Financial terms handbook

Follow along to learn these 62 essential financial terms every entrepreneur needs to know.

Financial terms

A

Accounting period

The accounting period is the range of time a set of financial statements will cover during the accounting cycle. This period can vary depending on the business, and it can last weeks, a month, a quarter, or fiscal or calendar years.

Accounts payable

Accounts payable are the funds you owe to a creditor or a supplier after purchasing goods and services. It includes the bills and liabilities you still have to pay within a few months.

Accounts receivable

Accounts receivable (A/R) is the amount your clients owe to your business. Usually, a business uses an invoice to notify clients of how much they owe, and if not paid, the debt is legally enforceable.

Accrual basis accounting

In accrual basis accounting, you record income when you earn them, and record expenses when they happen. This means you'll record the transaction in a balance sheet even if you haven't received the money for it yet.

Annual percentage rate (APR)

Annual percentage rate (APR) is the interest generated over a year on a loan, meaning it's the cost you pay in a year for borrowing money.

Assets

Assets are the economic resources a business has. They include everything your company owns that has some economic value. They are broken down into current, fixed, tangible, and intangible assets.

B

Balance sheet

The balance sheet is a document that reports your assets, liabilities, and equity and analyzes where money is going and coming from. This gives you a comprehensive snapshot of your company's financial situation at a given moment.

Book value

Book value is how much it costs to carry an asset, which is the asset cost minus the accumulated depreciation.

Bookkeeping

Bookkeeping is the process of recording your financial transactions in order to keep accurate financial records. Bookkeeping logs all transitions as debits and credits, which helps you make decisions about investments, operations, and financing.

C

Capital gain

Capital gains happen when you sell an asset for more than what you paid for it. It can apply to any type of asset, such as stock investments and property. You might have to pay capital gain tax, depending on the area, amount of capital, and type of asset.

Financial terms

Capital loss

Capital loss happens when you sell an asset for less than what you paid for it. When it comes time to pay taxes, capital losses can offset some capital gains tax.

Cash flow

Your cash flow is the movement of funds through your business each month, such as income and expenses. For example, cash flows into your business when a customer purchases your goods or services. Then, cash flows out of your business when you pay expenses like rent and taxes.

Cash flow statement

Cash flow statements track general cash flow, by showing money entering and exiting your business during a specific period of time. This helps determine your business's ability to pay bills.

Certificate of deposit

A certificate of deposit is a type of bank account that holds money for a fixed period of time while earning interest. Although it usually earns higher interest, you can not access funds until the end of the fixed period.

Compound interest

Compound interest happens when you earn interest on the funds in your savings as well as on the accumulated interest earned. Since you're generating interest on interest, your investment will grow at a higher rate.

Cost of goods sold (COGS)

Cost of goods sold is the cost of producing a good or service that your business sells. It helps you calculate profit and how to price your goods and services.

Credit

Credit happens when a borrower receives a good or service before making a payment, and then agrees to pay at a later date. Credit is also used to describe a journal entry when deposits are recorded as credits.

Current assets

Current assets include things that can be easily converted into cash, such as inventory, stock holdings, and short-term investments. Because this type of asset can be quickly turned into cash, it's also often termed "liquid assets."

Current liabilities

Current liabilities refers to immediate debts that must be repaid within one year, such as money you owe to suppliers or vendors.

D

Debit

Debit is a type of entry in accounting to record when you make or owe a payment. You'll debit an account whenever an asset increases or liability decreases.

Demand

Demand refers to consumers' desire and ability to purchase a certain good or service. It helps businesses make decisions about supply and prices, and it affects sales and revenue.

Depreciation

Depreciation is the loss of an asset value over time considering use, wear, tear, or obsolescence. Depreciating assets, such as computers, machinery, and cars, allows businesses to record expenses in increments.

Dividend

Dividends are payments a business makes to shareholders to share the profits with them. Businesses can make payments on a regular basis and issue them in cash, stock shares, or other property.

E

Equity

Equity refers to how much an owner or shareholder invested in a business. Essentially, equity is the net worth of the business, since it can also refer to its potential value.

Expenses

Expenses are any cost necessary to run a business and generate revenue. They are the costs your business collects each month in order to operate, such as rent, utilities, employee salaries, contractor pay, and marketing costs.

F

Financial statements

Financial statements are reports that show how a business performs financially. It includes the balance sheet, cash flow statement, and income statement. Accountants also use these statements to prepare tax reports.

Fixed assets

Fixed assets, also known as long-term assets or non-current assets, can't be easily converted into cash. They often require a significant amount of time before you can have their cash value in hand. These include land, real estate, machinery, equipment, and furniture.

G

General ledger

A general ledger is a record of the company's financial accounts and transactions, including its assets, liabilities, revenue, and expenses.

Gross margin

Gross margin, also known as gross profit margin, measures a business's gross earnings after paying for direct costs, and compares it to sales and revenue. Gross margin is reported as a percentage of sales by subtracting the cost of goods sold from net sales. A high gross margin means the business generates money efficiently.

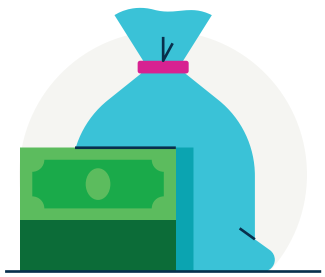
Gross profit

Gross profit refers to the profits a business generates after deducting all costs from production and distribution. You can calculate gross profit by subtracting the cost of goods sold from your total sales.

I

Income

Income is the money a person makes from working or investing, or that a business makes by selling goods or services. However, income has a different meaning depending on the context you use it.



Income statement

The income statement analyzes your company's profits and losses, and it's commonly referred to as the "profit and loss statement." It summarizes the profits and losses incurred during a period. It provides information about your company's ability to generate profit by increasing its revenue, decreasing its losses, or a combination of both.

Inflation

Inflation is when there is an overall increase in prices of goods and services. It happens when the purchasing power or a currency value decreases. In general, this means, you can buy less now than what you could buy before with the same amount of money, which can impact your small business.

Intangible assets

Intangible assets are the opposite of tangible assets and include any assets that you're not able to touch. It includes things such as franchise agreements, patents, brands, trademarks, and copyrights.

Interest

Interest is the price you have to pay a lender for borrowing money. It's usually a percentage of the remaining balance you owe.

Interest rate

Interest rate is the amount of interest a person charges on top of the money they lent and expressed as a percentage.

Inventory

Inventory, also known as stock, refers to the raw materials, finished goods, or work-in-progress goods a business has. There are many different types of inventory and they are an important part of a business's revenue.

J

Journal

An accounting journal contains the business's financial transactions. This allows businesses to keep track of all transactions and it's an important part of auditing.

Journal entry

A journal entry records business transactions in the accounting book. It will contain the date of the transaction, the amount debited and credited, a reference number, and a description of the transaction.

L

Liability

Liabilities are things your company is responsible for by law, such as debts and financial obligations. They are any debt accrued by a business in the course of starting, growing, and maintaining its operations. This could include bank loans, credit card debts, and money owed to vendors and product manufacturers.

Liquidity

Liquidity is how easy it is to buy or sell an asset or security and turn it into cash. The more liquid an asset is, the easier it is to convert it to cash. Liquidity can also show a business's ability to pay off its debts.

Loan

A loan is an amount of money borrowed from a financial institution or a person, such as a bank, credit union, or a family member.

M

Maturity date

A maturity date is the date you must pay a debt in full or when the final payment is due. Maturity dates apply to loans, bonds, and any other type of debt.

N

Net income

Net income is your revenue minus expenses, such as cost of goods sold, administrative expenses, and taxes. Net income helps businesses see how much they make and how many expenses they have.

Net margin

Net margin measures what percentage of the revenue makes up the profits. It shows how much profit a business can get from the total sales.

Net profit

Net profit is the total amount a business earned or lost at the end of an accounting period. To determine your net profit, you have to subtract all your business expenses from your total sales revenue. Net profit is usually used to determine whether a business's earnings are increasing or decreasing.

Non-current liabilities

Non-current liabilities, also referred to as long-term liabilities, include debts or obligations that your company must repay in over a year's time. For example, business loans, deferred tax liabilities, mortgages, and leases.

Non-operating assets

Non-operating assets refer to assets that aren't critical for a business to provide its product or service, but are still essential to establish and run a business. Many intangible assets fall into this category, such as brands, trademarks, and patents.

O

Operating assets

Operating assets are the type of assets a business needs to complete its day-to-day functions. They are used to produce products or services, including fixed and current.

Operating expenses

Operating expenses refers to the costs of running a business aside from the costs of making or delivering the product or service. Operating expenses include office supplies, rent, and utilities.

P

Payroll

Payroll refers to how a business pays their employees, and allows them to track payments throughout the year. It can also refer to the total number of employees employed or refer to the total amount spent on employees' salaries.

Profit and loss

Profit and loss refers to the difference between a business's revenues and expenses to determine a profit or loss. You can keep a record of these revenues and expenses with a profit and loss statement.

Profit and loss statement

A profit and loss statement is the same thing as an income statement. It summarizes your profit and losses during a period and provides information about the company's ability to generate profit.

R

Rate of return

Rate of return is a percentage showing the gain or loss of an investment over a period of time. You can calculate the rate of return of any investment by calculating the percentage change between the beginning and end of the period.

Return on investment (ROI)

Return on investment (ROI) is a formula to calculate how much money you made or lost during an investment. It evaluates whether your investment was efficient or profitable. To calculate ROI you need to divide the total profit by the amount you paid for the investment, then multiply it by 100 to reach a percentage.

Revenue

Revenue is the amount of money a business earns from the sale of goods or services. Total revenue includes both operating and non-operating revenue.

Financial terms

S

Shareholder

A shareholder is a person, institution, or company that owns one or more shares of a company's stock. It essentially means they own part of the company and give them rights and responsibilities, and get benefits such as dividends.

Supply chain

A supply chain refers to the steps it takes to create a product from raw materials and move from the supplier to the manufacturers leading all the way to a finished product ready for sale.

T

Tangible assets

Tangible assets are assets that you can see and touch, including current or fixed assets. For instance, cash is something you can physically touch. Most fixed assets are also tangible assets, such as land, real estate, machinery, equipment, and furniture.

W

W-2

A W-2 is a form that shows information about the income an employee earned, including benefits and the taxes withheld from paychecks. Generally, if a person worked as an employee for a business, they will receive a W-2 form from their employer.

W-4

A W-4 is a form letting your employer know how much money you want withheld from your paycheck for taxes. It can help you pay the correct amount of taxes each period to avoid complications when filing a tax return.

Y

Yield

Yield is a percentage that expresses how much you received from owning an asset or investment over a period of time compared to the investment itself.