

Case Study 8: Understanding Stocks

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Instructions:

1. Print and read the following case study.
2. On your own, complete the **Accounting Application** questions.
3. As a class, complete the **Class Interaction and Discussion** questions.
4. Optional: Complete the **Small Group Extension Activity** and **Internet Exploration and Research Activity**.
5. Complete the **Summary Questions**.

Objectives:

After completing the following case study, you will be able to:

- Calculate stockholders' equity
 - Read a basic stock quotation
 - Define the stock investing terms introduced
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Study Tips:

Complete this case study after Chapter 21, Glencoe Accounting, First-Year Course.
Approximate time to complete: 2 hours.

Overview:

The world's largest do-it-yourself retailer, Home Depot, created its incentive program to reward employees with stock options in 1997. In an interview with *Newsweek* magazine, Chairman Bernie Marcus said, "We told them, 'If we make it, you're going to get the rewards.' And that's the reason they work so hard." Of course, anyone who invested in Home Depot's stock shortly after it was first offered in 1981 has seen huge gains. Adjusting for splits, Home Depot's stock was worth 70 cents per share in November 1985. After splitting again, the stock closed in July 1997 at \$47.87. An investment of \$1,000 in 1982 was worth \$152,000 in August 1997. That's some return!

Accounting Applications:

Instructions: Now that you have reviewed the case study above, answer the following questions on your own.

1. Record the following transaction: On November 15, Home Depot issued 100,000 shares of common stock valued at 70 cents per share with a par value of 5 cents. Use Memorandum 212 as the source document. Record the transaction on page 24 of the general journal.

GENERAL JOURNAL					PAGE <u>24</u>
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	
1					1
2					2
3					3
4					4
5					5
6					6
7					7
8					8
9					9
10					10
11					11
12					12
13					13
14					14
15					15
16					16

2. If Home Depot were to declare an annual cash dividend on common stock of 20 cents per share on 25,000 shares of common stock issued, record the general journal entry for the declaration. Use today's date, Memorandum 476 as the source document, and page 32 of the general journal.

GENERAL JOURNAL						PAGE <u>32</u>
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT		
1					1	
2					2	
3					3	
4					4	
5					5	
6					6	
7					7	
8					8	
9					9	
10					10	
11					11	
12					12	
13					13	
14					14	
15					15	
16					16	

3. On February 2, 1997, Home Depot reported 480,515,000 shares of common stock sold with a par value of 5 cents; Paid-in Capital in Excess of Par was \$2,523,093,000; and Retained Earnings were \$3,406,592,000. (The actual balance sheet also included an adjustment of \$3,005,000 increase, so please add this to your total.) Calculate Total Stockholders' Equity. (Round to the nearest thousand. For example, \$211,755 would round to \$212,000.)

Calculation:

Class Interaction and Discussion:

Instructions: Read the question below. As a class, discuss your responses.

In the business section of any major city newspaper you will find a listing of stock quotations for the New York Stock Exchange (NYSE), American Stock Exchange (AMEX), and NASDAQ, which stands for the National Association of Security Dealers Automated Quotation system. At the top of each column are headings that describe the stocks that are listed. Here are what some of them mean. (*Note: Stock quotes can also be found on the Internet.*)

Issue: Standard abbreviation for name of stock. It contains no spaces. Letters following a space are a footnote.

Div.: Dividend or cash payment the company currently expects to pay per share in the next year.

PE: Price-to-earnings ratio, or price divided by earnings per share.

Sales 100s: Number of shares traded yesterday in 100s (10 = 1,000 shares traded, 100 = 10,000, etc.)

Cls: Price at which stock sold when the Exchange closed yesterday.

Chg: Change between yesterday's closing price and previous day's closing price expressed in decimals (i.e., 0.125 = 12.5 cents; 0.25 = 25 cents, etc.)

Locate a recent stock quotation for Home Depot (HD), which is traded on the New York Stock Exchange. In the space provided below, record the dividend, price-to-earnings ratio, number of shares traded yesterday, price at which stock sold when the Exchange closed the day before, and change between the closing prices.

Stock Name: Home Depot

Date: _____

Issue: _____

Div: _____

PE: _____

Sales 100s: _____

Cls: _____

Chg: _____

Optional Small Group Extension Activity:

Instructions: Break into pairs and complete the following activity.

Choose a stock and locate its recent stock quotation. Record the stock name, issue dividend, price-to-earnings ratio, number of shares traded yesterday, price at which stock sold when the Exchange closed the day before, and the change between the closing prices.

Date: _____

Stock Name: _____

Issue: _____

Div: _____

PE: _____

Sales 100s: _____

Cls: _____

Chg: _____

Optional Internet Exploration and Research Activity:

Instructions: Using the Internet, research the following activity.

The Internet is one place to look for information about stocks. Look up the stock investing dictionary at the Investopedia Web site (www.investopedia.com) or use a similar online dictionary to find the definitions of these terms:

bear

blue chip stock

margin

share repurchase

Summary Questions:

1. What is capital stock?

2. Name two transactions involving dividends that would require journal entries.
