



GLOSSARY

401(k)	U.S. tax-deferred retirement plan that allows workers to contribute a percentage of their pre-tax salary for investment in stocks, bonds, or other securities. The employer may match all or part of employees' contributions.
Accrued benefit	Amount of accumulated pension benefits of a pension plan member.
Accumulated benefit obligation (ABO)	Present value of pension benefits promised by a company to its employees, at a particular date and based on current salaries.
Actuarial gain/loss	An actuarial gain (loss) appears when actual experience is more (less) favorable than the actuary's estimate.
Annuity	A contract that provides an income for a specified period of time, such as a number of years or for life.
Asset-backed security (ABS)	A security that is collateralized by loans, leases, receivables, installment contracts on personal property, on real estate. Mortgage-backed securities, collateralized by commercial or residential mortgages, are a type of ABS.
Asset-liability management (ALM)	The management of assets to ensure that liabilities are sufficiently covered by suitable assets as and when the liabilities are due.
Assets under management (AUM)	The market value of assets that a financial institution (i.e., pension fund, insurance company, mutual fund, hedge fund, etc.) manages for itself or on behalf of investors.
Balance sheet mismatch	A balance sheet is a financial statement showing a company's assets, liabilities, and equity on a given date. Typically, a mismatch in a balance sheet implies that the maturities, currency, or interest rate structure of the liabilities differ from those of the assets.
Beneficiary	Individual who is entitled to a pension benefit (including the pension plan member and dependants).
Brady bonds	Bonds issued by emerging market countries as part of a restructuring of defaulted commercial bank loans. These bonds are named after former U.S. Treasury Secretary Nicholas Brady and the first bonds were issued in March of 1990.
Carry trade	A leveraged transaction in which borrowed funds are used to buy a security whose yield is expected to exceed the cost of the borrowed funds.
Cash securitization	The creation of securities from a pool of pre-existing assets and receivables that are placed under the legal control of investors through a special intermediary created for this purpose. This compares with a "synthetic" securitization where the securities are created out of derivative instruments.

Collateralized debt obligations (CDOs)	A structured debt security backed by a portfolio of securities or loans. Securitized interests in the pool of assets are divided into tranches with differing repayment and interest earning streams. In the event of nonpayment or default, the higher-risk “equity” tranches absorb the first loss from anywhere in the portfolio, but up to a limit. After the equity tranche loss limit has been reached, the next least-secured tranche then suffers the additional principal loss, and so on. Interest earnings are typically redistributed toward the high-risk tranche from the more senior or secured tranches. Rating agencies provide separate ratings for each tranche.
Collective action clause	A clause in bond contracts that includes provisions allowing a qualified majority of lenders to amend key financial terms of the debt contract and bind a minority to accept these new terms.
Credit default swap	A financial contract under which an agent buys or sells risk protection against credit risk for a periodic fee in return for a payment by the protection seller contingent on the occurrence of a credit/default event.
Credit enhancement	The process of reducing credit risk by requiring collateral, insurance, or other agreements to provide bondholders with reassurance that principal and interest payments will continue if the borrower defaults.
Credit spreads	The spread between benchmark securities and other debt securities that are comparable in all respects except for credit quality (e.g., the difference between yields on U.S. Treasuries and those on single A-rated corporate bonds of a certain term to maturity).
Debenture	An unsecured bond whose holder has the claim of a general creditor on all assets of the issuer not pledged specifically to secure other debt. A debenture is documented in an indenture.
Defined benefit plan	Pension plan in which benefits are determined by such factors as salary history and duration of employment. The sponsor company is responsible for the investment risk and portfolio management.
Defined contribution plan	Pension plan in which benefits are determined by returns on the plan’s investments. Beneficiaries bear the investment risk.
Dependency ratio	Ratio of pensioners to those of working age in a given population.
Derivatives	Financial contracts whose value derives from underlying securities prices, interest rates, foreign exchange rates, market indexes, or commodity prices.
Dollarization	The widespread domestic use of another country’s currency (typically the U.S. dollar) to perform the standard functions of money—that of a unit of account, medium of exchange, and store of value.
EMBI	The acronym for the JPMorgan <i>Emerging Market Bond Index</i> that tracks the total returns for traded external debt instruments in the emerging markets.

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Exchange market	An organized place or organization for trading securities and commodities, usually involving an auction process. Examples include the New York Stock Exchange (NYSE) and the American Stock Exchange (AMEX).
Exchange-traded funds	A type of an investment company whose objective is to achieve the same return as a particular market index or basket of securities. Shares issued by ETFs trade on a secondary market, like a stock, thus experiencing price changes throughout the day as they are bought and sold.
Fallen Angel	Bonds that at the time of issue carried investment grade credit ratings, but whose ratings have fallen over time to subinvestment-grade levels.
Fiscal agent	A bank or trust company that handles fiscal matters for a bond issuer, including paying coupons, redeeming bonds at maturity, and paying any relevant taxes. Unlike the trustee, the fiscal agent acts as a representative of the borrower.
Foreign direct investment	The acquisition abroad (i.e., outside the home country) of physical assets, such as plant and equipment, or of a controlling stake in a company, enterprise, or other entity.
Forward price-earnings ratio	The multiple of future expected earnings at which a stock sells. It is calculated by dividing the current stock price (adjusted for stock splits) by the estimated earnings per share for a future period (typically the next 12 months).
Funded pension plan	Pension plan that has accumulated dedicated assets to pay for the pension benefits.
Funding gap	The difference between the discounted value of accumulating future pension obligations and the present value of assets.
Funding ratio	Ratio of the amount of assets accumulated by a defined benefit pension plan to the sum of promised benefits.
Hedge funds	Investment pools, typically organized as private partnerships and often resident offshore for tax reasons. These funds face few restrictions on their portfolios and transactions. Consequently, they are free to use a variety of investment techniques, including short positions, transactions in derivatives, and leverage.
Hedging	Offsetting an existing exposure by taking an opposite position in the same or a similar risk, for example, by buying derivatives contracts.
High-yield bonds	Bonds with a speculative credit rating [below BB (S&P) or Ba (Moody's) or lower]. High-yield bonds offer investors higher yields than bonds of financially sound companies. High-yield bonds are also known as "junk" bonds.
Hybrid pension plan	Retirement plan that has characteristics typical of both defined benefit and defined contribution plans.

Indenture	Agreement between the issuer and bondholders that details specific terms of the bond issuance. It specifies legal obligations of the bond issuer and rights of bondholders. An indenture spells out the specific terms of a bond, as well as the rights and responsibilities of both the issuer of the security and the holder.
Individual retirement account (IRA)	In the United States, tax-deferred retirement plan permitting all individuals to set aside a fraction of their wages.
Interest rate swaps	An agreement between counterparties to exchange periodic interest payments on some predetermined principal value, which is called the notional principal amount. For example, one party will make fixed-rate and receive variable-rate interest payments.
Investment-grade issues (Subinvestment-grade issues)	A bond that is assigned a rating in the top four categories by commercial credit rating agencies. S&P classifies investment-grade bonds as BBB, or higher, and Moody's classifies investment grade bonds as Baa or higher. (Subinvestment-grade bond issues are rated bonds that are below investment grade.)
Large complex financial institution (LCFI)	A large financial institution that is involved in a diverse range of financial activities and/or in a diverse range of geographical areas.
Leverage	The proportion of debt to equity. Leverage can be built up by direct borrowing (on-balance-sheet leverage, commonly measured by debt-to-equity ratios) or by using off-balance-sheet transactions.
Life-cycle funds	Diversified mutual funds designed to adjust over time with an investor's assumed risk tolerance throughout a variety of life circumstances or savings goals.
Medium-term note (MTN)	A corporate debt instrument that is continuously offered to investors over a period of time by an agent of the issuer. Investors can select from maturity bands of 6 months to 1 year, more than 1 year to 18 months, more than 18 months to 2 years, etc., typically extending to 10-year maturities.
Lump sum payment	Withdrawal of accumulated benefits all at once, as opposed to in regular installments.
Mark-to-market	The valuation of a position or portfolio by reference to the most recent price of a financial instrument. The mark-to-market value might equal the current market value—as opposed to historic accounting or book value—or the present value of expected future cash flows.
Market microstructure	The institutional and behavioral aspects of securities trading process: how information arrives and is disseminated; arrival and execution of orders; impact of market makers and other intermediaries; role of market participants such as individual and institutional investors. Issues concerning market structure include transparency, liquidity, consolidation of order flow, price discovery, trading protocols, clearing and settlement, transaction costs, and regulation.

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Mutual fund	A fund operated by an investment company that raises money from shareholders and invests in a group of assets, in accordance with a stated set of objectives. Mutual funds may generally fall under the classification of “open-ended funds” that sell and redeem shares at any time directly to shareholders.
Occupational pension scheme	Pension plan set up and managed by a sponsor company for the benefit of its employees.
Overfunded plan	Pension plan in which assets accumulated are greater than the sum of promised benefits.
Over-the-counter market	A decentralized market where securities are typically traded over the telephone, facsimile, or electronic network. Also referred to as the “OTC market.”
(Pair-wise) correlations	A statistical measure of the degree to which the movements of two variables (for example asset returns) are related.
Pay-as-you-go basis (PAYG)	Arrangement under which benefits are paid out of revenue each period.
Pension contribution	Payment made to a pension plan by the sponsor company or by plan participants.
Primary market	The market where a newly issued security is first offered/sold to the public.
Private pension plan	Pension plan where a private entity receives pension contributions and administers the payment of pension benefits.
Projected benefit obligation (PBO)	Present value of pension benefits promised by a company to its employees at a particular date, and including assumption about future salary increases (i.e., assuming that the plan will not terminate in the foreseeable future).
Proprietary trading desk	Investment bank or dealer trading operation, using its own capital, in which direct gains are sought, rather than fee or commission income.
Public pension plan	Pension plan where a government body administers the payment of pension benefits (e.g., social security and similar schemes).
Put (call) option	A financial contract that gives the buyer the right, but not the obligation, to sell (buy) a financial instrument at a set price on or before a given date.
Reinsurance	Insurance placed by an underwriter in another company to cut down the amount of the risk assumed under the original insurance contract.
Secondary markets	Markets in which securities are traded after they are initially offered/sold in the primary market.
Self-regulatory organization	Nongovernment organization that has statutory responsibility to regulate its own members through the adoption and enforcement of rules of conduct for fair, ethical, and efficient practices.

Short sell	Selling a security that the seller does not own but is committed to repurchasing eventually. It is used to capitalize on an expected decline in the security's price.
Solvency	Generally defined as the ability of an insurer to meet its obligations (liabilities) as and when they fall due.
Sponsor company	Company that designs, negotiates, and normally helps to administer an occupational plan for its employees and members.
Spread	See "credit spreads" above (the word credit is sometimes omitted). Other definitions include the gap between bid and ask prices of a financial instrument.
Stop loss order	Order to sell a security when it reaches a certain price.
Syndicated loans	Loans made jointly by a group of banks to one borrower. Usually, one or several lead banks take a larger percentage of the loan (often with a commitment to hold an agreed percentage), and they partition (syndicate) the balance to other banks.
Tail events	The occurrence of large or extreme movements (e.g., price, volatility, correlation, longevity) that, in terms of their probability of occurring, lie within the tail region of the normal distribution of possible outcomes.
Trustee	Person or organization with a duty to receive, manage, and disburse the assets of a plan.
Underfunded plan	Pension plan in which assets accumulated are smaller than the sum of promised benefits.
Unfunded benefit liability	Amount of promised pension benefits that exceeds a plan's assets.
Underwriting	The process whereby a firm, usually an investment bank, purchases an issue of securities from a company and resells it to investors. In general, the underwriter guarantees the proceeds of a security sale to the issuer, thereby in effect taking ownership of the securities.
Value at Risk ("VaR")	An estimate of the loss, over a given horizon, that is unlikely to be exceeded at a given probability level.
Vesting	Right of an employee, on termination of employment, to obtain part or all of his accrued benefits.
Yield curve	A chart that plots the yield to maturity at a specific point in time for debt securities with equal or similar credit risk but different maturity dates.