Dictionary of Financial and Business Terms

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The Author

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Abandonment option::The option of terminating an investment earlier than originally planned.

Abnormal returns: Part of the return that is not due to systematic influences (market wide influences). In other words, abnormal returns are above those predicted by the market movement alone. **Related:** excess returns.

Absolute priority :Rule in bankruptcy proceedings whereby senior creditors are required to be paid in full before junior creditors receive any payment.

Accelerated cost recovery system (ACRS):Schedule of depreciation rates allowed for tax purposes.

Accelerated depreciation:Any depreciation method that produces larger deductions for depreciation in the early years of a project's life. Accelerated cost recovery system (ACRS), which is a depreciation schedule allowed for tax purposes, is one such example.

Accounting exposure:The change in the value of a firm's foreign currency denominated accounts due to a change in exchange rates.

Accounting earnings: Earnings of a firm as reported on its income statement.

Accounting insolvency:Total liabilities exceed total assets. A firm with a negative net worth is insolvent on the books.

Accounting liquidity:The ease and quickness with which assets can be converted to cash.

Accounts payable:Money owed to suppliers.

Accounts receivable: Money owed by customers.

Accounts receivable turnover: The ratio of net credit sales to average accounts receivable, a measure of how quickly customers pay their bills.

Accretion (of a discount) :In portfolio accounting, a straight-line accumulation of capital gains on discount bond in anticipation of receipt of par at maturity.

Accrual bond :A bond on which interest accrues, but is not paid to the investor during the time of accrual. The amount of accrued interest is added to the remaining principal of the bond and is paid at maturity.

Accrued interest :The accumulated coupon interest earned but not yet paid to the seller of a bond by the buyer (unless the bond is in default).

Accumulated Benefit Obligation (ABO) : An approximate measure of the liability of a plan in the event of a termination at the date the calculation is performed. **Related:** projected benefit obligation.

Acid-test ratio : Also called the quick ratio, the ratio of current assets minus inventories, accruals, and prepaid items to current liabilities.

Acquiree :A firm that is being acquired.

Acquirer :A firm or individual that is acquiring something.

Acquisition of assets :A merger or consolidation in which an acquirer purchases the selling firm's assets.

Acquisition of stock :A merger or consolidation in which an acquirer purchases the acquiree's stock.

Act of state doctrine :This doctrine says that a nation is sovereign within its own borders and its domestic actions may not be questioned in the courts of another nation.

Active :A market in which there is much trading.

Active portfolio strategy :A strategy that uses available information and forecasting techniques to seek a better performance than a portfolio that is simply diversified broadly. **Related:** passive portfolio strategy

Actuals : The physical commodity underlying a futures contract. Cash commodity, physical.

Additional hedge :A protection against borrower fallout risk in the mortgage pipeline.

Adjustable rate preferred stock (ARPS) :Publicly traded issues that may be collateralized by mortgages and MBSs.

Adjusted present value (APV) The net present value analysis of an asset if financed solely by equity (present value of un-levered cash flows), plus the present value of any financing decisions (levered cash flows). In other words, the various tax shields provided by the deductibility of interest and the benefits of other investment tax credits are calculated separately. This analysis is often used for highly leveraged transactions such as a leverage buy-out.

Administrative pricing rules IRS rules used to allocate income on export sales to a foreign sales corporation.

Advance commitment A promise to sell an asset before the seller has lined up purchase of the asset. This seller can offset risk by purchasing a futures contract to fix the sales price.

Adverse selection A situation in which market participation is a negative signal.

Affirmative covenant A bond covenant that specifies certain actions the firm must take.

After-tax profit margin The ratio of net income to net sales.

After-tax real rate of return Money after-tax rate of return minus the inflation rate.

Agencies Federal agency securities.

Agency bank A form of organization commonly used by foreign banks to enter the U.S. market. An agency bank cannot accept deposits or extend loans in its own name; it acts as agent for the parent bank.

Agency basis A means of compensating the broker of a program trade solely on the basis of commission established through bids submitted by various brokerage firms. agency incentive arrangement. A means of compensating the broker of a program trade using benchmark prices for issues to be traded in determining commissions or fees.

Agency cost view The argument that specifies that the various agency costs create a complex environment in which total agency costs are at a minimum with some, but less than 100%, debt financing.

Agency costs The incremental costs of having an agent make decisions for a principal.

Agency pass-throughs Mortgage pass-through securities whose principal and interest payments are guaranteed by government agencies, such as the Government National Mortgage Association (" Ginnie Mae "), Federal Home Loan Mortgage Corporation (" Freddie Mac") and Federal National Mortgage Association (" Fannie Mae").

Agency problem Conflicts of interest among stockholders, bondholders, and managers.

Agency theory The analysis of principal-agent relationships, wherein one person, an agent, acts on behalf of anther person, a principal.

Agent The decision-maker in a principal-agent relationship.

Aggregation Process in corporate financial planning whereby the smaller investment proposals of each of the firm's operational units are added up and in effect treated as a big picture.

Aging schedule A table of accounts receivable broken down into age categories (such as 0-30 days, 30-60 days, and 60-90 days), which is used to see whether customer payments are keeping close to schedule.

AIBD Association of International Bond Dealers.

All equity rate The discount rate that reflects only the business risks of a project and abstracts from the effects of financing.

All or none Requirement that none of an order be executed unless all of it can be executed at the specified price.

All-equity rate The discount rate that reflects only the business risks of a project and abstracts from the effects of financing.

All-in cost Total costs, explicit and implicit.

All-or-none underwriting An arrangement whereby a security issue is canceled if the underwriter is unable to re-sell the entire issue.

Alpha A measure of selection risk (also known as residual risk) of a mutual fund in relation to the market. A positive alpha is the extra return awarded to the investor for taking a risk, instead of accepting the market return. For example, an alpha of 0.4 means the fund outperformed the market-based return estimate by 0.4%. An alpha of -0.6 means a fund's monthly return was 0.6% less than would have been predicted from the change in the market alone. In a Jensen Index, it is factor to represent the portfolio's performance that diverges from its beta, representing a measure of the manager's performance.

Alpha equation The alpha of a fund is determined as follows:

[(sum of y) -((b)(sum of x))] / n

where: n =number of observations (36 months)

b = beta of the fund

x = rate of return for the S&P 500

y = rate of return for the fund

Alternative mortgage instruments Variations of mortgage instruments such as adjustable-rate and variable-rate mortgages, graduated-payment mortgages, reverse-annuity mortgages, and several seldom-used variations.

American Depositary Receipts (ADRs) Certificates issued by a U.S. depositary bank, representing foreign shares held by the bank, usually by a branch or correspondent in the country of issue. One ADR may represent a portion of a foreign share, one share or a bundle of shares of a foreign corporation. If the ADR's are "sponsored," the corporation provides financial information and other assistance to the bank and may subsidize the administration of the ADRs. "Unsponsored" ADRs do not receive such assistance. ADRs carry the same currency, political and economic risks as the underlying foreign share; the prices of the two, adjusted for the SDR/ordinary ratio, are kept essentially identical by arbitrage. American depositary shares(ADSs) are a similar form of certification.

American option An option that may be exercised at any time up to and including the expiration date. **Related:** European option

American shares Securities certificates issued in the U.S. by a transfer agent acting on behalf of the foreign issuer. The certificates represent claims to foreign equities.

American Stock Exchange (AMEX) The second-largest stock exchange in the United States. It trades mostly in small-to medium-sized companies.

American-style option An option contract that can be exercised at any time between the date of purchase and the expiration date. Most exchange-traded options are American style.

Amortization The repayment of a loan by installments.

Amortization factor The pool factor implied by the scheduled amortization assuming no prepayemts.

Amortizing interest rate swap Swap in which the principal or national amount rises (falls) as interest rates rise (decline).

Analyst Employee of a brokerage or fund management house who studies companies and makes buy-and-sell recommendations on their stocks. Most specialize in a specific industry.

Angels Individuals providing venture capital.

Announcement date Date on which particular news concerning a given company is announced to the public. Used in event studies, which researchers use to evaluate the economic impact of events of interest.

Annual fund operating expenses For investment companies, the management fee and "other expenses," including the expenses for maintaining shareholder records, providing shareholders with financial statements, and providing custodial and accounting services. For 12b-1 funds, selling and marketing costs are included.

Annual percentage rate (APR) The periodic rate times the number of periods in a year. For example, a 5% quarterly return has an APR of 20%.

Annual percentage yield (APY) The effective, or true, annual rate of return. The APY is the rate actually earned or paid in one year, taking into account the affect of compounding. The APY is calculated by taking one plus the periodic rate and raising it to the number of periods in a year. For example, a 1% per month rate has an APY of 12.68% (1.01^12).

Annual report Yearly record of a publicly held company's financial condition. It includes a description of the firm's operations, its balance sheet and income statement. SEC rules require that it be distributed to all shareholders. A more detailed version is called a 10-K.

Annualized gain If stock X appreciates 1.5% in one month, the annualized gain for that sock over a twelve month period is 12*1.5% = 18%. Compounded over the twelve month period, the gain is (1.015)^12 = 19.6%.

Annualized holding period return The annual rate of return that when compounded *t* times, would have given the same *t*-period holding return as actually occurred from period 1 to period *t*.

Annuity A regular periodic payment made by an insurance company to a policyholder for a specified period of time.

Annuity due An annuity with n payments, wherein the first payment is made at time $t = 0$ and the last payment is made at time $t = n - 1$.

Annuity factor Present value of $1 paid for each of t periods.

Annuity in arrears An annuity with a first payment on full period hence, rather than immediately.

Anticipation Arrangements whereby customers who pay before the final date may be entitled to deduct a normal rate of interest.

Antidilutive effect Result of a transaction that increases earnings per common share (e.g. by decreasing the number of shares outstanding).

Appraisal ratio The signal-to-noise ratio of an analyst's forecasts. The ratio of alpha to residual standard deviation.

Appraisal rights A right of shareholders in a merger to demand the payment of a fair price for their shares, as determined independently.

Appropriation request Formal request for funds for capital investment project.

Arbitrage The simultaneous buying and selling of a security at two different prices in two different markets, resulting in profits without risk. Perfectly efficient markets present no arbitrage opportunities. Perfectly efficient markets seldom exist.

Arbitrage Pricing Theory (APT) An alternative model to the capital asset pricing model developed by Stephen Ross and based purely on arbitrage arguments.

Arbitrage-free option-pricing models Yield curve option-pricing models.

Arbitrageurs People who search for and exploit arbitrage opportunities.

Arithmetic average (mean) rate of return Arithmetic mean return.

Arithmetic mean return An average of the subperiod returns, calculated by summing the subperiod returns and dividing by he number of subperiods.

Arms index Also known as a trading index (TRIN)= (number of advancing issues)/ (number of declining issues) (Total up volume)/ (total down volume). An advance/decline market indicator. Less than 1.0 indicates bullish demand, while above 1.0 is bearish. The index often is smoothed with a simple moving average.

Arm's length price The price at which a willing buyer and a willing unrelated seller would freely agree to transact.

ARMs Adjustable rate mortgage. A mortgage that features predetermined adjustments of the loan interest rate at regular intervals based on an established index. The interest rate is adjusted at each interval to a rate equivalent to the index value plus a predetermined spread, or margin, over the index, usually subject to per-interval and to life-of-loan interest rate and/or payment rate caps.

Articles of incorporation Legal document establishing a corporation and its structure and purpose.

Asian currency units (ACUs) Dollar deposits held in Singapore or other Asian centers.

Asian option Option based on the average price of the asset during the life of the option.

Ask This is the quoted ask, or the lowest price an investor will accept to sell a stock. Practically speaking, this is the quoted offer at which an investor can buy shares of stock; also called the offer price.

Ask price A dealer's price to sell a security; also called the offer price.

Asset Any possession that has value in an exchange.

Asset/equity ratio The ratio of total assets to stockholder equity.

Asset/liability management Also called surplus management, the task of managing funds of a financial institution to accomplish the two goals of a financial institution: (1) to earn an adequate return on funds invested and (2) to maintain a comfortable surplus of assets beyond liabilities.

Asset activity ratios Ratios that measure how effectively the firm is managing its assets.

Asset allocation decision The decision regarding how an institution's funds should be distributed among the major classes of assets in which it may invest.

Asset-backed security A security that is collateralized by loans, leases, receivables, or installment contracts on personal property, not real estate.

Asset-based financing Methods of financing in which lenders and equity investors look principally to the cash flow from a particular asset or set of assets for a return on, and the return of, their financing.

Asset classes Categories of assets, such as stocks, bonds, real estate and foreign securities.

Asset-coverage test A bond indenture restriction that permits additional borrowing on if the ratio of assets to debt does not fall below a specified minimum.

Asset for asset swap Creditors exchange the debt of one defaulting borrower for the debt of another defaulting borrower.

Asset pricing model A model for determining the required rate of return on an asset.

Asset substitution A firm's investing in assets that are riskier than those that the debtholders expected.

Asset substitution problem Arises when the stockholders substitute riskier assets for the firm's existing assets and expropriate value from the debtholders.

Asset swap An interest rate swap used to alter the cash flow characteristics of an institution's assets so as to provide a better match with its iabilities.

Asset turnover The ratio of net sales to total assets.

Asset pricing model A model, such as the Capital Asset Pricing Model (CAPM), that determines the required rate of return on a particular asset.

Assets A firm's productive resources.

Assets requirements A common element of a financial plan that describes projected capital spending and the proposed uses of net working capital.

Assignment The receipt of an exercise notice by an options writer that requires the writer to sell (in the case of a call) or purchase (in the case of a put) the underlying security at the specified strike price.

Asymmetry A lack of equivalence between two things, such as the unequal tax treatment of interest expense and dividend payments.

Asymmetric information Information that is known to some people but not to other people.

Asymmetric taxes A situation wherein participants in a transaction have different net tax rates.

At-the-money An option is at-the-money if the strike price of the option is equal to the market price of the underlying security. For example, if xyz stock is trading at 54, then the xyz 54 option is at-the-money.

Attribute bias The tendency of stocks preferred by the dividend discount model to share certain equity attributes such as low price-earnings ratios, high dividend yield, high book-value ratio or membership in a particular industry sector.

Auction markets Markets in which the prevailing price is determined through the free interaction of prospective buyers and sellers, as on the floor of the stock exchange.

Auction rate preferred stock (ARPS) Floating rate preferred stock, the dividend on which is adjusted every seven weeks through a Dutch auction.

Auditor's report A section of an annual report containing the auditor's opinion about the veracity of the financial statements.

Authorized shares Number of shares authorized for issuance by a firm's corporate charter.

Autocorrelation The correlation of a variable with itself over successive time intervals.

Automated Clearing House (ACH) A collection of 32 regional electronic interbank networks used to process transactions electronically with a guaranteed one-day bank collection float.

Automatic stay The restricting of liability holders from collection efforts of collateral seizure, which is automatically imposed when a firm files for bankruptcy under Chapter 11.

Autoregressive Using past data to predict future data.

Availability float Checks deposited by a company that have not yet been cleared.

Average An arithmetic mean of selected stocks intended to represent the behavior of the market or some component of it. One good example is the widely quoted Dow Jones Industrial Average, which adds the current prices of the 30 DJIA's stocks, and divides the results by a predetermined number, the divisor.

Average accounting return The average project earnings after taxes and depreciation divided by the average book value of the investment during its life.

Average age of accounts receivable The weighted-average age of all of the firm's outstanding invoices.

Average collection period, or days' receivables The ratio of accounts receivables to sales, or the total amount of credit extended per dollar of daily sales (average AR/sales * 365).

Average cost of capital A firm's required payout to the bondholders and to the stockholders expressed as a percentage of capital contributed to the firm. Average cost of capital is computed by dividing the total required cost of capital by the total amount of contributed capital.

Average life Also referred to as the weighted-average life (WAL). The average number of years that each dollar of unpaid principal due on the mortgage remains outstanding. Average life is computed as the weighted average time to the receipt of all future cash flows, using as the weights the dollar amounts of the principal paydowns.

Average maturity The average time to maturity of securities held by a mutual fund. Changes in interest rates have greater impact on funds with longer average life.

Average (across-day) measures An estimation of price that uses the average or representative price of a large number of trades.

Average rate of return (ARR) The ratio of the average cash inflow to the amount invested.

Average tax rate Taxes as a fraction of income; total taxes divided by total taxable income.

Away A trade, quote, or market that does not originate with the dealer in question, e.g., "the bid is 98-10 away from me."

Back fee The fee paid on the extension date if the buyer wishes to continue the option.

Back office Brokerage house clerical operations that support, but do not include, the trading of stocks and other securities. Includes all written confirmation and settlement of trades, record keeping and regulatory compliance.

Back-end loan fund A mutual fund that charges investors a fee to sell (redeem) shares, often ranging from 4% to 6%. Some back-end load funds impose a full commission if the shares are redeemed within a designated time, such as one year. The commission decreases the longer the investor holds the shares. The formal name for the back-end load is the contingent deferred sales charge, or CDSC.

Back-to-back financing An intercompany loan channeled through a bank.

Back-to-back loan A loan in which two companies in separate countries borrow each other's currency for a specific time period and repay the other's currency at an agreed upon maturity.

Back-up (1) When bond yields and prices fall, the market is said to back-up. (2) When an investor swaps out of one security into another of shorter current maturity he is said to back up.

Backwardation A market condition in which futures prices are lower in the distant delivery months than in the nearest delivery month. This situation may occur in when the costs of storing the product until eventual delivery are effectively subtracted from the price today. The opposite of contango.

Baker Plan A plan by U.S. Treasury Secretary James Baker under which 15 principal middle-income debtor countries (the Baker 15) would undertake growth-oriented structural reforms, to be supported by increased financing from the World Bank and continued lending from commercial banks.

Balance of payments A statistical compilation formulated by a sovereign nation of all economic transactions between residents of that nation and residents of all other nations during a stipulated period of time, usually a calendar year.

Balance of trade Net flow of goods (exports minus imports) between countries.

Balance sheet Also called the statement of financial condition, it is a summary of the assets, liabilities, and owners' equity.

Balance sheet exposure See:accounting exposure.

Balance sheet identity Total Assets = Total Liabilities + Total Stockholders' Equity

Balanced fund An investment company that invests in stocks and bonds. The same as a balanced mutual fund.

Balanced mutual fund This is a fund that buys common stock, preferred stock and bonds. The same as a balanced fund.

Balloon maturity Any large principal payment due at maturity for a bond or loan with or without a a sinking fund requirement.

BAN (Bank anticipation notes) Notes issued by states and municipalities to obtain interim financing for projects that will eventually be funded long term through the sale of a bond issue.

Bane In the words of Warren Buffet, Bill Bane Sr., is, "a great American and one of the last real traders around. I like to call him 'Salvo.'" His wife, Carol, is a huge NASCAR fan, and in her own words "delights in pulling the legs off central bankers." Cooper Bane, son number two, is a thriving artiste who specializes in making art that is much better than the stuff most folks are doing. Jackson, son number three, is a world renowned master chef and plans on opening a restaurant. Bill Bane Jr., son number one, plans on giving Mr. Monroe Trout a run for his money. [Bill Bane, Jr. helped Professor Harvey put the hypertextual glossary together while an MBA student at Duke University.]

Bank collection float The time that elapses between when a check is deposited into a bank account and when the funds are available to the depositor, during which period the bank is collecting payment from the payer's bank.

Bank discount basis A convention used for quoting bids and offers for treasury bills in terms of annualized yield , based on a 360-day year.

Bank draft A draft addressed to a bank.

Bank line Line of credit granted by a bank to a customer.

Bank wire A computer message system linking major banks. It is used not for effecting payments, but as a mechanism to advise the receiving bank of some action that has occurred, e.g. the payment by a customer of funds into that bank's account.

Banker's acceptance A short-term credit investment created by a non-financial firm and guaranteed by a bank as to payment. Acceptances are traded at discounts from face value in the secondary market. These instruments have been a popular investment for money market funds. They are commonly used in international transactions.

Bank for International Settlements (BIS) An international bank headquartered in Basel, Switzerland, which serves as a forum for monetary cooperation among several European central banks, the Bank of Japan, and the U.S. Federal Reserve System. Founded in 1930 to handle the German payment of World War I reparations, it now monitors and collects data on international banking activity and promulgates rules concerning international bank regulation.

Bankruptcy State of being unable to pay debts. Thus, the ownership of the firm's assets is transferred from the stockholders to the bondholders.

Bankruptcy cost view The argument that expected indirect and direct bankruptcy costs offset the other benefits from leverage so that the optimal amount of leverage is less than 100% debt finaning.

Bankruptcy risk The risk that a firm will be unable to meet its debt obligations. Also referred to as default or insolvency risk.

Bankruptcy view The argument that expected bankruptcy costs preclude firms from being financed entirely with debt.

Bar Slang for one million dollars.

Barbell strategy A strategy in which the maturities of the securities included in the portfolio are concentrated at two extremes.

Bargain-purchase-price option Gives the lessee the option to purchase the asset at a price below fair market value when the lease expires.

BARRA's performance analysis (PERFAN) A method developed by BARRA, a consulting firm in Berkeley, Calif. It is commonly used by institutional investors applying performance attribution analysis to evaluate their money managers' performances.

Barrier options Contracts with trigger points that, when crossed, automatically generate buying or selling of other options. These are very exotic options.

Base interest rate Related: Benchmark interest rate.

Base probability of loss The probability of not achieving a portfolio expected return.

Basic balance In a balance of payments, the basic balance is the net balance of the combination of the current account and the capital account.

Basic business strategies Key strategies a firm intends to pursue in carrying out its business plan.

Basic IRR rule Accept the project if IRR is greater than the discount rate; reject the project is lower than the discount rate.

Basis Regarding a futures contract, the difference between the cash price and the futures price observed in the market. Also, it is the price an investor pays for a security plus any out-of-pocket expenses. It is used to determine capital gains or losses for tax purposes when the stock is sold.

Basis point In the bond market, the smallest measure used for quoting yields is a basis point. Each percentage point of yield in bonds equals 100 basis points. Basis points also are used for interest rates. An interest rate of 5% is 50 basis points greater than an interest rate of 4.5%.

Basis price Price expressed in terms of yield to maturity or annual rate of return.

Basis risk The uncertainty about the basis at the time a hedge may be lifted. Hedging substitutes basis risk for price risk.

Basket options Packages that involve the exchange of more than two currencies against a base currency at expiration. The basket option buyer purchases the right, but not the obligation, to receive designated currencies in exchange for a base currency, either at the prevailing spot market rate or at a prearranged rate of exchange. A basket option is generally used by multinational corporations with multicurrency cash flows since it is generally cheaper to buy an option on a basket of currencies than to buy individual options on each of the currencies that make up the basket.

Basket trades Related: Program trades.

Bear An investor who believes a stock or the overall market will decline. A bear market is a prolonged period of falling stock prices, usually by 20% or more. Related: bull.

Bearer bond bonds that are not registered on the books of the issuer. Such bonds are held in physical form by the owner, who receives interest payments by physically detaching coupons from the bond certificate and delivering them to the paying agent.

Bear market Any market in which prices are in a declining trend.

Bear raid A situation in which large traders sell positions with the intention of driving prices down.

Before-tax profit margin The ratio of net income before taxes to net sales.

Beggar-thy-neighbor An international trade policy of competitive devaluations and increased protective barriers where one country seeks to gain at the expense of its trading partners.

Beggar-thy-neighbor devaluation A devaluation that is designed to cheapen a nation's currency and thereby increase its exports at other countries' expense and reduce imports. Such devaluations often lead to trade wars.

Bellwether issues Related:Benchmark issues.

Benchmark The performance of a predetermined set of securities, for comparison purposes. Such sets may be based on published indexes or may be customized to suit an investment strategy.

Benchmark error Use of an inappropriate proxy for the true market portfolio.

Benchmark interest rate Also called the base interest rate, it is the minimum interest rate investors will demand for investing in a non-Treasury security. It is also tied to the yield to maturity offered on a comparable-maturity Treasury security that was most recently issued ("on-the-run").

Benchmark issues Also called on-the-run or current coupon issues or bellwether issues. In the secondary market, it's the most recently auctioned Treasury issues for each maturity.

Best-efforts sale A method of securities distribution/ underwriting in which the securities firm agrees to sell as much of the offering as possible and return any unsold shares to the issuer. As opposed to a guaranteed or fixed price sale, where the underwriter agrees to sell a specific number of shares (with the securities firm holding any unsold shares in its own account if necessary).

Best-interests-of-creditors test The requirement that a claim holder voting against a plan of reorganization must receive at least as much as he would have if the debtor were liquidated.

Beta (Mutual Funds) The measure of a fund's or stocks risk in relation to the market. A beta of 0.7 means the fund's total return is likely to move up or down 70% of the market change; 1.3 means total return is likely to move up or down 30% more than the market. Beta is referred to as an index of the systematic risk due to general market conditions that cannot be diversified away.

Beta equation (Mutual Funds)

The beta of a fund is determined as follows:

[(n) (sum of (xy))]-[(sum of x) (sum of y)]

[(n) (sum of (xx))]-[(sum of x) (sum of x)]

where: n = # of observations (36 months)

x = rate of return for the S&P 500 Index

y = rate of return for the fund

Beta equation (Stocks)

The beta of a stock is determined as follows:

[(n) (sum of (xy))]-[(sum of x) (sum of y)]

[(n) (sum of (xx))]-[(sum of x) (sum of x)]

where: n = # of observations (24-60 months)

x = rate of return for the S&P 500 Index

y = rate of return for the stock

Biased expectations theories Related: pure expectations theory.

Bid price This is the quoted bid, or the highest price an investor is willing to pay to buy a security. Practically speaking, this is the available price at which an investor can sell shares of stock. Related: Ask , offer.

Bid-asked spread The difference between the bid and asked prices.

Bidder A firm or person that wants to buy a firm or security.

Big Bang The term applied to the liberalization in 1986 of the London Stock Exchange in which trading was automated with the use of computers.

Big Board A nickname for the New York Stock Exchange. Also known as The Exchange. More than 2,000 common and preferred stocks are traded. Founded in 1792, the NYSE is the oldest exchange in the United States, and the largest. It is located on Wall Street in New York City.

Bill of exchange General term for a document demanding payment.

Bill of ladingA contract between the exporter and a transportation company in which the latter agrees to transport the goods under specified conditions which limit its liability. It is the exporter's receipt for the goods as well as proof that goods have been or will be received.

Binomial option pricing model An option pricing model in which the underlying asset can take on only two possible, discrete values in the next time period for each value that it can take on in the preceding time period.

Black market An illegal market.

Black-Scholes option-pricing modelA model for pricing call options based on arbitrage arguments that uses the stock price, the exercise price, the risk-free interest rate, the time to expiration, and the standard deviation of the stock return.

Blanket inventory lienA secured loan that gives the lender a lien against all the borrower's inventories.

Block house Brokerage firms that help to find potential buyers or sellers of large block trades.

Block tradeA large trading order, defined on the New York Stock Exchange as an order that consists of 10,000 shares of a given stock or a total market value of $200,000 or more.

Block votingA group of shareholders banding together to vote their shares in a single block.

Blocked currency A currency that is not freely convertible to other currencies due to exchange controls.

Blow-off topA steep and rapid increase in price followed by a steep and rapid drop. This is an indicator seen in charts and used in technical analysis of stock price and market trends.

Blue-chip company Large and creditworthy company.

Blue-sky laws State laws covering the issue and trading of securities.

Bogey The return an investment manager is compared to for performance evaluation.

Boilerplate Standard terms and conditions.

Bond Bonds are debt and are issued for a period of more than one year. The U.S. government, local governments, water districts, companies and many other types of institutions sell bonds. When an investor buys bonds, he or she is lending money. The seller of the bond agrees to repay the principal amount of the loan at a specified time. Interest-bearing bonds pay interest periodically.

Bond agreement A contract for privately placed debt.

Bond covenant A contractual provision in a bond indenture. A positive covenant requires certain actions, and a negative covenant limits certain actions.

Bond equivalent yield Bond yield calculated on an annual percentage rate method. Differs from annual effective yield.

Bond indenture The contract that sets forth the promises of a corporate bond issuer and the rights of investors.

Bond indexing Designing a portfolio so that its performance will match the performance of some bond index.

Bond points A conventional unit of measure for bond prices set at $10 and equivalent to 1% of the $100 face value of the bond. A price of 80 means that the bond is selling at 80% of its face, or par value.

Bond value With respect to convertible bonds, the value the security would have if it were not convertible apart from the conversion option.

Bond-equivalent basis The method used for computing the bond-equivalent yield.

Bond-equivalent yield The annualized yield to maturity computed by doubling the semiannual yield.

BONDPAR A system that monitors and evaluates the performance of a fixed-income portfolio , as well as the individual securities held in the portfolio. BONDPAR decomposes the return into those elements beyond the manager's control--such as the interest rate environment and client-imposed duration policy constraints--and those that the management process contributes to, such as interest rate management, sector/quality allocations, and individual bond selection.

Boning Charging a lot more for an asset than it's worth.

Book A banker or trader's positions.

Book cash A firm's cash balance as reported in its financial statements. Also called ledger cash.

Book profit The cumulative book income plus any gain or loss on disposition of the assets on termination of the SAT.

Book runner The managing underwriter for a new issue. The book runner maintains the book of securities sold.

Book value A company's book value is its total assets minus intangible assets and liabilities, such as debt. A company's book value might be more or less than its market value.

Book value per share The ratio of stockholder equity to the average number of common shares. Book value per share should not be thought of as an indicator of economic worth, since it reflects accounting valuation (and not necessarily market valuation).

Book-entry securities The Treasury and federal agencies are moving to a book-entry system in which securities are not represented by engraved pieces of paper but are maintained in computerized records at the Fed in the names of member banks, which in turn keep records of the securities they own as well as those they are holding for customers. In the case of other securities where a book-entry has developed, engraved securities do exist somewhere in quite a few cases. These securities do not move from holder to holder but are usually kept in a central clearinghouse or by another agent.

Bootstrapping A process of creating a theoretical spot rate curve , using one yield projection as the basis for the yield of the next maturity.

Borrow To obtain or receive money on loan with the promise or understanding that it will be repaid.

Borrower fallout In the mortgage pipeline, the risk that prospective borrowers of loans committed to be closed will elect to withdraw from the contract.

Bottom-up equity management style A management style that de-emphasizes the significance of economic and market cycles, focusing instead on the analysis of individual stocks.

Bought deal Security issue where one or two underwriters buy the entire issue.

Bourse A term of French origin used to refer to stock markets.

Bracket A term signifying the extent an underwriter's commitment in a new issue, e.g., major bracket or minor bracket.

Brady bonds Bonds issued by emerging countries under a debt reduction plan.

Branch An operation in a foreign country incorporated in the home country.

Break A rapid and sharp price decline.

Break-even analysis An analysis of the level of sales at which a project would make zero profit.

Break-even lease payment The lease payment at which a party to a prospective lease is indifferent between entering and not entering into the lease arrangement.

Break-even payment rate The prepayment rate of a MBS coupon that will produce the same CFY as that of a predetermined benchmark MBS coupon. Used to identify for coupons higher than the benchmark coupon the prepayment rate that will produce the same CFY as that of the benchmark coupon; and for coupons lower than the benchmark coupon the lowest prepayment rate that will do so.

Break-even tax rate The tax rate at which a party to a prospective transaction is indifferent between entering into and not entering into the transaction.

Break-even time Related: Premium payback period.

Breakout A rise in a security's price above a resistance level (commonly its previous high price) or drop below a level of support (commonly the former lowest price.) A breakout is taken to signify a continuing move in the same direction. Can be used by technical analysts as a buy or sell indicator.

Bretton Woods Agreement An agreement signed by the original United Nations members in 1944 that established the International Monetary Fund (IMF) and the post-World War II international monetary system of fixed exchange rates.

Bridge financing Interim financing of one sort or another used to solidify a position until more permanent financing is arranged.

British clearers The large clearing banks that dominate deposit taking and short-term lending in the domestic sterling market.

Broker An individual who is paid a commission for executing customer orders. Either a floor broker who executes orders on the floor of the exchange, or an upstairs broker who handles retail customers and their orders.

Broker loan rate Related: Call money rate.

Brokered market A market where an intermediary offers search services to buyers and sellers.

Bubble theory Security prices sometimes move wildly above their true values.

Buck Slang for one million dollars.

Budget A detailed schedule of financial activity, such as an advertising budget, a sales budget, or a capital budget.

Budget deficit The amount by which government spending exceeds government revenues.

Builder buydown loan A mortgage loan on newly developed property that the builder subsidizes during the early years of the development. The builder uses cash to buy down the mortgage rate to a lower level than the prevailing market loan rate for some period of time. The typical buydown is 3% of the interest-rate amount for the first year, 2% for the second year, and 1% for the third year (also referred to as a 3-2-1 buydown).

Bull An investor who thinks the market will rise. Related: bear.

Bull-bear bond Bond whose principal repayment is linked to the price of another security. The bonds are issued in two tranches: in the first tranche repayment increases with the price of the other security, and in the second tranche repayment decreases with the price of the other security.

Bull CD, Bear CD A bull CD pays its holder a specified percentage of the increase in return on a specified market index while guaranteeing a minimum rate of return. A bear CD pays the holder a fraction of any fall in a given market index.

Bull market Any market in which prices are in an upward trend.

Bull spread A spread strategy in which an investor buys an out-of-the-money put option, financing it by selling an out-of-the money call option on the same underlying.

Bulldog bond Foreign bond issue made in London.

Bulldog market The foreign market in the United Kingdom.

Bullet contract A guaranteed investment contract purchased with a single (one-shot) premium. **Related:** Window contract.

Bullet loan A bank term loan that calls for no amortization.

Bullet strategy A strategy in which a portfolio is constructed so that the maturities of its securities are highly concentrated at one point on the yield curve.

Bullish, bearish Words used to describe investor attitudes. Bullish refers to an optimistic outlook while bearish means a pessimistic outlook.

Bundling, unbundling A trend allowing creation of securities either by combining primitive and derivative securities into one composite hybrid or by separating returns on an asset into classes.

Business cycle Repetitive cycles of economic expansion and recession.

Business failure A business that has terminated with a loss to creditors.

Business risk The risk that the cash flow of an issuer will be impaired because of adverse economic conditions, making it difficult for the issuer to meet its operating expenses.

Busted convertible Related: Fixed-income equivalent.

Butterfly shift A non-parallel shift in the yield curve involving the height of the curve.

Buy To purchase an asset; taking a long position.

Buy in To cover, offset or close out a short position. **Related:** evening up, liquidation.

Buy limit order A conditional trading order that indicates a security may be purchased only at the designated price or lower. **Related:** Sell limit order.

Buy on close To buy at the end of the trading session at a price within the closing range.

Buy on margin A transaction in which an investor borrows to buy additional shares, using the shares themselves as collateral.

Buy on opening To buy at the beginning of a trading session at a price within the opening range.

Buy-and-hold strategy A passive investment strategy with no active buying and selling of stocks from the time the portfolio is created until the end of the investment horizon.

BuydownsMortgages in which monthly payments consist of principal and interest, with portions of these payments during the early period of the loan being provided by a third party to reduce the borrower's monthly payments.

Buying the index Purchasing the stocks in the S&P 500 in the same proportion as the index to achieve the same return.

Buyout Purchase of a controlling interest (or percent of shares) of a company's stock. A leveraged buy-out is done with borrowed money.

Buy-back Another term for a repo.

Buy-side analyst A financial analyst employed by a non-brokerage firm, typically one of the larger money management firms that purchase securities on their own accounts.

Cable Exchange rate between British pounds sterling and the U.S.$.

Calendar List of new issues scheduled to come to market shortly.

Calendar effect The tendency of stocks to perform differently at different times, including such anomalies as the January effect, month-of-the-year effect, day-of-the-week effect, and holiday effect.

Call An option that gives the right to buy the underlying futures contract.

Call an option To exercise a call option.

Call date A date before maturity, specified at issuance, when the issuer of a bond may retire part of the bond for a specified call price.

Call money rate Also called the broker loan rate , the interest rate that banks charge brokers to finance margin loans to investors. The broker charges the investor the call money rate plus a service charge.

Call option An option contract that gives its holder the right (but not the obligation) to purchase a specified number of shares of the underlying stock at the given strike price, on or before the expiration date of the contract.

Call premium Premium in price above the par value of a bond or share of preferred stock that must be paid to holders to redeem the bond or share of preferred stock before its scheduled maturity date.

Call price The price, specified at issuance, at which the issuer of a bond may retire part of the bond at a specified call date.

Call protection A feature of some callable bonds that establishes an initial period when the bonds may not be called.

Call price The price for which a bond can be repaid before maturity under a call provision.

Call provision An embedded option granting a bond issuer the right to buy back all or part of the issue prior to maturity.

Call risk The combination of cash flow uncertainty and reinvestment risk introduced by a call provision.

Call swaption A swaption in which the buyer has the right to enter into a swap as a fixed-rate payer. The writer therefore becomes the fixed-rate receiver/floating rate payer.

Callable A financial security such as a bond with a call option attached to it, i.e., the issuer has the right to call the security.

Canadian agencies Agency banks established by Canadian banks in the U.S.

Cap An upper limit on the interest rate on a floating-rate note.

Capital Money invested in a firm.

Capital account Net result of public and private international investment and lending activities.

Capital allocation decision Allocation of invested funds between risk-free assets versus the risky portfolio.

Capital asset pricing model (CAPM) An economic theory that describes the relationship between risk and expected return, and serves as a model for the pricing of risky securities. The CAPM asserts that the only risk that is priced by rational investors is systematic risk, because that risk cannot be eliminated by diversification. The CAPM says that the expected return of a security or a portfolio is equal to the rate on a risk-free security plus a risk premium.

Capital budget A firm's set of planned capital expenditures.

Capital budgeting The process of choosing the firm's long-term capital assets.

Capital expenditures Amount used during a particular period to acquire or improve long-term assets such as property, plant or equipment.

Capital flight The transfer of capital abroad in response to fears of political risk.

Capital gain When a stock is sold for a profit, it's the difference between the net sales price of securities and their net cost, or original basis. If a stock is sold below cost, the difference is a capital loss.

Capital gains yield The price change portion of a stock's return.

Capital lease A lease obligation that has to be capitalized on the balance sheet.

Capital loss The difference between the net cost of a security and the net sale price, if that security is sold at a loss.

Capital market The market for trading long-term debt instruments (those that mature in more than one year).

Capital market efficiency Reflects the relative amount of wealth wasted in making transactions. An efficient capital market allows the transfer of assets with little wealth loss. **See:** efficient market hypothesis.

Capital market imperfections view The view that issuing debt is generally valuable but that the firm's optimal choice of capital structure is a dynamic process that involves the other views of capital structure (net corporate/personal tax, agency cost, bankruptcy cost, and pecking order), which result from considerations of asymmetric information, asymmetric taxes, and transaction costs.

Capital market line (CML) The line defined by every combination of the risk-free asset and the market portfolio.

Capital rationing Placing one or more limits on the amount of new investment undertaken by a firm, either by using a higher cost of capital, or by setting a maximum on parts of, and/or the entirety of, the capital budget.

Capital structure The makeup of the liabilities and stockholders' equity side of the balance sheet, especially the ratio of debt to equity and the mixture of short and long maturities.

Capital surplus Amounts of directly contributed equity capital in excess of the par value.

Capitalization The debt and/or equity mix that fund a firm's assets.

Capitalization method A method of constructing a replicating portfolio in which the manager purchases a number of the largest-capitalized names in the index stock in proportion to their capitalization.

Capitalization ratios Also called financial leverage ratios, these ratios compare debt to total capitalization and thus reflect the extent to which a corporation is trading on its equity. Capitalization ratios can be interpreted only in the context of the stability of industry and company earnings and cash flow.

Capitalization table A table showing the capitalization of a firm, which typically includes the amount of capital obtained from each source - long-term debt and common equity - and the respective capitalization ratios.

Capitalized Recorded in asset accounts and then depreciated or amortized, as is appropriate for expenditures for items with useful lives greater than one year.

Capitalized interest Interest that is not immediately expensed, but rather is considered as an asset and is then amortized through the income statement over time.

Car A loose quantity term sometimes used to describe a the amount of a commodity underlying one commodity contract; e.g., "a car of bellies." Derived from the fact that quantities of the product specified in a contract used to correspond closely to the capacity of a railroad car.

CARDs Certificates of Amortized Revolving Debt. Pass-through securities backed by credit card receivables.

Carry Related:net financing cost.

Carring costs Costs that increase with increases in the level of investment in current assets.

Carrying value Book value.

CARs Certificates of Automobile Receivables. Pass-through securities backed by automobile receivables.

Cash The value of assets that can be converted into cash immediately, as reported by a company. Usually includes bank accounts and marketable securities, such as government bonds and Banker's Acceptances. Cash equivalents on balance sheets include securities (e.g., notes) that mature within 90 days.

Cash budget A forecasted summary of a firm's expected cash inflows and cash outflows as well as its expected cash and loan balances.

Cash and carry Purchase of a security and simultaneous sale of a future, with the balance being financed with a loan or repo.

Cash and equivalents The value of assets that can be converted into cash immediately, as reported by a company. Usually includes bank accounts and marketable securities, such as government bonds and Banker's Acceptances. Cash equivalents on balance sheets include securities (e.g., notes) that mature within 90 days.

Cash commodity The actual physical commodity, as distinguished from a futures contract.

Cash conversion cycle The length of time between a firm's purchase of inventory and the receipt of cash from accounts receivable.

Cash cow A company that pays out all earnings per share to stockholders as dividends. Or, a company or division of a company that generates a steady and significant amount of free cash flow.

Cash cycle In general, the time between cash disbursement and cash collection. In net working capital management, it can be thought of as the operating cycle less the accounts payable payment period.

Cash deficiency agreement An agreement to invest cash in a project to the extent required to cover any cash deficiency the project may experience.

Cash delivery The provision of some futures contracts that requires not delivery of underlying assets but settlement according to the cash value of the asset.

Cash discount An incentive offered to purchasers of a firm's product for payment within a specified time period, such as ten days.

Cash dividend A dividend paid in cash to a company's shareholders. The amount is normally based on profitability and is taxable as income. A cash distribution may include capital gains and return of capital in addition to the dividend.

Cash equivalent A short-term security that is sufficiently liquid that it may be considered the financial equivalent of cash.

Cash flow In investments, it represents earnings before depreciation , amortization and non-cash charges. Sometimes called cash earnings. Cash flow from operations (called funds from operations) by real estate and other investment trusts is important because it indicates the ability to pay dividends.

Cash flow after interest and taxes Net income plus depreciation.

Cash flow coverage ratio The number of times that financial obligations (for interest, principal payments, preferred stock dividends, and rental payments) are covered by earnings before interest, taxes, rental payments, and depreciation.

Cash flow from operations A firm's net cash inflow resulting directly from its regular operations (disregarding extraordinary items such as the sale of fixed assets or transaction costs associated with issuing securities), calculated as the sum of net income plus non-cash expenses that were deducted in calculating net income.

Cash flow matching Also called dedicating a portfolio, this is an alternative to multiperiod immunization in which the manager matches the maturity of each element in the liability stream, working backward from the last liability to assure all required cash flows.

Cash flow per common share Cash flow from operations minus preferred stock dividends, divided by the number of common shares outstanding.

Cash flow time-line Line depicting the operating activities and cash flows for a firm over a particular period.

Cash-flow break-even point The point below which the firm will need either to obtain additional financing or to liquidate some of its assets to meet its fixed costs.

Cash management bill Very short maturity bills that the Treasury occasionally sells because its cash balances are down and it needs money for a few days.

Cash markets Also called spot markets, these are markets that involve the immediate delivery of a security or instrument. **Related:** derivative markets.

Cash offer A public equity issue that is sold to all interested investors.

Cash ratio The proportion of a firm's assets held as cash.

Cash settlement contracts Futures contracts, such as stock index futures, that settle for cash, not involving the delivery of the underlying.

Cash transaction A transaction where exchange is immediate, as contrasted to a forward contract, which calls for future delivery of an asset at an agreed-upon price.

Cash-equivalent items Temporary investments of currently excess cash in short-term, high-quality investment media such as treasury bills and Banker's Acceptances.

Cash-surrender value An amount the insurance company will pay if the policyholder ends a whole life insurance policy.

Cashout Refers to a situation where a firm runs out of cash and cannot readily sell marketable securities.

CBOE Chicago Board Options Exchange. A securities exchange created in the early 1970s for the public trading of standardized option contracts.

CEDEL A centralized clearing system for eurobonds.

Certainty equivalent An amount that would be accepted in lieu of a chance at a possible higher, but uncertain, amount.

Certificate of deposit (CD) Also called a time deposit, this is a certificate issued by a bank or thrift that indicates a specified sum of money has been deposited. A CD bears a maturity date and a specified interest rate, and can be issued in any denomination. The duration can be up to five years.

CFAT Cash flow after taxes.

CFTC The Commodity Futures Trading Commission is the federal agency created by Congress to regulate futures trading. The Commodity Exchange Act of 1974 became effective April 21, 1975. Previously, futures trading had been regulated by the Commodity Exchange Authority of the USDA.

Characteristic line The market model applied to a single security. The slope of the line is a security's beta.

Changes in Financial Position Sources of funds internally provided from operations that alter a company's cash flow position: depreciation, deferred taxes, other sources, and capital expenditures.

Chartists Related: technical analysts.

Cheapest to deliver issue The acceptable Treasury security with the highest implied repo rate; the rate that a seller of a futures contract can earn by buying an issue and then delivering it at the settlement date.

Chicago Mercantile Exchange (CME) A not-for-profit corporation owned by its members. Its primary functions are to provide a location for trading futures and options, collect and disseminate market information, maintain a clearing mechanism and enforce trading rules.

Chinese wall Communication barrier between financiers (investment bankers) and traders. This barrier is erected to prevent the sharing of inside information that bankers are likely to have.

Churning Excessive trading of a client's \ account in order to increase the broker's commissions.

Circle Underwriters, actual or potential, often seek out and "circle" investor interest in a new issue before final pricing. The customer circled basically made a commitment to purchase the issue if it comes at an agreed-upon price. In the latter case, if the price is other than that stipulated, the customer supposedly has first offer at the actual price.

Circus swap A fixed rate currency swap against floating U.S. dollar LIBOR payments.

Claim dilution A reduction in the likelihood one or more of the firm's claimants will be fully repaid, including time value of money considerations.

Claimant A party to an explicit or implicit contract.

Clean opinion An auditor's opinion reflecting an unqualified acceptance of a company's financial statements.

Clean price Bond price excluding accrued interest.

Clear A trade is carried out by the seller delivering securities and the buyer delivering funds in proper form. A trade that does not clear is said to fail.

Clear a position To eliminate a long or short position, leaving no ownership or obligation.

Clearing House Automated Payments System (CHAPS) A computerized clearing system for sterling funds that began operations in 1984. It includes 14 member banks, nearly 450 participating banks, and is one of the clearing companies within the structure of the Association for Payment Clearing Services (APACS).

Clearing House Interbank Payments System (CHIPS) An international wire transfer system for high-value payments operated by a group of major banks.

Clearing member A member firm of a clearing house. Each clearing member must also be a member of the exchange. Not all members of the exchange, however, are members of the clearing organization. All trades of a non-clearing member must be registered with, and eventually settled through, a clearing member.

Clearinghouse An adjunct to a futures exchange through which transactions executed its floor are settled by a process of matching purchases and sales. A clearing organization is also charged with the proper conduct of delivery procedures and the adequate financing of the entire operation.

Clientele effect The grouping of investors who have a preference that the firm follow a particular financing policy, such as the amount of leverage it uses.

Close, the The period at the end of the trading session. Sometimes used to refer to closing price. **Related:** Opening, the.

Closed-end fund An investment company that sells shares like any other corporation and usually does not redeem its shares. A publicly traded fund sold on stock exchanges or over the counter that may trade above or below its net asset value. **Related:** Open-end fund.

Closed-end mortgage Mortgage against which no additional debt may be issued.

Closing purchase A transaction in which the purchaser's intention is to reduce or eliminate a short position in a stock, or in a given series of options.

Closing range Also known as the range. The high and low prices, or bids and offers, recorded during the period designated as the official close. **Related:** settlement price.

Closing sale A transaction in which the seller's intention is to reduce or eliminate a long position in a stock, or a given series of options.

Cluster analysis A statistical technique that identifies clusters of stocks whose returns are highly correlated within each cluster and relatively uncorrelated between clusters. Cluster analysis has identified groupings such as growth, cyclical, stable and energy stocks.

Coefficient of determination A measure of the goodness of fit of the relationship between the dependent and independent variables in a regression analysis; for instance, the percentage of variation in the return of an asset explained by the market portfolio return.

Coinsurance effect Refers to the fact that the merger of two firms decreases the probability of default on either firm's debt.

Collar An upper and lower limit on the interest rate on a floating-rate note.

Collateral Assets than can be repossessed if a borrower defaults.

Collateral trust bonds A bond in which the issuer (often a holding company) grants investors a lien on stocks, notes, bonds, or other financial asset as security. Compare mortgage bond.

Collateralized mortgage obligation (CMO) A security backed by a pool of pass-throughs , structured so that there are several classes of bondholders with varying maturities, called tranches. The principal payments from the underlying pool of pass-through securities are used to retire the bonds on a priority basis as specified in the prospectus. **Related:** mortgage pass-through security

Collection float The negative float that is created between the time when you deposit a check in your account and the time when funds are made available.

Collection fractions The percentage of a given month's sales collected during the month of sale and each month following the month of sale.

Collection policy Procedures followed by a firm in attempting to collect accounts receivables.

Collective wisdom The combination of all of the individual opinions about a stock's or security's value.

Comanger A bank that ranks just below a lead manager in a syndicated Eurocredit or international bond issue. Comanagers may assist the lead manger bank in the pricing and issue of the instrument.

Combination matching Also called horizon matching, a variation of multiperiod immunization and cash flow matching in which a portfolio is created that is always duration matched and also cash-matched in the first few years.

Combination strategy A strategy in which a put and with the same strike price and expiration are either both bought or both sold. **Related:** Straddle

Commercial draft Demand for payment.

Commercial paper Short-term unsecured promissory notes issued by a corporation. The maturity of commercial paper is typically less than 270 days; the most common maturity range is 30 to 50 days or less.

Commercial risk The risk that a foreign debtor will be unable to pay its debts because of business events, such as bankruptcy.

Commission The fee paid to a broker to execute a trade, based on number of shares, bonds, options, and/or their dollar value. In 1975, deregulation led to the creation of discount brokers, who charge lower commissions than full service brokers. Full service brokers offer advice and usually have a full staff of analysts who follow specific industries. Discount brokers simply execute a client's order -- and usually do not offer an opinion on a stock. Also known as a round-turn.

Commission broker A broker on the floor of an exchange acts as agent for a particular brokerage house and who buys and sells stocks for the brokerage house on a commission basis.

Commission house A firm which buys and sells future contracts for customer accounts. **Related:** futures commission merchant, omnibus account.

Commitment A trader is said to have a commitment when he assumes the obligation to accept or make delivery on a futures contract. **Related:** Open interest

Commitment fee A fee paid to a commercial bank in return for its legal commitment to lend funds that have not yet been advanced.

Committee, AIMR Performance Presentation Standards Implementation Committee The Association for Investment Management and Research (AIMR)'s Performance Presentation Standards Implementation Committee is charged with the responsibility to interpret, revise and update the AIMR Performance Presentation Standards (AIMR-PPS(TM)) for portfolio performance presentations.

Commodities Exchange Center (CEC) The location of five New York futures exchanges: Commodity Exchange, Inc. (COMEX), the New York Mercantile exchange (NYMEX), the New York Cotton Exchange, the Coffee, Sugar and Cocoa exchange (CSC), and the New York futures exchange (NYFE). common size statement A statement in which all items are expressed as a percentage of a base figure, useful for purposes of analyzing trends and the changing relationship between financial statement items. For example, all items in each year's income statement could be presented as a percentage of net sales.

Commodity A commodity is food, metal, or another physical substance that investors buy or sell, usually via futures contracts.

Common market An agreement between two or more countries that permits the free movement of capital and labor as well as goods and services.

Common stock These are securities that represent equity ownership in a company. Common shares let an investor vote on such matters as the election of directors. They also give the holder a share in a company's profits via dividend payments or the capital appreciation of the security.

Common stock/other equity Value of outstanding common shares at par, plus accumulated retained earnings. Also called shareholders' equity.

Common stock equivalent A convertible security that is traded like an equity issue because the optioned common stock is trading high.

Common stock market The market for trading equities, not including preferred stock.

Common stock ratios Ratios that are designed to measure the relative claims of stockholders to earnings (cash flow per share), and equity (book value per share) of a firm.

Common-base-year analysis The representing of accounting information over multiple years as percentages of amounts in an initial year.

Common-size analysis The representing of balance sheet items as percentages of assets and of income statement items as percentages of sales.

Company-specific risk Related: Unsystematic risk

Comparative credit analysis A method of analysis in which a firm is compared to others that have a desired target debt rating in order to infer an appropriate financial ratio target.

Comparison universe The collection of money managers of similar investment style used for assessing relative performance of a portfolio manager.

Compensating balance An excess balance that is left in a bank to provide indirect compensation for loans extended or services provided.

Competence Sufficient ability or fitness for ones needs. Possessing the necessary abilities to be qualified to achieve a certain goal or complete a project.

Competition Intra- or intermarket rivalry between businesses trying to obtain a larger piece of the same market share.

Competitive bidding A securities offering process in which securities firms submit competing bids to the issuer for the securities the issuer wishes to sell.

Competitive offering An offering of securities through competitive bidding.

Complete capital market A market in which there is a distinct marketable security for each and every possible outcome.

Complete portfolio The entire portfolio, including risky and risk-free assets.

Completion bonding Insurance that a construction contract will be successfully completed.

Completion risk The risk that a project will not be brought into operation successfully.

Completion undertaking An undertaking either (1) to complete a project such that it meets certain specified performance criteria on or before a certain specified date or (2) to repay project debt if the completion test cannot be met.

Composition Voluntary arrangement to restructure a firm's debt, under which payment is reduced.

Compound interest Interest paid on previously earned interest as well as on the principal.

Compound option Option on an option.

Compounding The process of accumulating the time value of money forward in time. For example, interest earned in one period earns additional interest during each subsequent time period.

Compounding frequency The number of compounding periods in a year. For example, quarterly compounding has a compounding frequency of 4.

Compounding period The length of the time period (for example, a quarter in the case of quarterly compounding) that elapses before interest compounds.

Comprehensive due diligence investigation The investigation of a firm's business in conjunction with a securities offering to determine whether the firm's business and financial situation and its prospects are adequately disclosed in the prospectus for the offering.

Concentration account A single centralized account into which funds collected at regional locations (lockboxes) are transferred.

Concentration services Movement of cash from different lockbox locations into a single concentration account from which disbursements and investments are made.

Concession agreement An understanding between a company and the host government that specifies the rules under which the company can operate locally.

Conditional sales contracts Similar to equipment trust certificates except that the lender is either the equipment manufacturer or a bank or finance company to whom the manufacturer has sold the conditional sales contract.

Confidence indicator A measure of investors' faith in the economy and the securities market. A low or deteriorating level of confidence is considered by many technical analysts as a bearish sign.

Confidence level The degree of assurance that a specified failure rate is not exceeded.

Confirmation The written statement that follows any "trade" in the securities markets. Confirmation is issued immediately after a trade is executed. It spells out settlement date, terms, commission, etc.

Conflict between bondholders and stockholders These two groups may have interests in a corporation that conflict. Sources of conflict include dividends, distortion of investment, and underinvestment. Protective covenants work to resolve these conflicts.

Conglomerate A firm engaged in two or more unrelated businesses.

Conglomerate merger A merger involving two or more firms that are in unrelated businesses.

Consensus forecast The mean of all financial analysts' forecasts for a company.

Consol A type of bond that has an infinite life but is not issued in the U.S. capital markets.

Consolidation The combining of two or more firms to form an entirely new entity.

Consortium banks A merchant banking subsidiary set up by several banks that may or may not be of the same nationality. Consortium banks are common in the Euromarket and are active in loan syndication.

Constant-growth model Also called the Gordon-Shapiro model, an application of the dividend discount model which assumes (1) a fixed growth rate for future dividends and (2) a single discount rate.

Consumer credit Credit granted by a firm to consumers for the purchase of goods or services. Also called retail credit.

Consumer Price Index The CPI, as it is called, measures the prices of consumer goods and services and is a measure of the pace of U.S. inflation. The U.S.Department of Labor publishes the CPI very month.

Contango A market condition in which futures prices are higher in the distant delivery months.

Contingent claim A claim that can be made only if one or more specified outcomes occur.

Contingent deferred sales charge (CDSC) The formal name for the load of a back-end load fund.

Contingent immunization An arrangement in which the money manager pursues an active bond portfolio strategy until an adverse investment experience drives the then-available potential return down to the safety-net level. When that point is reached, the money manager is obligated to pursue an immunization strategy to lock in the safety-net level return.

Contingent pension liability Under ERISA, the firm is liable to the plan participants for up to 39% of the net worth of the firm.

Continuous compounding The process of accumulating the time value of money forward in time on a continuous, or instantaneous, basis. Interest is earned continuously, and at each instant, the interest that accrues immediately begins earning interest on itself.

Continuous random variable A random value that can take any fractional value within specified ranges, as contrasted with a discrete variable.

Contract A term of reference describing a unit of trading for a financial or commodity future. Also, the actual bilateral agreement between the buyer and seller of a transaction as defined by an exchange.

Contract month The month in which futures contracts may be satisfied by making or accepting a delivery. Also called value managers, those who assemble portfolios with relatively lower betas, lower price-book and P/E ratios and higher dividend yields, seeing value where others do not.

Contribution margin The difference between variable revenue and variable cost.

Control 50% of the outstanding votes plus one vote.

Controlled disbursement A service that provides for a single presentation of checks each day (typically in the early part of the day).

Controlled foreign corporation (CFC) A foreign corporation whose voting stock is more than 50% owned by U.S. stockholders, each of whom owns at least 10% of the voting power.

Controller The corporate manager responsible for the firm's accounting activities.

Convenience yield The extra advantage that firms derive from holding the commodity rather than the future.

Convention statement An annual statement filed by a life insurance company in each state where it does business in compliance with that state's regulations. The statement and supporting documents show, among other things, the assets, liabilities, and surplus of the reporting company.

Conventional mortgage A loan based on the credit of the borrower and on the collateral for the mortgage.

Conventional pass-throughs Also called private-label pass-throughs, any mortgage pass-through security not guaranteed by government agencies. Compare agency pass-throughs.

Conventional project A project with a negative initial cash flow (cash outflow), which is expected to be followed by one or more future positive cash flows (cash inflows).

Convergence The movement of the price of a futures contract toward the price of the underlying cash commodity. At the start, the contract price is higher because of the time value. But as the contract nears expiration, the futures price and the cash price converge.

Conversion factors Rules set by the Chicago Board of Trade for determining the invoice price of each acceptable deliverable Treasury issue against the Treasury Bond futures contract.

Conversion parity price Related:Market conversion price

Conversion premium The percentage by which the conversion price in a convertible security exceeds the prevailing common stock price at the time the convertible security is issued.

Convertibility The degree of freedom to exchange a currency without government restrictions or controls.

Convertible price The contractually specified price per share at which a convertible security can be converted into shares of common stock.

Conversion ratio The number of shares of common stock that the security holder will receive from exercising the call option of a convertible security.

Conversion value Also called parity value, the value of a convertible security if it is converted immediately.

Convertible bonds Bonds that can be converted into common stock at the option of the holder.

Convertible eurobond A eurobond that can be converted into another asset, often through exercise of attached warrants.

Convertible exchangeable preferred stock Convertible preferred stock that may be exchanged, at the issuer's option, into convertible bonds that have the same conversion features as the convertible preferred stock.

Convertible preferred stock Preferred stock that can be converted into common stock at the option of the holder.

Convertible security A security that can be converted into common stock at the option of the security holder, including convertible bonds and convertible preferred stock.

Convex Bowed, as in the shape of a curve. Usually referring to the price/required yield relationship for option-free bonds.

Core competency Primary area of competence. Narrowly defined fields or tasks at which a company or business excels. Primary areas of specialty.

Corner A Market To purchase enough of the available supply of a commodity or stock in order to manipulate its price.

Corporate acquisition The acquisition of one firm by anther firm.

Corporate bonds Debt obligations issued by corporations.

Corporate charter A legal document creating a corporation.

Corporate finance One of the three areas of the discipline of finance. It deals with the operation of the firm (both the investment decision and the financing decision) from that firm's point of view.

Corporate financial management The application of financial principals within a corporation to create and maintain value through decision making and proper resource management.

Corporate financial planning Financial planning conducted by a firm that encompasses preparation of both long- and short-term financial plans.

Corporate processing float The time that elapses between receipt of payment from a customer and the depositing of the customer's check in the firm's bank account; the time required to process customer payments.

Corporate tax view The argument that double (corporate and individual) taxation of equity returns makes debt a cheaper financing method.

Corporate taxable equivalent Rate of return required on a par bond to produce the same after-tax yield to maturity that the premium or discount bond quoted would.

Corporation A legal "person" that is separate and distinct from its owners. A corporation is allowed to own assets, incur liabilities, and sell securities, among other things.

Correlation See: Correlation coefficient.

Correlation coefficient A standardized statistical measure of the dependence of two random variables, defined as the covariance divided by the standard deviations of two variables.

Cost company arrangement Arrangement whereby the shareholders of a project receive output free of charge but agree to pay all operating and financing charges of the project.

Cost of capital The required return for a capital budgeting project.

Cost of carry Related: Net financing cost

Cost of funds Interest rate associated with borrowing money.

Cost of lease financing A lease's internal rate of return.

Cost of limited partner capital The discount rate that equates the after-tax inflows with outflows for capital raised from limited partners.

Cost-benefit ratio The net present value of an investment divided by the investment's initial cost. Also called the profitability index.

Counter trade The exchange of goods for other goods rather than for cash; barter.

Counterpart items In the balance of payments, counterpart items are analogous to unrequited transfers in the current account. They arise because the double-entry system in balance of payments accounting and refer to adjustments in reserves owing to monetization or demonetization of gold, allocation or cancellation of SDRs, and revaluation of the various components of total reserves.

Counterparties The parties to an interest rate swap.

Counterparty Party on the other side of a trade or transaction.

Counterparty risk The risk that the other party to an agreement will default. In an options contract, the risk to the option buyer that the option writer will not buy or sell the underlying as agreed.

Country economic risk Developments in a national economy that can affect the outcome of an international financial transaction.

Country beta Covariance of a national economy's rate of return and the rate of return the world economy divided by the variance of the world economy.

Country financial risk The ability of the national economy to generate enough foreign exchange to meet payments of interest and principal on its foreign debt.

Country risk General level of political and economic uncertainty in a country affecting the value of loans or investments in that country.

Country selection A type of active international management that measures the contribution to performance attributable to investing in the better-performing stock markets of the world.

Coupon The periodic interest payment made to the bondholders during the life of the bond.

Coupon equivalent yield True interest cost expressed on the basis of a 365-day year.

Coupon payments A bond's interest payments.

Coupon rate In bonds, notes or other fixed income securities, the stated percentage rate of interest, usually paid twice a year.

Covariance A statistical measure of the degree to which random variables move together.

Covenants Provisions in a bond indenture or preferred stock agreement that require the bond or preferred stock issuer to take certain specified actions (affirmative covenants) or to refrain from taking certain specified actions (negative covenants).

Cover The purchase of a contract to offset a previously established short position.

Coverage ratios Ratios used to test the adequacy of cash flows generated through earnings for purposes of meeting debt and lease obligations, including the interest coverage ratio and the fixed charge coverage ratio.

Covered call A short call option position in which the writer owns the number of shares of the underlying stock represented by the option contracts. Covered calls generally limit the risk the writer takes because the stock does not have to be bought at the market price, if the holder of that option decides to exercise it.

Covered call writing strategy A strategy that involves writing a call option on securities that the investor owns in his or her portfolio. See covered or hedge option strategies.

Covered interest arbitrage A portfolio manager invests dollars in an instrument denominated in a foreign currency and hedges his resulting foreign exchange risk by selling the proceeds of the investment forward for dollars.

Covered or hedge option strategies Strategies that involve a position in an option as well as a position in the underlying stock, designed so that one position will help offset any unfavorable price movement in the other, including covered call writing and protective put buying. **Related:** naked strategies

Covered Put A put option position in which the option writer also is short the corresponding stock or has deposited, in a cash account, cash or cash equivalents equal to the exercise of the option. This limits the option writer's risk because money or stock is already set aside. In the event that the holder of the put option decides to exercise the option, the writer's risk is more limited than it would be on an uncovered or naked put option.

Cramdown The ability of the bankruptcy court to confirm a plan of reorganization over the objections of some classes of creditors.

Crawling peg An automatic system for revising the exchange rate. It involves establishing a par value around which the rate can vary up to a given percent. The par value is revised regularly according to a formula determined by the authorities.

Credible signal A signal that provides accurate information; a signal that can be distinguish among senders.

Credit Money loaned.

Credit analysis The process of analyzing information on companies and bond issues in order to estimate the ability of the issuer to live up to its future contractual obligations. **Related:** default risk

Credit enhancement Purchase of the financial guarantee of a large insurance company to raise funds.

Credit period The length of time for which the customer is granted credit.

Credit risk The risk that an issuer of debt securities or a borrower may default on his obligations, or that the payment may not be made on a negotiable instrument. **Related:** Default risk

Credit scoring A statistical technique wherein several financial characteristics are combined to form a single score to represent a customer's creditworthiness.

Credit spread Related:Quality spread

Crediting rate The interest rate offered on an investment type insurance policy.

Creditor Lender of money.

Cross default A provision under which default on one debt obligation triggers default on another debt obligation.

Cross hedging The practice of hedging with a futures contract that is different from the underlying being hedged.

Cross holdings One corporation holds shares in another firm.

Cross rates The exchange rate between two currencies expressed as the ratio of two foreign exchange rates that are both expressed in terms of a third currency.

Cross-border risk Refers to the volatility of returns on international investments caused by events associated with a particular country as opposed to events associated solely with a particular economic or financial agent.

Cross-sectional approach A statistical methodology applied to a set of firms at a particular point in time.

Crossover rate The return at which two alternative projects have the same net present value.

Crown jewel A particularly profitable or otherwise particularly valuable corporate unit or asset of a firm.

Cum dividend With dividend.

Cum rights With rights.

Cumulative abnormal return (CAR) Sum of the differences between the expected return on a stock and the actual return that comes from the release of news to the market.

Cumulative dividend feature A requirement that any missed preferred or preference stock dividends be paid in full before any common dividend payment is made.

Cumulative preferred stock Preferred stock whose dividends accrue, should the issuer not make timely dividend payments. **Related:** non-cumulative preferred stock.

Cumulative probability distribution A function that shows the probability that the random variable will attain a value less than or equal to each value that the random variable can take on.

Cumulative Translation Adjustment (CTA) account An entry in a translated balance sheet in which gains and/or losses from translation have been accumulated over a period of years. The CTA account is required under the FASB No. 52 rule.

Cumulative voting A system of voting for directors of a corporation in which shareholder's total number of votes is equal to his number of shares held times the number of candidates.

Currency Money.

Currency arbitrage Taking advantage of divergences in exchange rates in different money markets by buying a currency in one market and selling it in another market.

Currency basket The value of a portfolio of specific amounts of individual currencies, used as the basis for setting the market value of another currency. It is also referred to as a currency cocktail.

Currency future A financial future contract for the delivery of a specified foreign currency.

Currency option An option to buy or sell a foreign currency.

Currency risk Related: Exchange rate risk

Currency risk sharing An agreement by the parties to a transaction to share the currency risk associated with the transaction. The arrangement involves a customized hedge contract embedded in the underlying transaction.

Currency selection Asset allocation in which the investor chooses among investments denominated in different currencies.

Currency swap An agreement to swap a series of specified payment obligations denominated in one currency for a series of specified payment obligations denominated in a different currency.

Current account Net flow of goods, services, and unilateral transactions (gifts) between countries.

Current assets Value of cash, accounts receivable, inventories, marketable securities and other assets that could be converted to cash in less than 1 year.

Current coupon A bond selling at or close to par, that is, a bond with a coupon close to the yields currently offered on new bonds of a similar maturity and credit risk.

Current liabilities Amount owed for salaries, interest, accounts payable and other debts due within 1 year.

Current issue In Treasury securities, the most recently auctioned issue. Trading is more active in current issues than in off-the-run issues.

Current maturity Current time to maturity on an outstanding debt instrument.

Current / noncurrent method Under this currency translation method, all of a foreign subsidiary's current assets and liabilities are translated into home currency at the current exchange rate while noncurrent assets and liabilities are translated at the historical exchange rate, that is, the rate in effect at the time the asset was acquired or the liability incurred.

Current rate method Under this currency translation method, all foreign currency balance-sheet and income statement items are translated at the current exchange rate.

Current ratio Indicator of short-term debt paying ability. Determined by dividing current assets by current liabilities. The higher the ratio, the more liquid the company.

Current yield For bonds or notes, the coupon rate divided by the market price of the bond.

Current-coupon issues Related: Benchmark issues

Cushion bonds High-coupon bonds that sell at only at a moderate premium because they are callable at a price below that at which a comparable non-callable bond would sell. Cushion bonds offer considerable downside protection in a falling market.

Custodial fees Fees charged by an institution that holds securities in safekeeping for an investor.

Customary payout ratios A range of payout ratios that is typical based on an analysis of comparable firms.

Customized benchmarks A benchmark that is designed to meet a client's requirements and long-term objectives.

Customs union An agreement by two or more countries to erect a common external tariff and to abolish restrictions on trade among members.

Date of payment Date dividend checks are mailed.

Date of record Date on which holders of record in a firm's stock ledger are designated as the recipients of either dividends or stock rights.

Dates convention Treating cash flows as being received on exact dates - date 0, date 1, and so forth - as opposed to the end-of-year convention.

Day order An order to buy or sell stock that automatically expires if it can't be executed on the day it is entered.

Day trading Refers to establishing and liquidating the same position or positions within one day's trading.

Days in receivables Average collection period.

Days' sales in inventory ratio The average number of days' worth of sales that is held in inventory.

Days' sales outstanding Average collection period.

DCF See: Discounted cash flows.

De facto Existing in actual fact although not by official recognition.

Dead cat bounce A small upmove in a bear market.

Dealer An entity that stands ready and willing to buy a security for its own account (at its bid price) or sell from its own account (at its ask price).

Dealer loan Overnight, collateralized loan made to a dealer financing his position by borrowing from a money market bank.

Dealer market A market where traders specializing in particular commodities buy and sell assets for their own accounts.

Dealer options Over-the-counter options, such as those offered by government and mortgage-backed securities dealers.

Debenture bond An unsecured bond whose holder has the claim of a general creditor on all assets of the issuer not pledged specifically to secure other debt. Compare subordinated debenture bond, and collateral trust bonds.

Debt/equity ratio Indicator of financial leverage. Compares assets provided by creditors to assets provided by shareholders. Determined by dividing long-term debt by common stockholder equity.

Debt Money borrowed.

Debt capacity Ability to borrow. The amount a firm can borrow up to the point where the firm value no longer increases.

Debt displacement The amount of borrowing that leasing displaces. Firms that do a lot of leasing will be forced to cut back on borrowing.

Debt instrument An asset requiring fixed dollar payments, such as a government or corporate bond.

Debt leverage The amplification of the return earned on equity when an investment or firm is financed partially with borrowed money.

Debt limitation A bond covenant that restricts in some way the firm's ability to incur additional indebtedness.

Debt market The market for trading debt instruments.

Debt ratio Total debt divided by total assets.

Debt relief Reducing the principal and/or interest payments on LDC loans.

Debt securities IOUs created through loan-type transactions - commercial paper, bank CDs, bills, bonds, and other instruments.

Debt service Interest payment plus repayments of principal to creditors, that is, retirement of debt.

Debt service parity approach An analysis wherein the alternatives under consideration will provide the firm with the exact same schedule of after-tax debt payments (including both interest and principal).

Debt-service coverage ratio Earnings before interest and income taxes plus one-third rental charges, divided by interest expense plus one-third rental charges plus the quantity of principal repayments divided by one minus the tax rate.

Debt swap A set of transactions (also called a debt-equity swap) in which a firm buys a country's dollar bank debt at a discount and swaps this debt with the central bank for local currency that it can use to acquire local equity.

Debtor in possession A firm that is continuing to operate under Chapter 11 bankruptcy process.

Debtor-in-possession financing New debt obtained by a firm during the Chapter 11 bankruptcy process.

Decile rank Performance over time, rated on a scale of 1-10.1 indicates that a mutual fund's return was in the top 10% of funds being compared, while 3 means the return was in the top 30%. Objective Rank compares all funds in the same investment strategy category. All Rank compares all funds.

Decision tree Method of representing alternative sequential decisions and the possible outcomes from these decisions.

Declaration date The date on which a firm's directors meet and announce the date and amount of the next dividend.

Dedicated capital Total par value (number of shares issued, multiplied by the par value of each share). Also called dedicated value.

Dedication strategy Refers to multi-period cash flow matching.

Dedicating a portfolio Related: cash flow matching.

Deductive reasoning The use of general fact to provide accurate information about a specific situation.

Deed of trust Indenture.

Deep-discount bond A bond issued with a very low coupon or no coupon and selling at a price far below par value. When the bond has no coupon, it's called a zero coupon bond.

Default Failure to make timely payment of interest or principal on a debt security or to otherwise comply with the provisions of a bond indenture.

Default premium A differential in promised yield that compensates the investor for the risk inherent in purchasing a corporate bond that entails some risk of default.

Default risk Also referred to as credit risk (as gauged by commercial rating companies), the risk that an issuer of a bond may be unable to make timely principal and interest payments.

Defeasance Practice whereby the borrower sets aside cash or bonds sufficient to service the borrower's debt. Both the borrower's debt and the offestting cash or bonds are removed from the balance sheet.

Deferred call A provision that prohibits the company from calling the bond before a certain date. During this period the bond is said to be call protected.

Deferred equity A common term for convertible bonds because of their equity component and the expectation that the bond will ultimately be converted into shares of common stock.

Deferred futures The most distant months of a futures contract. A bond that sells at a discount and does not pay interest for an initial period, typically from three to seven years. Compare step-up bond and payment-in-kind bond.

Deferred nominal life annuity A monthly fixed-dollar payment beginning at retirement age. It is nominal because the payment is fixed in dollar amount at any particular time, up to and including retirement.

Deferred taxes A non-cash expense that provides a source of free cash flow. Amount allocated during the period to cover tax liabilities that have not yet been paid.

Deferred-annuities Tax-advantaged life insurance product. Deferred annuities offer deferral of taxes with the option of withdrawing one's funds in the form of life annuity.

Deficit An excess of liabilities over assets, of losses over profits, or of expenditure over income.

Defined benefit plan A pension plan in which the sponsor agrees to make specified dollar payments to qualifying employees. The pension obligations are effectively the debt obligation of the plan sponsor. **Related:** defined contribution plan

Defined contribution plan A pension plan in which the sponsor is responsible only for making specified contributions into the plan on behalf of qualifying participants. **Related:** defined benefit plan

Delayed issuance pool Refers to MBSs that at the time of issuance were collateralized by seasoned loans originated prior to the MBS pool issue date.

Deliverable instrument The asset in a forward contract that will be delivered in the future at an agree-upon price.

Delivery The tender and receipt of an actual commodity or financial instrument in settlement of a futures contract.

Delivery notice The written notice given by the seller of his intention to make delivery against an open, short futures position on a particular date. **Related:** notice day

Delivery options The options available to the seller of an interest rate futures contract, including the quality option, the timing option, and the wild card option. Delivery options make the buyer uncertain of which Treasury Bond will be delivered or when it will be delivered.

Delivery points Those points designated by futures exchanges at which the financial instrument or commodity covered by a futures contract may be delivered in fulfillment of such contract.

Delivery price The price fixed by the Clearing house at which deliveries on futures are in invoiced; also the price at which the futures contract is settled when deliveries are made.

Delivery versus payment A transaction in which the buyer's payment for securities is due at the time of delivery (usually to a bank acting as agent for the buyer) upon receipt of the securities. The payment may be made by bank wire, check, or direct credit to an account.

Delta Also called the hedge ratio, the ratio of the change in price of a call option to the change in price of the underlying stock.

Delta hedge A dynamic hedging strategy using options with continuous adjustment of the number of options used, as a function of the delta of the option.

Delta neutral The value of the portfolio is not affected by changes in the value of the asset on which the options are written.

Demand deposits Checking accounts that pay no interest and can be withdrawn upon demand.

Demand line of credit A bank line of credit that enables a customer to borrow on a daily or on-demand basis.

Demand master notes Short-term securities that are repayable immediately upon the holder's demand.

Demand shock An event that affects the demand for goods in services in the economy.

Dependent Acceptance of a capital budgeting project contingent on the acceptance of another project.

Depository transfer check (DTC) Check made out directly by a local bank to a particular firm or person.

Depository Trust Company (DTC) DTC is a user-owned securities depository which accepts deposits of eligible securities for custody, executes book-entry deliveries and records book-entry pledges of securities in its custody, and provides for withdrawals of securities from its custody.

Depreciate To allocate the purchase cost of an asset over its life.

Depreciation A non-cash expense that provides a source of free cash flow. Amount allocated during the period to amortize the cost of acquiring Long term assets over the useful life of the assets.

Depreciation tax shield The value of the tax write-off on depreciation of plant and equipment.

Derivative instruments Contracts such as options and futures whose price is derived from the price of the underlying financial asset.

Derivative markets Markets for derivative instruments.

Derivative security A financial security, such as an option, or future, whose value is derived in part from the value and characteristics of another security, the underlying security.

Detachable warrant A warrant entitles the holder to buy a given number of shares of stock at a stipulated price. A detachable warrant is one that may be sold separately from the package it may have originally been issued with (usually a bond).

Deterministic models Liability-matching models that assume that the liability payments and the asset cash flows are known with certainty. **Related:** Compare stochastic models

Detrend To remove the general drift, tendency or bent of a set of statistical data as related to time.

Devaluation A decrease in the spot price of the currency.

Difference from S&P A mutual fund's return minus the change in the Standard & Poors 500 Index for the same time period. A notation of -5.00 means the fund return was 5 percentage points less than the gain in the S&P, while 0.00 means that the fund and the S&P had the same return.

Differential disclosure The practice of reporting conflicting or markedly different information in official corporate statements including annual and quarterly reports and the 10-Ks and 10-Qs.

Differential swap Swap between two LIBO rates of interest, e.g. yen LIBOR for dollar LIBOR. Payments are in one currency.

Diffusion process A conception of the way a stock's price changes that assumes that the price takes on all intermediate values. dirty price. **Related:** full price

Dilution Diminution in the proportion of income to which each share is entitled.

Dilutive effect Result of a transaction that decreases earnings per common share.

Direct estimate method A method of cash budgeting based on detailed estimates of cash receipts and cash disbursements category by category.

Direct lease Lease in which the lessor purchases new equipment from the manufacturer and leases it to the lessee.

Direct paper Commercial paper sold directly by the issuer to investors.

Direct placement Selling a new issue not by offering it for sale publicly, but by placing it with one of several institutional investors.

Direct quote For foreign exchange, the number of U.S. dollars needed to buy one unit of a foreign currency.

Direct search market Buyers and sellers seek each other directly and transact directly.

Direct stock-purchase programs The purchase by investors of securities directly from the issuer.

Dirty float A system of floating exchange rates in which the government occasionally intervenes to change the direction of the value of the country's currency.

Dirty price Bond price including accrued interest, i.e., the price paid by the bond buyer.

Disbursement float A decrease in book cash but no immediate change in bank cash, generated by checks written by the firm.

Disclaimer of opinion An auditor's statement disclaiming any opinion regarding the company's financial condition.

Discount Referring to the selling price of a bond, a price below its par value. **Related:** premium.

Discount bond Debt sold for less than its principal value. If a discount bond pays no interest, it is called a zero coupon bond.

Discount factor Present value of $1 received at a stated future date.

Discount period The period during which a customer can deduct the discount from the net amount of the bill when making payment.

Discount rate The interest rate that the Federal Reserve charges a bank to borrow funds when a bank is temporarily short of funds. Collateral is necessary to borrow, and such borrowing is quite limited because the Fed views it as a privilege to be used to meet short-term liquidity needs, and not a device to increase earnings.

Discount securities Non-interest-bearing money market instruments that are issued at a discount and redeemed at maturity for full face value, e.g. U.S. Treasury bills.

Discount window Facility provided by the Fed enabling member banks to borrow reserves against collateral in the form of governments or other acceptable paper.

Discounted basis Selling something on a discounted basis is selling below what its value will be at maturity, so that the difference makes up all or part of the interest.

Discounted cash flow (DCF) Future cash flows multiplied by discount factors to obtain present values.

Discounted dividend model (DDM) A formula to estimate the intrinsic value of a firm by figuring the present value of all expected future dividends.

Discounted payback period rule An investment decision rule in which the cash flows are discounted at an interest rate and the payback rule is applied on these discounted cash flows.

Discounting Calculating the present value of a future amount. The process is opposite to compounding.

Discrete compoundingM Compounding the time value of money for discrete time intervals.

Discrete random variable A random variable that can take only a certain specified set of discrete possible values **-** for example, the positive integers 1, 2, 3, . . .

Discretionary account Accounts over which an individual or organization, other than the person in whose name the account is carried, exercises trading authority or control.

Discretionary cash flow Cash flow that is available after the funding of all positive NPV capital investment projects; it is available for paying cash dividends, repurchasing common stock, retiring debt, and so on.

Discriminant analysis A statistical process that links the probability of default to a specified set of financial ratios.

Disintermediation Withdrawal of funds from a financial institution in order to invest them directly.

Distributed After a Treasury auction, there will be many new issues in dealer's hands. As those issues are sold, it is said that they are distributed.

Distributions Payments from fund or corporate cash flow. May include dividends from earnings, capital gains from sale of portfolio holdings and return of capital. Fund distributions can be made by check or by investing in additional shares. Funds are required to distribute capital gains (if any) to shareholders at least once per year. Some Corporations offer Dividend Reinvestment Plans (DRP).

Divergence When two or more averages or indices fail to show confirming trends.

Diversifiable risk Related: unsystematic risk.

Diversification Dividing investment funds among a variety of securities with different risk, reward, and correlation statistics so as to minimize unsystematic risk.

Dividend A dividend is a portion of a company's profit paid to common and preferred shareholders. A stock selling for $20 a share with an annual dividend of $1 a share yields the investor 5%.

Dividend clawback With respect to a project financing, an arrangement under which the sponsors of a project agree to contribute as equity any prior dividends received from the project to the extent necessary to cover any cash deficiencies.

Dividend clientele A group of shareholders who prefer that the firm follow a particular dividend policy. For example, such a preference is often based on comparable tax situations.

Dividend discount model (DDM) A model for valuing the common stock of a company, based on the present value of the expected cash flows.

Dividend growth model A model wherein dividends are assumed to be at a constant rate in perpetuity.

Dividend limitation A bond covenant that restricts in some way the firm's ability to pay cash dividends.

Dividend payout ratio Percentage of earnings paid out as dividends.

Dividends per share Amount of cash paid to shareholders expressed as dollars per share.

Dividend policy An established guide for the firm to determine the amount of money it will pay as dividends.

Dividend rate The fixed or floating rate paid on preferred stock based on par value.

Dividend reinvestment plan (DRP) Automatic reinvestment of shareholder dividends in more shares of a company's stock, often without commissions. Some plans provide for the purchase of additional shares at a discount to market price. Dividend reinvestment plans allow shareholders to accumulate stock over the Long term using dollar cost averaging. The DRP is usually administered by the company without charges to the holder.

Dividend rights A shareholders' rights to receive per-share dividends identical to those other shareholders receive.

Dividend yield (Funds) Indicated yield represents return on a share of a mutual fund held over the past 12 months. Assumes fund was purchased 1 year ago. Reflects effect of sales charges (at current rates), but not redemption charges.

Dividend yield (Stocks) Indicated yield represents annual dividends divided by current stock price.

Dividends per share Dividends paid for the past 12 months divided by the number of common shares outstanding, as reported by a company. The number of shares often is determined by a weighted average of shares outstanding over the reporting term.

DM Deutsche (German) marks.

Doctrine of sovereign immunity Doctrine that says a nation may not be tried in the courts of another country without its consent.

Documented discount notes Commercial paper backed by normal bank lines plus a letter of credit from a bank stating that it will pay off the paper at maturity if the borrower does not. Such paper is also referred to as LOC (letter of credit) paper.

Dollar bonds Municipal revenue bonds for which quotes are given in dollar prices. Not to be confused with "U.S. Dollar" bonds, a common term of reference in the Eurobond market.

Dollar duration The product of modified duration and the initial price.

Dollar price of a bond Percentage of face value at which a bond is quoted.

Dollar return The return realized on a portfolio for any evaluation period, including (1) the change in market value of the portfolio and (2) any distributions made from the portfolio during that period.

Dollar roll Similar to the reverse repurchase agreement **-** a simultaneous agreement to sell a security held in a portfolio with purchase of a similar security at a future date at an agreed-upon price.

Dollar safety margin The dollar equivalent of the safety cushion for a portfolio in a contingent immunization strategy.

Dollar-weighted rate of return Also called the internal rate of return, the interest rate that will make the present value of the cash flows from all the subperiods in the evaluation period plus the terminal market value of the portfolio equal to the initial market value of the portfolio.

Domestic International Sales Corporation (DISC) A U.S. corporation that receives a tax incentive for export activities.

Domestic market Part of a nation's internal market representing the mechanisms for issuing and trading securities of entities domiciled within that nation. Compare external market and foreign market.

Don't know (DK, Dked) "Don't know the trade." A Street expression used whenever one party lacks knowledge of a trade or receives conflicting instructions from the other party.

Double-declining-balance depreciation Method of accelerated depreciation.

Double-dip lease A cross-border lease in which the disparate rules of the lessor's and lessee's countries let both parties be treated as the owner of the leased equipment for tax purposes.

Double-tax agreement Agreement between two countries that taxes paid abroad can be offset against domestic taxes levied on foreign dividends.

Doubling option A sinking fund provision that may allow repurchase of twice the required number of bonds at the sinking fund call price.

Dow Jones industrial average This is the best known U.S.index of stocks. It contains 30 stocks that trade on the New York Stock Exchange. The Dow, as it is called, is a barometer of how shares of the largest U.S.companies are performing. There are thousands of investment indexes around the world for stocks, bonds, currencies and commodities.

Down-and-in option Barrier option that comes into existence if asset price hits a barrier.

Down-and-out option Barrier option that expires if asset price hits a barrier.

Downgrade A classic negative change in ratings for a stock, and or other rated security.

Draft An unconventional order in writing **-** signed by a person, usually the exporter, and addressed to the importer **-** ordering the importer or the importer's agent to pay, on demand (sight draft) or at a fixed future date (time draft), the amount specified on its face.

Drop, the With the dollar roll transaction the difference between the sale price of a mortgage-backed pass-through, and its re-purchase price on a future date at a predetermined price.

Drop lock An arrangement whereby the interest rate on a floating rate note or preferred stock becomes fixed if it falls to a specified level.

Dual syndicate equity offering An international equity placement where the offering is split into two tranches **-** domestic and foreign **-** and each tranche is handled by a separate lead manager.

Dual-currency issues Eurobonds that pay coupon interest in one currency but pay the principal in a different currency.

Due bill An instrument evidencing the obligation of a seller to deliver securities sold to the buyer. Occasionally used in the bill market.

Dupont system of financial control Highlights the fact that return on assets (ROA) can be expressed in terms of the profit margin and asset turnover.

Duration A common gauge of the price sensitivity of an asset or portfolio to a change in interest rates.

Dutch auction Auction in which the lowest price necessary to sell the entire offering becomes the price at which all securities offered are sold. This technique has been used in Treasury auctions.

Dynamic asset allocation An asset allocation strategy in which the asset mix is mechanistically shifted in response to -changing market conditions, as in a portfolio insurance strategy, for example.

Dynamic hedging A strategy that involves rebalancing hedge positions as market conditions change; a strategy that seeks to insure the value of a portfolio using a synthetic put option.

EAFE index The European, Australian, and Far East stock index, computed by Morgan Stanley.

Earning power Earnings before interest and taxes (EBIT) divided by total assets.

Earnings Net income for the company during the period.

Earnings before interest and taxes (EBIT) A financial measure defined as revenues less cost of goods sold and selling, general, and administrative expenses. In other words, operating and non-operating profit before the deduction of interest and income taxes.

Earnings per share (EPS) EPS, as it is called, is a company's profit divided by its number of outstanding shares. If a company earned $2 million in one year had 2 million shares of stock outstanding, its EPS would be $1 per share. The company often uses a weighted average of shares outstanding over the reporting term.

Earnings retention ratio Plowback rate.

Earnings surprises Positive or negative differences from the consensus forecast of earnings by institutions such as First Call or IBES. Negative earnings surprises generally have a greater adverse affect on stock prices than the reciprocal positive earnings surprise on stock prices.

Earnings yield The ratio of earnings per share after allowing for tax and interest payments on fixed interest debt, to the current share price. The inverse of the price/earnings ratio. It's the Total Twelve Months earnings divided by number of outstanding shares, divided by the recent price, multiplied by 100. The end result is shown in percentage.

Economic assumptions Economic environment in which the firm expects to reside over the life of the financial plan.

Economic defeasance See: in-substance defeasance.

Economic dependence Exists when the costs and/or revenues of one project depend on those of another.

Economic earnings The real flow of cash that a firm could pay out forever in the absence of any change in the firm's productive capacity.

Economic exposure The extent to which the value of the firm will change because of an exchange rate change.

Economic income Cash flow plus change in present value.

Economic order quantity (EOQ) The order quantity that minimizes total inventory costs.

Economic rents Profits in excess of the competitive level.

Economic risk In project financing, the risk that the project's output will not be salable at a price that will cover the project's operating and maintenance costs and its debt service requirements.

Economic surplus For any entity, the difference between the market value of all its assets and the market value of its liabilities.

Economic union An agreement between two or more countries that allows the free movement of capital, labor, all goods and services, and involves the harmonization and unification of social, fiscal, and monetary policies.

Economies of scale The decrease in the marginal cost of production as a plant's scale of operations increases.

Economies of scope Scope economies exist whenever the same investment can support multiple profitable activities less expensively in combination than separately.

EDGAR The Securities & Exchange Commission uses Electronic Data Gathering and Retrieval to transmit company documents such as 10-Ks, 10-Qs, quarterly reports, and other SEC filings, to investors.

Edge corporations Specialized banking institutions, authorized and chartered by the Federal Reserve Board in the U.S., which are allowed to engage in transactions that have a foreign or international character. They are not subject to any restrictions on interstate banking. Foreign banks operating in the U.S. are permitted to organize and own and Edge corporation.

Effective annual interest rate An annual measure of the time value of money that fully reflects the effects of compounding.

Effective annual yield Annualized interest rate on a security computed using compound interest techniques.

Effective call price The strike price in an optional redemption provision plus the accrued interest to the redemption date.

Effective convexity The convexity of a bond calculated with cash flows that change with yields.

Effective date In an interest rate swap, the date the swap begins accruing interest.

Effective duration The duration calculated using the approximate duration formula for a bond with an embedded option, reflecting the expected change in the cash flow caused by the option. Measures the responsiveness of a bond's price taking into account the expected cash flows will change as interest rates change due to the embedded option.

Effective margin (EM) Used with SAT performance measures, the amount equaling the net earned spread, or margin, of income on the assets in excess of financing costs for a given interest rate and prepayment rate scenario.

Effective rate A measure of the time value of money that fully reflects the effects of compounding.

Effective spread The gross underwriting spread adjusted for the impact of the announcement of the common stock offering on the firm's share price.

Efficiency Reflects the amount of wasted energy.

Efficient capital market A market in which new information is very quickly reflected accurately in share prices.

Efficient diversification The organizing principle of modern portfolio theory, which maintains that any risk-averse investor will search for the highest expected return for any level of portfolio risk.

Efficient frontier The combinations of securities portfolios that maximize expected return for any level of expected risk, or that minimizes expected risk for any level of expected return.

Efficient Market Hypothesis In general the hypothesis states that all relevant information is fully and immediately reflected in a security's market price thereby assuming that an investor will obtain an equilibrium rate of return. In other words, an investor should not expect to earn an abnormal return (above the market return) through either technical analysis or fundamental analysis. Three forms of efficient market hypothesis exist: weak form (stock prices reflect all information of past prices), semi-strong form (stock prices reflect all publicly available information) and strong form (stock prices reflect all relevant information including insider information).

Efficient portfolio A portfolio that provides the greatest expected return for a given level of risk (i.e. standard deviation), or equivalently, the lowest risk for a given expected return.

Efficient set Graph representing a set of portfolios that maximize expected return at each level of portfolio risk.

Either/or facility An agreement permitting a bank customer to borrow either domestic dollars from the bank's head office or Eurodollars from one of its foreign branches.

Either-way market In the interbank Eurodollar deposit market, an either-way market is one in which the bid and offered rates are identical.

Elasticity of an option Percentage change in the value of an option given a 1% change in the value of the option's underlying stock.

Electronic data interchange (EDI) The exchange of information electronically, directly from one firm's computer to another firm's computer, in a structured format.

Electronic depository transfers The transfer of funds between bank accounts through the Automated Clearing House (ACH) system.

Eligible bankers' acceptances In the BA market, an acceptance may be referred to as eligible because it is acceptable by the Fed as collateral at the discount window and/or because the accepting bank can sell it without incurring a reserve requirement.

Embedded option An option that is part of the structure of a bond that provides either the bondholder or issuer the right to take some action against the other party, as opposed to a bare option, which trades separately from any underlying security.

Emerging markets The financial markets of developing economies.

Employee stock fund A firm-sponsored program that enables employees to purchase shares of the firm's common stock on a preferential basis.

Employee stock ownership plan (ESOP) A company contributes to a trust fund that buys stock on behalf of employees.

Endogenous variable A value determined within the context of a model.

Endowment funds Investment funds established for the support of institutions such as colleges, private schools, museums, hospitals, and foundations. The investment income may be used for the operation of the institution and for capital expenditures.

End-of-year convention Treating cash flows as if they occur at the end of a year as opposed to the date convention. Under the end-of-year convention, the present is time 0, the end of year 1 occurs one year hence, etc.

Enhanced indexing Also called indexing plus, an indexing strategy whose objective is to exceed or replicate the total return performance of some predetermined index.

Enhancement An innovation that has a positive impact on one or more of a firm's existing products.

Equilibrium market price of risk The slope of the capital market line (CML). Since the CML represents the return offered to compensate for a perceived level of risk, each point on the line is a balanced market condition, or equilibrium. The slope of the line determines the additional return needed to compensate for a unit change in risk.

Equilibrium rate of interest The interest rate that clears the market. Also called the market-clearing interest rate.

Equipment trust certificates Certificates issued by a trust that was formed to purchase an asset and lease it to a lessee. When the last of the certificates has been repaid, title of ownership of the asset reverts to the lessee.

Equity Represents ownership interest in a firm. Also the residual dollar value of a futures trading account, assuming its liquidation at the going market price.

Equity cap An agreement in which one party, for an upfront premium, agrees to compensate the other at specific time periods if a designated stock market benchmark is greater than a predetermined level.

Equity claim Also called a residual claim, a claim to a share of earnings after debt obligation have been satisfied.

Equity collar The simultaneous purchase of an equity floor and sale of an equity cap.

Equity contribution agreement An agreement to contribute equity to a project under certain specified conditions.

Equity floor An agreement in which one party agrees to pay the other at specific time periods if a specific stock market benchmark is less than a predetermined level.

Equity kicker Used to refer to warrants because they are usually issued attached to privately placed bonds.

Equity market Related:Stock market

Equity multiplier Total assets divided by total common stockholders' equity; the amount of total assets per dollar of stockholders' equity.

Equity options Securities that give the holder the right to buy or sell a specified number of shares of stock, at a specified price for a certain (limited) time period. Typically one option equals 100 shares of stock.

Equity swap A swap in which the cash flows that are exchanged are based on the total return on some stock market index and an interest rate (either a fixed rate or a floating rate). **Related:** interest rate swap.

Equity-linked policies Related: Variable life

Equityholders Those holding shares of the firm's equity.

Equivalent annual annuity The equivalent amount per year for some number of years that has a present value equal to a given amount.

Equivalent annual benefit The equivalent annual annuity for the net present value of an investment project.

Equivalent annual cash flow Annuity with the same net present value as the company's proposed investment.

Equivalent annual cost The equivalent cost per year of owning an asset over its entire life.

Equivalent bond yield Annual yield on a short-term, non-interest bearing security calculated so as to be comparable to yields quoted on coupon securities.

Equivalent loan Given the after-tax stream associated with a lease, the maximum amount of conventional debt that the same period-by-period after-tax debt service stream is capable of supporting.

Equivalent taxable yield The yield that must be offered on a taxable bond issue to give the same after-tax yield as a tax-exempt issue.

Erosion An innovation that has a negative impact on one or more of a firm's existing assets.

Ethics Standards of conduct or moral judgement.

Euro CDs CDs issued by a U.S. bank branch or foreign bank located outside the U.S. Almost all Euro CDs are issued in London.

Euro lines Lines of credit granted by banks (foreign or foreign branches of U.S. banks) for Eurocurrencies.

Euro straight A fixed-rate coupon Eurobond.

Eurobank A bank that regularly accepts foreign currency denominated deposits and makes foreign currency loans.

Eurobond A bond that is (1) underwritten by an international syndicate, (2) offered at issuance simultaneously to investors in a number of countries, and (3) issued outside the jurisdiction of any single country.

Euroclear One of two principal clearing systems in the Eurobond market. It began operations in 1968, is located in Brussels, and is managed by Morgan Guaranty Bank.

Eurocredits Intermediate-term loans of Eurocurrencies made by banking syndicates to corporate and government borrowers.

Eurocurrency deposit A short-term fixed rate time deposit denominated in a currency other than the local currency (i.e. US$ deposited in a London bank).

Eurocurrency market The money market for borrowing and lending currencies that are held in the form of deposits in banks located outside the countries of the currencies issued as legal tender.

Eurodollar This is an American dollar that has been deposited in a European bank or an U.S. bank branch located in Europe. It got there as a result of payments made to overseas companies for merchandise.

Eurodollar bonds Eurobonds denominated in U.S.dollars.

Euroequity issues Securities sold in the Euromarket. That is, securities initially sold to investors simultaneously in several national markets by an international syndicate. Euromarket. **Related:** external market

European Currency Unit (ECU) An index of foreign exchange consisting of about 10 European currencies, originally devised in 1979.

European Monetary System (EMS) An exchange arrangement formed in 1979 that involves the currencies of European Union member countries.

European option Option that may be exercised only at the expiration date. **Related:** american option.

European Union (EU) An economic association of European countries founded by the Treaty of Rome in 1957 as a common market for six nations. It was known as the European Community before 1993 and is comprised of 15 European countries. Its goals are a single market for goods and services without any economic barriers and a common currency with one monetary authority. The EU was known as the European Community until January 1, 1994.

European-style option An option contract that can only be exercised on the expiration date.

Euroyen bonds Eurobonds denominated in Japanese yen.

Euro-commercial paper Short-term notes with maturities up to 360 days that are issued by companies in international money markets.

Euro-medium term note (Euro-MTN) A non-underwritten Euronote issued directly to the market. Euro-MTNs are offered continuously rather than all at once as a bond issue is. Most Euro-MTN maturities are under five years.

Euro-note Short- to medium-term debt instrument sold in the Eurocurrency market.

Evaluation period The time interval over which a money manager's performance is evaluated.

Evening up Buying or selling to offset an existing market position.

Event risk The risk that the ability of an issuer to make interest and principal payments will change because of rare, discontinuous, and very large, unanticipated changes in the market environment such as (1) a natural or industrial accident or some regulatory change or (2) a takeover or corporate restructuring.

Event study A statistical study that examines how the release of information affects prices at a particular time.

Events of default Contractually specified events that allow lenders to demand immediate repayment of a debt.

Evergreen credit Revolving credit without maturity.

Ex post return Related: Holding period return

Exact matching A bond portfolio management strategy that involves finding the lowest cost portfolio generating cash inflows exactly equal to cash outflows that are being financed by investment.

Exante return The expected return of a portfolio based on the expected returns of its component assets and their weights.

Except for opinion An auditor's opinion reflecting the fact that the auditor was unable to audit certain areas of the company's operations because of restrictions imposed by management or other conditions beyond the auditor's control.

Excess reserves Any excess of actual reserves above required reserves.

Excess return on the market portfolio The difference between the return on the market portfolio and the riskless rate.

Excess returns Also called abnormal returns, returns in excess of those required by some asset pricing model.

Exchange The marketplace in which shares, options and futures on stocks, bonds, commodities and indices are traded. Principal US stock exchanges are: New York Stock Exchange (NYSE), American Stock Exchange (AMEX) and the National Association of Securities Dealers (NASDAQ)

The Exchange A nickname for the New York stock exchange. Also known as the Big Board. More than 2,000 common and preferred stocks are traded. The exchange is the oldest in the United States, founded in 1792, and the largest. It is located on Wall Street in New York City.

Exchange controls Governmental restrictions on the purchase of foreign currencies by domestic citizens or on the purchase of the local domestic currency by foreigners.

Exchange of assets Acquisition of another company by purchase of its assets in exchange for cash or stock.

Exchange of stock Acquisition of another company by purchase of its stock in exchange for cash or shares.

Exchange offer An offer by the firm to give one security, such as a bond or preferred stock, in exchange for another security, such as shares of common stock.

Exchange rate The price of one country's currency expressed in another country's currency.

Exchange Rate Mechanism (ERM) The methodology by which members of the EMS maintain their currency exchange rates within an agreed upon range with respect to other member countries.

Exchange rate risk Also called currency risk, the risk of an investment's value changing because of currency exchange rates.

Exchange risk The variability of a firm's value that results from unexpected exchange rate changes or the extent to which the present value of a firm is expected to change as a result of a given currency's appreciation or depreciation.

Exchangeable Security Security that grants the security holder the right to exchange the security for the common stock of a firm other than the issuer of the security.

Exclusionary self-tender The firm makes a tender offer for a given amount of its own stock while excluding targeted stockholders.

Execution The process of completing an order to buy or sell securities. Once a trade is executed, it is reported by a Confirmation Report; settlement (payment and transfer of ownership) occurs in the U.S. between 1 (mutual funds) and 5 (stocks) days after an order is executed. Settlement times for exchange listed stocks are in the process of being reduced to three days in the U. S.

Execution costs The difference between the execution price of a security and the price that would have existed in the absence of a trade, which can be further divided into market impact costs and market timing costs.

Exempt securities Instruments exempt from the registration requirements of the Securities Act of 1933 or the margin requirements of the SEC Act of 1934. Such securities include government bonds, agencies, munis, commercial paper, and private placements.

Exercise To implement the right of the holder of an option to buy (in the case of a call) or sell (in the case of a put) the underlying security.

Exercise price The price at which the underlying future or options contract may be bought or sold.

Exercise value The amount of advantage over a current market transaction provided by an in-the-money option.

Exercising the option The act buying or selling the underlying asset via the option contract.

Exogenous variable A variable whose value is determined outside the model in which it is used. Also called a parameter.

Expectations hypothesis theories Theories of the term structure of interest rates which include the pure expectations theory, the liquidity theory of the term structure, and the preferred habitat theory. These theories hold that each forward rate equals the expected future interest rate for the relevant period. These three theories differ, however, on whether other factors also affect forward rates, and how.

Expectations theory of forward exchange rates A theory of foreign exchange rates that holds that the expected future spot foreign exchange rate *t* periods in the future equals the current *t*-period forward exchange rate.

Expected future cash flows Projected future cash flows associated with an asset of decision.

Expected future return The return that is expected to be earned on an asset in the future. Also called the expected return.

Expected return The return expected on a risky asset based on a probability distribution for the possible rates of return. Expected return equals some risk free rate (generally the prevailing U.S. Treasury note or bond rate) plus a risk premium (the difference between the historic market return, based upon a well diversified index such as the S&P500 and historic U.S. Treasury bond) multiplied by the assets beta.

Expected return on investment The return one can expect to earn on an investment. **See:** capital asset pricing model.

Expected return-beta relationship Implication of the CAPM that security risk premiums will be proportional to beta.

Expected value The weighted average of a probability distribution.

Expected value of perfect information The expected value if the future uncertain outcomes could be known minus the expected value with no additional information.

Expense ratio The percentage of the assets that were spent to run a mutual fund (as of the last annual statement). This includes expenses such as management and advisory fees, overhead costs and 12b-1 (distribution and advertising) fees. The expense ratio does not include brokerage costs for trading the portfolio, although these are reported as a percentage of assets to the SEC by the funds in a Statement of Additional Information (SAI). the SAI is available to shareholders on request. Neither the expense ratio or the SAI includes the transaction costs of spreads, normally incurred in unlisted securities and foreign stocks. These two costs can add significantly to the reported expenses of a fund. The expense ratio is often termed an Operating Expense Ratio (OER).

Expensed Charged to an expense account, fully reducing reported profit of that year, as is appropriate for expenditures for items with useful lives under one year.

Expiration The time when the option contract ceases to exist (expires).

Expiration cycle An expiration cycle relates to the dates on which options on a particular security expire. A given option will be placed in 1 of 3 cycles, the January cycle, the February cycle, or the March cycle. At any point in time, an option will have contracts with 4 expiration dates outstanding, 2 in near-term months and 2 in far-term months.

Expiration date The last day (in the case of American-style) or the only day (in the case of European-style) on which an option may be exercised. For stock options, this date is the Saturday immediately following the 3rd Friday of the expiration month; however, brokerage firms may set an earlier deadline for notification of an option holder's intention to exercise. If Friday is a holiday, the last trading day will be the preceding Thursday.

Export-Import Bank (Ex-Im Bank) The U.S. federal government agency that extends trade credits to U.S. companies to facilitate the financing of U.S. exports.

Exposure netting Offsetting exposures in one currency with exposures in the same or another currency, where exchange rates are expected to move in such a way that losses or gains on the first exposed position should be offset by gains or losses on the second currency exposure.

Expropriation The official seizure by a government of private property. Any government has the right to seize such property, according to international law, if prompt and adequate compensation is given.

Extendable bond Bond whose maturity can be extended at the option of the lender or issuer.

Extendable notes Note the maturity of which can be extended by mutual agreement of the issuer and investors.

Extension Voluntary arrangements to restructure a firm's debt, under which the payment date is postponed.

Extension date The day on which the first option either expires or is extended.

Extension swap Extending maturity through a swap, e.g. selling a 2-year note and buying one with a slightly longer current maturity.

External efficiency Related: pricing efficiency.

External finance Finance that is not generated by the firm: new borrowing or a stock issue.

External market Also referred to as the international market, the offshore market, or, more popularly, the Euromarket, the mechanism for trading securities that (1) at issuance are offered simultaneously to investors in a number of countries and (2) are issued outside the jurisdiction of any single country. **Related:** internal market

Extinguish Retire or pay off debt.

Extra or special dividends A dividend that is paid in addition to a firm's "regular" quarterly dividend.

Extraordinary positive value A positive net present value.

Extrapolative statistical models Models that apply a formula to historical data and project results for a future period. Such models include the simple linear trend model, the simple exponential model, and the simple autoregressive model.

Ex-dividend This literally means "without dividend." The buyer of shares when they are quoted ex-dividend is not entitled to receive a declared dividend.

Ex-dividend date The first day of trading when the seller, rather than the buyer, of a stock will be entitled to the most recently announced dividend payment. This date set by the NYSE (and generally followed on other US exchanges) is currently two business days before the record date. A stock that has gone ex-dividend is marked with an x in newspaper listings on that date.

Ex-rights In connection with a rights offering, shares of stock that are trading without the rights attached.

Ex-rights date The date on which a share of common stock begins trading ex-rights.

Face value See: Par value.

Factor A financial institution that buys a firm's accounts receivables and collects the debt.

Factor analysis A statistical procedure that seeks to explain a certain phenomenon, such as the return on a common stock, in terms of the behavior of a set of predictive factors.

Factor model A way of decomposing the factors that influence a security's rate of return into common and firm-specific influences.

Factor portfolio A well-diversified portfolio constructed to have a beta of 1.0 on one factor and a beta of zero on any other factors.

Factoring Sale of a firm's accounts receivable to a financial institution known as a factor.

Fail A trade is said to fail if on settlement date either the seller fails to deliver securities in proper form or the buyer fails to deliver funds in proper form.

Fair game An investment prospect that has a zero risk premium.

Fair market price Amount at which an asset would change hands between two parties, both having knowledge of the relevant facts. Also referred to as market price.

Fair price The equilibrium price for futures contracts. Also called the theoretical futures price, which equals the spot price continuously compounded at the cost of carry rate for some time interval.

Fair price provision See:appraisal rights.

Fair-and-equitable test A set of requirements for a plan of reorganization to be approved by the bankruptcy court.

Fallout risk A type of mortgage pipeline risk that is generally created when the terms of the loan to be originated are set at the same time as the sale terms are set. The risk is that either of the two parties, borrower or investor, fails to close and the loan "falls out" of the pipeline.

FASB Financial Accounting Standards Board. Sets accounting standards for U.S. firms.

FASB No. 8 U.S. accounting standard that requires U.S. firms to translate their foreign affiliates' accounts by the temporal method. Gains and losses from currency fluctuations were reported in current income. It was in effect between 1975 and 1981 and became the most controversial accounting standard in the U.S. It was replaced by FASB No. 52 in 1981.

FASB No. 52 The U.S. accounting standard which was replaced by FASB No. 8. U.S. companies are required to translate foreign accounts by the current rate and report the changes from currency fluctuations in a cumulative translation adjustment account in the equity section of the balance sheet.

FCIA Foreign Credit Insurance Association. A private U.S. consortium of insurance companies that offers trade credit insurance to U.S. exporters in conjunction with the U.S. Export-Import Bank.

FDIC Federal Deposit Insurance Corporation.

Feasible portfolio A portfolio that an investor can construct given the assets available.

Feasible set of portfolios The collection of all feasible portfolios.

Feasible target payout ratios Payout ratios that are consistent with the availability of excess funds to make cash dividend payments.

Federal agency securities Securities issued by corporations and agencies created by the U.S. government, such as the Federal Home Loan Bank Board and Ginnie Mae.

Federal credit agencies Agencies of the federal government set up to supply credit to various classes of institutions and individuals, e.g. S&Ls, small business firms, students, farmers, and exporters.

Federal Deposit Insurance Corporation (FDIC) A federal institution that insures bank deposits.

Federal Financing Bank A federal institution that lends to a wide array of federal credit agencies funds it obtains by borrowing from the U.S. Treasury.

Federal funds Non-interest bearing deposits held in reserve for depository institutions at their district Federal Reserve Bank. Also, excess reserves lent by banks to each other.

Federal funds market The market where banks can borrow or lend reserves, allowing banks temporarily short of their required reserves to borrow reserves from banks that have excess reserves.

Federal funds rate This is the interest rate that banks with excess reserves at a Federal Reserve district bank charge other banks that need overnight loans. The Fed Funds rate, as it is called, often points to the direction of U.S. interest rates.

Federal Home Loan Banks The institutions that regulate and lend to savings and loan associations. The Federal Home Loan Banks play a role analogous to that played by the Federal Reserve Banks vis-à-vis member commercial banks.

Federal Reserve System The central bank of the U.S., established in 1913, and governed by the Federal Reserve Board located in Washington, D.C. The system includes 12 Federal Reserve Banks and is authorized to regulate monetary policy in the U.S. as well as to supervise Federal Reserve member banks, bank holding companies, international operations of U.S.banks, and U.S.operations of foreign banks.

Federally related institutions Arms of the federal government that are exempt from SEC registration and whose securities are backed by the full faith and credit of the U.S. government (with the exception of the Tennessee Valley Authority).

Fedwire A wire transfer system for high-value payments operated by the Federal Reserve System.

FHA prepayment experience The percentage of loans in a pool of mortgages outstanding at the origination anniversary, based on annual statistical historic survival rates for FHA-insured mortgages.

Fiat money Nonconvertible paper money.

Field warehouse Warehouse rented by a warehouse company on another firm's premises.

Figuring the tail Calculating the yield at which a future money market (one available some period hence) is purchased when that future security is created by buying an existing instrument and financing the initial portion of its life with a term repo.

Fill The price at which an order is executed.

Fill or kill order A trading order that is canceled unless executed within a designated time period. **Related:** open order.

Filter A rule that stipulates when a security should be bought or sold according to past price action.

Finance A discipline concerned with determining value and making decisions. The finance function allocates resources, which includes acquiring, investing, and managing resources.

Financial analysts Also called securities analysts and investment analysts, professionals who analyze financial statements, interview corporate executives, and attend trade shows, in order to write reports recommending either purchasing, selling, or holding various stocks.

Financial assets Claims on real assets.

Financial control The management of a firm's costs and expenses in order to control them in relation to budgeted amounts.

Financial distress Events preceding and including bankruptcy, such as violation of loan contracts.

Financial distress costs Legal and administrative costs of liquidation or reorganization. Also includes implied costs associated with impaired ability to do business (indirect costs).

Financial engineering Combining or dividing existing instruments to create new financial products.

Financial future A contract entered into now that provides for the delivery of a specified asset in exchange for the selling price at some specified future date.

Financial intermediaries Institutions that provide the market function of matching borrowers and lenders or traders.

Financial lease Long-term, non-cancelable lease.

Financial leverage Use of debt to increase the expected return on equity. Financial leverage is measured by the ratio of debt to debt plus equity.

Financial leverage clientele A group of investors who have a preference for investing in firms that adhere to a particular financial leverage policy.

Financial leverage ratios Related: capitalization ratios.

Financial market An organized institutional structure or mechanism for creating and exchanging financial assets.

Financial objectives Objectives of a financial nature that the firm will strive to accomplish during the period covered by its financial plan.

Financial plan A financial blueprint for the financial future of a firm.

Financial planning The process of evaluating the investing and financing options available to a firm. It includes attempting to make optimal decisions, projecting the consequences of these decisions for the firm in the form of a financial plan, and then comparing future performance against that plan.

Financial press That portion of the media devoted to reporting financial news.

Financial ratio The result of dividing one financial statement item by another. Ratios help analysts interpret financial statements by focussing on specific relationships.

Financial risk The risk that the cash flow of an issuer will not be adequate to meet its financial obligations. Also referred to as the additional risk that a firm's stockholder bears when the firm utilizes debt and equity.

Financing decisions Decisions concerning the liabilities and stockholders' equity side of the firm's balance sheet, such as the decision to issue bonds.

Firm Refers to an order to buy or sell that can be executed without confirmation for some fixed period. Also, a synonym for company.

Firm commitment underwriting An undewriting in which an investment banking firm commits to buy the entire issue and assumes all financial responsibility for any unsold shares.

Firm's net value of debt Total firm value minus total firm debt.

Firm-specific risk See:diversifiable risk or unsystematic risk.

First notice day The first day, varying by contracts and exchanges, on which notices of intent to deliver actual financial instruments or physical commodities against futures are authorized.

First-call With CMOs, the start of the cash flow cycle for the cash flow window.

First-In-First-Out (FIFO) A method of valuing the cost of goods sold that uses the cost of the oldest item in inventory first.

First-pass regression A time series regression to estimate the betas of securities portfolios.

Fiscal agency agreement An alternative to a bond trust deed. Unlike the trustee, the fiscal agent acts as an agent of the borrower.

Fisher effect A theory that nominal interest rates in two or more countries should be equal to the required real rate of return to investors plus compensation for the expected amount of inflation in each country.

Fisher's separation theorem The firm's choice of investments is separate from its owner's attitudes towards investments. Also refered to as portfolio separation theorem.

Fiscal policy The use of government spending and taxing for the specific purpose of stabilizing the economy.

Five Cs of credit Five characteristics that are used to form a judgement about a customer's creditworthiness: character, capacity, capital, collateral, and conditions.

Fixed asset Long-lived property owned by a firm that is used by a firm in the production of its income. Tangible fixed assets include real estate, plant, and equipment. Intangible fixed assets include patents, trademarks, and customer recognition.

Fixed asset turnover ratio The ratio of sales to fixed assets.

Fixed cost A cost that is fixed in total for a given period of time and for given production levels.

Fixed-annuities Annuity contracts in which the insurance company or issuing financial institution pays a fixed dollar amount of money per period.

Fixed-charge coverage ratio A measure of a firm's ability to meet its fixed-charge obligations: the ratio of (net earnings before taxes plus interest charges paid plus long-term lease payments) to (interest charges paid plus long-term lease payments).

Fixed-dates In the Euromarket the standard periods for which Euros are traded (1 month out to a year out) are referred to as the fixed dates.

Fixed-dollar obligations Conventional bonds for which the coupon rate is set as a fixed percentage of the par value.

Fixed-dollar security A nonnegotiable debt security that can be redeemed at some fixed price or according to some schedule of fixed values, e.g., bank deposits and government savings bonds.

Fixed-exchange rate A country's decision to tie the value of its currency to another country's currency, gold (or another commodity), or a basket of currencies.

Fixed-income equivalent Also called a busted convertible, a convertible security that is trading like a straight security because the optioned common stock is trading low.

Fixed-income instruments Assets that pay a fixed-dollar amount, such as bonds and preferred stock.

Fixed-income market The market for trading bonds and preferred stock.

Fixed price basis An offering of securities at a fixed price.

Fixed-price tender offer A one-time offer to purchase a stated number of shares at a stated fixed price, usually a premium to the current market price.

Fixed-rate loan A loan on which the rate paid by the borrower is fixed for the life of the loan.

Fixed-rate payer In an interest rate swap the counterparty who pays a fixed rate, usually in exchange for a floating-rate payment.

Flat benefit formula Method used to determine a participant's benefits in a defined benefit plan by multiplying months of service by a flat monthly benefit.

Flat price risk Taking a position either long or short that does not involve spreading.

Flat trades (1) A bond in default trades flat; that is, the price quoted covers both principal and unpaid, accrued interest. (2) Any security that trades without accrued interest or at a price that includes accrued interest is said to trade flat.

Flattening of the yield curve A change in the yield curve where the spread between the yield on a long-term and short-term Treasury has decreased. Compare steepening of the yield curve and butterfly shift.

Flat price (also clean price) The quoted newspaper price of a bond that does not include accrued interest. The price paid by purchaser is the full price.

Flight to quality The tendency of investors to move towards safer, government bonds during periods of high economic uncertainty.

Flip-flop note Note that allows investors to switch between two different types of debt.

Float The number of shares that are actively tradable in the market, excluding shares that are held by officers and major stakeholders that have agreements not to sell until someone else is offered the stock.

Floater Floating rate bond.

Floating exchange rate A country's decision to allow its currency value to freely change. The currency is not constrained by central bank intervention and does not have to maintain its relationship with another currency in a narrow band. The currency value is determined by trading in the foreign exchange market.

Floating lien General lien against a company's assets or against a particular class of assets.

Floating supply The amount of securities believed to be available for immediate purchase, that is, in the hands of dealers and investors wanting to sell.

Floating-rate contract A guaranteed investment contract where the credit rating is tied to some variable ("floating") interest rate benchmark, such as a specific-maturity Treasury yield.

Floating-rate note (FRN) Note whose interest payment varies with short-term interest rates.

Floating-rate payer In an interest rate swap, the counterparty who pays a rate based on a reference rate, usually in exchange for a fixed-rate payment

Floating-rate preferred Preferred stock paying dividends that vary with short-term interest rates.

Floor broker A member who is paid a fee for executing orders for clearing members or their customers. A floor broker executing customer orders must be licensed by the CFTC.

Floor planning Arrangement used to finance inventory. A finance company buys the inventory, which is then held in trust by the user.

Floor trader A member who generally trades only for his own account, for an account controlled by him or who has such a trade made for him. Also referred to as a "local".

Flower bond Government bonds that are acceptable at par in payment of federal estate taxes when owned by the decedent at the time of death.

Flow-through basis An account for the investment credit to show all income statement benefits of the credit in the year of acquisition, rather than spreading them over the life of the asset acquired.

Flow-through method The practice of reporting to shareholders using straight-line depreciation and accelerated depreciation for tax purposes and "flowing through" the lower income taxes actually paid to the financial statement prepared for shareholders.

Force majeure risk The risk that there will be an interruption of operations for a prolonged period after a project finance project has been completed due to fire, flood, storm, or some other factor beyond the control of the project's sponsors.

Forced conversion Use of a firm's call option on a callable convertible bond when the firm knows that the bondholders will exercise their option to convert.

Foreign banking market That portion of domestic bank loans supplied to foreigners for use abroad.

Foreign bond A bond issued on the domestic capital market of anther company.

Foreign bond market That portion of the domestic bond market that represents issues floated by foreign companies to governments.

Foreign currency Foreign money.

Foreign currency option An option that conveys the right to buy or sell a specified amount of foreign currency at a specified price within a specified time period.

Foreign currency translation The process of restating foreign currency accounts of subsidiaries into the reporting currency of the parent company in order to prepare consolidated financial statements.

Foreign direct investment (FDI) The acquisition abroad of physical assets such as plant and equipment, with operating control residing in the parent corporation.

Foreign equity market That portion of the domestic equity market that represents issues floated by foreign companies.

Foreign exchange Currency from another country.

Foreign exchange controls Various forms of controls imposed by a government on the purchase/sale of foreign currencies by residents or on the purchase/sale of local currency by nonresidents.

Foreign exchange dealer A firm or individual that buys foreign exchange from one party and then sells it to another party. The dealer makes the difference between the buying and selling prices, or spread.

Foreign exchange risk The risk that a long or short position in a foreign currency might have to be closed out at a loss due to an adverse movement in the currency rates.

Foreign exchange swap An agreement to exchange stipulated amounts of one currency for another currency at one or more future dates.

Foreign market Part of a nation's internal market, representing the mechanisms for issuing and trading securities of entities domiciled outside that nation. Compare external market and domestic market.

Foreign market beta A measure of foreign market risk that is derived from the capital asset pricing model.

Foreign Sales Corporation (FSC) A special type of corporation created by the Tax Reform Act of 1984 that is designed to provide a tax incentive for exporting U.S.-produced goods.

Foreign tax credit Home country credit against domestic income tax for foreign taxes paid on foreign derived earnings.

Forex Foreign exchange.

Forfaiter Purchaser of promises to pay issued by importers.

Formula basis A method of selling a new issue of common stock in which the SEC declares the registration statement effective on the basis of a price formula rather than on a specific range.

48-hour rule The requirement that all pool information, as specified under the PSA Uniform Practices, in a TBA transaction be communicated by the seller to the buyer before 3 p.m. EST on the business day 48-hours prior to the agreed upon trade date.

Forward contract A cash market transaction in which delivery of the commodity is deferred until after the contract has been made. It is not standardized and is not traded on organized exchanges. Although the delivery is made in the future, the price is determined at the initial trade date.

Forward cover Purchase or sale of forward foreign currency in order to offset a known future cash flow.

Forward delivery A transaction in which the settlement will occur on a specified date in the future at a price agreed upon on the trade date.

Forward differential Annualized percentage difference between spot and forward rates.

Forward discount A currency trades at a forward discount when its forward price is lower than its spot price.

Forward exchange rate Exchange rate fixed today for exchanging currency at some future date.

Forward Fed funds Fed funds traded for future delivery.

Forward forward contract In Eurocurrencies, a contract under which a deposit of fixed maturity is agreed to at a fixed price for future delivery.

Forward interest rate Interest rate fixed today on a loan to be made at some future date.

Forward looking multiple A truncated expression for a P/E ratio that is based on forward (expected) earnings rather than on trailing earnings.

Forward market A market in which participants agree to trade some commodity, security, or foreign exchange at a fixed price for future delivery.

Forward premium A currency trades at a forward premium when its forward price is higher than its spot price.

Forward rate A projection of future interest rates calculated from either the spot rates or the yield curve.

Forward rate agreement (FRA) Agreement to borrow or lend at a specified future date at an interest rate that is fixed today.

Forward sale A method for hedging price risk which involves an agreement between a lender and an investor to sell particular kinds of loans at a specified price and future time.

Forward trade A transaction in which the settlement will occur on a specified date in the future at a price agreed upon the trade date.

Fourth market Direct trading in exchange-listed securities between investors without the use of a broker.

Freddie Mac (Federal Home Loan Mortgage Corporation) A Congressionally chartered corporation that purchases residential mortgages in the secondary market from S&Ls, banks, and mortgage bankers and securitizes these mortgages for sale into the capital markets.

Free cash flows Cash not required for operations or for reinvestment. Often defined as earnings before interest (often obtained from operating income line on the income statement) less capital expenditures less the change in working capital.

Free float An exchange rate system characterized by the absence of government intervention. Also known as clean float.

Free on board Implies that distributive services like transport and handling performed on goods up to the customs frontier of the economy from which the goods are classed as merchandise.

Free reserves Excess reserves minus member bank borrowings at the Fed.

Free rider A follower who avoids the cost and expense of finding the best course of action and by simply mimicking the behavior of a leader who made these investments.

Frequency distribution The organization of data to show how often certain values or ranges of values occur.

Friction costs Costs, both implied and direct, associated with a transaction. Such costs include time, effort, money, and associated tax effects of gathering information and making a transaction.

Frictions The "stickiness" in making transactions; the total hassle including time, effort, money, and tax effects of gathering information and making a transaction such as buying a stock or borrowing money.

Front fee The fee initially paid by the buyer upon entering a split-fee option contract.

Full faith-and-credit obligations The security pledges for larger municipal bond issuers, such as states and large cities which have diverse funding sources.

Full coupon bond A bond with a coupon equal to the going market rate, thereby, the bond is selling at par.

Full price Also called dirty price, the price of a bond including accrued interest. **Related**: flat price.

Full-payout lease See: financial lease.

Full-service lease Also called rental lease. Lease in which the lessor promises to maintain and insure the equipment leased.

Fully diluted earnings per shares Earnings per share expressed as if all outstanding convertible securities and warrants have been exercised.

Fully modified pass-throughs Agency pass-throughs that guarantee the timely payment of both interest and principal. **Related:** modified pass-throughs

Functional currency As defined by FASB No. 52, an affiliate's functional currency is the currency of the primary economic environment in which the affiliate generates and expends cash.

Fund family Set of funds with different investment objectives offered by one management company. In many cases, investors may move their assets from one fund to another within the family at little or no cost.

Fundamental analysis Security analysis that seeks to detect misvalued securities by an analysis of the firm's business prospects. Research analysis often focuses on earnings, dividend prospects, expectations for future interest rates, and risk evaluation of the firm.

Fundamental beta The product of a statistical model to predict the fundamental risk of a security using not only price data but other market-related and financial data.

Fundamental descriptors In the model for calculating fundamental beta, ratios in risk indexes other than market variability, which rely on financial data other than price data.

Funded debt Debt maturing after more than one year.

Funding ratio The ratio of a pension plan's assets to its liabilities.

Funding risk Related: interest rate risk

Funds From Operations (FFO) Used by real estate and other investment trusts to define the cash flow from trust operations. It is earnings with depreciation and amortization added back. A similar term increasingly used is Funds Available for Distribution (FAD), which is FFO less capital investments in trust property and the amortization of mortgages.

Future A term used to designate all contracts covering the sale of financial instruments or physical commodities for future delivery on a commodity exchange.

Future investment opportunities The options to identify additional, more valuable investment opportunities in the future that result from a current opportunity or operation.

Future value The amount of cash at a specified date in the future that is equivalent in value to a specified sum today.

Futures A term used to designate all contracts covering the sale of financial instruments or physical commodities for future delivery on a commodity exchange.

Futures commission merchant A firm or person engaged in soliciting or accepting and handling orders for the purchase or sale of futures contracts, subject to the rules of a futures exchange and, who, in connection with such solicitation or acceptance of orders, accepts any money or securities to margin any resulting trades or contracts. The FCM must be licensed by the CFTC. **Related:** commission house , omnibus account

Futures contract Agreement to buy or sell a set number of shares of a specific stock in a designated future month at a price agreed upon by the buyer and seller. The contracts themselves are often traded on the futures market. A futures contract differs from an option because an option is the right to buy or sell, whereas a futures contract is the promise to actually make a transaction. A future is part of a class of securities called derivatives, so named because such securities derive their value from the worth of an underlying investment.

Futures contract multiple A constant, set by an exchange, which when multiplied by the futures price gives the dollar value of a stock index futures contract.

Futures market A market in which contracts for future delivery of a commodity or a security are bought or sold.

Futures option An option on a futures contract. **Related:** options on physicals.

Futures price The price at which the parties to a futures contract agree to transact on the settlement date.

Gamma The ratio of a change in the option delta to a small change in the price of the asset on which the option is written.

Garmen-Kohlhagen option pricing model A widely used model for pricing foreign currency options.

Gearing Financial leverage.

GEMs (growing-equity mortgages) Mortgages in which annual increases in monthly payments are used to reduce outstanding principal and to shorten the term of the loan.

General cash offer A public offering made to investors at large.

General obligation bonds Municipal securities secured by the issuer's pledge of its full faith, credit, and taxing power.

General partner A partner who has unlimited liability for the obligations of the partnership.

General partnership A partnership in which all partners are general partners.

Generally Accepted Accounting Principals (GAAP) A technical accounting term that encompasses the conventions, rules, and procedures necessary to define accepted accounting practice at a particular time.

Generic Refers to the characteristics and/or experience of the total universe of a coupon of MBS sector type; that is, in contrast to a specific pool or collateral group, as in a specific CMO issue.

Geographic risk Risk that arises when an issuer has policies concentrated within certain geographic areas, such as the risk of damage from a hurricane or an earthquake.

Geometric mean return Also called the time weighted rate of return, a measure of the compounded rate of growth of the initial portfolio market value during the evaluation period, assuming that all cash distributions are reinvested in the portfolio. It is computed by taking the geometric average of the portfolio subperiod returns.

Gestation repo A reverse repurchase agreement between mortgage firms and securities dealers. Under the agreement, the firm sells federal agency-guaranteed MBS and simultaneously agrees to repurchase them at a future date at a fixed price.

Gilts British and Irish government securities.

Ginnie Mae See:Government National Mortgage Association.

Give up The loss in yield that occurs when a block of bonds is swapped for another block of lower-coupon bonds. Can also be referred to as "after-tax give up" when the implications of the profit or loss on taxes are considered.

Glass-Steagall Act A 1933 act in which Congress forbade commercial banks to own, underwrite, or deal in corporate stock and corporate bonds.

Global bonds Bonds that are designed so as to qualify for immediate trading in any domestic capital market and in the Euromarket.

Global fund A mutual fund that can invest anywhere in the world, including the U.S.

Globalization Tendency toward a worldwide investment environment, and the integration of national capital markets.

GMCs (guaranteed mortgage certificates) First issued by Freddie Mac in 1975, GMCs, like PCs, represent undivided interest in specified conventional whole loans and participations previously purchased by Freddie Mac.

GNMA-I Mortgage-backed securities (MBS) on which registered holders receive separate principal and interest payments on each of their certificates, usually directly from the servicer of the MBS pool. GNMA-I mortgage-backed securities are single-issuer pools.

GNMA-II Mortgage-backed securities (MBS) on which registered holders receive an aggregate principal and interest payment from a central paying agent on all of their certificates. Principal and interest payments are disbursed on the 20th day of the month. GNMA-II MBS are backed by multiple-issuer pools or custom pools (one issuer but different interest rates that may vary within one percentage point). Multiple-issuer pools are known as "Jumbos." Jumbo pools are generally longer and offer certain mortgages that are more geographically diverse than single-issuer pools. Jumbo pool mortgage interest rates may vary within one percentage point.

GNMA Midget A GNMA pass-through certificate backed by fixed rate mortgages with a 15 year maturity. GNMA Midget is a dealer term and is not used by GNMA in the formal description of its programs.

Gnomes Freddic Mac's 15-year, fixed-rate pass-through securities issued under its cash program.

Go-around When the Fed offers to buy securities, to sell securities, to do repo, or to do reverses, it solicits competitive bids or offers from all primary dealers.

Going-private transactions Publicly owned stock in a firm is replaced with complete equity ownership by a private group. The shares are delisted from stock exchanges and can no longer be purchased in the open markets.

Gold exchange standard A system of fixing exchange rates adopted in the Bretton Woods agreement. It involved the U.S. pegging the dollar to gold and other countries pegging their currencies to the dollar.

Gold standard An international monetary system in which currencies are defined in terms of their gold content and payment imbalances between countries are settled in gold. It was in effect from about 1870-1914.

Golden parachute Compensation paid to top-level management by a target firm if a takeover occurs.

Good delivery A delivery in which everything **-** endorsement, any necessary attached legal papers, etc. **-** is in order.

Good delivery and settlement procedures Refers to PSA Uniform Practices such as cutoff times on delivery of securities and notification, allocation, and proper endorsement.

Good 'til canceled Sometimes simply called "GTC", it means an order to buy or sell stock that is good until you cancel it. Brokerages usually set a limit of 30-60 days, at which the GTC expires if not restated.

Goodwill Excess of the purchase price over the fair market value of the net assets acquired under purchase accounting.

Government bond See: Government securities.

Government National Mortgage Association (Ginnie Mae) A wholly owned U.S. government corporation within the Department of Housing & Urban Development. Ginnie Mae guarantees the timely payment of principal and interest on securities issued by approved servicers that are collateralized by FHA-issued, VA-guaranteed, or Farmers Home Administration (FmHA)-guaranteed mortgages.

Government sponsored enterprises Privately owned, publicly chartered entities, such as the Student Loan Marketing Association, created by Congress to reduce the cost of capital for certain borrowing sectors of the economy including farmers, homeowners, and students.

Government securities Negotiable U.S. Treasury securities.

Graduated-payment mortgages (GPMs) A type of stepped-payment loan in which the borrower's payments are initially lower than those on a comparable level-rate mortgage. The payments are gradually increased over a predetermined period (usually 3,5, or 7 years) and then are fixed at a level-pay schedule which will be higher than the level-pay amortization of a level-pay mortgage originated at the same time. The difference between what the borrower actually pays and the amount required to fully amortize the mortgage is added to the unpaid principal balance.

Graham-Harvey Measure 1 Performance measure invented by John Graham and Campbell Harvey. The idea is to lever a fund's portfolio to exactly match the volatility of the S and P 500. The difference between the fund's levered return and the S&P 500 return is the performance measure.

Graham-Harvey Measure 2 Performance measure invented by John Graham and Campbell Harvey. The idea is to lever the S&P 500 portfolio to exactly match the volatility of the fund. The difference between the fund's return and the levered S&P 500 return is the performance measure.

Grantor trust A mechanism of issuing MBS wherein the mortgages' collateral is deposited with a trustee under a custodial or trust agreement.

Gray market Purchases and sales of eurobonds that occur before the issue price is finally set.

Greenmail Situation in which a large block of stock is held by an unfriendly company, forcing the target company to repurchase the stock at a substantial premium to prevent a takeover.

Greenshoe option Option that allows the underwriter for a new issue to buy and resell additional shares.

Gross domestic product (GDP) The market value of goods and services produced over time including the income of foreign corporations and foreign residents working in the U.S., but excluding the income of U.S. residents and corporations overseas.

Gross interest Interest earned before taxes are deducted.

Gross national product (GNP) Measures and economy's total income. It is equal to GDP plus the income abroad accruing to domestic residents minus income generated in domestic market accruing to non-residents.

Gross profit margin Gross profit divided by sales, which is equal to each sales dollar left over after paying for the cost of goods sold.

Gross spread The fraction of the gross proceeds of an underwritten securities offering that is paid as compensation to the underwriters of the offering.

Group of five (G-5) The five leading countries (France, Germany, Japan, United Kingdom, and the U.S.) that meet periodically to achieve some cooperative effort on international economic issues. When currency issues are discussed, the monetary authorities of these nations hold the meeting.

Group of seven (G-7) The G-5 countries plus Canada and Italy.

Group rotation manager A top-down manager who infers the phases of the business cycle and allocates assets accordingly.

Growing perpetuity A constant stream of cash flows without end that is expected to rise indefinitely.

Growth manager A money manager who seeks to buy stocks that are typically selling at relatively high P/E ratios due to high earnings growth, with the expectation of continued high or higher earnings growth.

Growth opportunity Opportunity to invest in profitable projects.

Growth phase A phase of development in which a company experiences rapid earnings growth as it produces new products and expands market share.

Growth rates Compound annual growth rate for the number of full fiscal years shown. If there is a negative or zero value for the first or last year, the growth is NM (not meaningful).

Growth stock Common stock of a company that has an opportunity to invest money and earn more than the opportunity cost of capital.

Guaranteed insurance contract A contract promising a stated nominal interest rate over some specific time period, usually several years.

Guaranteed investment contract (GIC) A pure investment product in which a life company agrees, for a single premium, to pay the principal amount of a predetermined annual crediting (interest) rate over the life of the investment, all of which is paid at the maturity date.

Guarantor program Under the Freddie Mac program, the aggregation by a single issuer (usually an S&L) for the purpose of forming a qualifying pool to be issued as PCs under the Freddie Mac guarantee.

Haircut The margin or difference between the actual market value of a security and the value assessed by the lending side of a transaction (ie. a repo).

Handle The whole-dollar price of a bid or offer is referred to as the handle (ie. if a security is quoted at 101.10 bid and 101.11 offered, 101 is the handle). Traders are assumed to know the handle.

Hard capital rationing Capital rationing that under no circumstances can be violated.

Hard currency A freely convertible currency that is not expected to depreciate in value in the foreseeable future.

Harmless warrant Warrant that allows the user to purchase a bond only by surrendering an existing bond with similar terms.

Head & shoulders In technical analysis, a chart formation in which a stock price reaches a peak and declines, rises above its former peak and again declines and rises again but not to the second peak and then again declines. The first and third peaks are shoulders, while the second peak is the formation's head. Technical analysts generally consider a head and shoulders formation to be a very bearish indication.

Hedge A transaction that reduces the risk of an investment.

Hedge fund A fund that may employ a variety of techniques to enhance returns, such as both buying and shorting stocks based on a valuation model.

Hedge ratio (delta) The ratio of volatility of the portfolio to be hedged and the return of the volatility of the hedging instrument.

Hedged portfolio A portfolio consisting of the long position in the stock and the short position in the call option, so as to be riskless and produce a return that equals the risk-free interest rate.

Hedgie Slang for a hedge fund.

Hedging A strategy designed to reduce investment risk using call options, put options, short selling, or futures contracts. A hedge can help lock in existing profits. Its purpose is to reduce the volatility of a portfolio, by reducing the risk of loss.

Hedging demands Demands for securities to hedge particular sources of consumption risk, beyond the usual mean-variance diversification motivation.

Hell-or-high-water contract A contract that obligates a purchaser of a project's output to make cash payments to the project in all events, even if no product is offered for sale.

Herstatt risk The risk of loss in foreign exchange trading that one party will deliver foreign exchange but the counterparty financial institution will fail to deliver its end of the contract. It is also referred to as settlement risk.

High-coupon bond refunding Refunding of a high-coupon bond with a new, lower coupon bond.

High price The highest (intraday) price of a stock over the past 52 weeks, adjusted for any stock splits.

High-yield bond See:junk bond.

Highly leveraged transaction (HLT) Bank loan to a highly leveraged firm.

Historical exchange rate An accounting term that refers to the exchange rate in effect when an asset or liability was acquired.

Hit A dealer who agrees to sell at the bid price quoted by another dealer is said to "hit" that bid.

Holder-of-record date The date on which holders of record in a firm's stock ledger are designated as the recipients of either dividends or stock rights. Also called date of record.

Holding company A corporation that owns enough voting stock in another firm to control management and operations by influencing or electing its board of directors.

Holding period Length of time that an individual holds a security.

Holding period return The rate of return over a given period.

Homemade dividend Sale of some shares of stock to get cash that would be similar to receiving a cash dividend.

Homemade leverage Idea that as long as individuals borrow (or lend) on the same terms as the firm, they can duplicate the affects of corporate leverage on their own. Thus, if levered firms are priced too high, rational investors will simply borrow on personal accounts to buy shares in unlevered firms.

Homogeneity The degree to which items are similar.

Homogeneous Exhibiting a high degree of homogeneity.

Homogenous expectations assumption An assumption of Markowitz portfolio construction that investors have the same expectations with respect to the inputs that are used to derive efficient portfolios: asset returns, variances, and covariances.

Horizon analysis An analysis of returns using total return to assess performance over some investment horizon.

Horizon return Total return over a given horizon.

Horizontal acquisition Merger between two companies producing similar goods or services.

Horizontal analysis The process of dividing each expense item of a given year by the same expense item in the base year. This allows for the exploration of changes in the relative importance of expense items over time and the behavior of expense items as sales change.

Horizontal merger A merger involving two or more firms in the same industry that are both at the same stage in the production cycle; that is two or more competitors.

Horizontal spread The simultaneous purchase and sale of two options that differ only in their exercise date.

Host security The security to which a warrant is attached.

Hot money Money that moves across country borders in response to interest rate differences and that moves away when the interest rate differential disappears.

Hubris An arrogance due to excessive pride and an insolence toward others.

Human capital The unique capabilities and expertise of individuals.

Hurdle rate The required return in capital budgeting.

Hybrid A package containing two or more different kinds of risk management instruments that are usually interactive.

Hybrid security A convertible security whose optioned common stock is trading in a middle range, causing the convertible security to trade with the characteristics of both a fixed-income security and a common stock instrument.

Idiosyncratic Risk Unsystematic risk or risk that is uncorrelated to the overall market risk. In other words, the risk that is firm specific and can be diversified through holding a portfolio of stocks.

Immediate settlement Delivery and settlement of securities within five business days.

Immunization The construction of an asset and a liability that are subject to offsetting changes in value.

Immunization strategy A bond portfolio strategy whose goal is to eliminate the portfolio's risk against a general change in the rate of interest through the use of duration.

Implied call The right of the homeowner to prepay, or call, the mortgage at any time.

Implied repo rate The rate that a seller of a futures contract can earn by buying an issue and then delivering it at the settlement date. **Related:** cheapest to deliver issue

Implied volatility The expected volatility in a stock's return derived from its option price, maturity date, exercise price, and riskless rate of return, using an option-pricing model such as Black/Scholes.

Import-substitution development strategy A development strategy followed by many Latin American countries and other LDCs that emphasized import substitution - accomplished through protectionism - as the route to economic growth.

Imputation tax system Arrangement by which investors who receive a dividend also receive a tax credit for corporate taxes that the firm has paid.

Income beneficiary One who receives income from a trust.

Income bond A bond on which the payment of interest is contingent on sufficient earnings. These bonds are commonly used during the reorganization of a failed or failing business.

Income fund A mutual fund providing for liberal current income from investments.

Income statement (statement of operations) A statement showing the revenues, expenses, and income (the difference between revenues and expenses) of a corporation over some period of time.

Income stock Common stock with a high dividend yield and few profitable investment opportunities.

Incremental cash flows Difference between the firm's cash flows with and without a project.

Incremental costs and benefits Costs and benefits that would occur if a particular course of action were taken compared to those that would occur if that course of action were not taken.

Incremental internal rate of return IRR on the incremental investment from choosing a large project instead of a smaller project.

Indenture Agreement between lender and borrower which details specific terms of the bond issuance. Specifies legal obligations of bond issuer and rights of bondholders.

Independent project A project whose acceptance or rejection is independent of the acceptance or rejection of other projects.

Index and Option Market (IOM) A division of the CME established in 1982 for trading stock index products and options. **Related:** Chicago Mercantile Exchange (CME).

Index arbitrage An investment/trading strategy that exploits divergences between actual and theoretical futures prices.

Index fund Investment fund designed to match the returns on a stockmarket index.

Index model A model of stock returns using a market index such as the S&P 500 to represent common or systematic risk factors.

Index option A call or put option based on a stock market index.

Index warrant A stock index option issued by either a corporate or sovereign entity as part of a security offering, and guaranteed by an option clearing corporation.

Indexed bond Bond whose payments are linked to an index, e.g. the consumer price index.

Indexing A passive instrument strategy consisting of the construction of a portfolio of stocks designed to track the total return performance of an index of stocks.

Indicated dividend Total amount of dividends that would be paid on a share of stock over the next 12 months if each dividend were the same amount as the most recent dividend. Usually represent by the letter "e" in stock tables.

Indicated yield The yield, based on the most recent quarterly rate times four. To determine the yield, divide the annual dividend by the price of the stock. The resulting number is represented as a percentage. **See:** dividend yield.

Indifference curve The graphical expression of a utility function, where the horizontal axis measures risk and the vertical axis measures expected return. The curve connects all portfolios with the same utilities according to γ and σ .

Indirect quote For foreign exchange, the number of units of a foreign currency needed to buy one U.S.$.

Inductive reasoning The attempt to use information about a specific situation to draw a conclusion.

Industry The category describing a company's primary business activity. This category is usually determined by the largest portion of revenue.

Industrial revenue bond (IRB) Bond issued by local government agencies on behalf of corporations.

Inflation The rate at which the general level of prices for goods and services is rising.

Inflation risk Also called purchasing-power risk, the risk that changes in the real return the investor will realize after adjusting for inflation will be negative.

Inflation uncertainty The fact that future inflation rates are not known. It is a possible contributing factor to the makeup of the term structure of interest rates.

Inflation-escalator clause A clause in a contract providing for increases or decreases in inflation based on fluctuations in the cost of living, production costs, and so forth.

Information asymmetry A situation involving information that is known to some, but not all, participants.

Information Coefficient (IC) The correlation between predicted and actual stock returns, sometimes used to measure the value of a financial analyst. An IC of 1.0 indicates a perfect linear relationship between predicted and actual returns, while an IC of 0.0 indicates no linear relationship.

Information costs Transaction costs that include the assessment of the investment merits of a financial asset. **Related:** search costs.

Information services Organizations that furnish investment and other types of information, such as information that helps a firm monitor its cash position.

Information-content effect The rise in the stock price following the dividend signal.

Informational efficiency The speed and accuracy with which prices reflect new information.

Informationless trades Trades that are the result of either a reallocation of wealth or an implementation of an investment strategy that only utilizes existing information.

Information-motivated trades Trades in which an investor believes he or she possesses pertinent information not currently reflected in the stock's price.

Initial margin requirement When buying securities on margin, the proportion of the total market value of the securities that the investor must pay for in cash. The Security Exchange Act of 1934 gives the board of governors of the Federal Reserve the responsibility to set initial margin requirements, but individual brokerage firms are free to set higher requirements. In futures contracts, initial margin requirements are set by the exchange.

Initial public offering (IPO) A company's first sale of stock to the public. Securities offered in an IPO are often, but not always, those of young, small companies seeking outside equity capital and a public market for their stock. Investors purchasing stock in IPOs generally must be prepared to accept very large risks for the possibility of large gains. IPO's by investment companies (closed-end funds) usually contain underwriting fees which represent a load to buyers.

Input-output tables Tables that indicate how much each industry requires of the production of each other industry in order to produce each dollar of its own output.

Insider information Relevant information about a company that has not yet been made public. It is illegal for holders of this information to make trades based on it, however received.

Insider trading Trading by officers, directors, major stockholders, or others who hold private inside information allowing them to benefit from buying or selling stock.

Insiders These are directors and senior officers of a corporation -- in effect those who have access to inside information about a company. An insider also is someone who owns more than 10% of the voting shares of a company.

Insolvency risk The risk that a firm will be unable to satisfy its debts. Also known as bankruptcy risk.

Insolvent A firm that is unable to pay debts (liabilities are greater than assets).

Installment sale The sale of an asset in exchange for a specified series of payments (the installments).

Institutional investors Organizations that invest, including insurance companies, depository institutions, pension funds, investment companies, mutual funds, and endowment funds.

Institutionalization The gradual domination of financial markets by institutional investors, as opposed to individual investors. This process has occurred throughout the industrialized world.

Instruments Financial securities, such as money market instruments or capital market insturments.

Insurance principle The law of averages. The average outcome for many independent trials of an experiment will approach the expected value of the experiment.

Insured bond A municipal bond backed both by the credit of the municipal issuer and by commercial insurance policies.

Insured plans Defined benefit pension plans that are guaranteed by life insurance products. **Related:** non-insured plans

Intangible asset A legal claim to some future benefit, typically a claim to future cash. Goodwill, intellectual property, patents, copyrights, and trademarks are examples of intangible assets.

Integer programming Variant of linear programming whereby the solution values must be integers.

Intercompany loan Loan made by one unit of a corporation to another unit of the same corporation.

Intercompany transaction Transaction carried out between two units of the same corporation.

Interest The price paid for borrowing money. It is expressed as a percentage rate over a period of time and reflects the rate of exchange of present consumption for future consumption. Also, a share or title in property.

Interest coverage ratio The ratio of the earnings before interest and taxes to the annual interest expense. This ratio measures a firm's ability to pay interest.

Interest coverage test A debt limitation that prohibits the issuance of additional long-term debt if the issuer's interest coverage would, as a result of the issue, fall below some specified minimum.

Interest equalization tax Tax on foreign investment by residents of the U.S. which was abolished in 1974.

Interest payments Contractual debt payments based on the coupon rate of interest and the principal amount.

Interest on interest Interest earned on reinvestment of each interest payment on money invested. **See:** compound interest.

Interest-only strip (IO) A security based solely on the interest payments form a pool of mortgages, Treasury bonds, or other bonds. Once the principal on the mortgages or bonds has been repaid, interest payments stop and the value of the IO falls to zero.

Interest rate agreement An agreement whereby one party, for an upfront premium, agrees to compensate the other at specific time periods if a designated interest rate (the reference rate) is different from a predetermined level (the strike rate).

Interest rate cap Also called an interest rate ceiling, an interest rate agreement in which payments are made when the reference rate exceeds the strike rate.

Interest rate ceiling Related: interest rate cap.

Interest rate floor An interest rate agreement in which payments are made when the reference rate falls below the strike rate.

Interest rate on debt The firm's cost of debt capital.

Interest rate parity theorem Interest rate differential between two countries is equal to the difference between the forward foreign exchange rate and the spot rate.

Interest rate risk The risk that a security's value changes due to a change in interest rates. For example, a bond's price drops as interest rates rise. For a depository institution, also called funding risk, the risk that spread income will suffer because of a change in interest rates.

Interest rate swap A binding agreement between counterparties to exchange periodic interest payments on some predetermined dollar principal, which is called the notional principal amount. For example, one party will pay fixed and receive variable.

Interest subsidy A firm's deduction of the interest payments on its debt from its earnings before it calculates its tax bill under current tax law.

Interest tax shield The reduction in income taxes that results from the tax-deductibility of interest payments.

Intermarket sector spread The spread between the interest rate offered in two sectors of the bond market for issues of the same maturity.

Intermarket spread swaps An exchange of one bond for another based on the manager's projection of a realignment of spreads between sectors of the bond market.

Intermediate-term Typically 1-10 years.

Intermediation Investment through a financial institution. **Related:** disintermediation.

Internal finance Finance generated within a firm by retained earnings and depreciation.

Internal growth rate Maximum rate a firm can expand without outside source of funding. Growth generated by cash flows retained by company.

Internal market The mechanisms for issuing and trading securities within a nation, including its domestic market and foreign market. **Compare:** external market.

Internal measure The number of days that a firm can finance operations without additional cash income.

Internal rate of return Dollar-weighted rate of return. Discount rate at which net present value (NPV) investment is zero. The rate at which a bond's future cash flows, discounted back to today, equals its price.

Internally efficient market Operationally efficient market.

International Bank for Reconstruction and Development - IBRD or World Bank International Bank for Reconstruction and Development makes loans at nearly conventional terms to countries for projects of high economic priority.

International Banking Facility (IBF) International Banking Facility. A branch that an American bank establishes in the United States to do Eurocurrency business.

International bonds A collective term that refers to global bonds, Eurobonds, and foreign bonds.

International Depository Receipt (IDR) A receipt issued by a bank as evidence of ownership of one or more shares of the underlying stock of a foreign corporation that the bank holds in trust. The advantage of the IDR structure is that the corporation does not have to comply with all the regulatory issuing requirements of the foreign country where the stock is to be traded. The U.S. version of the IDR is the American Depository Receipt (ADR).

International diversification The attempt to reduce risk by investing in the more than one nation. By diversifying across nations whose economic cycles are not perfectly correlated, investors can typically reduce the variability of their returns.

International finance subsidiary A subsidiary incorporated in the U.S., usually in Delaware, whose sole purpose was to issue debentures overseas and invest the proceeds in foreign operations, with the interest paid to foreign bondholders not subject to U.S. withholding tax. The elimination of the corporate withholding tax has ended the need for this type of subsidiary.

International Fisher effect States that the interest rate differential between two countries should be an unbiased predictor of the future change in the spot rate.

International fund A mutual fund that can invest only outside the United States.

International market Related: See external market.

International Monetary Fund An organization founded in 1944 to oversee exchange arrangements of member countries and to lend foreign currency reserves to members with short-term balance of payment problems.

International Monetary Market (IMM) A division of the CME established in 1972 for trading financial futures. **Related:** Chicago Mercantile Exchange (CME).

In-the-money A put option that has a strike price higher than the underlying futures price, or a call option with a strike price lower than the underlying futures price. For example, if the March COMEX silver futures contract is trading at $6 an ounce, a March call with a strike price of $5.50 would be considered in-the-money by $0.50 an ounce. **Related:** put.

Intramarket sector spread The spread between two issues of the same maturity within a market sector. For instance, the difference in interest rates offered for five-year industrial corporate bonds and five-year utility corporate bonds.

Intrinsic value of an option The amount by which an option is in-the-money. An option which is not in-the-money has no intrinsic value. **Related:** in-the-money.

Intrinsic value of a firm The present value of a firm's expected future net cash flows discounted by the required rate of return.

Inventory For companies: Raw materials, items available for sale or in the process of being made ready for sale. They can be individually valued by several different means, including cost or current market value, and collectively by FIFO, LIFO or other techniques. The lower value of alternatives is usually used to preclude overstating earnings and assets. For security firms: securities bought and held by a broker or dealer for resale.

Inventory loan A secured short-term loan to purchase inventory. The three basic forms are a blanket inventory lien, a trust receipt, and field warehousing financing.

Inventory turnover The ratio of annual sales to average inventory which measures the speed that inventory is produced and sold. Low turnover is an unhealthy sign, indicating excess stocks and/or poor sales.

Inverse floating rate note A variable rate security whose coupon rate increases as a benchmark interest rate declines.

Inverted market A futures market in which the nearer months are selling at price premiums to the more distant months. **Related:** premium.

Investment analysts Related: financial analysts

Investment bank Financial intermediaries who perform a variety of services, including aiding in the sale of securities, facilitating mergers and other corporate reorganizations, acting as brokers to both individual and institutional clients, and trading for their own accounts. Underwriters.

Investment decisions Decisions concerning the asset side of a firm's balance sheet, such as the decision to offer a new product.

Investment grade bonds A bond that is assigned a rating in the top four categories by commercial credit rating companies. For example, S&P classifies investment grade bonds as BBB or higher, and Moodys' classifies investment grade bonds as Ba or higher. **Related:** High-yield bond.

Investment income The revenue from a portfolio of invested assets.

Investment management Also called portfolio management and money management, the process of managing money.

Investment manager Also called a portfolio manager and money manager, the individual who manages a portfolio of investments.

Investment product line (IPML) The line of required returns for investment projects as a function of beta (nondiversifiable risk).

Investment tax credit Proportion of new capital investment that can be used to reduce a company's tax bill (abolished in 1986).

Investment trust A closed-end fund regulated by the Investment Company Act of 1940. These funds have a fixed number of shares which are traded on the secondary markets similarly to corporate stocks. The market price may exceed the net asset value per share, in which case it is considered at a "premium." When the market price falls below the NAV/share, it is at a "discount." Many closed-end funds are of a specialized nature, with the portfolio representing a particular industry, country, etc. These funds are usually listed on US and foreign exchanges.

Investment value Related:straight value.

Investments As a discipline, the study of financial securities, such as stocks and bonds, from the investor's viewpoint. This area deals with the firm's financing decision, but from the other side of the transaction.

Investor The owner of a financial asset.

Investor fallout In the mortgage pipeline, risk that occurs when the originator commits loan terms to the borrowers and gets commitments from investors at the time of application, or if both sets of terms are made at closing.

Investor relations The process by which the corporation communicates with its investors.

Investor's equity The balance of a margin account. **Related:** buying on margin, initial margin requirement.

Invoice Bill written by a seller of goods or services and submitted to the purchaser.

Invoice billing Billing system in which the invoices are sent off at the time of customer orders are all separate bills to be paid.

Invoice date Usually the date when goods are shipped. Payment dates are set relative to the invoice date.

Invoice price The price that the buyer of a futures contract must pay the seller when a Treasury Bond is delivered.

In-house processing float Refers to the time it takes the receiver of a check to process the payment and deposit it in a bank for collection.

In-substance defeasance Defeasance whereby debt is removed from the balance sheet but not cancelled.

In the box This means that a dealer has a wire receipt for securities indicating that effective delivery on them has been made.

Involuntary liquidation preference A premium that must be paid to preferred or preference stockholders if the issuer of the stock is forced into involuntary liquidation.

IRA/Keogh accounts Special accounts where you can save and invest, and the taxes are deferred until money is withdrawn. These plans are subject to frequent changes in law with respect to the deductibility of contributions. Withdrawals of tax deferred contributions are taxed as income, including the capital gains from such accounts.

Irrational call option The implied call imbedded in the MBS. Identified as irrational because the call is sometimes not exercised when it is in the money (interest rates are below the threshold to refinance). Sometimes exercised when not in the money (home sold without regard to the relative level of interest rates).

Irrelevance result The Modigliani and Miller theorem that a firm's capital structure is irrelevant to the firm's value.

ISDA International Swap Dealers Association. Formed in 1985 to promote uniform practices in the writing, trading, and settlement of swaps and other derivatives.

ISMA International Security Market Association. ISMA is a Swiss law association located in Zurich that regroups all the participants on the Eurobond primary and secondary markets. Establishes uniform trading procedures in the international bond markets.

Issue A particular financial asset.

Issued share capital Total amount of shares that are in issue. **Related:** outstanding shares.

Issuer An entity that issues a financial asset.

J-curve Theory that says a country's trade deficit will initially worsen after its currency depreciates because higher prices on foreign imports will more than offset the reduced volume of imports in the short-run.

Jensen index An index that uses the capital asset pricing model to determine whether a money manager outperformed a market index. The "alpha" of an investment or investment manager.

Joint account An agreement between two or more firms to share risk and financing responsibility in purchasing or underwriting securities.

Joint clearing members Firms that clear on more than one exchange.

Jumbo loan Loans of $1 billion or more. Or, loans that exceed the statutory size limit eligible for purchase or securitization by the federal agencies.

Junk bond A bond with a speculative credit rating of BB (S&P) or Ba (Moody's) or lower is a junk or high yield bond. Such bonds offer investors higher yields than bonds of financially sound companies. Two agencies, Standard & Poors and Moody's investor Services, provide the rating systems for companies' credit.

Junior debt (subordinate debt) Debt whose holders have a claim on the firm's assets only after senior debtholder's claims have been satisfied. Subordinated debt.

Just-in-time inventory systems Systems that schedule materials/inventory to arrive exactly as they are needed in the production process.

Kappa The ratio of the dollar price change in the price of an option to a 1% change in the expected price volatility.

Kiretsu A network of Japanese companies organized around a major bank.

Ladder strategy A bond portfolio strategy in which the portfolio is constructed to have approximately equal amounts invested in every maturity within a given range.

Lag Payment of a financial obligation later than is expected or required, as in lead and lag. Also, the number of periods that an independent variable in a regression model is "held back" in order to predict the dependent variable.

Lag response of prepayments There is typically a lag of about three months between the time the weighted average coupon of an MBS pool has crossed the threshold for refinancing and an acceleration in prepayment speed is observed.

Lambda The ratio of a change in the option price to a small change in the option volatility. It is the partial derivative of the option price with respect to the option volatility.

Last split After a stock split, the number of shares distributed for each share held and the date of the distribution.

Last trading day The final day under an exchange's rules during which trading may take place in a particular futures or options contract. Contracts outstanding at the end of the last trading day must be settled by delivery of underlying physical commodities or financial instruments, or by agreement for monetary settlement depending upon futures contract specifications.

Last-In-First-Out (LIFO) A method of valuing inventory that uses the cost of the most recent item in inventory first.

Law of large numbers The mean of a random sample approaches the mean (expected value) of the population as the sample grows.

Law of one price An economic rule stating that a given security must have the same price regardless of the means by which one goes about creating that security. This implies that if the payoff of a security can be synthetically created by a package of other securities, the price of the package and the price of the security whose payoff it replicates must be equal.

Lead Payment of a financial obligation earlier than is expected or required.

Lead manager The commercial or investment bank with the primary responsibility for organizing syndicated bank credit or bond issue. The lead manager recruits additional lending or underwriting banks, negotiates terms of the issue with the issuer, and assesses market conditions.

Leading economic indicators Economic series that tend to rise or fall in advance of the rest of the economy.

Leakage Release of information to some persons before official public announcement.

LEAPS Long-term equity anticipation securities. Long-term options.

Lease A long-term rental agreement, and a form of secured long-term debt.

Lease Rate The payment per period stated in a lease contract.

Ledger cash A firm's cash balance as reported in its financial statements. Also called book cash.

Legal capital Value at which a company's shares are recorded in its books.

Legal bankruptcy A legal proceeding for liquidating or reorganizing a business.

Legal defeasance The deposit of cash and permitted securities, as specified in the bond indenture, into an irrevocable trust sufficient to enable the issuer to discharge fully its obligations under the bond indenture.

Legal investments Investments that a regulated entity is permitted to make under the rules and regulations that govern its investing.

Lend To provide money temporarily on the condition that it or its equivalent will be returned, often with an interest fee.

Lessee An entity that leases an asset from another entity.

Lessor An entity that leases an asset to another entity.

Letter of comment A communication to the firm from the SEC that suggests changes to its registration statement.

Letter of credit (L/C) A form of guarantee of payment issued by a bank used to guarantee the payment of interest and repayment of principal on bond issues.

Letter stock Privately placed common stock, so-called because the SEC requires a letter from the purchaser stating that the stock is not intended for resale.

Level pay The characteristic of the scheduled principal and interest payments due under a mortgage such that total monthly payment of P&I is the same while characteristically the principal payment component of the monthly payment becomes gradually greater while the monthly interest payment becomes less.

Level-coupon bond Bond with a stream of coupon payments that are the same throughout the life of the bond.

Leverage The use of debt financing.

Leverage clientele A group of shareholders who, because of their personal leverage, seek to invest in corporations that maintain a compatible degree of corporate leverage.

Leverage ratios Measures of the relative contribution of stockholders and creditors, and of the firm's ability to pay financing charges. Value of firm's debt to the total value of the firm.

Leverage rebalancing Making transactions to adjust (rebalance) a firm's leverage ratio back to its target.

Leveraged beta The beta of a leveraged required return; that is, the beta as adjusted for the degree of leverage in the firm's capital structure.

Leveraged buyout (LBO) A transaction used for taking a public corporation private financed through the use of debt funds: bank loans and bonds. Because of the large amount of debt relative to equity in the new corporation, the bonds are typically rated below investment grade, properly referred to as high-yield bonds or junk bonds. Investors can participate in an LBO through either the purchase of the debt (i.e., purchase of the bonds or participation in the bank loan) or the purchase of equity through an LBO fund that specializes in such investments.

Leveraged equity Stock in a firm that relies on financial leverage. Holders of leveraged equity face the benefits and costs of using debt.

Leveraged lease A lease arrangement under which the lessor borrows a large proportion of the funds needed to purchase the asset and grants the lender a lien on the assets and a pledge of the lease payments to secure the borrowing.

Leveraged portfolio A portfolio that includes risky assets purchased with funds borrowed.

Leveraged required return The required return on an investment when the investment is financed partially by debt.

Liability A financial obligation, or the cash outlay that must be made at a specific time to satisfy the contractual terms of such an obligation.

Liability funding strategies Investment strategies that select assets so that cash flows will equal or exceed the client's obligations.

Liability swap An interest rate swap used to alter the cash flow characteristics of an institution's liabilities so as to provide a better match with its assets.

LIBOR The London Interbank Offered Rate; the rate of interest that major international banks in London charge each other for borrowings. Many variable interest rates in the U.S. are based on spreads off of LIBOR. There are many different LIBOR tenors.

Lien A security interest in one or more assets that is granted to lenders in connection with secured debt financing.

LIFO (Last-in-first-out) The last-in-first-out inventory valuation methodology. A method of valuing inventory that uses the cost of the most recent item in inventory first.

Lifting a leg Closing out one side of a long-short arbitrage before the other is closed.

Limit order An order to buy a stock at or below a specified price or to sell a stock at or above a specified price. For instance, you could tell a broker "Buy me 100 shares of XYZ Corp at $8 or less" or to "sell 100 shares of XYZ at $10 or better." The customer specifies a price and the order can be executed only if the market reaches or betters that price. A conditional trading order designed to avoid the danger of adverse unexpected price changes.

Limit order book A record of unexecuted limit orders that is maintained by the specialist. These orders are treated equally with other orders in terms of priority of execution.

Limit price Maximum price fluctuation

Limitation on asset dispositions A bond covenant that restricts in some way a firm's ability to sell major assets.

Limitation on liens A bond covenant that restricts in some way a firm's ability to grant liens on its assets.

Limitation on merger, consolidation, or sale A bond covenant that restricts in some way a firm's ability to merge or consolidate with another firm.

Limitation on sale-and-leaseback A bond covenant that restricts in some way a firm's ability to enter into sale and lease-back transactions.

Limitation on subsidiary borrowing A bond covenant that restricts in some way a firm's ability to borrow at the subsidiary level.

Limited liability Limitation of possible loss to what has already been invested.

Limited partner A partner who has limited legal liability for the obligations of the partnership.

Limited partnership A partnership that includes one or more partners who have limited liability.

Limited-liability instrument A security, such as a call option, in which the owner can only lose his initial investment.

Limited-tax general obligation bond A general obligation bond that is limited as to revenue sources.

Line of credit An informal arrangement between a bank and a customer establishing a maximum loan balance that the bank will permit the borrower to maintain.

Linear programming Technique for finding the maximum value of some equation subject to stated linear constraints.

Linear regression A statistical technique for fitting a straight line to a set of data points.

Linter's observations John Lintner's work (1956) suggested that dividend policy is related to a target level of dividends and the speed of adjustment of change in dividends.

Liquid asset Asset that is easily and cheaply turned into cash **-** notably cash itself and short-term securities.

Liquid yield option note (LYON) Zero-coupon, callable, putable, convertible bond invented by Merrill Lynch & Co.

Liquidating dividend Payment by a firm to its owners from capital rather than from earnings.

Liquidation When a firm's business is terminated, assets are sold, proceeds pay creditors and any leftovers are distributed to shareholders. Any transaction that offsets or closes out a Long or short position. **Related:** buy in, evening up, offsetliquidity.

Liquidation rights The rights of a firm's securityholders in the event the firm liquidates.

Liquidation value Net amount that could be realized by selling the assets of a firm after paying the debt.

Liquidator Person appointed by unsecured creditors in the United Kingdom to oversee the sale of an insolvent firm's assets and the repayment of its debts.

Liquidity A market is liquid when it has a high level of trading activity, allowing buying and selling with minimum price disturbance. Also a market characterized by the ability to buy and sell with relative ease.

Liquidity diversification Investing in a variety of maturities to reduce the price risk to which holding long bonds exposes the investor.

Liquidity preference hypothesis The argument that greater liquidity is valuable, all else equal. Also, the theory that the forward rate exceeds expected future interest rates.

Liquidity premium Forward rate minus expected future short-term interest rate.

Liquidity ratios Ratios that measure a firm's ability to meet its short-term financial obligations on time.

Liquidity risk The risk that arises from the difficulty of selling an asset. It can be thought of as the difference between the "true value" of the asset and the likely price, less commissions.

Liquidity theory of the term structure A biased expectations theory that asserts that the implied forward rates will not be a pure estimate of the market's expectations of future interest rates because they embody a liquidity premium.

Listed stocks Stocks that are traded on an exchange.

Load fund A mutual fund with shares sold at a price including a large sales charge **--** typically 4% to 8% of the net amount indicated. Some "no-load" funds have distribution fees permitted by article 12b-1 of the Investment Company Act; these are typically 0. 25%. A "true no-load" fund has neither a sales charge nor Freddie Mac program, the aggregation that the fund purchaser receives some investment advice or other service worthy of the charge.

Load-to-load Arrangement whereby the customer pays for the last delivery when the next one is received.

Loan amortization schedule The schedule for repaying the interest and principal on a loan.

Loan syndication Group of banks sharing a loan. **See:** syndicate.

Loan value The amount a policyholder may borrow against a whole life insurance policy at the interest rate specified in the policy.

Local expectations theory A form of the pure expectations theory which suggests that the returns on bonds of different maturities will be the same over a short-term investment horizon.

Lockbox A collection and processing service provided to firms by banks, which collect payments from a dedicated postal box that the firm directs its customers to send payment to. The banks make several collections per day, process the payments immediately, and deposit the funds into the firm's bank account.

Locked market A market is locked if the bid = ask price. This can occur, for example, if the market is brokered and brokerage is paid by one side only, the initiator of the transaction.

Lock-out With PAC bond CMO classes, the period before the PAC sinking fund becomes effective. With multifamily loans, the period of time during which prepayment is prohibited.

Lock-up CDs CDs that are issued with the tacit understanding that the buyer will not trade the certificate. Quite often, the issuing bank will insist that the certificate be safekept by it to ensure that the understanding is honored by the buyer.

Log-linear least-squares method A statistical technique for fitting a curve to a set of data points. One of the variables is transformed by taking its logarithm, and then a straight line is fitted to the transformed set of data points.

Lognormal distribution A distribution where the logarithm of the variable follows a normal distribution. Lognormal distributions are used to describe returns calculated over periods of a year or more.

London International Financial Futures Exchange (LIFFE) A London exchange where Eurodollar futures as well as futures-style options are traded.

Long One who has bought a contract(s) to establish a market position and who has not yet closed out this position through an offsetting sale; the opposite of short.

Long bonds Bonds with a long current maturity. The "long bond" is the 30-year U.S. government bond.

Long coupons (1) Bonds or notes with a long current maturity. (2) A bond on which one of the coupon periods, usually the first, is longer than the other periods or the standard period.

Long hedge The purchase of a futures contract(s) in anticipation of actual purchases in the cash market. Used by processors or exporters as protection against an advance in the cash price. **Related:** Hedge, short hedge

Long position An options position where a person has executed one or more option trades where the net result is that they are an "owner" or holder of options (i. e. the number of contracts bought exceeds the number of contracts sold).

Occurs when an individual owns securities. An owner of 1,000 shares of stock is said to be "Long the stock." Related: Short position

Long run A period of time in which all costs are variable; greater than one year.

Long straddle A straddle in which a long position is taken in both a put and call option.

Long-term In accounting information, one year or greater.

Long-term assets Value of property, equipment and other capital assets minus the depreciation. This is an entry in the bookkeeping records of a company, usually on a "cost" basis and thus does not necessarily reflect the market value of the assets.

Long-term debt An obligation having a maturity of more than one year from the date it was issued. Also called funded debt.

Long-term debt/capitalization Indicator of financial leverage. Shows long-term debt as a proportion of the capital available. Determined by dividing long-term debt by the sum of long-term debt, preferred stock and common stockholder equity.

Long-term debt ratio The ratio of long-term debt to total capitalization.

Long-term financial plan Financial plan covering two or more years of future operations.

Long-term liabilities Amount owed for leases, bond repayment and other items due after 1 year.

Long-term debt to equity ratio A capitalization ratio comparing long-term debt to shareholders' equity.

Look-thru A method for calculating U.S. taxes owed on income from controlled foreign corporations that was introduced by the Tax Reform Act of 1986.

Lookback option An option that allows the buyer to choose as the option strike price any price of the underlying asset that has occurred during the life of the option. If a call, the buyer will choose the minimal price, whereas if a put, the buyer will choose the maximum price. This option will always be in the money.

Low-coupon bond refunding Refunding of a low coupon bond with a new, higher coupon bond.

Low price This is the day's lowest price of a security that has changed hands between a buyer and a seller.

Low price-earnings ratio effect The tendency of portfolios of stocks with a low price-earnings ratio to outperform portfolios consisting of stocks with a high price-earnings ratio.

Ladder strategy A bond portfolio strategy in which the portfolio is constructed to have approximately equal amounts invested in every maturity within a given range.

Lag Payment of a financial obligation later than is expected or required, as in lead and lag. Also, the number of periods that an independent variable in a regression model is "held back" in order to predict the dependent variable.

Lag response of prepayments There is typically a lag of about three months between the time the weighted average coupon of an MBS pool has crossed the threshold for refinancing and an acceleration in prepayment speed is observed.

Lambda The ratio of a change in the option price to a small change in the option volatility. It is the partial derivative of the option price with respect to the option volatility.

Last split After a stock split, the number of shares distributed for each share held and the date of the distribution.

Last trading day The final day under an exchange's rules during which trading may take place in a particular futures or options contract. Contracts outstanding at the end of the last trading day must be settled by delivery of underlying physical commodities or financial instruments, or by agreement for monetary settlement depending upon futures contract specifications.

Last-In-First-Out (LIFO) A method of valuing inventory that uses the cost of the most recent item in inventory first.

Law of large numbers The mean of a random sample approaches the mean (expected value) of the population as the sample grows.

Law of one price An economic rule stating that a given security must have the same price regardless of the means by which one goes about creating that security. This implies that if the payoff of a security can be synthetically created by a package of other securities, the price of the package and the price of the security whose payoff it replicates must be equal.

Lead Payment of a financial obligation earlier than is expected or required.

Lead manager The commercial or investment bank with the primary responsibility for organizing syndicated bank credit or bond issue. The lead manager recruits additional lending or underwriting banks, negotiates terms of the issue with the issuer, and assesses market conditions.

Leading economic indicators Economic series that tend to rise or fall in advance of the rest of the economy.

Leakage Release of information to some persons before official public announcement.

LEAPS Long-term equity anticipation securities. Long-term options.

Lease A long-term rental agreement, and a form of secured long-term debt.

Lease Rate The payment per period stated in a lease contract.

Ledger cash A firm's cash balance as reported in its financial statements. Also called book cash.

Legal capital Value at which a company's shares are recorded in its books.

Legal bankruptcy A legal proceeding for liquidating or reorganizing a business.

Legal defeasance The deposit of cash and permitted securities, as specified in the bond indenture, into an irrevocable trust sufficient to enable the issuer to discharge fully its obligations under the bond indenture.

Legal investments Investments that a regulated entity is permitted to make under the rules and regulations that govern its investing.

Lend To provide money temporarily on the condition that it or its equivalent will be returned, often with an interest fee.

Lessee An entity that leases an asset from another entity.

Lessor An entity that leases an asset to another entity.

Letter of comment A communication to the firm from the SEC that suggests changes to its registration statement.

Letter of credit (L/C) A form of guarantee of payment issued by a bank used to guarantee the payment of interest and repayment of principal on bond issues.

Letter stock Privately placed common stock, so-called because the SEC requires a letter from the purchaser stating that the stock is not intended for resale.

Level pay The characteristic of the scheduled principal and interest payments due under a mortgage such that total monthly payment of P&I is the same while characteristically the principal payment component of the monthly payment becomes gradually greater while the monthly interest payment becomes less.

Level-coupon bond Bond with a stream of coupon payments that are the same throughout the life of the bond.

Leverage The use of debt financing.

Leverage clientele A group of shareholders who, because of their personal leverage, seek to invest in corporations that maintain a compatible degree of corporate leverage.

Leverage ratios Measures of the relative contribution of stockholders and creditors, and of the firm's ability to pay financing charges. Value of firm's debt to the total value of the firm.

Leverage rebalancing Making transactions to adjust (rebalance) a firm's leverage ratio back to its target.

Leveraged beta The beta of a leveraged required return; that is, the beta as adjusted for the degree of leverage in the firm's capital structure.

Leveraged buyout (LBO) A transaction used for taking a public corporation private financed through the use of debt funds: bank loans and bonds. Because of the large amount of debt relative to equity in the new corporation, the bonds are typically rated below investment grade, properly referred to as high-yield bonds or junk bonds. Investors can participate in an LBO through either the purchase of the debt (i.e., purchase of the bonds or participation in the bank loan) or the purchase of equity through an LBO fund that specializes in such investments.

Leveraged equity Stock in a firm that relies on financial leverage. Holders of leveraged equity face the benefits and costs of using debt.

Leveraged lease A lease arrangement under which the lessor borrows a large proportion of the funds needed to purchase the asset and grants the lender a lien on the assets and a pledge of the lease payments to secure the borrowing.

Leveraged portfolio A portfolio that includes risky assets purchased with funds borrowed.

Leveraged required return The required return on an investment when the investment is financed partially by debt.

Liability A financial obligation, or the cash outlay that must be made at a specific time to satisfy the contractual terms of such an obligation.

Liability funding strategies Investment strategies that select assets so that cash flows will equal or exceed the client's obligations.

Liability swap An interest rate swap used to alter the cash flow characteristics of an institution's liabilities so as to provide a better match with its assets.

LIBOR The London Interbank Offered Rate; the rate of interest that major international banks in London charge each other for borrowings. Many variable interest rates in the U.S. are based on spreads off of LIBOR. There are many different LIBOR tenors.

Lien A security interest in one or more assets that is granted to lenders in connection with secured debt financing.

LIFO (Last-in-first-out) The last-in-first-out inventory valuation methodology. A method of valuing inventory that uses the cost of the most recent item in inventory first.

Lifting a leg Closing out one side of a long-short arbitrage before the other is closed.

Limit order An order to buy a stock at or below a specified price or to sell a stock at or above a specified price. For instance, you could tell a broker "Buy me 100 shares of XYZ Corp at $8 or less" or to "sell 100 shares of XYZ at $10 or better." The customer specifies a price and the order can be executed only if the market reaches or betters that price. A conditional trading order designed to avoid the danger of adverse unexpected price changes.

Limit order book A record of unexecuted limit orders that is maintained by the specialist. These orders are treated equally with other orders in terms of priority of execution.

Limit price Maximum price fluctuation

Limitation on asset dispositions A bond covenant that restricts in some way a firm's ability to sell major assets.

Limitation on liens A bond covenant that restricts in some way a firm's ability to grant liens on its assets.

Limitation on merger, consolidation, or sale A bond covenant that restricts in some way a firm's ability to merge or consolidate with another firm.

Limitation on sale-and-leaseback A bond covenant that restricts in some way a firm's ability to enter into sale and lease-back transactions.

Limitation on subsidiary borrowing A bond covenant that restricts in some way a firm's ability to borrow at the subsidiary level.

Limited liability Limitation of possible loss to what has already been invested.

Limited partner A partner who has limited legal liability for the obligations of the partnership.

Limited partnership A partnership that includes one or more partners who have limited liability.

Limited-liability instrument A security, such as a call option, in which the owner can only lose his initial investment.

Limited-tax general obligation bond A general obligation bond that is limited as to revenue sources.

Line of credit An informal arrangement between a bank and a customer establishing a maximum loan balance that the bank will permit the borrower to maintain.

Linear programming Technique for finding the maximum value of some equation subject to stated linear constraints.

Linear regression A statistical technique for fitting a straight line to a set of data points.

Linter's observations John Lintner's work (1956) suggested that dividend policy is related to a target level of dividends and the speed of adjustment of change in dividends.

Liquid asset Asset that is easily and cheaply turned into cash **-** notably cash itself and short-term securities.

Liquid yield option note (LYON) Zero-coupon, callable, putable, convertible bond invented by Merrill Lynch & Co.

Liquidating dividend Payment by a firm to its owners from capital rather than from earnings.

Liquidation When a firm's business is terminated, assets are sold, proceeds pay creditors and any leftovers are distributed to shareholders. Any transaction that offsets or closes out a Long or short position. **Related:** buy in, evening up, offsetliquidity.

Liquidation rights The rights of a firm's securityholders in the event the firm liquidates.

Liquidation value Net amount that could be realized by selling the assets of a firm after paying the debt.

Liquidator Person appointed by unsecured creditors in the United Kingdom to oversee the sale of an insolvent firm's assets and the repayment of its debts.

Liquidity A market is liquid when it has a high level of trading activity, allowing buying and selling with minimum price disturbance. Also a market characterized by the ability to buy and sell with relative ease.

Liquidity diversification Investing in a variety of maturities to reduce the price risk to which holding long bonds exposes the investor.

Liquidity preference hypothesis The argument that greater liquidity is valuable, all else equal. Also, the theory that the forward rate exceeds expected future interest rates.

Liquidity premium Forward rate minus expected future short-term interest rate.

Liquidity ratios Ratios that measure a firm's ability to meet its short-term financial obligations on time.

Liquidity risk The risk that arises from the difficulty of selling an asset. It can be thought of as the difference between the "true value" of the asset and the likely price, less commissions.

Liquidity theory of the term structure A biased expectations theory that asserts that the implied forward rates will not be a pure estimate of the market's expectations of future interest rates because they embody a liquidity premium.

Listed stocks Stocks that are traded on an exchange.

Load fund A mutual fund with shares sold at a price including a large sales charge **--** typically 4% to 8% of the net amount indicated. Some "no-load" funds have distribution fees permitted by article 12b-1 of the Investment Company Act; these are typically 0. 25%. A "true no-load" fund has neither a sales charge nor Freddie Mac program, the aggregation that the fund purchaser receives some investment advice or other service worthy of the charge.

Load-to-load Arrangement whereby the customer pays for the last delivery when the next one is received.

Loan amortization schedule The schedule for repaying the interest and principal on a loan.

Loan syndication Group of banks sharing a loan. **See:** syndicate.

Loan value The amount a policyholder may borrow against a whole life insurance policy at the interest rate specified in the policy.

Local expectations theory A form of the pure expectations theory which suggests that the returns on bonds of different maturities will be the same over a short-term investment horizon.

Lockbox A collection and processing service provided to firms by banks, which collect payments from a dedicated postal box that the firm directs its customers to send payment to. The banks make several collections per day, process the payments immediately, and deposit the funds into the firm's bank account.

Locked market A market is locked if the bid = ask price. This can occur, for example, if the market is brokered and brokerage is paid by one side only, the initiator of the transaction.

Lock-out With PAC bond CMO classes, the period before the PAC sinking fund becomes effective. With multifamily loans, the period of time during which prepayment is prohibited.

Lock-up CDs CDs that are issued with the tacit understanding that the buyer will not trade the certificate. Quite often, the issuing bank will insist that the certificate be safekept by it to ensure that the understanding is honored by the buyer.

Log-linear least-squares method A statistical technique for fitting a curve to a set of data points. One of the variables is transformed by taking its logarithm, and then a straight line is fitted to the transformed set of data points.

Lognormal distribution A distribution where the logarithm of the variable follows a normal distribution. Lognormal distributions are used to describe returns calculated over periods of a year or more.

London International Financial Futures Exchange (LIFFE) A London exchange where Eurodollar futures as well as futures-style options are traded.

Long One who has bought a contract(s) to establish a market position and who has not yet closed out this position through an offsetting sale; the opposite of short.

Long bonds Bonds with a long current maturity. The "long bond" is the 30-year U.S. government bond.

Long coupons (1) Bonds or notes with a long current maturity. (2) A bond on which one of the coupon periods, usually the first, is longer than the other periods or the standard period.

Long hedge The purchase of a futures contract(s) in anticipation of actual purchases in the cash market. Used by processors or exporters as protection against an advance in the cash price. **Related:** Hedge, short hedge

Long position An options position where a person has executed one or more option trades where the net result is that they are an "owner" or holder of options (i. e. the number of contracts bought exceeds the number of contracts sold).

Occurs when an individual owns securities. An owner of 1,000 shares of stock is said to be "Long the stock." Related: Short position

Long run A period of time in which all costs are variable; greater than one year.

Long straddle A straddle in which a long position is taken in both a put and call option.

Long-term In accounting information, one year or greater.

Long-term assets Value of property, equipment and other capital assets minus the depreciation. This is an entry in the bookkeeping records of a company, usually on a "cost" basis and thus does not necessarily reflect the market value of the assets.

Long-term debt An obligation having a maturity of more than one year from the date it was issued. Also called funded debt.

Long-term debt/capitalization Indicator of financial leverage. Shows long-term debt as a proportion of the capital available. Determined by dividing long-term debt by the sum of long-term debt, preferred stock and common stockholder equity.

Long-term debt ratio The ratio of long-term debt to total capitalization.

Long-term financial plan Financial plan covering two or more years of future operations.

Long-term liabilities Amount owed for leases, bond repayment and other items due after 1 year.

Long-term debt to equity ratio A capitalization ratio comparing long-term debt to shareholders' equity.

Look-thru A method for calculating U.S. taxes owed on income from controlled foreign corporations that was introduced by the Tax Reform Act of 1986.

Lookback option An option that allows the buyer to choose as the option strike price any price of the underlying asset that has occurred during the life of the option. If a call, the buyer will choose the minimal price, whereas if a put, the buyer will choose the maximum price. This option will always be in the money.

Low-coupon bond refunding Refunding of a low coupon bond with a new, higher coupon bond.

Low price This is the day's lowest price of a security that has changed hands between a buyer and a seller.

Low price-earnings ratio effect The tendency of portfolios of stocks with a low price-earnings ratio to outperform portfolios consisting of stocks with a high price-earnings ratio.

Macaulay duration The weighted-average term to maturity of the cash flows from the bond, where the weights are the present value of the cash flow divided by the price.

Magic of diversification The effective reduction of risk (variance) of a portfolio, achieved without reduction to expected returns through the combination of assets with low or negative correlations (covariances). **Related:** Markowitz diversification

Mail float Refers to the part of the collection and disbursement process where checks are trapped in the postal system.

Maintenance margin requirement A sum, usually smaller than -but part of the original margin, which must be maintained on deposit at all times. If a customer's equity in any futures position drops to, or under, the maintenance margin level, the broker must issue a margin call for the amount at money required to restore the customer's equity in the account to the original margin level. **Related:** margin, margin call.

Make a market A dealer is said to make a market when he quotes bid and offered prices at which he stands ready to buy and sell.

Making delivery Refers to the seller's actually turning over to the buyer the asset agreed upon in a forward contract.

Majority voting Voting system under which each director is voted upon separately. **Related:** cumulative voting.

Managed float Also known as "dirty" float, this is a system of floating exchange rates with central bank intervention to reduce currency fluctuations.

Management/closely held shares Percentage of shares held by persons closely related to a company, as defined by the Securities and exchange commission. Part of these percentages often is included in Institutional Holdings **--** making the combined total of these percentages over 100. There is overlap as institutions sometimes acquire enough stock to be considered by the SEC to be closely allied to the company.

Management buyout (MBO) Leveraged buyout whereby the acquiring group is led by the firm's management.

Management fee An investment advisory fee charged by the financial advisor to a fund based on the fund's average assets, but sometimes determined on a sliding scale that declines as the dollar amount of the fund increases.

Mangement's discussion A report from management to the shareholders that accompanies the firm's financial statements in the annual report. This report explains the period's financial results and enables management to discuss other ideas that may not be apparent in the financial statements in the annual report.

Managerial decisions Decisions concerning the operation of the firm, such as the choice of firm size, firm growth rates, and employee compensation.

Mandatory redemption schedule Schedule according to which sinking fund payments must be made.

Manufactured housing securities (MHSs) Loans on manufactured homes **-** that is, factory-built or prefabricated housing, including mobile homes.

Margin This allows investors to buy securities by borrowing money from a broker. The margin is the difference between the market value of a stock and the loan a broker makes. Related: security deposit (initial).

Margin account (Stocks) A leverageable account in which stocks can be purchased for a combination of cash and a loan. The loan in the margin account is collateralized by the stock and, if the value of the stock drops sufficiently, the owner will be asked to either put in more cash, or sell a portion of the stock. Margin rules are federally regulated, but margin requirements and interest may vary among broker/dealers.

Margin call A demand for additional funds because of adverse price movement. Maintenance margin requirement, security deposit maintenance

Margin of safety With respect to working capital management, the difference between 1) the amount of long-term financing, and 2) the sum of fixed assets and the permanent component of current assets.

Margin requirement (Options) The amount of cash an uncovered (naked) option writer is required to deposit and maintain to cover his daily position valuation and reasonably foreseeable intra-day price changes.

Marginal Incremental.

Marginal tax rate The tax rate that would have to be paid on any additional dollars of taxable income earned.

Mark-to-market The process whereby the book value or collateral value of a security is adjusted to reflect current market value.

Marked-to-market An arrangement whereby the profits or losses on a futures contract are settled each day.

Market capitalization The total dollar value of all outstanding shares. Computed as shares times current market price. It is a measure of corporate size.

Market capitalization rate Expected return on a security. The market-consensus estimate of the appropriate discount rate for a firm's cash flows.

Market clearing Total demand for loans by borrowers equals total supply of loans from lenders. The market, any market, clears at the equilibrium rate of interest or price.

Market conversion price Also called conversion parity price, the price that an investor effectively pays for common stock by purchasing a convertible security and then exercising the conversion option. This price is equal to the market price of the convertible security divided by the conversion ratio.

Market cycle The period between the 2 latest highs or lows of the S&P 500, showing net performance of a fund through both an up and a down market. A market cycle is complete when the S&P is 15% below the highest point or 15% above the lowest point (ending a down market). The dates of the last market cycle are: 12/04/87 to 10/11/90 (low to low).

Market impact costs Also called price impact costs, the result of a bid/ask spread and a dealer's price concession.

Market model This relationship is sometimes called the single-index model. The market model says that the return on a security depends on the return on the market portfolio and the extent of the security's responsiveness as measured, by beta. In addition, the return will also depend on conditions that are unique to the firm. Graphically, the market model can be depicted as a line fitted to a plot of asset returns against returns on the market portfolio.

Market order This is an order to immediately buy or sell a security at the current trading price.

Market overhang The theory that in certain situations, institutions wish to sell their shares but postpone the share sales because large orders under current market conditions would drive down the share price and that the consequent threat of securities sales will tend to retard the rate of share price appreciation. Support for this theory is largely anecdotal.

Market portfolio A portfolio consisting of all assets available to investors, with each asset held -in proportion to its market value relative to the total market value of all assets.

Market price of risk A measure of the extra return, or risk premium, that investors demand to bear risk. The reward-to-risk ratio of the market portfolio.

Market prices The amount of money that a willing buyer pays to acquire something from a willing seller, when a buyer and seller are independent and when such an exchange is motivated by only commercial consideration.

Market return The return on the market portfolio.

Market risk Risk that cannot be diversified away. **Related:** systematic risk

Market sectors The classifications of bonds by issuer characteristics, such as state government, corporate, or utility.

Market segmentation theory or preferred habitat theory A biased expectations theory that asserts that the shape of the yield curve is determined by the supply of and demand for securities within each maturity sector.

Market timer A money manager who assumes he or she can forecast when the stock market will go up and down.

Market timing Asset allocation in which the investment in the market is increased if one forecasts that the market will outperform T-bills.

Market timing costs Costs that arise from price movement of the stock during the time of the transaction which is attributed to other activity in the stock.

Market value (1) The price at which a security is trading and could presumably be purchased or sold. (2) The value investors believe a firm is worth; calculated by multiplying the number of shares outstanding by the current market price of a firm's shares.

Market value ratios Ratios that relate the market price of the firm's common stock to selected financial statement items.

Market value-weighted index An index of a group of securities computed by calculating a weighted average of the returns on each security in the index, with the weights proportional to outstanding market value.

Market-book ratio Market price of a share divided by book value per share.

Market-if-touched (MIT) A price order, below market if a buy or above market if a sell, that automatically becomes a market order if the specified price is reached.

Marketability A negotiable security is said to have good marketability if there is an active secondary market in which it can easily be resold.

Marketed claims Claims that can be bought and sold in financial markets, such as those of stockholders and bondholders.

Marketplace price efficiency The degree to which the prices of assets reflect the available marketplace information. Marketplace price efficiency is sometimes estimated as the difficulty faced by active management of earning a greater return than passive management would, after adjusting for the risk associated with a strategy and the transactions costs associated with implementing a strategy.

Markowitz diversification A strategy that seeks to combine assets a portfolio with returns that are less than perfectly positively correlated, in an effort to lower portfolio risk (variance) without sacrificing return. **Related:** naive diversification

Markowitz efficient frontier The graphical depiction of the Markowitz efficient set of portfolios representing the boundary of the set of feasible portfolios that have the maximum return for a given level of risk. Any portfolios above the frontier cannot be achieved. Any below the frontier are dominated by Markowitz efficient portfolios.

Markowitz efficient portfolio Also called a mean-variance efficient portfolio, a portfolio that has the highest expected return at a given level of risk.

Markowitz efficient set of portfolios The collection of all efficient portfolios, graphically referred to as the Markowitz efficient frontier.

Master limited partnership (MLP) A publicly traded limited partnership.

Matador market The foreign market in Spain.

Match fund A bank is said to match fund a loan or other asset when it does so by buying (taking) a deposit of the same maturity. The term is commonly used in the Euromarket.

Matched book A bank runs a matched book when the distribution of maturities of its assets and liabilities are equal.

Matching concept The accounting principle that requires the recognition of all costs that are associated with the generation of the revenue reported in the income statement.

Materials requirement planning Computer-based systems that plan backward from the production schedule to make purchases in order to manage inventory levels.

Mathematical programming An operations research technique that solves problems in which an optimal value is sought subject to specified constraints. Mathematical programming models include linear programming, quadratic programming, and dynamic programming.

Mature To cease to exist; to expire.

Maturity For a bond, the date on which the principal is required to be repaid. In an interest rate swap, the date that the swap stops accruing interest.

Maturity factoring Factoring arrangement that provides collection and insurance of accounts receivable.

Maturity phase A phase of company development in which earnings continue to grow at the rate of the general economy. **Related:** Three-phase DDM.

Maturity spread The spread between any two maturity sectors of the bond market.

Maturity value Related: par value.

Maximum price fluctuation The maximum amount the contract price can change, up or down, during one trading session, as fixed by exchange rules in the contract specification. **Related:** limit price.

MBS Depository A book-entry depository for GNMA securities. The depository was initially operated by MBSCC and is currently in the process of becoming a separately incorporated, participant-owned, limited-purpose trust company organized under the State of New York Banking Law.

MBS servicing The requirement that the mortgage servicer maintain payment of the full amount of contractually due principal and interest payments whether or not actually collected.

Mean The expected value of a random variable.

Mean of the sample The arithmetic average; that is, the sum of the observations divided by the number of observations.

Mean-variance analysis Evaluation of risky prospects based on the expected value and variance of possible outcomes.

Mean-variance criterion The selection of portfolios based on the means and variances of their returns. The choice of the higher expected return portfolio for a given level of variance or the lower variance portfolio for a given expected return.

Mean-variance efficient portfolio Related: Markowitz efficient portfolio

Measurement error Errors in measuring an explanatory variable in a regression that leads to biases in estimated parameters.

Medium-term note A corporate debt instrument that is continuously offered to investors over a period of time by an agent of the issuer. Investors can select from the following maturity bands: 9 months to 1 year, more than 1 year to 18 months, more than 18 months to 2 years, etc., up to 30 years.

Membership or a seat on the exchange A limited number of exchange positions that enable the holder to trade for the holder's own accounts and charge clients for the execution of trades for their accounts.

Merchandise All movable goods such as cars, textiles, appliances, etc. and 'f.o.b.' means free on board.

Merchant bank A British term for a bank that specializes not in lending out its own funds, but in providing various financial services such as accepting bills arising out of trade, underwriting new issues, and providing advice on acquisitions, mergers, foreign exchange, portfolio management, etc.

Merger (1) Acquisition in which all assets and liabilities are absorbed by the buyer. (2) More generally, any combination of two companies.

Mimic An imitation that sends a false signal.

Minimum price fluctuation Smallest increment of price movement possible in trading a given contract. Also called point or tick. The zero-beta portfolio with the least risk.

Minimum purchases For mutual funds, the amount required to open a new account (Minimum Initial Purchase) or to deposit into an existing account (Minimum Additional Purchase). These minimums may be lowered for buyers participating in an automatic purchase plan

Minimum-variance frontier Graph of the lowest possible portfolio variance that is attainable for a given portfolio expected return.

Minimum-variance portfolio The portfolio of risky assets with lowest variance.

Minority interest An outside ownership interest in a subsidiary that is consolidated with the parent for financial reporting purposes.

Mismatch bond Floating rate note whose interest rate is reset at more frequent intervals than the rollover period (e.g. a note whose payments are set quarterly on the basis of the one-year interest rate).

Modeling The process of creating a depiction of reality, such as a graph, picture, or mathematical representation.

Modern portfolio theory Principles underlying the analysis and evaluation of rational portfolio choices based on risk-return trade-offs and efficient diversification.

Modified duration The ratio of Macaulay duration to (1 + y), where y = the bond yield. Modified duration is inversely related to the approximate percentage change in price for a given change in yield.

Modified pass-throughs Agency pass-throughs that guarantee (1) timely interest payments and (2) principal payments as collected, but no later than a specified time after they are due. **Related:** fully modified pass-throughs

Modigliani and Miller Proposition I A proposition by Modigliani and Miller which states that a firm cannot change the total value of its outstanding securities by changing its capital structure proportions. Also called the irrelevance proposition.

Modigliani and Miller Proposition II A proposition by Modigliani and Miller which states that the cost of equity is a linear function of the firm's debt_equity_ratio.

Monetary gold Gold held by governmental authorities as a financial asset.

Monetary policy Actions taken by the Board of Governors of the Federal Reserve System to influence the money supply or interest rates.

Monetary / non-monetary method Under this translation method, monetary items (e.g. cash, accounts payable and receivable, and long-term debt) are translated at the current rate while non-monetary items (e.g. inventory, fixed assets, and long-term investments) are translated at historical rates.

Money base Composed of currency and coins outside the banking system plus liabilities to the deposit money banks.

Money center banks Banks that raise most of their funds from the domestic and international money markets , relying less on depositors for funds.

Money management Related: Investment management.

Money manager Related: Investment manager.

Money market Money markets are for borrowing and lending money for three years or less. The securities in a money market can be U.S.government bonds, treasury bills and commercial paper from banks and companies.

Money market demand account An account that pays interest based on short-term interest rates.

Money market fund A mutual fund that invests only in short term securities, such as bankers' acceptances, commercial paper, repurchase agreements and government bills. The net asset value per share is maintained at $1. 00. Such funds are not federally insured, although the portfolio may consist of guaranteed securities and/or the fund may have private insurance protection.

Money market hedge The use of borrowing and lending transactions in foreign currencies to lock in the home currency value of a foreign currency transaction.

Money market notes Publicly traded issues that may be collateralized by mortgages and MBSs.

Money purchase plan A defined benefit contribution plan in which the participant contributes some part and the firm contributes at the same or a different rate. Also called and individual account plan.

Money rate of return Annual money return as a percentage of asset value.

Money supply M1-A: Currency plus demand deposits

M1-B: M1-A plus other checkable deposits.

M2: M1-B plus overnight repos, money market funds, savings, and small (less than $100M) time deposits.

M3: M-2 plus large time deposits and term repos.

L: M-3 plus other liquid assets.

Monitor To seek information about an agent's behavior; a device that provides such information.

Monte Carlo simulation An analytical technique for solving a problem by performing a large number of trail runs, called simulations, and inferring a solution from the collective results of the trial runs. Method for calculating the probability distribution of possible outcomes.

Monthly income preferred security (MIP) Preferred stock issued by a subsidiary located in a tax haven. The subsidiary relends the money to the parent.

Moral hazard The risk that the existence of a contract will change the behavior of one or both parties to the contract, e.g. an insured firm will take fewer fire precautions.

Mortality tables Tables of probability that individuals of various ages will die within one year.

Mortgage A loan secured by the collateral of some specified real estate property which obliges the borrower to make a predetermined series of payments.

Mortgage bond A bond in which the issuer has granted the bondholders a lien against the pledged assets. Collateral trust bonds

Mortgage duration A modification of standard duration to account for the impact on duration of MBSs of changes in prepayment speed resulting from changes in interest rates. Two factors are employed: one that reflects the impact of changes in prepayment speed or price.

Mortgage pass-through security Also called a passthrough, a security created when one or more mortgage holders form a collection (pool) of mortgages sells shares or participation certificates in the pool. The cash flow from the collateral pool is "passed through" to the security holder as monthly payments of principal, interest, and prepayments. This is the predominant type of MBS traded in the secondary market.

Mortgage pipeline The period from the taking of applications from prospective mortgage borrowers to the marketing of the loans.

Mortgage-pipeline risk The risk associated with taking applications from prospective mortgage borrowers who may opt to decline to accept a quoted mortgage rate within a certain grace period.

Mortgage rate The interest rate on a mortgage loan.

Mortgage-Backed Securities Clearing Corporation A wholly owned subsidiary of the Midwest Stock Exchange that operates a clearing service for the comparison, netting, and margining of agency-guaranteed MBSs transacted for forward delivery.

Mortgage-backed securities Securities backed by a pool of mortgage loans.

Mortgagee The lender of a loan secured by property.

Mortgager The borrower of a loan secured by property.

Most distant futures contract When several futures contracts are considered, the contract settling last. **Related:** nearby futures contract

Moving average Used in charts and technical analysis, the average of security or commodity prices constructed in a period as short as a few days or as Long as several years and showing trends for the latest interval. As each new variable is included in calculating the average, the last variable of the series is deleted.

Multicurrency clause Such a clause on a Euro loan permits the borrower to switch from one currency to another currency on a rollover date.

Multicurrency loans Give the borrower the possibility of drawing a loan in different currencies.

Multifactor CAPM A version of the capital asset pricing model derived by Merton that includes extra-market sources of risk referred to as factor.

Multinational corporation A firm that operates in more than one country.

Multifamily loans Loans usually represented by conventional mortgages on multi-family rental apartments.

Multiperiod immunization A portfolio strategy in which a portfolio is created that will be capable of satisfying more than one predetermined future liability regardless if interest rates change.

Multiple rates of return More than one rate of return from the same project that make the net present value of the project equal to zero. This situation arises when the IRR method is used for a project in which negative cash flows follow positive cash flows. For each sign change in the cash flows, there is a rate of return.

Multiple regression The estimated relationship between a dependent variable and more than one explanatory variable.

Multiples Another name for price/earnings ratios.

Multiple-discriminant analysis (MDA) Statistical technique for distinguishing between two groups on the basis of their observed characteristics.

Multiple-issuer pools Under the GNMA-II program, pools formed through the aggregation of individual issuers' loan packages.

Multirule system A technical trading strategy that combines mechanical rules, such as the CRISMA (cumulative volume, relative strength, moving average) Trading System of Pruitt and White.

Multi-option financing facility A syndicated confirmed credit line with attached options.

Municipal bond State or local governments offer muni bonds or municipals, as they are called, to pay for special projects such as highways or sewers. The interest that investors receive is exempt from some income taxes.

Municipal notes Short-term notes issued by municipalities in anticipation of tax receipts, proceeds from a bond issue, or other revenues.

Mutual fund Mutual funds are pools of money that are managed by an investment company. They offer investors a variety of goals, depending on the fund and its investment charter. Some funds, for example, seek to generate income on a regular basis. Others seek to preserve an investor's money. Still others seek to invest in companies that are growing at a rapid pace. Funds can impose a sales charge, or load, on investors when they buy or sell shares. Many funds these days are no load and impose no sales charge. Mutual funds are investment companies regulated by the Investment Company Act of 1940. **Related:** open-end fund, closed-end fund.

Mutual fund theorem A result associated with the CAPM, asserting that investors will choose to invest their entire risky portfolio in a market-index or mutual fund.

Mutual offset A system, such as the arrangement between the CME and SIMEX, which allows trading positions established on one exchange to be offset or transferred on another exchange.

Mutually exclusive investment decisions Investment decisions in which the acceptance of a project precludes the acceptance of one or more alternative projects.

Naive diversification A strategy whereby an investor simply invests in a number of different assets and hopes that the variance of the expected return on the portfolio is lowered. **Related:** Markowitz diversification.

Naked option strategies An unhedged strategy making exclusive use of one of the following: Long call strategy (buying call options), short call strategy (selling or writing call options), Long put strategy (buying put options), and short put strategy (selling or writing put options). By themselves, these positions are called naked strategies because they do not involve an offsetting or risk-reducing position in another option or the underlying security. **Related:** covered option strategies.

NASDAQ National Association of Securities Dealers Automatic Quotation System. An electronic quotation system that provides price quotations to market participants about the more actively traded common stock issues in the OTC market. About 4,000 common stock issues are included in the NASDAQ system.

National Futures Association (NFA) The futures industry self regulatory organization established in 1982.

National market Related: internal market

Nationalization A government takeover of a private company.

Natural logarithm Logarithm to the base *e* (approximately 2.7183).

Nearby The nearest active trading month of a financial or commodity futures market. **Related:** deferred futures

Nearby futures contract When several futures contracts are considered, the contract with the closest settlement date is called the nearby futures contract. The next futures contract is the one that settles just after the nearby futures contract. The contract farthest away in time from settlement is called the most distant futures contract.

Negative amortization A loan repayment schedule in which the outstanding principal balance of the loan increases, rather than amortizing, because the scheduled monthly payments do not cover the full amount required to amortize the loan. The unpaid interest is added to the outstanding principal, to be repaid later.

Negative carry Related: net financing cost

Negative convexity A bond characteristic such that the price appreciation will be less than the price depreciation for a large change in yield of a given number of basis points.

Negative covenant A bond covenant that limits or prohibits altogether certain actions unless the bondholders agree.

Negative duration A situation in which the price of the MBS moves in the same direction as interest rates.

Negative pledge clause A bond covenant that requires the borrower to grant lenders a lien equivalent to any liens that may be granted in the future to any other currently unsecured lenders.

Neglected firm effect The tendency of firms that are neglected by security analysts to outperform firms that are the subject of considerable attention.

Negotiated certificate of deposit A large-denomination CD, generally $1MM or more, that can be sold but cannot be cashed in before maturity.

Negotiated markets Markets in which each transaction is separately negotiated between buyer and seller (i.e. an investor and a dealer).

Negotiated offering An offering of securities for which the terms, including underwriters' compensation, have been negotiated between the issuer and the underwriters.

Negotiated sale Situation in which the terms of an offering are determined by negotiation between the issuer and the underwriter rather than through competitive bidding by underwriting groups.

Negotiable order of withdrawal (NOW) Demand deposits that pay interest.

Net adjusted present value The adjusted present value minus the initial cost of an investment.

Net advantage of refunding The net present value of the savings from a refunding.

Net advantage to leasing The net present value of entering into a lease financing arrangement rather than borrowing the necessary funds and buying the asset.

Net advantage to merging The difference in total post- and pre-merger market value minus the cost of the merger.

Net asset value (NAV) The value of a fund's investments. For a mutual fund, the net asset value per share usually represents the fund's market price, subject to a possible sales or redemption charge. For a closed end fund, the market price may vary significantly from the net asset value.

Net assets The difference between total assets on the one hand and current liabilities and noncapitalized long-term liabilities on the other hand.

Net benefit to leverage factor A linear approximation of a factor, *T**, that enables one to operationalize the total impact of leverage on firm value in the capital market imperfections view of capital structure.

Net book value The current book value of an asset or liability; that is, its original book value net of any accounting adjustments such as depreciation.

Net cash balance Beginning cash balance plus cash receipts minus cash disbursements.

Net change This is the difference between a day's last trade and the previous day's last trade.

Net errors and omissions In balance of payments accounting, net errors and omissions record the statistical discrepancies that arise in gathering balance of payments data.

Net financing cost Also called the cost of carry or, simply, carry, the difference between the cost of financing the purchase of an asset and the asset's cash yield. Positive carry means that the yield earned is greater than the financing cost; negative carry means that the financing cost exceeds the yield earned.

Net float Sum of disbursement float and collection float.

Net income The company's total earnings, reflecting revenues adjusted for costs of doing business, depreciation, interest, taxes and other expenses.

Net investment Gross, or total, investment minus depreciation.

Net lease A lease arrangement under which the lessee is responsible for all property taxes, maintenance expenses, insurance, and other costs associated with keeping the asset in good working condition.

Net operating losses Losses that a firm can take advantage of to reduce taxes.

Net operating margin The ratio of net operating income to net sales.

Net period The period of time between the end of the discount period and the date payment is due.

Net present value (NPV) The present value of the expected future cash flows minus the cost.

Net present value of growth opportunities A model valuing a firm in which net present value of new investment opportunities is explicitly examined.

Net present value of future investments The present value of the total sum of NPVs expected to result from all of the firm's future investments.

Net present value rule An investment is worth making if it has a positive NPV. Projects with negative NPVs should be rejected.

Net profit margin Net income divided by sales; the amount of each sales dollar left over after all expenses have been paid.

Net salvage value The after-tax net cash flow for terminating the project.

Net working capital Current assets minus current liabilities. Often simply referred to as working capital.

Net worth Common stockholders' equity which consists of common stock, surplus, and retained earnings.

Netting Reducing transfers of funds between subsidiaries or separate companies to a net amount.

Netting out To get or bring in as a net; to clear as profit.

Neutral period In the Euromarket, a period over which Eurodollars are sold is said to be neutral if it does not start or end on either a Friday or the day before a holiday.

New York Stock Exchange (NYSE) Also known as the Big Board or The Exhange. More than 2,00 common and preferred stocks are traded. The exchange is the older in the United States, founded in 1792, and the largest. It is lcoated on Wall Street in New York City

New-issues market The market in which a new issue of securities is first sold to investors.

New money In a Treasury auction, the amount by which the par value of the securities offered exceeds that of those maturing.

Next futures contract The contract settling immediately after the nearby futures contract.

Nexus (of contracts) A set or collection of something.

NM Abbreviation for Not Meaningful.

No load mutual fund An open-end investment company, shares of which are sold without a sales charge. There can be other distribution charges, however, such as Article 12B-1 fees. A true "no load" fund will have neither a sales charge nor a distribution fee.

Noise Price and volume fluctuations that can confuse interpretation of market direction.

No-load fund A mutual fund that does not impose a sales commission. **Related:** load fund

Nominal In name only. Differences in compounding cause the nominal rate to differ from the effective interest rate. Inflation causes the purchasing power of money to differ from one time to another.

Nominal annual rate An effective rate per period multiplied by the number of periods in a year.

Nominal cash flow A cash flow expressed in nominal terms if the actual dollars to be received or paid out are given.

Nominal exchange rate The actual foreign exchange quotation in contrast to the real exchange rate that has been adjusted for changes in purchasing power.

Nominal interest rate The interest rate unadjusted for inflation.

Nominal price Price quotations on futures for a period in which no actual trading took place.

Non-cumulative preferred stock Preferred stock whose holders must forgo dividend payments when the company misses a dividend payment. **Related:** Cumulative preferred stock

Non-financial services Include such things as freight, insurance, passenger services, and travel.

Non-insured plans Defined benefit pension plans that are not guaranteed by life insurance products. **Related:** insured plans

Non-parallel shift in the yield curve A shift in the yield curve in which yields do not change by the same number of basis points for every maturity. **Related:** Parallel shift in the yield curve.

Non-reproducible assets A tangible asset with unique physical properties, like a parcel of land, a mine, or a work of art.

Non-tradables Refer to goods and services produced and consumed domestically that are not close substitutes to import or export goods and services.

Noncash charge A cost, such as depreciation, depletion, and amortization, that does not involve any cash outflow.

Noncompetitive bid In a Treasury auction, bidding for a specific amount of securities at the price, whatever it may turn out to be, equal to the average price of the accepted competitive bids.

Nondiversifiability of human capital The difficulty of diversifying one's human capital (the unique capabilities and expertise of individuals) and employment effort.

Nondiversifiable risk Risk that cannot be eliminated by diversification.

Nonmarketed claims Claims that cannot be easily bought and sold in the financial markets, such as those of the government and litigants in lawsuits.

Nonrecourse Without recourse, as in a non-recourse lease.

Nonredeemable Not permitted, under the terms of indenture, to be redeemed.

Nonrefundable Not permitted, under the terms of indenture, to be refundable.

Nonsystematic risk Nonmarket or firm-specific risk factors that can be eliminated by diversification. Also called unique risk or diversifiable risk. Systematic risk refers to risk factors common to the entire economy.

Normal annuity form The manner in which retirement benefits are paid out.

Normal backwardation theory Holds that the futures price will be bid down to a level below the expected spot price.

Normal deviate Related: standardized value

Normal probability distribution A probability distribution for a continuous random variable that is forms a symmetrical bell-shaped curve around the mean.

Normal portfolio A customized benchmark that includes all the securities from which a manager normally chooses, weighted as the manager would weight them in a portfolio.

Normal random variable A random variable that has a normal probability distribution.

Normalizing method The practice of making a charge in the income account equivalent to the tax savings realized through the use of different depreciation methods for shareholder and income tax purposes, thus washing out the benefits of the tax savings reported as final net income to shareholders.

Note Debt instruments with initial maturities greater than one year and less than 10 years.

Note agreement A contract for privately placed debt.

Note issuance facility (NIF) An agreement by which a syndicate of banks indicates a willingness to accept short-term notes from borrowers and resell these notes in the Eurocurrency markets.

Notes to the financial statements A detailed set of notes immediately following the financial statements in an annual report that explain and expand on the information in the financial statements.

Notice day A day on which notices of intent to deliver pertaining to a specified delivery month may be issued. **Related:** delivery notice.

Notification date The day the option is either exercised or expires.

Notional principal amount In an interest rate swap, the predetermined dollar principal on which the exchanged interest payments are based.

Novation Defeasance whereby the firm's debt is canceled.

NPV See: Net present value.

NPV profile A graph of NPV as a function of the discount rate.

Objective (mutual funds) The fund's investment strategy category as stated in the prospectus. There are more than 20 standardized categories.

Odd lot A trading order for less than 100 shares of stock. Compare round lot.

Odd lot dealer A broker who combines odd lots of securities from multiple buy or sell orders into round lots and executes transactions in those round lots.

Off-balance-sheet financing Financing that is not shown as a liability in a company's balance sheet.

Offer Indicates a willingness to sell at a given price. **Related:** bid

Offer price See: offer.

Offering memorandum A document that outlines the terms of securities to be offered in a private placement.

Official reserves Holdings of gold and foreign currencies by official monetary institutions.

Official statement A statement published by an issuer of a new municipal security describing itself and the issue

Official unrequited transfers Include a variety of subsidies, military aid, voluntary cancellation of debt, contributions to international organizations, indemnities imposed under peace treaties, technical assistance, taxes, fines, etc.

Offset Elimination of a long or short position by making an opposite transaction. **Related:** liquidation.

Offshore finance subsidiary A wholly owned affiliate incorporated overseas, usually in a tax haven country, whose function is to issue securities abroad for use in either the parent's domestic or its foreign business.

Old-line factoring Factoring arrangement that provides collection, insurance, and finance for accounts receivable.

Omnibus account An account carried by one futures commission merchant with another futures commission merchant in which the transactions of two or more persons are combined and carried in the name of the originating broker, rather than designated separately. **Related:** commission house.

On the run The most recently issued (and, therefore, typically the most liquid) government bond in a particular maturity range.

One man picture The picture quoted by a broker is said to be a one-man picture if both the bid and offered prices come from the same source.

One-factor APT A special case of the arbitrage pricing theory that is derived from the one-factor model by using diversification and arbitrage. It shows the expected return on any risky asset is a linear function of a single factor.

One-way market (1) A market in which only one side, the bid or asked, is quoted or firm. (2) A market that is moving strongly in one direction.

OPEC (Organization of Petroleum Exporting Countries) A cartel of oil-producing countries.

Open account Arrangement whereby sales are made with no formal debt contract. The buyer signs a receipt, and the seller records the sale in the sales ledger.

Open book See: unmatched book.

Open contracts Contracts which have been bought or sold without the transaction having been completed by subsequent sale or purchase, or by making or taking actual delivery of the financial instrument or physical commodity.

Open interest The total number of derivative contracts traded that not yet been liquidated either by an offsetting derivative transaction or by delivery. **Related:** liquidation

Open (good-til-cancelled) order An individual investor can place an order to buy or sell a security. That open order stays active until it is completed or the investor cancels it.

Open position A net long or short position whose value will change with a change in prices.

Open repo A repo with no definite term. The agreement is made on a day-to-day basis and either the borrower or the lender may choose to terminate. The rate paid is higher than on overnight repo and is subject to adjustment if rates move.

Open-end fund Also called a mutual fund, an investment company that stands ready to sell new shares to the public and to redeem its outstanding shares on demand at a price equal to an appropriate share of the value of its portfolio, which is computed daily at the close of the market.

Open-end mortgage Mortgage against which additional debts may be issued. **Related:** closed-end mortgage.

Open-market operation Purchase or sale of government securities by the monetary authorities to increase or decrease the domestic money supply.

Open-market purchase operation A systematic program of repurchasing shares of stock in market transactions at current market prices, in competition with other prospective investors.

Open-outcry The method of trading used at futures exchanges, typically involving calling out the specific details of a buy or sell order, so that the information is available to all traders.

Opening, the The period at the beginning of the trading session officially designated by the exchange during which all transactions are considered made "at the opening". **Related:** Close, the

Opening price The range of prices at which the first bids and offers were made or first transactions were completed.

Opening purchase A transaction in which the purchaser's intention is to create or increase a long position in a given series of options.

Opening sale A transaction in which the seller's intention is to create or increase a short position in a given series of options.

Operating cash flow Earnings before depreciation minus taxes. It measures the cash generated from operations, not counting capital spending or working capital requirements.

Operating cycle The average time intervening between the acquisition of materials or services and the final cash realization from those acquisitions.

Operating exposure Degree to which exchange rate changes, in combination with price changes, will alter a company's future operating cash flows.

Operating profit margin The ratio of operating margin to net sales.

Operating lease Short-term, cancelable lease. A type of lease in which the period of contract is less than the life of the equipment and the lessor pays all maintenance and servicing costs.

Operating leverage Fixed operating costs, so-called because they accentuate variations in profits.

Operating risk The inherent or fundamental risk of a firm, without regard to financial risk. The risk that is created by operating leverage. Also called business risk.

Operationally efficient market Also called an internally efficient market, one in which investors can obtain transactions services that reflect the true costs associated with furnishing those services.

Opinion shopping A practice prohibited by the SEC which involves attempts by a corporation to obtain reporting objectives by following questionable accounting principles with the help of a pliable auditor willing to go along with the desired treatment.

Opportunity cost of capital Expected return that is foregone by investing in a project rather than in comparable financial securities.

Opportunity costs The difference in the performance of an actual investment and a desired investment adjusted for fixed costs and execution costs. The performance differential is a consequence of not being able to implement all desired trades. Most valuable alternative that is given up.

Opportunity set The possible expected return and standard deviation pairs of all portfolios that can be constructed from a given set of assets.

Optimal contract The contract that balances the three types of agency costs (contracting, monitoring, and misbehavior) against one another to minimize the total cost.

Optimal portfolio An efficient portfolio most preferred by an investor because its risk/reward characteristics approximate the investor's utility function. A portfolio that maximizes an investor's preferences with respect to return and risk.

Optimal redemption provision Provision of a bond indenture that governs the issuer's ability to call the bonds for redemption prior to their scheduled maturity date.

Optimization approach to indexing An approach to indexing which seeks to Optimize some objective, such as to maximize the portfolio yield, to maximize convexity, or to maximize expected total returns.

Option Gives the buyer the right, but not the obligation, to buy or sell an asset at a set price on or before a given date. Investors, not companies, issue options. Investors who purchase call options bet the stock will be worth more than the price set by the option (the strike price), plus the price they paid for the option itself. Buyers of put options bet the stock's price will go down below the price set by the option. An option is part of a class of securities called derivatives, so named because these securities derive their value from the worth of an underlying investment.

Option elasticity The percentage increase in an option's value given a 1% change in the value of the underlying security.

Option not to deliver In the mortgage pipeline, an additional hedge placed in tandem with the forward or substitute sale.

Option premium The option price.

Option price Also called the option premium, the price paid by the buyer of the options contract for the right to buy or sell a security at a specified price in the future.

Option seller Also called the option writer , the party who grants a right to trade a security at a given price in the future.

Option writer Option seller.

Option-adjusted spread (OAS) (1) The spread over an issuer's spot rate curve, developed as a measure of the yield spread that can be used to convert dollar differences between theoretical value and market price. (2) The cost of the implied call embedded in a MBS, defined as additional basis-yield spread. When added to the base yield spread of an MBS without an operative call produces the option-adjusted spread.

Options contract A contract that, in exchange for the option price, gives the option buyer the right, but not the obligation, to buy (or sell) a financial asset at the exercise price from (or to) the option seller within a specified time period, or on a specified date (expiration date).

Options contract multiple A constant, set at $100, which when multiplied by the cash index value gives the dollar value of the stock index underlying an option. That is, dollar value of the underlying stock index = cash index value x $100 (the options contract multiple).

Options on physicals Interest rate options written on fixed-income securities, as opposed to those written on interest rate futures contracts.

Organized exchange A securities marketplace wherein purchasers and sellers regularly gather to trade securities according to the formal rules adopted by the exchange.

Original face value The principal amount of the mortgage as of its issue date.

Original issue discount debt (OID debt) Debt that is initially offered at a price below par.

Original margin The margin needed to cover a specific new position. **Related:** Margin, security deposit (initial)

Original maturity Maturity at issue. For example, a five year note has an original maturity of 5 years; one year later it has a maturity of 4 years.

Origination The making of mortgage loans.

OTC See: over-the-counter.

Other capital In the balance of payments, other capital is a residual category that groups all the capital transactions that have not been included in direct investment, portfolio investment, and reserves categories. It is divided into long-term capital and short-term capital and, because of its residual status, can differ from country to country. Generally speaking, other long-term capital includes most non-negotiable instruments of a year or more like bank loans and mortgages. Other short-term capital includes financial assets of less than a year such as currency, deposits, and bills.

Other current assets Value of non-cash assets, including prepaid expenses and accounts receivable, due within 1 year.

Other long term liabilities Value of leases, future employee benefits, deferred taxes and other obligations not requiring interest payments that must be paid over a period of more than 1 year.

Other sources Amount of funds generated during the period from operations by sources other than depreciation or deferred taxes. Part of Free cash flow calculation.

Out-of-the-money option A call option is out-of-the-money if the strike price is greater than the market price of the underlying security. A put option is out-of-the-money if the strike price is less than the market price of the underlying security.

Outright rate Actual forward rate expressed in dollars per currency unit, or vice versa.

Outsourcing The practice of purchasing a significant percentage of intermediate components from outside suppliers.

Outstanding share capital Issued share capital less the par value of shares that are held in the company's treasury.

Outstanding shares Shares that are currently owned by investors.

Overbought\oversold indicator An indicator that attempts to define when prices have moved too far and too fast in either direction and thus are vulnerable to reaction.

Overfunded pension plan A pension plan that has a positive surplus (i.e., assets exceed liabilities).

Overlay strategy A strategy of using futures for asset allocation by pension sponsors to avoid disrupting the activities of money managers.

Overnight delivery risk A risk brought about because differences in time zones between settlement centers require that payment or delivery on one side of a transaction be made without knowing until the next day whether the funds have been received in an account on the other side. Particularly apparent where delivery takes place in Europe for payment in dollars in New York.

Overnight repo A repurchase agreement with a term of one day.

Overperform When a security is expected to appreciate at a rate faster than the overall market.

Overreaction hypothesis The supposition that investors overreact to unanticipated news, resulting in exaggerated movement in stock prices followed by corrections.

Overshooting The tendency of a pool of MBSs to reflect an especially high rate or prepayments the first time it crosses the threshold for refinancing, especially if two or more years have passed since the date of issue without the WAC of the pool having crossed the refinancing threshold.

Oversubscribed issue Investors are not able to buy all of the shares or bonds they want, so underwriters must allocate the shares or bonds among investors. This occurs when a new issue is underpriced or in great demand because of growth prospects.

Oversubscription privilege In a rights issue, arrangement by which shareholders are given the right to apply for any shares that are not taken up.

Over-the-counter market (OTC) A decentralized market (as opposed to an exchange market) where geographically dispersed dealers are linked together by telephones and computer screens. The market is for securities not listed on a stock or bond exchange. The NASDAQ market is an OTC market for U.S. stocks.

P&L Profit and loss statement for a trader.

P&S Purchase and sale statement. A statement provided by the broker showing change in the customer's net ledger balance after the offset of a previously established position(s).

P/E See Price/Earnings ratio.

P/E ratio Assume XYZ Co. sells for $25.50 per share and has earned $2.55 per share this year; $25. 50 = 10 times $2. 55

XYZ stock sells for 10 times earnings. P/E = Current stock price divided by trailing annual earnings per share *or* expected annual earnings per share.

P/E effect That portfolios with low P/E stocks have exhibited higher average risk-adjusted returns than high P/E stocks.

PSA A prepayment model based on an assumed rate of prepayment each month of the then unpaid principal balance of a pool of mortgages. PSA is used primarily to derive an implied prepayment speed of new production loans, a 100% PSA assumes a prepayment rate of 2% per month in the first month following the date of issue, increasing at 2% per month thereafter until the 30th month. Thereafter, 100% PSA is the same as 6% CPR.

Pac-Man strategy Takeover defense strategy in which the prospective acquiree retaliates against the acquirer's tender offer by launching its own tender offer for the other firm.

Pairoff A buy-back to offset and effectively liquidate a prior sale of securities.

Paper Money market instruments, commercial paper and other.

Paper gain (loss) Unrealized capital gain (loss) on securities held in portfolio, based on a comparison of current market price to original cost.

Par value Also called the maturity value or face value, the amount that the issuer agrees to pay at the maturity date.

Parallel loan A process whereby two companies in different countries borrow each other's currency for a specific period of time, and repay the other's currency at an agreed maturity for the purpose of reducing foreign exchange risk. Also referred to as back-to-back loans.

Parallel shift in the yield curve A shift in the yield curve in which the change in the yield on all maturities is the same number of basis points. In other words, if the 3 month T-bill increases 100 basis points (one percent), then the 6 month, 1 year, 5 year, 10 year, 20 year, and 30 year rates increase by 100 basis points as well. **Related:** Non-parallel shift in the yield curve.

Parameter A representation that characterizes a part of a model (e.g. a growth rate), the value of which is determined outside of the model. **See:** exogenous variable.

Parity value Related:conversion value

Participating GIC A guaranteed investment contract where the policyholder is not guaranteed a crediting rate, but instead receives a return based on the actual experience of the portfolio managed by the life company.

Participating fees The portion of total fees in a syndicated credit that go to the participating banks.

Partnership Shared ownership among two or more individuals, some of whom may, but do not necessarily, have limited liability. **See:** general partnership, limited partnership, and master limited partnership.

Passive portfolio strategy A strategy that involves minimal expectational input, and instead relies on diversification to match the performance of some market index. A passive strategy assumes that the marketplace will reflect all available information in the price paid for securities, and therefore, does not attempt to find mispriced securities. Related: active portfolio strategy

Pass-through rate The net interest rate passed through to investors after deducting servicing, management, and guarantee fees from the gross mortgage coupon.

Pass-through securities A pool of fixed-income securities backed by a package of assets (i.e. mortgages) where the holder receives the principal and interest payments. Related: mortgage pass-through security

Pass-through coupon rate The interest rate paid on a securitized pool of assets, which is less than the rate paid on the underlying loans by an amount equal to the servicing and guaranteeing fees.

Passive investment strategy See: passive management.

Passive investment management Buying a well-diversified portfolio to represent a broad-based market index without attempting to search out mispriced securities.

Passive portfolio A market index portfolio.

Path dependent option An option whose value depends on the sequence of prices of the underlying asset rather than just the final price of the asset.

Payable through drafts A method of making payment that is used to maintain control over payments made on behalf of the firm by personnel in noncentral locations. The payer's bank delivers the payable through draft to the payer, which must approve it and return it to the bank before payment can be received.

Payables

Related: Accounts payable.

Payback The length of time it takes to recover the initial cost of a project, without regard to the time value of money.

Paydown In a Treasury refunding, the amount by which the par value of the securities maturing exceeds that of those sold.

Payment date The date on which each shareholder of record will be sent a check for the declared dividend.

Payment float Company-written checks that have not yet cleared.

Payments netting Reducing fund transfers between affiliates to only a netted amount. Netting can be done on a bilateral basis (between pairs of affiliates), or on a multi-lateral basis (taking all affiliates together).

Payments pattern Describes the lagged collection pattern of receivables, for instance the probability that a 72-day-old account will still be unpaid when it is 73-days-old.

Payout ratio Generally, the proportion of earnings paid out to the common stockholders as cash dividends. More specifically, the firm's cash dividend divided by the firm's earnings in the same reporting period.

Pay-up The loss of cash resulting from a swap into higher price bonds or the need/willingness of a bank or other borrower to pay a higher rate of interest to get funds.

Payment-In-Kind (PIK) bond A bond that gives the issuer an option (during an initial period) either to make coupon payments in cash or in the form of additional bonds.

Peak The transition from the end of an economic expansion to the start of a contraction.

Pecking-order view (of capital structure) The argument that external financing transaction costs, especially those associated with the problem of adverse selection, create a dynamic environment in which firms have a preference, or pecking-order of preferred sources of financing, when all else is equal. Internally generated funds are the most preferred, new debt is next, debt-equity hybrids are next, and new equity is the least preferred source.

Pension Benefit Guaranty Corporation (PBGC) A federal agency that insures the vested benefits of pension plan participants (established in 1974 by the ERISA legislation).

Pension plan A fund that is established for the payment of retirement benefits.

Pension sponsors Organizations that have established a pension plan.

Perfect capital market A market in which there are never any arbitrage opportunities.

Perfect competition An idealized market environment in which every market participant is too small to affect the market price by acting on its own.

Perfect hedge A financial result in which the profit and loss from the underlying asset and the hedge position are equal.

Perfect market view (of capital structure) Analysis of a firm's capital structure decision, which shows the irrelevance of capital structure in a perfect capital market.

Perfect market view (of dividend policy) Analysis of a decision on dividend policy, in a perfect capital market environment, that shows the irrelevance of dividend policy in a perfect capital market.

Perfectly competitive financial markets Markets in which no trader has the power to change the price of goods or services. Perfect capital markets are characterized by the following conditions: 1) trading is costless, and access to the financial markets is free, 2) information about borrowing and lending opportunities is freely available, 3) there are many traders, and no single trader can have a significant impact on market prices.

Perfected first lien A first lien that is duly recorded with the cognizant governmental body so that the lender will be able to act on it should the borrower default.

Performance attribution analysis The decomposition of a money manager's performance results to explain the reasons why those results were achieved. This analysis seeks to answer the following questions: (1) What were the major sources of added value? (2) Was short-term factor timing statistically significant? (3) Was market timing statistically significant? And (4), Was security selection statistically significant?

Performance evaluation The evaluation of a manager's performance which involves, first, determining whether the money manager added value by outperforming the established benchmark (performance measurement) and, second, determining how the money manager achieved the calculated return (performance attribution analysis).

Performance measurement The calculation of the return realized by a money manager over some time interval.

Performance shares Shares of stock given to managers on the basis of performance as measured by earnings per share and similar criteria. A control device used by shareholders to tie management to the self-interest of shareholders.

Perpetual warrants Warrants that have no expiration date.

Perpetuity A constant stream of identical cash flows without end, such as a British consol.

Perquisites Personal benefits, including direct benefits, such as the use of a firm car or expense account for personal business, and indirect benefits, such as up-to-date office décor.

Personal tax view (of capital structure) The argument that the difference in personal tax rates between income from debt and income from equity eliminates the disadvantage from the double taxation (corporate and personal) of income from equity.

Personal trust An interest in an asset held by a trustee for the benefit of another person.

Philadelphia Stock Exchange (PHLX) A securities exchange where American and European foreign currency options on spot exchange rates are traded.

Phone switching In mutual funds, the ability to transfer shares between funds in the same family by telephone request. There may be a charge associated with these transfers. Phone switching is also possible among different fund families if the funds are held in street name by a participating broker/dealer.

PIBOR (Paris Interbank Offer Rate) The deposit rate on interbank transactions in the Eurocurrency market quoted in Paris.

Pickup The gain in yield that occurs when a block of bonds is swapped for another block of higher-coupon bonds.

Picture The bid and asked prices quoted by a broker for a given security.

Pie model of capital structure A model of the debt/equity ratio of the firms, graphically depicted in slices of a pie that represent the value of the firm in the capital markets.

Pit A specific area of the trading floor that is designed for the trading of commodities, individual futures, or option contracts.

Pit committee A committee of the exchange that determines the daily settlement price of futures contracts.

Pivot Price level established as being significant by market's failure to penetrate or as being significant when a sudden increase in volume accompanies the move through the price level.

Placement A bank depositing Eurodollars with (selling Eurodollars to) another bank is often said to be making a placement.

Plain vanilla A term that refers to a relatively simple derivative financial instrument, usually a swap or other derivative that is issued with standard features.

Plan for reorganizationA plan for reorganizing a firm during the Chapter 11 bankruptcy process.

Plan sponsors The entities that establish pension plans, including private business entities acting for their employees; state and local entities operating on behalf of their employees; unions acting on behalf of their members; and individuals representing themselves.

Planned amortization class CMO (1) One class of CMO that carries the most stable cash flows and the lowest prepayement risk of any class of CMO. Because of that stable cash flow, it is considered the least risky CMO. (2) A CMO bond class that stipulates cash-flow contributions to a sinking fund. With the PAC, principal payments are directed to the sinking fund on a priority basis in accordance with a predetermined payment schedule, with prior claim to the cash flows before other CMO classes. Similarly, cash flows received by the trust in excess of the sinking fund requirement are also allocated to other bond classes. The prepayment experience of the PAC is therefore very stable over a wide range of prepayment experience.

Planned capital expenditure program Capital expenditure program as outlined in the corporate financial plan.

Planned financing program Program of short-term and long-term financing as outlined in the corporate financial plan.

Planning horizon The length of time a model projects into the future.

Plowback rate Related: retention rate.

Plug A variable that handles financial slack in the financial plan.

Plus Dealers in government bonds normally give price quotes in 32nds. To quote a bid or offer in 64ths, they use pluses; a dealer who bids 4+ is bidding the handle plus 4/32 + 1/64, which equals the handle plus 9/64.

Point The smallest unit of price change quoted or, one one-hundredth of a percent. Related: minimum price fluctuation and tick.

Point and figure chart A price-only chart that takes into account only whole integer changes in price, i.e., a 2-point change. Point and figure charting disregards the element of time and is solely used to record changes in price.

Poison pill Anit-takeover device that gives a prospective acquiree's shareholders the right to buy shares of the firm or shares of anyone who acquires the firm at a deep discount to their fair market value. Named after the cyanide pill that secret agents are instructed to swallow if capture is imminent.

Poison put A covenant allowing the bondholder to demand repayment in the event of a hostile merger.

Policy asset allocation A long-term asset allocation method, in which the investor seeks to assess an appropriate long-term "normal" asset mix that represents an ideal blend of controlled risk and enhanced return.

Political risk Possibility of the expropriation of assets, changes in tax policy, restrictions on the exchange of foreign currency, or other changes in the business climate of a country.

Pool factor The outstanding principal balance divided by the original principal balance with the result expressed as a decimal. Pool factors are published monthly by the Bond Buyer newspaper for Ginnie Mae, Fannie Mae, and Freddie Mac(Federal Home Loan Mortgage Corporation) MBSs.

Pooling of interests An accounting method for reporting acquisitions accomplished through the use of equity. The combined assets of the merged entity are consolidated using book value, as opposed to the purchase method, which uses market value. The merging entities' financial results are combined as though the two entities have always been a single entity.

Portfolio A collection of investments, real and/or financial.

Portfolio insurance A strategy using a leveraged portfolio in the underlying stock to create a synthetic put option. The strategy's goal is to ensure that the value of the portfolio does not fall below a certain level.

Portfolio internal rate of return The rate of return computed by first determining the cash flows for all the bonds in the portfolio and then finding the interest rate that will make the present value of the cash flows equal to the market value of the portfolio.

Portfolio opportunity set The expected return/standard deviation pairs of all portfolios that can be constructed from a given set of assets.

Portfolio management Related: Investment management

Portfolio manager Related: Investment manager

Portfolio separation theorem An investor's choice of a risky investment portfolio is separate from his attitude towards risk. Related:Fisher's separation theorem.

Portfolio turnover rate For an investment company, an annualized rate found by dividing the lesser of purchases and sales by the average of portfolio assets.

Portfolio variance Weighted sum of the covariance and variances of the assets in a portfolio.

Position A market commitment; the number of contracts bought or sold for which no offsetting transaction has been entered into. The buyer of a commodity is said to have a long position and the seller of a commodity is said to have a short position . **Related:** open contracts

Position diagram Diagram showing the possible payoffs from a derivative investment.

Positive carry Related:net financing cost

Positive convexity A property of option-free bonds whereby the price appreciation for a large upward change in interest rates will be greater (in absolute terms) than the price depreciation for the same downward change in interest rates.

Positive covenant (of a bond) A bond covenant that specifies certain actions the firm must take. Also called and affirmative covenant.

Positive float See:float.

Possessions corporation A type of corporation permitted under the U.S. tax code whereby a branch operation in a U.S. possessions can obtain tax benefits as though it were operating as a foreign subsidiary.

Post Particular place on the floor of an exchange where transactions in stocks listed on the exchange occur.

Post-audit A set of procedures for evaluating a capital budgeting decision after the fact.

Postponement option The option of postponing a project without eliminating the possibility of undertaking it.

Posttrade benchmarks Prices after the decision to trade.

Preauthorized checks (PACs) Checks that are authorized by the payer in advance and are written either by the payee or by the payee's bank and then deposited in the payee's bank account.

Preauthorized electronic debits (PADs) Debits to its bank account in advance by the payer. The payer's bank sends payment to the payee's bank through the _ACH)Automated Clearing House (ACH) system.

Precautionary demand (for money) The need to meet unexpected or extraordinary contingencies with a buffer stock of cash.

Precautionary motive A desire to hold cash in order to be able to deal effectively with unexpected events that require cash outlay.

Preemptive right Common stockholder's right to anything of value distributed by the company.

Preferred equity redemption stock (PERC) Preferred stock that converts automatically into equity at a stated date. A limit is placed on the value of the shares the investor receives.

Preference stock A security that ranks junior to preferred stock but senior to common stock in the right to receive payments from the firm; essentially junior preferred stock.

Preferred habitat theory A biased expectations theory that believes the term structure reflects the expectation of the future path of interest rates as well as risk premium. However, the theory rejects the assertion that the risk premium must rise uniformly with maturity. Instead, to the extent that the demand for and supply of funds does not match for a given maturity range, some participants will shift to maturities showing the opposite imbalances. As long as such investors are compensated by an appropriate risk premium whose magnitude will reflect the extent of aversion to either price or reinvestment risk.

Preferred shares Preferred shares give investors a fixed dividend from the company's earnings. And more importantly: preferred shareholders get paid before common shareholders. **See:** preferred stock.

Preferred stock A security that shows ownership in a corporation and gives the holder a claim, prior to the claim of common stockholders, on earnings and also generally on assets in the event of liquidation. Most preferred stock pays a fixed dividend that is paid prior to the common stock dividend, stated in a dollar amount or as a percentage of par value. This stock does not usually carry voting rights. The stock shares characteristics of both common stock and debt.

Preferred stock agreement A contract for preferred stock.

Preliminary prospectus A preliminary version of a prospectus.

Premium (1) Amount paid for a bond above the par value. (2) The price of an option contract; also, in futures trading, the amount the futures price exceeds the price of the spot commodity. Related: inverted market premium payback period. Also called break-even time, the time it takes to recover the premium per share of a convertible security.

Premium bond A bond that is selling for more than its par value.

Prepackaged bankruptcy A bankruptcy in which a debtor and its creditors pre-negotiate a plan or reorganization and then file it along with the bankruptcy petition.

Prepayment speed Also called speed, the estimated rate at which mortgagors pay off their loans ahead of schedule, critical in assessing the value of mortgage pass-through securities.

Prepayments Payments made in excess of scheduled mortgage principal repayments.

Prerefunded bond Refunded bond.

Present value The amount of cash today that is equivalent in value to a payment, or to a stream of payments, to be received in the future.

Present value factor Factor used to calculate an estimate of the present value of an amount to be received in a future period.

Present value of growth opportunities (NPV) Net present value of investments the firm is expected to make in the future.

Presold issue An issue that is sold out before the coupon announcement.

Pre-trade benchmarks Prices occurring before or at the decision to trade.

Price/book ratio Compares a stock's market value to the value of total assets less total liabilities (book value). Determined by dividing current stock price by common stockholder equity per share (book value), adjusted for stock splits. Also called Market-to-Book.

Price/earnings ratio Shows the "multiple" of earnings at which a stock sells. Determined by dividing current stock price by current earnings per share (adjusted for stock splits). Earnings per share for the P/E ratio is determined by dividing earnings for past 12 months by the number of common shares outstanding. Higher "multiple" means investors have higher expectations for future growth, and have bid up the stock's price.

Price/sales ratio Determined by dividing current stock price by revenue per share (adjusted for stock splits). Revenue per share for the P/S ratio is determined by dividing revenue for past 12 months by number of shares outstanding.

Price compression The limitation of the price appreciation potential for a callable bond in a declining interest rate environment, based on the expectation that the bond will be redeemed at the call price.

Price discovery process The process of determining the prices of the assets in the marketplace through the interactions of buyers and sellers.

Price elasticities The percentage change in the quantity divided by the percentage change in the price.

Price impact costs Related: market impact costs

Price momentum Related: Relative strength

Price persistence Related: Relative strength

Price risk The risk that the value of a security (or a portfolio) will decline in the future. Or, a type of mortgage-pipeline risk created in the production segment when loan terms are set for the borrower in advance of terms being set for secondary market sale. If the general level of rates rises during the production cycle, the lender may have to sell his originated loans at a discount.

Price takers Individuals who respond to rates and prices by acting as though they have no influence on them.

Priced out The market has already incorporated information, such as a low dividend, into the price of a stock.

Price value of a basis point (PVBP) Also called the dollar value of a basis point, a measure of the change in the price of the bond if the required yield changes by one basis point.

Prices Price of a share of common stock on the date shown. Highs and lows are based on the highest and lowest intraday trading price.

Price-specie-flow mechanism Adjustment mechanism under the classical gold standard whereby disturbances in the price level in one country would be wholly or partly offset by a countervailing flow of specie (gold coins) that would act to equalize prices across countries and automatically bring international payments back in balance.

Price-volume relationship A relationship espoused by some technical analysts that signals continuing rises and falls in security prices based on accompanying changes in volume traded.

Pricing efficiency Also called external efficiency, a market characteristic where prices at all times fully reflect all available information that is relevant to the valuation of securities.

Primary market The first buyer of a newly issued security buys that security in the primary market. All subsequent trading of those securities is done in the secondary market.

Primary offering A firm selling some of its own newly issued shares to investors.

Primitive security An instrument such as a stock or bond for which payments depend only on the financial status of the issuer.

Prime rate The interest rate at which banks lend to their best (prime) customers. Much more often than not, a bank's most creditworthy customers borrow at rates below the prime rate.

Principal (1) The total amount of money being borrowed or lent. (2) The party affected by agent decisions in a principal-agent relationship.

Principal of diversification Highly diversified portfolios will have negligible unsystematic risk. In other words, unsystematic risks disappear in portfolios, and only systematic risks survive.

Principal-agent relationship A situation that can be modeled as one person, an agent, who acts on the behalf of another person, the principal.

Principal amount The face amount of debt; the amount borrowed or lent. Often called principal.

Principal only (PO) A mortgage-backed security in which the holder receives only principal cash flows on the underlying mortgage pool. The principal-only portion of a stripped MBS. For PO securities, all of the principal distribution due from the underlying collateral pool is paid to the registered holder of the stripped MBS based on the current face value of the underlying collateral pool.

Private Export Funding Corporation (PEFCO) Company that mobilizes private capital for financing the export of big-ticket items by U.S. firms by purchasing at fixed interest rates the medium- to long-term debt obligations of importers of U.S. products.

Private-label pass-throughs Related: Conventional pass-throughs.

Private placement The sale of a bond or other security directly to a limited number of investors.

Private unrequited transfers Refers to resident immigrant workers' remittances to their country of origin as well as gifts, dowries, inheritances, prizes, charitable contributions, etc.

Privatization The act of returning state-owned or state-run companies back to the private sector, usually by selling them.

Pro forma capital structure analysis A method of analyzing the impact of alternative capital structure choices on a firm's credit statistics and reported financial results, especially to determine whether the firm will be able to use projected tax shield benefits fully.

Pro forma financial statements Financial statements as adjusted to reflect a projected or planned transaction.

Pro forma statement A financial statement showing the forecast or projected operating results and balance sheet, as in pro forma income statements, balance sheets, and statements of cash flows.

Probability The relative likelihood of a particular outcome among all possible outcomes.

Probability density function The probability function for a continuous random variable.

Probability distribution

Also called a probability function, a function that describes all the values that the random variable can take and the probability associated with each.

Probability function A function that assigns a probability to each and every possible outcome.

Product cycle The time it takes to bring new and/or improved products to market.

Product risk A type of mortgage-pipeline risk that occurs when a lender has an unusual loan in production or inventory but does not have a sale commitment at a prearranged price.

Production payment financing A method of nonrecourse asset-based financing in which a specified percentage of revenue realized from the sale of the project's output is used to pay debt service.

Production-flow commitment An agreement by the loan purchaser to allow the monthly loan quota to be delivered in batches.

Profit margin Indicator of profitability. The ratio of earnings available to stockholders to net sales. Determined by dividing net income by revenue for the same 12-month period. Result is shown as a percentage.

Profitability index The present value of the future cash flows divided by the initial investment. Also called the benefit-cost ratio.

Profitability ratios Ratios that focus on the profitability of the firm. Profit margins measure performance with relation to sales. Rate of return ratios measure performance relative to some measure of size of the investment.

Pro forma financial statements Financial statements as adjusted to reflect a projected or planned transaction.

Program trades Also called basket trades, orders requiring the execution of trades in a large number of different stocks at as near the same time as possible. Related: block trade

Program trading Trades based on signals from computer programs, usually entered directly from the trader's computer to the market's computer system and executed automatically.

Progress review A periodic review of a capital investment project to evaluate its continued economic viability.

Progressive tax system A tax system wherein the average tax rate increases for some increases in income but never decreases with an increase in income.

Project loan certificate (PLC) A primary program of Ginnie Mae for securitizing FHA-insured and co-insured multifamily, hospital, and nursing home loans.

Project loan securities Securities backed by a variety of FHA-insured loan types - primarily multi-family apartment buildings, hospitals, and nursing homes.

Project loans Usually FHA-insured and HUD-guaranteed mortgages on multiple-family housing complexes, nursing homes, hospitals, and other development types.

Project notes (PNs) Project notes are issued by municipalities to finance federally sponsored programs in urban renewal and housing and are guaranteed by the U.S. Department of Housing and Urban Development.

Project financing A form of asset-based financing in which a firm finances a discrete set of assets on a stand-alone basis.

Projected benefit obligation (PBO) A measure of a pension plan's liability at the calculation date assuming that the plan is ongoing and will not terminate in the foreseeable future. Related:accumulated benefit obligation.

Projected maturity date With CMOs, final payment at the end of the estimated cash flow window.

Promissory note Written promise to pay.

Property rights Rights of individuals and companies to own and utilize property as they see fit and to receive the stream of income that their property generates.

Prospectus Formal written document to sell securities that describes the plan for a proposed business enterprise, or the facts concerning an existing one, that an investor needs to make an informed decision. Prospectuses are used by mutual funds to describe the fund objectives, risks and other essential information.

Protectionism Protecting domestic industry from import competition by means of tariffs, quotas, and other trade barriers.

Protective covenant A part of the indenture or loan agreement that limits certain actions a company takes during the term of the loan to protect the lender's interests.

Protective put buying strategy A strategy that involves buying a put option on the underlying security that is held in a portfolio. Related: Hedge option strategies

Provisional call feature A feature in a convertible issue that allows the issuer to call the issue during the non-call period if the price of the stock reaches a certain level.

Proxy Document intended to provide shareholders with information necessary to vote in an informed manner on matters to be brought up at a stockholders' meeting. Includes information on closely held shares. Shareholders can and often do give management their proxy, representing the right and responsibility to vote their shares as specified in the proxy statement.

Proxy contest A battle for the control of a firm in which the dissident group seeks, from the firm's other shareholders, the right to vote those shareholder's shares in favor of the dissident group's slate of directors. Also called proxy fight.

Proxy vote Vote cast by one person on behalf of another.

Public offering The sale of registered securities by the issuer (or the underwriters acting in the interests of the issuer) in the public market. Also called public issue.

Public Securities Administration (PSA) The trade association for primary dealers in U.S. government securities, including MBSs.

Public warehouse Warehouse operated by an independent warehouse company on its own premises.

Publicly traded assets Assets that can be traded in a public market, such as the stock market.

Puke Slang for a trader selling a position, usually a losing position, as in, "When in doubt, puke it out."

Purchase To buy, to be long, to have an ownership position.

Purchase accounting Method of accounting for a merger in which the acquirer is treated as having purchased the assets and assumed liabilities of the acquiree, which are all written up or down to their respective fair market values, the difference between the purchase price and the net assets acquired being attributed to goodwill.

Purchase agreement As used in connection with project financing, an agreement to purchase a specific amount of project output per period.

Purchase and sale A method of securities distribution in which the securities firm purchases the securities from the issuer for its own account at a stated price and then resells them, as contrasted with a best-efforts sale.

Purchase fund Resembles a sinking fund except that money is used only to purchase bonds if they are selling below their par value.

Purchase method Accounting for an acquisition using market value for the consolidation of the two entities' net assets on the balance sheet. Generally, depreciation/amortization will increase for this method compared with pooling and will result in lower net income.

Purchasing power parity The notion that the ratio between domestic and foreign price levels should equal the equilibrium exchange rate between domestic and foreign currencies.

Purchasing-power risk Related: inflation risk

Pure-discount bond A bond that will make only one payment of principal and interest. Also called a zero-coupon bond or a single-payment bond.

Pure expectations theory A theory that asserts that the forward rates exclusively represent the expected future rates. In other words, the entire term structure reflects the markets expectations of future short-term rates. For example, an increasing sloping term structure implies increasing short-term interest rates. Related: biased expectations theories

Pure index fund A portfolio that is managed so as to perfectly replicate the performance of the market portfolio.

Pure yield pickup swap Moving to higher yield bonds.

Put An option granting the right to sell the underlying futures contract. Opposite of a call.

Put an option To exercise a put option.

Put bond A bond that the holder may choose either to exchange for par value at some date or to extend for a given number of years.

Put option This security gives investors the right to sell (or put) fixed number of shares at a fixed price within a given time frame. An investor, for example, might wish to have the right to sell shares of a stock at a certain price by a certain time in order to protect, or hedge, an existing investment.

Put price The price at which the asset will be sold if a put option is exercised. Also called the strike or exercise price of a put option.

Put provision Gives the holder of a floating-rate bond the right to redeem his note at par on the coupon payment date.

Put swaption A financial tool in which the buyer has the right, or option, to enter into a swap as a floating-rate payer. The writer of the swaption therefore becomes the floating-rate receiver/fixed-rate payer.

Put-call parity relationship The relationship between the price of a put and the price of a call on the same underlying security with the same expiration date, which prevents arbitrage opportunities. Holding the stock and buying a put will deliver the exact payoff as buying one call and investing the present value (PV) of the exercise price. The call value equals C=S+P-PV(k).

Pyramid scheme An illegal, fraudulent scheme in which a con artist contrives victims to invest by promising an extraordinary return but simply uses newly invested funds to pay off any investors who insist on terminating their investment.

Q ratio or Tobin's Q ratio Market value of a firm's assets divided by replacement value of the firm's assets.

Quadratic programming Variant of linear programming whereby the equations are quadratic rather than linear.

Quality option Also called the swap option, the seller's choice of deliverables in Treasury Bond and Treasury note futures contract. **Related:** cheapest to deliver issue

Quality spread Also called credit spread, the spread between Treasury securities and non-Treasury securities that are identical in all respects except for quality rating. For instance, the difference between yields on Treasuries and those on single A-rated industrial bonds.

Quanto swap See: differential swap.

Quantos Currency options with a guaranteed exchange rate that enable buyers who like the asset, German bonds for example, but not the asset's pricing currency, to arrange to be paid in a different currency for a fee.

Quick assets Current assets minus inventories.

Quick ratio Indicator of a company's financial strength (or weakness). Calculated by taking current assets less inventories, divided by current liabilities. This ratio provides information regarding the firm's liquidity and ability to meet its obligations. Also called the Acid Test ratio.

Quotation The bid and offered prices a dealer is willing to buy or sell at.

R squared (R^2) Square of the correlation coefficient proportion of the variability explained by the linear regression model. For example, an r squared of 75% means that 75% of the variability observed in the dependent variable is explained by the independent variable.

Rally (recovery) An upward movement of prices. Opposite of reaction.

RAMs (Reverse-annuity mortgages) Mortgages in which the bank makes a loan for an amount equal to a percentage of the appraisal value of the home. The loan is then paid to the homeowner in the form of an annuity.

Random variable A function that assigns a real number to each and every possible outcome of a random experiment.

Random walk Theory that stock price changes from day to day are at random; the changes are independent of each other and have the same probability distribution. Many believers of the random walk theory believe that it is impossible to outperform the market consistently without taking additional risk.

Randomized strategy A strategy of introducing into the decision-making process a random element that is designed to reduce the information content of the decision-maker's observed choices.

Range The high and low prices, or high and low bids and offers recorded during a specified time.

Range forward A forward exchange rate contract that places upper and lower bounds on the cost of foreign exchange.

Rate anticipation swaps An exchange of bonds in a portfolio for new bonds that will achieve the target portfolio duration, based on the investor's assumptions about future changes in interest rates.

Rate lock An agreement between the mortgage banker and the loan applicant guaranteeing a specified interest rate for a designated period, usually 60 days.

Rate of interest The rate, as a proportion of the principal, at which interest is computed.

Rate of return ratios Ratios that are designed to measure the profitability of the firm in relation to various measures of the funds invested in the firm.

Rate risk In banking, the risk that profits may decline or losses occur because a rise in interest rates forces up the cost of funding fixed-rate loans or other fixed-rate assets.

Ratings An evaluation of credit quality Moody's, S&P, and Fitch Investors Service give to companies used by investors and analysts.

Rational expectations The idea that people rationally anticipate the future and respond to what they see ahead.

Raw material supply agreement As used in connection with project financing, an agreement to furnish a specified amount per period of a specified raw material.

Reaction A decline in prices following an advance. Opposite of rally.

Real assets Identifiable assets, such as buildings, equipment, patents, and trademarks, as distinguished from a financial obligation.

Real capital Wealth that can be represented in financial terms, such as savings account balances, financial securities, and real estate.

Real cash flow A cash flow is expressed in real terms if the current, or date 0, purchasing power of the cash flow is given.

Real exchange rates Exchange rates that have been adjusted for the inflation differential between two countries.

Real interest rate The rate of interest excluding the effect of inflation; that is, the rate that is earned in terms of constant-purchasing-power dollars. Interest rate expressed in terms of real goods, i.e. nominal interest rate adjusted for inflation.

Real market The bid and offer prices at which a dealer could do "size." Quotes in the brokers market may reflect not the real market, but pictures painted by dealers playing trading games.

Real time A real time stock or bond quote is one that states a security's most recent offer to sell or bid (buy). A delayed quote shows the same bid and ask prices 15 minutes and sometimes 20 minutes after a trade takes place.

Realized compound yield Yield assuming that coupon payments are invested at the going market interest rate at the time of their receipt and rolled over until the bond matures.

Realized return The return that is actually earned over a given time period.

Rebalancing Realigning the proportions of assets in a portfolio as needed.

Receivables balance fractions The percentage of a month's sales that remain uncollected (and part of accounts receivable) at the end of succeeding months.

Receivables turnover ratio Total operating revenues divided by average receivables. Used to measure how effectively a firm is managing its accounts receivable.

Receiver A bankruptcy practitioner appointed by secured creditors in the United Kingdom to oversee the repayment of debts.

Reclamation A claim for the right to return or the right to demand the return of a security that has been previously accepted as a result of bad delivery or other irregularities in the delivery and settlement process.

Record date (1) Date by which a shareholder must officially own shares in order to be entitled to a dividend. For example, a firm might declare a dividend on Nov 1, payable Dec 1 to holders of record Nov 15. Once a trade is executed an investor becomes the "owner of record" on settlement, which currently takes 5 business days for securities, and one business day for mutual funds. Stocks trade ex-dividend the fourth day before the record date, since the seller will still be the owner of record and is thus entitled to the dividend. (2) The date that determines who is entitled to payment of principal and interest due to be paid on a security. The record date for most MBSs is the last day of the month, however the last day on which they may be presented for the transfer is the last business day of the month. The record date for CMOs and asset-backed securities vary with each issue.

Recourse Term describing a type of loan. If a loan is with recourse, the lender has a general claim against the parent company if the collateral is insufficient to repay the debt.

Red herring A preliminary prospectus containing information required by the SEC. It excludes the offering price and the coupon of the new issue.

Redeemable Eligible for redemption under the terms of the indenture.

Redemption charge The commission charged by a mutual fund when redeeming shares. For example, a 2% redemption charge (also called a "back end load") on the sale of shares valued at $1000 will result in payment of $980 (or 98% of the value) to the investor. This charge may decrease or be eliminated as shares are held for longer time periods.

Redemption cushion The percentage by which the conversion value of a convertible security exceeds the redemption price (strike price).

Reference rate A benchmark 'interest rate (such as LIBOR), used to specify conditions of an interest rate swap or an interest rate agreement.

Refundable Eligible for refunding under the terms of indenture.

Refunded bond Also called a prerefunded bond, one that originally may have been issued as a general obligation or revenue bond but that is now secured by an "escrow fund" consisting entirely of direct U.S. government obligations that are sufficient for paying the bondholders.

Refunding The redemption of a bond with proceeds received from issuing lower-cost debt obligations ranking equal to or superior to the debt to be redeemed.

Regional fund A mutual fund that invests in a specific geographical area overseas, such as Asia or Europe.

Registered bond A bond whose issuer records ownership and interest payments. Differs from a bearer bond which is traded without record of ownership and whose possession is the only evidence of ownership.

Registered representative A person registered with the CFTC who is employed by, and soliciting business for, a commission house or futures commission merchant.

Registered trader A member of the exchange who executes frequent trades for his or her own account.

Registrar Financial institution appointed to record issue and ownership of company securities.

Registration statement A legal document that is filed with the SEC to register securities for public offering.

Regression analysis A statistical technique that can be used to estimate relationships between variables.

Regression equation An equation that describes the average relationship between a dependent variable and a set of explanatory variables.

Regression toward the mean The tendency for subsequent observations of a random variable to be closer to its mean.

Regular way settlement In the money and bond markets, the regular basis on which some security trades are settled is that the delivery of the securities purchased is made against payment in Fed funds on the day following the transaction.

Regulation A The securities regulation that exempts small public offerings, those valued at less than $1.5MM, from most registration requirements with the SEC.

Regulation D Fed regulation currently that required member banks to hold reserves against their net borrowings from foreign offices of other banks over a 28-day averaging period. Regulation D has been merged with Regulation M.

Regulation M Fed regulation currently requiring member banks to hold reserves against their net borrowings from their foreign branches over a 28-day averaging period. Reg M has also required member banks to hold reserves against Eurodollars lent by their foreign branches to domestic corporations for domestic purposes.

Regulation Q Fed regulation imposing caps on the rates that banks may pay on savings and time deposits. Currently time deposits with a denomination of $100,000 or more are exempt from Reg Q.

Regulatory accounting procedures Accounting principals required by the FHLB that allow S&Ls to elect annually to defer gains and losses on the sale of assets and amortize these deferrals over the average life of the asset sold.

Regulatory pricing risk Risk that arises when regulators restrict the premium rates that insurance companies can charge.

Regulatory surplus The surplus as measured using regulatory accounting principles (RAP) which may allow the non-market valuation of assets or liabilities and which may be materially different from economic surplus.

Reinvestment rate The rate at which an investor assumes interest payments made on a debt security can be reinvested over the life of that security.

Reinvestment risk The risk that proceeds received in the future will have to be reinvested at a lower potential interest rate.

Reinvoicing center A central financial subsidiary used by an MNC to reduce transaction exposure by having all home country exports billed in the home currency and then reinvoiced to each operating affililate in that affiliate's local currency. It can also be used as a netting center.

REIT (real estate investment trust) Real estate investment trust, which is similar to a closed-end mutual fund. REITs invest in real estate or loans secured by real estate and issue shares in such investments.

Relative purchasing power parity (RPPP) Idea that the rate of change in the price level of commodities in one country relative to the price level in another determines the rate of change of the exchange rate between the two countries' currencies.

Relative strength A stock's price movement over the past year as compared to a market index (the S&P 500). Value below 1.0 means the stock shows relative weakness in price movement (underperformed the market); a value above 1.0 means the stock shows relative strength over the 1-year period. Equation for Relative Strength: [current stock price/year-ago stock price] [current S&P 500/year-ago S&P 500]

Relative value The attractiveness measured in terms of risk, liquidity, and return of one instrument relative to another, or for a given instrument, of one maturity relative to another.

Relative yield spread The ratio of the yield spread to the yield level.

Remainderman One who receives the principal of a trust when it is dissolved.

Remaining maturity The length of time remaining until a bond's maturity.

Remaining principal balance The amount of principal dollars remaining to be paid under the mortgage as of a given point in time.

Rembrandt market The foreign market in the Netherlands.

REMIC (real estate mortgage investment conduit) A pass-through tax entity that can hold mortgages secured by any type of real property and issue multiple classes of ownership interests to investors in the form of pass-through certificates, bonds, or other legal forms. A financing vehicle created under the Tax Reform Act of 1986.

Remote disbursement Technique that involves writing checks drawn on banks in remote locations so as to increase disbursement float.

Rental lease See:full-service lease.

Reoffering yield In a purchase and sale, the yield to maturity at which the underwriter offers to sell the bonds to investors.

Reopen an issue The Treasury, when it wants to sell additional securities, will occasionally sell more of an existing issue (reopen it) rather than offer a new issue.

Reorganization Creating a plan to restructure a debtor's business and restore its financial health.

Replacement cost Cost to replace a firm's assets.

Replacement cycle The frequency with which an asset is replaced by an equivalent asset.

Replacement value Current cost of replacing the firm's assets.

Replacement-chain problem Idea that future replacement decisions must be taken into account in selecting among projects.

Replicating portfolio A portfolio constructed to match an index or benchmark.

Repo A agreement in which one party sells a security to another party and agrees to repurchase it on a specified date for a specified price. See: repurchase agreement.

Reported factor The pool factor as reported by the bond buyer for a given amortization period.

Reporting currency The currency in which the parent firm prepares its own financial statements; that is, U.S. dollars for a U.S. company.

Reproducible assets A tangible asset with physical properties that can be reproduced, such as a building or machinery.

Repurchase agreement An agreement with a commitment by the seller (dealer) to buy a security back from the purchaser (customer) at a specified price at a designated future date. Also called a repo, it represents a collateralized short-term loan, where the collateral may be a Treasury security, money market instrument, federal agency security, or mortgage-backed security. From the purchaser (customer) perspective, the deal is reported as a reverse Repo.

Repurchase of stock Device to pay cash to firm's shareholders that provides more preferable tax treatment for shareholders than dividends. Treasury stock is the name given to previously issued stock that has been repurchased by the firm. A repurchase is achieved through either a dutch auction, open market, or tender offer.

Required reserves The dollar amounts based on reserve ratios that banks are required to keep on deposit at a Federal Reserve Bank.

Required return The minimum expected return you would require to be willing to purchase the asset, that is, to make the investment.

Required yield Generally referring to bonds, the yield required by the marketplace to match available returns for financial instruments with comparable risk.

Reserve An accounting entry that properly reflects the contingent liabilities.

Reserve currency A foreign currency held by a central bank or monetary authority for the purposes of exchange intervention and the settlement of inter-governmental claims.

Reserve ratios Specified percentages of deposits, established by the Federal Reserve Board, that banks must keep in a non-interest-bearing account at one of the twelve Federal Reserve Banks.

Reserve requirements The percentage of different types of deposits that member banks are required to hold on deposit at the Fed.

Reset frequency The frequency with which the floating rate changes.

Residuals (1) Parts of stock returns not explained by the explanatory variable (the market-index return). They measure the impact of firm-specific events during a particular period. (2) Remainder cash flows generated by pool collateral and those needed to fund bonds supported by the collateral.

Residual assets Assets that remain after sufficient assets are dedicated to meet all senior debtholder's claims in full.

Residual claim Related: equity claim

Residual dividend approach An approach that suggests that a firm pay dividends if and only if acceptable investment opportunities for those funds are currently unavailable.

Residual losses Lost wealth of the shareholders due to divergent behavior of the managers.

Residual method A method of allocating the purchase price for the acquisition of another firm among the acquired assets.

Residual risk Related: unsystematic risk

Residual value Usually refers to the value of a lessor's property at the time the lease expires.

Resistance level A price level above which it is supposedly difficult for a security or market to rise.

Restrictive covenants Provisions that place constraints on the operations of borrowers, such as restrictions on working capital, fixed assets, future borrowing, and payment of dividend.

Retail Individual and institutional customers as opposed to dealers and brokers.

Retail credit Credit granted by a firm to consumers for the purchase of goods or services. **See:** consumer credit.

Retail investors individual investors Small investors who commit capital for their personal account.

Retained earnings Accounting earnings that are retained by the firm for reinvestment in its operations; earnings that are not paid out as dividends.

Retention rate The percentage of present earnings held back or retained by a corporation, or one minus the dividend payout rate. Also called the retention ratio.

Retire To extinguish a security, as in paying off a debt.

Retracement A price movement in the opposite direction of the previous trend.

Return The change in the value of a portfolio over an evaluation period, including any distributions made from the portfolio during that period.

Return on assets (ROA) Indicator of profitability. Determined by dividing net income for the past 12 months by total average assets. Result is shown as a percentage. ROA can be decomposed into return on sales (net income/sales) multiplied by asset utilization (sales/assets).

Return on equity (ROE) Indicator of profitability. Determined by dividing net income for the past 12 months by common stockholder equity (adjusted for stock splits). Result is shown as a percentage. Investors use ROE as a measure of how a company is using its money. ROE may be decomposed into return on assets (ROA) multiplied by financial leverage (total assets/total equity).

Return on investment (ROI) Generally, book income as a proportion of net book value.

Return on total assets The ratio of earnings available to common stockholders to total assets.

Return-to-maturity expectations A variant of pure expectations theory which suggests that the return that an investor will realize by rolling over short-term bonds to some investment horizon will be the same as holding a zero-coupon bond with a maturity that is the same as that investment horizon.

Revaluation An increase in the foreign exchange value of a currency that is pegged to other currencies or gold.

Revenue bond A bond issued by a municipality to finance either a project or an enterprise where the issuer pledges to the bondholders the revenues generated by the operating projects financed, for instance, hospital revenue bonds and sewer revenue bonds.

Revenue fund A fund accounting for all revenues from an enterprise financed by a municipal revenue bond.

Reverse price risk A type of mortgage-pipeline risk that occurs when a lender commits to sell loans to an investor at rates prevailing at application but sets the note rates when the borrowers close. The lender is thus exposed to the risk of falling rates.

Reverse repo In essence, refers to a repurchase agreement. From the customer's perspective, the customer provides a collateralized loan to the seller.

Reverse stock split A proportionate decrease in the number of shares, but not the value of shares of stock held by shareholders. Shareholders maintain the same percentage of equity as before the split. For example, a 1-for-3 split would result in stockholders owning 1 share for every 3 shares owned before the split. After the reverse split, the firm's stock price is, in this example, worth three times the pre-reverse split price. A firm generally institutes a reverse split to boost its stock's market price and attract investors.

Reversing trade Entering the opposite side of a currently held futures position to close out the position.

Revolving credit agreement A legal commitment wherein a bank promises to lend a customer up to a specified maximum amount during a specified period.

Revolving line of credit A bank line of credit on which the customer pays a commitment fee and can take down and repay funds according to his needs. Normally the line involves a firm commitment from the bank for a period of several years.

Reward-to-volatility ratio Ratio of excess return to portfolio standard deviation.

Riding the yield curve Buying long-term bonds in anticipation of capital gains as yields fall with the declining maturity of the bonds.

Right A short-lived (typically less than 90 days) call option for purchasing additional stock in a firm, issued by the firm to all its shareholders on a pro rata basis.

Rights offering Issuance of "rights" to current shareholders allowing them to purchase additional shares, usually at a discount to market price. Shareholders who do not exercise these rights are usually diluted by the offering. Rights are often transferable, allowing the holder to sell them on the open market to others who may wish to exercise them. Rights offerings are particularly common to closed end funds, which cannot otherwise issue additional common stock.

Rights-on Shares trading with rights attached to them.

Rings Trading arenas located on the floor of an exchange in which traders execute orders. Sometimes called a pit.

Risk Typically defined as the standard deviation of the return on total investment. Degree of uncertainty of return on an asset.

Risk-adjusted profitability A probability used to determine a "sure" expected value (sometimes called a certainty equivalent) that would be equivalent to the actual risky expected value.

Risk arbitrage Speculation on perceived mispriced securities, usually in connection with merger and acquisition deals. Mike Donatelli, John Demasi, Frank Cohane, and Scott Lewis are all hardcore arbs. They had a huge BT/MCI position in the summer of 1997, and came out smelling like roses.

Risk averse A risk-averse investor is one who, when faced with two investments with the same expected return but two different risks, prefers the one with the lower risk.

Risk classes Groups of projects that have approximately the same amount of risk.

Risk controlled arbitrage A self-funding, self-hedged series of transactions that generally utilize mortgage securities as the primary assets.

Risk indexes Categories of risk used to calculate fundamental beta, including (1) market variability, (2) earnings variability, (3) low valuation, (4) immaturity and smallness, (5) growth orientation, and (6) financial risk.

Risk lover A person willing to accept lower expected returns on prospects with higher amounts of risk.

Risk management The process of identifying and evaluating risks and selecting and managing techniques to adapt to risk exposures.

Risk neutral Insensitive to risk.

Risk prone Willing to pay money to transfer risk from others.

Risk premium The reward for holding the risky market portfolio rather than the risk-free asset. The spread between Treasury and non-Treasury bonds of comparable maturity.

Risk premium approach The most common approach for tactical asset allocation to determine the relative valuation of asset classes based on expected returns.

Riskless rate The rate earned on a riskless investment, typically the rate earned on the 90-day U.S. Treasury Bill.

Riskless rate of return The rate earned on a riskless asset.

Riskless arbitrage The simultaneous purchase and sale of the same asset to yield a profit.

Riskless or risk-free asset An asset whose future return is known today with certainty. The risk free asset is commonly defined as short-term obligations of the U.S. government.

Risky asset An asset whose future return is uncertain.

Risk-adjusted return Return earned on an asset normalized for the amount of risk associated with that asset.

Risk-free asset An asset whose future return is known today with certainty.

Risk-free rate The rate earned on a riskless asset.

Roll over Reinvest funds received from a maturing security in a new issue of the same or a similar security.

Rollover Most term loans in the Euromarket are made on a rollover basis, which means that the loan is periodically repriced at an agreed spread over the appropriate, currently prevailing LIBO rate.

Round lot A trading order typically of 100 shares of a stock or some multiple of 100. Related: odd lot.

Round-trip transactions costs Costs of completing a transaction, including commissions, market impact costs, and taxes.

Round-turn Procedure by which the Long or short position of an individual is offset by an opposite transaction or by accepting or making delivery of the actual financial instrument or physical commodity.

R squared (R^2) Square of the correlation coefficientthe proportion of the variability in one series that can be explained by the variability of one or more other series.

Rule 144a SEC rule allowing qualified institutional buyers to buy and trade unregistered securities.

Run A run consists of a series of bid and offer quotes for different securities or maturities. Dealers give to and ask for runs from each other.

Rule 415 Rule enacted in 1982 that permits firms to file shelf registration statements.

Safe harbor lease A lease to transfer tax benefits of ownership (depreciation and debt tax shield) from the lessee, if the lessee could not use them, to a lessor that could use them.

Safekeep For a fee, bankers will hold in their vault, clip coupons on, and present for payment at maturity bonds and money market instruments.

Safety cushion In a contingent immunization strategy, the difference between the initially available immunization level and the safety-net return.

Safety-net return The minimum available return that will trigger an immunization strategy in a contingent immunization strategy.

Sale and lease-back Sale of an existing asset to a financial institution that then leases it back to the user. **Related:** lease.

Sales charge The fee charged by a mutual fund when purchasing shares, usually payable as a commission to marketing agent, such as a financial advisor, who is thus compensated for his assistance to a purchaser. It represents the difference, if any, between the share purchase price and the share net asset value.

Sales forecast A key input to a firm's financial planning process. External sales forecasts are based on historical experience, statistical analysis, and consideration of various macroeconomic factors.

Sales-type lease An arrangement whereby a firm leases its own equipment, such as IBM leasing its own computers, thereby competing with an independent leasing company.

Salvage value Scrap value of plant and equipment.

Samurai bond A yen-denominated bond issued in Tokyo by a non-Japanese borrower. **Related:** bulldog bond and Yankee bond.

Samurai market The foreign market in Japan.

Savings and Loan association National- or state-chartered institution that accepts savings deposits and invests the bulk of the funds thus received in mortgages.

Savings deposits Accounts that pay interest, typically at below-market interest rates, that do not have a specific maturity, and that usually can be withdrawn upon demand.

SBIC Small Business Investment Company.

Scale A bank that offers to pay different rates of interest on CDs of varying rates is said to "post a scale." Commercial paper dealers also post scales.

Scale enhancing Describes a project that is in the same risk class as the whole firm.

Scale in When a trader or investor gradually takes a position in a security or market over time.

Scalp To trade for small gains. It normally involves establishing and liquidating a position quickly, usually within the same day.

Scenario analysis The use of horizon analysis to project bond total returns under different reinvestment rates and future market yields.

Scheduled cash flows The mortgage principal and interest payments due to be paid under the terms of the mortgage not including possible prepayments.

Search costs Costs associated with locating a counterparty to a trade, including explicit costs (such as advertising) and implicit costs (such as the value of time). **Related:**information costs.

Seasoned datings Extended credit for customers who order goods in periods other than peak seasons.

Seasoned issue Issue of a security for which there is an existing market. **Related:** Unseasoned issue.

Seasoned new issue A new issue of stock after the company's securities have previously been issued. A seasoned new issue of common stock can be made by using a cash offer or a rights offer.

SEC The Securities and Exchange Commission, the primary federal regulatory agency of the securities industry.

Second pass regression A cross-sectional regression of portfolio returns on betas. The estimated slope is the measurement of the reward for bearing systematic risk during the period analyzed.

Secondary issue (1) Procedure for selling blocks of seasoned issues of stocks. (2) More generally, sale of already issued stock.

Secondary market The market where securities are traded after they are initially offered in the primary market. Most trading is done in the secondary market. The New York stock Exchange, as well as all other stock exchanges, the bond markets, etc., are secondary markets. Seasoned securities are traded in the secondary market.

Sector Refers to a group of securities that are similar with respect to maturity, type, rating, industry, and/or coupon.

Section 482 United States Department of Treasury regulations governing transfer prices.

Secured debt Debt that, in the event of default, has first claim on specified assets.

Securities & Exchange Commission The SEC is a federal agency that regulates the U.S.financial markets.

Securities analysts Related:financial analysts

Securitization The process of creating a passthrough, such as the mortgage pass-through security, by which the pooled assets become standard securities backed by those assets. Also, refers to the replacement of nonmarketable loans and/or cash flows provided by financial intermediaries with negotiable securities issued in the public capital markets.

Security Piece of paper that proves ownership of stocks, bonds and other investments.

Security characteristic line A plot of the excess return on a security over the risk-free rate as a function of the excess return on the market.

Security deposit (initial) Synonymous with the term margin. A cash amount of funds that must be deposited with the broker for each contract as a guarantee of fulfillment of the futures contract. It is not considered as part payment or purchase. **Related:** margin

Security deposit (maintenance)Related: Maintenance margin security market line (SML). A description of the risk return relationship for individual securities, expressed in a form similar to the capital market line.

Security market line Line representing the relationship between expected return and market risk.

Security market plane A plane that shows the equilibrium between expected return and the beta coefficient of more than one factor.

Security selection See: security selection decision.

Security selection decision Choosing the particular securities to include in a portfolio.

Self-liquidating loan Loan to finance current assets, The sale of the current assets provides the cash to repay the loan.

Self-selection Consequence of a contract that induces only one group (e.g. low risk individuals) to participate.

Sell hedge Related: short hedge.

Sell limit order Conditional trading order that indicates that a, security may be sold at the designated price or higher. Related: buy limit order.

Selling group All banks involved in selling or marketing a new issue of stock or bonds

Selling short If an investor thinks the price of a stock is going down, the investor could borrow the stock from a broker and sell it. Eventually, the investor must buy the stock back on the open market. For instance, you borrow 1000 shares of XYZ on July 1 and sell it for $8 per share. Then, on Aug 1, you purchase 1000 shares of XYZ at $7 per share. You've made $1000 (less commissions and other fees) by selling short.

Sell-side analyst Also called a Wall Street analyst, a financial analyst who works for a brokerage firm and whose recommendations are passed on to the brokerage firm's customers.

Semi-strong form efficiency A form of pricing efficiency where the price of the security fully reflects all public information (including, but not limited to, historical price and trading patterns). Compare weak form efficiency and strong form efficiency.

Senior debt Debt that, in the event of bankruptcy, must be repaid before subordinated debt receives any payment.

SeniorityThe order of repayment. In the event of bankruptcy, senior debt must be repaid before subordinated debt is repaid.

Sensitivity analysis Analysis of the effect on a project's profitability due to changes in sales, cost, and so on.

Separation property The property that portfolio choice can be separated into two independent tasks: 1) determination of the optimal risky portfolio, which is a purely technical problem, and 2) the personal choice of the best mix of the risky portfolio and the risk-free asset.

Separation theorem The value of an investment to an individual is not dependent on consumption preferences. All investors will want to accept or reject the same investment projects by using the NPV rule, regardless of personal preference.

Serial bonds Corporate bonds arranged so that specified principal amounts become due on specified dates. Related: term bonds.

Serial covariance The covariance between a variable and the lagged value of the variable; the same as autocovariance.

Series bond Bond that may be issued in several series under the same indenture.

Series Options: All option contracts of the same class that also have the same unit of trade, expiration date, and exercise price. Stocks: shares which have common characteristics, such as rights to ownership and voting, dividends, par value, etc. In the case of many foreign shares, one series may be owned only by citizens of the country in which the stock is registered.

Set of contracts perspective View of corporation as a set of contracting relationships, among individuals who have conflicting objectives, such as shareholders or managers. The corporation is a legal contrivance that serves as the nexus for the contracting relationships.

Settlement When payment is made for a trade.

Settlement date The date on which payment is made to settle a trade. For stocks traded on US exchanges, settlement is currently 3 business days after the trade. For mutual funds, settlement usually occurs in the U.S.the day following the trade. In some regional markets, foreign shares may require months to settle.

Settlement price A figure determined by the closing range which is used to calculate gains and losses in futures market accounts. Settlement prices are used to determine gains, losses, margin calls, and invoice prices for deliveries. Related: closing range.

Settlement rate The rate suggested in Financial Accounting Standard Board (FASB) 87 for discounting the obligations of a pension plan. The rate at which the pension benefits could be effectively settled off the pension plan wished to terminate its pension obligation.

Seykota, Ed Ed Seykota is interviewed by Jack Schwager in Schwager's book, Market Wizards. Seykota was graduated from MIT in the early 1970s, and went on to develop the first commercially sold commodities trading system. Seykota went into business for himself, and in the years 1974-1989, managed to grow a $5,000 trading account to over $15 million dollars. Mr. Seykota is a trading genius who has been able to identify robust patterns of price action that repeat themselves in different markets. His quantitative and systematic approach to trading has been an inspiration for many. Mr. Seykota is also a genius when it comes to understanding human psychology.

Share repurchase Program by which a corporation buys back its own shares in the open market. It is usually done when shares are undervalued. Since it reduces the number of shares outstanding and thus increases earnings per share, it tends to elevate the market value of the remaining shares held by stockholders.

Shareholders' equity This is a company's total assets minus total liabilities. A company's net worth is the same thing.

Shareholders' letter A section of an annual report where one can find jargon-free discussions by management of successful and failed strategies which provides guidance for the probing of the rest of the report.

Shares Certificates or book entries representing ownership in a corporation or similar entity

Shark repellant Amendment to company charter intended to protect it against takeover.

Sharpe benchmark A statistically created benchmark that adjusts for a managers' index-like tendencies.

Sharpe ratio A measure of a portfolio's excess return relative to the total variability of the portfolio. Related: treynor index

Shelf registration A procedure that allows firms to file one registration statement covering several issues of the same security.

Shirking The tendency to do less work when the return is smaller. Owners may have more incentive to shirk if they issue equity as opposed to debt, because they retain less ownership interest in the company and therefore may receive a smaller return. Thus, shirking is considered an agency cost of equity.

Shogun bond Dollar bond issued in Japan by a nonresident.

Shop Wall Street jargon for a firm.

Shopping Seeking to obtain the best bid or offer available by calling a number of dealers and/or brokers.

Short One who has sold a contract to establish a market position and who has not yet closed out this position through an offsetting purchase; the opposite of a long position. Related: Long.

Short bonds Bonds with short current maturities.

Short book See: unmatched book.

Short hedge The sale of a futures contract(s) to eliminate or lessen the possible decline in value ownership of an approximately equal amount of the actual financial instrument or physical commodity.Related: Long hedge.

Short interest This is the total number of shares of a security that investors have borrowed, then sold in the hope that the security will fall in value. An investor then buys back the shares and pockets the difference as profit.

Short position Occurs when a person sells stocks he or she does not yet own. Shares must be borrowed, before the sale, to make "good delivery" to the buyer. Eventually, the shares must be bought to close out the transaction. This technique is used when an investor believes the stock price will go down.

Short sale Selling a security that the seller does not own but is committed to repurchasing eventually. It is used to capitalize on an expected decline in the security's price.

Short selling Establishing a market position by selling a security one does not own in anticipation of the price of that security falling.

Short squeeze A situation in which a lack of supply tends to force prices upward.

Short straddle A straddle in which one put and one call are sold.

Shortage cost Costs that fall with increases in the level of investment in current assets.

Shortfall risk The risk of falling short of any investment target.

Short-run operating activities Events and decisions concerning the short-term finance of a firm, such as how much inventory to order and whether to offer cash terms or credit terms to customers.

Short-term financial plan A financial plan that covers the coming fiscal year.

Short-term investment services Services that assist firms in making short-term investments.

Short-term solvency ratios Ratios used to judge the adequacy of liquid assets for meeting short-term obligations as they come due, including (1) the current ratio, (2) the acid-test ratio, (3) the inventory turnover ratio, and (4) the accounts receivable turnover ratio.

Short-term tax exempts Short-term securities issued by states, municipalities, local housing agencies, and urban renewal agencies.

SIC Abbreviation for Standard Industrial Classification. Each 4-digit code represents a unique business activity.

Side effects Effects of a proposed project on other parts of the firm.

Sight draft Demand for immediate payment.

SIMEX (Singapore International Monetary Exchange) A leading futures and options exchange in Singapore.

Simple prospect An investment opportunity where a certain initial wealth is placed at risk and only two outcomes are possible.

Single country fund A mutual fund that invests in individual countries outside the United States.

Single factor model A model of security returns that acknowledges only one common factor. See: factor model.

Single index model A model of stock returns that decomposes influences on returns into a systematic factor, as measured by the return on the broad market index, and firm specific factors.

Signal The process of conveying information through a firm's actions.

Signaling approach Approach to the determination of the optimal capital structure asserting that insiders in a firm have information that the market does not have; therefore, the choice of capital structure by insiders can signal information to outsiders and change the value of the firm. This theory is also called the asymmetric information approach.

Signaling view (on dividend policy) The argument that dividend changes are important signals to investors about changes in management's expectation about future earnings.

Simple compound growth method A method of calculating the growth rate by relating the terminal value to the initial value and assuming a constant percentage annual rate of growth between these two values.

Simple interest Interest calculated only on the initial investment. Related:compound interest.

Simple linear regression A regression analysis between only two variables, one dependent and the other explanatory.

Simple linear trend model An extrapolative statistical model that asserts that earnings have a base level and grow at a constant amount each period.

Simple moving average The mean, calculated at any time over a past period of fixed length.

Simulation The use of a mathematical model to imitate a situation many times in order to estimate the likelihood of various possible outcomes. **See:** Monte Carlo simulation.

Single-index model Related: market model

Single-payment bond A bond that will make only one payment of principal and interest.

Single-premium deferred annuity An insurance policy bought by the sponsor of a pension plan for a single premium. In return, the insurance company agrees to make lifelong payments to the employee (the policyholder) when that employee retires.

Sinker Sinking fund.

Sinking fund requirement A condition included in some corporate bond indentures that requires the issuer to retire a specified portion of debt each year. Any principal due at maturity is called the balloon maturity.

Size Large in size, as in the size of an offering, the size of an order, or the size of a trade. Size is relative from market to market and security to security. Context: "I can buy size at 102-22," means that a trader can buy a significant amount at 102-22.

Skewed distribution Probability distribution in which an unequal number of observations lie below and above the mean.

Skip-day settlement The trade is settled one business day beyond what is normal.

Slippage The difference between estimated transaction costs and actual transaction costs. The difference is usually composed of revisions to price difference or spread and commission costs.

Small-firm effect The tendency of small firms (in terms of total market capitalization) to outperform the stock market (consisting of both large and small firms).

Small issues exemption Securities issues that involve less than $1.5 million are not required to file a registration statement with the SEC. Instead, they are governed by Regulation A, for which only a brief offering statement is needed.

Smithsonian agreement A revision to the Bretton Woods international monetary system which was signed at the Smithsonian Institution in Washington, D.C., U.S.A., in December 1971. Included were a new set of par values, widened bands to +/- 2.25% of par, and an increase in the official value of gold to US$38.00 per ounce.

Society for Worldwide Interbank Financial Telecommunications (SWIFT) A dedicated computer network to support funds transfer messages internationally between over 900 member banks worldwide.

"Soft" Capital Rationing Capital rationing that under certain circumstances can be violated or even viewed as made up of targets rather than absolute constraints.

Soft currency A currency that is expected to drop in value relative to other currencies.

Soft dollars The value of research services that brokerage houses supply to investment managers "free of charge" in exchange for the investment manager's business/commissions.

Sole proprietorship A business owned by a single individual. The sole proprietorship pays no corporate income tax but has unlimited liability for business debts and obligations.

Sovereign risk The risk that a central bank will impose foreign exchange regulations that will reduce or negate the value of FX contracts. Also refers to the risk of government default on a loan made to it or guaranteed by it.

Span To cover all contingencies within a specified range.

Special dividend Also referred to as an extra dividend. Dividend that is unlikely to be repeated.

Special drawing rights (SDR) A form of international reserve assets, created by the IMF in 1967, whose value is based on a portfolio of widely used currencies.

Specialist On an exchange, the member firm that is designated as the market maker (or dealer for a listed common stock). Only one specialist can be designated for a given stock, but dealers may be specialists for several stocks. In contrast, there can be multiple market makers in the OTC market.

Specific issues market The market in which dealers reverse in securities they wish to short.

Specific risk See:unique risk.

Spectail A dealer that does business with retail but that concentrates more on acquiring and financing its own speculative positions.

Speculative demand (for money) The need for cash to take advantage of investment opportunities that may arise.

Speculative grade bond Bond rated Ba or lower by Moody's, or BB or lower by S&P, or an unrated bond.

Speculative motive A desire to hold cash for the purpose of being in a position to exploit any attractive investment opportunity requiring a cash expenditure that might arise.

Speculator One, who attempts to anticipate price changes and, through buying and selling contracts, aims to make profits. A speculator does not use the market in connection with the production, processing, marketing or handling of a product.See: trader.

Speed Related:prepayment speed

Spin-off A company can create an independent company from an existing part of the company by selling or distributing new shares in the so-called spinoff.

Split Sometimes, companies split their outstanding shares into a larger number of shares. If a company with 1 million shares did a two-for-one split, the company would have 2 million shares. An investor with 100 shares before the split would hold 200 shares after the split. The investor's percentage of equity in the company remains the same, and the price of the stock he owns is one-half the price of the stock on the day prior to the split.

Split-fee option An option on an option. The buyer generally executes the split fee with first an initial fee, with a window period at the end of which upon payment of a second fee the original terms of the option may be extended to a later predetermined final notification date.

Split-rate tax system A tax system that taxes retained earnings at a higher rate than earnings that are distributed as dividends.

Spot exchange rates Exchange rate on currency for immediate delivery. Related: forward exchange rate.

Spot futures parity theorem Describes the theoretically correct relationship between spot and futures prices. Violation of the parity relationship gives rise to arbitrage opportunities.

Spot interest rate Interest rate fixed today on a loan that is made today. **Related:** forward interest rates.

Spot lending The origination of mortgages by processing applications taken directly from prospective borrowers.

Spot markets Related: cash markets

Spot month The nearest delivery month on a futures contract.

Spot price The current marketprice of the actual physical commodity. Also called cash price.

Spot rate The theoretical yield on a zero-coupon Treasury security.

Spot rate curve The graphical depiction of the relationship between the spot rates and maturity.

Spot trade The purchase and sale of a foreign currency, commodity, or other item for immediate delivery.

Spread (1) The gap between bid and ask prices of a stock or other security. (2) The simultaneous purchase and sale of separate futures or options contracts for the same commodity for delivery in different months. Also known as a straddle. (3) Difference between the price at which an underwriter buys an issue from a firm and the price at which the underwriter sells it to the public. (4) The price an issuer pays above a benchmark fixed-income yield to borrow money.

Spread income Also called margin income, the difference between income and cost. For a depository institution, the difference between the assets it invests in (loans and securities) and the cost of its funds (deposits and other sources).

Spread strategy A strategy that involves a position in one or more options so that the cost of buying an option is funded entirely or in part by selling another option in the same underlying. Also called spreading.

Spreadsheet A computer program that organizes numerical data into rows and columns on a terminal screen, for calculating and making adjustments based on new data.

Stakeholders All parties that have an interest, financial or otherwise, in a firm - stockholders, creditors, bondholders, employees, customers, management, the community, and the government.

Stand-alone principle Investment principle that states a firm should accept or reject a project by comparing it with securities in the same risk class.

Standard deviation The square root of the variance. A measure of dispersion of a set of data from their mean.

Standard error In statistics, a measure of the possible error in an estimate.

Standardized normal distribution A normal distribution with a mean of 0 and a standard deviation of 1.

Standardized value Also called the normal deviate, the distance of one data point from the mean, divided by the standard deviation of the distribution.

Standby agreement In a rights issue, agreement that the underwriter will purchase any stock not purchased by investors.

Standby fee Amount paid to an underwriter who agrees to purchase any stock that is not subscribed to the public investor in a rights offering.

Standstill agreements Contracts where the bidding firm in a takeover attempt agrees to limit its holdings another firm.

Stated annual interest rate The interest rate expressed as a per annum percentage, by which interest payment is determined.

Stated conversion price At the time of issuance of a convertible security, the price the issuer effectively grants the security holder to purchase the common stock, equal to the par value of the convertible security divided by the conversion ratio.

Stated maturity For the CMO tranche, the date the last payment would occur at zero CPR.

Statement billing Billing method in which the sales for a period such as a month (for which a customer also receives invoices) are collected into a single statement and the customer must pay all of the invoices represented on the statement.

Statement of cash flows A financial statement showing a firm's cash receipts and cash payments during a specified period.

Statement-of-cash-flows method A method of cash budgeting that is organized along the lines of the statement of cash flows.

Statement of Financial Accounting Standards No. 8 This is a currency translation standard previously in use by U.S. accounting firms. See: Statement of Accounting Standards No. 52.

Statement of Financial Accounting Standards No. 52 This is the currency translation standard currently used by U.S. firms. It mandates the use of the current rate method. See: Statement of Financial Accounting Standards No. 8.

Static theory of capital structure Theory that the firm's capital structure is determined by a trade-off of the value of tax shields against the costs of bankruptcy.

Statutory surplus The surplus of an insurance company determined by the accounting treatment of both assets and liabilities as established by state statutes.

Steady state As the MBS pool ages, or four to six months after it was passed at least once through the threshold for refinancing, the prepayment speed tends to stabilize within a fairly steady range.

Steepening of the yield curve A change in the yield curve where the spread between the yield on a long-term and short-term Treasury has increased. Compare flattening of the yield curve and butterfly shift.

Step-up To increase, as in step up the tax basis of an asset.

Step-up bond A bond that pays a lower coupon rate for an initial period which then increases to a higher coupon rate. **Related:** Deferred-interest bond, Payment-in-kind bond

Sterilized intervention Foreign exchange market intervention in which the monetary authorities have insulated their domestic money supplies from the foreign exchange transactions with offsetting sales or purchases of domestic assets.

Stochastic models Liability-matching models that assume that the liability payments and the asset cash flows are uncertain. Related: Deterministic models.

Stock Ownership of a corporation which is represented by shares which represent a piece of the corporation's assets and earnings.

Stock dividend Payment of a corporate dividend in the form of stock rather than cash. The stock dividend may be additional shares in the company, or it may be shares in a subsidiary being spun off to shareholders. Stock dividends are often used to conserve cash needed to operate the business. Unlike a cash dividend, stock dividends are not taxed until sold.

Stock exchanges Formal organizations, approved and regulated by the Securities and Exchange Commission (SEC), that are made up of members that use the facilities to exchange certain common stocks. The two major national stock exchanges are the New York Stock Exchange (NYSE) and the American Stock Exchange (ASE or AMEX). Five regional stock exchanges include the Midwest, Pacific, Philadelphia, Boston, and Cincinnati. The Arizona stock exchange is an after hours electronic marketplace where anonymous participants trade stocks via personal computers.

Stock repurchase A firm's repurchase of outstanding shares of its common stock.

Stock selection An active portfolio management technique that focuses on advantageous selection of particular stocks rather than on broad asset allocation choices.

Stockholder equity Balance sheet item that includes the book value of ownership in the corporation. It includes capital stock, paid in surplus, and retained earnings.

Stock index option An option in which the underlying is a common stock index.

Stock market Also called the equity market, the market for trading equities.

Stock option An option in which the underlying is the common stock of a corporation.

Stock replacement strategy A strategy for enhancing a portfolio's return, employed when the futures contract is expensive based on its theoretical price, involving a swap between the futures, treasury bills portfolio and a stock portfolio.

Stock split Occurs when a firm issues new shares of stock but in turn lowers the current market price of its stock to a level that is proportionate to pre-split prices. For example, if IBM trades at $100 before a 2-for-1 split, after the split it will trade at $50 and holders of the stock will have twice as many shares than they had before the split. **See:** split.

Stock ticker This is a lettered symbol assigned to securities and mutual funds that trade on U.S.financial exchanges.

Stockholder Holder of equity shares in a firm.

Stockholder's books Set of books kept by firm management for its annual report that follows Financial Accounting Standards Board rules. The tax books follow IRS tax rules.

Stockholder's equity The residual claims that stockholders have against a firm's assets, calculated by subtracting total liabilities from total assets.

Stockout Running out of inventory.

Stop-loss order An order to sell a stock when the price falls to a specified level.

Stop order (or stop) An order to buy or sell at the market when a definite price is reached, either above (on a buy) or below (on a sell) the price that prevailed when the order was given.

Stopping curve A curve showing the refunding rates for different points in time at which the expected value of refunding immediately equals the expected value of waiting to refund.

Stopping curve refunding rate A refunding rate that falls on the stopping curve.

Stop-limit order A stop order that designates a price limit. In contrast to the stop order, which becomes a market order once the stop is reached, the stop-limit order becomes a limit order once the stop is reached.

Straddle Purchase or sale of an equal number of puts and calls with the same terms at the same time. **Related:** spread

Straight line depreciation An equal dollar amount of depreciation in each accounting period.

Straight value Also called investment value, the value of a convertible security without the con-version option.

Straight voting A shareholder may cast all of his votes for each candidate for the board of directors.

Stratified equity indexing A method of constructing a replicating portfolio in which the stocks in the index are classified into stratum, and each stratum is represented in the portfolio.

Stratified sampling approach to indexing An approach in which the index is divided into cells, each representing a different characteristic of the index, such as duration or maturity.

Stratified sampling bond indexing A method of bond indexing that divides the index into cells, each cell representing a different characteristic, and that buys bonds to match those characteristics.

Street Brokers, dealers, underwriters, and other knowledgeable members of the financial community; from Wall Street financial community.

Street name Describes securities held by a broker on behalf of a client but registered in the name of the Wall Street firm.

Strike index For a stock index option, the index value at which the buyer of the option can buy or sell the underlying stock index. The strike index is converted to a dollar value by multiplying by the option's contract multiple. Related: strike price

Strike price The stated price per share for which underlying stock may be purchased (in the case of a call) or sold (in the case of a put) by the option holder upon exercise of the option contract.

Strip mortgage participation certificate (strip PC) Ownership interests in specified mortgages purchased by Freddie Mac from a single seller in exchange for strip PCs representing interests in the same mortgages.

Stripped bond Bond that can be subdivided into a series of zero-coupon bonds.

Stripped mortgage-backed securities (SMBSs) Securities that redistribute the cash flows from the underlying generic MBS collateral into the principal and interest components of the MBS to enhance their use in meeting special needs of investors.

Strip, strap Variants of a straddle. A strip is two puts and one call on a stock, a strap is two calls and one put on a stock. In both cases, the puts and calls have the same strike price and expiration date.

Strong-form efficiency Pricing efficiency, where the price of a, security reflects all information, whether or not it is publicly available. **Related:** Weak form efficiency, semi strong form efficiency

Structured arbitrage transaction A self-funding, self-hedged series of transactions that usually utilize mortgage securities as the primary assets.

Structured debt Debt that has been customized for the buyer, often by incorporating unusual options.

Structured portfolio strategy A strategy in which a portfolio is designed to achieve the performance of some predetermined liabilities that must be paid out in the future.

Structured settlement An agreement in settlement of a lawsuit involving specific payments made over a period of time. Property and casualty insurance companies often buy life insurance products to pay the costs of such settlements.

Subject Refers to a bid or offer that cannot be executed without confirmation from the customer.

Subject to opinion An auditor's opinion reflecting acceptance of a company's financial statements subject to pervasive uncertainty that cannot be adequately measured, such as information relating to the value of inventories, reserves for losses, or other matters subject to judgment.

Subjective probabilities Probabilities that are determined subjectively (for example, on the basis of judgement rather than using statistical sampling).

Subordinated debenture bond An unsecured bond that ranks after secured debt, after debenture bonds, and often after some general creditors in its claim on assets and earnings. Related: Debenture bond, mortgage bond, collateral trust bonds.

Subordinated debt Debt over which senior debt takes priority. In the event of bankruptcy, subordinated debtholders receive payment only after senior debt claims are paid in full.

Subordination clause A provision in a bond indenture that restricts the issuer's future borrowing by subordinating the new lender's claims on the firm to those of the existing bond holders.

Subpart F Special category of foreign-source "unearned" income that is currently taxed by the IRS whether or not it is remitted to the U.S.

Subperiod return The return of a portfolio over a shorter period of time than the evaluation period.

Subscription price Price that the existing shareholders are allowed to pay for a share of stock in a rights offering.

Subsidiary A foreign-based affiliate that is a separately incorporated entity under the host country's law.

Substitute sale A method for hedging price risk that utilizes debt-market instruments, such as interest rate futures, or that involves selling borrowed securities as the primary assets.

Substitution swap A swap in which a money manager exchanges one bond for another bond that is similar in terms of coupon, maturity, and credit quality, but offers a higher yield.

Sum-of-the-years'-digits depreciation Method of accelerated depreciation.

Sunk costs Costs that have been incurred and cannot be reversed.

Supermajority Provision in a company's charter requiring a majority of, say, 80% of shareholders to approve certain changes, such as a merger.

Supply shock An event that influences production capacity and costs in an economy.

Support level A price level below which it is supposedly difficult for a security or market to fall.

Surplus funds Cash flow available after payment of taxes in the project.

Surplus management Related: asset management

Sushi bond A eurobond issued by a Japanese corporation.

Sustainable growth rate Maximum rate of growth a firm can sustain without increasing financial leverage.

Swap An arrangement whereby two companies lend to each other on different terms, e.g. in different currencies, and/or at different interest rates, fixed or floating.

Swap assignment Related: swap sale.

Swap buy-back The sale of an interest rate swap by one counterparty to the other, effectively ending the swap.

Swap option See:Swaption. Related: Quality option.

Swap rate The difference between spot and forward rates expressed in points, e.g., $0.0001 per pound sterling.

Swap reversal An interest rate swap designed to end a counterparty's role in another interest rate swap, accomplished by counterbalancing the original swap in maturity, reference rate, and notional amount.

Swap sale Also called a swap assignment, a transaction that ends one counterparty's role in an interest rate swap by substituting a new counterparty whose credit is acceptable to the other original counterparty.

Swaption Options on interest rate swaps. The buyer of a swaption has the right to enter into an interest rate swap agreement by some specified date in the ' future. The swaption agreement will specify whether the buyer of the swaption will be a fixed-rate receiver or a fixed-rate payer. The writer of the swaption becomes the counterparty to the swap if the buyer exercises.

Sweep account Account in which the bank takes all of the excess available funds at the close of each business day and invests them for the firm.

Swingline facility Bank borrowing facility to provide finance while the firm replaces U.S. commercial paper with eurocommercial paper.

Swissy Jargon for the Swiss Franc.

Switching Liquidating an existing position and simultaneously reinstating a position in another futures contract of the same type. Symmetric cash matching An extension of cash flow matching that allows for the short-term borrowing of funds to satisfy a liability prior to the liability due date, resulting in a reduction in the cost of funding liabilities.

Symmetric cash matching An extension of cash flow matching that allows for the short-term borrowing of funds to satisfy a liability prior to the liability due date, resulting in a reduction in the cost of funding liabilities.

Synchronous data Data available at the same time. In testing option-pricing models, the price of the option and of the underlying should be synchronous, representing the same moment in the market.

Syndicate A group of banks that acts jointly, on a temporary basis, to loan money in a bank credit (syndicated credit) or to underwrite a new issue of bonds.

Synergistic effect A violation of value-additivity whereby the value of the combination is greater than the sum of the individual values.

Synthetics Customized hybrid instruments created by blending an underlying price on a cash instrument with the price of a derivative instrument.

Systematic Common to all businesses.

Systematic risk Also called undiversifiable risk or market risk, the minimum level of risk that can be obtained for a portfolio by means of diversification across a large number of randomly chosen assets. Related: unsystematic risk.

Systematic risk principle Only the systematic portion of risk matters in large, well-diversified portfolios. The, expected returns must be related only to systematic risks.

T-period holding-period return The percentage return over the T-year period an investment lasts.

Tactical Asset Allocation (TAA) An asset allocation strategy that allows active departures from the normal asset mix based upon rigorous objective measures of value. Often called active management. It involves forecasting asset returns, volatilities and correlations. The forecasted variables may be functions of fundamental variables, economic variables or even technical variables.

Tail (1) The difference between the average price in Treasury auctions and the stopout price. (2) A future money market instrument (one available some period hence) created by buying an existing instrument and financing the initial portion of its life with a term repo. (3) The extreme end under a probability curve. (4) The odd amount in a MBS pool.

Take (1) A dealer or customer who agrees to buy at another dealer's offered price is said to take that offer. (2) Also, Euro bankers speak of taking deposits rather than buying money.

Take a position To buy or sell short; that is, to have some amount that is owned or owed on an asset or derivative security.

Take-or-pay contract A contract that obligates the purchaser to take any product that is offered to it (and pay the cash purchase price) or pay a specified amount if it refuses to take the product.

Take-out A cash surplus generated by the sale of one block of securities and the purchase of another, e.g. selling a block of bonds at 99 and buying another block at 95. Also, a bid made to a seller of a security that is designed (and generally agreed) to take him out of the market.

Take-up fee A fee paid to an underwriter in connection with an underwritten rights offering or an underwritten forced conversion as compensation for each share of common stock he underwriter obtains and must resell upon the exercise of rights or conversion of bonds.

Takeover General term referring to transfer of control of a firm from one group of shareholder's to another group of shareholders.

Taking a view A London expression for forming an opinion as to where market prices are headed and acting on it.

Taking delivery Refers to the buyer's actually assuming possession from the seller of the asset agreed upon in a forward contract or a futures contract.

Tandem programs Under Ginnie Mae, mortgage funds provided at below-market rates to residential mortgage buyers with FHA Section 203 and 235 loans and to developers of multifamily projects with Section 236 loans initially and later with Section 221(d)(4) loans.

TANs (tax anticipation notes) Tax anticipation notes issued by states or municipalities to finance current operations in anticipation of future tax receipts.

Tangible asset An asset whose value depends on particular physical properties. These i nclude reproducible assets such as buildings or machinery and non-reproducible assets such as land, a mine, or a work of art. Also called real assets. **Related:** Intangible asset

Target cash balance Optimal amount of cash for a firm to hold, considering the trade-off between the opportunity costs of holding too much cash and the trading costs of holding too little cash.

Target firm A firm that is the object of a takeover by another firm.

Target payout ratio A firm's long-run dividend-to-earnings ratio. The firm's policy is to attempt to pay out a certain percentage of earnings, but it pays a stated dollar dividend and adjusts it to the target as base-line increases in earnings occur.

Target zone arrangement A monetary system under which countries pledge to maintain their exchange rates within a specific margin around agreed-upon, fixed central exchange rates.

Targeted repurchase The firm buys back its own stock from a potential bidder, usually at a substantial premium, to forestall a takeover attempt.

Tax anticipation bills (TABs) Special bills that the Treasury occasionally issues that mature on corporate quarterly income tax dates and can be used at face value by corporations to pay their tax liabilities.

Tax books Set of books kept by a firm's management for the IRS that follows IRS rules. The stockholder's books follow Financial Accounting Standards Board rules.

Tax clawback agreement An agreement to contribute as equity to a project the value of all previously realized project-related tax benefits not already clawed back to the extent required to cover any cash deficiency of the project.

Tax differential view (of dividend policy) The view that shareholders prefer capital gains over dividends, and hence low payout ratios, because capital gains are effectively taxed at lower rates than dividends.

Tax-exempt sector The municipal bond market where state and local governments raise funds. Bonds issued in this sector are exempt from federal income taxes.

Tax free acquisition A merger or consolidation in which 1) the acquirer's tax basis in each asset whose ownership is transferred in the transaction is generally the same as the acquiree's, and 2) each seller who receives only stock does not have to pay any tax on the gain he realizes until the shares are sold.

Tax haven A nation with a moderate level of taxation and/or liberal tax incentives for undertaking specific activities such as exporting or investing.

Tax Reform Act of 1986 A 1986 law involving a major overhaul of the U.S. tax code.

Tax shield The reduction in income taxes that results from taking an allowable deduction from taxable income.

Tax swap Swapping two similar bonds to receive a tax benefit.

Tax deferral option The feature of the U.S. Internal Revenue Code that the capital gains tax on an asset is payable only when the gain is realized by selling the asset.

Tax-deferred retirement plans Employer-sponsored and other plans that allow contributions and earnings to be made and accumulate tax-free until they are paid out as benefits.

Tax-timing option The option to sell an asset and claim a loss for tax purposes or not to sell the asset and defer the capital gains tax.

Taxable acquisition A merger or consolidation that is not a tax-fee acquisition. The selling shareholders are treated as having sold their shares.

Taxable income Gross income less a set of deductions.

Taxable transaction Any transaction that is not tax-free to the parties involved, such as a taxable acquisition.

TBA (to be announced) A contract for the purchase or sale of a MBS to be delivered at an agreed-upon future date but does not include a specified pool number and number of pools or precise amount to be delivered.

Technical analysis Security analysis that seeks to detect and interpret patterns in past security prices.

Technical analysts Also called chartists or technicians, analysts who use mechanical rules to detect changes in the supply of and demand for a stock and capitalize on the expected change.

Technical condition of a market Demand and supply factors affecting price, in particular the net position, either long or short, of the dealer community.

Technical descriptors Variables that are used to describe the market on a technical basis.

Technical insolvency Default on a legal obligation of the firm. For example, technical insolvency occurs when a firm doesn't pay a bill.

Technician Related: technical analysts

TED spread Difference between U.S. Treasury bill rate and eurodollar rate; used by some traders as a measure of investor/trader anxiety.

Temporal method Under this currency translation method, the choice of exchange rate depends on the underlying method of valuation. Assets and liabilities valued at historical cost (market cost) are translated at the historical (current market) rate.

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Tender To offer for delivery against futures.

Tender offer General offer made publicly and directly to a firm's shareholders to buy their stock at a price well above the current market price.

Tender offer premium The premium offered above the current market price in a tender offer.

10-K Annual report required by the SEC each year. Provides a comprehensive overview of a company's state of business. Must be filed within 90 days after fiscal year end. A 10Q report is filed quarterly.

Term bonds Often referred to as bullet-maturity bonds or simply bullet bonds, bonds whose principal is payable at maturity. **Related:** serial bonds

Tenor Maturity of a loan.

Term Fed Funds Fed Funds sold for a period of time longer than overnight.

Term life insurance A contract that provides a death benefit but no cash build-up or investment component. The premium remains constant only for a specified term of years, and the policy is usually renewable at the end of each term.

Term bonds Often referred to as bullet-maturity bonds or simply bullet bonds, bonds whose principal is payable at maturity. **Compare to:** Serial bonds.

Term loan A bank loan, typically with a floating interest rate, for a specified amount that matures in between one and ten years and requires a specified repayment schedule.

Term insurance Provides a death benefit only, no build-up of cash value.

Term repo A repurchase \agreement with a term of more than one day.

Term structure of interest rates Relationship between \interest rates on bonds of different maturities usually depicted in the form of a graph often depicted as a yield curve. Harvey shows that inverted term structures (long rates below short rates) have preceded every recession over the past 30 years.

Term to maturity The time remaining on a bond's life, or the date on which the debt will cease to exist and the borrower will have completely paid off the amount borrowed. **See:** Maturity.

Term premiums Excess of the yields to maturity on long-term bonds over those of short-term bonds.

Term trust A closed-end fund that has a fixed termination or maturity date.

Terminal value The value of a bond at maturity, typically its par value, or the value of an asset (or an entire firm) on some specified future valuation date.

Terms of sale Conditions on which a firm proposes to sell its goods services for cash or credit.

Terms of trade The weighted average of a nation's export prices relative to its import prices.

Theoretical futures price Also called the fair price, the equilibrium futures price.

Theoretical spot rate curve A curve derived from theoretical considerations as applied to the yields of actually traded Treasury debt securities because there are no zero-coupon Treasury debt issues with a maturity greater than one year. Like the yield curve, this is a graphical depiction of the term structure of interest rates.

Theta Also called time decay, the ratio of the change in an option price to the decrease in time to expiration.

Thin market A market in which trading volume is low and in which consequently bid and asked quotes are wide and the liquidity of the instrument traded is low.

Thinly traded Infrequently traded.

Third market Exchange-listed securities trading in the OTC market.

Three-phase DDM A version of the dividend discount model which applies a different expected dividend rate depending on a company's life-cycle phase, growth phase, transition phase, or maturity phase.

Threshold for refinancing The point when the WAC of an MBS is at a level to induce homeowners to prepay the mortgage in order to refinance to a lower-rate mortgage, generally reached when the WAC of the MBS is 2% or more above currently available mortgage rates.

Throughput agreement An agreement to put a specified amount of product per period through a particular facility. For example, an agreement to ship a specified amount of crude oil per period through a particular pipeline.

Tick Refers to the minimum change in price a security can have, either up or down. **Related:** point.

Tick indicator A market indicator based on the number of stocks whose last trade was an uptick or a downtick. Used as an indicator of market sentiment or psychology to try to predict the market's trend.

Tick-test rules SEC-imposed restrictions on when a short sale may be executed, intended to prevent investors from destabilizing the price of a stock when the market price is falling. A short sale can be made only when either (1) the sale price of the particular stock is higher than the last trade price (referred to as an uptick trade) or (2) if there is no change in the last trade price of the particular stock, the previous trade price must be higher than the trade price that preceded it (referred to as a zero uptick).

Tight market A tight market, as opposed to a thin market, is one in which volume is large, trading is active and highly competitive, and spreads between bid and ask prices are narrow.

Tilted portfolio An indexing strategy that is linked to active management through the emphasis of a particular industry sector, selected performance factors such as earnings momentum, dividend yield, price-earnings ratio, or selected economic factors such as interest rates and inflation.

Time decay Related: theta.

Time deposit Interest-bearing deposit at a savings institution that has a specific maturity. **Related:** certificate of deposit.

Time draft Demand for payment at a stated future date.

Time premium Also called time value, the amount by which the option price exceeds its intrinsic value. The value of an option beyond its current exercise value representing the optionholder's control until expiration, the risk of the underlying asset, and the riskless return.

Time until expiration The time remaining until a financial contract expires. Also called time to maturity.

Time to maturity The time remaining until a financial contract expires. Also called time until expiration.

Time value of an option The portion of an option's premium that is based on the amount of time remaining until the expiration date of the option contract, and that the underlying components that determine the value of the option may change during that time. Time value is generally equal to the difference between the premium and the intrinsic value. Related: in-the-money.

Time value of money The idea that a dollar today is worth more than a dollar in the future, because the dollar received today can earn interest up until the time the future dollar is received.

Time-weighted rate of return Related: Geometric mean return.

Times-interest-earned ratio Earnings before interest and tax, divided by interest payments.

Timing option For a Treasury Bond or note futures contract, the seller's choice of when in the delivery month to deliver.

Tobin's Q Market value of assets divided by replacement value of assets. A Tobin's Q ratio greater than 1 indicates the firm has done well with its investment decisions.

Tolling agreement An agreement to put a specified amount of raw material per period through a particular processing facility. For example, an agreement to process a specified amount of alumina into aluminum at a particular aluminum plant.

Tom next In the interbank market in Eurodollar deposits and the foreign exchange market, the value (delivery) date on a Tom next transaction is the next business day. Refers to "tomorrow next."

Tombstone Advertisement listing the underwriters to a security issue.

Top-down equity management style A management style that begins with an assessment of the overall economic environment and makes a general asset allocation decision regarding various sectors of the financial markets and various industries. The bottom-up manager, in contrast, selects the specific securities within the favored sectors.

Total asset turnover The ratio of net sales to total assets.

Total debt to equity ratio A capitalization ratio comparing current liabilities plus long-term debt to shareholders' equity.

Total dollar return The dollar return on a nondollar investment, which includes the sum of any dividend/interest income, capital gains or losses, and currency gains or losses on the investment. **See also:** total return.

Total return In performance measurement, the actual rate of return realized over some evaluation period. In fixed income analysis, the potential return that considers all three sources of return (coupon interest, interest on interest, and any capital gain/loss) over some i nvestment horizon.

Total revenue Total sales and other revenue for the period shown. Known as "turnover" in the UK.

Tracking error In an indexing strategy, the difference between the performance of the benchmark and the replicating portfolio.

Trade A verbal (or electronic) transaction involving one party buying a security from another party. Once a trade is consummated, it is considered "done" or final. Settlement occurs 1-5 business days later.

Trade acceptance Written demand that has been accepted by an industrial company to pay a given sum at a future date. **Related:** banker's acceptance.

Trade credit Credit granted by a firm to another firm for the purchase of goods or services.

Trade date In an interest rate swap, the date that the counterparties commit to the swap. Also, the date on which a trade occurs. Trades generally settle (are paid for) 1-5 business days after a trade date. With stocks, settlement is generally 3 business days after the trade.

Trade debt Accounts payable.

Trade draft A draft addressed to a commercial enterprise. **See:**draft.

Trade on top of Trade at a narrow or no spread in basis points relative to some other bond yield, usually Treasury bonds.

Trade house A firm which deals in actual commodities.

Traders Persons who take positions in securities and their derivatives with the objective of making profits. Traders can make markets by trading the flow. When they do that, their objective is to earn the bid/ask spread. Traders can also be of the sort who take proprietary positions whereby they seek to profit from the directional movement of prices or spread positions.

Trading Buying and selling securities.

Trading costs Costs of buying and selling marketable securities and borrowing. Trading costs include commissions, slippage, and the bid/ask spread. **See:** transaction costs.

Trading halt Trading of a stock, bond, option or futures contract can be halted by an exchange while news is being broadcast about the security.

Trading paper CDs purchased by accounts that are likely to resell them. The term is commonly used in the Euromarket.

Trading posts The posts on the floor of a stock exchange where the specialists stand and securities are traded.

Trading range The difference between the high and low prices traded during a period of time; with commodities, the high/low price limit established by the exchange for a specific commodity for any one day's trading.

Traditional view (of dividend policy) An argument that "within reason," investors prefer large dividends to smaller dividends because the dividend is sure but future capital gains are uncertain.

Tranche One of several related securities offered at the same time. Tranches from the same offering usually have different risk, reward, and/or maturity characteristics.

Transaction exposure Risk to a firm with known future cash flows in a foreign currency that arises from possible changes in the exchange rate. **Related:**translation exposure.

Transactions costs The time, effort, and money necessary, including such things as commission fees and the cost of physically moving the asset from seller to buyer. **Related:** Round-trip transaction costs, Information costs, search costs.

Transaction loan A loan extended by a bank for a specific purpose. In contrast, lines of credit and revolving credit agreements involve loans that can be used for various purposes.

Transaction demand (for money) The need to accommodate a firm's expected cash transactions.

Transactions motive A desire to hold cash for the purpose of conducting cash based transactions.

Transfer agent Individual or institution appointed by a company to look after the transfer of securities.

Transfer price The price at which one unit of a firm sells goods or services to another unit of the same firm.

Transferable put right An option issued by the firm to its shareholders to sell the firm one share of its common stock at a fixed price (the strike price) within a stated period (the time to maturity). The put right is "transferable" because it can be traded in the capital markets.

Transition phase A phase of development in which the company's earnings begin to mature and decelerate to the rate of growth of the economy as a whole. **Related:** three-phase DDM.

Translation exposure Risk of adverse effects on a firm's financial statements that may arise from changes in exchange rates. **Related:** transaction exposure.

Treasurer The corporate officer responsible for designing and implementing many of the firm's financing and investing activities.

Treasurer's check A check issued by a bank to make a payment. Treasurer's checks outstanding are counted as part of a bank's reservable depostits and as part of the money supply.

Treasuries Related: treasury securities.

Treasury bills Debt obligations of the U.S. Treasury that have maturities of one year or less. Maturities for T-bills are usually 91 days, 182 days, or 52 weeks.

Treasury bonds debt obligations of the U.S. Treasury that have maturities of 10 years or more.

Treasury notes Debt obligations of the U.S. Treasury that have maturities of more than 2 years but less than 10 years.

Treasury securities Securities issued by the U.S. Department of the Treasury.

Treasury stock Common stock that has been repurchased by the company and held in the company's treasury.

Trend The general direction of the market.

Treynor Index A measure of the excess return per unit of risk, where excess return is defined as the difference between the portfolio's return and the risk-free rate of return over the same evaluation period and where the unit of risk is the portfolio's beta.

Triangular arbitrage Striking offsetting deals among three markets simultaneously to obtain an arbitrage profit.

Triple witching hour The four times a year that the S&P futures contract expires at the same time as the S&P 100 index option contract and option contracts on individual stocks.

Trough The transition point between economic recession and recovery.

True interest cost For a security such as commercial paper that is sold on a discount basis, the coupon rate required to provide an identical return assuming a coupon-bearing instrument of like maturity that pays interest in arrears.

True lease A contract that qualifies as a valid lease agreement under the Internal Revenue code.

Trust deed Agreement between trustee and borrower setting out terms of bond.

Trust receipt Receipt for goods that are to be held in trust for the lender.

TT&L account Treasury tax and loan account at a bank.

Turnaround Securities bought and sold for settlement on the same day. Also, when a firm that has been performing poorly changes its financial course and improves its performance.

Turnaround time Time available or needed to effect a turnaround.

Turnkey construction contract A type of construction contract under which the construction firm is obligated to complete a project according to prespecified criteria for a price that is fixed at the time the contract is signed.

Turnover Mutual Funds: A measure of trading activity during the previous year, expressed as a percentage of the average total assets of the fund. A turnover ratio of 25% means that the value of trades represented one-fourth of the assets of the fund. Finance: The number of times a given asset, such as inventory, is replaced during the accounting period, usually a year. Corporate: The ratio of annual sales to net worth, representing the extent to which a company can growth without outside capital. Markets: The volume of shares traded as a percent of total shares listed during a specified period, usually a day or a year. Great Britain: total revenue.

12B-1 fees The percent of a mutual fund's assets used to defray marketing and distribution expenses. The amount of the fee is stated in the fund's prospectus. The SEC has recently proposed that 12B-1 fees in excess of 0.25% be classed as a load. A true " no load" fund has neither a sales charge nor 12b-1 fee.

12b-1 funds Mutual funds that do not charge an upfront or back-end commission, but instead take out up to 1.25% of average daily fund assets each year to cover the costs of selling and marketing shares, an arrangement allowed by the SEC's Rule 12b-I (passed in 1980).

Two-factor model Black's zero-beta version of the capital asset pricing model.

Two-fund separation theorem The theoretical result that all investors will hold a combination of the risk-free asset and the market portfolio.

Two-sided market A market in which both bid and asked prices, good for the standard unit of trading, are quoted.

Two-state option pricing model An option pricing model in which the underlying asset can take on only two possible (discrete) values in the next time period for each value it can take on in the preceding time period. Also called the binomial option pricing model.

Two-tier tax system A method of taxation in which the income going to shareholders is taxed twice.

Type The classification of an option contract as either a put or a call.

Unbiased predictorA theory that spot prices at some future date will be equal to today's forward rates.

Unbundling When a multinational firm unbundles its transfer of funds into separate flows for specific purposes. **See:** bundling.

Uncovered call A short call option position in which the writer does not own shares of underlying stock represented by his option contracts. Also called a "naked" call, it is much riskier for the writer than a covered call, where the writer owns the underlying stock. If the buyer of a call exercises the option to call, the writer would be forced to buy the stock at market price.

Uncovered put A short put option position in which the writer does not have a corresponding short stock position or has not deposited, in a cash account, cash or cash equivalents equal to the exercise value of the put. Also called "naked" puts, the writer has pledged to buy the stock at a certain price if the buyer of the options chooses to exercise it. The nature of uncovered options means the writer's risk is unlimited.

Underfunded pension plan A pension plan that has a negative surplus (i.e., liabilities exceed assets).

Underinvestment problem The mirror image of the asset substitution problem, wherein stockholders refuse to invest in low-risk assets to avoid shifting wealth from themselves to the debtholders.

Underlying The "something" that the parties agree to exchange in a derivative contract.

Underlying asset The asset that an option gives the option holder the right to buy or to sell.

Underlying security Options: the security subject to being purchased or sold upon exercise of an option contract. For example, IBM stock is the underlying security to IBM options. Depository receipts: The class, series and number of the foreign shares represented by the depository receipt.

Underperform When a security is expected to appreciate at a slower rate than the overall market.

Underpricing Issue of securities below their market value.

Underwrite To guarantee, as to guarantee the issuer of securities a specified price by entering into a purchase and sale agreement. To bring securities to market.

Underwriter A party that guarantees the proceeds to the firm from a security sale, thereby in effect taking ownership of the securities. Or, stated differently, a firm, usually an investment bank, that buys an issue of securities from a company and resells it to investors.

Underwriting Acting as the underwriter in a purchase and sale.

Underwriting fee The portion of the gross underwriting spread that compensates the securities firms that underwrite a public offering for their underwriting risk.

Underwriting income For an insurance company, the difference between the premiums earned and the costs of settling claims.

Underwriting syndicate A group of investment banks that work together to sell new security offerings to investors. The underwriting syndicate is led by the lead underwriter. **See also:** lead underwriter.

Underwritten offering A purchase and sale.

Undiversifiable risk Related: Systematic risk

Unemployment rate The ratio of the number of people classified as unemployed to the total labor force.

Unfunded debt Debt maturing within one year (short-term debt). **See:** funded debt.

Unilateral transfers Items in the current account of the balance of payments of a country's accounting books that corresponds to gifts from foreigners or pension payments to foreign residents who once worked in the country whose balance of payments is being considered.

Unique risk Also called unsystematic risk or idiosyncratic risk. Specific company risk that can be eliminated through diversification. **See:** diversifiable risk and unsystematic risk.

Unit benefit formula Method used to determine a participant's benefits in a defined benefit plan by multiplying years of service by the percentage of salary.

Unit investment trust Money invested in a portfolio whose composition is fixed for the life of the fund. Shares in a unit trust are called redeemable trust certificates, and they are sold at a premium above net asset value.

Universal life A whole life insurance product whose investment component pays a competitive interest rate rather than the below-market crediting rate.

Unleveraged beta The beta of an unleveraged required return (i.e. no debt) on an investment when the investment is financed entirely by equity.

Unleveraged required return The required return on an investment when the investment is financed entirely by equity (i.e. no debt).

Unlimited liability Full liability for the debt and other obligations of a legal entity. The general partners of a partnership have unlimited liability.

Unmatched book If the average maturity of a bank's liabilities is less than that of its assets, it is said to be running an unmatched book. The term is commonly used with the Euromarket. Term also refers to the condition when a firm enters into OTC derivatives contracts and chooses to hedge that risk by not making trades in the opposite direction to another financial intermediary. In this case, the firm with an unmatched book hedges its net market risk with futures and options, usually. **Related expressions:** open book and short book.

Unseasoned issue Issue of a security for which there is no existing market. **See:** seasoned issue.

Unsecured debt Debt that does not identify specific assets that can be taken over by the debtholder in case of default.

Unsterilized intervention Foreign exchange market intervention in which the monetary authorities have not insulated their domestic money supplies from the foreign exchange transactions.

Unsystematic risk Also called the diversifiable risk or residual risk. The risk that is unique to a company such as a strike, the outcome of unfavorable litigation, or a natural catastrophe that can be eliminated through diversification. **Related:** Systematic risk

Upstairs market A network of trading desks for the major brokerage firms and institutional investors that communicate with each other by means of electronic display systems and telephones to facilitate block trades and program trades.

Uptick A term used to describe a transaction that took place at a higher price than the preceding transaction involving the same security.

Uptick trade Related:Tick-test rules

U.S. Treasury bill U.S. government debt with a maturity of less than a year.

U.S. Treasury bond U.S. government debt with a maturity of more than 10 years.

U.S. Treasury note U.S. government debt with a maturity of one to 10 years.

Utility The measure of the welfare or satisfaction of an investor or person.

Utility value The welfare a given investor assigns to an investment with a particular return and risk.

Utility function A mathematical expression that assigns a value to all possible choices. In portfolio theory the utility function expresses the preferences of economic entities with respect to perceived risk and expected return.

Value-added tax Method of indirect taxation whereby a tax is levied at each stage of production on the value added at that specific stage.

Value-at-Risk model (VAR) Procedure for estimating the probability of portfolio losses exceeding some specified proportion based on a statistical analysis of historical market price trends, correlations, and volatilities.

Value additivity principal Prevails when the value of a whole group of assets exactly equals the sum of the values of the individual assets that make up the group of assets. Stated differently, the principle that the net present value of a set of independent projects is just the sum of the net present values of the individual projects.

Value date In the market for Eurodollar deposits and foreign exchange, value date refers to the delivery date of funds traded. Normally it is on spot transactions two days after a transaction is agreed upon and the future date in the case of a forward foreign exchange trade.

Value dating Refers to when value or credit is given for funds transferred between banks.

Value manager A manager who seeks to buy stocks that are at a discount to their "fair value" and sell them at or in excess of that value. Often a value stock is one with a low price to book value ratio.

Vanilla issue A security issue that has no unusual features.

Variable A value determined within the context of a model. Also called endogenous variable.

Variable annuities Annuity contracts in which the issuer pays a periodic amount linked to the investment performance of an underlying portfolio.

Variable cost A cost that is directly proportional to the volume of output produced. When production is zero, the variable cost is equal to zero.

Variable life insurance policy A whole life insurance policy that provides a death benefit dependent on the insured's portfolio market value at the time of death. Typically the company invests premiums in common stocks, and hence variable life policies are referred to as equity-linked policies.

Variable price security A security, such as stocks or bonds, that sells at a fluctuating, market-determined price.

Variable rate CDs Short-term certificate of deposits that pay interest periodically on roll dates. On each roll date, the coupon on the CD is adjusted to reflect current market rates.

Variable rated demand bond (VRDB) Floating rate bond that can be sold back periodically to the issuer.

Variable rate loan Loan made at an interest rate that fluctuates based on a base interest rate such as the Prime Rate or LIBOR.

Variance A measure of dispersion of a set of data points around their mean value. The mathematical expectation of the squared deviations from the mean. The square root of the variance is the standard deviation.

Variance minimization approach to tracking An approach to bond indexing that uses historical data to estimate the variance of the tracking error.

Variance rule Specifies the permitted minimum or maximum quantity of securities that can be delivered to satisfy a TBA trade. For Ginnie Mae, Fannie Mae, and Feddie Mac pass-through securities, the accepted variance is plus or minus 2.499999 percent per million of the par value of the TBA quantity.

Variation margin An additional required deposit to bring an investor's equity account up to the initial margin level when the balance falls below the maintenance margin requirement.

Venture capital An investment in a start-up business that is perceived to have excellent growth prospects but does not have access to capital markets. Type of financing sought by early-stage companies seeking to grow rapidly.

Vertical acquisition Acquisition in which the acquired firm and the acquiring firm are at different steps in the production process.

Vertical analysis The process of dividing each expense item in the income statement of a given year by net sales to identify expense items that rise faster or slower than a change in sales.

Vertical merger A merger in which one firm acquires another firm that is in the same industry but at another stage in the production cycle. For example, the firm being acquired serves as a supplier to the firm doing the acquiring.

Vertical spread Simultaneous purchase and sale of two options that differ only in their exercise price. See: horizontal spread.

Virtual currency option A new option contract introduced by the PHLX in 1994 that is settled in US$ rather than in the underlying currency. These options are also called 3-Ds (dollar denominated delivery).

Visible supply New muni bond issues scheduled to come to market within the next 30 days.

Volatility A measure of risk based on the standard deviation of investment fund performance over 3 years. Scale is 1-9; higher rating indicates higher risk. Also, the standard deviation of changes in the logarithm of an asset price, expressed as a yearly rate. Also, volatility is a variable that appears in option pricing formulas. In the option pricing formula, it denotes the volatility of the underlying asset return from now to the expiration of the option.

Std Deviation	**Rating**	**Std Deviation**	**Rating**
up to 7. 99	1	20. 00-22. 99	6
8. 00-10. 99	2	23. 00-25. 99	7
11. 00-13. 99	3	26. 00-28. 99	8
14. 00-16. 99	4	29. 00 and up	9
17. 00-19. 99	5		

Volatility risk The risk in the value of options portfolios due to the unpredictable changes in the volatility of the underlying asset.

Volume This is the daily number of shares of a security that change hands between a buyer and a seller.

Voting rights The right to vote on matters that are put to a vote of security holders. For example the right to vote for directors.

WACC See: Weighted average cost of capital.

Waiting period Time during which the SEC studies a firm's registration statement. During this time the firm may distribute a preliminary prospectus.

Wall Street Generic term for firms that buy, sell, and underwrite securities.

Wall Street analyst Related: Sell-side analyst.

Wallflower Stock that has fallen out of favor with investors; tends to have a low P/E (price to earnings ratio).

Wanted for cash A statement displayed on market tickers indicating that a bidder will pay cash for same day settlement of a block of a specified security.

Warehouse receipt Evidence that a firm owns goods stored in a warehouse.

Warehousing The interim holding period from the time of the closing of a loan to its subsequent marketing to capital market investors.

Warrant A security entitling the holder to buy a proportionate amount of stock at some specified future date at a specified price, usually one higher than current market. This "warrant" is then traded as a security, the price of which reflects the value of the underlying stock. Warrants are issued by corporations and often used as a "sweetener" bundled with another class of security to enhance the marketability of the latter. Warrants are like call options, but with much longer time spans **--** sometimes years. In addition, warrants are offered by corporations whereas exchange traded call options are not issued by firms.

WashGains equal losses.

Wasting asset An asset which has a limited life and thus, decreases in value (depreciates) over time. Also applied to consumed assets, such as gas, and termed "depletion."

Watch list A list of securities selected for special surveillance by a brokerage, exchange or regulatory organization; firms on the list are often takeover targets, companies planning to issue new securities or stocks showing unusual activity.

Weak form efficiency A form of pricing efficiency where the price of the security reflects the past price and trading history of the security. In such a market, security prices follow a random walk. **Related:** Semistrong form efficiency, strong form efficiency.

Weekend effect The common recurrent low or negative average return from Friday to Monday in the stock market.

Weighted average cost of capital Expected return on a portfolio of all the firm's securities. Used as a hurdle rate for capital investment.

Weighted average coupon The weighted average of the gross interest rate of the mortgages underlying the pool as of the pool issue date, with the balance of each mortgage used as the weighting factor.

Weighted average life See:Average life.

Weighted average maturity The WAM of a MBS is the weighted average of the remaining terms to maturity of the mortgages underlying the collateral pool at the date of issue, using as the weighting factor the balance of each of the mortgages as of the issue date.

Weighted average remaining maturity The average remaining term of the mortgages underlying a MBS.

Weighted average portfolio yield The weighted average of the yield of all the bonds in a portfolio.

Well diversified portfolioA portfolio spread out over many securities in such a way that the weight in any security is small. The risk of a well-diversified portfolio closely approximates the systemic risk of the overall market, the unsystematic risk of each security having been diversified out of the portfolio.

White knight A friendly potential acquirer of a firm sought out by a target firm that is threatened by a less welcome suitor.

Whole life insurance A contract with both insurance and investment components: (1) It pays off a stated amount upon the death of the insured, and (2) it accumulates a cash value that the policyholder can redeem or borrow against.

Wholesale mortgage banking The purchasing of loans originated by others, with the servicing rights released to the buyer.

Wi When issued.

Wi wi Treasury bills trade on a wi basis between the day they are auctioned and the day settlement is made. Bills traded before they are auctioned are said to be traded wi wi.

Wild card option The right of the seller of a Treasury Bond futures contract to give notice of intent to deliver at or before 8:00 p.m. Chicago time after the closing of the exchange (3:15 p.m. Chicago time) when the futures settlement price has been fixed. **Related:** Timing option.

Window contract A guaranteed investment contract purchased with deposits over some future designated time period (the "window"), usually between 3 and 12 months. All deposits made are guaranteed the same credit rating. **Related:** bullet contract.

Winners's curse Problem faced by uninformed bidders. For example, in an initial public offering uninformed participants are likely to receive larger allotments of issues that informed participants know are overpriced.

Wire house A firm operating a private wire to its own branch offices or to other firms, commission houses or brokerage houses.

With dividend Purchase of shares in which the buyer is entitled to the forthcoming dividend. **Related:** ex-dividend.

With rights Purchase of shares in which the buyer is entitled to the rights to buy shares in the company's rights issue.

Withdrawal plan The ability to establish automatic periodic mutual fund redemptions and have proceeds mailed directly to the investor.

Withholding tax A tax levied by a country of source on income paid, usually on dividends remitted to the home country of the firm operating in a foreign country. Tax levied on dividends paid abroad.

Without If 70 were bid in the market and there was no offer, the quote would be "70 bid without." The expression "without" indicates a one-way market.

Without recourse Without the lender having any right to seek payment or seize assets in the event of nonpayment from anyone other than the party (such as a special-purpose entity) specified in the debt contract.

Woody Sexual slang for a market moving strongly upward, as in, "This market has a woody."

Working capital Defined as the difference in current assets and current liabilities (excluding short-term debt). Current assets may or may not include cash and cash equivalents, depending on the company.

Working capital management The management of current assets and current liabilities to maximize short-term liquidity.

Working capital ratio Working capital expressed as a percentage of sales.

Workout Informal arrangement between a borrower and creditors.

Workout period Realignment period of a temporary misaligned yield relationship that sometimes occurs in fixed income markets.

World Bank A multilateral development finance agency created by the 1944 Bretton Woods, New Hampshire negotiations. It makes loans to developing countries for social overhead capital projects, which are guaranteed by the recipient country. **See:** International Bank for Reconstruction and Development.

World investible wealth The part of world wealth that is traded and is therefore accessible to investors.

Write-down Decreasing the book value of an asset if its book value is overstated compared to current market values.

Writer The seller of an option, usually an individual, bank, or company, that issues the option and consequently has the obligation to sell the asset (if a call) or to buy the asset (if a put) on which the option is written if the option buyer exercises the option.

W-type bottom A double bottom where the price or indicator chart has the appearance of a W. **See:** technical analysis.

Yankee bonds Foreign bonds denominated in US$ issued in the United States by foreign banks and corporations. These bonds are usually registered with the SEC. For example, bonds issued by originators with roots in Japan are called Samurai bonds.

Yankee CD A CD issued in the domestic market, typically New York, by a branch of a foreign bank.

Yankee market The foreign market in the United States.

Yard Slang for one billion dollars. Used particularly in currency trading, e.g. for Japanese yen since on billion yen only equals approximately US$10 million. It is clearer to say, " I'm a buyer of a yard of yen," than to say, "I'm a buyer of a billion yen," which could be misheard as, "I'm a buyer of a million yen."

Yield The percentage rate of return paid on a stock in the form of dividends, or the effective rate of interest paid on a bond or note.

Yield curve The graphical depiction of the relationship between the yield on bonds of the same credit quality but different maturities. **Related:** Term structure of interest rates. Harvey (1991) finds that the inversions of the yield curve (short-term rates greater than long term rates) have preceded the last five U.S. recessions. The yield curve can accurately forecast the turning points of the business cycle.

Yield curve option-pricing models Models that can incorporate different volatility assumptions along the yield curve, such as the Black-Derman-Toy model. Also called arbitrage-free option-pricing models.

Yield curve strategies Positioning a portfolio to capitalize on expected changes in the shape of the Treasury yield curve.

Yield ratio The quotient of two bond yields.

Yield spread strategies Strategies that involve positioning a portfolio to capitalize on expected changes in yield spreads between sectors of the bond market.

Yield to call The percentage rate of a bond or note, if you were to buy and hold the security until the call date. This yield is valid only if the security is called prior to maturity. Generally bonds are callable over several years and normally are called at a slight premium. The calculation of yield to call is based on the coupon rate, length of time to the call and the market price.

Yield to maturity The percentage rate of return paid on a bond, note or other fixed income security if you buy and hold it to its maturity date. The calculation for YTM is based on the coupon rate, length of time to maturity and market price. It assumes that coupon interest paid over the life of the bond will be reinvested at the same rate.

Yield to worst The bond yield computed by using the lower of either the yield to maturity or the yield to call on every possible call date.

Z bond Also known as an accrual bond or accretion bond; a bond on which interest accretes interest but is not paid currently to the i nvestor but rather is accrued, with accrual added to the principal balance of the Z and becoming payable upon satisfaction of all prior bond classes.

Z score Statistical measure that quantifies the distance (measured in standard deviations) a data point is from the mean of a data set. Separately, z score is the output from a credit-strength test that gauges the likelihood of bankruptcy.

Zero coupon bond Such a debt security pays an investor no interest. It is sold at a discount to its face price and matures in one year or longer.

Zero prepayment assumption The assumption of payment of scheduled principal and interest with no payments.

Zero uptick Related: tick-test rules.

Zero-balance account (ZBA) A checking account in which zero balance is maintained by transfers of funds from a master account in an amount only large enough to cover checks presented.

Zero-beta portfolio A portfolio constructed to represent the risk-free asset, that is, having a beta of zero.

Zero-coupon bond A bond in which no periodic coupon is paid over the life of the contract. Instead, both the principal and the interest are paid at the maturity date.

Zero-investment portfolio A portfolio of zero net value established by buying and shorting component securities, usually in the context of an arbitrage strategy.

Zero-one integer programming An analytical method that can be used to determine the solution to a capital rationing problem.

Zero-sum game A type of game wherein one player can gain only at the expense of another player.