Wealth Management

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Asset classes

How can asset allocation help you balance investment risk and return?

When you're ready to start **investing**, an important step is understanding the broad categories of investments. Why? So you can choose investments that are appropriate for you.

An **asset class** is a group or category of investments that share similar characteristics. There are three basic asset classes: cash and cash equivalents, fixed income and equities.

Cash and cash equivalents

Sometimes referred to as money market, these are very short-term investments (less than one year). They are liquid, which means easily cashable, and they are stable, meaning they don't fluctuate in value. Usually, investors earn a little bit of interest. Some examples include high-interest savings accounts, some guaranteed investment certificates (GICs), treasury bills (T-bills), commercial paper, and money market mutual funds.

Objectives for this asset class: Liquidity and stability.

Fixed income

This asset class covers investments that are called debt securities. This is where money is loaned to a borrower (for example, a government or corporation) for a specific period of time, in exchange for payment of interest. The original investment amount is repaid at the maturity date. Some fixed income investments can be sold prior to maturity. Examples of fixed income securities include bonds, asset-backed securities and mortgage-backed securities. Longer-term GICs and preferred shares which pay a fixed dividend are also included in this asset class.

Objectives for this asset class: Income, through interest or dividends; preservation of capital (the expectation that you'll receive your original investment back in the future).

Equities

As an asset class, equities refers to stocks, or shares of a company — usually a publicly traded company, which means listed on a stock exchange. Stocks represent partial ownership of a corporation. The price of the stock moves up and down throughout the day, and stocks can be bought and sold, often instantly, when the stock market is open.

Objectives for this asset class: Income from dividends and capital appreciation (the growth of your investment over time).

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Each asset class has different risk exposure and return potential. Asset allocation is an investment strategy where you choose how much of each asset class is appropriate for you. It is one way to balance risk and return in your investment portfolio. Portfolios with a higher weighting of equities may have more volatility and are considered to carry more risk. Portfolios with a lower weighting of equities may have less volatility and are considered to carry less risk. Asset allocation is one of the most important investment decisions you can make. Periodically reviewing your asset allocation and rebalancing — bringing the asset mix back into line — will help your investments to stay on track.

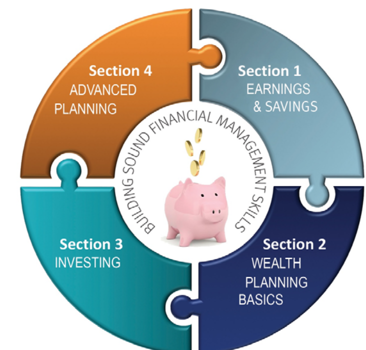
Cash	Fixed income	Equity
usually held in short-term money market or T-bill investments	typically refers to bonds or credit issued by governments or corporations	refers to shares of publicly traded companies

Expected return

Expected volatility

Source: RBC Global Asset Management Inc. (GAM). "Finding the right balance between volatility and returns." Accessed October 2022. www.rbcgam.com/en/ca/learn-plan/investment-basics/understanding-the-relationship-between-volatility-and-returns/detail

Inflation is the increase in the cost of goods and services over time. When prices increase, a dollar doesn't buy as much as it did in the past. The result is reduced **purchasing power**, or a reduction in the value of a dollar. Inflation impacts your savings and investments. If your rate of return from your investments is lower than the rate of inflation, you've effectively lost money through reduced purchasing power.



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