What are the Different Classes of Assets?

Answer:

When it comes to investing their money, many people are content to take a random approach. They may have received a hot tip for a particular investment and decided to plow a large amount of money into it with no regard to the overall balance of their portfolios. However, research has shown that it is through the careful selection of the various asset classes, rather than the individual investments themselves, that people prosper financially. Therefore, the careful selection and distribution of your investments among the various asset classes is likely to prove crucial to the future success of your investment portfolio.

Generally, you should consider five broad asset classes when constructing your investment portfolio: cash, fixed-principal investments, debt, equity, and tangibles.

Cash refers to the most liquid holdings in your portfolio. This asset class includes the balance in your checking account, money market account, and certificates of deposit. Conventional wisdom holds that you should keep three to six months' salary in cash to cover yourself in the event of an emergency.

Fixed-principal investments are those that do not put your principal at risk due to market forces. Fixed annuities and trust deeds fall into this category.

Debt makes up the third asset class. It includes municipal, corporate, government, and government agency bonds. It also covers other debt-secured investments such as collateralized mortgage obligations.

Equity represents an ownership interest in a business entity; this class covers any investment you might make in stocks. It also covers any interest you may have in a closely held corporation or partnership.

Tangibles include your holdings in real estate, art, gold, precious stones, stamps, baseball cards, or other valuable collector's items.

How you choose to distribute your investments among the various asset classes depends on your goals, your risk tolerance, and your expected rate of return. Keep in mind that asset allocation does not guarantee a profit or protect against loss; it is a method used to help manage investment risk. All investments are subject to market fluctuation, risk, and loss of principal. When sold, investments may be worth more or less than their original cost.

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