

Understanding the language of investing

Your guide to investment terms

The investment world seems to have a language of its own. The novice or even veteran investor can be confused by it from time to time.

Many of today's investment terms have been passed down through the years from the early days of Wall Street trading, while others have come about as the world of investing has evolved and expanded. It is important to understand the terminology in order to help you make better-informed investment decisions.

That's why we have developed this brochure. This guide to investment terms can help you better understand the words you may hear when talking one-on-one with your Financial Advisor, what you see on your monthly statement or what you may hear in the financial media.

Keep this information handy for those times when you need a quick reference guide, or share it with someone you know who might want to learn more about investment terminology. And remember, you can always turn to your Financial Advisor to help you make sense of it all when it comes to understanding the language of investing.

A

Accrued interest

The amount of interest due on a bond since the last interest payment was made. A bond buyer pays the market price plus accrued interest.

Alternative minimum tax (AMT)

A federal income tax calculated on specific tax benefits or preferences, such as interest income received from certain municipal bonds. To ensure that individuals taking advantage of such benefits pay at least a minimum amount of tax, the AMT applies whenever it is greater than a person's taxes calculated without these benefits.

Annual report

An annual financial statement published by a publicly-owned corporation. The annual report provides shareholders with information about a firm's revenues, earnings, assets, liabilities and expenses. According to SEC rules, all shareholders must receive a copy of this report.

Annuity

A contract between an insurance company and an individual in which a sum of money is deposited for a specified period of time. During the accumulation phase, the funds grow tax deferred. During the income phase, income is paid for a specified period of time.

Ask price

The current price at which a security may be bought. It is the lowest price any seller will accept at a given time. In the case of a mutual fund, it is the net asset value plus the sales charge, if any. Also known as the offer price.

Together we'll go far



Asset allocation

The process of selecting and blending investments from different asset categories, such as stocks, bonds cash alternatives (money market funds, CDs, and T-bills) and cash equivalents (checking and savings accounts), to help reduce investment risk and reach long-term investment goals.

Asset class

A way to categorize different investment vehicles. The three basic asset classes are stocks, bonds and cash.

Auction rate securities

A debt instrument (corporate or municipal bonds) with a long-term nominal maturity for which the interest rate is regularly reset through an auction.

B

Bear market

The cycle of the stock market in which stock prices fall for an extended period of time.

Bid price

The current price at which a security may be sold. It is the highest price anyone will pay for a security at a given time.

Blue chip

The common stock of a company known nationally for the quality of its products or services; it has a long history of sustained earnings and dividend payments.

Bond

A debt instrument in which the issuing authority promises to pay the bondholders a specified amount of interest for a specified length of time and to repay the principal invested on a given maturity date.

Bond insurance

Insurance purchased by an issuer for either an entire issue or specific maturities, which guarantees the payment of principal and/or interest.

Bull market

The cycle of the stock market in which the market rises for an extended period of time and stock prices are driven up by market optimists (or “bulls”).

C

Call

A right to buy a specific asset at a predetermined price until a certain date. In the case of a bond, it is the issuer’s right to repurchase an issue of bonds at a certain price on or after a specific date before the maturity date.

Capital gain or loss

Profit or loss from the sale of an investment.

Cash

A nonearning asset; also known as coins or currency.

Certificate of deposit (CD)

Time-deposit investments issued by a bank or savings & loan association with a stated date of maturity and interest rate.

Closed-end fund

A type of mutual fund with a fixed number of shares that trade on an exchange or over-the-counter. (Most mutual funds [also known as open-end funds] have an unlimited number of shares and are bought and sold directly through a Financial Advisor or the mutual fund company.)

Collateralized mortgage obligation (CMO)

A mortgage-backed security collateralized by residential mortgages that are commonly backed by government agencies and government-sponsored enterprises. (See also “Mortgage-backed security.”)

Committee on Uniform Securities

Identification Procedures (CUSIP) number

The individual identification number assigned to most securities in the United States.

Commodity

A product traded on an authorized commodity exchange. Types of commodities include agricultural products, metals, petroleum, foreign currencies, and financial instruments and indexes.

Common stock

Securities that represent an ownership interest in a corporation. Shareholders have the right to vote on major decisions (usually one vote per share owned). This class of stock has no preference to dividends or any distribution of assets. (See also “Stock.”)

Concentrated equity position

A substantial or significant portion of stock holdings in a single industry sector or individual security.

Confirmation

Written acknowledgment of a security trade detailing the security, price, commission or fee, and trade date of the transaction also known as a confirm.

Consumer price index (CPI)

This index is calculated monthly by the Bureau of Labor Statistics. It is used to show economic trends in the changes in prices and to measure the rate of inflation. The factors that make up the CPI are the costs of housing, food, transportation, medical care, clothing, education and entertainment. The government uses this index to adjust Social Security payments and determine cost-of-living increases in pensions and wages.

Convertible security

A security that can be exchanged for common stock or another security at a specified rate or price.

Corporate bond

A bond issued by a corporation with a stated interest rate and maturity.

Cost basis

A means of measuring the value of a security or other assets for tax purposes. When you sell a security, you compare its selling price with your cost basis to determine whether you've realized a taxable gain or a tax-deductible loss.

Coupon rate

The rate of interest paid on a bond, usually semiannually. This term originated when bond certificates were issued with coupons attached to be clipped and presented for payment of interest. While bonds are no longer issued with coupons, this term is still used synonymously with interest rate.

Coverdell Education Savings Account (ESA) *(formerly known as the Education IRA)*

An education savings plan that can be made by individuals, corporations, tax-exempt organizations and other entities and can be used for qualified elementary and secondary school education expenses. Contributions are nondeductible and distributions are free from federal income tax when used for qualified education expenses.

Current yield

The annual rate of return on an investment based on the income received during the year compared with the investment's current price.

D

Debt

An obligation to repay an amount owed. Bonds are a type of debt instrument.

Defined benefit plan

A pension plan in which the retirement benefits, rather than the contributions to the plans, are specified. For example, a retired employee who has reached a certain age with a given number of years of service at a certain income level is entitled to a specific monthly payment.

Defined portfolio

(See "Unit investment trusts.")

Derivative

A contract or payment exchange agreement whose value is derived from an underlying asset, reference rate or index.

Discount

The amount by which a bond is priced below its par value. (See also "Premium.")

Diversification

The process of deciding what mix of investments to own within each asset category after you have determined the proper asset allocation for your investments. (See also "Asset allocation.")

Dividend

The payment designated by the board of directors to be distributed pro rata among the shares outstanding of common or preferred stock or a mutual fund.

Dollar cost averaging

A system of purchasing securities at regular intervals, usually each month, with a fixed dollar amount. This results in the purchase of more shares when prices are low and fewer shares when prices rise.

Dow Jones Industrial Average (DJIA)

The most widely recognized market indicator, made up of 30 large and actively traded industrial stocks.

E

Equity

Ownership position in a company. Also known as stock.

Estate

All assets a person possesses at the time of death, such as securities, real estate, interests in businesses, physical possessions and cash.

Exchange

A system for the organized trading of securities. The major U.S. exchanges are the New York Stock Exchange, American Stock Exchange and Chicago Board Options Exchange. There are also regional exchanges throughout the country.

Exchange-traded funds (ETFs)

Unmanaged portfolios designed to track the performance of a certain basket of stocks. They allow investors to gain overall exposure to a particular industry. Can be bought and sold throughout the day just like stocks and are priced continuously during the trading day.

Ex-dividend

“Without dividend”; the buyer of a stock selling ex-dividend does not receive the recently declared dividend. After the ex-dividend date, the stock tables include the symbol “x” following the stock name.

F

401(k)

An employer-sponsored retirement plan that lets employees make payroll-deduction contributions to a tax-deferred savings account.

403(b)

A retirement plan, also known as a tax-sheltered annuity, that lets employees of tax-exempt charitable, educational or religious organizations contribute a certain portion of their wages or salary into a tax-sheltered fund. Taxes on income earned in the plan are deferred. The annuity includes a death benefit and an option to receive income for life.

529 plans

Qualified tuition-assistance programs used to pay higher education expenses. Named for the section of the tax code that created them, these plans let individuals save on a tax-deferred basis. Earnings have the opportunity to grow tax deferred if used for qualified expenses, and withdrawals are free from federal income tax.

Financial Industry Regulatory Authority (FINRA)

The Financial Industry Regulatory Authority (FINRA) is the largest nongovernmental regulator for all securities firms doing business in the United States. All told, FINRA oversees more than 5,000 brokerage firms, about 172,000 branch offices and more than 676,000 registered securities representatives. FINRA was created in July 2007 through the consolidation of NASD and the member regulation, enforcement and arbitration functions of the New York Stock Exchange.

Fixed annuity

An annuity policy in which the issuing insurance company guarantees a fixed interest rate for a specified period of time.

Fixed-income security

A security that pays a regular income on a set time schedule. Bonds are fixed-income investments.

Futures

Contracts traded on an exchange specifying a future date of delivery or receipt of a specific commodity.

G

Gift tax

A graduated tax assessment against a person who has given money or assets to another person. As of 2009, an individual can gift up to \$13,000 (or \$26,000 for a married couple) annually to any recipient without incurring a gift tax. Gifts of more than \$13,000 per year will incur a gift tax and will be deducted from an individual's lifetime exemption of \$1 million for total assets that can be gifted.

Ginnie Mae

A mortgage-backed security issued and backed by the Government National Mortgage Association (GNMA), an agency of the federal government. (See also “Mortgage-backed security.”)

Government bond

A direct debt obligation of the U.S. government, including Treasury bonds, notes, bills and savings bonds.

H

Hedge funds

Funds that let investors borrow money, sell short and use options by offering them the possibility of extraordinary gains with above-average risk.

I

Index of leading economic indicators

The average of ten leading indicators released monthly by government economists that provides an easy way to gauge the state of the economy. The indicators that are averaged include durable goods, housing starts, jobless claims, new factory orders, monthly averages of stock prices and several other measures of manufacturing performances:

- **Durable goods.** Measures orders of a wide range of products that have a useful life over a number of years. A backlog of orders usually indicates an expanding economy.
- **Housing starts.** Measures the number of residential building permits being issued. In a growing economy, there is usually an increased demand for new housing.
- **Jobless claims.** Reports the number of new unemployment claims for state unemployment insurance. A falling number is reported in a growing economy.
- **New factory orders.** Measures the number of manufacturers' orders. An increase in orders usually shows a willingness by consumers to spend.

Individual retirement account (IRA)

An account that lets individuals set aside earned income in a tax-deferred retirement plan. For some individuals, contributions are deductible from taxable income. (See also "Coverdell Education Savings Account" and "Roth IRA.")

Inflation

The decline in the purchasing power of money over time. The consumer price index (CPI) is used to measure the rate of inflation.

Initial public offering (IPO)

A corporation's first sale of stock to the public. Also referred to as "going public."

Interest

Payments a borrower makes to a lender for use of the lender's money (e.g., a corporation pays interest to its bondholders).

L

Large-cap stock

A stock of a company with market capitalization of more than \$10 billion.

Life insurance

An insurance company contract that provides for payment to the beneficiary upon the death of the insured. Some life insurance policies provide a tax-deferred cash buildup that can be accessed by the policy owner.

Limit order

An order to buy or sell a stated amount of a security at a specified price (the limit) or better. A limit order to buy would be at the limit price or lower, and a limit order to sell would be at the limit price or higher.

Limited partnership

An organization made up of a general partner, who manages the partnership, and limited partners, who invest money but have limited liability to the organization's creditors.

Load

A sales charge that an investor must pay when buying certain mutual fund shares.

Long

Signifies the net ownership position in a particular security.

Long-term care insurance

The type of coverage that pays for the assistance people may need when they can no longer take care of themselves due to illness or prolonged disability or if they have difficulty performing daily living tasks. Care can be provided in their own home, an assisted care facility, an adult day care facility or a nursing home.

M

Margin

Purchasing securities “on credit” by using other securities as collateral.

Market capitalization

The total value of all of a firm’s outstanding shares. This is calculated by multiplying the market price per share by the total number of shares outstanding.

Market order

An order to buy or sell a stated amount of a security at the best price available when the order reaches the marketplace.

Market price

The last price or current quote at which a security trades in the secondary market.

Maturity

The date on which the issuer of a bond or CD is scheduled to repay the principal to the bondholder or CD holder.

Mid-cap stock

A stock of a company with a market capitalization between \$2 billion and \$10 billion.

Money market mutual fund

A mutual fund that invests in high-quality, short-term securities, such as Treasury bills, CDs and commercial paper.

Mortgage-backed security

A bond that represents a share in a pool of mortgages issued by government agencies, government-sponsored enterprises or mortgage lenders. Investors receive regular (normally monthly) interest payments, and the principal is returned incrementally over the life of the investment. (See also “Collateralized mortgage obligation” [CMO] and “Ginnie Mae” [GNMA].)

Municipal bond

A bond issued by a state or political subdivision that pays interest that is usually free from federal, and sometimes state, taxes. (See also “Alternative minimum tax [AMT].”)

Mutual fund

An investment that lets a group of people pool their assets in a diversified portfolio of stocks, bonds, or a combination of stocks and bonds. An investment company then professionally manages the assets in the portfolio in an effort to achieve a specified investment objective, such as growth or income.

N

Nasdaq

An electronic information network that provides brokers and dealers with current price quotations on many actively traded over-the-counter (OTC) securities.

Net asset value (NAV)

The per-share value of a mutual fund figured by taking the total market value of a fund’s assets and dividing the figure by the total number of shares outstanding. Also, the price at which you sell mutual fund shares.

New issue

The first offering to the public of a stock, bond or mutual fund.

No-load

A mutual fund that does not impose a sales charge when an investor purchases or sells shares.

O

Odd lot

Shares are typically sold in “lots” of 100. Purchases for shares in amounts of less than 100 are called “odd lots.”

Offer price

(See “Ask price.”)

Official statement

The document that provides key information regarding a municipal bond new issue.

Open-end fund

A fund that sells as many shares as investors are willing to purchase. As money comes in, the fund increases in value. If investors want to sell, the fund buys their shares back. Most mutual funds are open-end funds.

Option

A contract that lets an investor sell or purchase an asset at a fixed price until a specific date. An option to purchase an asset is a call; an option to sell an asset is a put.

Over-the-counter (OTC)

A highly sophisticated communications network on which dealers trade securities that are not listed on any exchange. All government bonds and all other nonlisted stocks and bonds are traded on the OTC network.

P

Par value

The dollar amount on which a bond's interest is calculated and the amount paid to bondholders at maturity. Also known as face value.

Preferred stock

A class of stock that entitles holders to receive dividends before dividends are paid to common stockholders; dividends are usually fixed. Should the company liquidate, preferred stockholders have prior claim on assets over common stockholders. (See also "Stock.")

Premium

The amount by which a bond sells above its par value. (See also "Discount.")

Price-earnings ratio (P/E)

The current price of a share of stock divided by the earnings per share of the issuing firm. The P/E is used to compare stocks selling at different price levels.

Principal

The amount of invested dollars.

Professional money management

Provides full-time management of individual portfolios, which includes evaluating the overall market and its risks, the risks of individual securities, and exposure and investment opportunities.

Prospectus

The official document highlighting the key information about securities registered with the Securities and Exchange Commission.

R

Rating

A rating assigned to debt securities by independent rating services based on the issuer's ability to meet interest and principal payments.

Real estate investment trust (REIT)

A company that owns and manages a portfolio of real estate properties. REITs serve as conduits through which rental income is passed from real estate holdings to shareholders.

Rollover

Occurs when an individual reinvests the money from one investment into a similar investment. For example, you can take the proceeds from your 401(k), tax-deferred annuity or IRA and deposit the proceeds into another qualified plan or IRA. Or you can roll over funds from a maturing CD and deposit them into another CD.

Roth IRA

Created by the Taxpayer Relief Act of 1997, the Roth IRA lets individuals within certain income limits contribute yearly. Contributions are not tax-deductible, but they can accumulate tax free; after five years' ownership and upon reaching age 59 1/2, individuals can withdraw the contributions and earnings without paying taxes on this income.

Round lot

An order to trade 100 or a multiple of 100 shares of stock. If an order consists of fewer than 100 shares, it is called an odd lot.

S

Savings bond

A debt security issued by the U.S. government that can be purchased in relatively small denominations through most financial institutions. The principal and interest are backed by the full faith and credit of the U.S. government, and the interest is exempt from local and state income tax.

Sector

A group of securities that share specific characteristics (e.g., industry).

Securities and Exchange Commission (SEC)

A federal agency established in 1934 to protect investors, enforce regulations and maintain the integrity of the securities markets.

Securities Investor Protection Corporation (SIPC)

A nonprofit organization created by an act of Congress. SIPC provides funds for use, if necessary, to protect customers' cash and securities that are on deposit with a SIPC member firm in the event the firm fails and is liquidated (does not protect against market losses). SIPC protects the lost securities of its members up to \$500,000, including \$250,000 for claims for cash. Explanatory brochure available upon request or at sipc.org.

Settlement date

The date by which either cash (for a buyer) or a security (for a seller) must be delivered to a Financial Advisor, in order to complete a securities transaction.

Short

A net investment position in a security in which the security has been borrowed and sold but not yet replaced.

Small-cap stock

A stock of a company with a market capitalization of less than \$2 billion. Typically, a small-cap stock is more volatile than a large-cap or mid-cap stock, but the potential for growth can be greater.

Spin-off

An independent company created when a parent corporation separates a subsidiary or a division from itself through the sale or distribution of shares in the new company.

Spread

The difference between the bid and ask price for a particular security.

Standard & Poor's 500 Stock Index (S&P 500)

A broad-based weighted index based on the average performance of 500 common stocks.

Stock

A share of ownership in a company. Shareholders are entitled to a "share" in the profits of the company (paid in dividends). (See also "Common stock" or "Preferred stock.") Also known as equity.

Stock option

The right to purchase a company's stock at an established price, called the exercise price or strike price, on or before a specified date.

Stock split

An increase in a company's number of authorized shares by issuing additional stock to shareholders. For example, in a 2-for-1 split, an investor who owned 100 shares of ABC Company at \$50 per share would receive 200 shares at \$25 per share. A stock split does not change the shareholder's percentage of equity in the company and requires shareholder approval. A reverse split is a decrease in the number of shares.

Stock symbol

The unique identification symbol given to every corporation whose stock is traded on a stock exchange or the Nasdaq over-the-counter market.

Stop-limit order

A variation of the stop order that stipulates when the stock trades at the stop price, the order becomes a limit order and not a market order. (See also "Limit order" and "Stop order.")

Stop order

An order to buy or sell a stated amount of securities that becomes a market order when the market price of the security reaches the specific price stated in the stop order. (See also "Market order.")

Street name

Securities registered in the name of the brokerage firm but credited to the account of a client. A security is held in street name to simplify trading because no certificate delivery or signature is required. In margin accounts, securities must be held in street name.

T

Taxable-equivalent yield

The yield an investor would need to obtain on a taxable investment to equal the tax-free yield on a municipal bond.

Total return

The total earnings from an investment, including dividends or interest and any profit or loss realized on the liquidation of the investment.

Trade date

The date on which a transaction is executed.

Trust

Fiduciary relationship in which a person, called a trustee, holds title to property for the benefit of another person, called a beneficiary.

U

Unit investment trust

An investment company that invests in a defined portfolio of bonds and/or stocks. Unlike a mutual fund, the portfolio's investments are fixed over the life of the trust, are not managed, and have a stated or known maturity. Units of the trust's investment portfolio are sold to investors through Financial Advisors as a pro rata share. Also known as a defined portfolio.

V

Variable annuity

An annuity offering several professionally-managed investment portfolios. The investment return will vary depending on the portfolio's investment performance.

Volatility

The fluctuation in value of a security or asset class. Volatility is typically measured by standard deviation, which evaluates the performance of a particular investment or an asset class by measuring the fluctuation of total returns around an average during a specified period of time.

W

Wash sale rule

Prohibits selling a security at a loss and purchasing the same or a "substantially identical security" within 30 calendar days before or after the sale date that established a loss. If you do sell a security at a loss and purchase the same security during the 61-day period surrounding the sale, you cannot take the loss on your taxes.

Wrap account

A professionally-managed stock or bond portfolio that uses asset allocation to help meet investment needs. Wrap accounts have an annual wrap fee and do not charge commissions for each transaction.

Y

Yield

Also known as return; the dividends or interest paid on a security calculated as a percentage of the price paid. In the case of a bond, this figure is known as current return.

Yield to maturity

The yield on a bond, taking into account the interest rate, the purchase price in relation to the par value and the number of years left to maturity. For example, if an investor purchases a \$1,000 bond for \$800, the \$200 profit (\$1,000 - \$800) the owner will receive at maturity will be added to the interest earned when calculating yield to maturity.

Z

Zero coupon bond

A bond that pays no interest to its owner but is issued at a fraction of its par value. The money invested in the bond grows at a fixed rate as the interest automatically compounds within the investment.