FREQUENTLY USED INVESTMENT TERMS

Don't let investment jargon confuse you. Take control by brushing up on these financial terms.

529 plan: an education savings plan with tax advantages designed to help families set aside funds for K-12 tuition or future college costs with potentially less of a tax burden.

Alpha: a fund's excess return relative to the return of the benchmark index. An alpha greater than 0.0 means an investment has performed better than the index (given its level of risk).

Asset allocation funds: a type of mutual fund that switches among stocks, bonds, cash and other investments in pursuit of maximized returns while minimizing risks.

Asset management company: a business that invests and manages assets on behalf of financial advisors and their clients.

Beta: a measure of a fund's risk relative to its benchmark. The index is equivalent to 1.0. A fund with a beta greater than 1.0 is usually more volatile than the benchmark index, while a fund with a beta less than 1.0 is usually less volatile.

Capital gain/Capital loss: the profit or loss made on the sale of securities. Either can occur when a mutual fund sells underlying securities. When a mutual fund company sells securities at a profit, net capital gains (capital gains in excess of capital losses) are distributed to fund shareholders and reported to the IRS and shareholders on Form 1099-DIV, Dividends and Distributions.

Correlation: a statistical measure of how two securities move in relation to each other. A correlation of +1 implies that as one security moves up or down, the other security will move in lockstep in the same direction. A correlation of -1 means that if one security moves in either direction, the security that is negatively correlated will move by an equal amount in the opposite direction. If the correlation is 0, the movement of the securities is random and has no correlation.

Derivatives: a financial contract whose value is based on an underlying financial asset (such as a stock or a bond), a commodity (such as gold), a market index (such as the S&P 500) or a reference rate (such as the prime lending interest rate). Examples of derivative instruments include futures, options, index-, equity-, commodity- and currency-linked securities, warrants and swap contracts.

Diversification: a risk management technique that uses a variety of investments. Diversification helps reduce the risks inherent in investing so that the positive performance of some investments may offset the negative performance of others.

Dividends: payments a company makes to its shareholders from its corporate profits. These are paid to mutual funds by the companies they invest in, which may then be passed along to investors as cash or additional fund shares.

Exchange traded fund (ETF): a pooled investment vehicle (similar to a mutual fund) that trades throughout the day on an exchange (like a stock). ETFs can help provide consistency, diversification, transparency and risk management through a rules-based, repeatable approach.

Expense ratio: reflects fees to run a fund, listed as a percentage of fund assets. This includes the cost of investment management, distribution, investor services and other expenses.

Fiduciary duty: a duty to put the interest of the principal (usually the client) first and a responsibility to disclose conflicts of interest.

Growth funds: seek to buy stocks with good growth potential. In most cases, a growth stock is defined as shares of a company whose earnings are expected to grow at an above-average rate compared with its industry or the overall market.

Morningstar ratings: one of the most common (and trusted) rating systems for mutual funds and ETFs. Funds are given from one to five stars (five being the best) based on a set criteria that evaluates fund performance.

Mutual fund: an investment vehicle that pools together the money of many investors. The money is managed by investment professionals who select securities (stocks or bonds) to meet specific investment goals.

Net asset value (NAV): the daily price used to value a single share of a mutual fund. It is calculated as the total value of a mutual fund's assets minus its liabilities. This is the price investors receive when they redeem their investments.

Prospectus: an overview of an investment vehicle (mutual fund or ETF), including its investment objective, strategies, the portfolio manager's experience, the fee structure and other important fund-specific information.

Sector: a broad category used to classify companies, such as energy, health care or technology, to name a few.

Total return: investment performance over a designated period, including any income from the investment (dividends, interest and capital gains) as well as any changes in the share price.

Value funds: seek investments that are undervalued by the market because of an overreaction to daily news and events. These market overreactions result in stock price movements that do not correspond with the company's long-term fundamentals. This may create an opportunity for value investors to profit by buying when the price is deflated.

Volatility: how much a traded security or market index fluctuates in price. Generally, the higher the volatility, the higher the level of risk.

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