Unbiased Financial Information Provided by Financial Wisdom.

Building a Ladder of Saving Certificates

Choosing the length of savings certificates is an important decision. The issues of liquidity and the future direction of interest rates can make the decision difficult. Longer maturity certificates usually provide the highest returns, but they also tie up your funds longer. Shorter maturities provide flexibility to take advantage of rising rates, but usually with lower returns. Ideally, you would want the highest current return coupled with the ability to invest at higher rates if interest rates rose.

Creating a "ladder" of maturities is a way to create a "portfolio" of certificates that will put you in a position to earn good rates and invest at higher rates if interest rates rise. Simply stated, with this strategy, you divide your funds into pieces and buy equal amounts of different maturity certificates. Here is an example:

Let us assume you have $25,000 and want to buy certificates with maturities up to five years. The rates on certificates are:

Maturity	Rate
1 year	1.05%
2 year	1.15%
3 year	1.30%
4 year	1.60%
5 year	2.15%

By making initial purchases of $5000 each of the different maturities, your average rate would be about 1.45%. Each year, as a certificate matures, you would use the proceeds to buy a 5-year certificate. That way, as time went on, more and more of your funds would be earning the highest rate and you would still have annual liquidity. If rates rise, you have liquidity to buy higher yielding certificates. If rates fall, you are still earning high rates on your existing positions.

No one can accurately predict the future of interest rates. Using this "Ladder of Maturities" strategy can help position you to benefit regardless of the direction of interest rate changes.