GetSmarterAboutMoney.ca
Invest Wisely

OSC ONTARIO SECURITIES COMMISSION
Investor Education

View alternative text version

Risk by asset class

Understanding the risk characteristics of each asset class can help you decide how to balance your portfolio.

An asset class is a group of investments with similar risk and return characteristics. One way to diversify your portfolio is to invest in different asset classes. As risk in a portfolio increases, there is greater potential to earn higher returns. But the risk comes with a greater chance of losing money.

RISK/POTENTIAL RETURN

ASSET CLASS	RISK/RETURN DRIVERS	ROLE IN PORTFOLIO
Real estate For example, Real Estate Investment Trusts (REITs)	• Risks and rewards of ownership • Interest rates • Rents • Capital gain/loss on sale of direct holdings	• Diversification • Generation of return • Protection against inflation
Foreign stocks	• Risks and rewards of ownership • Profits of foreign companies • Exchange rates • Foreign investment risk	• Diversification • Generation of return • Protection against inflation • Foreign currency exposure
Canadian stocks	• Risks and rewards of ownership • Profits of Canadian companies • Favourable tax treatment for dividends	• Diversification • Generation of return • Protection against inflation
Bonds	• Rights of a creditor • Interest rates • Creditworthiness of issuer • Duration • Reinvestment risk • Inflation	• Diversification • Income generation • Protection of capital
Cash*	• Rights of a creditor • Interest rates • Inflation	• Diversification • Income generation • Protection of capital • Cushion for unexpected expenses • Reserve to take advantage of unexpected opportunities

*Cash includes investments such as bank deposits, guaranteed investment certificates (GICs), treasury bills (T-bills), commercial paper and bank acceptances. Treasury bills are regarded as risk-free for all practical purposes. Bank deposits and GICs, to the extent they are covered by the Canada Deposit Insurance Corporation (CDIC), are also risk-free. Other cash instruments carry varying degrees of risk, depending on the creditworthiness of the issuer.