

Yield from GNMA's isn't all it's cracked up to be

Recently I had a very pleasant, but intense, argument with my client, C.B., over the true yield he is receiving on his GNMA investment. C.B. argued, quite correctly, that he receives 12 percent from his GNMA fund even though in today's market of 9 percent would appear to be quite attractive. In this article I will demonstrate the problem of calculating the true yield from a GNMA fund.

Income	Year ended 12-31-1988	\$1.90	\$1.72 - 11.4%
Expenses		(\$0.20)	\$15.15
Not Income		\$1.70	ending NAV + distributions - 12-month performance
Distributions		(1.72)	beginning NAV
Not realized and unrealized gain (loss) on investments		(0.77)	15.15 + 1.72 = 5.8%
		(0.79)	15.94

NAV beginning of period \$15.94
NAV end of period \$15.15

Note that the fund paid more in dividends (\$1.72) than what was available after expenses (\$1.70). The key to this puzzle is in the loss of investments.

The explanation lies in the fact that this fund had included in the portfolio high-coupon mortgages by buying them for more than face value. High coupons allow the fund to make large distributions, which increase the yield.

When the mortgages backing the GNMA are paid off due to refinancing or people moving, the holder receives the portfolio of the mortgage's principal assigned to the certificate. Unable to reinvest this money at a high rate, the fund loses part of the premium it paid to high coupon payments.

The investor may have thought that he or she received large dividend payments, and certainly paid tax on them, but the true yield was much less than the perceived yield.

Let us now compare yield and performance for ABC GNMA fund for the year ending Dec. 31, 1988:

Distributions - yield
final NAV

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STANDARD YIELD: Calculation of the standard yield in the case of a no-load fund is relatively easy. Divide the previous 12 month's dividends by the net asset value (NAV). Then study the average maturity and the quality of the portfolio.

These two independent variables will have an effect on yield, with the old truism, "high risk equals high return," still applicable.

The next step is a bit more complicated. Compare the yield to the latest 12-month performance.

The latest 12-month performance is the total return of the fund, which equals the sum of the dividends and the capital gains during that period added to the recent NAV, divided by the NAV a year ago. The 12-month performance figure should be greater than the yield.

THE GNMA YIELD: The GNMA yield calculation is more complicated. Assume the ABC GNMA fund shows a 12-month yield of 10.3 percent and a total return of 8.1 percent. Here is how the NAV calculation is done:

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Thursday, May 18 - "Reducing the Cost of Claims Administrations" discussed at meeting of Construction Financial Management Association in Detroit. Information: 491-2500.

ACCOUNTANTS ASSOCIATION

Thursday, May 18 - National Association of Accountants meets in Bloomfield Hills. Information: 652-8797.

FINANCES FOR THE SURVIVOR

Thursday, May 18 - "Taking Care of Finances When You Are Alone" presented 10:30 a.m. to 7 p.m. in Farmington Hills. Free. Information: 851-7222. Sponsor: Empire of America.

RETIREMENT PLANNING

Thursday, May 18 - "Retirement Planning After Tax Reform" begins at 7:30 p.m. in Bloomfield Hills. Information: Emily, 652-3200 or 1-800-772-8225.

TAX-FREE EXCHANGES

Friday, May 19 - "How You Can Profit From Tax-Free Exchanges" offered 8:30 a.m. to noon in Southfield. Fee: \$75. Information: 646-7701. Sponsor: The Dietz Organization.

CPA WEEKEND

Friday-Sunday, May 19-21 - Certified Public Accountant Weekend offering up to 58 continuing professional education credits. Registration fee: \$25. Information: 370-3120. Sponsor: Oakland University.

INVESTING FOR RETIREMENT

Monday, May 22 - "Financial

Survival in Retirement" offered 7:30-9:30 p.m. in Birmingham. Fee: \$12. Information: 644-5832. Sponsor: The Community House.

REAL ESTATE LICENSE

Monday, May 22, through Thursday, June 22 - Prelicense training course for real estate sales people offered in Farmington Hills. Information: 655-2222 or 1-800-372-2597. Sponsor: Century 21 of Michigan Inc.

Information for this column should be sent to the business editor, Observer & Eccentric Newspapers, 36251 Schoolcraft, Livonia 48150. Information must be received by Monday to be published in the Thursday issue. Publication cannot be guaranteed. Information should contain a daytime telephone number where information can be verified.



Michigan Bone and Joint and Rehabilitation Institute is pleased to announce it has moved to the new Beaumont Medical Building, West Bloomfield, 6900 Orchard Lake Road, Suite 103 (313) 855-7400

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