Quadrant
ASSET MANAGEMENT

QAM Update
February 2012

The QAM letter that highlights recent developments that we think either affect the markets or are important to understanding them.

"I do not think it is an exaggeration to say history is largely a history of inflation, usually inflations engineered by governments for the gain of governments." - Friedrich August von Hayek

Of Bonds, Gold and Labels

As we have mentioned in QAM Updates over the last year, we at QAM see inflation as the number one threat to long-term investors.

In an article from the February 27 edition of the Fortune magazine Warren Buffet - the legendary investor and CEO of Berkshire Hathaway – blatantly says "Right now bonds should come with a warning sign".

This article is a must read for anybody with any type of interest in understanding the current state of affairs for investment portfolios (1).

We think the article is so on point that we are just going to provide our readers with some highlights here:

- Investing is the transfer to others of purchasing power now with the reasoned expectation of receiving more purchasing power in the future, as opposed to laying out money now in the expectation of receiving more money in the future.

- Investments come in many shapes and forms but for the most part they can all be classified into one of the three main categories: Currency-based investments, assets that do not produce anything (i.e. gold) and investment in productive assets.

- Currency-based investments are thought as "safe". They represent money-market funds, bonds, GICs and the like. But under current conditions they are priced to provide return-free risk as opposed to offer risk-free returns.

- If you own one ounce of gold for an eternity you will still own one ounce at its end.

- As "bandwagon" investors join any party, they create their own truth – for a while.

- Bubbles blown large enough inevitably pop. And then the old proverb is confirmed once again: "What the wise man does in the beginning, the fool does in the end".

- Terror over economic collapse drives individuals to currency-based assets and fears of currency collapse fosters movement to sterile assets such as gold.

- Investments in productive assets (stocks, private businesses, farms and real estate) have the ability in inflationary times to deliver output that will retain its purchasing power value.

- Over an extended period of time stocks will be winners over gold and bonds. Moreover, they will be by far the safest.

We feel that inflation is still the number one risk for the long-term investor and are fully aware of the challenges that the current environment represents in the Fixed Income space.

Mindful of their liquidity requirements and risk tolerances, investors should be fully aware of this danger and protect their portfolios accordingly.

For our Fixed-Income Policy, we still suggest a conservative mix and shorter duration compared to the market.

We remain firm in our belief that inflation protected growth in the long-run comes from holding high quality stocks, while liquidity requirements and stability has to be provided by a cautiously selected Fixed Income position in the portfolio.

(1) http://finance.fortune.cnn.com/2012/02/09/warren-buffett-berkshire-shareholder-letter/