Interest rates are on the rise, and that's bad news for investors in high-quality bonds.

Spooked by signals that the Fed may be preparing to end the intervention that has kept interest rates low, bond investors in June started selling in droves. Yields on 10-year Treasury notes soared to their highest levels in almost two years as sellers drove down prices.

Bond prices have stabilized some what—for now—as investors start to realize they might have overreacted. Still, conservative bond investors, whose money is in things like Treasuries and high-grade corporate paper, absorbed hits of 5%-7% or more in the span of a few weeks. That kind of volatility is going to keep such investors awake at night unless they make some adjustments.

The good news is that several types of investments are available to help you to fight rising rates. Residential mortgage-backed securities (RMBS), high-yield bonds and dividend-paying stocks are three areas where we see opportunity.

RMBS: Discounted non-agency residential mortgage-backed securities have been a good fit for several of our clients. These bonds are usually backed by loans issued to good-credit borrowers—mostly in California, Florida, and New York—that for technical reasons did not qualify to be in a Freddie Mac or Fannie Mae portfolio.

The securities are backed by homeowners and physical homes, and generally have performed well as home prices have risen. But because non-agency RMBS are not held as widely in bank and insurance portfolios, demand for them is lighter than when they were originally issued. That creates an opportunity to buy these securities at a discount—which creates potential yields of 6% to 7% based on their 12 month trailing numbers.*

In my opinion non-agencies RMBS will remain a safe haven as long as interest rates do not rise dramatically, which would cause property values to drop. Provided that rates stay reasonable by historical standards, increasing home prices will serve to offset rising rates.

One caveat is that RMBS involve liquidity risk in times of falling home prices. If housing prices plunge, it would be very difficult to sell a large position. But right now, based on the positive direction of the housing market, it looks unlikely that the liquidity factor will come into play for the foreseeable future. And if income and cash flow is an investor's main objective, non-agency RMBS fit the bill.

High-Yield Bonds. High-yield bonds can be another effective way to fight rising rates. Specifically, we're looking for the bonds of companies that are successfully cleaning up their balance sheets and have good prospects of improving their credit rating.

Advanced Micro Devices fit this mold. The chip-maker's debt had been downgraded as it struggled to find customers. But it's successfully pivoting to the video game console market, and with its fundamentals looking better and better, a credit rating upgrade appears to be in AMD's future. In the meantime, the company's bonds can yield more than 8%.

Dividend stocks. We have been increasing our exposure to stocks with a history of increasing their dividend. A great example is Kellogg Company, which has a long history of raising its payout year after year. Rising interest rates can drive down the price of dividend stocks that can't or won't increase their dividend. But with companies like Kellogg, dividend increases typically help sustain the stock's price.

Corporate bonds, by comparison, can't increase their interest rates—and that's why they get hammered when 10-year Treasury rates rise. Investors in rising-dividend companies have the opportunity to not only get more stable prices but to get an increasing stream of income as well.

The bottom line: June's interest-rate spike is probably a sign of things to come. The good news is that you can reposition your investments to gain yield and decrease interest-rate risk. If you'd like to discuss this topic further, don't hesitate to get in touch with us.

*based on the past 12 months' prepayment, default and liquidation values of the properties underlying the mortgages.