Glossary

acid test: a check in the company's balance sheet to see if it has enough liquid assets to meet its current debts.

Alternative Investment Market: the part of the London Stock Exchange for small companies or ones too young to meet the requirements for full quotation; often abbreviated to Aim.

assets: in a company's balance sheet these are the things it owns or are owed to it; net assets in the balance sheet are defined as capital plus reserves, or total assets minus current liabilities, and deducting the long-term creditors.

authorized share capital: every company has a memorandum and articles of association and these show how many shares it may issue. It is not compelled to issue all of them and many companies keep some in reserve for rights issues, employee incentives and the like (*see also* issued share capital).

bear market: a time of generally falling share prices.

bid: the price at which the managers of unit trusts will buy back the units from investors, compared with the offer at which they sell units; also loosely used for the offer in a takeover.

blue chip: a top-quality company and its shares, derived from the top-value gaming chips used in casinos and poker.

bond: an IOU issued by a borrower to the lender to acknowledge the debt; it normally carries a fixed rate of interest and can be traded (eg gilts, debentures).

bonus issue: another name for a scrip issue; the distribution of shares to existing holders at no cost to them.

broker: *see* stockbroker.

bull market: a period of rising share prices.

call option: the right to buy a share at a set price within the period of the agreement.

capitalization issue: *see* scrip issue.

common stock: US name for ordinary shares.

consumer price index: a weighted index of a collection of goods chosen by the government to measure the change in average prices and so indicate the rate of inflation. Known commonly as the CPI, it is an alternative to the retail prices index (RPI).

convertible: a class of paper issued by companies (such as loan stock or preference shares) that can be converted into ordinary shares at a pre-set price, and usually on a set date.

coupon: the interest rate on a corporate bond; it comes from the practice in the past of attaching to the certificate a series of coupons that one had to clip off and send to the company to collect the interest.

Crest: an electronic share registry and transfer system operated by the London Stock Exchange, which gets rid of the need for paper certificates.

cum dividend: the share is sold with the entitlement to the newly declared dividend.

dead-cat bounce: a small short-term recovery in a falling stock market, derived from a rather sick metaphor: even a dead cat will bounce slightly if dropped from high enough, but that does not mean it has come back to life.

debenture: a type of corporate bond.

depository receipt: a negotiable certificate representing a foreign company's publicly traded securities making it easier to buy shares in foreign companies because they do not have to leave the home state; it also gets round restrictions on foreigners owning shares.

derivative: a generic term to cover something at some stage removed from the direct investment but dependent on it, so it includes options, warrants, futures, swaps, indices, structured debt obligations and deposits, caps, floors, collars, forwards and combinations of these; standardized versions of some (eg futures and options) are traded on exchanges.

disintermediation: cutting out the middleman.

dividend: it is stated as so much per share, so a company declaring a dividend of 12p pays that amount to the holder for every share on issue. The owner of 1,000 shares would get £12, minus tax.

dividend cover: shows what proportion of the company's earnings are being paid to shareholders or, to put it another way, a measure of the number of times a company's net of tax dividend is covered by its net profit.

dividend yield: the amount of dividend per share (usually quoted net of tax) as a percentage of the share price.

equities: another name for ordinary shares.

exceptional items: profits or losses in the company accounts from dealings that are not part of the company's main trading activities, such as the sale of a factory.

ex-dividend: a share being sold soon after a dividend has been declared, with the seller still getting the payment.

flotation: bringing a company to the stock market to get its shares publicly traded.

FTSE100: stock market index covering the 100 companies with the largest market capitalization. Since companies grow or shrink, become fashionable or are suddenly shunned, the constituents of the index change continually. As a result it is an indication of the temper of the market as a whole rather than showing the performance of any specific set of companies.

FTSE All-Share: the aggregation of the FTSE100, FTSE250 and FTSE Small Cap indices; it does not cover all shares on the market.

fundamental analysis: looking at the company behind the share, it involves calculating net asset value and probable future dividends, which may involve economic predictions as well; it is in contrast to technical analysis, which looks only at the changes in share prices.

gearing: in balance sheets, a ratio of a company's borrowings to its equity.

gilts: short for gilt-edged, the usual name for government-issued bonds.

hedging: protecting against a potential liability.

independent financial adviser: provider of unbiased advice on financial instruments including life policies, units, stakeholder and personal pensions, investment trusts and their savings schemes, and packaged derivatives, but not necessarily shares and bonds (*see* restricted).

insider: somebody with privileged access to information about a company, such as a director; it is illegal to trade in shares on such knowledge.

IPO: initial public offering; US term for flotation.

issued share capital: these are the shares the company has actually sold as opposed to the authorized share capital that it is allowed to sell.

leverage: US name for gearing.

LIBOR: London Inter-Bank Offered Rate, the interest charged by most stable banks lending to each other.

liquidation: the sale of an insolvent company's assets to pay creditors.

liquidity: one meaning is a measure of the market: how easy it is to buy or sell the shares, which is a function of how many shares are available, how many people trade in them and how great the volume of dealings is; another meaning is a measure of how readily an asset can be turned into cash: the more readily, the more liquid it is.

long: owning an investment in anticipation of the price rising; opposite of going short.

market capitalization: the value of a quoted company on the stock market: a simple procedure multiplying the value of each share by the number of shares on issue; so if a company has issued 5 million shares and they are now trading at 125p, the company's market capitalization is £6,250,000.

market correction: a fall in share prices.

members: the shareholders of a company.

MSCI world index: a stock market index of shares traded on several markets around the world. It is maintained by MSCI, formerly known as Morgan Stanley Capital International.

Nasdaq: National Association of Securities Dealers Automated Quotation system; New York-based electronic stock market with a heavy emphasis on companies using advanced technology.

Nasdaq OMX Europe: London-based trading facility for approximately 800 European blue-chip shares.

net asset value: all the assets of a company minus all its liabilities and capital charges.

Neuer Markt: Frankfurt-based market for shares of smaller, younger companies than are normally admitted to the main stock exchange.

noise trader: someone dealing for the wrong reasons, caught up by the 'noise' in the market and seduced into trades by gossip, fashion and phoney analysis.

nominee account: shares held by an institution or company on behalf of individual shareholders.

offer: the price at which managers of unit trusts sell the units to the public; it is higher than the bid price at which they are prepared to buy them back, and the difference is the spread.

open-ended: an investment vehicle that issues paper in ratio to the amount of investment it receives from the public; unit trusts (called mutual funds in the United States); there is no secondary market in the paper, so buying and selling is only with the management company.

pound cost averaging: accumulating a holding by investing the same amount of pounds in the securities at intervals; you get more shares for the money when the price is falling and that reduces the average cost per share.

preferred stock: US name for preference shares.

price/earnings ratio: this compares the current price of the share with the attributable earnings per share. It is the way the market compares expected growth in a company's dividend with the required rate of return of an investor. The formula says the correct price equals the expected current dividend, divided by the required return and expected growth in the company's dividends. So if the dividend now is 10p per share and this is expected to grow by 5 per cent a year, but the current demand is for a return of 8 per cent, the calculation is 10/(0.08 – 0.05), which would make the right share price 333p.

put option: the right to sell a share at a set price within the period of the agreement.

registrar: the organization that maintains the record of a company's shares and their ownership; run by specialist registrar companies, most of them owned by major banks.

re-rating: a change of opinion by the stock market: a surge of good news, a series of analysts' reports, the promise of new products and the like may make investors feel the company's prospects are better than the price rises, with a corresponding rise in the price/earnings ratio and fall in the yield, and conversely the other way.

reserves: the non-distributed profits of a company, plus profits from revaluing assets, plus any share premium; this is not money in the bank but is used in the business, though it remains part of the shareholders' funds.

restricted: a financial adviser who does not cover the range demanded of an independent and who must designate being restricted and explain to clients the restriction by product or provider.

retail prices index: a measure of prices in a set basket of domestic retail goods and services. Known as the RPI, it is generally considered to give a more accurate picture of the cost of living than the alternative, the consumer price index (CPI).

return on capital: measures the efficiency with which the company is using its long-term funds by dividing trading profit (before exceptional items, interest and tax) by the average capital employed over the period (shareholders' funds plus borrowings) and multiplies the result by 100.

return on investments: *see* yield.

rights issue: one way a company raises money is by selling more shares, and sometimes it does this by giving the people who already own its shares the right of first refusal in proportion to the shares they already own.

rule of 20: a way of judging the euphoria or gloom of the market as a whole; it says the price/earnings ratio plus the inflation rate should equal 20.

scrip issue: free issue of shares to existing holders converting corporate reserves into equities – an accounting exercise.

SEATS Plus: a trading system used for Aim stocks and for other shares without enough market-makers to create a competitive market; the computer screen shows any market-makers' prices plus orders from buyers and sellers seeking a counter-party.

sell short: selling shares one does not own in the hope of buying them cheaper in a falling market before delivery is due.

share premium: if the nominal value of a company's share is 20p but it issues them at 50p, the 30p difference is in the books as the share premium account.

shareholders' funds: the assets of a company minus its liabilities; since the shareholders own the business what is left ultimately belongs to them.

short: going short means a dealer is committed to delivering shares he or she does not own; it is done in anticipation of a falling price.

spread: the difference between the buying and selling price of a share or other asset.

stockbroker: a professional dealer in securities who acts as an agent for investors.

straddle: buying simultaneously a buy and a put option in a share with the same exercise price and expiry date; a technique in options trading used by investors who expect volatility in the price of the underlying shares, it widens the break-even point but means they can make money if there is a substantial movement in either direction.

structured notes: debt securities not backed by mortgages, with cash flow dependent on an index or indices and/or with embedded forwards or options.

support: in chartism it is the level at which falling prices stop or bounce because buyers are being tempted back.

technical analysis: in practice another name for the chartist way of looking at the market; it uses not just the conventional method of having a line to depict price movements, but also 'point and figure' charts.

The Undertakings for Collective Investment in Transferable Securities (UCITS): allow collective investment schemes to operate throughout the EU if authorized by one member state. The funds can invest in a wide range of financial instruments (including derivatives), which are subject to the same regulation in every member state. In practice many EU members imposed extra rules to protect local asset managers.

Tradepoint: a company (itself traded on the Alternative Investment Market) providing an electronic market in shares.

unit trusts: an open-ended investment vehicle (see above).

volatility: the amount of fluctuation in a share price; the more it moves the greater the risk.

warrants: a type of investment allowing the holder to buy paper from the issuer at a fixed price sometime in the future; most are listed on the stock exchange and can be traded like any other investment, prior to their expiry date.

with-profits policy: an insurance cover that guarantees a payment at the end of the set term or on death, but which also adds an annual and a terminal bonus, the size of which depends on the company's profit; that in turn is affected mainly by its investment in shares.

yield: calculated by taking the amount of a dividend as a percentage of the current share price. If the shares stand at 120p (irrespective of what the nominal price might be) a dividend of 12p represents a yield of 10 per cent. If the shares then drop to 100p, the yield will have correspondingly risen to 12 per cent. It is listed in the newspapers as yield and compares directly with what can be had in a bank or building society for the money, but should be higher.