Investment Terms You Should Know

The investment world can be a complicated and overwhelming place to those on the outside. If you're already finance savvy – consider the below a recap and if you're new to the investment world, you're in the right spot. Read on for a mini-financial dictionary of investment terms you should know.

Asset Allocation: This is a strategy that adjusts the amounts or percentages you own in certain asset classes in order to balance risk versus reward based on your overall risk tolerance, goals and timeframe for holding investments.

Bonds: A bond is a debt investment where as the investor, you loan your money to an issuer (a corporation or government) for a set period of time. In exchange for the loan, the issuer promises to repay the principal and a set interest amount over the life of the bond, which is a predetermined time. Think of this as an IOU where you loan a company money and in exchange they agree to a set of terms for repayment.

The value of a bond will increase or decrease based on changes in interest rates (increase when interest rates fall and decrease when interest rates increase). They tend to offer more moderate returns and risk when compared to stocks and can sometimes work in a portfolio to even out risk.

Employer Match: An employer contribution to a company sponsored retirement plan, in which your employer contributes an amount to your plan equal to a specified percentage of your personal contribution. Your employer is essentially "matching" a portion of your contribution. If your employer provides a company match, you'll typically see language similar to this in your benefits handbook: We will match 50% of your personal contribution to your 401(k) up to 6% of your salary.

Exchange Traded Funds* (ETF)*: An exchange traded fund (ETF) is similar to a mutual fund in that it pools together funds to purchase a set of stocks, bonds or securities. However it trades throughout the day instead of at the end of the day. The price of an ETF is determined throughout the day and they trade just like stocks.

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Note: Most ETFs are passive in nature and therefore tend to come with lower internal expense ratios than similar mutual funds. Be sure to check the expense ratios of any mutual funds or ETFs you're investing in.

Mutual Funds: A mutual fund pools together money from a group of investors and purchases stocks, bonds and other securities. The fund acts as one investment and as the underlying securities increase or decrease in value, so does the overall value of the fund.

Mutual funds help individuals to take advantage of diversification, asset allocation and professional money management when they're unsure or don't have the time to do it themselves. Each mutual fund has a manager and a strategy for the fund's overall objective, which can be found in the fund's prospectus. Some may be geared towards growth or capital appreciation and others may be geared towards income generation or stability.

Even though a mutual fund may own stocks, bonds and other securities, its price does *not* fluctuate throughout the day, but instead is set at the end of each trading day. This means that if you want to purchase or sell a mutual fund, you will do so at the end of the day *after* its price has been set based on the value of its underlying securities.

Note: You'll likely see a variety of mutual fund offerings for you to choose from in your employer's 401(k), 403(b) or TSP plan. Among these options you may see a *Target Date Fund*, which is a type of mutual fund whose asset allocation is set according to a selected time frame. The allocation becomes more conservative as the "target date" approaches.

Risk Tolerance: As an investor, this describes your comfort level with certain levels of uncertainty when it comes to fluctuations (large and small) in the value of your portfolio.

Stocks: One share of stock represents a single share of ownership (equity) in a company. When you purchase a share of stock, you become a part owner in the company (proportionally to the number of shares owned by others) and you can even vote on how the company operates. The price of the stock will fluctuate up and down over time depending on how much an investor is willing to pay for it (or think it will be worth).

Fun homework assignment: Visit www.yahoofinance.com and look up the stock prices for some of your favorite companies. You can track the movement in price throughout the day and overtime.