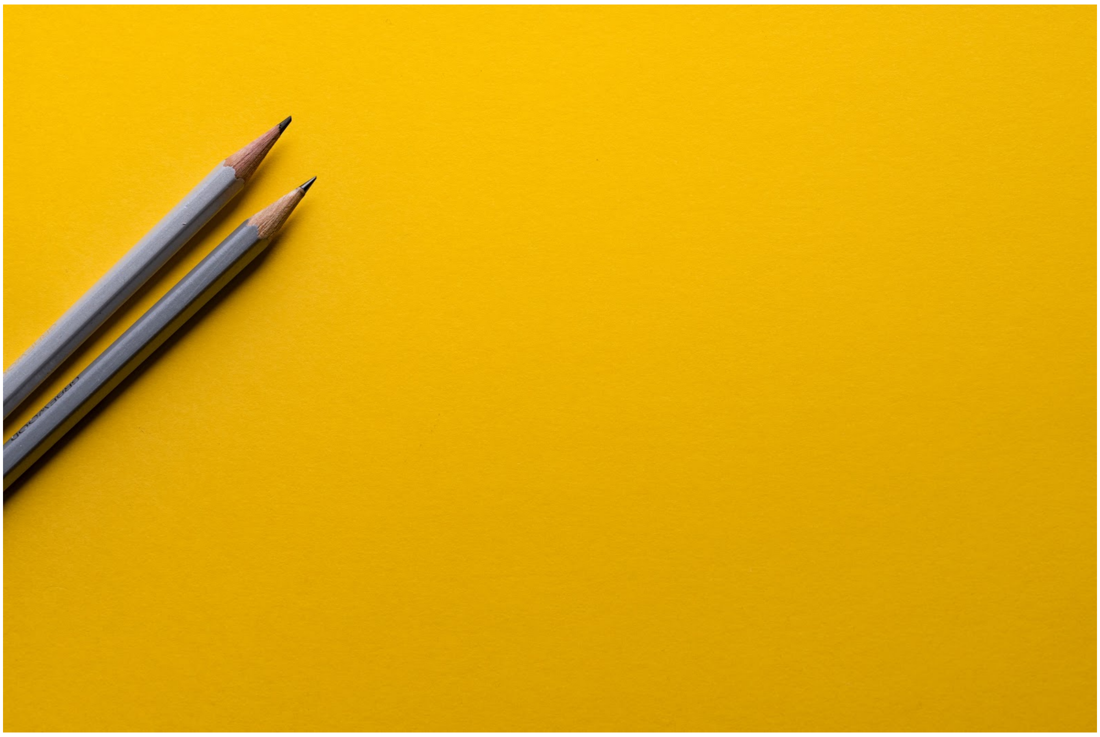
Investment Vocabulary Part 1

Estimated time: 3 minutes / Difficulty: Basic

Before going any further, we want to give you the basic investment vocabulary to work with. It will help the rest of our lessons make sense, and more importantly allow you to explore and understand a bit more of all the daily noise about investing.

Like we said, one of the best things about learning how to invest is that it changes the way you see the world around you. If you're subtle about it, you can even start to sound smart, but please keep your cool. Nobody likes a show-off.



We all start with a blank page.

The Investment

As you know, **stock** is ownership in a company. An individual unit of stock is oftentimes referred to as a ***share***. As someone who owns stock, a ***shareholder*** has a claim on the assets and earnings (see definitions below) of the company. Stocks are also referred to as ***equities***, and are identified by a ***ticker symbol***, which is an abbreviation of the company's name, such as AAPL for Apple.

Share price is the amount an investor must pay to acquire a single share of a company's stock. In later lessons we will discuss what affects a share's price, but it is important to know that after the **Initial Public Offering**, share price is not decided by any entity or authority, but rather by how much investors are willing to ***trade****, or buy or sell,* for. For this reason, share price can change from one minute to the next.

Common Stock is one of two main kinds of stock. As we mentioned, owning a share entitles you to certain claims on a company. One benefit of common stock is that it typically entitles you to vote on important matters affecting the company, including deciding on the board of directors. These votes many times happen at the ***annual shareholder meeting***, but many shareholders vote via ***proxy***, which means they let someone else vote for them.

These votes can be a powerful way for you to participate, however it's not all good news for common stock. In a company with both common and preferred stock, common shareholders are typically the last in line to receive any **earnings** or **assets**. If a company earns a profit, and decides to give some to shareholders (see **Dividends**), it will go to **preferred shareholders** first. If a company goes bankrupt and sells all of the assets (liquidates), the money it receives will go to employees, banks, suppliers, and preferred shareholders before any of it goes to **common shareholders**. Oftentimes this means receiving nothing.

Preferred Stock has priority over **common shares** when a company has excess earnings or is in ***liquidation***. However, preferred shares rarely have voting rights, and are not as prevalent.

The Characteristics

Assets, broadly speaking are anything of value that a person or a company can own. Naturally this means that your stock investments are an asset, and in a later lesson we will discuss **Asset Classes**. In the case of a company, it can mean any number of things, from manufacturing machines, buildings, and product for sale, to computers and valuable brand names.

Earnings are the profits, or extra income, a company has after paying for all of its expenses during a given period of time. If a company has sales of 100€, and it pays 40€ to employees, 40€ for materials, and 10€ for transport, the earnings will be 10€. Earnings are one of the key factors in determining a company's share price, as they indicate how well a company is doing.

Dividends are a distribution of a portion of a company's earnings to shareholders, either in the form of cash, additional shares, or other property, although cash is most typical. Whether or not dividends are paid is decided by shareholders, at the recommendation of the board of directors, which must consider whether the excess earnings are needed for investing in growth or other projects. Typically younger or rapidly growing companies do not pay dividends as they cannot afford it.

Publicly Traded or **Publicly Listed Companies** are companies that have decided to offer a portion of shares for sale to the general population, usually through the **stock exchanges,** but in return they must follow strict rules on sharing information. In contrast, **private companies** are usually owned by the founders or management, and not required to share information or sell stock to the public.

Initial Public Offering (**IPO**) is the process a private company goes through to become ***publicly traded*** by selling a portion of its shares on the stock market. Before selling the shares, the company will undergo a long process of working with investment banks (*underwriters*) to share financial information, seek regulatory approval, and establish a share price. Typically companies pursue an IPO in order to raise funds or to allow investors to "exit" or sell their ownership.

The Environment

An **Exchange** is a place where investments, including public stocks, are traded. Some of the largest and most well-known exchanges are the New York Stock Exchange (NYSE), NASDAQ, the Tokyo Stock Exchange, the London Stock Exchange, and the Euronext.

Market, within the context of investing, can refer to both the place where shares are traded, and to the potential buyers of a given share or other asset. When you hear someone refer to the stock market, they are referring to all of the places where shares can be traded, but typically the stock exchanges. News reports will typically discuss the market being **up** or **down**, and this simply means whether or not the total value of shares traded on the exchanges is increasing or decreasing.

As we will discuss in later lessons, the reasons for up or down markets depends on a variety of factors, but it is important to note that if the *market* is down it doesn't necessarily mean all the *exchanges* or individual *stocks* are.

A **Bull Market** is when share prices, and/or the overall exchange values, are increasing, characterized by optimism, and a **Bear Market** is when they are decreasing characterized by pessimism. When discussing the market and individual stocks, investors can be described as ***bullish*** or ***bearish.***

Analysts are professionals dedicated to projecting the future value of the markets, sectors, or individual stocks by examining financial statements, economic trends, and other data. Analysts can work independently, for banks, or for investment groups, and their methods can vary. The effect of their differences means that they rarely have identical projections for share prices, but when many analysts are *bullish or bearish* about a certain stock, it will affect investor opinion and move the share price.

Brokers are the middlemen, or intermediaries, who buy or sell shares for investors, in return for a fee. **Traders** also buy and sell shares, but typically do so as a representative of their employer, which may be an investment bank or portfolio manager. Traditionally, brokers and traders had to be physically present at the exchange, but much of their work is now carried out electronically.