

Managing Cash as a Strategic Asset

Implications and Solutions

Cash, having reached unprecedented levels in companies around the world, has been cast in a new light. Once considered a consequence of business activities, cash has evolved into a strategic asset—valued as a hedge against market volatility and amassed to stay nimble in a world of business opportunities.

This sea change in how cash assets are viewed and treated has implications for corporate treasurers, who are looking to minimize risks, optimize returns and make the most of their valuable time.

Cash's Emergence as a Strategic Asset

"The historical market perception was that holding cash would erode shareholder value and so cash should be quickly deployed," says Tom Schickler, senior vice president, who heads liquidity and investment products in Asia Pacific for JPMorgan Chase's Treasury & Securities Services business. "That's not necessarily the case today." Companies are holding more cash than ever before. For example, corporate sector profitability and expenditure patterns have led to high levels of corporate liquidity—\$400 billion to \$500 billion for the G4 nations (Brazil, Germany, India and Japan).

The build-up of cash can be attributed to a number of factors ranging from geopolitical instability, to a preference for expansion via acquisition rather than organic growth, to unprecedented profit levels, to expansion in developed and emerging markets. Schickler points out that all throughout the recent cycles in monetary policy and capital market conditions, companies have consistently expanded their cash holdings. He says, "This suggests a fundamental shift in how companies view cash—as an asset class in its own right."

The Implications

Managing cash as a strategic asset has implications for corporations and their treasurers:

Heightened attention to risk management

While treasurers are looking to get the most yield from cash, risk management is also a key priority. Recent events in the global capital markets have led to a wholesale reassessment

of risk, and emphasized the importance of synchronizing the credit and liquidity components embedded in investment alternatives with the needs and risk tolerance of the corporation. In times of increased complexity and volatility, full transparency is critical. "Market events are driving companies to place increased emphasis on managing their investment mandates," says Schickler. "Companies are seeking external assistance to create greater visibility in the cash investment process."

Increased focus on understanding cash returns

"We're seeing a greater focus on total economic return, which incorporates the total costs associated with managing the investment risk and executing the investment, and is a better means of evaluating yield than focusing solely on absolute rate of return," says Schickler. "For instance, if I had to call nine banks to get 5%, and I factor in my time and the transaction costs for booking, confirming and settling the trade, I'm most likely getting less than 5%."

Changes in working capital management to better delineate cash components

To enhance the return on the overall cash portfolio, corporate treasurers are seeing more of a need to break down the portfolio into different types of cash: frictional cash, the least predictable, to meet daily needs; reserve cash, providing a liquidity cushion; and strategic cash, for discretionary use. "The ability to predict the size and duration of the cash components enables a company to select and make use of the appropriate types of investment vehicles. Greater insight into the cash components provides true pricing power," says Schickler. "A failure to sufficiently delineate cash components can significantly deteriorate total returns."

Emphasis on aligning the corporate structure and cash operating model

To some extent, cash is influencing treasury structures. To improve cash dynamics, tax position and other considerations, companies are analyzing the benefits of centralizing treasury functions or making global treasury the beneficial owner of a greater percentage of cash holdings. "Many of the corporate structural changes that we see today," comments Schickler, "are because treasury

requires greater visibility and control over cash.” He points out that restructuring to optimize liquidity may necessitate that local operations break away from legacy structures. “For those who choose to undertake a shift in the internal corporate culture to achieve cash and liquidity management objectives,” he says, “the challenges can be great. But so can the rewards.”

A shift from tactical to strategic management of cash

The sheer volume of cash and increasing complexity of investments has created a dilemma for corporate treasurers. Should they focus on day-to-day monitoring and execution of cash

investments or overall strategies for investing? Many are looking for a better balance between the tactical and strategic. Notes Schickler, “When it comes to cash investing, treasurers are recognizing that they can add more value by intensifying their focus on strategic priorities, rather than spending time getting bids, booking and settling trades.”

Solutions for Managing Cash Strategically

Faced with these implications, many corporate treasurers are engaging their banking partners to manage their cash portfolios in a more programmatic way. At the heart of any program of this type is cash consolidation. By linking all sources of cash for purposes of aggregation, clients gain visibility and control. Whether through physical cash concentration or notional pooling, companies can not only offset short and long positions, but also maximize the amount for investing. For instance, says Schickler, “Consolidating balances from multiple entities into a single position may enable a company to meet the minimum for a higher-yielding share class in a money market fund.”

To achieve an optimal return on the overall portfolio, companies should select a banking partner with access to a full array of investment options that can be matched to different cash components. “For frictional cash,” says Schickler, “you want short-term, overnight investments that give you quick access to cash, such as interest-bearing accounts and money market funds. For reserve cash, you can go a little further out on

the curve with time deposits, enhanced yield funds and fixed-income instruments. And for strategic cash, you’re looking at a bit of a longer time horizon, with fixed-income securities and separately managed accounts.”

Given the heightened turbulence in the market, adds Schickler, “a bank must be able to offer a multi-dimensional approach to managing investments that enables an optimal balance between risk and return in sync with both the risk tolerance of the client and shifting market dynamics.”

Through automated sweeps and other

capabilities, a banking partner can help clients gain efficiencies in the investment process, “and free their minds of concerns over whether investments are being made according to the mandate,” says Schickler.

“Recently, we have worked with clients to establish parameters for cash investments based on their needs, and have taken on the repetitive tasks of the day-to-day investment process,” says Schickler. There is no discretion on the bank’s part in choosing the investments. The client pre-selects all instruments and sets the rules. “We simply provide the investment options, market access, execution

capability and visibility over what has been executed,” notes Schickler.



Tom Schickler, senior vice president, liquidity and investment products - Asia Pacific, JPMorgan Chase Treasury & Securities Services

A New Discussion Between Banks and Clients

Schickler emphasizes that the best investment solutions are not provided on a commoditized basis, but rather result from a discussion of the client’s objectives, priorities and concerns. Instead of centering a discussion on multi-currency cross-border sweeps, for instance, a more productive conversation would zero in on the forces that led to the need for such a product.

He concludes, “Just as corporations and treasurers are changing the way they view and treat cash, so banks and their corporate clients can change their engagement model. We will have more success optimizing liquidity and the investment process if we shift the orientation from ‘buying/selling services’ to ‘creating solutions.’” ■