

Glossary of Essential Small Cap Terms

Market Terminology

Small Cap Stock: Companies with a market capitalization (total value of all shares) typically between \$300 million and \$2 billion. Smaller than large corporations but established enough to have proven business models.

Micro Cap Stock: Even smaller companies, usually with market capitalizations between \$50 million and \$300 million. Generally riskier than small caps.

Market Capitalization (Market Cap): The total dollar value of a company's outstanding shares. Calculated by multiplying the current share price by the total number of shares.

Float: The number of shares actually available for trading by the public. A low float means fewer shares available, which can lead to higher volatility.

Liquidity: How easily shares can be bought or sold without affecting the stock price. Small caps typically have lower liquidity than large caps.

Bid-Ask Spread: The difference between the highest price a buyer is willing to pay and the lowest price a seller is willing to accept. Wider spreads in small caps can increase trading costs.

Market Maker: A broker-dealer who facilitates trading by maintaining an inventory of shares and quoting both buy and sell prices. Small caps often have fewer market makers.

Russell 2000: The most common small cap stock index, consisting of the smallest 2,000 companies in the Russell 3000 index.

S&P 600: Another small cap index that includes 600 small-cap U.S. companies selected by Standard & Poor's.

Sector: A group of companies in the same industry. Common sectors include Technology, Healthcare, Financials, Consumer Discretionary, etc.

Short Interest: The percentage of a company's outstanding shares that have been sold short (betting the price will fall). High short interest can indicate skepticism about a company.

Financial Statement Terms

Revenue/Sales: The total amount of money a company receives from selling its products or services before any expenses are deducted.

Gross Margin: The percentage of revenue that exceeds the cost of goods sold. Calculated as $(\text{Revenue} - \text{Cost of Goods Sold}) / \text{Revenue} \times 100\%$.

Operating Income: Profit after deducting operating expenses but before interest and taxes. Shows how much profit the company's core business generates.

Net Income: The company's total profit after all expenses, taxes, and costs have been deducted from revenue.

Cash Flow: The net amount of cash moving in and out of a business. Positive cash flow is especially important for small caps.

Free Cash Flow (FCF): Operating cash flow minus capital expenditures. Shows how much cash a company generates after accounting for investments to maintain or expand its asset base.

Burn Rate: The rate at which a company is losing money, typically expressed as negative cash flow per month. Critical for evaluating pre-profit small caps.

Debt-to-Equity Ratio: Total liabilities divided by shareholders' equity. Shows how much a company is financing its operations through debt versus its own resources.

Working Capital: Current assets minus current liabilities. Indicates a company's short-term financial health and operational efficiency.

Dilution: The decrease in existing shareholders' ownership percentage due to the company issuing new shares, often to raise capital (common in small caps).

Valuation Metrics

Price-to-Earnings Ratio (P/E): The current share price divided by earnings per share. For small caps, forward P/E (using projected earnings) may be more relevant if current earnings are low or negative.

Price-to-Sales Ratio (P/S): Market capitalization divided by annual revenue. Useful for evaluating companies that aren't yet profitable.

Price-to-Book Ratio (P/B): Share price divided by book value per share. A P/B ratio under 1.0 can indicate a potentially undervalued company.

Enterprise Value (EV): Market cap plus debt minus cash. Represents the total value of a company.

EV/EBITDA: Enterprise value divided by earnings before interest, taxes, depreciation, and amortization. A common valuation metric that accounts for debt levels.

PEG Ratio: P/E ratio divided by the expected earnings growth rate. A PEG below 1.0 might indicate an undervalued company relative to its growth prospects.

Return on Equity (ROE): Net income divided by shareholders' equity. Shows how efficiently a company uses equity to generate profits.

Return on Assets (ROA): Net income divided by total assets. Indicates how efficiently management is using assets to generate earnings.

Small Cap-Specific Concepts

Catalyst: An event or development expected to move a stock price significantly (product launch, FDA approval, contract win, etc.).

Insider Ownership: The percentage of shares owned by company executives, board members, and employees. High insider ownership in small caps often indicates management confidence.

Institutional Ownership: The percentage of shares owned by large financial organizations. Lower institutional ownership is common in small caps and can mean less analyst coverage.

Shell Risk: The risk that a small company is just a "shell" with minimal actual business operations, sometimes used in pump-and-dump schemes.

Uplisting: When a company moves from a smaller exchange (like OTC) to a major exchange like NYSE or NASDAQ, often increasing visibility and liquidity.

Window Dressing: When fund managers buy high-performing stocks near the end of a reporting period to improve the appearance of their portfolio performance.

Quiet Period: A SEC-mandated blackout period surrounding an IPO during which company insiders cannot discuss certain information.

Reverse Split: Consolidating shares to increase the share price. Often seen as a negative in small caps as it may be done to avoid delisting.

Forward Split: Increasing the number of shares by dividing the current share price. Often seen as positive as it may increase liquidity.

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