- **downgrade** (verb)
- **downgrade** (downgrades) (N-count)

It you downgrade something, you reduce its status.

The move follows yesterday's <u>downgrade</u> of Anglo Irish Bank's debt by Moody's.

- **leverage** (N-uncountable)

  leveraged (adjective)

Leverage - also called financial leverage - refers to the degree to which an investor or business is utilizing borrowed money. If a company is leveraged, it means that they have borrowed money to supplement investment. Companies that are highly leveraged may be at risk of bankruptcy if they are unable to make payments on their debt; they may also be unable to find new lenders in the future. Leverage is not always bad, however; it can increase the shareholders' return on their investment and often there are tax advantages associated with borrowing.

"… rules that make sure we only have sensible amounts of <u>leverage</u> when people buy football clubs because we all know what happens when debt gets out of control," Hunt told the BBC.

Aviva would need to engage in disposals of unattractive businesses to reduce <u>leverage</u> which would help drive more comfort around its ability to pay a full cash dividend.

Common collocations

leveraged <u>buyout</u>, leveraged <u>debt</u>, leveraged <u>takeover</u>, <u>to reduce</u> leverage, <u>highly</u> leveraged

- **deleverage** (verb)

When a company decides to deleverage, it reduces its amount of debt. In other words, it reduces the amount it is borrowing.

Communications. INM is pursuing the sale as part of its aim to <u>deleverage</u> in order to pay off bondholders who are owed €200m.

- **gearing** (N-variable)

Gearing is another word for leverage.

Instead WPP has focused on paying down its debt pile to get the company's <u>gearing</u> ratio of net debt to earnings down to about two times.

- **convertible arbitrage** (N-uncountable)

Convertible arbitrage is a strategy involving the purchase of convertible securities and the subsequent shorting of the corresponding stock. Conversion will offset the short position. The transaction may be profitable if the convertible is priced incorrectly relative to the stock.

- **derivative** (N-count)

  derivative markets (N-count)

A derivative is a financial instrument that has been developed to allow investors to manage and exploit risk. The name 'derivative' is used because they derive from the fundamental financial products. The most common derivatives are futures contracts and options. The most common examples of derivative markets are futures, options and swaps.

- **securitisation** (N-uncount)

  security (N-count)

Securitisation is the process by which something is turned into a security, for example, taking the debt from a number of mortgages and combining them to make a financial product which can then be traded. Examples of securities are stocks, bonds, mortgage-backed securities and other derivatives.

- **toxic debt** (N-uncount)

Toxic debt refers to a whole package of loans where it is now unlikely that it will be repaid.

- **sub-prime mortgage** (N-count)

Sub-prime mortgages carry a higher risk to the lender; therefore, they tend to be at higher interest rates because they are offered to people who have had financial problems or who have low or unpredictable incomes.

- **short selling** (N-uncountable)

  shorting (N-uncountable)

  sell short (verb)

  short seller (short sellers) (N- countable)

Short selling or shorting is a technique used by investors who think the price of an asset, such as shares, currencies or oil contracts, will fall. When you sell short you borrow the asset from another investor and then sell it in the relevant market. The aim is to buy back the asset at a lower price and return it to its owner, pocketing the difference. An investor who uses short selling is a short seller.

1. Use the terms in the box to complete the sentences

leveraging	derivatives	convertible arbitrage	short selling
downgrade	toxic debt	highly leveraged	

a. …………… offer highly geared bets on the future price of things such as shares or commodities.
b. The more you borrow on top of the funds (or equity) you already have, the more …………… you are.
c. …………… can maximise both gains and losses.
d. US regulators have tried to steer a middle ground on the controversial issue of …………… by voting to adopt a rule that will impose restrictions only when a stock's price is in free fall.
e. One credit ratings agency has threatened to …………… Britain's AAA status because of their huge deficit.
f. Hedge funds employ strategies such as long-short, ……………, distressed securities and market timing.
g. Investment bankers spent the boom making ……………, the famous substance that has clogged up the arteries of the financial system.

2. Match each half on the left with one on the right.

1. The good news is that the UK banks are somewhat healthier;
2. But they still face significant perils,
3. Although banks are banned from mixing speculative activities with their day-to-day savings and loans operations,
4. The immediate reason for the start of the crisis was the housing market bubble in the US, which began to deflate in 2006.

a. they can continue to trade most derivatives and to own private equity arms and hedge funds.
b. Other factors – such as sub-prime lending, securitisation, leverage and opacity of financial instruments – magnified the problems resulting from the decline in housing prices.
c. including sovereign debt crises, a ratings downgrade if the support extended by the UK government is perceived to be in doubt and a rise in bad debts in the household and corporate sector if austerity takes its toll on the economy.
d. they are better capitalised, they have reduced their leverage, they have more liquidity and they are more attentive to risk management.

3. Read the passage and answer the questions.

To ensure a company's long-term survival and prosperity, finance managers need to make decisions about the gearing of the company. The higher the gearing (in other words, the greater the proportion of long-term debt), the more exposed the company is in times of economic difficulty. In times of prosperity, a high gearing will give the owners a much better return as net profits will be a much higher percentage of equity even after interest payment on the long-term debt. However, in harder times the owner's earnings will drop dramatically as interest payments soak up most of the company's profits.

a. Why do finance managers need to make decisions about the gearing of the company?
b. When is it useful for a company to have a high gearing?
c. Why is it a disadvantage for a company to have a high gearing when there is an economic downturn?