# Decoding Financial Jargon: Stocks and Bonds

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*This article is part 1 of a series attempting to teach the concepts of often misunderstood financial terms and phrases.*

Stocks, bonds, equities, fixed income, mutual funds, asset allocation, dividends, diversification, the stock market. Our industry is filled with terms and phrases. What I've learned from thousands of meetings with clients over the past decade is that few people understand what these terms truly mean. Many people have heard and read them enough to be able to use them in a sentence. We have a vague idea of the meanings, but almost no one understands them well enough to teach them to their children or make tough decisions regarding their finances. So, over the course of a few articles I'd like to share how I teach these concepts to my children, and hopefully shed some light for those who were never taught themselves.

Let's start with stocks (also called equities) and bonds (also called fixed income). These are the basic building blocks within our investment accounts, 401(k)s, IRAs, and college savings accounts. But what are they?

Stock is ownership. When you purchase a share of stock in a company you are buying a piece of that company. How much of the company you own is determined by the total number of shares that exist for that company and the total number you hold. For example, if a company has 10 shares of stock and you own one share then you are a 10 percent owner of that company. The world's largest companies often have millions or even billions of shares of stock. Stock ownership is how millions of average people become business owners. As owners you often have rights to vote on important company business, such as electing a board of directors. In addition, you'll share in the company's profits (often in the form of dividends – to be covered in an upcoming article). The price of the stock on any given day is based on the amount of money a willing buyer will give a current owner for their stock.

Bonds are loans. When a bond is issued (sold by a company or government entity), the purchaser (bondholder) gives his or her money to the issuer in return for a promise to pay the bondholder back the principal investment along with interest. Companies and government entities use bonds to get the money they need for major projects such as new equipment, manufacturing lines, buildings and infrastructure development. The companies or entities are given credit ratings (like your credit score) which play a major role in determining the interest rate. The terms of the bond vary, similar to the loans with which we are familiar (i.e. length of time before principal is paid back, how often the interest is paid, ability of the issuer to pay back the loan early, etc.). Once a bond has been issued, the bondholder can then sell it to another willing buyer and the price is set based on how much someone else is willing to pay for that bond. If the bond is not sold it will be repaid with interest according to its terms unless the company or entity defaults on its payments.

Taking the risk of oversimplification, remember these basic principles: stocks are ownership and bonds are loans. And if you have questions about what you currently own or should own in your portfolio please find and talk to a CERTIFIED FINANCIAL PLANNER™ professional.