access
PRIVATE BANK

GLOSSARY
OF INVESTMENT TERMS

A

Absolute Return — Absolute return funds look to make positive returns whether the overall market is up or down, while index tracking funds try to beat the index they are tracking. Absolute return differs from relative return because it is concerned with the return of the asset being looked at and does not compare it to any other measure.

Alpha — 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 0.3 means the fund outperformed the benchmark by 0.3%. An alpha of −0.5 means a fund's return was 0.5% less than would have been predicted from the change in the benchmark alone.

Alternative Assets — Includes private real estate, public real estate, venture capital, non-venture private equity, hedge funds, distressed securities, oil and gas partnerships, event arbitrage, general arbitrage, managed funds, commodities, timber and other.

Annual Rate of Return — There are several ways of calculating this. The most commonly used methodologies reflect the compounding effect of each period's increase or decrease from the previous period.

Arbitrage — A financial transaction or strategy that seeks to profit from a differential price perceived with respect to related or correlated instruments in different markets and typically involves the simultaneous purchase of an instrument in one market and the sale of the same or related instrument in another market.

Asset Allocation — The process of apportioning investment funds among categories of assets such as cash equivalents, stock, fixed income investments, alternative investments such as hedge funds and managed futures funds, and tangible assets like real estate, precious metals and collectibles.

B

Basis Point — A basis point is one one-hundredth of a percent i.e. 50 basis points or "bps" is 0.5%.

Bear / Bear Market — Bear is a term describing an investor who thinks that a market will decline. The term also refers to a short position held by a market maker. A Bear Market is a market where prices are falling over an extended period.

Beta — The Beta measures the extent to which a fund (or security) will move in relation to market movements. A beta value of 1.1 indicates a 1.10% movement in the fund or security for a 1% move in the index, regardless of direction.

Bid Price — The price at which an investor may sell units of a fund back to the fund manager. It is also the price at which you can sell shares in the stock market.

Blue Chip Stock — Shares in the largest companies in the stock market, which are often presumed to be among the safer share investments on an exchange.

Bond — A debt investment, with which the investor loans money to an entity (company or government) that borrows the funds for a defined period of time at a specified interest rate. The company or government issues investors a certificate, or bond, that states the interest rate (coupon rate) that will be paid and when the loaned funds are to be returned (maturity date). Interest on bonds is usually paid every six months (semi-annually).

Bond Rating Codes — Rating agencies such as S&P or Moody's analyse companies and give them a rating on their financial strength and the likelihood of them failing to pay interest or capital on the debt instruments (Bonds)

	S&P	Moody's
Highest quality	AAA	Aaa
High quality	AA	Aa
Upper medium quality	A	A
Medium grade	BBB	Baa
Somewhat speculative	BB	Ba
Low grade, speculative	B	B
Low grade, default possible	CCC	Caa
Low grade, partial recovery possible	CC	Ca
Default, recovery unlikely	C	C

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B

Bottom up Investing An approach to investing which seeks to identify well performing individual securities before considering the impact of economic trends. This approach pays less attention to asset allocation.

BRIC A term used to refer to the combination of Brazil, Russia, India and China. General consensus is that the term was first prominently used in a thesis of the Goldman Sachs Investment Bank. The main point of this 2003 paper was to argue that the economies of the BRICs are rapidly developing and by the year 2050 will eclipse most of the current richest countries of the world. Due to the popularity of the Goldman Sachs thesis, "BRIC" and "BRIMC" (M for Mexico), these terms are also extended to "BRICS" (S for South Africa) and "BRICKET" (including Eastern Europe and Turkey) and have become more generic terms to refer to these emerging markets.

Bull / Bull Market An investor who believes that the market is likely to rise. A Bull Market is a market where prices are rising over an extended period.

C

Call Option An option giving the holder the right, but not the obligation, to buy a specific quantity of an asset for a fixed price during a specific period.

Closed-end Fund Type of fund that has a fixed number of shares or units. Unlike open-ended mutual funds, closed-end funds do not stand ready to issue and redeem shares on a continuous basis. As such, their shares or units can often trade at discounts or premiums to their net asset value.

Convertible Arbitrage This is a hedge fund investment strategy that involves taking a long position on a convertible security and a short position in its converting common stock. This strategy attempts to exploit profits when there is a pricing error made in the conversion factor of the convertible security.

Convertible Bond A bond that can be exchanged, at the option of the holder, for a specific number of shares of the company's underlying shares. Convertibility affects the performance of the bond in certain ways. First and foremost, convertible bonds tend to have lower interest rates than non-convertibles because they also accrue value as the price of the underlying stock rises. In this way, convertible bonds offer some of the benefits of both stocks and bonds. Convertibles earn interest even when the stock is trading down or sideways, but when the stock prices rise, the value of the convertible increases. Therefore, convertibles can offer protection against a decline in stock price. Because they are sold at a premium over the price of the stock, convertibles should be expected to earn that premium back in the first three or four years after purchase.

Correlation A standardised measure of the relative movement between two variables, such as the price of a fund and an index. The degree of correlation between two variables is measured on a scale of −1 to +1. If two variables move up or down together, they are positively correlated. If they tend to move in opposite directions, they are negatively correlated.

Coupon Denotes the rate of interest on a fixed interest security (or bond). A 10 % coupon pays interest of 10 % a year on the nominal value of the stock.

Cyclical Stock The stock or shares of a company which is sensitive to business cycles and whose performance is strongly tied to the overall economy. Cyclical companies tend to make products or provide services that are in lower demand during downturns in the economy and higher demand during upswings. Examples include the automobile, steel, and housing industries. The stock price of a cyclical company will often rise just before an economic upturn begins, and fall just before a downturn begins. Investors in cyclical stocks try to make the largest gains by buying the stock at the bottom of a business cycle, just before a turnaround begins. Opposite of defensive stock.

D

Debenture A loan raised by a company, paying a fixed rate of interest and secured on the assets of the company. It is another word for a bond or debt instrument.

Defensive Stock A stock that tends to remain stable under difficult economic conditions. Defensive stocks can include food, tobacco and utilities. These stocks hold up in hard times because demand does not decrease as dramatically as it may in other sectors. Defensive stocks tend to lag behind the rest of the market during economic expansion because demand does not increase as dramatically in an upswing.

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D

Derivatives	Financial contracts whose value is tied to an underlying asset. Derivatives include futures and options.
Distressed Securities	A distressed security is a security of a company which is currently in default, bankruptcy, financial distress or a turnaround situation.
Diversification	An investment strategy that involves buying a variety of investment instruments that are not highly correlated to each other in order to reduce the risk of an overall portfolio. It is the product of the asset allocation process.
Due Diligence	Process of evaluating the soundness of an investment.
Draw-Down	The decline in value of an investment, from peak to trough, over a given period.

E

Efficient Frontier	The efficient frontier represents a series of optimal portfolios that have the highest return for given amounts of risk, normally calculated using a range of risk levels from low to high risk.
Emerging Markets	Typically includes markets within countries that have an underdeveloped or developing infrastructure with significant potential for economic growth and increased capital market participation for foreign investors. These countries generally possess some of the following characteristics; per capita GNP less than $9,000, recent economic liberalisation, debt ratings below investment grade, recent liberalisation of the political system and non membership of the Organisation of Economic Cooperation and Development. Because many emerging countries do not allow short selling or offer viable futures or other derivatives products with which to hedge, emerging market investing entails investing in geographic regions that have underdeveloped capital markets and exhibit high growth rates and high rates of inflation. Investing in emerging markets can be very volatile and may also involve currency risk, political risk and liquidity risk. Generally a long-only investment strategy.
Emerging Markets Debt	Debt instruments of emerging market countries and their companies. Most bonds are US Dollar denominated.
Equities	Ownership positions in companies that can be traded in public markets. Often produce current income which is paid in the form of quarterly dividends. In the event of the company going bankrupt equity holders' claims are subordinate to the claims of preferred stockholders and bondholders.
Equity Hedge	Also known as long / short equity, these are hedge funds that combine core long holdings of equities with short sales of stock or stock index options. Equity hedge portfolios may be anywhere from net long to net short depending on market conditions. Equity hedge managers generally increase net long exposure in bull markets and decrease net long exposure or are even net short in a bear market.
Equity Market Neutral	This investment strategy is designed to exploit equity market inefficiencies and usually involves a hedge fund being simultaneously long and short equity portfolios of the same size within a country. Market neutral portfolios are designed to be either beta or currency neutral or both. Attempts are often made to control industry, sector and market capitalisation exposures. The strategy is designed to achieve returns regardless of the direction of the market.
Equity Risk	The risk of owning stock or shares or having some other form of ownership interest.
EU	European Union. The economic association of over 25 European countries which seek to create a unified, barrier-free market for products and services throughout the continent. The majority of countries share a common currency with a unified authority over that currency. Notable exceptions to the common currency are the UK, Sweden, Norway, Denmark.
Eurobond	A bond issued and traded outside the country whose currency it is denominated in, and outside the regulations of a single country; usually a bond issued by a non-European company for sale in Europe. Interest is paid gross.
Eurozone or Euroland	The collective group of countries which use the Euro as their common currency.
Exposure	The condition of being subjected to a source of risk.

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F

Fixed Income Arbitrage	Investment strategy that seeks to exploit pricing inefficiencies in fixed income securities and their derivative instruments. Typical investment is long a fixed income security or related instrument that is perceived to be undervalued and short a similar related fixed income security or related instrument. Hedge funds that employ this type of strategy are often highly leveraged (borrowed) because the relative returns are very small.
Floating Rate	Any interest rate that changes on a periodic basis. The change is usually tied to movement of an outside indicator, such as the Bank of England Base Rate. Movement above or below certain levels is often prevented by a predetermined floor and ceiling for a given rate. For example, you might see a rate set at "base plus 2%". This means that the rate on the loan will always be 2% higher than the base rate, which changes regularly to take into account changes in the inflation rate. For an individual taking out a loan when rates are low, a fixed rate loan would allow him or her to "lock in" the low rates and not be concerned with fluctuations. On the other hand, if interest rates were historically high at the time of the loan, he or she would benefit from a floating rate loan, because as the prime rate fell to historically normal levels, the rate on the loan would decrease. Also called adjustable rate.
Forward	An agreement to execute a transaction at some time in the future. In the foreign exchange market this is a tailor made deal where an investor agrees to buy or sell an amount of currency at a given date, often at the point that the investor requires the currency.
FTSE 100	The Financial Times Stock Exchange 100 stock index, a market cap weighted index of stocks traded on the London Stock Exchange. Similar to the S&P 500 in the United States.
Fund of Funds	An investment vehicle (fund) that invests in more than one fund. A portfolio will typically diversify across a variety of investment managers, investment strategies and subcategories. It provides investors with access to managers with higher minimums than individuals might otherwise afford.
Futures Markets	Exchanges where futures contracts are traded. Different exchanges specialise in particular kinds of contracts. Major exchanges include the Commodity Exchange, the New York Mercantile Exchange, the Chicago Board of Trade and the Chicago Mercantile Exchange.

G

Gearing	The effect that borrowing has on the equity capital of a company or the asset value of a fund. If the assets bought with funds borrowed appreciate in value, the excess of value over funds borrowed will accrue to the shareholder, thus augmenting, or gearing up the value of their investment.
Geographic Spread	The distribution in a fund's portfolio over different parts of the world, either by countries or larger regions.
Gilt-Edged Securities	Stocks and shares issued and guaranteed by the British government to raise funds and traded on the Stock Exchange. A relatively low-risk investment, gilts bear fixed interest and are usually redeemable on a specified date. The term is now used generally to describe securities of the highest value. According to the redemption date, gilts are described as short (up to five years), medium, or long (15 years or more).
GNMA (Ginnie Mae)	Government National Mortgage Association. A U.S. Government-owned agency which buys mortgages from lending institutions, and then sells them to investors. Because the payments to investors are guaranteed by the full faith and credit of the U.S. Government, they return slightly less interest than other mortgage-backed securities. These securities were at the heart of the credit crunch in the US where their value was severely affected by the collapse in US house prices.
Growth Stocks	Stock of a company which is growing earnings and/or revenue faster than its industry or the overall market. Such companies usually pay little or no dividends, preferring to use the income instead to finance further expansion.
Global Macro	This hedge fund investment strategy is based on shifts in global economies. Derivatives are often used to speculate on currency and interest rate movements.

H

Hedge	Any transaction with the objective of limiting exposure to risk such as changes in exchange rates or prices.

H

Hedge Fund	A pooled investment vehicle that is privately organised, administered by investment management professionals and generally not widely available to the general public. Many hedge funds share a number of characteristics; they hold long and short positions, use leverage to enhance returns, pay performance or incentive fees to their managers, have high minimum investment requirements and target absolute returns. Generally, hedge funds are not constrained by legal limitations on their investment discretion and can adopt a variety of trading strategies. The hedge fund manager often has its own capital (or that of its principals) invested in the hedge fund it manages.
High Water Mark	The assurance that a fund only takes fees on profits actually earned by an individual investment. For example, a £10 million investment is made in year one and the fund declines by 50%, leaving £5 million in the fund. In year two, the fund returns 100% bringing the investment value back to £10 million. If a fund has a high water mark it will not take incentive fees on the return in year two since the investment has never grown. The fund will only take incentive fees if the investment grows above the initial level of £10 million.
High-Yield Bond	Often called junk bonds, these are low grade (i.e. S&P or Moody's rated) fixed income securities of companies. The bond has to pay a high yield due to significant credit risk.
Hurdle Rate	The minimum investment return a fund must exceed before a performance-based incentive fee can be taken. For example if a fund has a hurdle rate of 10% and the fund returned 18% for the year, the fund will only take incentive fees on the 8 percentage points above the hurdle rate.

I

Index	An arithmetic mean of selected stocks intended to represent the behaviour of the market or some component of it. One example is the FTSE 100 which adds the current prices of the one hundred FTSE 100 stocks and divides the results by a pre-determined number, the divisor.
Index Funds	A fund that attempts to achieve a performance similar to that stated in an index. The purpose of this fund is to realise an investment return at least equal to the broad market covered by the indices while reducing management costs.
Index Linked Gilt	This is a security like a gilt, but where the interest and capital change in line with the Retail Price Index. This means that the investment provides a virtually guaranteed return over inflation as long as it is held to redemption.
Investment Grade	Something classified as investment grade is, by implication, medium to high quality. 1) In the case of a stock, a firm that has a strong balance sheet, considerable capitalization, and is recognized as a leader in its industry. 2) In the case of fixed income, a bond with a rating of BBB or higher.

J

Junk Bond	A bond that pays a high yield due to significant credit risk.

L

Leverage	When investors borrow funds to increase the amount they have invested in a particular position, they use leverage. Sometimes managers use leverage to enable them to put on new positions without having to take off other positions prematurely. Managers who target very small price discrepancies or spreads will often use leverage to magnify the returns from these discrepancies. Leverage both magnifies the risk of the strategy as well as creates risk by giving the lender power over the disposition of the investment portfolio. This may occur in the form of increased margin requirements or adverse market shifts, forcing a partial or complete liquidation of the portfolio. The amount of leverage used by the fund is commonly expressed as a percentage of the fund. For example if the fund has £1 million and borrows another £2 million to bring the total invested to £3 million, then the fund is leveraged 200%.

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L

LIBOR	London Inter Bank Offered Rate. This is seen as the market standard index for short-term money market interest rates.
Liquidity	1) The degree to which an asset or security can be bought or sold in the market without affecting the asset's price. Liquidity is characterized by a high level of trading activity. 2) The ability to convert an asset to cash quickly. Investing in illiquid assets is riskier because there might not be a way for you to get your money out of the investment. Examples of assets with good liquidity include blue chip common stock and those assets in the money market. A fund with good liquidity would be characterised by having enough units outstanding to allow large transactions without a substantial change in price.
Liquidity Risk	Risk from a lack of liquidity, i.e. an investor having difficulty getting their money out of an investment.
Listed Security	Stock or bond that has been accepted for trading by an organised and registered securities exchange. Advantages of being listed are an orderly market place, more liquidity, fair price determination, accurate and continuous reporting on sales and quotations, information on listed companies and strict regulations for the protection of securities holders.
Long Position	Holding a positive amount of an asset (or an asset underlying a derivative instrument).
Long / Short Hedged	A hedge fund buys securities it believes will go up in price and sells short securities it believes will decline in price. The fund will be either net long or net short and may change the net position frequently. For example a hedge fund may be 60% long and 100% short, giving him a market exposure of 40% net short. The basic belief behind this strategy is that it will enhance the manager's stock picking ability and protect investors in all market conditions.

M

Macro-Economics	The field of economics that studies the behaviour of the economy as a whole. Macroeconomics looks at economy-wide phenomena such as changes in unemployment, national income, rate of growth, and price levels.
Management Fee	The fees taken by the manager on the entire asset level of the investment. For example, if at the end of the period the investment is valued at £1 million and the management fee is 1.2%, then the fee would be £12,000.
Market Maker	An Exchange member firm that is obliged to make a continuous two way price, that is to offer to buy and sell securities in which it is registered throughout the mandatory quote period.
Market Neutral Investing	A hedge fund investment strategy that aims to produce almost the same profit regardless of market circumstances, often by taking a combination of long and short positions. This approach relies on the manager's ability to make money through relative valuation analysis, rather than through market direction forecasting. The strategy attempts to eliminate market risk and be profitable in any market condition.
Market Risk	Risk from changes in market prices. It is not possible to invest without market risk.
Market Timing	An accepted practice of allocating assets among investments by switching into investments that appear to be beginning an uptrend, and switching out of investments that appear to be starting a downtrend.
Market Value	The value at which an asset traded, or would trade in the market at a specific point in time.
Maximum Draw Down	The largest loss suffered by a security or fund, peak to trough, over a given period.
Micro-Economics	A branch of economic that studies the behaviour and purchasing decisions of individuals and firms rather than the whole economy
Money Market Funds	Mutual funds that invest in short term highly liquid money market instruments. These funds are used when preservation of capital is paramount. They may be used to "park" money between investments, especially during periods of market uncertainty.

M

Mortgage Backed Security	A pass-through security that aggregates a pool of mortgage-backed debt obligations. Mortgage-backed securities' principal amounts are usually government guaranteed. Homeowners' principal and interest payments pass from the originating bank through a government agency or investment bank, to investors, net of a loan servicing fee payable to the originator.
Mutual Fund	A security that gives small investors access to a well diversified portfolio of equities, bonds, and other securities. Each shareholder participates in the gain or loss of the fund. Shares are issued and can be redeemed as needed. The fund's net asset value (NAV) is determined each day. Each mutual fund portfolio is invested to match the objective stated in the prospectus. Some examples of mutual funds are UK Unit Trusts, Open-ended Investment Companies (OEICs), EU registered UCITS, Luxembourg based SICAVs.

N

Net Asset Value (NAV)	NAV equals the closing market value of all assets within a portfolio after subtracting all liabilities including accrued fees and expenses. NAV per share is the NAV divided by the number of shares in issue. This is often used as the price of a fund.
Nominee Name	Name in which a security is registered and held in trust on behalf of the beneficial owner (the client).

O

OEICs	An OEIC or Open Ended Investment Company is a company (rather than a fund) that is structured to invest in other companies. These are open ended, which means that they can adjust the amount of shares in the fund by either issuing or eliminating shares. When an investor places money with the OEIC, the company issues shares, receives money and invests it. When an investor decides to sell his shares, the company eliminates the shares and pays out money to the investor.
Offer Price	The price at which a fund manager or market maker will sell shares to you (i.e. offer them to you). The offer price is higher than the Bid Price which is the price at which they will buy shares from you (i.e. they will make a bid). This is one way in which a market maker turns a profit. A fund manager may use the difference to cover dealing administration costs.
Offshore	Located or based outside of one's national boundaries. These locations may have preferential tax treatments and fund legislation.
Open-ended Funds	These are funds where units or shares can be bought and sold daily and where the number of units or shares in issue can vary daily.
Option	A privilege sold by one party to another that offers the buyer the right, but not the obligation, to buy (call) or sell (put) a security at an agreed-upon price during a certain period of time or on a specific date. Options are extremely versatile securities that can be used in many different ways. Traders use options to speculate, which is a relatively risky practice, while hedgers use options to reduce the risk of holding an asset.
Overweight	Refers to an investment position that is larger than the generally accepted benchmark. For example, if a company normally holds a portfolio whose weighting of cash is 10%, and then increases cash holdings to 15%, the portfolio would have an overweight position in cash.

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P

Pair Trading — This is a strategy often used by Hedge Funds which matches a long position with a short position in two stocks of the same sector. This creates a hedge against the sector and the overall market that the two stocks are in. The hedge created is essentially a bet that you are placing on the two stocks; the stock you are long in versus the stock you are short in. If the market or the sector moves in one direction or the other, the gain on the long stock is offset by a loss on the short.

Performance Fee — The fee payable to the fund adviser on new profits earned by the fund for the period.

Premium — The difference between the higher price paid for a fixed-income security and the security's face amount at issue. If a fixed-income security (bond) is purchased at a premium, existing interest rates are lower than the coupon rate. Investors pay a premium for an investment that will return an amount greater than existing interest rates.

The total cost of an option. The premium of an option is the sum of the option's intrinsic and time value. It is important to note that volatility also affects the premium.

Price Earnings Ratio (P/E Ratio) — A valuation ratio of a company's current share price compared to its per-share earnings.

Calculated as : Market Value per Share divided by Earnings per Share (EPS)

EPS is usually from the last four quarters (trailing P/E), but sometimes can be taken from the estimates of earnings expected in the next four quarters (projected or forward P/E). A third variation is the sum of the last two actual quarters and the estimates of the next two quarters. Sometimes the P/E is referred to as the "multiple," because it shows how much investors are willing to pay per dollar of earnings. In general, a high P/E means high projected earnings in the future. However, the P/E ratio actually doesn't tell us the whole story by itself. It's usually only useful to compare the P/E ratios of companies in the same industry, or to the market in general, or against the company's own historical P/E.

Private Placement / Private Equity — When equity capital is made available to companies or investors, but not quoted on a stock market. The funds raised through private equity can be used to develop new products and technologies, to expand working capital, to make acquisitions, or to strengthen a company's balance sheet. The average individual investor will not have access to private equity because it requires a very large investment. The result is the sale of securities to a relatively small number of investors. Private placements do not have to be registered with organizations such as the FSA SEC because no public offering is involved.

Prospectus — In the case of mutual funds, a prospectus describes the fund's objectives, history, manager background, and financial statements. A prospectus makes investors aware of the risks of an investment and in most jurisdictions is required to be published by law.

Protected Cell Company — A standard limited company that has been separated into legally distinct portions or cells. The revenue streams, assets and liabilities of each cell are kept separate from all other cells. Each cell has its own separate portion of the PCC's overall share capital, allowing shareholders to maintain sole ownership of an entire cell while owning only a small proportion of the PCC as a whole. PCCs can provide a means of entry into captive insurance market to entities for which it was previously uneconomic. The overheads of a protected cell captive can be shared between the owners of each of the cells, making the captive cheaper to run from the point of view of the insured.

Put Option — An option giving the holder the right, but not the obligation, to sell a specific quantity of an asset for a fixed price during a specific period.

Q

Qualitative Analysis — Analysis that uses subjective judgment in evaluating securities based on non-financial information such as management expertise, cyclicality of industry, strength of research and development, and labour relations.

Quantitative Analysis — A security analysis that uses financial information derived from company annual reports and income statements to evaluate an investment decision. Some examples are financial ratios, the cost of capital, asset valuation, and sales and earnings trends.

It can also mean statistical analysis of past performance of fund managers to try and find the characteristics of each manager and predict which managers are likely to outperform over the longer-term.

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R

REIT	Real Estate Investment Trust – A security that trades like a stock on the major exchanges and invests in real estate directly, either through properties or mortgages. REITs receive special tax considerations and typically offer investors high yields, as well as a highly liquid method of investing in real estate. Equity REITs invest in and own properties (thus responsible for the equity or value of their real estate assets). Their revenues come principally from their properties' rents. Mortgage REITs deal in investment and ownership of property mortgages. These REITs loan money for mortgages to owners of real estate, or purchase existing mortgages or mortgage-backed securities. Their revenues are generated primarily by the interest that they earn on the mortgage loans. Hybrid REITs combine the investment strategies of equity REITs and mortgage REITs by investing in both properties and mortgages.
Risk Adjusted Rate of Return	A measure of how much risk a fund or portfolio took on to earn its returns, usually expressed as a number or a rating. This is often represented by the Sharpe Ratio. The more return per unit of risk, the better.
Risk Arbitrage	A broad definition for three types of arbitrage that contain an element of risk that are often used by hedge funds: 1) Merger and Acquisition Arbitrage - The simultaneous purchase of stock in a company being acquired and the sale (or short sale) of stock in the acquiring company. 2) Liquidation Arbitrage - The exploitation of a difference between a company's current value and its estimated liquidation value. 3) Pairs Trading - The exploitation of a difference between two very similar companies in the same industry that have historically been highly correlated. When the two company's values diverge to a historically high level you can take an offsetting position in each (e.g. go long in one and short the other) because, as history has shown, they will inevitably come to be similarly valued. In theory, true arbitrage is riskless, however, the world in which we operate offers very few of these opportunities. Despite these forms of arbitrage being somewhat risky, they are still relatively low-risk trading strategies which money managers (mainly hedge fund managers) and retail investors alike can employ.
Risk-Free Rate	The quoted rate on an asset that has virtually no risk. The rate quoted for US treasury or UK Government Treasury bills are widely used as the risk free rate.

S

Secondary Market	A market in which an investor purchases an asset from another investor, rather than an issuing corporation. A good example is the London Stock Exchange. All stock exchanges are part of the secondary market, as investors buy securities from other investors instead of an issuing company.
Sector Fund	A mutual fund whose objective is to invest in a particular industry or sector of the economy to capitalize on returns. Because most of the stocks in this type of fund are all in the same industry, there is a lack of diversification. The fund tends to do very well or not well at all, depending on the conditions of the specific sector.
Securities	General name for all stocks, bonds and shares of all types.
SICAV	SICAV stands for Societe D'Investissement a Capital Variable. It is a Luxembourg incorporated company that is responsible for the management of a mutual fund and manages a portfolio of securities. The share capital is equal to the net assets of the fund. The units in the portfolio are delivered as shares and the investors are referred to as shareholders. SICAVs are common fund structures in Luxembourg.
Shares	Ownership positions in companies that can be traded in public markets. Often produce current income which is paid in the form of quarterly dividends. In the event of the company going bankrupt equity holders' claims are subordinate to the claims of preferred stockholders and bondholders.
Sharpe Ratio	A ratio to measure risk-adjusted performance. It is calculated by subtracting the risk free rate from the rate of return for a portfolio and dividing the result by the standard deviation of the portfolio returns. The Sharpe ratio tells us whether the returns of a portfolio are because of investment decisions or a result of excess risk.

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S

Short Selling	The selling of a security that the seller does not own, or any sale that is completed by the delivery of a security borrowed by the seller. Short sellers assume that they will be able to buy the stock at a lower amount than the price at which they sold short. Selling short is the opposite of going long. That is, short sellers make money if the stock goes down in price. This is an advanced trading strategy with many unique risks and pitfalls.
Small Caps	Stocks or funds with smaller capitalisation. They tend to be less liquid than blue chips, but they tend to have higher returns.
Sovereign Debt	A debt instrument guaranteed by a government.
Specific Risk	Risk that affects a very small number of assets. This is sometimes referred to as "unsystematic risk." An example would be news that is specific to either one stock or a small number of stocks, such as a sudden strike by the employees of a company or a new governmental regulation affecting a particular group of companies. Unlike systematic risk or market risk, specific risk can be diversified away.
Spread	1) The difference between the bid and the offer prices of a security or asset. 2) An option position established by purchasing one option and selling another option of the same class, but of a different series.
Standard Deviation	Tells us how much the return on the fund or security is deviating from the average returns over the period selected.
Strike Price	The stated price per share for which underlying stock may be purchased (for a call) or sold (for a put) by the option holder upon exercise of the option contract.
Swap	Traditionally, the exchange of one security for another to change the maturity (bonds), quality of issues (stocks or bonds), or because investment objectives have changed. Recently, swaps have grown to include currency swaps and interest rates swaps. If firms in different countries have comparative advantages on interest rates, then a swap could benefit both firms. For example, one firm may have a lower fixed interest rate, while another has access to a lower floating interest rate. These firms could swap to take advantage of the lower rates.
Systematic Risk	The risk inherent to the entire market or entire market segment. Also known as "un-diversifiable risk" or "market risk." interest rates, recession and wars all represent sources of systematic risk because they will affect the entire market and cannot be avoided through diversification. Whereas this type of risk affects a broad range of securities, unsystematic risk affects a very specific group of securities or an individual security. Systematic risk can be mitigated only by being hedged.
Systemic Risk	Risk that threatens an entire financial system.
S&P500	Standard & Poor's Index of the New York Stock Exchange. A basket of 500 stocks that are considered to be widely held. The S&P 500 index is weighted by market value, and its performance is thought to be representative of the stock market as a whole.

T

Treasury Bill "Treasury"	A negotiable debt obligation issued by a government and backed by its full faith and credit, having a maturity of one year or less. Exempt from state and local taxes. Also called Bill or T-Bill or Treasury Bill.
Time Value	The amount by which an option's premium exceeds its intrinsic value. Also called time premium.
Top-Down Investing	An investment strategy which first finds the best asset classes, geographic regions, sectors or industries to invest in, and then searches for the best companies or funds within those sectors or industries. This investing strategy begins with a look at the overall economic picture and then narrows it down to areas that are expected to perform well. Analysis of the fundamentals of a given security is the final step.
Traded Options	Transferable options with the right to buy or sell a standardised amount of a security at a fixed price within a specified period.
Traditional Investments	Includes cash, equities and bonds.

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U

Underlier or Underlying Security	A security or commodity which is subject to delivery upon exercise of an option contract or convertible security. Exceptions include index options and futures, which cannot be delivered and are therefore settled in cash.
Underweight	A situation where a portfolio does not hold a sufficient amount of securities to satisfy the accepted benchmark of the portfolio's asset allocation strategy. For example, if a portfolio normally holds 40% stock and currently holds 30%, the position in equities would be considered underweight.
Unit Trust	A common form of collective investment (similar to a mutual fund) where investors' money is pooled and invested into a variety of shares and bonds in order to reduce risk. Its capital structure is open ended as units can be created or redeemed, depending on demand from investors. It should be noted that a Unit Trust means something completely different in the US.

V

Value Stocks	Stocks which are perceived to be selling at a discount to their intrinsic or potential worth, ie undervalued; or stocks which are out of favour with the market and are under-followed by analysts. It is believed that the share price of these stocks will increase as the value of the company is recognised by the market.
Venture Capital	Money and resources made available to start-up firms and small businesses with exceptional growth potential. Venture capital often also includes managerial and technical expertise. Most venture capital money comes from an organized group of wealthy investors who seek substantially above average returns and who are willing to accept correspondingly high risks. This form of raising capital is increasingly popular among new companies that, because of a limited operating history, can't raise money through a debt issue. The downside for entrepreneurs is that venture capitalists usually receive a say in the major decisions of the company in addition to a portion of the equity.
Volatility	The relative rate at which the price of a security or fund moves up and down. Volatility is found by calculating the annualised standard deviation of daily change in price. If the price of a stock moves up and down rapidly over short time periods, it has high volatility. If the price almost never changes, it has low volatility.

W

Warrants	A certificate usually issued along with a bond or preferred stock, entitling the holder to buy a specific amount of securities at a specific price, usually above the current market price at the time of issuance, for an extended period, anywhere from a few years to forever. In the case that the price of the security rises to above that of the warrant's exercise price, then the investor can buy the security at the warrant's exercise price and resell it for a profit. Otherwise, the warrant will simply expire or remain unused. The main difference between warrants and call options is that warrants are issued and guaranteed by the company, whereas options are exchange instruments and not issued by the company. Also, the lifetime of a warrant is often measured in years, while the lifetime of a typical option is measured in months. Warrants are often included in a new debt issue as a "sweetener" to entice investors.
Withholding Tax	Tax deducted from dividends which are paid to investors who are non-residents. Tax can often be reclaimed if there is a double taxation agreement with the investor's country.

Y

Yield	1) The annual rate of return on an investment, expressed as a percentage. 2) For bonds and notes, the coupon rate divided by the market price. This is not an accurate measure of total return, since it does not factor in capital gains. 3) For securities, the annual dividends divided by the purchase price. This is not an accurate measure of total return, since it does not factor in capital gains. Also called dividend yield or current yield.
Yield Curve	A curve that shows the relationship between yields and maturity dates for a set of similar bonds, usually Treasuries, at a given point in time.

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Z

Zero Coupon Bond	A bond which pays no coupons, is sold at a deep discount to its face value, and matures at its face value. A zero-coupon bond has the important advantage of being free of reinvestment risk, though the downside is that there is no opportunity to enjoy the effects of a rise in market interest rates. Also, such bonds tend to be very sensitive to changes in interest rates, since there are no coupon payments to reduce the impact of interest rate changes. In addition, markets for zero-coupon bonds are relatively illiquid.