# BUILDING BLOCKS FOR RETIREMENT

## Investment Strategy

## Basic Investment Terms

### Asset Allocation
Asset allocation means spreading your investments over different types of investment categories.

### Asset Class
A group of investments considered similar in potential risk and return.  There are three basic asset classes: stocks, bonds, and fixed income securities.

### Assets
Assets are the property and resources (such as cash and investments) of a person or company.  An investment fund's assets include whatever securities (stocks, bonds, Treasury bills, etc.) it owns, plus any cash.

### Blue-Chip Stock
In a poker game, blue-chips traditionally are the most valuable.  In Wall Street slang, blue-chip stocks are shares in the nation's biggest and most consistently profitable companies.  Needless to say, there is no official list of blue-chip companies because they keep changing.

### Bonds
Bonds are essentially loans—or debt.  They are issued by corporations, governments, or municipalities to raise money.  A bond certificate is like an IOU; it shows the amount loaned (principal), the rate of interest to be paid on the loan, and the date that the principal will be paid back (maturity date).  Mutual funds that invest primarily in bonds are called "income" funds.

### Common Stocks
When people talk about a company's stock, they usually mean common stock.  When you own common stock in a company, you share in its success or failure.  If the company prospers, you may get part of the profits, called dividends.  Common stock generally has the greatest potential for growth.  However, it also carries the greatest risk since that value can drop if the company does poorly.  If the company goes bankrupt, common stockholders are the last to receive any payment.

701 Westchester Ave, Suite 320E, White Plains, New York, 10604

### Compounding

When you put money in the bank, it earns interest. When that interest earns interest, the result is "compound" interest. Of course, investing in a retirement plan is different from putting money in the bank, but you still get the benefits of compounding. For example, if income from bonds or dividends from stocks or investment funds is reinvested, their earnings compound as well. Compounding can help your account grow.

### Diversification

Diversification, the concept of spreading your money across different kinds of investments, could potentially moderate your investment risk. It is the idea of not putting all your eggs in one basket. A diversified portfolio can help shield you from large losses because even if some securities falter, others may perform well. However, diversification cannot protect against loss.

### Dollar Cost Averaging

Dollar cost averaging is a method of investing. Money is invested at regular intervals in the same investment. Because you invest the same amount each time, you automatically buy less of this investment when its price is higher and more when its price is lower. Though dollar cost averaging doesn't guarantee a profit or guard against loss in declining markets, the average cost of each share is usually lower than if you buy at random times. For dollar cost averaging to work, you must continue to invest regularly over time and purchase shares in both up and down markets.

### Equity

Equity is ownership in a company. When you own shares of stock of a company, it also means that you own equity in that company. Stock investments are also called "equities." Similarly, funds that invest in stocks are often called "equity funds."

### 401(k)

Under Section 401(k) of the Internal Revenue Code, employees can set aside money for retirement on a pretax basis through a plan sponsored by their employer. To encourage savings for retirement through these plans, the federal government created special tax advantages for 401(k) contributions.

### Guaranteed Investment Contracts

Investments generally issued by insurance companies or banks which pay a set interest rate over a set time period, with a promise to repay the principal at maturity. Your risk is low if the contracts are issued by a financially sound organization. The issuer of the contract bears any risk associated with the securities underlying the contract. Also called Guaranteed Investment Contracts (GICs), Synthetic GICs, or Bank Investment Contracts (BICs), what differentiates these investments is the protection of loss of principal by the insurance companies or banks issuing the contracts.

### Index/Benchmarks

An index measures the price and performance of a specific group of stocks. There are many indices that an investor can track, including:

- Dow Jones Industrial Average – a formula that represents the stock prices of 30 major industrial companies in the United States. Because it includes companies that represent core sectors of our economy, the Dow is considered the most accepted indicator of overall market performance. When the Dow is up, it means the prices of these companies rose during the day; when it is down, these prices fell.

- NASDAQ 100 Index – reflects NASDAQ's largest one hundred non-financial companies across major industry groups, including computer hardware and software, telecommunications, retail/wholesale trade and biotechnology.

- Russell 2000 Index – is a subset of the Russell 3000 Index. The Russell 3000 Index is based on a ranking of all U.S. publicly traded companies by market capitalization size. The Russell 2000 represents those 2000 companies ranked by size below the top 1000 companies and has become one of the better known indexes used to measure the performance of U.S. small company stocks. It is broadly diversified in terms of industries and economic sectors.

- S&P 500 Index – an index of 500 widely held U.S. stocks. These stocks represent 500 of the largest and most established public companies in the U.S. (based on the market value of their shares), and account for more than 70% of the market capitalization of all publicly traded stocks in the U.S. The Standard & Poor's Corporation calculates the market prices of these stocks, which includes the reinvestment of dividends, as a way to track the overall performance of the stock market.

- S&P/BARRA Growth Index – This index represents approximately 50% of the market capitalization of the S&P 500 Stock Index. The S&P/BARRA Growth and Value indexes are constructed by rating the stocks in the S&P 500 by a single attribute: market price to book value ratio. The Growth Index includes companies with higher price to book ratios.

- S&P/BARRA Value Index – This index represents approximately 50% of the market capitalization of the S&P 500 Stock Index. The S&P/BARRA Value and Growth Indexes are constructed by rating the stocks in the S&P 500 by a single attribute: market price to book value ratio. The Value Index includes companies with lower price to book ratios.

- S&P MidCap 400 Index – These stocks represent the middle tier of the US stock market, while the S&P 500 Index represents the largest tier of the US stock market.

**Inflation**
When the price of goods and services rises over time, the result is called inflation. This means that things you buy today will cost more in the future.

**Investment Mix**
The combination of investment options that you choose.

**Issuer**
A company, government, or municipality that offers bonds to investors. (See bonds.)

### Large-Cap Stock

The stocks of public companies whose market value (the total number of shares outstanding multiplied by their price) is more than $10 billion. Large cap companies are generally well-established corporations with a long track record of steady earnings growth and reliable dividend payments.

### Portfolio

A portfolio is a collection of securities and other investments. Your "investment portfolio" refers to your investments within the plan.

### Return

This is the rate an investment earns—it is expressed as a percentage. It generally refers to the change in value (increase or decrease in share or unit price) and any income earned on the investment over a period of time. It is a way of comparing investments.

### Securities

This term refers to all investment options, including stocks, bonds, short-term securities, and shares of mutual funds, etc.

### Small Cap Stock

The stocks of public companies whose market value (total number of shares outstanding multiplied by their price) is less than $500 million. Small cap companies grow faster than large cap companies and typically use any profits for expansion rather than for paying dividends. But they can also be more volatile than large cap companies and can fail more often.

### Stock

A company sells stock to raise money. When individuals or other companies buy stocks, they become owners of a part of the corporation. This ownership is called "equity".

### Tax-Deferred Contributions

The amount you choose to have deducted from your paycheck and contributed into your retirement savings plan. Your contributions are deducted from your paycheck before income taxes are taken out, which reduces your current taxable income. Taxes will be due on these contributions when you withdraw these contributions from the plan.

### Total Return

The total that you are earning on an investment. Total return is the dividends and interest you get, plus any change in the value of your principal or original investment. If your investment fund share price increased from $23 to $25, and you also received a 20 cent per share dividend, your total return was $2.20—a little over 9%.

### Yield

Yield is the effective interest rate or dividend on an investment. Yield is not the same as total return. It's possible to earn a good yield on an investment, but lose money anyway because of a drop in principal value. A $1,000 bond that pays 10% will continue paying 10% after the prevailing interest rate rises to 11%—but the bond will be worth less than $1,000.

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701 Westchester Ave, Suite 320E, White Plains, New York, 10604