June 2, 2011 - Many people depend on certificates of deposit (CDs) to provide extra income. Yet CD rates have been fairly low for a while. In recent months, in fact, one-year CDs were paying about 0.5%, two-year CDs topped out at around 1%, and five-year CDs paid in the 2% to 2. 3% range. Those rates are scanty enough, but they can seem even lower in an economic environment marked by rising food and gas prices.

Before you consider alternatives, keep in mind that CDs still offer a key advantage:safety of principal. The Federal Deposit Insurance Corporation (FDIC) typically insures CDs up to $250,000. And since CDs are relatively short-term in nature, you don't have to worry about locking away that money for long periods of time. So there can be a place for CDs in the fixed-income portion of your portfolio.

However, during times such as these, you might consider looking at additional options, keeping in mind that, when seeking greater income, you'll likely be taking on more risk. Let's consider a few alternatives:

Fixed annuities -- Many people buy fixed annuities to supplement their retirement income. But most annuities also allow you to take up to 10% of your account value each year without penalty. Plus, the interest rate you receive on a fixed annuity may be more competitive than that currently paid by a CD. Keep in mind, though, that annuities are not backed by FDIC insurance, and any guarantees are backed solely by the paying ability of the insurance company. Additionally, early or excessive withdrawals may be subject to penalties. If you believe a fixed annuity might be appropriate for your situation, speak with your financial advisor.

Bond ladders -- If appropriate for your situation, you can potentially gain extra income through a strategy known as a bond "ladder." To build a ladder, you buy several bonds with varying maturities -- short-, intermediate- and long-term. Once you've constructed your ladder, you could gain some advantage in various interest rate environments. When market rates are low, you'll still have your longer-term bonds earning higher interest rates. And when market rates rise, you can reinvest your maturing short-term bonds at the higher rates. But if you need income in addition to your regular interest payments, you can get it from the maturing bonds. Unlike CDs, however, bonds are not covered by FDIC insurance and are subject to credit risks. Bonds are also subject to interest rate risk: When interest rates rise, bond prices generally fall, and you may lose some or all of your principal if you sell your bond prior to maturity. But by holding your bonds until maturity, you can avoid loss of principal, assuming the issuer doesn't default.

Dividend-paying stocks -- Some companies have paid -- and increased -- their stock dividends for many years now. If you don't need the dividends to boost your cash flow, you can reinvest them to help boost your ownership stake. However, companies can reduce or discontinue their dividends at any time, and since stock prices fluctuate, you risk losing some or all of your principal.

By exploring alternatives to short-term CDs, you may find other appropriate investments that may better position you to reach your financial goals -- so look around to see what's available in the financial marketplace.

This article was written by Edward Jones for use by your local Edward Jones Financial Advisor.