Wealth for Life Glossary

Aggressive growth fund: A mutual fund that aims for the highest capital gains. They often invest in smaller emerging companies that offer maximum growth potential.

Adjustable Rate Mortgage (ARM): A mortgage loan where the interest rate is periodically adjusted based on an index. ARMs permit borrowers to lower their initial payments because they are assuming the risk of an interest rate change. The adjustments are necessary for the lender to ensure that it maintains a steady profit margin on the loan, i.e., the cost to the bank of funding a loan also goes up when interest rates rise, so that cost is passed along to the borrower.

Asset allocation: The process of reviewing a portfolio to divide assets among different types of investments—such as stocks, bonds, and real estate—to ensure that the overall risk is in line with the investor's goals and circumstance.

Balanced fund: A mutual fund with a mix of stocks and bonds. It offers safety of principal, regular income and modest growth.

Bond: An interest-bearing government or corporate security in which an investor lends a corporation money. In turn, that company pays the bondholder, interest, usually at specific intervals, and pays the principal amount at maturity.

Closed-end mutual funds: Funds that issue a fixed number of shares. The price of the share is set by the supply and demand of the marketplace, and not the net asset value of the securities held by the fund.

Credit quality: The ability of issuers to pay principal and interest on bonds when due.

Diversification: An investment strategy focused on reducing overall risk by assembling a portfolio comprised of a variety of investment vehicles, such as stocks, bonds, and real estate.

Dividend Reinvestment Plan (DRIP): Offered by some corporations, such a plan allows you to automatically reinvest cash dividends and capital gains distributions, allowing you to purchase more shares, often without commissions.

Dividend yield: This compares the dividend paid to the price of the stock. It's calculated by dividing the dividend per share by the share price of the stock.

Dow Jones industrial average: Thirty actively traded blue-chip stocks that represent a wide array of industries, including energy, financial services, technology, and transportation.

Earnings Per Share (EPS): A key statistic in evaluating the performance of a company, it represents the portion of earnings that's allocated to each share of outstanding common stock. For example, a company that reported earnings of $1 million, and that had 2 million shares outstanding, would report earnings of $.50 per share. Analysts' earnings estimates are a key indicator of their outlook for a particular stock.

Emerging market fund: A mutual fund that invests primarily in countries with developing economies—they tend to be more volatile due to political instability and currency fluctuations.

ETF (Exchange Traded Fund): an investment vehicle that trades like a stock, but holds a basket of stocks or bonds. Some ETFs track indexes, others have holdings that follow a particular theme, with investments in gold or currencies. ETFs are similar to mutual funds in that they represent a collection of investments. Unlike mutual funds, ETFs trade on an exchange (hence the name). Some investors prefer ETFs to mutual funds because they have low expense ratios and generate lower capital gains taxes than similar mutual funds.

Expense ratio: This figure reveals how much a mutual fund charges for its operating expenses. It's expressed as a percentage of the fund's total assets under management. For example, a fund with an expense ratio of 1.05%, charges $1.05 for every $100 it has under management.

The Federal Deposit Insurance Corporation (FDIC): An independent agency of the U.S. government that insures depositors of up to $250,000 per bank, for each account ownership category, as long as the bank is a member of the firm.

FICO score: Though there are several measures of creditworthiness, FICO scores, issued by the Fair Isaac Corporation, are the most widely used. Scores range from 300 to 850—scores above 700 are a very good sign of strong financial health.

Fixed-income: A type of security that pays a fixed rate of return. It usually refers to corporate, municipal, and government bonds, which pay a fixed interest rate until the bond matures, and to preferred stock, which pays a fixed dividend.

Fund family: A group of mutual funds with a common investment adviser.

Growth fund: A mutual fund that seeks long-term capital appreciation. These funds invest principally in common stock.

Growth investment style: An investment approach that looks for stocks with earnings that have grown rapidly and seem likely to continue to do so in the future.

High-yield bonds: Non-investment grade corporate bonds that have a higher risk/return potential. Usually called junk bonds.

Home Equity Line of Credit (HELOC): A revolving line of credit for a fixed period of time, where the collateral is the borrower's equity in his or her home.

Index fund: These mutual funds invest in securities tied to an index, such as the S&P 500. Index funds seek to have their returns equal the performance of the index.
Keogh plan: A retirement plan for self-employed individuals, sole proprietors or partners in a business and their employees.

Ladder: A bond portfolio strategy where investors stagger the maturities of their holdings in order to provide a regular income stream as the bonds come due.

Large cap: Describes the market capitalization of the largest companies—generally regarded as equal to $5 billion or more.

Limit order: When you place a limit order, you specify the highest price you're willing to shell out for shares if you are in the market to buy, and the lowest offer you'd be willing to entertain if you're selling. If the broker can't meet your price or do better, the order won't be executed.

Liquidity: The ability of an individual or corporation to convert assets into cash or cash equivalents without significant loss.

Load: A sales charge paid by an investor who buys shares in a mutual fund that is sold by a brokerage firm or other sales representative.

Market capitalization: The value of a corporation determined by the market price of its outstanding common stock. It is calculated by multiplying the number of outstanding shares by the current price of the shares.

Market order: A market order is an instruction to buy a certain number of shares at the best price available.

Maturity: The date on which a bond or other debt instrument becomes due and payable.

Mid cap: Describes the market capitalization of mid-size companies—generally regarded as being from $1 billion to $5 billion.

Mutual fund: A professionally managed fund that pools the money of its investors to buy a variety of securities.

NASDAQ: The National Association of Securities Dealers Automated Quotations system is the largest U.S. equities exchange. With a total of approximately 3,200 companies, it lists more companies and, on average, trades more shares per day than any other U.S. electronic market. The NASDAQ is owned by The Nasdaq Stock Market, Inc. (NDAQ).

Nasdaq Composite Index: An index that tracks all of the stocks traded on the NASDAQ stock market. It's widely followed as an indicator for the performance of technology companies.

Net Asset Value (NAV): The current value of one share in a mutual fund.

Net worth: The difference between an individual's total assets and his or her liabilities. (See "BE Wealth Calculator," page 17)

No-load fund: A mutual fund offered by an open-end investment company that does not impose a sales charge or "load" on its shareholders.

Open-end mutual fund: A fund that has an unfixed number of shares available to its investors. The number of shares changes as investors buy and sell shares.

Portfolio manager: The person, or group of people, who decide which securities the fund buys and sells in order to maximize returns.

Price/Earnings ratio (P/E): The P/E ratio is the price of a stock divided by its earnings per share. The P/E, also known as the multiple, gives investors an idea of how much they are paying for a company's earning power. The higher the P/E, the more investors are paying, and therefore the more earnings growth and risk they are expecting. A low P/E ratio may indicate that a stock has fallen out of favor, or it may be a blue chip stock with a long record of earnings stability and regular dividends.
A trailing P/E ratio is calculated using earnings over the past 12 months, while a forward P/E is calculated using earnings estimates for the year ahead.

Real Estate Investment Trust (REIT): A publicly traded company that invests in a specific type of property, from shopping centers and office buildings, to apartment complexes and hotels. REITs typically provide high dividends because, by law, they are required to distribute 90% of their taxable income to shareholders.

Security: a general investing term for a financial instrument—such as a stock or bond—that can be owned, bought, or sold.

Small cap: Describes the market capitalization of smaller companies—generally regarded as being less than $1 billion.

Standard & Poor's 500 Index: An index of 500 leading U.S. companies that's maintained by the S&P Index Committee. Though the index focuses on large cap stocks, the S&P 500 is widely viewed as proxy for the performance of the total market.

Stock: Ownership of a corporation represented by shares that are a claim on the corporation's earnings and assets. Common stock usually entitles the shareholder to vote in the election of directors and other matters taken up at shareholder meetings. Preferred stock generally does not give the shareholder voting rights, but it has a prior claim on assets and earnings.

Stop loss order: A stop loss order helps limit your losses on a stock trade by specifying a price at which your broker has instructions to sell shares. For instance, if you purchased shares of Apple Inc. at $20, and the stock climbed all the way to $90 per share. If you then placed a stop loss order of $70 on the shares, as soon as the stock falls to $70, your broker will sell them for you. Used effectively they can help protect your profit, or at least help minimize losses on a plummeting stock.

Treasuries: Bonds, notes and bills issued by the U.S. government and backed by its full faith and credit.

Value investment style: An investment approach that looks for stocks whose market price appears to be less than the intrinsic value of the company.

Yield: The percentage rate of return on the principal invested by the holder of the security.