The Stan Clark Financial Team's

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Economics and asset allocation

Three Major Asset Classes…according to Warren Buffett

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In Warren Buffett's 2011 letter to shareholders, published last March, the renowned investment magnate discusses the "basic choices for investors," and his strong preference for one of the choices in particular. First, Buffett defines what investing is: foregoing consumption now, in order to have the ability to consume more later. To be able to consume more, you have to receive more purchasing power. In other words, you have to beat inflation and taxes.

Investments can be classified into three major categories. The first is *currency-based investments*, like money market funds, bonds and bank deposits. Most people think of these investments as safe because they don't fluctuate much in price. But really, they are probably the most dangerous. That's because these investments usually don't keep up with inflation. It's hard to notice the effects of inflation, e.g., a candy bar today costs about the same as what it cost last year. But what about 50 years ago? In the U.S., the dollar has fallen 86 percent since the 1960s. That means it takes $7 today to buy what a dollar did then. In other words, you needed to make four percent just to keep up with inflation – and that's not including tax!

Higher interest rates can compensate for inflation. But today, with interest rates so low, the risk is that such compensation won't occur. That being said, we still own currency-based investments. It makes sense to have some, both for liquidity and your short-term needs, regardless of what the rates are. Beyond that, it's difficult to justify having more.

The second category is assets that don't produce anything, such as gold. An ounce of gold today will still be an ounce of gold in the future. Gold doesn't generate any profits or pay any interest. People buy such assets in the hope that someone else will pay more for them later. People buy gold because they believe the ranks of the fearful will rise. This has worked well in the past decade, attracting even more investors on to the bandwagon. But, with so many on the bandwagon now, and gold up six fold, really, how much more room is there for it to rise?

The third category – and this is Buffett's strong preference – is productive assets such as companies, real estate or farms. These assets should have the ability to produce items that can maintain purchasing power. Buffett believes that, over any extended period of time, productive assets will be the winner compared to the other categories. That's also why he thinks productive assets are also the safest.

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To learn more about CIBC Wood Gundy, The Stan Clark Financial Team and the many ways we can help manage your wealth, please contact us by phone or by email as listed below.

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