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What’s the best place to stash your savings?

With interest rates near zero, you have to weigh risk and return

By Todd Wallack, Globe Staff | August 2, 2009

Just as Americans are saving more money, interest rates on traditional savings vehicles have hit rock bottom.

For example, the US government is currently paying zero percent on a type of savings bond indexed to inflation. That’s not a typo: zero percent.

Bank of America, the largest bank in Massachusetts, is paying just 0.10 percent a year on its most popular savings account. That means you’d earn a dime for every $100 you deposit - before taxes. And money markets, certificates of deposit, and treasuries are offering only slightly better returns. Most short-term places to stash your cash are now paying well below 1 percent.

“We are extremely close to record lows,’’ said Greg McBride, senior financial analyst with Bankrate.com, a personal finance website.

Several factors are driving down rates.

In an effort to stimulate the economy by making it easier to borrow money, the Federal Reserve has slashed the interest rates it controls to nearly zero.

Meanwhile many investors are skittish after last year’s stock market collapse, so they are flocking to safe investments like US Treasury bonds. The higher demand has pushed down the rates lenders have to pay on these investments.

With such infinitesimal rates, you might be tempted to brave the stock market in the hope of higher returns. But think twice. Your savings are supposed to be handy for a reason: to cover unexpected household expenses or illness, or for a specific goal such as college tuition or a down payment on a home - places where you can’t afford to lose money.

“You don’t put emergency savings somewhere because of the fabulous returns,’’ McBride said. “You put money in liquid investments because you are unable to take investment risk.’’

So here’s the latest on the savings options most financial advisers recommend:

Bank savings accounts. The best reason to stick with a savings account is your money is insured, even if your credit union or bank fails - no longer a hypothetical concern after scores of institutions have shut down over the past year. Your money is also available at any time. But earning anything more than a pittance for an interest rate will require shopping around, with online accounts generally offering the higher rates. Beverly National Bank's online division is offering 1.75 percent.

Bankrate.com has a comparison tool, MoneyAisle.com lets you "auction'' off your business to the bank willing to pay the highest rate. One caveat: Banks can reduce their rates at any time, and some have minimum deposits or fees, so read the fine print.

Money market bank accounts. Many banks offer money market accounts that pay slightly higher interest rates than standard savings accounts, but typically include a higher minimum balance. For instance, Bank of America is now offering 0.85 percent interest or more, but you'll be hit with a $10 monthly fee if your balance falls below $5,000. Like savings accounts, though, your money is insured.

Certificates of deposit. Again, CDs offer a safe insured haven for your money. But in exchange for a better interest rate, you typically have to agree to lock your money up for a period, say six months or a year. On average, one-year CDs are paying just over 1 percent, triple the average for savings accounts and money market accounts. But many banks, including Ally Bank, are offering double that. Longer term CD rates aren't much better - with five-year deposits paying in the 3 percent range.

US bonds. Another option if you're willing to lock up your money for a short period are savings bonds. EE Savings Bonds are currently paying 0.70 percent interest. And I-Savings pay a combination of a fixed rate and another rate tied to inflation. Interest on both is exempt from local and state taxes. But inflation is so low that new I-Savings are paying zero interest through at least Oct. 31.

Other caveats: You are required to hold savings bonds for at least a year. And you forfeit three months interest if you sell the bonds in less than five years. Learn more at treasurydirect.gov. You can also buy short-term treasury bills through the government or a broker, but the interest rates are currently very low. For instance, 26-week bills are currently yielding only 0.28 percent interest.

Money market mutual funds. Unlike bank accounts, your money isn't insured. But money market funds generally invest in US treasuries and other relatively safe, short-term investments, so it's very rare to lose money. And you can cash out any time, making it a convenient place to park cash. But the interest rates are currently meager, even compared with bank accounts. The average taxable fund is paying 0.09 percent interest, while the average tax-free fund paid 0.13 percent, according to iMoneyNet, a website that tracks money market funds.

Short-term bond funds. If you're willing to accept more risk, you might consider investing in short-term bond funds. Over the past year, the average short-term bond fund has generated a return of nearly 2.92 percent, better than the returns for bank accounts and CDs, according to

Morningstar Inc. You can also sell anytime. But these are investment accounts, not savings accounts. That means fund prices can fluctuate, and you can lose money.

“You need to be very careful and do your research or work with a financial adviser’’ before picking a fund, said Ted Yoos, president of Cornerstone Financial Management LLC in Burlington. “You need to stay away from the riskier funds.’’ And if you need a guarantee you won’t lose any of your savings, Yoos says you’re better off parking your money in savings account or other option.

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