September 14, 2012

What's the likely effect of the Fed's decision to engage in QE3 on fixed income accounts that rely heavily on MBS's? (GNMA, FNMA FHLMC)

Are interest rates going to continue to stay low or fall? How will this affect yields on corporate and Treasury bonds or other fixed income instruments? Should we consider moving more into blue-chip equities that pay regular dividends as an alternative?

Just Wondering . . .

ANSWER: The answer to all of your questions is 'yes'. I am working on this now, in terms of how to compensate for what the Fed did yesterday. This was an action that impacts us directly in terms of the yields that we can generate. I am thinking that we will need to work up a list of the higher dividend yielding stocks and begin to add them to our portfolio. This would include stocks like Verizon, Intel, Conoco, etc. The Fed action effectively raises the price of the GNMA, FNMA, and FHLMC bonds to a point where there is nothing to buy - no product available! I am working on a list of stocks, including preferred stock. This does not mean that I will not be able to find corporate bonds that meet our criteria, but it will mean that we will no longer be able to rely on the government guaranteed mortgage backed bonds for both yields and stability. It makes my job more difficult.

I will come back to you when I am ready with a recommendation, but your thinking is astute and correct.