

Short Selling Mini-Lesson

1. Explain that sometimes people can make money on stocks when the actual stocks themselves lose value and this mini-simulation will demonstrate how.
2. Cut apart the cards for BUYING and SELLING “Yellow Corp.” stock and distribute about 10 of each to students in the room. To the students with “Buying” cards, also give them \$5 in fake currency or beans or paper clips or some other suitable substitute. To the students with “Selling” cards, also give them at least one share.
3. Hand out copies of the script to four students that are good public speakers/actors and are willing to portray one of the roles in the skit. Position them in the room away from each other so that they have to speak up to hear each other and actually can walk to each other when prompted.
4. Begin the skit with students reading their parts.
5. Pause after Trader 2 says “You can use my broker – over there” and ask the following:
 - a. Can someone briefly review what has happened so far? *(Answers will vary, but should recap that Trader 1 thinks Yellow Corp is going to do poorly next quarter and wants to make money off that.)*
 - b. Has Trader 1 done anything illegal? *(No. A common misconception about short selling is that it requires inside information or some sort of subversive methods to benefit from. This is not the case.)*
 - c. Why would a broker lend shares to someone just looking to sell them? *(This is a previewing question of what is about to happen so answers will vary. Tell students they are about to find out instead of confirming or denying their answers.)*
6. Continue the skit up until Trader 1 says “Who wants some?” At this point, help facilitate trades. Students with cards that say they are willing to “BUY” Yellow Corp stock should offer Trader 1 \$5 in exchange for stock. Remember – the people BUYING the stock may have various reasons for buying the stock and may not know the same information Trader 1 knows. Try to get 10 trades, but if that is not happening, as long as there are at least five or six that’s fine.
7. Make sure everyone understands what has happened; point out that Trader 1 now has \$50 s/he didn’t have before and people who wanted Yellow Corp stock now have it. Ask
 - a. What does Trader 1 owe the broker? *(10 shares of Yellow Corp stock. This is important! S/He doesn’t owe money – S/He owes shares of stock!)*
 - b. What does Trader 1 hope happens to the price of the stock? *(Falls so that when s/he buys the stock back it is cheaper than when s/he sold it.)*
8. Continue with the skit until Trader 1 says “I’m now buying shares of Yellow Corp. stock for \$2 a share.” At this point, students with “SELL” cards should be offering their Yellow Corp. Stock to Trader 1 and exchanging it for \$2.
9. Allow the rest of the skit to play out as written.

- 10.** Debrief the skit with questions that address the following important points:
- a.** No one did anything illegal in the skit. All actions were voluntary.
 - b.** Everyone gains something: The Broker gets a fee, Trader 1 gets profit, Buyers of Yellow Corp still have a valuable asset that could grow over time, and Sellers profited on their sale of stock.
 - c.** There is a VERY big risk to this, however. Since you are legally obligated to re-purchase the stock and return it to the broker, you can lose significant amounts of money if the stock increases in price. In theory, the stock price can increase forever putting you at significant risk for loss at higher prices.

Short Selling Script

SMG NEWS: Good morning/afternoon! The Dow fell about 1% yesterday while the S&P 500 also dropped about a half a percent. Some traders are wondering if a bear market is coming our way while others think this recent dip is just a minor correction and we are in store for another record setting quarter. Traders are anxiously awaiting reports this week from the Yellow Corporation as they will report earnings and sales numbers. Yellow Corp stock is currently trading at \$5.00 per share.

TRADER 1: Hmmm...I was just in a Yellow Corporation store the other day and I didn't see anyone really buying anything. I also know that several friends of mine who used to work for Yellow Corp got laid off. I bet this report won't be very good. Wonder if there's a way to make money off of this?

TRADER 2: Sounds like you need to do a short sell!

TRADER 1: Hey, who you calling a short sell?

TRADER 2: No no no...a short sell is when you sell a stock to someone when you think it will lose value. You agree to buy it back later in the hopes that the stock will be cheaper.

TRADER 1: But I don't have any Yellow Corp stock.

TRADER 2: Then visit a broker and borrow some. You can use my broker – over there! [point to broker].

TRADER 1: [walk over to Broker] I would like to borrow 10 shares of Yellow Corp stock to short sell.

BROKER: No problem, I have plenty and plan to hold them for at least a year. Here's the deal, though. When you return these to me, you also owe me a \$2.00 fee.

TRADER 1: Thanks. "Attention MARKET: I am now selling shares of Yellow Corp for \$5 each. Who wants some?" [Take money from buyers and give them shares of stock].

SMG NEWS: [WAIT UNTIL PROMPTED BY TEACHER]: Today, Yellow Corp announced earnings and sales in a dismal report that came in well under market expectations. Furthermore, because of increased competition, Yellow Corp expects next quarter to be even worse, but they announced development of a long term plan to improve that they will unveil next month. Their share price dropped from \$5 a share on the market to \$2 a share this morning.

TRADER 1: THIS....IS....AWESOME!!!! Now I need to go into the market and buy 10 shares to return to my broker. "ATTENTION MARKET: I am now buying shares of Yellow Corp for \$2.00 a share!" [Take shares from sellers and give them their money].

[Walk over to Broker] Here you go, here are your 10 shares AND your \$2.00 fee.

BROKER: This is great, thank you.

TRADER 1: Aren't you mad the shares are worth less now than when I borrowed them?

BROKER: Not really. We had planned to hold these shares for at least a year. They could greatly increase in value between now and then. Your transaction helped us make a little money on them now.

TRADER 1: I feel so smart right now.

TRADER 2: And you should. You made money, the broker made money, the people who bought the stock for \$.50 made money and even the people who bought your short sell still have an asset that has value.

TRADER 1: I am going to do this all the time!

TRADER 2: Be careful though, this can be very risky.

SMG NEWS: And here with us today to explain the risks of short selling is [Insert Teacher's Name], thank you.

YELLOW CORP STOCK:
1 Share

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TRADER 1

TRADER 2

SMG News