RBC Wealth Management

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*"Yesterday, all my troubles seemed so far away.
Now it looks as though they're here to stay.
Oh, I believe in yesterday."*

— Paul McCartney, 1965

Dear Friends,

Alright. We admit it. Paul would not be pleased with a hijacking of his heart-wrenching lyrics about lost love when expressing sentiments about interest rates which have simply vanished. But yesterday, all our troubles seemed so far away. Now it looks like low rates are here to stay. Oh, do we believe in yesterday.

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As in five one-hundredths of 1%. Per annum. Street offerings for 30-day CDs hit that number last week. If you were willing to go out two years, the rate jumped all the way to two-tenths of 1%. Let's put that in dollars and cents terms. If you were a retiree and had managed to save $300,000 in your 401k over your lifetime, at two-tenths your IRA rollover would return $600 a year. Before tax. Until about 90 days ago we were able to go into the marketplace for "previously owned" short-term CDs and obtain rates at or above 2.25% for you. While this rate was not earth shaking it certainly was preferred to money market funds paying a small fraction of this rate. Then along came COVID-19. In a matter of weeks, both because of Federal Reserve policy changes and a flight to safety on the part of investors, interest rates simply collapsed.

In this environment, if we are to earn higher rates, we have to go out longer (i.e. up to three years) and down in credit quality from government insured CDs to investment grade corporate bonds. Last week we purchased bonds issued by major banks at rates a bit above 1.6%. But even those rates are skidding. The alternative is to wait it out in money market funds paying near zero.

Plan B

Do you have a mortgage? If so, could you use your low-yielding cash to pay it down or pay it off entirely? Is the absence of monthly payments virtually the same as monthly income? Yes and yes. While mortgage rates as low as 3% are not uncommon these days and do strike us as cheap long-term debt, that 3% expense doesn't seem so great when compared to the bond rates starting with the number 1. Throw into the equation the fact that for many of you, your ability to deduct interest against your income taxes vanished last year, effectively increasing the cost of carrying a mortgage. There is also a psychic benefit to eliminating what is for most of us our largest monthly expense. Your monthly statement likely carries a contact number for payoff information. If you would like to discuss the pros and cons of this alternative to owning bonds and CDs, please give us a call.

McCartney had it right… "Yesterday, love was such an easy game to play. Now I need a place to hide away. Oh, I believe in yesterday." Stay safe. Stay healthy.

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