Vocabulary Part 2

Estimated time: 3 minutes / Difficulty: Basic

By now you're probably starting to feel a little more comfortable with the world of investing. If you pick up a copy of the Financial Times, you're likely to get a lot more out of it than you used to. However, would you feel ready to purchase a stock yet? There are a few more terms we'd like to explain before we get into what to look for when considering an investment.

Building up, page by page.

Trading Terms

Execution refers to when you successfully buy or sell a stock. Usually this is carried out by a broker, but these processes are becoming increasingly automated.

When you first look at a stock, you will likely see the **quote** next to the ticker symbol. This represents the price at which the last transaction occurred, while **open** refers to the price when the market opened that day.

As we discussed earlier though, it's not as simple as deciding to buy or sell. The buyer and the seller have to agree on a price, and this means you may not receive the quote price.

The price a buyer is looking to pay is the **bid**, and the point at which the seller is offering to sell is the **ask.** Logically, the difference between the two is known as the **bid-ask spread.**

As in most interactions between humans, reaching an agreement can take time, and sometimes it never happens. This is why different types of buy or sell orders exist.

A **limit order** is an instruction to execute within certain price ranges, usually a maximum price the buyer is willing to pay and the minimum a seller is willing to accept. Generally you will establish a certain time frame for which the limit order is valid. This is done to protect you from changes in the market or in your personal strategy if you aren't able to execute immediately. A variant of this is the **day order**, which limits the time frame to the day it is placed.

A **market order**, which is something we recommend avoiding, instructs the broker to execute a trade immediately at the best price available.

We will discuss this further in later lessons, but there are a number of important aspects surrounding the price and availability of stock and market activity as a whole.

When a share price is changing or a company has released important news, this can often cause an increase in **trading volume**, or the number of shares being traded each day, as investors become more or less interested in owning the stock. This can also have an effect on **liquidity**, or how easily you can buy or sell shares.

Market Terms

If a stock or the entire market is rapidly increasing, this is often referred to as a **rally.** However, as you will learn, stocks do not always move with the market, which is why investors often consider a stock's **beta**.

Beta is a measure of a stock's volatility in comparison to the market. When a stock is said to be **volatile,** this means that it moves up and down frequently and in an unpredictable manner, making it riskier to buy. A stock that is more volatile than the market will have a beta of greater than 1.

If a given stock or industry, sometimes called a **sector**, moves closely with the overall market, it will have a beta closer to 1. A stock that is less volatile than the overall market will have a beta of less than 1, and is typically a safer investment than those with higher betas.

Some of the least volatile, or most stable, stocks are what are known as **blue chips**. These are usually large, financially sound, and well-established companies like Coca-Cola or Apple that tend not to see their share price move much. Typically blue chip stocks pay dividends, and have a large **market capitalization**, which refers to the total value of all the shares.

While, as per usual, this could be much longer, you should be prepared to begin considering specific stocks as we share what to look for in each of them in the next lesson.