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PENDER

Net Worth



Finding a decent yield in today's markets

In the old days, they put debtors in prison, but these days it's savers who feel like they are being punished.

The Federal Reserve added two years to their sentence last month when it said it would keep short-term interest rates at "exceptionally low levels" through at least mid-2013.

The Fed hopes low interest rates will stimulate the economy by prodding banks to lend, borrowers to borrow and companies to stop hoarding cash and put it to better use.

It also wants to force cautious investors out of savings accounts and money market funds into riskier assets such as stocks and longer-term bonds. Rising stock prices presumably would make people feel richer and more willing to spend. A strong bond market would help keep long-term rates low.

If you have been hiding out in safe havens, is it finally time to venture into something higher-risk and higher-yielding?

The answer depends on when you need the money and how much risk you can take.

For money you cannot lose, your options are FDIC-insured bank deposits, money market funds and short-term Treasury bills or Treasury funds. You can get a little more than 1 percent by shopping around, but to get a higher yield you must risk losing some - or in rare cases all - of your principal.

"There is no free lunch," says Eric Jacobson, Morningstar's director of fixed-income research.

Most fixed-income investments pose at least one of three risks:

-- Interest-rate risk: If you buy a bond or other fixed-income investment and interest rates subsequently rise, the price of your bond will probably fall. The longer the maturity of your bond, the bigger the drop. If you need to sell it before it matures, you could get back less than you paid. (The reverse is also true: If interest rates fall, the bond's price will rise.)

You can mitigate this risk by never buying a bond that matures before you need the money.

-- Credit risk: If the issuer of your security falls out of favor or has its credit rating cut, the price could fall and you could lose money if you need to sell before maturity. If the issuer goes bankrupt, you could lose it all.

-- Liquidity risk. Many fixed-income investments don't trade in large numbers or very often. If you need to sell in a hurry, it might be at a fire-sale price.

Last week, I asked several experts how they would advise people looking for yield in the current environment. Here's what they said:

James E. Demmert –

For money you don't need soon and can afford to risk, James Demmert, Managing Partner of **Main Street Research** in Sausalito, would consider dividend-paying common stocks in recession-resistant sectors such as consumer staples, utilities and health care.

Some companies that have dividend yields (annual dividend divided by current price) ranging from 2.7 to nearly 5 percent include: Procter & Gamble, McDonald's, Coca-Cola, Unilever, Bristol-Myers Squibb, Johnson & Johnson, Abbott Laboratories, Dominion Resources, AstraZeneca and American Electric Power.

Demmert says he would put a stop-loss

on these stocks, which will automatically sell them if they fall below a certain price. The key is putting the stop loss "below where the stocks trade in a normal market correction," he says.

Warning: Common stocks are not a fixed-income investment. They are far more volatile and are subject to different risk than those above.

Demmert also would consider some preferred stocks, which are generally less volatile than common stocks but pose the same risks as fixed-income securities. Most preferreds are issued by financial institutions and many got clobbered during the financial crisis. That could happen again, but Demmert says he would buy certain ones such as a Goldman Sachs preferred yielding 6.2 percent and a Wells Fargo Preferred Series J yielding about 8 percent.

Another option is master limited partnerships, which require "a lot of research." Many are set up by energy companies. Rather than retain earnings, they must pay out all profit to shareholders. Demmert owns Magellan Midstream and Buckeye Partners, which both yield around 6 percent and trade on the New York Stock Exchange. For tax reasons, these should not be purchased in retirement accounts.

The key, he says, is to diversify among many of these options.

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