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# INVESTMENT TERMINOLOGY HANDBOOK



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# INTRODUCTION

**Do you struggle with knowing what investment terms mean, and how to correctly interpret them for your organization?**

**Do you want to be confident when discussing your nonprofit's finances with board members, advisers, and committees?**

Responsibly managing investments is critical to your nonprofit's success, but it starts with understanding common investment terms and how to apply them to your nonprofit.

- ✓ Oftentimes, learning investment terminology may feel like trying to understand a foreign language, which can be difficult and challenging.

Save time and clear up confusion today with Eder Financial's **Investment Terminology Handbook**, which simplifies the process of learning common investment terms and applying them to your nonprofit.

The **Investment Terminology Handbook**:

- ✓ **Walks you through common investment terms with definitions** *written in plain language*, making complex concepts easier to read and understand.
- ✓ **Provides practical information**, showing you how to apply the definition of each term.

- ✓ **Organizes investment terms by category**, helping you connect similarities across terms. Categories for investment terms include:

- **Concepts, Processes, and Strategies**
- **Publicly-traded Companies**
- **Investment Types and Loans**

**Plus** – You'll get several examples and real-world **insights** across investment terms, giving you the confidence you need to navigate financial discussions with your teams.

The **Investment Terminology Handbook** is one of the companion tools designed to accompany the **Investment Guidelines Video** in the Nonprofit Toolkit training series.

## **TIP:**

For assistance with creating your own investment guidelines, contact **Eder's Organizational Investing Team**. They'll provide you with our handy **Investment Guidelines Template** to simplify the process. Let us know if you need help by emailing us at [oi@eder.org](mailto:oi@eder.org) or by calling 800-746-1505, extension 3.



# CONCEPTS, PROCESSES, & STRATEGIES



## WHAT IS BENCHMARKING ?

**Benchmarking** is the process of comparing an investment's financial performance against *industry standards*, such as the S&P 500 Index, to identify areas for improvement and optimize performance.

In addition to the S&P 500 Index, other common investment benchmarking indexes include the:

- ✓ Dow Jones Industrial Average Index
- ✓ Russell 2000 Index
- ✓ Nasdaq Composite Index

### HOW DOES BENCHMARKING WORK?

Benchmarking helps you to better understand which investments have historically performed well, and the investments that you may want to avoid.

- ✓ You can then set realistic investment goals for the future based on present and past investment performance.

## WHAT IS CORE EQUITY?

**Core equity** is a long-term investment strategy that focuses on holding high-quality, stable company stocks within a portfolio.

### HOW DOES CORE EQUITY WORK?

Core equity emphasizes predictable returns from established businesses, rather than rapid growth or *speculative plays*, which involve taking calculated risks to achieve significant returns in a short period of time.

## WHAT IS DIVERSIFICATION?

**Diversification** is an investment strategy that involves spreading investments across various asset classes, industries, and geographic regions.

### HOW DOES DIVERSIFICATION WORK?

The primary purpose of diversification is to reduce the risk and volatility of an investment portfolio by limiting exposure to any single asset or risk factor.

- ✓ In simpler terms, diversification means ***not*** “*putting all your eggs in one basket.*”

## WHAT IS A FIDUCIARY?

A **fiduciary** is a person or organization that acts in good faith on behalf of others' interests, instead of their own.

- ✓ A fiduciary's duty is to preserve the trust that their clients have in them.

### HOW DOES A FIDUCIARY WORK?

A fiduciary's task usually involves overseeing another's finances.

### EXAMPLES:

- ✓ Managing an organization's assets
- ✓ Managing assets for a specific group of people

## WHAT IS RISK TOLERANCE?

**Risk tolerance** is a concept that describes the degree to which an individual or organization is willing and able to endure risk in pursuit of potential rewards.

- ✓ Risk tolerance involves both a psychological willingness to accept volatility and uncertainty, and the financial capacity to absorb potential losses.

### HOW DOES RISK TOLERANCE WORK?

In plain words, your risk tolerance is the *relationship between your willingness to take investment risks and its impact on your investment allocation decisions.*

**Key factors influencing risk tolerance are:**

- ✓ The financial goals of your organization
- ✓ Your time horizon
- ✓ Your need for income
- ✓ Your investment expertise

## WHAT IS A TIME HORIZON?

An investment **time horizon** describes the length of time an investor expects to hold onto an investment before accessing the money, or before reaching a specific financial goal.

### HOW DOES A TIME HORIZON WORK?

A time horizon is a crucial factor in determining investment strategies and the types of investments suitable for a portfolio.

- ✓ The length of your specific time horizon plays a significant role in determining how much risk you can comfortably take with your investments.
- ✓ The relationship between your time horizon and your investments directly influences your asset allocation.
  - The relationship also influences how your investment portfolio is divided among different asset classes, such as stocks, bonds, and cash equivalents.

### EXAMPLES:

- ✓ A longer time horizon typically allows for greater risk exposure, as there's more time to recover from market volatility and potentially generate higher returns.
- ✓ Conversely, a shorter time horizon usually necessitates a more conservative approach to preserve capital.

# PUBLICLY-TRADED COMPANIES



## WHAT IS A STOCK?

A **stock** represents ownership in a publicly-traded company.

- ✓ Each stock, or unit of ownership, is referred to as a share of a company.
- ✓ The company's stock is traded publicly on a stock exchange, which is a marketplace for buying and selling stocks and bonds.

### HOW DOES A STOCK WORK?

When you buy a stock, you're purchasing a share in the company, making you a partial owner of the company.

## WHAT IS EQUITY?

The proportion of shares, or stocks, that **you own** in a publicly-traded company, compared to the total shares, is called your **equity** in that company.

- ✓ The more stock you own in a company, the more equity you have in that company.

### TIP:

*All stocks are considered equities because they represent company ownership.*

But not all equities are just made up of stocks.

- ✓ *Equities can also include other types of company ownership beyond stock ownership.*

### HOW DOES EQUITY WORK?

To calculate your equity, *divide the total number of shares available by the number of shares that you own.* Refer to the examples shown next.

### EXAMPLES:

If you own 10 shares out of 100 total shares, your equity in the company is 10%:  
 $100 / 10 = 10\%$

- ✓ The remaining 90% equity is comprised of shares that others own in the same company.

If you own 1,000 shares out of 100,000 total shares, your equity in the company is 1%:  
 $100,000 / 1,000 = 1\%$

- ✓ The other 99% equity is the combination of shares from other owners.

## WHAT IS A GROWTH STOCK?

A **growth stock** represents a share in a **growth company**, which is expected to increase its earnings and/or revenue faster than average, *when compared to the industry or broader market averages.*

### HOW DO GROWTH COMPANIES WORK?

Growth companies prioritize aggressive expansion and innovation, reinvesting their profits back into the business, rather than paying dividends to shareholders.

### WHAT IS A VALUE STOCK?

**Value stocks** are shares of companies trading below their intrinsic value and are often overlooked by the market despite their solid fundamentals.

#### HOW DOES A VALUE STOCK WORK?

Unlike high-growth stocks that dominate headlines, value stocks usually present steady returns and long-term potential.

### WHAT ARE SECURITIES?

**Securities** represent ownership (like stocks) or debt (like bonds) and can be bought and sold on financial markets.

### WHAT IS MARKET CAPITALIZATION?

**Market capitalization**, also called **market cap**, is the current market value of all of a company's outstanding stock shares

#### HOW DOES MARKET CAPITALIZATION WORK?

##### EXAMPLE:

ABC Company, with 1 million outstanding shares worth \$100 each, would have a market cap of \$100 million dollars.

- ✓ Market cap is often used to indicate a company's size and worth in comparison to its peers.

### WHAT IS A SMALL-CAP COMPANY?

A **small-cap company** is a publicly traded company with a relatively small market capitalization, generally *ranging from \$300 million to \$2 billion*.

- ✓ **Small-cap companies** are smaller in size and less established than large-cap companies, offering the potential for high growth, but they are also higher risk.

### WHAT IS A MID-CAP COMPANY?

A **mid-cap company** is a publicly-traded company with a market capitalization falling within a medium range, generally *considered to be between \$2 billion and \$10 billion*.

### WHAT IS A LARGE-CAP COMPANY?

A **large-cap company** is a publicly-traded company with a large market capitalization, generally *defined as \$10 billion or more*.

- ✓ **Large-cap companies** are typically well-established and are often leaders in their respective industries.
- ✓ Investing in **large-cap stocks** is often seen as a relatively lower-risk strategy due to the stability and maturity of these companies.

#### TIP:

Stock investment offerings will often use the words **Small-, Mid-, or Large-Cap** in their names to indicate the relative size of the companies owned.





## WHAT ARE INTERNATIONAL STOCKS?

**International stocks** are shares of companies that are based in countries outside of the investor's home country.

- ✓ International stocks are often in the developed market, in contrast to stocks that are in emerging markets.

### EXAMPLE:

If you reside in the United States, international stocks would be any stocks that are not related to a U.S.-based company, which may include companies listed on foreign exchanges or those with American Depositary Receipts (ADRs) listed on US exchanges.

## WHAT ARE EMERGING MARKET STOCKS?

**Emerging market stocks** are shares in companies located in countries with rapidly growing economies that are in the process of industrialization and modernization. These countries are transitioning from a *developing* status to a *developed* status.

### HOW DO EMERGING MARKETS WORK?

Emerging markets include countries such as China, India, and Brazil.

Emerging market stocks offer higher potential returns, but also come with increased volatility and risk due to a country's:

- ✓ Less developed financial systems
- ✓ Potential political instability
- ✓ Less stringent regulatory standards compared with developed markets

# INVESTMENT TYPES & LOANS



## WHAT IS AN INVESTMENT PORTFOLIO?

An **investment portfolio** refers to a collection of investments, such as stocks, bonds, real estate, and other assets, which an individual or an organization holds.

### HOW DOES AN INVESTMENT PORTFOLIO WORK?

The purpose of an investment portfolio is to manage risk and generate returns based on an investor's financial goals, risk tolerance, and investment time horizon.

## WHAT ARE CASH EQUIVALENT INVESTMENTS?

**Cash equivalents** are short-term, highly liquid investments that can be readily converted into a known amount of cash.

### HOW DO CASH EQUIVALENTS WORK?

A key characteristic is that cash equivalents are so close to their maturity dates that they present a very low risk of changes in value due to interest rate fluctuations.

Generally, investments qualify as cash equivalents if they have an original maturity of *three months or less*.

#### **Cash equivalents include:**

- ✓ Treasury bills
- ✓ Commercial paper
- ✓ Money market funds
- ✓ Short-term government bonds

## WHAT ARE ALTERNATIVE INVESTMENTS?

**Alternative investments** go beyond traditional stocks and bonds, meaning that they can open doors to unique opportunities that help increase and protect your wealth.

Alternative investments offer enhanced returns, portfolio diversification, lower volatility, and potential tax efficiency.

**These investments encompass a wide range of strategies and asset types, including:**

- ✓ Private equity
- ✓ Hedge funds
- ✓ Real estate
- ✓ Digital currency
- ✓ Infrastructure
- ✓ And many more

### HOW DO ALTERNATIVE INVESTMENTS WORK?

**Alternative investments** often have lower correlations with traditional markets, potentially offering diversification benefits and higher returns.

- ✓ However, they also tend to be more complex and illiquid, meaning they can't be quickly converted into cash without a loss in value.

## WHAT IS A BOND?

A **bond**, in the financial sense, represents a loan made by an investor to a borrower, such as a corporation or government entity.

### HOW DOES A BOND WORK?

When investors buy bonds, they are essentially *lending money to the issuer*.

- ✓ In return, the issuer agrees to make regular interest payments to the bondholder (determined by the coupon rate, or the fixed annual interest rate).
- ✓ The issuer makes payments until the bond matures. Then, the issuer *repays the original principal amount to the bondholder*.

#### KEY:

**Bond terms** may vary from a couple of months to a couple of decades. Bond issuers can vary in creditworthiness from prime or high grades, down to speculative or high-risk credit ratings.



## NEED HELP WITH INVESTMENT FUNDS?

Learning investment terminology helps you to better understand its meaning and purpose. However, it's equally important for you to utilize your new knowledge to achieve organizational investment goals.

#### EXAMPLE:

If you want to minimize your nonprofit's investment risk, you need to know which types of stocks will work the best for your organization.

- ✓ Lowering your risk, then, would mean that you'd want to steer clear of investing in growth stocks, and instead, choose other stocks that are less risky.

**If you're setting up an investment fund for your nonprofit, let us know if we can help.**

Contact **Eder's Organizational Investing Team** at [OI@eder.org](mailto:OI@eder.org) or **800-746-1505, extension 3**, and we'll be glad to talk with you and conduct a complimentary review of your investing needs.

- ✓ As a **BONUS**, you'll also receive a **FREE Investment Guidelines Template**, which you can use right away to facilitate investment decisions in your own organization.

**We look forward to hearing from you soon!**



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*If you have questions, need assistance,  
or want to share your feedback, please  
let us know. We'd love to hear from you!*

*Thank you for entrusting us to walk with you  
along your nonprofit investing journey.*

*Sincerely,*

**The Eder Financial Team**

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