Glossary

A priori probability A probability based on logical analysis rather than on observation or personal judgment.
Abnormal return The amount by which a security's actual return differs from its expected return, given the security's risk and the market's return.
Absolute advantage A country's ability to produce a good or service at a lower absolute cost than its trading partner.
Absolute dispersion The amount of variability present without comparison to any reference point or benchmark.
Absolute frequency The number of observations in a given interval (for grouped data).
Accelerated book build An offering of securities by an investment bank acting as principal that is accomplished in only one or two days.
Accelerated methods Depreciation methods that allocate a relatively large proportion of the cost of an asset to the early years of the asset's useful life.
Accounting costs Monetary value of economic resources used in performing an activity. These can be explicit, out-of-pocket, current payments, or an allocation of historical payments (depreciation) for resources. They do not include implicit opportunity costs.
Accounting profit Income as reported on the income statement, in accordance with prevailing accounting standards, before the provisions for income tax expense. Also called *income before taxes* or *pretax income*.
Accounts payable Amounts that a business owes to its vendors for goods and services that were purchased from them but which have not yet been paid.
Accounts receivable turnover Ratio of sales on credit to the average balance in accounts receivable.
Accrued expenses Liabilities related to expenses that have been incurred but not yet paid as of the end of an accounting period—an example of an accrued expense is rent that has been incurred but not yet paid, resulting in a liability "rent payable." Also called *accrued liabilities*.
Accrued interest Interest earned but not yet paid.
Acid-test ratio A stringent measure of liquidity that indicates a company's ability to satisfy current liabilities with its most liquid assets, calculated as (cash + short-term marketable investments + receivables) divided by current liabilities.
Acquisition method A method of accounting for a business combination where the acquirer is required to measure each identifiable asset and liability at fair value. This method was the result of a joint project of the IASB and FASB aiming at convergence in standards for the accounting of business combinations.
Action lag Delay from policy decisions to implementation.
Active investment An approach to investing in which the investor seeks to outperform a given benchmark.
Active return The return on a portfolio minus the return on the portfolio's benchmark.
Active strategy In reference to short-term cash management, an investment strategy characterized by monitoring and attempting to capitalize on market conditions to optimize the risk and return relationship of short-term investments.
Activity ratios Ratios that measure how efficiently a company performs day-to-day tasks, such as the collection of receivables and management of inventory. Also called *asset utilization ratios* or *operating efficiency ratios*.
Add-on rates Bank certificates of deposit, repos, and indexes such as Libor and Euribor are quoted on an add-on rate basis (bond equivalent yield basis).
Addition rule for probabilities A principle stating that the probability that *A* or *B* occurs (both occur) equals the probability that *A* occurs, plus the probability that *B* occurs, minus the probability that both *A* and *B* occur.
Agency bonds See *quasi-government bond*.
Agency RMBS In the United States, securities backed by residential mortgage loans and guaranteed by a federal agency or guaranteed by either of the two GSEs (Fannie Mae and Freddie Mac).
Aggregate demand The quantity of goods and services that households, businesses, government, and foreign customers want to buy at any given level of prices.
Aggregate demand curve Inverse relationship between the price level and real output.
Aggregate income The value of all the payments earned by the suppliers of factors used in the production of goods and services.
Aggregate output The value of all the goods and services produced in a specified period of time.
Aggregate supply The quantity of goods and services producers are willing to supply at any given level of price.
Aggregate supply curve The level of domestic output that companies will produce at each price level.
Aging schedule A breakdown of accounts into categories of days outstanding.
All-or-nothing (AON) orders An order that includes the instruction to trade only if the trade fills the entire quantity (size) specified.
Allocationally efficient A characteristic of a market, a financial system, or an economy that promotes the allocation of resources to their highest value uses.
Alternative data Non-traditional data types generated by the use of electronic devices, social media, satellite and sensor networks, and company exhaust.
Alternative investment markets Market for investments other than traditional securities investments (i.e., traditional common and preferred shares and traditional fixed income instruments). The term usually encompasses direct and indirect investment in real estate (including timberland and farmland) and commodities (including precious metals); hedge funds, private equity, and other investments requiring specialized due diligence.
Alternative trading systems Trading venues that function like exchanges but that do not exercise regulatory authority over their subscribers except with respect to the conduct of the subscribers' trading in their trading systems. Also called *electronic communications networks* or *multilateral trading facilities*.
American depository receipt A US dollar-denominated security that trades like a common share on US exchanges.

American depository share The underlying shares on which American depository receipts are based. They trade in the issuing company's domestic market.

American-style Type of option contract that can be exercised at any time up to the option's expiration date.

Amortisation The process of allocating the cost of intangible long-term assets having a finite useful life to accounting periods; the allocation of the amount of a bond premium or discount to the periods remaining until bond maturity.

Amortised cost The historical cost (initially recognised cost) of an asset, adjusted for amortisation and impairment.

Amortizing bond Bond with a payment schedule that calls for periodic payments of interest and repayments of principal.

Amortizing loan Loan with a payment schedule that calls for periodic payments of interest and repayments of principal.

Annual percentage rate The cost of borrowing expressed as a yearly rate.

Annuity A finite set of level sequential cash flows.

Annuity due An annuity having a first cash flow that is paid immediately.

Anticipation stock Excess inventory that is held in anticipation of increased demand, often because of seasonal patterns of demand.

Antidilutive With reference to a transaction or a security, one that would increase earnings per share (EPS) or result in EPS higher than the company's basic EPS—antidilutive securities are not included in the calculation of diluted EPS.

Arbitrage 1) The simultaneous purchase of an undervalued asset or portfolio and sale of an overvalued but equivalent asset or portfolio, in order to obtain a riskless profit on the price differential. Taking advantage of a market inefficiency in a risk-free manner. 2) The condition in a financial market in which equivalent assets or combinations of assets sell for two different prices, creating an opportunity to profit at no risk with no commitment of money. In a well-functioning financial market, few arbitrage opportunities are possible. 3) A risk-free operation that earns an expected positive net profit but requires no net investment of money.

Arbitrage-free pricing The overall process of pricing derivatives by arbitrage and risk neutrality. Also called the *principle of no arbitrage*.

Arbitrageurs Traders who engage in arbitrage. See *arbitrage*.

Arithmetic mean The sum of the observations divided by the number of observations.

Arms index A flow of funds indicator applied to a broad stock market index to measure the relative extent to which money is moving into or out of rising and declining stocks.

Artificial intelligence Computer systems that exhibit cognitive and decision-making ability comparable (or superior) to that of humans.

Asian call option A European-style option with a value at maturity equal to the difference between the stock price at maturity and the average stock price during the life of the option, or $0, whichever is greater.

Ask The price at which a dealer or trader is willing to sell an asset, typically qualified by a maximum quantity (ask size). See *offer*.

Ask size The maximum quantity of an asset that pertains to a specific ask price from a trader. For example, if the ask for a share issue is $30 for a size of 1,000 shares, the trader is offering to sell at $30 up to 1,000 shares.

Asset allocation The process of determining how investment funds should be distributed among asset classes.

Asset-backed securities A type of bond issued by a legal entity called a *special purpose entity* (SPE) on a collection of assets that the SPE owns. Also, securities backed by receivables and loans other than mortgages.

Asset-based loan A loan that is secured with company assets.

Asset-based valuation models Valuation based on estimates of the market value of a company's assets.

Asset beta The unlevered beta; reflects the business risk of the assets; the asset's systematic risk.

Asset class A group of assets that have similar characteristics, attributes, and risk/return relationships.

Asset swap Converts the periodic fixed coupon of a specific bond to a Libor plus or minus a spread.

Asset utilization ratios Ratios that measure how efficiently a company performs day-to-day tasks, such as the collection of receivables and management of inventory.

Assets Resources controlled by an enterprise as a result of past events and from which future economic benefits to the enterprise are expected to flow.

Assignment of accounts receivable The use of accounts receivable as collateral for a loan.

At the money An option in which the underlying's price equals the exercise price.

Auction A type of bond issuing mechanism often used for sovereign bonds that involves bidding.

Autarkic price The price of a good or service in an autarkic economy.

Autarky A state in which a country does not trade with other countries.

Automated Clearing House (ACH) An electronic payment network available to businesses, individuals, and financial institutions in the United States, US Territories, and Canada.

Automatic stabilizer A countercyclical factor that automatically comes into play as an economy slows and unemployment rises.

Available-for-sale Under US GAAP, debt securities not classified as either held-to-maturity or held-for-trading securities. The investor is willing to sell but not actively planning to sell. In general, available-for-sale debt securities are reported at fair value on the balance sheet, with unrealized gains included as a component of other comprehensive income.

Average accounting rate of return (ARR) Over the life of a project, the AAR can be defined as the average net income divided by the average book value.

Average fixed cost Total fixed cost divided by quantity produced.

Average life See *weighted average life*.

Average product Measures the productivity of inputs on average and is calculated by dividing total product by the total number of units for a given input that is used to generate that output.

Average revenue Total revenue divided by quantity sold.

Average total cost Total cost divided by quantity produced.

Average variable cost Total variable cost divided by quantity produced.

Back simulation Another term for the historical method of estimating VaR. This term is somewhat misleading in that the method involves not a *simulation* of the past but rather what *actually happened* in the past, sometimes adjusted to reflect the fact that a different portfolio may have existed in the past than is planned for the future.

Back-testing With reference to portfolio strategies, the application of a strategy's portfolio selection rules to historical data to assess what would have been the strategy's historical performance.

Backup lines of credit A type of credit enhancement provided by a bank to an issuer of commercial paper to ensure that the issuer will have access to sufficient liquidity to repay maturing commercial paper if issuing new paper is not a viable option.

Balance of payments A double-entry bookkeeping system that summarizes a country's economic transactions with the rest of the world for a particular period of time, typically a calendar quarter or year.

Balance of trade deficit When the domestic economy is spending more on foreign goods and services than foreign economies are spending on domestic goods and services.

Balance sheet The financial statement that presents an entity's current financial position by disclosing resources the entity controls (its assets) and the claims on those resources (its liabilities and equity claims), as of a particular point in time (the date of the balance sheet). Also called *statement of financial position* or *statement of financial condition*.

Balance sheet ratios Financial ratios involving balance sheet items only.

Balanced With respect to a government budget, one in which spending and revenues (taxes) are equal.

Balloon payment Large payment required at maturity to retire a bond's outstanding principal amount.

Bar chart A price chart with four bits of data for each time interval—the high, low, opening, and closing prices. A vertical line connects the high and low. A cross-hatch left indicates the opening price and a cross-hatch right indicates the close.

Barter economy An economy where economic agents as house-holds, corporations, and governments "pay" for goods and services with another good or service.

Base rates The reference rate on which a bank bases lending rates to all other customers.

Basic EPS Net earnings available to common shareholders (i.e., net income minus preferred dividends) divided by the weighted average number of common shares outstanding.

Basis point Used in stating yield spreads, one basis point equals one-hundredth of a percentage point, or 0.01%.

Basket of listed depository receipts An exchange-traded fund (ETF) that represents a portfolio of depository receipts.

Bearer bonds Bonds for which ownership is not recorded; only the clearing system knows who the bond owner is.

Behavioral finance A field of finance that examines the psychological variables that affect and often distort the investment decision making of investors, analysts, and portfolio managers.

Behind the market Said of prices specified in orders that are worse than the best current price; e.g., for a limit buy order, a limit price below the best bid.

Benchmark A comparison portfolio; a point of reference or comparison.

Benchmark issue The latest sovereign bond issue for a given maturity. It serves as a benchmark against which to compare bonds that have the same features but that are issued by another type of issuer.

Benchmark rate Typically the yield-to-maturity on a government bond having the same, or close to the same, time-to-maturity.

Benchmark spread The yield spread over a specific benchmark, usually measured in basis points.

Bernoulli random variable A random variable having the outcomes 0 and 1.

Bernoulli trial An experiment that can produce one of two outcomes.

Best bid The highest bid in the market.

Best effort offering An offering of a security using an investment bank in which the investment bank, as agent for the issuer, promises to use its best efforts to sell the offering but does not guarantee that a specific amount will be sold.

Best-in-class An ESG implementation approach that seeks to identify the most favorable companies in an industry based on ESG considerations.

Best offer The lowest offer (ask price) in the market.

Beta A measure of the sensitivity of a given investment or portfolio to movements in the overall market.

Bid The price at which a dealer or trader is willing to buy an asset, typically qualified by a maximum quantity.

Bid–ask spread The difference between the prices at which dealers will buy from a customer (bid) and sell to a customer (offer or ask). It is often used as an indicator of liquidity.

Bid–offer spread The difference between the prices at which dealers will buy from a customer (bid) and sell to a customer (offer or ask). It is often used as an indicator of liquidity.

Bid size The maximum quantity of an asset that pertains to a specific bid price from a trader.

Big Data The vast amount of data being generated by industry, governments, individuals, and electronic devices that arises from both traditional and non-traditional data sources.

Bilateral loan A loan from a single lender to a single borrower.

Binomial model A model for pricing options in which the underlying price can move to only one of two possible new prices.

Binomial random variable The number of successes in n Bernoulli trials for which the probability of success is constant for all trials and the trials are independent.

Binomial tree The graphical representation of a model of asset price dynamics in which, at each period, the asset moves up with probability p or down with probability $(1 - p)$.

Bitcoin A cryptocurrency using blockchain technology that was created in 2009.

Block brokers A broker (agent) that provides brokerage services for large-size trades.

Blockchain A type of digital ledger in which information is recorded sequentially and then linked together and secured using cryptographic methods.

Blue chip Widely held large market capitalization companies that are considered financially sound and are leaders in their respective industry or local stock market.

Bollinger Bands A price-based technical analysis indicator consisting of a moving average plus a higher line representing the moving average plus a set number of standard deviations from average price (for the same number of periods as used to calculate the moving average) and a lower line that is a moving average minus the same number of standard deviations.

Bond Contractual agreement between the issuer and the bondholders.

Bond equivalent yield A calculation of yield that is annualized using the ratio of 365 to the number of days to maturity. Bond equivalent yield allows for the restatement and comparison of securities with different compounding periods.

Bond indenture The governing legal credit agreement, typically incorporated by reference in the prospectus. Also called *trust deed*.

Bond market vigilantes Bond market participants who might reduce their demand for long-term bonds, thus pushing up their yields.

Bond yield plus risk premium approach An estimate of the cost of common equity that is produced by summing the before-tax cost of debt and a risk premium that captures the additional yield on a company's stock relative to its bonds. The additional yield is often estimated using historical spreads between bond yields and stock yields.

Bonus issue of shares A type of dividend in which a company distributes additional shares of its common stock to shareholders instead of cash.

Book building Investment bankers' process of compiling a "book" or list of indications of interest to buy part of an offering.

Book value The net amount shown for an asset or liability on the balance sheet; book value may also refer to the company's excess of total assets over total liabilities. Also called *carrying value*.

Boom An expansionary phase characterized by economic growth "testing the limits" of the economy.

Bottom-up analysis An investment selection approach that focuses on company-specific circumstances rather than emphasizing economic cycles or industry analysis.

Break point In the context of the weighted average cost of capital (WACC), a break point is the amount of capital at which the cost of one or more of the sources of capital changes, leading to a change in the WACC.

Breakeven point The number of units produced and sold at which the company's net income is zero (Revenues = Total cost); in the case of perfect competition, the quantity at which price, average revenue, and marginal revenue equal average total cost.

Bridge financing Interim financing that provides funds until permanent financing can be arranged.

Broad money Encompasses narrow money plus the entire range of liquid assets that can be used to make purchases.

Broker 1) An agent who executes orders to buy or sell securities on behalf of a client in exchange for a commission. 2) See *futures commission merchants*.

Broker–dealer A financial intermediary (often a company) that may function as a principal (dealer) or as an agent (broker) depending on the type of trade.

Brokered market A market in which brokers arrange trades among their clients.

Budget surplus/deficit The difference between government revenue and expenditure for a stated fixed period of time.

Bullet bond Bond in which the principal repayment is made entirely at maturity.

Business risk The risk associated with operating earnings. Operating earnings are uncertain because total revenues and many of the expenditures contributed to produce those revenues are uncertain.

Buy-side firm An investment management company or other investor that uses the services of brokers or dealers (i.e., the client of the sell side firms).

Buyback A transaction in which a company buys back its own shares. Unlike stock dividends and stock splits, share repurchases use corporate cash.

Call An option that gives the holder the right to buy an underlying asset from another party at a fixed price over a specific period of time.

Call market A market in which trades occur only at a particular time and place (i.e., when the market is called).

Call money rate The interest rate that buyers pay for their margin loan.

Call option An option that gives the holder the right to buy an underlying asset from another party at a fixed price over a specific period of time.

Call protection The time during which the issuer of the bond is not allowed to exercise the call option.

Callable bond A bond containing an embedded call option that gives the issuer the right to buy the bond back from the investor at specified prices on pre-determined dates.

Candlestick chart A price chart with four bits of data for each time interval. A candle indicates the opening and closing price for the interval. The body of the candle is shaded if the opening price was higher than the closing price, and the body is clear if the opening price was lower than the closing price. Vertical lines known as wicks or shadows extend from the top and bottom of the candle to indicate the high and the low prices for the interval.

Cannibalization Cannibalization occurs when an investment takes customers and sales away from another part of the company.

Capacity The ability of the borrower to make its debt payments on time.

Capital account A component of the balance of payments account that measures transfers of capital.

Capital allocation line (CAL) A graph line that describes the combinations of expected return and standard deviation of return available to an investor from combining the optimal portfolio of risky assets with the risk-free asset.

Capital asset pricing model (CAPM) An equation describing the expected return on any asset (or portfolio) as a linear function of its beta relative to the market portfolio.

Capital budgeting The process that companies use for decision making on capital projects—those projects with a life of one year or more.

Capital consumption allowance A measure of the wear and tear (depreciation) of the capital stock that occurs in the production of goods and services.

Capital deepening investment Increases the stock of capital relative to labor.

Capital expenditure Expenditure on physical capital (fixed assets).

Capital lease See *finance lease*.

Capital market expectations An investor's expectations concerning the risk and return prospects of asset classes.

Capital market line (CML) The line with an intercept point equal to the risk-free rate that is tangent to the efficient frontier of risky assets; represents the efficient frontier when a risk-free asset is available for investment.

Capital market securities Securities with maturities at issuance longer than one year.

Capital markets Financial markets that trade securities of longer duration, such as bonds and equities.

Capital rationing A capital rationing environment assumes that the company has a fixed amount of funds to invest.

Capital restrictions Controls placed on foreigners' ability to own domestic assets and/or domestic residents' ability to own foreign assets.
Capital stock The accumulated amount of buildings, machinery, and equipment used to produce goods and services.
Capital structure The mix of debt and equity that a company uses to finance its business; a company's specific mixture of long-term financing.
Captive finance subsidiary A wholly-owned subsidiary of a company that is established to provide financing of the sales of the parent company.
Carry The net of the costs and benefits of holding, storing, or "carrying" an asset.
Carrying amount The amount at which an asset or liability is valued according to accounting principles.
Carrying value The net amount shown for an asset or liability on the balance sheet; book value may also refer to the company's excess of total assets over total liabilities. For a bond, the purchase price plus (or minus) the amortized amount of the discount (or premium).
Cartel Participants in collusive agreements that are made openly and formally.
Cash collateral account Form of external credit enhancement whereby the issuer immediately borrows the credit-enhancement amount and then invests that amount, usually in highly rated short-term commercial paper.
Cash conversion cycle A financial metric that measures the length of time required for a company to convert cash invested in its operations to cash received as a result of its operations; equal to days of inventory on hand + days of sales outstanding – number of days of payables. Also called *net operating cycle*.
Cash flow additivity principle The principle that dollar amounts indexed at the same point in time are additive.
Cash flow from operating activities The net amount of cash provided from operating activities.
Cash flow from operations The net amount of cash provided from operating activities.
Cash flow yield The internal rate of return on a series of cash flows.
Cash market securities Money market securities settled on a "same day" or "cash settlement" basis.
Cash markets See *spot markets.*
Cash prices See *spot prices.*
Cash-settled forwards See *non-deliverable forwards.*
CBOE Volatility Index A measure of near-term market volatility as conveyed by S&P 500 stock index option prices.
Central bank funds market The market in which deposit-taking banks that have an excess reserve with their national central bank can loan money to banks that need funds for maturities ranging from overnight to one year. Called the Federal or Fed funds market in the United States.
Central bank funds rates Interest rates at which central bank funds are bought (borrowed) and sold (lent) for maturities ranging from overnight to one year. Called Federal or Fed funds rates in the United States.
Central banks The dominant bank in a country, usually with official or semi-official governmental status.
Certificate of deposit An instrument that represents a specified amount of funds on deposit with a bank for a specified maturity and interest rate. CDs are issued in various denominations and can be negotiable or non-negotiable.
Change in polarity principle A tenet of technical analysis that once a support level is breached, it becomes a resistance level. The same holds true for resistance levels; once breached, they become support levels.
Change of control put A covenant giving bondholders the right to require the issuer to buy back their debt, often at par or at some small premium to par value, in the event that the borrower is acquired.
Character The quality of a debt issuer's management.
Classified balance sheet A balance sheet organized so as to group together the various assets and liabilities into subcategories (e.g., current and noncurrent).
Clawback A requirement that the general partner return any funds distributed as incentive fees until the limited partners have received back their initial investment and a percentage of the total profit.
Clearing The process by which the exchange verifies the execution of a transaction and records the participants' identities.
Clearing instructions Instructions that indicate how to arrange the final settlement ("clearing") of a trade.
Clearinghouse An entity associated with a futures market that acts as middleman between the contracting parties and guarantees to each party the performance of the other.
Closed economy An economy that does not trade with other countries; an *autarkic economy*.
Closed-end fund A mutual fund in which no new investment money is accepted. New investors invest by buying existing shares, and investors in the fund liquidate by selling their shares to other investors.
Code of ethics An established guide that communicates an organization's values and overall expectations regarding member behavior. A code of ethics serves as a general guide for how community members should act.
Coefficient of variation (CV) The ratio of a set of observations' standard deviation to the observations' mean value.
Coincident economic indicators Turning points that are usually close to those of the overall economy; they are believed to have value for identifying the economy's present state.
Collateral manager Buys and sells debt obligations for and from the CDO's portfolio of assets (i.e., the collateral) to generate sufficient cash flows to meet the obligations to the CDO bondholders.
Collateral trust bonds Bonds secured by securities such as common shares, other bonds, or other financial assets.
Collateralized bond obligations A structured asset-backed security that is collateralized by a pool of bonds.
Collateralized debt obligation Generic term used to describe a security backed by a diversified pool of one or more debt obligations.
Collateralized loan obligations A structured asset-backed security that is collateralized by a pool of loans.
Collateralized mortgage obligation A security created through the securitization of a pool of mortgage-related products (mortgage pass-through securities or pools of loans).
Collaterals Assets or financial guarantees underlying a debt obligation that are above and beyond the issuer's promise to pay.
Combination A listing in which the order of the listed items does not matter.
Commercial paper A short-term, negotiable, unsecured promissory note that represents a debt obligation of the issuer.

Committed capital The amount that the limited partners have agreed to provide to the private equity fund.

Committed lines of credit A bank commitment to extend credit up to a pre-specified amount; the commitment is considered a short-term liability and is usually in effect for 364 days (one day short of a full year).

Commodity swap A swap in which the underlying is a commodity such as oil, gold, or an agricultural product.

Common market Level of economic integration that incorporates all aspects of the customs union and extends it by allowing free movement of factors of production among members.

Common shares A type of security that represent an ownership interest in a company.

Common-size analysis The restatement of financial statement items using a common denominator or reference item that allows one to identify trends and major differences; an example is an income statement in which all items are expressed as a percent of revenue.

Common stock See *common shares*.

Company analysis Analysis of an individual company.

Comparable company A company that has similar business risk; usually in the same industry and preferably with a single line of business.

Comparative advantage A country's ability to produce a good or service at a lower relative cost, or opportunity cost, than its trading partner.

Competitive strategy A company's plans for responding to the threats and opportunities presented by the external environment.

Complements Goods that tend to be used together; technically, two goods whose cross-price elasticity of demand is negative.

Complete markets Informally, markets in which the variety of distinct securities traded is so broad that any desired payoff in a future state-of-the-world is achievable.

Component cost of capital The rate of return required by suppliers of capital for an individual source of a company's funding, such as debt or equity.

Compounding The process of accumulating interest on interest.

Comprehensive income The change in equity of a business enterprise during a period from nonowner sources; includes all changes in equity during a period except those resulting from investments by owners and distributions to owners; comprehensive income equals net income plus other comprehensive income.

Conditional expected value The expected value of a stated event given that another event has occurred.

Conditional probability The probability of an event given (conditioned on) another event.

Conditional variances The variance of one variable, given the outcome of another.

Consistent With reference to estimators, describes an estimator for which the probability of estimates close to the value of the population parameter increases as sample size increases.

Constant-yield price trajectory A graph that illustrates the change in the price of a fixed-income bond over time assuming no change in yield-to-maturity. The trajectory shows the "pull to par" effect on the price of a bond trading at a premium or a discount to par value.

Constituent securities With respect to an index, the individual securities within an index.

Consumer surplus The difference between the value that a consumer places on units purchased and the amount of money that was required to pay for them.

Contingency provision Clause in a legal document that allows for some action if a specific event or circumstance occurs.

Contingent claims Derivatives in which the payoffs occur if a specific event occurs; generally referred to as options.

Contingent convertible bonds Bonds that automatically convert into equity if a specific event or circumstance occurs, such as the issuer's equity capital falling below the minimum requirement set by the regulators. Also called *CoCos*.

Continuation patterns A type of pattern used in technical analysis to predict the resumption of a market trend that was in place prior to the formation of a pattern.

Continuous random variable A random variable for which the range of possible outcomes is the real line (all real numbers between $-\infty$ and $+\infty$ or some subset of the real line).

Continuous time Time thought of as advancing in extremely small increments.

Continuous trading market A market in which trades can be arranged and executed any time the market is open.

Continuously compounded return The natural logarithm of 1 plus the holding period return, or equivalently, the natural logarithm of the ending price over the beginning price.

Contra account An account that offsets another account.

Contract rate See *mortgage rate*.

Contraction The period of a business cycle after the peak and before the trough; often called a *recession* or, if exceptionally severe, called a *depression*.

Contraction risk The risk that when interest rates decline, the security will have a shorter maturity than was anticipated at the time of purchase because borrowers refinance at the new, lower interest rates.

Contractionary Tending to cause the real economy to contract.

Contractionary fiscal policy A fiscal policy that has the objective to make the real economy contract.

Contracts for differences See *non-deliverable forwards*.

Contribution margin The amount available for fixed costs and profit after paying variable costs; revenue minus variable costs.

Controlling shareholders A particular shareholder or block of shareholders holding a percentage of shares that gives them significant voting power.

Convenience yield A non-monetary advantage of holding an asset.

Conventional bond See *plain vanilla bond*.

Conventional cash flow A conventional cash flow pattern is one with an initial outflow followed by a series of inflows.

Convergence The tendency for differences in output per capita across countries to diminish over time; in technical analysis, a term that describes the case when an indicator moves in the same manner as the security being analyzed.

Conversion price For a convertible bond, the price per share at which the bond can be converted into shares.

Conversion ratio For a convertible bond, the number of common shares that each bond can be converted into.

Conversion value For a convertible bond, the current share price multiplied by the conversion ratio.

Convertible bond Bond that gives the bondholder the right to exchange the bond for a specified number of common shares in the issuing company.

Convertible preference shares A type of equity security that entitles shareholders to convert their shares into a specified number of common shares.

Convexity adjustment For a bond, one half of the annual or approximate convexity statistic multiplied by the change in the yield-to-maturity squared.

Core inflation The inflation rate calculated based on a price index of goods and services except food and energy.

Corporate governance The system of internal controls and procedures by which individual companies are managed.

Correlation A number between −1 and +1 that measures the comovement (linear association) between two random variables.

Correlation coefficient A number between −1 and +1 that measures the consistency or tendency for two investments to act in a similar way. It is used to determine the effect on portfolio risk when two assets are combined.

Cost averaging The periodic investment of a fixed amount of money.

Cost of capital The rate of return that suppliers of capital require as compensation for their contribution of capital.

Cost of carry See *carry*.

Cost of debt The cost of debt financing to a company, such as when it issues a bond or takes out a bank loan.

Cost of preferred stock The cost to a company of issuing preferred stock; the dividend yield that a company must commit to pay preferred stockholders.

Cost-push Type of inflation in which rising costs, usually wages, compel businesses to raise prices generally.

Cost structure The mix of a company's variable costs and fixed costs.

Counterparty risk The risk that the other party to a contract will fail to honor the terms of the contract.

Coupon rate The interest rate promised in a contract; this is the rate used to calculate the periodic interest payments.

Cournot assumption Assumption in which each firm determines its profit-maximizing production level assuming that the other firms' output will not change.

Covariance A measure of the co-movement (linear association) between two random variables.

Covariance matrix A matrix or square array whose entries are covariances; also known as a variance–covariance matrix.

Covenants The terms and conditions of lending agreements that the issuer must comply with; they specify the actions that an issuer is obligated to perform (affirmative covenant) or prohibited from performing (negative covenant).

Covered bond Debt obligation secured by a segregated pool of assets called the cover pool. The issuer must maintain the value of the cover pool. In the event of default, bondholders have recourse against both the issuer and the cover pool.

Credit analysis The evaluation of credit risk; the evaluation of the creditworthiness of a borrower or counterparty.

Credit curve A curve showing the relationship between time to maturity and yield spread for an issuer with comparable bonds of various maturities outstanding, usually upward sloping.

Credit default swap (CDS) A type of credit derivative in which one party, the credit protection buyer who is seeking credit protection against a third party, makes a series of regularly scheduled payments to the other party, the credit protection seller. The seller makes no payments until a credit event occurs.

Credit derivatives A contract in which one party has the right to claim a payment from another party in the event that a specific credit event occurs over the life of the contract.

Credit enhancements Provisions that may be used to reduce the credit risk of a bond issue.

Credit-linked coupon bond Bond for which the coupon changes when the bond's credit rating changes.

Credit-linked note (CLN) Fixed-income security in which the holder of the security has the right to withhold payment of the full amount due at maturity if a credit event occurs.

Credit migration risk The risk that a bond issuer's creditworthiness deteriorates, or migrates lower, leading investors to believe the risk of default is higher. Also called *downgrade risk*.

Credit risk The risk of loss caused by a counterparty's or debtor's failure to make a promised payment. Also called *default risk*.

Credit scoring model A statistical model used to classify borrowers according to creditworthiness.

Credit spread option An option on the yield spread on a bond.

Credit tranching A structure used to redistribute the credit risk associated with the collateral; a set of bond classes created to allow investors a choice in the amount of credit risk that they prefer to bear.

Credit-worthiness The perceived ability of the borrower to pay what is owed on the borrowing in a timely manner; it represents the ability of a company to withstand adverse impacts on its cash flows.

Cross-default provisions Provisions whereby events of default such as non-payment of interest on one bond trigger default on all outstanding debt; implies the same default probability for all issues.

Cross-price elasticity of demand The percentage change in quantity demanded for a given percentage change in the price of another good; the responsiveness of the demand for Product A that is associated with the change in price of Product B.

Cross-sectional analysis Analysis that involves comparisons across individuals in a group over a given time period or at a given point in time.

Cross-sectional data Observations over individual units at a point in time, as opposed to time-series data.

Crossing networks Trading systems that match buyers and sellers who are willing to trade at prices obtained from other markets.

Crowding out The thesis that government borrowing may divert private sector investment from taking place.

Cryptocurrency An electronic medium of exchange that lacks physical form.

Cryptography An algorithmic process to encrypt data, making the data unusable if received by unauthorized parties.

Cumulative distribution function A function giving the probability that a random variable is less than or equal to a specified value.

Cumulative preference shares Preference shares for which any dividends that are not paid accrue and must be paid in full before dividends on common shares can be paid.

Cumulative relative frequency For data grouped into intervals, the fraction of total observations that are less than the value of the upper limit of a stated interval.

Cumulative voting A voting process whereby each shareholder can accumulate and vote all his or her shares for a single candidate in an election, as opposed to having to allocate their voting rights evenly among all candidates.

Currencies Monies issued by national monetary authorities.

Currency option bonds Bonds that give the bondholder the right to choose the currency in which he or she wants to receive interest payments and principal repayments.

Currency swap A swap in which each party makes interest payments to the other in different currencies.

Current account A component of the balance of payments account that measures the flow of goods and services.

Current assets Assets that are expected to be consumed or converted into cash in the near future, typically one year or less. *Also called liquid assets.*

Current cost With reference to assets, the amount of cash or cash equivalents that would have to be paid to buy the same or an equivalent asset today; with reference to liabilities, the undiscounted amount of cash or cash equivalents that would be required to settle the obligation today.

Current government spending With respect to government expenditures, spending on goods and services that are provided on a regular, recurring basis including health, education, and defense.

Current liabilities Short-term obligations, such as accounts payable, wages payable, or accrued liabilities, that are expected to be settled in the near future, typically one year or less.

Current ratio A liquidity ratio calculated as current assets divided by current liabilities.

Current yield The sum of the coupon payments received over the year divided by the flat price; also called the *income* or *interest yield* or *running yield*.

Curve duration The sensitivity of the bond price (or the market value of a financial asset or liability) with respect to a benchmark yield curve.

Customs union Extends the free trade area (FTA) by not only allowing free movement of goods and services among members, but also creating a common trade policy against nonmembers.

CVaR Conditional VaR, a tail loss measure. The weighted average of all loss outcomes in the statistical distribution that exceed the VaR loss.

Cyclical See *cyclical companies*.

Cyclical companies Companies with sales and profits that regularly expand and contract with the business cycle or state of economy.

Daily settlement See *mark to market* and *marking to market*.

Dark pools Alternative trading systems that do not display the orders that their clients send to them.

Data mining The practice of determining a model by extensive searching through a dataset for statistically significant patterns. Also called *data snooping*.

Data science An interdisciplinary field that brings computer science, statistics, and other disciplines together to analyze and produce insights from Big Data.

Data snooping See *data mining*.

Day order An order that is good for the day on which it is submitted. If it has not been filled by the close of business, the order expires unfilled.

Day's sales outstanding Estimate of the average number of days it takes to collect on credit accounts.

Days in receivables Estimate of the average number of days it takes to collect on credit accounts.

Days of inventory on hand An activity ratio equal to the number of days in the period divided by inventory turnover over the period.

Dealers A financial intermediary that acts as a principal in trades.

Dealing securities Securities held by banks or other financial intermediaries for trading purposes.

Death cross A technical analysis term that describes a situation where a short-term moving average crosses from above a longer-term moving average to below it; this movement is considered bearish.

Debentures Type of bond that can be secured or unsecured.

Debt incurrence test A financial covenant made in conjunction with existing debt that restricts a company's ability to incur additional debt at the same seniority based on one or more financial tests or conditions.

Debt-rating approach A method for estimating a company's before-tax cost of debt based upon the yield on comparably rated bonds for maturities that closely match that of the company's existing debt.

Debt-to-assets ratio A solvency ratio calculated as total debt divided by total assets.

Debt-to-capital ratio A solvency ratio calculated as total debt divided by total debt plus total shareholders' equity.

Debt-to-equity ratio A solvency ratio calculated as total debt divided by total shareholders' equity.

Declaration date The day that the corporation issues a statement declaring a specific dividend.

Decreasing returns to scale When a production process leads to increases in output that are proportionately smaller than the increase in inputs.

Deductible temporary differences Temporary differences that result in a reduction of or deduction from taxable income in a future period when the balance sheet item is recovered or settled.

Deep learning Machine learning using neural networks with many hidden layers.

Deep learning nets Machine learning using neural networks with many hidden layers.

Default probability The probability that a borrower defaults or fails to meet its obligation to make full and timely payments of principal and interest, according to the terms of the debt security. Also called *default risk*.

Default risk The probability that a borrower defaults or fails to meet its obligation to make full and timely payments of principal and interest, according to the terms of the debt security. Also called *default probability*.

Default risk premium An extra return that compensates investors for the possibility that the borrower will fail to make a promised payment at the contracted time and in the contracted amount.

Defensive companies Companies with sales and profits that have little sensitivity to the business cycle or state of the economy.

Defensive interval ratio A liquidity ratio that estimates the number of days that an entity could meet cash needs from liquid assets; calculated as (cash + short-term marketable investments + receivables) divided by daily cash expenditures.

Deferred coupon bond Bond that pays no coupons for its first few years but then pays a higher coupon than it otherwise normally would for the remainder of its life. Also called *split coupon bond*.

Deferred income A liability account for money that has been collected for goods or services that have not yet been delivered; payment received in advance of providing a good or service.

Deferred revenue A liability account for money that has been collected for goods or services that have not yet been delivered; payment received in advance of providing a good or service.

Deferred tax assets A balance sheet asset that arises when an excess amount is paid for income taxes relative to accounting profit. The taxable income is higher than accounting profit and income tax payable exceeds tax expense. The company expects to recover the difference during the course of future operations when tax expense exceeds income tax payable.

Deferred tax liabilities A balance sheet liability that arises when a deficit amount is paid for income taxes relative to accounting profit. The taxable income is less than the accounting profit and income tax payable is less than tax expense. The company expects to eliminate the liability over the course of future operations when income tax payable exceeds tax expense.

Defined benefit pension plans Plans in which the company promises to pay a certain annual amount (defined benefit) to the employee after retirement. The company bears the investment risk of the plan assets.

Defined contribution pension plans Individual accounts to which an employee and typically the employer makes contributions during their working years and expect to draw on the accumulated funds at retirement. The employee bears the investment and inflation risk of the plan assets.

Deflation Negative inflation.

Degree of confidence The probability that a confidence interval includes the unknown population parameter.

Degree of financial leverage (DFL) The ratio of the percentage change in net income to the percentage change in operating income; the sensitivity of the cash flows available to owners when operating income changes.

Degree of operating leverage (DOL) The ratio of the percentage change in operating income to the percentage change in units sold; the sensitivity of operating income to changes in units sold.

Degree of total leverage The ratio of the percentage change in net income to the percentage change in units sold; the sensitivity of the cash flows to owners to changes in the number of units produced and sold.

Degrees of freedom (df) The number of independent observations used.

Delta The sensitivity of the derivative price to a small change in the value of the underlying asset.

Demand curve Graph of the inverse demand function. A graph showing the demand relation, either the highest quantity willingly purchased at each price or the highest price willingly paid for each quantity.

Demand function A relationship that expresses the quantity demanded of a good or service as a function of own-price and possibly other variables.

Demand-pull Type of inflation in which increasing demand raises prices generally, which then are reflected in a business's costs as workers demand wage hikes to catch up with the rising cost of living.

Demand shock A typically unexpected disturbance to demand, such as an unexpected interruption in trade or transportation.

Dependent With reference to events, the property that the probability of one event occurring depends on (is related to) the occurrence of another event.

Depository bank A bank that raises funds from depositors and other investors and lends it to borrowers.

Depository institutions Commercial banks, savings and loan banks, credit unions, and similar institutions that raise funds from depositors and other investors and lend it to borrowers.

Depository receipt A security that trades like an ordinary share on a local exchange and represents an economic interest in a foreign company.

Depreciation The process of systematically allocating the cost of long-lived (tangible) assets to the periods during which the assets are expected to provide economic benefits.

Depression See *contraction*.

Derivative pricing rule A pricing rule used by crossing networks in which a price is taken (derived) from the price that is current in the asset's primary market.

Derivatives A financial instrument whose value depends on the value of some underlying asset or factor (e.g., a stock price, an interest rate, or exchange rate).

Descriptive statistics The study of how data can be summarized effectively.

Development capital Minority equity investments in more mature companies that are seeking capital to expand or restructure operations, enter new markets, or finance major acquisitions.

Diffuse prior The assumption of equal prior probabilities.

Diffusion index Reflects the proportion of the index's components that are moving in a pattern consistent with the overall index.

Diluted EPS The EPS that would result if all dilutive securities were converted into common shares.

Diluted shares The number of shares that would be outstanding if all potentially dilutive claims on common shares (e.g., convertible debt, convertible preferred stock, and employee stock options) were exercised.

Diminishing balance method An accelerated depreciation method, i.e., one that allocates a relatively large proportion of the cost of an asset to the early years of the asset's useful life.

Diminishing marginal productivity Describes a state in which each additional unit of input produces less output than previously.

Direct debit program An arrangement whereby a customer authorizes a debit to a demand account; typically used by companies to collect routine payments for services.

Direct financing leases Under US GAAP, a type of finance lease, from a lessor perspective, where the present value of the lease payments (lease receivable) equals the carrying value of the leased asset. No selling profit is recognized at lease inception. The revenues earned by the lessor are financing in nature.

Direct format With reference to the cash flow statement, a format for the presentation of the statement in which cash flow from operating activities is shown as operating cash receipts less operating cash disbursements. Also called *direct method*.

Direct method See *direct format*.

Direct taxes Taxes levied directly on income, wealth, and corporate profits.

Direct write-off method An approach to recognizing credit losses on customer receivables in which the company waits until such time as a customer has defaulted and only then recognizes the loss.

Disbursement float The amount of time between check issuance and a check's clearing back against the company's account.

Discount To reduce the value of a future payment in allowance for how far away it is in time; to calculate the present value of some future amount. Also, the amount by which an instrument is priced below its face (par) value.

Discount interest A procedure for determining the interest on a loan or bond in which the interest is deducted from the face value in advance.

Discount margin See *required margin.*

Discount rates In general, the interest rate used to calculate a present value. In the money market, however, discount rate is a specific type of quoted rate.

Discounted cash flow models Valuation models that estimate the intrinsic value of a security as the present value of the future benefits expected to be received from the security.

Discounted payback period the number of years it takes for the cumulative discounted cash flows from a project to equal the original investment.

Discouraged worker A person who has stopped looking for a job or has given up seeking employment.

Discrete random variable A random variable that can take on at most a countable number of possible values.

Discriminatory pricing rule A pricing rule used in continuous markets in which the limit price of the order or quote that first arrived determines the trade price.

Diseconomies of scale Increase in cost per unit resulting from increased production.

Dispersion The variability around the central tendency.

Display size The size of an order displayed to public view.

Distressed investing Investing in securities of companies in financial difficulty. Private equity funds that specialize in distressed investing typically buy the debt of mature companies in financial difficulty.

Distributed ledger A type of database that may be shared among entities in a network.

Distributed ledger technology Technology based on a distributed ledger.

Divergence In technical analysis, a term that describes the case when an indicator moves differently from the security being analyzed.

Diversification ratio The ratio of the standard deviation of an equally weighted portfolio to the standard deviation of a randomly selected security.

Dividend A distribution paid to shareholders based on the number of shares owned.

Dividend discount model (DDM) A present value model that estimates the intrinsic value of an equity share based on the present value of its expected future dividends.

Dividend discount model based approach An approach for estimating a country's equity risk premium. The market rate of return is estimated as the sum of the dividend yield and the growth rate in dividends for a market index. Subtracting the risk-free rate of return from the estimated market return produces an estimate for the equity risk premium.

Dividend payout ratio The ratio of cash dividends paid to earnings for a period.

Divisor A number (denominator) used to determine the value of a price return index. It is initially chosen at the inception of an index and subsequently adjusted by the index provider, as necessary, to avoid changes in the index value that are unrelated to changes in the prices of its constituent securities.

Domestic content provisions Stipulate that some percentage of the value added or components used in production should be of domestic origin.

Double bottoms In technical analysis, a reversal pattern that is formed when the price reaches a low, rebounds, and then sells off back to the first low level; used to predict a change from a downtrend to an uptrend.

Double coincidence of wants A prerequisite to barter trades, in particular that both economic agents in the transaction want what the other is selling.

Double declining balance depreciation An accelerated depreciation method that involves depreciating the asset at double the straight-line rate. This rate is multiplied by the book value of the asset at the beginning of the period (a declining balance) to calculate depreciation expense.

Double top In technical analysis, a reversal pattern that is formed when an uptrend reverses twice at roughly the same high price level; used to predict a change from an uptrend to a downtrend.

Down transition probability The probability that an asset's value moves down in a model of asset price dynamics.

Downgrade risk The risk that a bond issuer's creditworthiness deteriorates, or migrates lower, leading investors to believe the risk of default is higher. Also called *credit migration risk*.

Drag on liquidity When receipts lag, creating pressure from the decreased available funds.

Drawdown A percentage peak-to-trough reduction in net asset value.

Dual-currency bonds Bonds that make coupon payments in one currency and pay the par value at maturity in another currency.

DuPont analysis An approach to decomposing return on investment, e.g., return on equity, as the product of other financial ratios.

Duration A measure of the approximate sensitivity of a security to a change in interest rates (i.e., a measure of interest rate risk).

Duration gap A bond's Macaulay duration minus the investment horizon.

Dutch Book theorem A result in probability theory stating that inconsistent probabilities create profit opportunities.

Early repayment option See *prepayment option.*

Earnings per share The amount of income earned during a period per share of common stock.

Earnings surprise The portion of a company's earnings that is unanticipated by investors and, according to the efficient market hypothesis, merits a price adjustment.

Economic costs All the remuneration needed to keep a productive resource in its current employment or to acquire the resource for productive use; the sum of total accounting costs and implicit opportunity costs.

Economic indicator A variable that provides information on the state of the overall economy.

Economic loss The amount by which accounting profit is less than normal profit.

Economic order quantity–reorder point (EOQ–ROP) An approach to managing inventory based on expected demand and the predictability of demand; the ordering point for new inventory is determined based on the costs of ordering and carrying inventory, such that the total cost associated with inventory is minimized.

Economic profit Equal to accounting profit less the implicit opportunity costs not included in total accounting costs; the difference between total revenue (TR) and total cost (TC). Also called *abnormal profit* or *supernormal profit*.
Economic stabilization Reduction of the magnitude of economic fluctuations.
Economic union Incorporates all aspects of a common market and in addition requires common economic institutions and coordination of economic policies among members.
Economies of scale Reduction in cost per unit resulting from increased production.
Effective annual rate The amount by which a unit of currency will grow in a year with interest on interest included.
Effective convexity A *curve convexity* statistic that measures the secondary effect of a change in a benchmark yield curve on a bond's price.
Effective duration The sensitivity of a bond's price to a change in a benchmark yield curve.
Effective interest rate The borrowing rate or market rate that a company incurs at the time of issuance of a bond.
Efficient market A market in which asset prices reflect new information quickly and rationally.
Elastic Said of a good or service when the magnitude of elasticity is greater than one.
Elasticity The percentage change in one variable for a percentage change in another variable; a general measure of how sensitive one variable is to a change in the value of another variable.
Elasticity of demand A measure of the sensitivity of quantity demanded to a change in a product's own price: $\%\Delta Q^D/\%\Delta P$.
Elasticity of supply A measure of the sensitivity of quantity supplied to a change in price: $\%\Delta Q^S/\%\Delta P$.
Electronic communications networks See *alternative trading systems*.
Electronic funds transfer (EFT) The use of computer networks to conduct financial transactions electronically.
Elliott wave theory A technical analysis theory that claims that the market follows regular, repeated waves or cycles.
Embedded option Contingency provisions that provide the issuer or the bondholders the right, but not the obligation, to take action. These options are not part of the security and cannot be traded separately.
Empirical probability The probability of an event estimated as a relative frequency of occurrence.
Employed The number of people with a job.
Engagement/active ownership An ESG investment style that uses shareholder power to influence corporate behavior through direct corporate engagement (i.e., communicating with senior management and/or boards of companies), filing or co-filing shareholder proposals, and proxy voting that is directed by ESG guidelines.
Enterprise risk management An overall assessment of a company's risk position. A centralized approach to risk management sometimes called firmwide risk management.
Enterprise value A measure of a company's total market value from which the value of cash and short-term investments have been subtracted.
Equal weighting An index weighting method in which an equal weight is assigned to each constituent security at inception.
Equipment trust certificates Bonds secured by specific types of equipment or physical assets.
Equity Assets less liabilities; the residual interest in the assets after subtracting the liabilities.
Equity risk premium The expected return on equities minus the risk-free rate; the premium that investors demand for investing in equities.
Equity swap A swap transaction in which at least one cash flow is tied to the return to an equity portfolio position, often an equity index.
ESG An acronym that encompasses environmental, social and governance.
ESG integration The integration of qualitative and quantitative environmental, social, and governance factors into traditional security and industry analysis; also known as *ESG incorporation*.
ESG investing The consideration of environmental, social, and governance factors in the investment process.
Estimate The particular value calculated from sample observations using an estimator.
Estimation With reference to statistical inference, the subdivision dealing with estimating the value of a population parameter.
Estimator An estimation formula; the formula used to compute the sample mean and other sample statistics are examples of estimators.
Ethical principles Beliefs regarding what is good, acceptable, or obligatory behavior and what is bad, unacceptable, or forbidden behavior.
Ethics The study of moral principles or of making good choices. Ethics encompasses a set of moral principles and rules of conduct that provide guidance for our behavior.
Eurobonds Type of bond issued internationally, outside the jurisdiction of the country in whose currency the bond is denominated.
European option An option that can only be exercised on its expiration date.
European-style Said of an option contract that can only be exercised on the option's expiration date.
Event Any outcome or specified set of outcomes of a random variable.
Ex-dividend date The first date that a share trades without (i.e., "ex") the dividend.
Excess kurtosis Degree of kurtosis (fatness of tails) in excess of the kurtosis of the normal distribution.
Exchanges Places where traders can meet to arrange their trades.
Exclusionary screening An ESG implementation approach that excludes certain sectors or companies that deviate from an investor's accepted standards. Also called *negative screening* or *norms-based screening*.
Execution instructions Instructions that indicate how to fill an order.
Exercise The process of using an option to buy or sell the underlying.
Exercise price The fixed price at which an option holder can buy or sell the underlying. Also called *strike price*, *striking price*, or *strike*.
Exercise value The value obtained if an option is exercised based on current conditions. Also known as *intrinsic value*.
Exhaustive Covering or containing all possible outcomes.
Expansion The period of a business cycle after its lowest point and before its highest point.
Expansionary Tending to cause the real economy to grow.
Expansionary fiscal policy Fiscal policy aimed at achieving real economic growth.

Expected inflation The level of inflation that economic agents expect in the future.

Expected loss Default probability times Loss severity given default.

Expected value The probability-weighted average of the possible outcomes of a random variable.

Expenses Outflows of economic resources or increases in liabilities that result in decreases in equity (other than decreases because of distributions to owners); reductions in net assets associated with the creation of revenues.

Experience curve A curve that shows the direct cost per unit of good or service produced or delivered as a typically declining function of cumulative output.

Export subsidy Paid by the government to the firm when it exports a unit of a good that is being subsidized.

Exports Goods and services that an economy sells to other countries.

Extension risk The risk that when interest rates rise, fewer prepayments will occur because homeowners are reluctant to give up the benefits of a contractual interest rate that now looks low. As a result, the security becomes longer in maturity than anticipated at the time of purchase.

Externality An effect of a market transaction that is borne by parties other than those who transacted.

Extra dividend A dividend paid by a company that does not pay dividends on a regular schedule, or a dividend that supplements regular cash dividends with an extra payment.

Extreme value theory A branch of statistics that focuses primarily on extreme outcomes.

Face value The amount of cash payable by a company to the bondholders when the bonds mature; the promised payment at maturity separate from any coupon payment.

Factor A common or underlying element with which several variables are correlated.

Fair value The amount at which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's-length transaction; the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants.

Fed funds rate The US interbank lending rate on overnight borrowings of reserves.

Federal funds rate The US interbank lending rate on overnight borrowings of reserves.

Fiat money Money that is not convertible into any other commodity.

Fibonacci sequence A sequence of numbers starting with 0 and 1, and then each subsequent number in the sequence is the sum of the two preceding numbers. In Elliott Wave Theory, it is believed that market waves follow patterns that are the ratios of the numbers in the Fibonacci sequence.

Fiduciary call A combination of a European call and a risk-free bond that matures on the option expiration day and has a face value equal to the exercise price of the call.

FIFO method The first in, first out, method of accounting for inventory, which matches sales against the costs of items of inventory in the order in which they were placed in inventory.

Fill or kill See *immediate or cancel order*.

Finance lease From the lessee perspective, under US GAAP, a type of lease which is more akin to the purchase of an asset by the lessee. From the lessor perspective, under IFRS, a lease which "transfers substantially all the risks and rewards incidental to ownership of an underlying asset."

Financial account A component of the balance of payments account that records investment flows.

Financial flexibility The ability to react and adapt to financial adversity and opportunities.

Financial leverage The extent to which a company can effect, through the use of debt, a proportional change in the return on common equity that is greater than a given proportional change in operating income; also, short for the financial leverage ratio.

Financial leverage ratio A measure of financial leverage calculated as average total assets divided by average total equity.

Financial risk The risk that environmental, social, or governance risk factors will result in significant costs or other losses to a company and its shareholders; the risk arising from a company's obligation to meet required payments under its financing agreements.

Financing activities Activities related to obtaining or repaying capital to be used in the business (e.g., equity and long-term debt).

Fintech Technological innovation in the design and delivery of financial services and products in the financial industry.

Firm commitment offering See *underwritten offering*.

First-degree price discrimination Where a monopolist is able to charge each customer the highest price the customer is willing to pay.

First lien debt Debt secured by a pledge of certain assets that could include buildings, but may also include property and equipment, licenses, patents, brands, etc.

First mortgage debt Debt secured by a pledge of a specific property.

Fiscal multiplier The ratio of a change in national income to a change in government spending.

Fiscal policy The use of taxes and government spending to affect the level of aggregate expenditures.

Fisher effect The thesis that the real rate of interest in an economy is stable over time so that changes in nominal interest rates are the result of changes in expected inflation.

Fisher index The geometric mean of the Laspeyres index.

Fixed charge coverage A solvency ratio measuring the number of times interest and lease payments are covered by operating income, calculated as (EBIT + lease payments) divided by (interest payments + lease payments).

Fixed costs Costs that remain at the same level regardless of a company's level of production and sales.

Fixed-for-floating interest rate swap An interest rate swap in which one party pays a fixed rate and the other pays a floating rate, with both sets of payments in the same currency. Also called *plain vanilla swap* or *vanilla swap*.

Fixed rate perpetual preferred stock Nonconvertible, non-callable preferred stock that has a fixed dividend rate and no maturity date.

Flags A technical analysis continuation pattern formed by parallel trendlines, typically over a short period.

Flat price The full price of a bond minus the accrued interest; also called the *quoted* or *clean* price.

Float In the context of customer receipts, the amount of money that is in transit between payments made by customers and the funds that are usable by the company.

Float-adjusted market-capitalization weighting An index weighting method in which the weight assigned to each constituent security is determined by adjusting its market capitalization for its market float.

Float factor An estimate of the average number of days it takes deposited checks to clear; average daily float divided by average daily deposit.

Floaters See *floating-rate notes*.

Floating-rate notes A note on which interest payments are not fixed, but instead vary from period to period depending on the current level of a reference interest rate.

Flotation cost Fees charged to companies by investment bankers and other costs associated with raising new capital.

Foreclosure Allows the lender to take possession of a mortgaged property if the borrower defaults and then sell it to recover funds.

Foreign currency reserves Holding by the central bank of non-domestic currency deposits and non-domestic bonds.

Foreign direct investment Direct investment by a firm in one country (the source country) in productive assets in a foreign country (the host country).

Foreign exchange gains (or losses) Gains (or losses) that occur when the exchange rate changes between the investor's currency and the currency that foreign securities are denominated in.

Foreign portfolio investment Shorter-term investment by individuals, firms, and institutional investors (e.g., pension funds) in foreign financial instruments such as foreign stocks and foreign government bonds.

Forward commitments Class of derivatives that provides the ability to lock in a price to transact in the future at a previously agreed-upon price.

Forward contract An agreement between two parties in which one party, the buyer, agrees to buy from the other party, the seller, an underlying asset at a later date for a price established at the start of the contract.

Forward curve A series of forward rates, each having the same timeframe.

Forward market For future delivery, beyond the usual settlement time period in the cash market.

Forward price The fixed price or rate at which the transaction scheduled to occur at the expiration of a forward contract will take place. This price is agreed on at the initiation date of the contract.

Forward rate The interest rate on a bond or money market instrument traded in a forward market. A forward rate can be interpreted as an incremental, or marginal, return for extending the time-to-maturity for an additional time period.

Forward rate agreements A forward contract calling for one party to make a fixed interest payment and the other to make an interest payment at a rate to be determined at the contract expiration.

Fractile A value at or below which a stated fraction of the data lies.

Fractional reserve banking Banking in which reserves constitute a fraction of deposits.

Free cash flow The actual cash that would be available to the company's investors after making all investments necessary to maintain the company as an ongoing enterprise (also referred to as free cash flow to the firm); the internally generated funds that can be distributed to the company's investors (e.g., shareholders and bondholders) without impairing the value of the company.

Free cash flow to equity (FCFE) The cash flow available to a company's common shareholders after all operating expenses, interest, and principal payments have been made, and necessary investments in working and fixed capital have been made.

Free-cash-flow-to-equity models Valuation models based on discounting expected future free cash flow to equity.

Free cash flow to the firm (FCFF) The cash flow available to the company's suppliers of capital after all operating expenses have been paid and necessary investments in working capital and fixed capital have been made.

Free float The number of shares that are readily and freely tradable in the secondary market.

Free trade When there are no government restrictions on a country's ability to trade.

Free trade areas One of the most prevalent forms of regional integration, in which all barriers to the flow of goods and services among members have been eliminated.

Frequency distribution A tabular display of data summarized into a relatively small number of intervals.

Frequency polygon A graph of a frequency distribution obtained by drawing straight lines joining successive points representing the class frequencies.

Full integration An ESG investment style that focuses on the explicit inclusion of ESG factors into the traditional financial analysis of individual stocks for the purpose of valuation (e.g., as inputs into cash flow forecasts and/or cost-of-capital estimates).

Full price The price of a security with accrued interest; also called the *invoice* or *dirty* price.

Fundamental analysis The examination of publicly available information and the formulation of forecasts to estimate the intrinsic value of assets.

Fundamental value The underlying or true value of an asset based on an analysis of its qualitative and quantitative characteristics. Also called *intrinsic value*.

Fundamental weighting An index weighting method in which the weight assigned to each constituent security is based on its underlying company's size. It attempts to address the disadvantages of market-capitalization weighting by using measures that are independent of the constituent security's price.

Funds of hedge funds Funds that hold a portfolio of hedge funds, more commonly shortened to *funds of funds*.

Future value (FV) The amount to which a payment or series of payments will grow by a stated future date.

Futures contract A variation of a forward contract that has essentially the same basic definition but with some additional features, such as a clearinghouse guarantee against credit losses, a daily settlement of gains and losses, and an organized electronic or floor trading facility.

Futures price The agreed-upon price of a futures contract.

FX swap The combination of a spot and a forward FX transaction.

G-spread The yield spread in basis points over an actual or interpolated government bond.

Gains Asset inflows not directly related to the ordinary activities of the business.

Game theory The set of tools decision makers use to incorporate responses by rival decision makers into their strategies.

Gamma A numerical measure of how sensitive an option's delta (the sensitivity of the derivative's price) is to a change in the value of the underlying.

GDP deflator A gauge of prices and inflation that measures the aggregate changes in prices across the overall economy.

General partner The partner that runs the business and ultimately bears unlimited liability for the business's debts and obligations.

Geometric mean A measure of central tendency computed by taking the *n*th root of the product of *n* non-negative values.

Giffen goods Goods that are consumed more as the price of the good rises because it is a very inferior good whose income effect overwhelms its substitution effect when price changes.

Gilts Bonds issued by the UK government.

Giro system An electronic payment system used widely in Europe and Japan.

Global depository receipt A depository receipt that is issued outside of the company's home country and outside of the United States.

Global minimum-variance portfolio The portfolio on the minimum-variance frontier with the smallest variance of return.

Global registered share A common share that is traded on different stock exchanges around the world in different currencies.

Gold standard With respect to a currency, if a currency is on the gold standard a given amount can be converted into a prespecified amount of gold.

Golden cross A technical analysis term that describes a situation where a short-term moving average crosses from below a longer-term moving average to above it; this movement is considered bullish.

Good-on-close An execution instruction specifying that an order can only be filled at the close of trading. Also called *market on close*.

Good-on-open An execution instruction specifying that an order can only be filled at the opening of trading.

Good-till-cancelled order An order specifying that it is valid until the entity placing the order has cancelled it (or, commonly, until some specified amount of time such as 60 days has elapsed, whichever comes sooner).

Goodwill An intangible asset that represents the excess of the purchase price of an acquired company over the value of the net assets acquired.

Government equivalent yield A yield that restates a yield-to-maturity based on 30/360 day-count to one based on actual/actual.

Green bonds A bond used in green finance whereby the proceeds are earmarked towards environmental-related products.

Green finance A type of finance that addresses environmental concerns while achieving economic growth.

Grey market The forward market for bonds about to be issued. Also called "when issued" market.

Gross domestic product The market value of all final goods and services produced within the economy in a given period of time (output definition) or, equivalently, the aggregate income earned by all households, all companies, and the government within the economy in a given period of time (income definition).

Gross margin Sales minus the cost of sales (i.e., the cost of goods sold for a manufacturing company).

Gross profit Sales minus the cost of sales (i.e., the cost of goods sold for a manufacturing company).

Gross profit margin The ratio of gross profit to revenues.

Grouping by function With reference to the presentation of expenses in an income statement, the grouping together of expenses serving the same function, e.g. all items that are costs of goods sold.

Grouping by nature With reference to the presentation of expenses in an income statement, the grouping together of expenses by similar nature, e.g., all depreciation expenses.

Growth cyclical A term sometimes used to describe companies that are growing rapidly on a long-term basis but that still experience above-average fluctuation in their revenues and profits over the course of a business cycle.

Growth investors With reference to equity investors, investors who seek to invest in high-earnings-growth companies.

Guarantee certificate A type of structured financial instrument that provides investors capital protection. It combines a zero-coupon bond and a call option on some underlying asset.

Haircut See *repo margin*.

Harmonic mean A type of weighted mean computed by averaging the reciprocals of the observations, then taking the reciprocal of that average.

Head and shoulders pattern In technical analysis, a reversal pattern that is formed in three parts: a left shoulder, head, and right shoulder; used to predict a change from an uptrend to a downtrend.

Headline inflation The inflation rate calculated based on the price index that includes all goods and services in an economy.

Hedge funds Private investment vehicles that typically use leverage, derivatives, and long and short investment strategies.

Hedge portfolio A hypothetical combination of the derivative and its underlying that eliminates risk.

Held-to-maturity Debt (fixed-income) securities that a company intends to hold to maturity; these are presented at their original cost, updated for any amortisation of discounts or premiums.

Herding Clustered trading that may or may not be based on information.

Hidden order An order that is exposed not to the public but only to the brokers or exchanges that receive it.

High-frequency trading A form of algorithmic trading that makes use of vast quantities of data to execute trades on ultra-high-speed networks in fractions of a second.

High-water mark The highest value, net of fees, that a fund has reached in history. It reflects the highest cumulative return used to calculate an incentive fee.

Histogram A bar chart of data that have been grouped into a frequency distribution.

Historical cost In reference to assets, the amount paid to purchase an asset, including any costs of acquisition and/or preparation; with reference to liabilities, the amount of proceeds received in exchange in issuing the liability.

Historical equity risk premium approach An estimate of a country's equity risk premium that is based upon the historical averages of the risk-free rate and the rate of return on the market portfolio.

Historical simulation Another term for the historical method of estimating VaR. This term is somewhat misleading in that the method involves not a *simulation* of the past but rather what *actually happened* in the past, sometimes adjusted to reflect the fact that a different portfolio may have existed in the past than is planned for the future.

Holder-of-record date The date that a shareholder listed on the corporation's books will be deemed to have ownership of the shares for purposes of receiving an upcoming dividend.

Holding period return The return that an investor earns during a specified holding period; a synonym for total return.

Homogeneity of expectations The assumption that all investors have the same economic expectations and thus have the same expectations of prices, cash flows, and other investment characteristics.

Horizon yield The internal rate of return between the total return (the sum of reinvested coupon payments and the sale price or redemption amount) and the purchase price of the bond.

Horizontal analysis Common-size analysis that involves comparing a specific financial statement with that statement in prior or future time periods; also, cross-sectional analysis of one company with another.

Horizontal demand schedule Implies that at a given price, the response in the quantity demanded is infinite.

Hostile takeover An attempt by one entity to acquire a company without the consent of the company's management.

Household A person or a group of people living in the same residence, taken as a basic unit in economic analysis.

Human capital The accumulated knowledge and skill that workers acquire from education, training, or life experience and the corresponding present value of future earnings to be generated by said skilled individual.

Hurdle rate The rate of return that must be met for a project to be accepted.

Hypothesis With reference to statistical inference, a statement about one or more populations.

Hypothesis testing With reference to statistical inference, the subdivision dealing with the testing of hypotheses about one or more populations.

I-spread The yield spread of a specific bond over the standard swap rate in that currency of the same tenor.

Iceberg order An order in which the display size is less than the order's full size.

If-converted method A method for accounting for the effect of convertible securities on earnings per share (EPS) that specifies what EPS would have been if the convertible securities had been converted at the beginning of the period, taking account of the effects of conversion on net income and the weighted average number of shares outstanding.

Immediate or cancel order An order that is valid only upon receipt by the broker or exchange. If such an order cannot be filled in part or in whole upon receipt, it cancels immediately. Also called *fill or kill*.

Impact lag The lag associated with the result of actions affecting the economy with delay.

Implicit price deflator for GDP A gauge of prices and inflation that measures the aggregate changes in prices across the overall economy.

Implied forward rates Calculated from spot rates, an implied forward rate is a break-even reinvestment rate that links the return on an investment in a shorter-term zero-coupon bond to the return on an investment in a longer-term zero-coupon bond.

Implied volatility The volatility that option traders use to price an option, implied by the price of the option and a particular option-pricing model.

Import license Specifies the quantity of a good that can be imported into a country.

Imports Goods and services that a domestic economy (i.e., house-holds, firms, and government) purchases from other countries.

In the money Options that, if exercised, would result in the value received being worth more than the payment required to exercise.

Incentive fee Fees paid to the general partner from the limited partner(s) based on realized net profits.

Income Increases in economic benefits in the form of inflows or enhancements of assets, or decreases of liabilities that result in an increase in equity (other than increases resulting from contributions by owners).

Income elasticity of demand A measure of the responsiveness of demand to changes in income, defined as the percentage change in quantity demanded divided by the percentage change in income.

Income tax paid The actual amount paid for income taxes in the period; not a provision, but the actual cash outflow.

Income tax payable The income tax owed by the company on the basis of taxable income.

Income trust A type of equity ownership vehicle established as a trust issuing ownership shares known as units.

Increasing marginal returns When the marginal product of a resource increases as additional units of that input are employed.

Increasing returns to scale When a production process leads to increases in output that are proportionately larger than the increase in inputs.

Incremental cash flow The cash flow that is realized because of a decision; the changes or increments to cash flows resulting from a decision or action.

Indenture Legal contract that describes the form of a bond, the obligations of the issuer, and the rights of the bondholders. Also called the *trust deed*.

Independent With reference to events, the property that the occurrence of one event does not affect the probability of another event occurring.

Independent projects Independent projects are projects whose cash flows are independent of each other.

Independently and identically distributed (IID) With respect to random variables, the property of random variables that are independent of each other but follow the identical probability distribution.

Index-linked bond Bond for which coupon payments and/or principal repayment are linked to a specified index.

Index of Leading Economic Indicators A composite of economic variables used by analysts to predict future economic conditions.

Indexing An investment strategy in which an investor constructs a portfolio to mirror the performance of a specified index.

Indifference curve A curve representing all the combinations of two goods or attributes such that the consumer is entirely indifferent among them.

Indirect format With reference to cash flow statements, a format for the presentation of the statement which, in the operating cash flow section, begins with net income then shows additions and subtractions to arrive at operating cash flow. Also called *indirect method*.

Indirect method See *indirect format*.

Indirect taxes Taxes such as taxes on spending, as opposed to direct taxes.

Industry A group of companies offering similar products and/or services.
Industry analysis The analysis of a specific branch of manufacturing, service, or trade.
Inelastic Said of a good or service when the magnitude of elasticity is less than one. Insensitive to price changes.
Inferior goods A good whose consumption decreases as income increases.
Inflation The percentage increase in the general price level from one period to the next; a sustained rise in the overall level of prices in an economy.
Inflation-linked bond Type of index-linked bond that offers investors protection against inflation by linking the bond's coupon payments and/or the principal repayment to an index of consumer prices. Also called *linkers*.
Inflation premium An extra return that compensates investors for expected inflation.
Inflation rate The percentage change in a price index—that is, the speed of overall price level movements.
Inflation Reports A type of economic publication put out by many central banks.
Inflation uncertainty The degree to which economic agents view future rates of inflation as difficult to forecast.
Information cascade The transmission of information from those participants who act first and whose decisions influence the decisions of others.
Information-motivated traders Traders that trade to profit from information that they believe allows them to predict future prices.
Informationally efficient market A market in which asset prices reflect new information quickly and rationally.
Initial coin offering An unregulated process whereby companies raise capital by selling crypto tokens to investors in exchange for fiat money or another agreed-upon cryptocurrency.
Initial margin The amount that must be deposited in a clearinghouse account when entering into a futures contract.
Initial margin requirement The margin requirement on the first day of a transaction as well as on any day in which additional margin funds must be deposited.
Initial public offering (IPO) The first issuance of common shares to the public by a formerly private corporation.
Input productivity The amount of output produced by workers in a given period of time—for example, output per hour worked; measures the efficiency of labor.
Intangible assets Assets lacking physical substance, such as patents and trademarks.
Interbank market The market of loans and deposits between banks for maturities ranging from overnight to one year.
Interbank money market The market of loans and deposits between banks for maturities ranging from overnight to one year.
Interest Payment for lending funds.
Interest coverage A solvency ratio calculated as EBIT divided by interest payments.
Interest-only mortgage A loan in which no scheduled principal repayment is specified for a certain number of years.
Interest rate A rate of return that reflects the relationship between differently dated cash flows; a discount rate.
Interest rate swap A swap in which the underlying is an interest rate. Can be viewed as a currency swap in which both currencies are the same and can be created as a combination of currency swaps.
Intergenerational data mining A form of data mining that applies information developed by previous researchers using a dataset to guide current research using the same or a related dataset.
Intermarket analysis A field within technical analysis that combines analysis of major categories of securities—namely, equities, bonds, currencies, and commodities—to identify market trends and possible inflections in a trend.
Internal rate of return (IRR) The discount rate that makes net present value equal 0; the discount rate that makes the present value of an investment's costs (outflows) equal to the present value of the investment's benefits (inflows).
Internet of Things A network arrangement of structures and devices whereby the objects on the network are able to interact and share information.
Interpolated spread The yield spread of a specific bond over the standard swap rate in that currency of the same tenor.
Interquartile range The difference between the third and first quartiles of a dataset.
Interval With reference to grouped data, a set of values within which an observation falls.
Interval scale A measurement scale that not only ranks data but also gives assurance that the differences between scale values are equal.
Intrinsic value See *exercise value*.
Inventory blanket lien The use of inventory as collateral for a loan. Though the lender has claim to some or all of the company's inventory, the company may still sell or use the inventory in the ordinary course of business.
Inventory investment Net change in business inventory.
Inventory turnover An activity ratio calculated as cost of goods sold divided by average inventory.
Inverse demand function A restatement of the demand function in which price is stated as a function of quantity.
Inverse floater A type of leveraged structured financial instrument. The cash flows are adjusted periodically and move in the opposite direction of changes in the reference rate.
Investing activities Activities associated with the acquisition and disposal of property, plant, and equipment; intangible assets; other long-term assets; and both long-term and short-term investments in the equity and debt (bonds and loans) issued by other companies.
Investment banks Financial intermediaries that provide advice to their mostly corporate clients and help them arrange transactions such as initial and seasoned securities offerings.
Investment opportunity schedule A graphical depiction of a company's investment opportunities ordered from highest to lowest expected return. A company's optimal capital budget is found where the investment opportunity schedule intersects with the company's marginal cost of capital.
Investment policy statement (IPS) A written planning document that describes a client's investment objectives and risk tolerance over a relevant time horizon, along with constraints that apply to the client's portfolio.
Investment property Property used to earn rental income or capital appreciation (or both).
January effect Calendar anomaly that stock market returns in January are significantly higher compared to the rest of the months of the year, with most of the abnormal returns reported during the first five trading days in January. Also called *turn-of-the-year effect*.
Joint probability The probability of the joint occurrence of stated events.

Joint probability function A function giving the probability of joint occurrences of values of stated random variables.
Just-in-time (JIT) method Method of managing inventory that minimizes in-process inventory stocks.
Key rate duration A method of measuring the interest rate sensitivities of a fixed-income instrument or portfolio to shifts in key points along the yield curve.
Keynesians Economists who believe that fiscal policy can have powerful effects on aggregate demand, output, and employment when there is substantial spare capacity in an economy.
Kondratieff wave A 54-year long economic cycle postulated by Nikolai Kondratieff.
Kurtosis The statistical measure that indicates the combined weight of the tails of a distribution relative to the rest of the distribution.
Labor force The portion of the working age population (over the age of 16) that is employed or is available for work but not working (unemployed).
Labor productivity The quantity of goods and services (real GDP) that a worker can produce in one hour of work.
Laddering strategy A form of active strategy which entails scheduling maturities on a systematic basis within the investment portfolio such that investments are spread out equally over the term of the ladder.
Lagging economic indicators Turning points that take place later than those of the overall economy; they are believed to have value in identifying the economy's past condition.
Laspeyres index A price index created by holding the composition of the consumption basket constant.
Law of demand The principle that as the price of a good rises, buyers will choose to buy less of it, and as its price falls, they will buy more.
Law of diminishing marginal returns The observation that a variable factor's marginal product must eventually fall as more of it is added to a fixed amount of the other factors.
Law of diminishing returns The smallest output that a firm can produce such that its long run average costs are minimized.
Law of one price The condition in a financial market in which two equivalent financial instruments or combinations of financial instruments can sell for only one price. Equivalent to the principle that no arbitrage opportunities are possible.
Lead underwriter The lead investment bank in a syndicate of investment banks and broker–dealers involved in a securities underwriting.
Leading economic indicators Turning points that usually precede those of the overall economy; they are believed to have value for predicting the economy's future state, usually near-term.
Legal tender Something that must be accepted when offered in exchange for goods and services.
Lender of last resort An entity willing to lend money when no other entity is ready to do so.
Leptokurtic Describes a distribution that has fatter tails than a normal distribution.
Lessee The party obtaining the use of an asset through a lease.
Lessor The owner of an asset that grants the right to use the asset to another party.
Letter of credit Form of external credit enhancement whereby a financial institution provides the issuer with a credit line to reimburse any cash flow shortfalls from the assets backing the issue.
Level of significance The probability of a Type I error in testing a hypothesis.
Leverage In the context of corporate finance, leverage refers to the use of fixed costs within a company's cost structure. Fixed costs that are operating costs (such as depreciation or rent) create operating leverage. Fixed costs that are financial costs (such as interest expense) create financial leverage.
Leveraged buyout A transaction whereby the target company's management team converts the target to a privately held company by using heavy borrowing to finance the purchase of the target company's outstanding shares.
Liabilities Present obligations of an enterprise arising from past events, the settlement of which is expected to result in an outflow of resources embodying economic benefits; creditors' claims on the resources of a company.
Life-cycle stage The stage of the life cycle: embryonic, growth, shakeout, mature, declining.
LIFO layer liquidation With respect to the application of the LIFO inventory method, the liquidation of old, relatively low-priced inventory; happens when the volume of sales rises above the volume of recent purchases so that some sales are made from relatively old, low-priced inventory. Also called *LIFO liquidation*.
LIFO method The last in, first out, method of accounting for inventory, which matches sales against the costs of items of inventory in the reverse order the items were placed in inventory (i.e., inventory produced or acquired last are assumed to be sold first).
LIFO reserve The difference between the reported LIFO inventory carrying amount and the inventory amount that would have been reported if the FIFO method had been used (in other words, the FIFO inventory value less the LIFO inventory value).
Likelihood The probability of an observation, given a particular set of conditions.
Limit down A limit move in the futures market in which the price at which a transaction would be made is at or below the lower limit.
Limit order Instructions to a broker or exchange to obtain the best price immediately available when filling an order, but in no event accept a price higher than a specified (limit) price when buying or accept a price lower than a specified (limit) price when selling.
Limit order book The book or list of limit orders to buy and sell that pertains to a security.
Limit up A limit move in the futures market in which the price at which a transaction would be made is at or above the upper limit.
Limitations on liens Meant to put limits on how much secured debt an issuer can have.
Limited partners Partners with limited liability. Limited partnerships in hedge and private equity funds are typically restricted to investors who are expected to understand and to be able to assume the risks associated with the investments.
Line chart In technical analysis, a plot of price data, typically closing prices, with a line connecting the points.
Linear interpolation The estimation of an unknown value on the basis of two known values that bracket it, using a straight line between the two known values.
Linear scale A scale in which equal distances correspond to equal absolute amounts. Also called *arithmetic scale.*
Linker See *inflation-linked bond.*

Liquid market Said of a market in which traders can buy or sell with low total transaction costs when they want to trade.

Liquidation To sell the assets of a company, division, or subsidiary piecemeal, typically because of bankruptcy; the form of bankruptcy that allows for the orderly satisfaction of creditors' claims after which the company ceases to exist.

Liquidity The ability to purchase or sell an asset quickly and easily at a price close to fair market value. The ability to meet short-term obligations using assets that are the most readily converted into cash.

Liquidity premium An extra return that compensates investors for the risk of loss relative to an investment's fair value if the investment needs to be converted to cash quickly.

Liquidity ratios Financial ratios measuring the company's ability to meet its short-term obligations.

Liquidity risk The risk that a financial instrument cannot be purchased or sold without a significant concession in price due to the size of the market.

Liquidity trap A condition in which the demand for money becomes infinitely elastic (horizontal demand curve) so that injections of money into the economy will not lower interest rates or affect real activity.

Load fund A mutual fund in which, in addition to the annual fee, a percentage fee is charged to invest in the fund and/or for redemptions from the fund.

Loan-to-value ratio The ratio of a property's purchase price to the amount of its mortgage.

Lockbox system A payment system in which customer payments are mailed to a post office box and the banking institution retrieves and deposits these payments several times a day, enabling the company to have use of the fund sooner than in a centralized system in which customer payments are sent to the company.

Locked limit A condition in the futures markets in which a transaction cannot take place because the price would be beyond the limits.

Lockup period The minimum holding period before investors are allowed to make withdrawals or redeem shares from a fund.

Logarithmic scale A scale in which equal distances represent equal proportional changes in the underlying quantity.

London interbank offered rate (Libor) Collective name for multiple rates at which a select set of banks believe they could borrow unsecured funds from other banks in the London interbank market for different currencies and different borrowing periods ranging from overnight to one year.

Long The buyer of a derivative contract. Also refers to the position of owning a derivative.

Long-lived assets Assets that are expected to provide economic benefits over a future period of time, typically greater than one year. Also called *long-term assets*.

Long position A position in an asset or contract in which one owns the asset or has an exercisable right under the contract.

Long-run average total cost The curve describing average total cost when no costs are considered fixed.

Longitudinal data Observations on characteristic(s) of the same observational unit through time.

Look-ahead bias A bias caused by using information that was unavailable on the test date.

Loss aversion The tendency of people to dislike losses more than they like comparable gains.

Loss severity Portion of a bond's value (including unpaid interest) an investor loses in the event of default.

Losses Asset outflows not directly related to the ordinary activities of the business.

Lower bound The lowest possible value of an option.

M^2 A measure of what a portfolio would have returned if it had taken on the same total risk as the market index.

M^2 alpha Difference between the risk-adjusted performance of the portfolio and the performance of the benchmark.

Macaulay duration The approximate amount of time a bond would have to be held for the market discount rate at purchase to be realized if there is a single change in interest rate. It indicates the point in time when the coupon reinvestment and price effects of a change in yield-to- maturity offset each other.

Machine learning Computer based techniques that seek to extract knowledge from large amounts of data by "learning" from known examples and then generating structure or predictions. ML algorithms aim to "find the pattern, apply the pattern."

Macroeconomics The branch of economics that deals with aggregate economic quantities, such as national output and national income.

Maintenance covenants Covenants in bank loan agreements that require the borrower to satisfy certain financial ratio tests while the loan is outstanding.

Maintenance margin The minimum amount that is required by a futures clearinghouse to maintain a margin account and to protect against default. Participants whose margin balances drop below the required maintenance margin must replenish their accounts.

Maintenance margin requirement The margin requirement on any day other than the first day of a transaction.

Management buy-ins Leveraged buyout in which the current management team is being replaced and the acquiring team will be involved in managing the company.

Management buyout A leveraged buyout event in which a group of investors consisting primarily of the company's existing management purchase at least controlling interest in its outstanding shares. At the extreme, they may purchase all shares and take the company private.

Management fee A fee based on assets under management or committed capital, as applicable, also called a *base fee*.

Manufacturing resource planning (MRP) The incorporation of production planning into inventory management. A MRP analysis provides both a materials acquisition schedule and a production schedule.

Margin The amount of money that a trader deposits in a margin account. The term is derived from the stock market practice in which an investor borrows a portion of the money required to purchase a certain amount of stock. In futures markets, there is no borrowing so the margin is more of a down payment or performance bond.

Margin bond A cash deposit required by the clearinghouse from the participants to a contract to provide a credit guarantee. Also called a *performance bond*.

Margin call A request for the short to deposit additional funds to bring their balance up to the initial margin.

Margin loan Money borrowed from a broker to purchase securities.

Marginal cost The cost of producing an additional unit of a good.

Marginal probability The probability of an event *not* conditioned on another event.

Marginal product Measures the productivity of each unit of input and is calculated by taking the difference in total product from adding another unit of input (assuming other resource quantities are held constant).

Marginal propensity to consume The proportion of an additional unit of disposable income that is consumed or spent; the change in consumption for a small change in income.

Marginal propensity to save The proportion of an additional unit of disposable income that is saved (not spent).

Marginal revenue The change in total revenue divided by the change in quantity sold; simply, the additional revenue from selling one more unit.

Marginal value curve A curve describing the highest price consumers are willing to pay for each additional unit of a good.

Mark to market The revaluation of a financial asset or liability to its current market value or fair value.

Market anomaly Change in the price or return of a security that cannot directly be linked to current relevant information known in the market or to the release of new information into the market.

Market bid–ask spread The difference between the best bid and the best offer.

Market-capitalization weighting An index weighting method in which the weight assigned to each constituent security is determined by dividing its market capitalization by the total market capitalization (sum of the market capitalization) of all securities in the index. Also called *value weighting*.

Market discount rate The rate of return required by investors given the risk of the investment in a bond; also called the *required yield* or the *required rate of return*.

Market float The number of shares that are available to the investing public.

Market liquidity risk The risk that the price at which investors can actually transact—buying or selling—may differ from the price indicated in the market.

Market model A regression equation that specifies a linear relationship between the return on a security (or portfolio) and the return on a broad market index.

Market multiple models Valuation models based on share price multiples or enterprise value multiples.

Market-on-close An execution instruction specifying that an order can only be filled at the close of trading.

Market order Instructions to a broker or exchange to obtain the best price immediately available when filling an order.

Market-oriented investors With reference to equity investors, investors whose investment disciplines cannot be clearly categorized as value or growth.

Market rate of interest The rate demanded by purchasers of bonds, given the risks associated with future cash payment obligations of the particular bond issue.

Market risk The risk that arises from movements in interest rates, stock prices, exchange rates, and commodity prices.

Market value The price at which an asset or security can currently be bought or sold in an open market.

Marketable limit order A buy limit order in which the limit price is placed above the best offer, or a sell limit order in which the limit price is placed below the best bid. Such orders generally will partially or completely fill right away.

Markowitz efficient frontier The graph of the set of portfolios offering the maximum expected return for their level of risk (standard deviation of return).

Matching principle The accounting principle that expenses should be recognized in the same period in which the associated revenue is recognized.

Matching strategy An active investment strategy that includes intentional matching of the timing of cash outflows with investment maturities.

Matrix pricing Process of estimating the market discount rate and price of a bond based on the quoted or flat prices of more frequently traded comparable bonds.

Maturity premium An extra return that compensates investors for the increased sensitivity of the market value of debt to a change in market interest rates as maturity is extended.

Maturity structure A factor explaining the differences in yields on similar bonds; also called *term structure*.

Mean absolute deviation With reference to a sample, the mean of the absolute values of deviations from the sample mean.

Mean–variance analysis An approach to portfolio analysis using expected means, variances, and covariances of asset returns.

Measure of central tendency A quantitative measure that specifies where data are centered.

Measure of value A standard for measuring value; a function of money.

Measurement scales A scheme of measuring differences. The four types of measurement scales are nominal, ordinal, interval, and ratio.

Measures of location A quantitative measure that describes the location or distribution of data; includes not only measures of central tendency but also other measures such as percentiles.

Median The value of the middle item of a set of items that has been sorted into ascending or descending order; the 50th percentile.

Medium of exchange Any asset that can be used to purchase goods and services or to repay debts; a function of money.

Medium-term note A corporate bond offered continuously to investors by an agent of the issuer, designed to fill the funding gap between commercial paper and long-term bonds.

Menu costs A cost of inflation in which businesses constantly have to incur the costs of changing the advertised prices of their goods and services.

Mesokurtic Describes a distribution with kurtosis identical to that of the normal distribution.

Mezzanine financing Debt or preferred shares with a relationship to common equity resulting from a feature such as attached warrants or conversion options. Mezzanine financing is subordinate to both senior and high-yield debt but is senior to equity. It is referred to as "mezzanine" because of its location on the balance sheet.

Microeconomics The branch of economics that deals with markets and decision making of individual economic units, including consumers and businesses.

Minimum efficient scale The smallest output that a firm can produce such that its long-run average total cost is minimized.

Minimum-variance portfolio The portfolio with the minimum variance for each given level of expected return.

Minority shareholders A particular shareholder or block of shareholders holding a small proportion of a company's outstanding shares, resulting in a limited ability to exercise control in voting activities.

Minsky moment Named for Hyman Minksy: A point in a business cycle when, after individuals become overextended in borrowing to finance speculative investments, people start realizing that something is likely to go wrong and a panic ensues leading to asset sell-offs.

Mismatching strategy An active investment strategy whereby the timing of cash outflows is not matched with investment maturities.

Modal interval With reference to grouped data, the most frequently occurring interval.

Mode The most frequently occurring value in a set of observations.

Modern portfolio theory (MPT) The analysis of rational portfolio choices based on the efficient use of risk.

Modified duration A measure of the percentage price change of a bond given a change in its yield-to-maturity.

Momentum oscillators A graphical representation of market sentiment that is constructed from price data and calculated so that it oscillates either between a high and a low or around some number.

Monetarists Economists who believe that the rate of growth of the money supply is the primary determinant of the rate of inflation.

Monetary policy Actions taken by a nation's central bank to affect aggregate output and prices through changes in bank reserves, reserve requirements, or its target interest rate.

Monetary transmission mechanism The process whereby a central bank's interest rate gets transmitted through the economy and ultimately affects the rate of increase of prices.

Monetary union An economic union in which the members adopt a common currency.

Money A generally accepted medium of exchange and unit of account.

Money convexity For a bond, the annual or approximate convexity multiplied by the full price.

Money creation The process by which changes in bank reserves translate into changes in the money supply.

Money duration A measure of the price change in units of the currency in which the bond is denominated given a change in its yield-to-maturity.

Money market The market for short-term debt instruments (one-year maturity or less).

Money market securities Fixed-income securities with maturities at issuance of one year or less.

Money market yield A yield on a basis comparable to the quoted yield on an interest-bearing money market instrument that pays interest on a 360-day basis; the annualized holding period yield, assuming a 360-day year.

Money multiplier Describes how a change in reserves is expected to affect the money supply; in its simplest form, 1 divided by the reserve requirement.

Money neutrality The thesis that an increase in the money supply leads in the long-run to an increase in the price level, while leaving real variables like output and employment unaffected.

Money-weighted return The internal rate of return on a portfolio, taking account of all cash flows.

Moneyness The relationship between the price of the underlying and an option's exercise price.

Monopolistic competition Highly competitive form of imperfect competition; the competitive characteristic is a notably large number of firms, while the monopoly aspect is the result of product differentiation.

Monopoly In pure monopoly markets, there are no substitutes for the given product or service. There is a single seller, which exercises considerable power over pricing and output decisions.

Monte Carlo simulation An approach to estimating a probability distribution of outcomes to examine what might happen if particular risks are faced. This method is widely used in the sciences as well as in business to study a variety of problems.

Moral principles Beliefs regarding what is good, acceptable, or obligatory behavior and what is bad, unacceptable, or forbidden behavior.

Mortgage-backed securities Debt obligations that represent claims to the cash flows from pools of mortgage loans, most commonly on residential property.

Mortgage loan A loan secured by the collateral of some specified real estate property that obliges the borrower to make a predetermined series of payments to the lender.

Mortgage pass-through security A security created when one or more holders of mortgages form a pool of mortgages and sell shares or participation certificates in the pool.

Mortgage rate The interest rate on a mortgage loan; also called *contract rate* or *note rate*.

Moving average The average of the closing price of a security over a specified number of periods. With each new period, the average is recalculated.

Moving-average convergence/divergence oscillator (MACD) A momentum oscillator that is constructed based on the difference between short-term and long-term moving averages of a security's price.

Multi-factor model A model that explains a variable in terms of the values of a set of factors.

Multi-market indexes Comprised of indexes from different countries, designed to represent multiple security markets.

Multi-step format With respect to the format of the income statement, a format that presents a subtotal for gross profit (revenue minus cost of goods sold).

Multilateral trading facilities See *alternative trading systems*.

Multinational corporation A company operating in more than one country or having subsidiary firms in more than one country.

Multiplication rule for probabilities The rule that the joint probability of events A and B equals the probability of A given B times the probability of B.

Multiplier models Valuation models based on share price multiples or enterprise value multiples.

Multivariate distribution A probability distribution that specifies the probabilities for a group of related random variables.

Multivariate normal distribution A probability distribution for a group of random variables that is completely defined by the means and variances of the variables plus all the correlations between pairs of the variables.

Municipal bonds A type of non-sovereign bond issued by a state or local government in the United States. It very often (but not always) offers income tax exemptions.

Munis A type of non-sovereign bond issued by a state or local government in the United States. It very often (but not always) offers income tax exemptions.

Mutual fund A comingled investment pool in which investors in the fund each have a pro-rata claim on the income and value of the fund.

Mutually exclusive projects Mutually exclusive projects compete directly with each other. For example, if Projects A and B are mutually exclusive, you can choose A or B, but you cannot choose both.

***n* Factorial** For a positive integer *n*, the product of the first *n* positive integers; 0 factorial equals 1 by definition. *n* factorial is written as *n*!.

Narrow money The notes and coins in circulation in an economy, plus other very highly liquid deposits.

Nash equilibrium When two or more participants in a non-coop-erative game have no incentive to deviate from their respective equilibrium strategies given their opponent's strategies.

National income The income received by all factors of production used in the generation of final output. National income equals gross domestic product (or, in some countries, gross national product) minus the capital consumption allowance and a statistical discrepancy.

Natural language processing Computer programs developed to analyze and interpret human language.

Natural rate of unemployment Effective unemployment rate, below which pressure emerges in labor markets.

Negative screening An ESG investment style that focuses on the exclusion of certain sectors, companies, or practices in a fund or portfolio on the basis of specific ESG criteria.

Neo-Keynesians A group of dynamic general equilibrium models that assume slow-to-adjust prices and wages.

Net book value The remaining (undepreciated) balance of an asset's purchase cost. For liabilities, the face value of a bond minus any unamortized discount, or plus any unamortized premium.

Net exports The difference between the value of a country's exports and the value of its imports (i.e., value of exports minus imports).

Net income The difference between revenue and expenses; what remains after subtracting all expenses (including depreciation, interest, and taxes) from revenue.

Net operating cycle An estimate of the average time that elapses between paying suppliers for materials and collecting cash from the subsequent sale of goods produced.

Net present value (NPV) The present value of an investment's cash inflows (benefits) minus the present value of its cash outflows (costs).

Net profit margin An indicator of profitability, calculated as net income divided by revenue; indicates how much of each dollar of revenues is left after all costs and expenses. Also called *profit margin* or *return on sales*.

Net realisable value Estimated selling price in the ordinary course of business less the estimated costs necessary to make the sale.

Net revenue Revenue after adjustments (e.g., for estimated returns or for amounts unlikely to be collected).

Net tax rate The tax rate net of transfer payments.

Neural networks Computer programs based on how our own brains learn and process information.

Neutral rate of interest The rate of interest that neither spurs on nor slows down the underlying economy.

New classical macroeconomics An approach to macroeconomics that seeks the macroeconomic conclusions of individuals maximizing utility on the basis of rational expectations and companies maximizing profits.

New Keynesians A group of dynamic general equilibrium models that assume slow-to-adjust prices and wages.

No-load fund A mutual fund in which there is no fee for investing in the fund or for redeeming fund shares, although there is an annual fee based on a percentage of the fund's net asset value.

Node Each value on a binomial tree from which successive moves or outcomes branch.

Nominal GDP The value of goods and services measured at current prices.

Nominal rate A rate of interest based on the security's face value.

Nominal risk-free interest rate The sum of the real risk-free interest rate and the inflation premium.

Nominal scale A measurement scale that categorizes data but does not rank them.

Non-accelerating inflation rate of unemployment Effective unemployment rate, below which pressure emerges in labor markets.

Non-agency RMBS In the United States, securities issued by private entities that are not guaranteed by a federal agency or a GSE.

Non-cumulative preference shares Preference shares for which dividends that are not paid in the current or subsequent periods are forfeited permanently (instead of being accrued and paid at a later date).

Non-current assets Assets that are expected to benefit the company over an extended period of time (usually more than one year).

Non-current liabilities Obligations that broadly represent a probable sacrifice of economic benefits in periods generally greater than one year in the future.

Non-cyclical A company whose performance is largely independent of the business cycle.

Non-deliverable forwards Cash-settled forward contracts, used predominately with respect to foreign exchange forwards. Also called *contracts for differences.*

Non-financial risks Risks that arise from sources other than changes in the external financial markets, such as changes in accounting rules, legal environment, or tax rates.

Non-participating preference shares Preference shares that do not entitle shareholders to share in the profits of the company. Instead, shareholders are only entitled to receive a fixed dividend payment and the par value of the shares in the event of liquidation.

Non-recourse loan Loan in which the lender does not have a shortfall claim against the borrower, so the lender can look only to the property to recover the outstanding mortgage balance.

Non-renewable resources Finite resources that are depleted once they are consumed, such as oil and coal.

Non-sovereign bonds A bond issued by a government below the national level, such as a province, region, state, or city.

Non-sovereign government bonds A bond issued by a government below the national level, such as a province, region, state, or city.

Nonconventional cash flow In a nonconventional cash flow pattern, the initial outflow is not followed by inflows only, but the cash flows can flip from positive (inflows) to negative (outflows) again (or even change signs several times).

Nonparametric test A test that is not concerned with a parameter, or that makes minimal assumptions about the population from which a sample comes.

Nonsystematic risk Unique risk that is local or limited to a particular asset or industry that need not affect assets outside of that asset class.

Normal distribution A continuous, symmetric probability distribution that is completely described by its mean and its variance.

Normal goods Goods that are consumed in greater quantities as income increases.

Normal profit The level of accounting profit needed to just cover the implicit opportunity costs ignored in accounting costs.

Notching Ratings adjustment methodology where specific issues from the same borrower may be assigned different credit ratings.

Note rate See *mortgage rate.*

Notice period The length of time (typically 30–90 days) in advance that investors may be required to notify a fund of their intent to redeem some or all of their investment.

Notional principal An imputed principal amount.

Number of days of inventory An activity ratio equal to the number of days in a period divided by the inventory ratio for the period; an indication of the number of days a company ties up funds in inventory.

Number of days of payables An activity ratio equal to the number of days in a period divided by the payables turnover ratio for the period; an estimate of the average number of days it takes a company to pay its suppliers.

Number of days of receivables Estimate of the average number of days it takes to collect on credit accounts.

Objective probabilities Probabilities that generally do not vary from person to person; includes a priori and objective probabilities.

Off-the-run Seasoned government bonds are off-the-run securities; they are not the most recently issued or the most actively traded.

Offer The price at which a dealer or trader is willing to sell an asset, typically qualified by a maximum quantity (ask size).

Official interest rate An interest rate that a central bank sets and announces publicly; normally the rate at which it is willing to lend money to the commercial banks. Also called *official policy rate* or *policy rate*.

Official policy rate An interest rate that a central bank sets and announces publicly; normally the rate at which it is willing to lend money to the commercial banks.

Oligopoly Market structure with a relatively small number of firms supplying the market.

On-the-run The most recently issued and most actively traded sovereign securities.

One-sided hypothesis test A test in which the null hypothesis is rejected only if the evidence indicates that the population parameter is greater than (smaller than) θ_0. The alternative hypothesis also has one side.

One-tailed hypothesis test A test in which the null hypothesis is rejected only if the evidence indicates that the population parameter is greater than (smaller than) θ_0. The alternative hypothesis also has one side.

Open economy An economy that trades with other countries.

Open-end fund A mutual fund that accepts new investment money and issues additional shares at a value equal to the net asset value of the fund at the time of investment.

Open interest The number of outstanding contracts in a clearinghouse at any given time. The open interest figure changes daily as some parties open up new positions, while other parties offset their old positions.

Open market operations The purchase or sale of bonds by the national central bank to implement monetary policy. The bonds traded are usually sovereign bonds issued by the national government.

Operating activities Activities that are part of the day-to-day business functioning of an entity, such as selling inventory and providing services.

Operating breakeven The number of units produced and sold at which the company's operating profit is zero (revenues = operating costs).

Operating cash flow The net amount of cash provided from operating activities.

Operating cycle A measure of the time needed to convert raw materials into cash from a sale; it consists of the number of days of inventory and the number of days of receivables.

Operating efficiency ratios Ratios that measure how efficiently a company performs day-to-day tasks, such as the collection of receivables and management of inventory.

Operating lease An agreement allowing a lessee to use some asset for a period of time; essentially a rental.

Operating leverage The use of fixed costs in operations.

Operating profit A company's profits on its usual business activities before deducting taxes. Also called *operating income*.

Operating profit margin A profitability ratio calculated as operating income (i.e., income before interest and taxes) divided by revenue. Also called *operating margin*.

Operating risk The risk attributed to the operating cost structure, in particular the use of fixed costs in operations; the risk arising from the mix of fixed and variable costs; the risk that a company's operations may be severely affected by environmental, social, and governance risk factors.

Operational independence A bank's ability to execute monetary policy and set interest rates in the way it thought would best meet the inflation target.

Operational risk The risk that arises from inadequate or failed people, systems, and internal policies, procedures, and processes, as well as from external events that are beyond the control of the organization but that affect its operations.

Operationally efficient Said of a market, a financial system, or an economy that has relatively low transaction costs.

Opportunity cost The value that investors forgo by choosing a particular course of action; the value of something in its best alternative use.

Option A financial instrument that gives one party the right, but not the obligation, to buy or sell an underlying asset from or to another party at a fixed price over a specific period of time. Also referred to as *contingent claim* or *option contract.*

Option-adjusted price The value of the embedded option plus the flat price of the bond.

Option-adjusted spread OAS = Z-spread – Option value (in basis points per year).

Option-adjusted yield The required market discount rate whereby the price is adjusted for the value of the embedded option.

Option contract See *option*.

Option premium The amount of money a buyer pays and seller receives to engage in an option transaction.

Order A specification of what instrument to trade, how much to trade, and whether to buy or sell.

Order-driven markets A market (generally an auction market) that uses rules to arrange trades based on the orders that traders submit; in their pure form, such markets do not make use of dealers.

Order precedence hierarchy With respect to the execution of orders to trade, a set of rules that determines which orders execute before other orders.

Ordinal scale A measurement scale that sorts data into categories that are ordered (ranked) with respect to some characteristic.

Ordinary annuity An annuity with a first cash flow that is paid one period from the present.

Ordinary shares Equity shares that are subordinate to all other types of equity (e.g., preferred equity). Also called *common stock* or *common shares*.

Organized exchange A securities marketplace where buyers and seller can meet to arrange their trades.

Other comprehensive income Items of comprehensive income that are not reported on the income statement; comprehensive income minus net income.

Out-of-sample test A test of a strategy or model using a sample outside the time period on which the strategy or model was developed.

Out of the money Options that, if exercised, would require the payment of more money than the value received and therefore would not be currently exercised.

Outcome A possible value of a random variable.

Over-the-counter (OTC) markets A decentralized market where buy and sell orders initiated from various locations are matched through a communications network.

Overbought A market condition in which market sentiment is thought to be unsustainably bullish.

Overcollateralization Form of internal credit enhancement that refers to the process of posting more collateral than needed to obtain or secure financing.

Overfitting An undesirable result from fitting a model so closely to a dataset that it does not perform well on new data.

Overlay/portfolio tilt An ESG investment style that focuses on the use of certain investment strategies or products to change specific aggregate ESG characteristics of a fund or investment portfolio to a desired level (e.g., tilting an investment portfolio toward a desired carbon footprint).

Oversold A market condition in which market sentiment is thought to be unsustainably bearish.

Own price The price of a good or service itself (as opposed to the price of something else).

Own-price elasticity of demand The percentage change in quantity demanded for a percentage change in good's own price, holding all other things constant.

Owners' equity The excess of assets over liabilities; the residual interest of shareholders in the assets of an entity after deducting the entity's liabilities. Also called *shareholders' equity* or *shareholders' funds*.

Paasche index An index formula using the current composition of a basket of products.

Paired comparisons test A statistical test for differences based on paired observations drawn from samples that are dependent on each other.

Paired observations Observations that are dependent on each other.

Pairs arbitrage trade A trade in two closely related stocks involving the short sale of one and the purchase of the other.

Panel data Observations through time on a single characteristic of multiple observational units.

Par curve A sequence of yields-to-maturity such that each bond is priced at par value. The bonds are assumed to have the same currency, credit risk, liquidity, tax status, and annual yields stated for the same periodicity.

Par value The amount of principal on a bond.

Parallel shift A parallel yield curve shift implies that all rates change by the same amount in the same direction.

Parameter A descriptive measure computed from or used to describe a population of data, conventionally represented by Greek letters.

Parametric test Any test (or procedure) concerned with parameters or whose validity depends on assumptions concerning the population generating the sample.

Pari passu On an equal footing.

Partial duration See *key rate duration*.

Participating preference shares Preference shares that entitle shareholders to receive the standard preferred dividend plus the opportunity to receive an additional dividend if the company's profits exceed a pre-specified level.

Pass-through rate The coupon rate of a mortgage pass-through security.

Passive investment A buy and hold approach in which an investor does not make portfolio changes based on short-term expectations of changing market or security performance.

Passive strategy In reference to short-term cash management, it is an investment strategy characterized by simple decision rules for making daily investments.

Payable date The day that the company actually mails out (or electronically transfers) a dividend payment.

Payback period the number of years required to recover the original investment in a project. The payback is based on cash flows.

Payment date The day that the company actually mails out (or electronically transfers) a dividend payment.

Payments system The system for the transfer of money.

Peak The highest point of a business cycle.

Peer group A group of companies engaged in similar business activities whose economics and valuation are influenced by closely related factors.

Pennants A technical analysis continuation pattern formed by trendlines that converge to form a triangle, typically over a short period.

Per capita real GDP Real GDP divided by the size of the population, often used as a measure of the average standard of living in a country.

Per unit contribution margin The amount that each unit sold contributes to covering fixed costs—that is, the difference between the price per unit and the variable cost per unit.

Percentiles Quantiles that divide a distribution into 100 equal parts.

Perfect competition A market structure in which the individual firm has virtually no impact on market price, because it is assumed to be a very small seller among a very large number of firms selling essentially identical products.

Perfectly elastic When the quantity demanded or supplied of a given good is infinitely sensitive to a change in the value of a specified variable (e.g., price).

Perfectly inelastic When the quantity demanded or supplied of a given good is completely insensitive to a change in the value of a specified variable (e.g., price).

Performance bond See *margin bond*.

Performance evaluation The measurement and assessment of the outcomes of investment management decisions.

Performance fee Fees paid to the general partner from the limited partner(s) based on realized net profits.

Period costs Costs (e.g., executives' salaries) that cannot be directly matched with the timing of revenues and which are thus expensed immediately.

Periodicity The assumed number of periods in the year, typically matches the frequency of coupon payments.

Permanent differences Differences between tax and financial reporting of revenue (expenses) that will not be reversed at some future date. These result in a difference between the company's effective tax rate and statutory tax rate and do not result in a deferred tax item.

Permissioned networks Networks that are fully open only to select participants on a DLT network.

Permissionless networks Networks that are fully open to any user on a DLT network.

Permutation An ordered listing.

Perpetual bonds Bonds with no stated maturity date.

Perpetuity A perpetual annuity, or a set of never-ending level sequential cash flows, with the first cash flow occurring one period from now. A bond that does not mature.

Personal consumption expenditures All domestic personal consumption; the basis for a price index for such consumption called the PCE price index.

Personal disposable income Equal to personal income less personal taxes.

Personal income A broad measure of household income that includes all income received by households, whether earned or unearned; measures the ability of consumers to make purchases.

Plain vanilla bond Bond that makes periodic, fixed coupon payments during the bond's life and a lump-sum payment of principal at maturity. Also called *conventional bond*.

Platykurtic Describes a distribution that has relatively less weight in the tails than the normal distribution.

Point and figure chart A technical analysis chart that is constructed with columns of X's alternating with columns of O's such that the horizontal axis represents only the number of changes in price without reference to time or volume.

Point estimate A single numerical estimate of an unknown quantity, such as a population parameter.

Point of sale (POS) Systems that capture transaction data at the physical location in which the sale is made.

Policy rate An interest rate that a central bank sets and announces publicly; normally the rate at which it is willing to lend money to the commercial banks.

Population All members of a specified group.

Population mean The arithmetic mean value of a population; the arithmetic mean of all the observations or values in the population.

Population standard deviation A measure of dispersion relating to a population in the same unit of measurement as the observations, calculated as the positive square root of the population variance.

Population variance A measure of dispersion relating to a population, calculated as the mean of the squared deviations around the population mean.

Portfolio company In private equity, the company in which the private equity fund is investing.

Portfolio demand for money The demand to hold speculative money balances based on the potential opportunities or risks that are inherent in other financial instruments.

Portfolio planning The process of creating a plan for building a portfolio that is expected to satisfy a client's investment objectives.

Position The quantity of an asset that an entity owns or owes.

Positive screening An ESG investment style that focuses on the inclusion of certain sectors, companies, or practices in a fund or portfolio on the basis of specific minimum ESG criteria.

Posterior probability An updated probability that reflects or comes after new information.

Potential GDP The level of real GDP that can be produced at full employment; measures the productive capacity of the economy.

Power of a test The probability of correctly rejecting the null—that is, rejecting the null hypothesis when it is false.

Precautionary money balances Money held to provide a buffer against unforeseen events that might require money.

Precautionary stocks A level of inventory beyond anticipated needs that provides a cushion in the event that it takes longer to replenish inventory than expected or in the case of greater than expected demand.

Preference shares A type of equity interest which ranks above common shares with respect to the payment of dividends and the distribution of the company's net assets upon liquidation. They have characteristics of both debt and equity securities. Also called *preferred stock.*

Preferred stock See *preference shares*.

Premium In the case of bonds, premium refers to the amount by which a bond is priced above its face (par) value. In the case of an option, the amount paid for the option contract.

Prepaid expense A normal operating expense that has been paid in advance of when it is due.

Prepayment option Contractual provision that entitles the borrower to prepay all or part of the outstanding mortgage principal prior to the scheduled due date when the principal must be repaid. Also called *early repayment option*.

Prepayment penalty mortgages Mortgages that stipulate a monetary penalty if a borrower prepays within a certain time period after the mortgage is originated.

Prepayment risk The uncertainty that the timing of the actual cash flows will be different from the scheduled cash flows as set forth in the loan agreement due to the borrowers' ability to alter payments, usually to take advantage of interest rate movements.

Present value (PV) The present discounted value of future cash flows: For assets, the present discounted value of the future net cash inflows that the asset is expected to generate; for liabilities, the present discounted value of the future net cash outflows that are expected to be required to settle the liabilities.

Present value models Valuation models that estimate the intrinsic value of a security as the present value of the future benefits expected to be received from the security. Also called *discounted cash flow models*.

Pretax margin A profitability ratio calculated as earnings before taxes divided by revenue.

Price elasticity of demand Measures the percentage change in the quantity demanded, given a percentage change in the price of a given product.

Price index Represents the average prices of a basket of goods and services.

Price limits Limits imposed by a futures exchange on the price change that can occur from one day to the next.

Price multiple A ratio that compares the share price with some sort of monetary flow or value to allow evaluation of the relative worth of a company's stock.

Price priority The principle that the highest priced buy orders and the lowest priced sell orders execute first.

Price relative A ratio of an ending price over a beginning price; it is equal to 1 plus the holding period return on the asset.

Price return Measures *only* the price appreciation or percentage change in price of the securities in an index or portfolio.

Price return index An index that reflects *only* the price appreciation or percentage change in price of the constituent securities. Also called *price index*.

Price stability In economics, refers to an inflation rate that is low on average and not subject to wide fluctuation.

Price takers Producers that must accept whatever price the market dictates.

Price to book value A valuation ratio calculated as price per share divided by book value per share.

Price to cash flow A valuation ratio calculated as price per share divided by cash flow per share.

Price to earnings ratio (P/E ratio or P/E) The ratio of share price to earnings per share.

Price to sales A valuation ratio calculated as price per share divided by sales per share.

Price value of a basis point A version of money duration, it is an estimate of the change in the full price of a bond given a 1 basis point change in the yield-to-maturity.

Price weighting An index weighting method in which the weight assigned to each constituent security is determined by dividing its price by the sum of all the prices of the constituent securities.

Priced risk Risk for which investors demand compensation for bearing (e.g. equity risk, company-specific factors, macroeconomic factors).

Primary bond markets Markets in which issuers first sell bonds to investors to raise capital.

Primary capital markets (primary markets) The market where securities are first sold and the issuers receive the proceeds.

Primary dealers Financial institutions that are authorized to deal in new issues of sovereign bonds and that serve primarily as trading counterparties of the office responsible for issuing sovereign bonds.

Primary market The market where securities are first sold and the issuers receive the proceeds.

Prime brokers Brokers that provide services that commonly include custody, administration, lending, short borrowing, and trading.

Principal The amount of funds originally invested in a project or instrument; the face value to be paid at maturity.

Principal–agent relationship A relationship in which a principal hires an agent to perform a particular task or service; also known as an *agency relationship*.

Principal amount Amount that an issuer agrees to repay the debt holders on the maturity date.

Principal business activity The business activity from which a company derives a majority of its revenues and/or earnings.

Principal value Amount that an issuer agrees to repay the debt holders on the maturity date.

Principle of no arbitrage See *arbitrage-free pricing*.

Prior probabilities Probabilities reflecting beliefs prior to the arrival of new information.

Priority of claims Priority of payment, with the most senior or highest ranking debt having the first claim on the cash flows and assets of the issuer.

Private equity fund A hedge fund that seeks to buy, optimize, and ultimately sell portfolio companies to generate profits. See *venture capital fund*.

Private equity securities Securities that are not listed on public exchanges and have no active secondary market. They are issued primarily to institutional investors via non-public offerings, such as private placements.

Private investment in public equity (PIPE) An investment in the equity of a publicly traded firm that is made at a discount to the market value of the firm's shares.

Private placement Typically, a non-underwritten, unregistered offering of securities that are sold only to an investor or a small group of investors. It can be accomplished directly between the issuer and the investor(s) or through an investment bank.

Probability A number between 0 and 1 describing the chance that a stated event will occur.

Probability density function A function with non-negative values such that probability can be described by areas under the curve graphing the function.

Probability distribution A distribution that specifies the probabilities of a random variable's possible outcomes.

Probability function A function that specifies the probability that the random variable takes on a specific value.

Producer price index Reflects the price changes experienced by domestic producers in a country.

Production function Provides the quantitative link between the levels of output that the economy can produce and the inputs used in the production process.

Productivity The amount of output produced by workers in a given period of time—for example, output per hour worked; measures the efficiency of labor.

Profession An occupational group that has specific education, expert knowledge, and a framework of practice and behavior that underpins community trust, respect, and recognition.

Profit The return that owners of a company receive for the use of their capital and the assumption of financial risk when making their investments.

Profit and loss (P&L) statement A financial statement that provides information about a company's profitability over a stated period of time. Also called the *income statement*.

Profit margin An indicator of profitability, calculated as net income divided by revenue; indicates how much of each dollar of revenues is left after all costs and expenses.

Profitability index (PI) For a simple project, the PI is the present value of a project's future cash flows divided by the initial investment.

Profitability ratios Ratios that measure a company's ability to generate profitable sales from its resources (assets).

Project sequencing To defer the decision to invest in a future project until the outcome of some or all of a current project is known. Projects are sequenced through time, so that investing in a project creates the option to invest in future projects.

Promissory note A written promise to pay a certain amount of money on demand.

Property, plant, and equipment Tangible assets that are expected to be used for more than one period in either the production or supply of goods or services, or for administrative purposes.

Prospectus The document that describes the terms of a new bond issue and helps investors perform their analysis on the issue.

Protective put An option strategy in which a long position in an asset is combined with a long position in a put.

Proxy contest Corporate takeover mechanism in which shareholders are persuaded to vote for a group seeking a controlling position on a company's board of directors.

Proxy voting A process that enables shareholders who are unable to attend a meeting to authorize another individual to vote on their behalf.

Pseudo-random numbers Numbers produced by random number generators.

Public offer See *public offering*.

Public offering An offering of securities in which any member of the public may buy the securities. Also called *public offer*.

Pull on liquidity When disbursements are paid too quickly or trade credit availability is limited, requiring companies to expend funds before they receive funds from sales that could cover the liability.

Pure discount bonds See *zero-coupon bonds*.

Pure-play method A method for estimating the beta for a company or project; it requires using a comparable company's beta and adjusting it for financial leverage differences.

Put An option that gives the holder the right to sell an underlying asset to another party at a fixed price over a specific period of time.

Put–call–forward parity The relationship among puts, calls, and forward contracts.

Put–call parity An equation expressing the equivalence (parity) of a portfolio of a call and a bond with a portfolio of a put and the underlying, which leads to the relationship between put and call prices.

Put/call ratio A technical analysis indicator that evaluates market sentiment based upon the volume of put options traded divided by the volume of call options traded for a particular financial instrument.

Put option An option that gives the holder the right to sell an underlying asset to another party at a fixed price over a specific period of time.

Putable bonds Bonds that give the bondholder the right to sell the bond back to the issuer at a predetermined price on specified dates.

Quantile A value at or below which a stated fraction of the data lies. Also called *fractile*.

Quantitative easing An expansionary monetary policy based on aggressive open market purchase operations.

Quantity equation of exchange An expression that over a given period, the amount of money used to purchase all goods and services in an economy, $M \times V$, is equal to monetary value of this output, $P \times Y$.

Quantity theory of money Asserts that total spending (in money terms) is proportional to the quantity of money.

Quartiles Quantiles that divide a distribution into four equal parts.

Quasi-fixed cost A cost that stays the same over a range of production but can change to another constant level when production moves outside of that range.

Quasi-government bonds A bond issued by an entity that is either owned or sponsored by a national government. Also called *agency bond*.

Quick assets Assets that can be most readily converted to cash (e.g., cash, short-term marketable investments, receivables).

Quick ratio A stringent measure of liquidity that indicates a company's ability to satisfy current liabilities with its most liquid assets, calculated as (cash + short-term marketable investments + receivables) divided by current liabilities.

Quintiles Quantiles that divide a distribution into five equal parts.

Quota rents Profits that foreign producers can earn by raising the price of their goods higher than they would without a quota.

Quotas Government policies that restrict the quantity of a good that can be imported into a country, generally for a specified period of time.

Quote-driven market A market in which dealers acting as principals facilitate trading.

Quoted interest rate A quoted interest rate that does not account for compounding within the year. Also called *stated annual interest rate*.

Quoted margin The specified yield spread over the reference rate, used to compensate an investor for the difference in the credit risk of the issuer and that implied by the reference rate.

Random number An observation drawn from a uniform distribution.

Random number generator An algorithm that produces uniformly distributed random numbers between 0 and 1.

Random variable A quantity whose future outcomes are uncertain.

Range The difference between the maximum and minimum values in a dataset.

Ratio scales A measurement scale that has all the characteristics of interval measurement scales as well as a true zero point as the origin.

Real GDP The value of goods and services produced, measured at base year prices.

Real income Income adjusted for the effect of inflation on the purchasing power of money. Also known as the *purchasing power of income*. If income remains constant and a good's price falls, real income is said to rise, even though the number of monetary units (e.g., dollars) remains unchanged.

Real interest rate Nominal interest rate minus the expected rate of inflation.

Real risk-free interest rate The single-period interest rate for a completely risk-free security if no inflation were expected.

Realizable (settlement) value With reference to assets, the amount of cash or cash equivalents that could currently be obtained by selling the asset in an orderly disposal; with reference to liabilities, the undiscounted amount of cash or cash equivalents expected to be paid to satisfy the liabilities in the normal course of business.

Rebalancing Adjusting the weights of the constituent securities in an index.

Rebalancing policy The set of rules that guide the process of restoring a portfolio's asset class weights to those specified in the strategic asset allocation.

Recession A period during which real GDP decreases (i.e., negative growth) for at least two successive quarters, or a period of significant decline in total output, income, employment, and sales usually lasting from six months to a year.

Recognition lag The lag in government response to an economic problem resulting from the delay in confirming a change in the state of the economy.

Recourse loan Loan in which the lender has a claim against the borrower for any shortfall between the outstanding mortgage balance and the proceeds received from the sale of the property.
Redemption yield See *yield to maturity*.
Redemptions Withdrawals of funds by investors, as allowed by the notice period and other terms in the partnership agreement.
Refinancing rate A type of central bank policy rate.
Registered bonds Bonds for which ownership is recorded by either name or serial number.
Relative/best-in-class screening An ESG investment style that focuses on sectors, companies, or projects selected for ESG performance relative to industry peers.
Relative dispersion The amount of dispersion relative to a reference value or benchmark.
Relative frequency With reference to an interval of grouped data, the number of observations in the interval divided by the total number of observations in the sample.
Relative price The price of a specific good or service in comparison with those of other goods and services.
Relative strength analysis A comparison of the performance of one asset with the performance of another asset or a benchmark based on changes in the ratio of the securities' respective prices over time.
Relative strength index A technical analysis momentum oscillator that compares a security's gains with its losses over a set period.
Renewable resources Resources that can be replenished, such as a forest.
Rent Payment for the use of property.
Reorganization Agreements made by a company in bankruptcy under which a company's capital structure is altered and/or alternative arrangements are made for debt repayment; US Chapter 11 bankruptcy. The company emerges from bankruptcy as a going concern.
Replication The creation of an asset or portfolio from another asset, portfolio, and/or derivative.
Repo A form of collateralized loan involving the sale of a security with a simultaneous agreement by the seller to buy the same security back from the purchaser at an agreed-on price and future date. The party who sells the security at the inception of the repurchase agreement and buys it back at maturity is borrowing money from the other party, and the security sold and subsequently repurchased represents the collateral.
Repo margin The difference between the market value of the security used as collateral and the value of the loan. Also called *haircut*.
Repo rate The interest rate on a repurchase agreement.
Repurchase agreement A form of collateralized loan involving the sale of a security with a simultaneous agreement by the seller to buy the same security back from the purchaser at an agreed-on price and future date. The party who sells the security at the inception of the repurchase agreement and buys it back at maturity is borrowing money from the other party, and the security sold and subsequently repurchased represents the collateral.
Repurchase date The date when the party who sold the security at the inception of a repurchase agreement buys the security back from the cash lending counterparty.
Repurchase price The price at which the party who sold the security at the inception of the repurchase agreement buys the security back from the cash lending counterparty.
Required margin The yield spread over, or under, the reference rate such that an FRN is priced at par value on a rate reset date.
Required rate of return See *market discount rate*.
Required yield See *market discount rate*.
Required yield spread The difference between the yield-to-maturity on a new bond and the benchmark rate; additional compensation required by investors for the difference in risk and tax status of a bond relative to a government bond. Sometimes called the *spread over the benchmark*.
Reserve accounts Form of internal credit enhancement that relies on creating accounts and depositing in these accounts cash that can be used to absorb losses. Also called *reserve funds*.
Reserve funds See *reserve accounts*.
Reserve requirement The requirement for banks to hold reserves in proportion to the size of deposits.
Resistance In technical analysis, a price range in which selling activity is sufficient to stop the rise in the price of a security.
Responsible investing The practice of identifying companies that can efficiently manage their financial, environmental, and human capital resources to generate attractive long-term profitability; often synonymous with *sustainable investing*.
Restricted payments A bond covenant meant to protect creditors by limiting how much cash can be paid out to shareholders over time.
Retracement In technical analysis, a reversal in the movement of a security's price such that it is counter to the prevailing longerterm price trend.
Return-generating model A model that can provide an estimate of the expected return of a security given certain parameters and estimates of the values of the independent variables in the model.
Return on assets (ROA) A profitability ratio calculated as net income divided by average total assets; indicates a company's net profit generated per dollar invested in total assets.
Return on equity (ROE) A profitability ratio calculated as net income divided by average shareholders' equity.
Return on sales An indicator of profitability, calculated as net income divided by revenue; indicates how much of each dollar of revenues is left after all costs and expenses. Also referred to as *net profit margin*.
Return on total capital A profitability ratio calculated as EBIT divided by the sum of short- and long-term debt and equity.
Revaluation model Under IFRS, the process of valuing long-lived assets at fair value, rather than at cost less accumulated depreciation. Any resulting profit or loss is either reported on the income statement and/or through equity under revaluation surplus.
Revenue The amount charged for the delivery of goods or services in the ordinary activities of a business over a stated period; the inflows of economic resources to a company over a stated period.
Reversal patterns A type of pattern used in technical analysis to predict the end of a trend and a change in direction of the security's price.
Reverse repo A repurchase agreement viewed from the perspective of the cash lending counterparty.
Reverse repurchase agreement A repurchase agreement viewed from the perspective of the cash lending counterparty.

Reverse stock split A reduction in the number of shares outstanding with a corresponding increase in share price, but no change to the company's underlying fundamentals.
Revolving credit agreements The strongest form of short-term bank borrowing facilities; they are in effect for multiple years (e.g., 3–5 years) and may have optional medium-term loan features.
Rho The sensitivity of the option price to the risk-free rate.
Ricardian equivalence An economic theory that implies that it makes no difference whether a government finances a deficit by increasing taxes or issuing debt.
Risk Exposure to uncertainty. The chance of a loss or adverse outcome as a result of an action, inaction, or external event.
Risk averse The assumption that an investor will choose the least risky alternative.
Risk aversion The degree of an investor's inability and unwillingness to take risk.
Risk budgeting The establishment of objectives for individuals, groups, or divisions of an organization that takes into account the allocation of an acceptable level of risk.
Risk exposure The state of being exposed or vulnerable to a risk. The extent to which an organization is sensitive to underlying risks.
Risk factor/risk premium investing An ESG investment style that focuses on the inclusion of ESG information in the analysis of systematic risks as, for example, in smart beta and factor investment strategies (similar to size, value, momentum, and growth strategies).
Risk governance The top-down process and guidance that directs risk management activities to align with and support the overall enterprise.
Risk management The process of identifying the level of risk an organization wants, measuring the level of risk the organization currently has, taking actions that bring the actual level of risk to the desired level of risk, and monitoring the new actual level of risk so that it continues to be aligned with the desired level of risk.
Risk management framework The infrastructure, process, and analytics needed to support effective risk management in an organization.
Risk-neutral pricing Sometimes said of derivatives pricing, uses the fact that arbitrage opportunities guarantee that a risk-free portfolio consisting of the underlying and the derivative must earn the risk-free rate.
Risk-neutral probabilities Weights that are used to compute a binomial option price. They are the probabilities that would apply if a risk-neutral investor valued an option.
Risk premium An extra return expected by investors for bearing some specified risk.
Risk shifting Actions to change the distribution of risk outcomes.
Risk tolerance The amount of risk an investor is willing and able to bear to achieve an investment goal.
Risk transfer Actions to pass on a risk to another party, often, but not always, in the form of an insurance policy.
Robo-adviser A machine-based analytical tool or service that provides technology-driven investment solutions through online platforms.
Robust The quality of being relatively unaffected by a violation of assumptions.
Rule of 72 The principle that the approximate number of years necessary for an investment to double is 72 divided by the stated interest rate.
Running yield See *current yield.*
Safety-first rules Rules for portfolio selection that focus on the risk that portfolio value will fall below some minimum acceptable level over some time horizon.
Safety stock A level of inventory beyond anticipated needs that provides a cushion in the event that it takes longer to replenish inventory than expected or in the case of greater than expected demand.
Sales Generally, a synonym for revenue; "sales" is generally understood to refer to the sale of goods, whereas "revenue" is understood to include the sale of goods or services.
Sales risk Uncertainty with respect to the quantity of goods and services that a company is able to sell and the price it is able to achieve; the risk related to the uncertainty of revenues.
Sales-type leases Under US GAAP, a type of finance lease, from a lessor perspective, where the present value of the lease payments (lease receivable) exceeds the carrying value of the leased asset. The revenues earned by the lessor both a selling profit at inception and financing (interest) revenues.
Sample A subset of a population.
Sample excess kurtosis A sample measure of the degree of a distribution's kurtosis in excess of the normal distribution's kurtosis.
Sample kurtosis A sample measure of the degree of a distribution's peakedness.
Sample mean The sum of the sample observations, divided by the sample size.
Sample selection bias Bias introduced by systematically excluding some members of the population according to a particular attribute—for example, the bias introduced when data availability leads to certain observations being excluded from the analysis.
Sample skewness A sample measure of degree of asymmetry of a distribution.
Sample standard deviation The positive square root of the sample variance.
Sample statistic A quantity computed from or used to describe a sample.
Sample variance A sample measure of the degree of dispersion of a distribution, calculated by dividing the sum of the squared deviations from the sample mean by the sample size minus 1.
Sampling The process of obtaining a sample.
Sampling distribution The distribution of all distinct possible values that a statistic can assume when computed from samples of the same size randomly drawn from the same population.
Sampling error The difference between the observed value of a statistic and the quantity it is intended to estimate.
Sampling plan The set of rules used to select a sample.
Say on pay A process whereby shareholders may vote on executive remuneration (compensation) matters.
Say's law Named for French economist J.B. Say: All that is produced will be sold because supply creates its own demand.
Scatter plot A two-dimensional plot of pairs of observations on two data series.
Scenario analysis Analysis that shows the changes in key financial quantities that result from given (economic) events, such as the loss of customers, the loss of a supply source, or a catastrophic event; a risk management technique involving examination of the performance of a portfolio under specified situations. Closely related to stress testing.

Screening The application of a set of criteria to reduce a set of potential investments to a smaller set having certain desired characteristics.

Seasoned offering An offering in which an issuer sells additional units of a previously issued security.

Second-degree price discrimination When the monopolist charges different per-unit prices using the quantity purchased as an indicator of how highly the customer values the product.

Second lien A secured interest in the pledged assets that ranks below first lien debt in both collateral protection and priority of payment.

Secondary bond markets Markets in which existing bonds are traded among investors.

Secondary market The market where securities are traded among investors.

Secondary precedence rules Rules that determine how to rank orders placed at the same time.

Sector A group of related industries.

Sector indexes Indexes that represent and track different economic sectors—such as consumer goods, energy, finance, health care, and technology—on either a national, regional, or global basis.

Secured bonds Bonds secured by assets or financial guarantees pledged to ensure debt repayment in case of default.

Secured debt Debt in which the debtholder has a direct claim—a pledge from the issuer—on certain assets and their associated cash flows.

Securitization A process that involves moving assets into a special legal entity, which then uses the assets as guarantees to secure a bond issue.

Securitized assets Assets that are typically used to create asset-backed bonds; for example, when a bank securitizes a pool of loans, the loans are said to be securitized.

Security characteristic line A plot of the excess return of a security on the excess return of the market.

Security market index A portfolio of securities representing a given security market, market segment, or asset class.

Security market line (SML) The graph of the capital asset pricing model.

Security selection The process of selecting individual securities; typically, security selection has the objective of generating superior risk-adjusted returns relative to a portfolio's benchmark.

Self-investment limits With respect to investment limitations applying to pension plans, restrictions on the percentage of assets that can be invested in securities issued by the pension plan sponsor.

Sell-side firm A broker/dealer that sells securities and provides independent investment research and recommendations to their clients (i.e., buy-side firms).

Semi-strong-form efficient market A market in which security prices reflect all publicly known and available information.

Semiannual bond basis yield An annual rate having a periodicity of two; also known as a *semiannual bond equivalent yield*.

Semiannual bond equivalent yield See *semiannual bond basis yield*.

Semideviation The positive square root of semivariance (sometimes called *semistandard deviation*).

Semilogarithmic Describes a scale constructed so that equal intervals on the vertical scale represent equal rates of change, and equal intervals on the horizontal scale represent equal amounts of change.

Semivariance The average squared deviation below the mean.

Seniority ranking Priority of payment of various debt obligations.

Sensitivity analysis Analysis that shows the range of possible outcomes as specific assumptions are changed.

Separately managed account (SMA) An investment portfolio managed exclusively for the benefit of an individual or institution.

Serial maturity structure Structure for a bond issue in which the maturity dates are spread out during the bond's life; a stated number of bonds mature and are paid off each year before final maturity.

Settlement The process that occurs after a trade is completed, the securities are passed to the buyer, and payment is received by the seller.

Settlement date Date when the buyer makes cash payment and the seller delivers the security.

Settlement price The official price, designated by the clearinghouse, from which daily gains and losses will be determined and marked to market.

Share repurchase A transaction in which a company buys back its own shares. Unlike stock dividends and stock splits, share repurchases use corporate cash.

Shareholder activism Strategies used by shareholders to attempt to compel a company to act in a desired manner.

Shareholder engagement The process whereby companies engage with their shareholders.

Shareholders' equity Assets less liabilities; the residual interest in the assets after subtracting the liabilities.

Sharpe ratio The average return in excess of the risk-free rate divided by the standard deviation of return; a measure of the average excess return earned per unit of standard deviation of return.

Shelf registration Type of public offering that allows the issuer to file a single, all-encompassing offering circular that covers a series of bond issues.

Short The seller of an asset or derivative contract. Also refers to the position of being short an asset or derivative contract.

Short position A position in an asset or contract in which one has sold an asset one does not own, or in which a right under a contract can be exercised against oneself.

Short-run average total cost The curve describing average total cost when some costs are considered fixed.

Short selling A transaction in which borrowed securities are sold with the intention to repurchase them at a lower price at a later date and return them to the lender.

Shortfall risk The risk that portfolio value will fall below some minimum acceptable level over some time horizon.

Shutdown point The point at which average revenue is equal to the firm's average variable cost.

Simple interest The interest earned each period on the original investment; interest calculated on the principal only.

Simple random sample A subset of a larger population created in such a way that each element of the population has an equal probability of being selected to the subset.

Simple random sampling The procedure of drawing a sample to satisfy the definition of a simple random sample.

Simple yield The sum of the coupon payments plus the straight-line amortized share of the gain or loss, divided by the flat price.

Simulation Computer-generated sensitivity or scenario analysis that is based on probability models for the factors that drive outcomes.

Simulation trial A complete pass through the steps of a simulation.

Single-step format With respect to the format of the income statement, a format that does not subtotal for gross profit (revenue minus cost of goods sold).

Sinking fund arrangement Provision that reduces the credit risk of a bond issue by requiring the issuer to retire a portion of the bond's principal outstanding each year.

Situational influences External factors, such as environmental or cultural elements, that shape our behavior.

Skewed Not symmetrical.

Skewness A quantitative measure of skew (lack of symmetry); a synonym of skew.

Small country A country that is a price taker in the world market for a product and cannot influence the world market price.

Smart beta Involves the use of simple, transparent, rules-based strategies as a basis for investment decisions.

Smart contract A computer program that is designed to self-execute on the basis of pre-specified terms and conditions agreed to by parties to a contract.

Socially responsible investing An investment approach that excludes investments in companies or industries that deviate from an organization's beliefs and sometimes includes investments with favorable environmental or social profiles.

Solvency With respect to financial statement analysis, the ability of a company to fulfill its long-term obligations.

Solvency ratios Ratios that measure a company's ability to meet its long-term obligations.

Solvency risk The risk that an organization does not survive or succeed because it runs out of cash, even though it might otherwise be solvent.

Sovereign A bond issued by a national government.

Sovereign bond A bond issued by a national government.

Sovereign yield spread An estimate of the country spread (country equity premium) for a developing nation that is based on a comparison of bonds yields in country being analyzed and a developed country. The sovereign yield spread is the difference between a government bond yield in the country being analyzed, denominated in the currency of the developed country, and the Treasury bond yield on a similar maturity bond in the developed country.

Spearman rank correlation coefficient A measure of correlation applied to ranked data.

Special dividend A dividend paid by a company that does not pay dividends on a regular schedule, or a dividend that supplements regular cash dividends with an extra payment.

Special purpose entity A non-operating entity created to carry out a specified purpose, such as leasing assets or securitizing receivables; can be a corporation, partnership, trust, limited liability, or partnership formed to facilitate a specific type of business activity. Also called *special purpose vehicle* or *variable interest entity*.

Special purpose vehicle See *special purpose entity*.

Specific identification method An inventory accounting method that identifies which specific inventory items were sold and which remained in inventory to be carried over to later periods.

Speculative demand for money The demand to hold speculative money balances based on the potential opportunities or risks that are inherent in other financial instruments. Also called *portfolio demand for money*.

Speculative money balances Monies held in anticipation that other assets will decline in value.

Split coupon bond See *deferred coupon bond*.

Sponsored A type of depository receipt in which the foreign company whose shares are held by the depository has a direct involvement in the issuance of the receipts.

Spot curve A sequence of yields-to-maturity on zero-coupon bonds. Sometimes called *zero* or *strip curve* because coupon payments are "stripped" off of the bonds.

Spot markets Markets in which assets are traded for immediate delivery.

Spot prices The price of an asset for immediately delivery.

Spot rates A sequence of market discount rates that correspond to the cash flow dates; yields-to-maturity on zero-coupon bonds maturing at the date of each cash flow.

Spread In general, the difference in yield between different fixed income securities. Often used to refer to the difference between the yield-to-maturity and the benchmark.

Spread over the benchmark See *required yield spread*.

Spread risk Bond price risk arising from changes in the yield spread on credit-risky bonds; reflects changes in the market's assessment and/or pricing of credit migration (or downgrade) risk and market liquidity risk.

Spurious correlation A correlation that misleadingly points toward associations between variables.

Stackelberg model A prominent model of strategic decision making in which firms are assumed to make their decisions sequentially.

Stagflation When a high inflation rate is combined with a high level of unemployment and a slowdown of the economy.

Staggered boards Election process whereby directors are typically divided into multiple classes that are elected separately in consecutive years—that is, one class every year.

Stakeholder management The identification, prioritization, and understanding of the interests of stakeholder groups, and managing the company's relationships with these groups.

Stakeholders Individuals or groups of individuals who may be affected either directly or indirectly by a decision and thus have an interest, or stake, in the decision.

Standard deviation The positive square root of the variance; a measure of dispersion in the same units as the original data.

Standard normal distribution The normal density with mean (μ) equal to 0 and standard deviation (σ) equal to 1.

Standardizing A transformation that involves subtracting the mean and dividing the result by the standard deviation.

Standards of conduct Behaviors required by a group; established benchmarks that clarify or enhance a group's code of ethics.

Standing limit orders A limit order at a price below market and which therefore is waiting to trade.

Stated annual interest rate A quoted interest rate that does not account for compounding within the year. Also called *quoted interest rate*.

Statement of changes in equity (statement of owners' equity) A financial statement that reconciles the beginning-of-period and end-of-period balance sheet values of shareholders' equity; provides information about all factors affecting shareholders' equity. Also called *statement of owners' equity*.

Statement of financial condition The financial statement that presents an entity's current financial position by disclosing resources the entity controls (its assets) and the claims on those resources (its liabilities and equity claims), as of a particular point in time (the date of the balance sheet).
Statement of financial position The financial statement that presents an entity's current financial position by disclosing resources the entity controls (its assets) and the claims on those resources (its liabilities and equity claims), as of a particular point in time (the date of the balance sheet).
Statement of operations A financial statement that provides information about a company's profitability over a stated period of time.
Statistic A quantity computed from or used to describe a sample of data.
Statistical inference Making forecasts, estimates, or judgments about a larger group from a smaller group actually observed; using a sample statistic to infer the value of an unknown population parameter.
Statistically significant A result indicating that the null hypothesis can be rejected; with reference to an estimated regression coefficient, frequently understood to mean a result indicating that the corresponding population regression coefficient is different from 0.
Statutory voting A common method of voting where each share represents one vote.
Step-up coupon bond Bond for which the coupon, which may be fixed or floating, increases by specified margins at specified dates.
Stock dividend A type of dividend in which a company distributes additional shares of its common stock to shareholders instead of cash.
Stock-out losses Profits lost from not having sufficient inventory on hand to satisfy demand.
Stock split An increase in the number of shares outstanding with a consequent decrease in share price, but no change to the company's underlying fundamentals.
Stop-loss order See *stop order*.
Stop order An order in which a trader has specified a stop price condition. Also called *stop-loss order*.
Store of value The quality of tending to preserve value.
Store of wealth Goods that depend on the fact that they do not perish physically over time, and on the belief that others would always value the good.
Straight-line method A depreciation method that allocates evenly the cost of a long-lived asset less its estimated residual value over the estimated useful life of the asset.
Straight voting A shareholder voting process in which shareholders receive one vote for each share owned.
Strategic analysis Analysis of the competitive environment with an emphasis on the implications of the environment for corporate strategy.
Strategic asset allocation The set of exposures to IPS-permissible asset classes that is expected to achieve the client's long-term objectives given the client's investment constraints.
Strategic groups Groups sharing distinct business models or catering to specific market segments in an industry.
Street convention Yield measure that neglects weekends and holidays; the internal rate of return on cash flows assuming payments are made on the scheduled dates, even when the scheduled date falls on a weekend or holiday.
Stress testing A specific type of scenario analysis that estimates losses in rare and extremely unfavorable combinations of events or scenarios.
Strong-form efficient market A market in which security prices reflect all public and private information.
Structural (or cyclically adjusted) budget deficit The deficit that would exist if the economy was at full employment (or full potential output).
Structural subordination Arises in a holding company structure when the debt of operating subsidiaries is serviced by the cash flow and assets of the subsidiaries before funds can be passed to the holding company to service debt at the parent level.
Structured financial instruments Financial instruments that share the common attribute of repackaging risks. Structured financial instruments include asset-backed securities, collateralized debt obligations, and other structured financial instruments such as capital protected, yield enhancement, participation and leveraged instruments.
Subjective probability A probability drawing on personal or subjective judgment.
Subordinated debt A class of unsecured debt that ranks below a firm's senior unsecured obligations.
Subordination Form of internal credit enhancement that relies on creating more than one bond tranche and ordering the claim priorities for ownership or interest in an asset between the tranches. The ordering of the claim priorities is called a senior/subordinated structure, where the tranches of highest seniority are called senior followed by subordinated or junior tranches. Also called *credit tranching.*
Substitutes Said of two goods or services such that if the price of one increases the demand for the other tends to increase, holding all other things equal (e.g., butter and margarine).
Sunk cost A cost that has already been incurred.
Supervised learning A machine learning approach that makes use of labeled training data.
Supply shock A typically unexpected disturbance to supply.
Support In technical analysis, a price range in which buying activity is sufficient to stop the decline in the price of a security.
Support tranche A class or tranche in a CMO that protects the PAC tranche from prepayment risk.
Supranational bonds A bond issued by a supranational agency such as the World Bank.
Surety bond Form of external credit enhancement whereby a rated and regulated insurance company guarantees to reimburse bondholders for any losses incurred up to a maximum amount if the issuer defaults.
Survey approach An estimate of the equity risk premium that is based upon estimates provided by a panel of finance experts.
Survivorship bias The bias resulting from a test design that fails to account for companies that have gone bankrupt, merged, or are otherwise no longer reported in a database.
Sustainable growth rate The rate of dividend (and earnings) growth that can be sustained over time for a given level of return on equity, keeping the capital structure constant and without issuing additional common stock.
Sustainable investing The practice of identifying companies that can efficiently manage their financial, environmental, and human capital resources to generate attractive long-term profitability; often synonymous with *responsible investing*.

Sustainable rate of economic growth The rate of increase in the economy's productive capacity or potential GDP.

Swap contract An agreement between two parties to exchange a series of future cash flows.

Syndicated loans Loans from a group of lenders to a single borrower.

Syndicated offering A bond issue that is underwritten by a group of investment banks.

Systematic risk Risk that affects the entire market or economy; it cannot be avoided and is inherent in the overall market. Systematic risk is also known as non-diversifiable or market risk.

Systematic sampling A procedure of selecting every *k*th member until reaching a sample of the desired size. The sample that results from this procedure should be approximately random.

***t*-Test** A hypothesis test using a statistic (*t*-statistic) that follows a *t*-distribution.

Tactical asset allocation The decision to deliberately deviate from the strategic asset allocation in an attempt to add value based on forecasts of the near-term relative performance of asset classes.

Target balance A minimum level of cash to be held available—estimated in advance and adjusted for known funds transfers, seasonality, or other factors.

Target capital structure A company's chosen proportions of debt and equity.

Target independent A bank's ability to determine the definition of inflation that they target, the rate of inflation that they target, and the horizon over which the target is to be achieved.

Target semideviation The positive square root of target semivariance.

Target semivariance The average squared deviation below a target value.

Tariffs Taxes that a government levies on imported goods.

Tax base The amount at which an asset or liability is valued for tax purposes.

Tax expense An aggregate of an entity's income tax payable (or recoverable in the case of a tax benefit) and any changes in deferred tax assets and liabilities. It is essentially the income tax payable or recoverable if these had been determined based on accounting profit rather than taxable income.

Tax loss carry forward A taxable loss in the current period that may be used to reduce future taxable income.

Taxable income The portion of an entity's income that is subject to income taxes under the tax laws of its jurisdiction.

Taxable temporary differences Temporary differences that result in a taxable amount in a future period when determining the taxable profit as the balance sheet item is recovered or settled.

Technical analysis A form of security analysis that uses price and volume data, which is often displayed graphically, in decision making.

Technology The process a company uses to transform inputs into outputs.

Tender offer Corporate takeover mechanism which involves shareholders selling their interests directly to the group seeking to gain control.

Tenor The time-to-maturity for a bond or derivative contract. Also called *term to maturity*.

Term maturity structure Structure for a bond issue in which the bond's notional principal is paid off in a lump sum at maturity.

Term structure See *maturity structure*.

Term structure of credit spreads The relationship between the spreads over the "risk-free" (or benchmark) rates and times-to-maturity.

Term structure of yield volatility The relationship between the volatility of bond yields-to-maturity and times-to-maturity.

Terminal stock value The expected value of a share at the end of the investment horizon—in effect, the expected selling price. Also called *terminal value*.

Terminal value The expected value of a share at the end of the investment horizon—in effect, the expected selling price.

Terms of trade The ratio of the price of exports to the price of imports, representing those prices by export and import price indexes, respectively.

Text analytics The use of computer programs to analyze and derive meaning from typically large, unstructured text- or voice-based datasets.

Thematic investment An ESG investing style that focuses on investing in themes or assets specifically relating to ESG factors, such as clean energy, green technology, or sustainable agriculture.

Third-degree price discrimination When the monopolist segregates customers into groups based on demographic or other characteristics and offers different pricing to each group.

Time-period bias The possibility that when we use a time-series sample, our statistical conclusion may be sensitive to the starting and ending dates of the sample.

Time-series data Observations of a variable over time.

Time tranching The creation of classes or tranches in an ABS/MBS that possess different (expected) maturities.

Time value The difference between the market price of the option and its intrinsic value.

Time value decay Said of an option when, at expiration, no time value remains and the option is worth only its exercise value.

Time value of money The principles governing equivalence relationships between cash flows with different dates.

Time-weighted rate of return The compound rate of growth of one unit of currency invested in a portfolio during a stated measurement period; a measure of investment performance that is not sensitive to the timing and amount of withdrawals or additions to the portfolio.

Tokenization The process of representing ownership rights to physical assets on a blockchain or distributed ledger.

Top-down analysis An investment selection approach that begins with consideration of macroeconomic conditions and then evaluates markets and industries based upon such conditions.

Total comprehensive income The change in equity during a period resulting from transaction and other events, other than those changes resulting from transactions with owners in their capacity as owners.

Total cost The summation of all costs, for which costs are classified as fixed or variable.

Total factor productivity A scale factor that reflects the portion of growth that is not accounted for by explicit factor inputs (e.g. capital and labor).

Total fixed cost The summation of all expenses that do not change as the level of production varies.

Total invested capital The sum of market value of common equity, book value of preferred equity, and face value of debt.

Total probability rule A rule explaining the unconditional probability of an event in terms of probabilities of the event conditional on mutually exclusive and exhaustive scenarios.

Total probability rule for expected value A rule explaining the expected value of a random variable in terms of expected values of the random variable conditional on mutually exclusive and exhaustive scenarios.

Total return Measures the price appreciation, or percentage change in price of the securities in an index or portfolio, plus any income received over the period.

Total return index An index that reflects the price appreciation or percentage change in price of the constituent securities plus any income received since inception.

Total return swap A swap in which one party agrees to pay the total return on a security. Often used as a credit derivative, in which the underlying is a bond.

Total variable cost The summation of all variable expenses.

Tracking error The standard deviation of the differences between a portfolio's returns and its benchmark's returns; a synonym of active risk.

Tracking risk The standard deviation of the differences between a portfolio's returns and its benchmarks returns. Also called *tracking error*.

Trade creation When regional integration results in the replacement of higher cost domestic production by lower cost imports from other members.

Trade credit A spontaneous form of credit in which a purchaser of the goods or service is financing its purchase by delaying the date on which payment is made.

Trade diversion When regional integration results in lower-cost imports from non-member countries being replaced with higher-cost imports from members.

Trade payables Amounts that a business owes to its vendors for goods and services that were purchased from them but which have not yet been paid.

Trade protection Government policies that impose restrictions on trade, such as tariffs and quotas.

Trade surplus (deficit) When the value of exports is greater (less) than the value of imports.

Trading securities Under US GAAP, a category of debt securities held by a company with the intent to trade them. Also called *held-for-trading securities*.

Traditional investment markets Markets for traditional investments, which include all publicly traded debts and equities and shares in pooled investment vehicles that hold publicly traded debts and/or equities.

Transactions money balances Money balances that are held to finance transactions.

Transactions motive In the context of inventory management, the need for inventory as part of the routine production–sales cycle.

Transfer payments Welfare payments made through the social security system that exist to provide a basic minimum level of income for low-income households.

Transparency Said of something (e.g., a market) in which information is fully disclosed to the public and/or regulators.

Treasury Inflation-Protected Securities A bond issued by the United States Treasury Department that is designed to protect the investor from inflation by adjusting the principal of the bond for changes in inflation.

Treasury stock method A method for accounting for the effect of options (and warrants) on earnings per share (EPS) that specifies what EPS would have been if the options and warrants had been exercised and the company had used the proceeds to repurchase common stock.

Tree diagram A diagram with branches emanating from nodes representing either mutually exclusive chance events or mutually exclusive decisions.

Trend A long-term pattern of movement in a particular direction.

Treynor ratio A measure of risk-adjusted performance that relates a portfolio's excess returns to the portfolio's beta.

Triangle patterns In technical analysis, a continuation chart pattern that forms as the range between high and low prices narrows, visually forming a triangle.

Trimmed mean A mean computed after excluding a stated small percentage of the lowest and highest observations.

TRIN A flow of funds indicator applied to a broad stock market index to measure the relative extent to which money is moving into or out of rising and declining stocks.

Triple bottoms In technical analysis, a reversal pattern that is formed when the price forms three troughs at roughly the same price level; used to predict a change from a downtrend to an uptrend.

Triple tops In technical analysis, a reversal pattern that is formed when the price forms three peaks at roughly the same price level; used to predict a change from an uptrend to a downtrend.

Trough The lowest point of a business cycle.

True yield The internal rate of return on cash flows using the actual calendar including weekends and bank holidays.

Trust deed The governing legal credit agreement, typically incorporated by reference in the prospectus. Also called *bond indenture*.

Trust receipt arrangement The use of inventory as collateral for a loan. The inventory is segregated and held in trust, and the proceeds of any sale must be remitted to the lender immediately.

Turn-of-the-year effect Calendar anomaly that stock market returns in January are significantly higher compared to the rest of the months of the year, with most of the abnormal returns reported during the first five trading days in January.

Two-fund separation theorem The theory that all investors regardless of taste, risk preferences, and initial wealth will hold a combination of two portfolios or funds: a risk-free asset and an optimal portfolio of risky assets.

Two-sided hypothesis test A test in which the null hypothesis is rejected in favor of the alternative hypothesis if the evidence indicates that the population parameter is either smaller or larger than a hypothesized value.

Two-tailed hypothesis test A test in which the null hypothesis is rejected in favor of the alternative hypothesis if the evidence indicates that the population parameter is either smaller or larger than a hypothesized value.

Two-week repo rate The interest rate on a two-week repurchase agreement; may be used as a policy rate by a central bank.

Type I error The error of rejecting a true null hypothesis.

Type II error The error of not rejecting a false null hypothesis.

Unanticipated (unexpected) inflation The component of inflation that is a surprise.

Unconditional probability The probability of an event *not* conditioned on another event.

Underemployed A person who has a job but has the qualifications to work a significantly higher-paying job.

Underlying An asset that trades in a market in which buyers and sellers meet, decide on a price, and the seller then delivers the asset to the buyer and receives payment. The underlying is the asset or other derivative on which a particular derivative is based. The market for the underlying is also referred to as the *spot market*.

Underwriter A firm, usually an investment bank, that takes the risk of buying the newly issued securities from the issuer, and then reselling them to investors or to dealers, thus guaranteeing the sale of the securities at the offering price negotiated with the issuer.

Underwritten offering A type of securities issue mechanism in which the investment bank guarantees the sale of the securities at an offering price that is negotiated with the issuer. Also known as *firm commitment offering*.

Unearned revenue A liability account for money that has been collected for goods or services that have not yet been delivered; payment received in advance of providing a good or service. Also called *deferred revenue* or *deferred income*.

Unemployed People who are actively seeking employment but are currently without a job.

Unemployment rate The ratio of unemployed to the labor force.

Unexpected inflation The component of inflation that is a surprise.

Unit elastic An elasticity with a magnitude of negative one. Also called *unitary elastic*.

Unit labor cost The average labor cost to produce one unit of output.

Unit normal distribution The normal density with mean (μ) equal to 0 and standard deviation (σ) equal to 1.

Units-of-production method A depreciation method that allocates the cost of a long-lived asset based on actual usage during the period.

Univariate distribution A distribution that specifies the probabilities for a single random variable.

Universal owners Long-term investors, such as pension funds, that have significant assets invested in globally diversified portfolios.

Unlimited funds An unlimited funds environment assumes that the company can raise the funds it wants for all profitable projects simply by paying the required rate of return.

Unsecured debt Debt which gives the debtholder only a general claim on an issuer's assets and cash flow.

Unsponsored A type of depository receipt in which the foreign company whose shares are held by the depository has no involvement in the issuance of the receipts.

Unsupervised learning A machine learning approach that does not make use of labeled training data.

Up transition probability The probability that an asset's value moves up.

Validity instructions Instructions which indicate when the order may be filled.

Valuation allowance A reserve created against deferred tax assets, based on the likelihood of realizing the deferred tax assets in future accounting periods.

Valuation ratios Ratios that measure the quantity of an asset or flow (e.g., earnings) in relation to the price associated with a specified claim (e.g., a share or ownership of the enterprise).

Value at risk (VaR) A money measure of the minimum value of losses expected during a specified time period at a given level of probability.

Value investors With reference to equity investors, investors who are focused on paying a relatively low share price in relation to earnings or assets per share.

VaR See *value at risk*.

Variable costs Costs that fluctuate with the level of production and sales.

Variance The expected value (the probability-weighted average) of squared deviations from a random variable's expected value.

Variation margin Additional margin that must be deposited in an amount sufficient to bring the balance up to the initial margin requirement.

Veblen goods Goods that increase in desirability with increasing price.

Vega A measure of the sensitivity of an option's price to changes in the underlying's volatility.

Venture capital Investments that provide "seed" or startup capital, early-stage financing, or later-stage financing (including mezzanine-stage financing) to companies that are in early development stages and require additional capital for expansion or preparation for an initial public offering.

Venture capital fund A hedge fund that seeks to buy, optimize, and ultimately sell portfolio companies to generate profits. See *private equity fund*.

Vertical analysis Common-size analysis using only one reporting period or one base financial statement; for example, an income statement in which all items are stated as percentages of sales.

Vertical demand schedule Implies that some fixed quantity is demanded, regardless of price.

Volatility As used in option pricing, the standard deviation of the continuously compounded returns on the underlying asset.

Voluntarily unemployed A person voluntarily outside the labor force, such as a jobless worker refusing an available vacancy.

Voluntary export restraint A trade barrier under which the exporting country agrees to limit its exports of the good to its trading partners to a specific number of units.

Vote by proxy A mechanism that allows a designated party—such as another shareholder, a shareholder representative, or management—to vote on the shareholder's behalf.

Warehouse receipt arrangement The use of inventory as collateral for a loan; similar to a trust receipt arrangement except there is a third party (i.e., a warehouse company) that supervises the inventory.

Warrant Attached option that gives its holder the right to buy the underlying stock of the issuing company at a fixed exercise price until the expiration date.

Weak-form efficient market hypothesis The belief that security prices fully reflect all past market data, which refers to all historical price and volume trading information.

Wealth effect An increase (decrease) in household wealth increases (decreases) consumer spending out of a given level of current income.

Weighted average cost method An inventory accounting method that averages the total cost of available inventory items over the total units available for sale.

Weighted average cost of capital A weighted average of the aftertax required rates of return on a company's common stock, preferred stock, and long-term debt, where the weights are the fraction of each source of financing in the company's target capital structure.

Weighted average coupon rate Weighting the mortgage rate of each mortgage loan in the pool by the percentage of the mortgage outstanding relative to the outstanding amount of all the mortgages in the pool.

Weighted average life A measure that gives investors an indication of how long they can expect to hold the MBS before it is paid off; the convention-based average time to receipt of all principal repayments. Also called *average life*.

Weighted average maturity Weighting the remaining number of months to maturity for each mortgage loan in the pool by the amount of the outstanding mortgage balance.

Weighted mean An average in which each observation is weighted by an index of its relative importance.

Wholesale price index Reflects the price changes experienced by domestic producers in a country.

Winsorized mean A mean computed after assigning a stated percent of the lowest values equal to one specified low value, and a stated percent of the highest values equal to one specified high value.

Working capital The difference between current assets and current liabilities.

Working capital management The management of a company's short-term assets (such as inventory) and short-term liabilities (such as money owed to suppliers).

World price The price prevailing in the world market.

Yield The actual return on a debt security if it is held to maturity.

Yield duration The sensitivity of the bond price with respect to the bond's own yield-to-maturity.

Yield to maturity Annual return that an investor earns on a bond if the investor purchases the bond today and holds it until maturity. It is the discount rate that equates the present value of the bond's expected cash flows until maturity with the bond's price. Also called *yield-to-redemption* or *redemption yield*.

Yield to redemption See *yield to maturity*.

Yield-to-worst The lowest of the sequence of yields-to-call and the yield-to-maturity.

Zero-coupon bonds Bonds that do not pay interest during the bond's life. It is issued at a discount to par value and redeemed at par. Also called *pure discount bonds*.

Zero volatility spread (Z-spread) Calculates a constant yield spread over a government (or interest rate swap) spot curve.