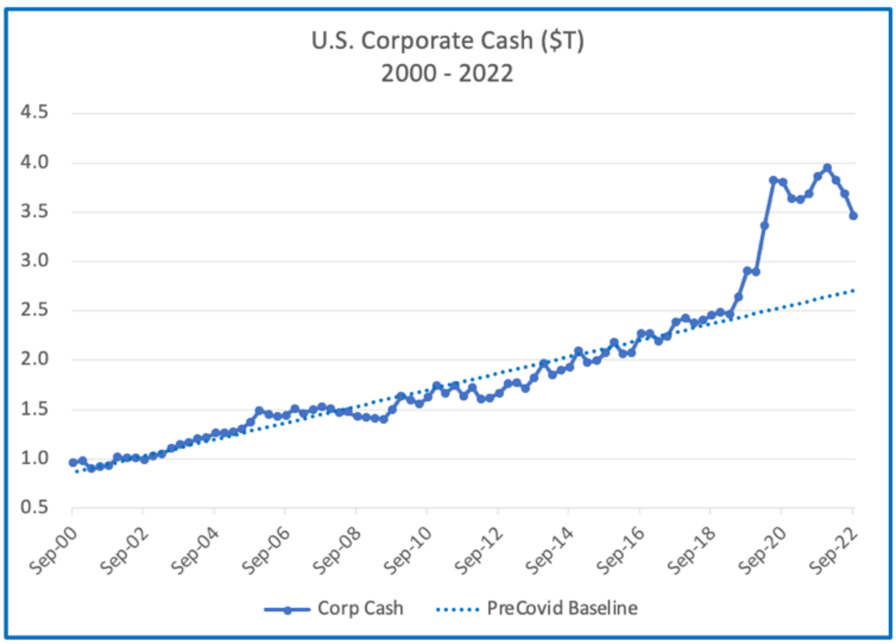
The Carfang Group

U.S. Corporate Cash Decline Continues

Now at $3.46 Trillion
Down $488 Billion YTD

December 12, 2022. Corporations are rapidly reducing the huge cash reserves accumulated during the Covid pandemic according to The Carfang Group's analysis of the Federal Reserve's Quarterly Flow of Funds report just released. At $3.46 trillion, U.S. corporate cash levels have now retraced 46% of their pandemic related surge.

According to Anthony J. Carfang, Managing Director at The Carfang Group, "Corporate cash fell by $225 billion during the third quarter and $488 billion from the post-pandemic high set at year end 2021. Companies still harbor concerns about the economy, interest rates and inflation. Treasurers are very worried about the hidden risks of quantitative tightening following the unprecedented decade-long monetary expansion that is now being reversed."



Source: Federal Reserve, The Carfang Group

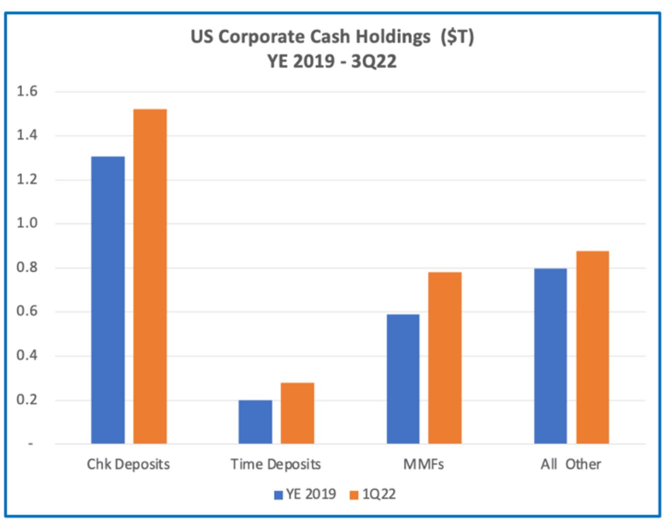
After more than doubling its assets from $4.1T to $8.9T in 2020-21, the Fed is now reducing its massive balance sheet. The quantitative tightening phase has begun, leading to reduced money supply and bank deposits. Since GDP = Money Supply times Velocity, there is a very real threat of recession. *We believe corporate treasurers, after reducing some of their excess cash, are still holding on to above average levels of cash as a precaution against this economic and policy uncertainty.*

Corporate cash declined to 13.5% of US nominal GDP in the quarter, still above the long-term trendline. During the pandemic, cash soared to 20% of GDP but that percentage has since declined by a third. In part, that is because real GDP rebounded, and inflation emerged.

There had been a decades long upward trend in cash as a share of GDP, so the current reversion back toward the trendline is welcome. However, these levels are still unprecedented, and the long-term effects remain to be seen. Since cash is a stranded asset, these levels could become an economic drag.

Source: Federal Reserve, The Carfang Group

Corporate cash allocations have shifted significantly during the pandemic. While corporate investments into all instruments categories increased, the magnitude varied. For example, domestic checkable deposits and cash soared by $580B through 2021 but have fallen by $366B so far this year. On the other hand, corporate holdings of money market funds and time deposits remain close to their recent highs. It will be useful to monitor this trend as rates rise.



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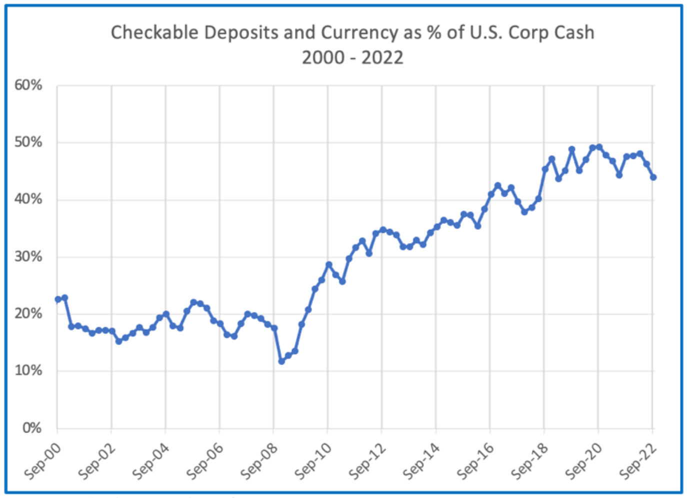
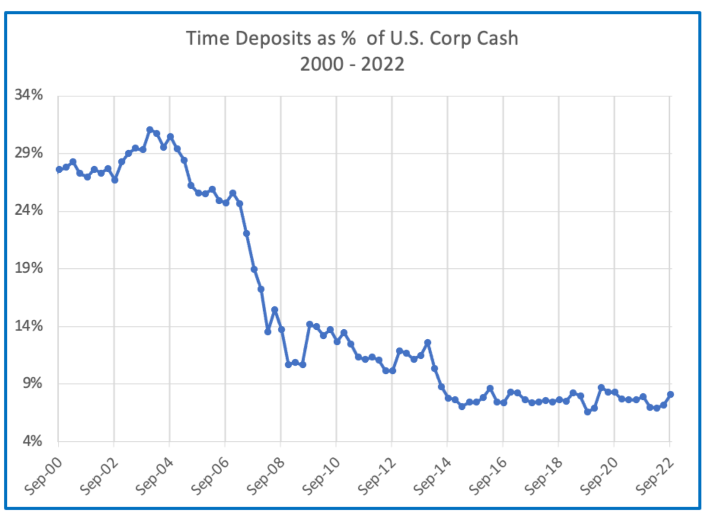
Checkable deposits and currency are 10% below their all-time highs, now at 44% of corporate cash. The percentage had been stable at 20% for more than ten years but began a long upward trend following the 2008 financial crisis as the Fed expanded the money supply and interest rates remained near zero. Now that rates are rising, it will be interesting to see how rate sensitive those deposits will be.



Source: Federal Reserve, The Carfang Group

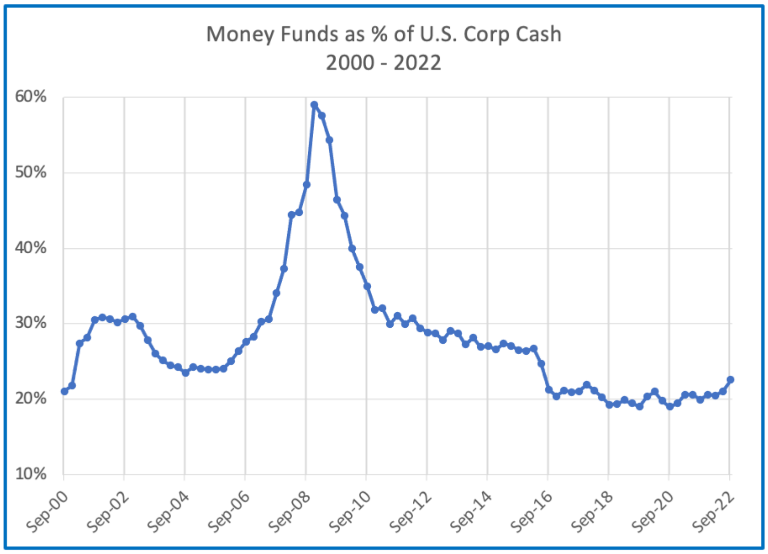
Time deposits now account for 8.1% of corporate cash, very near the all-time low set in 2019. However, they have increased for three consecutive quarters.

Between 1990 and 2010, these deposits ranged between 15% to 30% of corporate cash. During the quantitative easing of the past dozen years, its share fell to a low of 6.6% from which there has now been a small rebound. The inverse relationship between time and checkable deposits suggests that time deposits may be poised to increase now that rates are rising, and quantitative tightening has begun.



Source: Federal Reserve, The Carfang Group

Money Market Funds may be regaining prominence. Assets are back to 22.6% of corporate cash, a level last seen in 2016. Assets, however, are still well below the peak 59% level of December 2008.



Source: Federal Reserve, The Carfang Group

Commercial & Industrial Loans are an important source of corporate liquidity. Many companies actively drew down credit lines to further build their liquidity buffers during 2020. Then, they seemed to be trimming a bit in early 2021. However, C&I loans are now trending back up at $2.75T, a YTD increase of 10%.

In conclusion, current liquidity markets represent a challenge for both treasurers and bankers. The Fed has become such a dominant player that traditionally reliable market signals are both distorted and muted. Inflation, rising short term rates and the beginning of the Fed's balance sheet reduction are just a few of the wild cards. Treasurers are remaining very cautious.

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