

Retirement Weekly



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Investing for Income: satellite funds

By **Robert Powell**, MarketWatch

Some bond watchers are predicting that interest rates are on the verge of spiking upward now that the U.S. 10-Year Treasury is trading above 2% (It was trading Friday at 2.17% at the time of this writing.)

Prateek Mehrotra, the chief investment officer at Endowment Wealth Management, is not, however, in that camp. Instead, Mehrotra predicts that interest rates will rise gradually over the course of years. “The Fed has started talking about tapering (its monetary stimulus program) but it hasn’t discussed when and how,” he said.

Given the uncertainty over when and how the Federal Reserve will stop pumping money into the economy, Mehrotra has revised his approach to investing in fixed-income securities. Typically, he uses what’s called a core-and-satellite approach in which he either invests in government bonds for the core or in nontraditional fixed-income securities as the satellites.

But given what’s likely to happen to government bonds, if not over the short term, then certainly over long term, he’s now investing in the satellites rather than the core. “We want to make sure we are in the right sectors in fixed income,” he said, also noting that he would rather take credit risk than duration risk at the moment.

In general, he’s fond of investing in ETFs that invest in floating-rate securities, emerging market debt and high-yield securities.

Some names to consider:

PowerShares Senior Loan Portfolio (NAR:BKLN) . This fund seeks investment results that correspond generally to the price and yield of an index called the S&P/LSTA U.S. Leveraged Loan 100 Index. The fund normally invests at least 80% of its total assets in bank loans and presently has a yield of 4.89%.

iShares Floating Rate Note Fund (NAR:FLOT) . This fund, which has dividend yield of 1.09%, seeks investment results that correspond generally to the price and yield performance, before fees and expenses, of the Barclays Capital US Floating Rate Note < 5 Years Index. The underlying index measures the performance of U.S. dollar-dominated, investment-grade floating rate notes. Mehrotra said the yield is not attractive at the moment, but it will get reset as interest rates rise.

iShares Emerging Markets Local Currency Bond Fund (NAR:LEMB) . The fund seeks investment results that correspond generally to the price and

yield performance, before fees and expenses, of the Barclays Capital Emerging Markets Broad Local Currency Bond Index. The yield is now 3.25%

iShares Global ex USD High Yield Corporate Bond Fund (BTT:HYXU) . This fund, which has a yield of 4.26, seeks investment results that correspond generally to the price and yield performance, before fees and expenses of the Markit iBoxx Global Developed Markets ex-US High Yield Index.

SPDR Barclays Short Term High Yield Bond ETF (NAR:SJNK) . This fund, which has a yield of 5.38%, seeks to provide investment results that, before fees and expenses, correspond generally to the price and yield performance of the Barclays US High Yield 350mn Cash Pay 0-5 Yr 2% Capped Index.

Over the transom

There are those who say it's too late to invest in high-yield bonds. That demand for income has pushed up prices and driven down yields to record lows and that investing in such bonds is not worth the additional risk. But a new white paper from TIAA-CREF, "The enduring case for high-yield bonds," shows that a long-term allocation to high yield bonds can provide attractive risk-adjusted returns and enhanced diversification. According to author of the paper, Kevin Lorenz, CFA, portfolio manager of the TIAA-CREF High Yield Strategy, high yield bonds offer higher income that drives long-term returns, despite price fluctuations; lower sensitivity to interest-rate increases than Treasuries and high-grade bonds; and low correlations to help manage fixed-income portfolio risk. Watch Lorenz discuss the benefits of investing in high yield bonds here.

Robert Powell is editor of Retirement Weekly, published by MarketWatch. [Follow his tweets at RJPIII](#). Got questions about retirement? Get answers. Email rpowell@marketwatch.com.

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