneurs can also appeal directly to savers and investors by issuing shares. Savers that buy shares in a company help the company to develop new products or explore new markets.

An investor who buys a share becomes a **shareholder** and therefore also a part-owner of the company. Accordingly, a shareholder is prepared to take risk. He is entitled to a share of the profits of the company if things go well, and he will also share in any loss the company sustains if things go less well, as the value of the share then generally goes down. In the worst case, the value can even fall to zero, for example in case of bankruptcy.

As part owner of a company, you have certain rights. You have a right to:

- a share in any annual distributed profit, referred to as the dividend.
- A part of the assets of the company if it stops operating and is liquidated.
- The right to vote at the general meeting of shareholders and information about the company.

If you buy a share of a company, you are entitled to an annual **dividend**. To receive this dividend, two conditions must be fulfilled. First, the company must make a profit or build up reserves; second, the general meeting of shareholders must decide to pay out a part of the profit to the shareholders. If one of these two conditions is not fulfilled, then you will not receive any dividend.

You can buy shares when the company decides to acquire capital from the public at large. The company then issues new shares. But usually shares are bought and sold on an exchange. This is a market where buyers and sellers of shares find each other. Shares that are traded on an exchange are referred to as listed shares.

The **market price** indicates the price of a share. This is the price at which shares can be bought and sold on the exchange. In theory, the market price is a compromise between the expected return on the one hand and the internal and external risks associated with the share on the other. This is because the supply of and demand for a share are also influenced by the risks to which it is exposed at any given time. As a result, the price fluctuates not only from day to day, but usually also within the same day.

If you buy and sell shares on the exchange, you can also benefit from a **capital gain** in addition to dividend. If you sell a share at a higher price than the price you paid for it in the past, you benefit from a capital gain. If you sell the share for less than the amount you paid for it, you sustain a **capital loss**.

Features

Issuing company: this is the company that acquires capital by issuing shares.

Dividend: you receive a dividend for the share in which you invest only if the general meeting of shareholders decides to pay out a part of the profit or the accumulated reserves to the shareholders. So you have no assurance that you will receive an annual dividend.

Some companies give the shareholders an **optional dividend**. You then have the choice to take payment of the dividend in cash or to buy new shares with your dividend. This choice is not always straightforward. Choosing to receive payment in cash makes sense if your focus is on minimising risk, if the shares in the company in question comprise a rather large part of your portfolio, or if the share is expensive. Otherwise, you can choose to have the dividend paid out in shares, as this gives you a tax benefit (i.e. no withholding tax) in some cases.

Capital gain: the price that you paid for a share in the past can be higher or lower than the current market price. If you sell your share on the exchange, then you will book a profit (i.e. capital gain) or loss (i.e. capital loss), depending upon the market conditions.

Term: in contrast to bonds, for example, shares do not have a fixed term. You get (part of) your initial investment back when you sell your share on the exchange. Please bear in mind that this can take quite some time.

Currency: a share may be listed on the exchange in a foreign currency.

Information: you can find information online about the company you invest in. For example, you can usually find the annual report, the reports of the shareholder meetings et cetera. If you would like more information, then you must ask for it.

Risks

Currency risk: a share that is listed on the exchange in a foreign currency constitutes a currency risk against the euro. Each time that you buy or sell a share, your euros are converted into the foreign currency or vice versa. In other words, due to fluctuations in exchange rates, the amount in euros that you receive if you sell it may end up being less or more than the amount you originally invested.

Liquidity risk: the liquidity of a share is an indication of how easy or difficult it is to buy or sell it on the market. Liquid shares are easy to buy or sell. Non-liquid shares are difficult or impossible to buy or sell.

Capital risk: If a company is in financial difficulties, the value of its shares on the exchange can drop steeply. In the worst case involving a bankruptcy, you will be paid back only after the debtors have been paid first. The chance that you will then still receive something is practically zero. The price of a share often anticipates difficulties. Even without bankruptcy, the value of the share can still fall to almost zero. So obtain sufficient information before investing in shares of a company, and preferably invest in shares of companies that you are familiar with.

Interest rate risk: changes in interest rates can have an indirect influence on the stock markets. If interest rates rise, it becomes more difficult for companies to borrow, and this increases the costs incurred by the company.

Price volatility risk: the price of a share fluctuates. This is referred to as volatility. The volatility of share depends heavily on the quality of the company, its activities, its results, and the general market situation. If a share is volatile, its price fluctuates strongly, and you can make a great deal of profit as well as sustain a great deal of loss.

Performance risk: you buy a share and the dividends turn out to be lower than expected year after year. You cannot know this beforehand. You will then receive little or no income.

Costs and taxes

If you buy or sell shares, you should also take into account the costs and taxes that you need to pay. After all, these will influence the return on your share.

COSTS

Brokerage costs: banks charge costs to trade your shares on the exchange.

Custody fee: Most banks charge fees to hold your shares in a custody account.

TAXES

Tax on stock exchange transactions (TOB): Each time you buy or sell a share on the exchange, you have to pay a tax on stock exchange transactions. If you buy a new share issued by a company to acquire fresh capital, you do not pay this tax.

Withholding tax on the dividends: you have to pay tax on the dividends paid by companies: withholding tax. The dividends on shares of non-Belgian companies are first taxed in the country of origin, after which they are subject to withholding tax in Belgium.

Capital gains tax: in principle, you do not have to pay any tax on the capital gain. An exception to this rule is the **speculation tax**. This tax is payable by every natural person who transfers shares for consideration (i.e. sells them) within six months of acquiring them for consideration (i.e. buys them).

Would you like to know more about shares?

Read our *Information brochure on financial instruments* on our website www.bnpparibasfortis.be. Some sections of this document were taken from www.wikifin.be.

032809800668

Responsible editor: A Moenaert - BNP Paribas Fortis SA/NV, Montagne du Parc/Warandeberg 3, 1000 Brussels, RPM/RPR Brussels, VAT BE0403.199.702 – june 2016