Yield Alert: This Rock Solid ETF Pays 9.3%

Description

As current interest rates march ever-closer to zero, many retirees are forced to respond by reaching for yield. They put their cash to work in risky securities, enticed by what they view as succulent dividends.

You can probably guess what happens next. Some piece of bad economic news hits — like a COVID-19 pandemic — and many of these precarious stocks are forced to cut their dividends. The share price often tumbles at the same time, creating the kind of double whammy no income investor wants to see.

There are, however, a few interesting high yield securities out there — stocks that look poised to pay excessively high dividends for years to come. Let's take a closer look at one, an ETF that offers a very compelling 9.3% yield.

Covered calls

The ETF we'll look at today is the **BMO Canadian High Dividend Covered Call ETF** (TSX:ZWC). This ETF uses a covered call strategy to generate a solid income stream.

Here's how it works. First, the fund holds a diversified basket of solid dividend stocks, blue chips that make up the core of every good income portfolio. The next step is to sell call options on these stocks, a move that generates income immediately.

The only downside to the strategy is that it limits upside potential, since it creates an obligation to sell the underlying stock at a certain price on a certain date.

Investors can easily use their own covered call strategy to generate some eye-popping yields, especially in today's volatile environment. But there are downsides to doing it that way. It's an active trading strategy, something many part-time investors don't have time to do. And if you're doing it in a taxable account, the paperwork can be annoying.

Many investors therefore turn to a covered call ETF to get themselves exposure to the nice income the strategy generates. Generally, there are two types of covered call funds. One kind uses leverage to really goose yields, while the other takes a more sustainable strategy. The BMO Covered Call ETF uses the second strategy, which is good news for investors looking for a more stable yield.

There are a few downsides to this fund, however. On a capital gains basis, it will likely lag the market going forward. That's because a covered call strategy intentionally gives up capital gains potential in exchange for more income and charges a 0.65% management fee, which many investors think is too high.

A great income source

Although this ETF has only been around since 2017, it has already cemented itself as a solid income source for investors looking for a little extra yield.

The fund pays investors distributions each and every month, with the payout starting at $0.10 per share each month. It has since been hiked; it now pays $0.11 per month.

Not surprisingly, the fund has sold off of late, although it has performed better than the overall market. That has pushed the yield up to 9.3%. That's an excellent payout, and it should be safe. After all, the fund was able to pay a similar distribution before all the volatility hit the market. It should be able to do so again.

The bottom line on this interesting yield ETF

The BMO Canadian High Dividend Covered Call ETF is a solid choice for the yield it provides, but there's more to it than just that. It also gives investors exposure to an asset class they wouldn't normally own, offering downside protection just in case the market tanks once again.

The time to buy an ETF like this one is today, before the market recovers. It's a great time to lock in a solid yield with some upside potential. That's a great combination.

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