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SHOW ME THE MONEY

Is cash still king?

The sudden market rebound took many funds by surprise, many were caught out holding large sums of cash

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AT AN interview with **Yeo Seng Chong of Yeoman Capital** a month back, he alerted me to a Bloomberg article that I had missed. The article was filed on Dec 29, 2008 - a long time given the speed of change in the markets nowadays. But I think much of the data and the premise of the article still stands.

The article said that there was US$8.85 trillion in cash, bank deposits and money-market funds in the US - equal to 74 per cent of the market value of US companies. The ratio was the highest since 1990, according to Federal Reserve data compiled by Leuthold Group and Bloomberg.

The ratio of cash on hand to US market capitalisation jumped 86 per cent in the first 11 months of 2008 - the biggest increase since the Fed began keeping records in 1959. The so-called money of zero maturity, the central bank's measure of US assets available for immediate spending, is mostly held by households, according to Richard G Anderson, an economist at the Federal Reserve Bank of St Louis.

The data showed that the eight previous times that cash peaked compared with the market's capitalisation, the S&P 500 rose an average 24 per cent in six months.

Cash holding peaked one month before equities began to recover during the two longest recessions since World War II. In July 1982, money of zero maturity as a percentage of the US stock market's value rose to 95 per cent. That marked the end of a 20-month bear market, and the S&P 500 began a six-month, 36 per cent advance, data compiled by Bloomberg showed.

In September 1974, cash on hand reached US$604.5 billion - a record 1.21 times US stock capitalisation. What followed was a 31 per cent gain in equities between October 1974 and March 1975.

Of course, those who acted immediately upon seeing the report and deployed their cash into the market at end-December last year might not have done that great since. Between Jan 1, 2009 and March 9, 2009, stock prices slumped by a significant 27 per cent. But then, things suddenly turned around on March 10. And since then, the markets have advanced by some 24 per cent. Year to date, however, the S&P 500 is still down by about 4 per cent and the Dow Jones Industrial Index, about 7.4 per cent.

Still, the very sudden and sharp rebound had caught many funds by surprise - many, as the numbers presented earlier showed, were caught out holding large amounts of cash. But as the rally is looking more and more like a sustainable one, many are scrambling to get back into the market.

State Street, which tracks buying and selling within the US$12 trillion of assets it holds as custodian, said this week that flows into US equities were close to the highest they have been in 12 years.

So as the recent experience shows, a two-decade high in cash to market value ratio at 74 per cent is still not an outright signal to use up one's bullets at one go. One will not know for sure when the ratio will peak. In the case of 1974, cash levels reached 1.21 times US stock capitalisation. But it is definitely a good indicator to gradually deploy one's cash.

So how about Singapore? How much cash do we have now in our banks, and how does it compare to the combined market value of all the stocks listed on Singapore Exchange?

According to the latest issue of the Monthly Digest of Statistics Singapore, deposits of non-bank customers with domestic banking units totalled $355 billion as at end February this year. That amounted to a whopping 97 per cent of the combined market value of all SGX stocks. Add in deposits with finance companies, and the ratio rises to 99 per cent.

The previous peak was in 2002, when total bank deposits to stock market cap ratio stood at 87 per cent. Add in finance companies' share of deposits, and the ratio increases to 91 per cent. We all know that the market bottomed in 2003, and the bull rampaged for a good five years. During that period, the bank deposit to stock market cap ratio slowly declined and hit a low of 39 per cent in 2007. That's lower than the 60 per cent registered in 1997. Again 2007, as we all know now, was the peak of the market.

The market rebound in March this year lifted the total SGX market cap, and hence reduced the ratio of cash to the market value of stocks. Still, it is a high 92 per cent. **As Mr Yeo put it: 'This amount of cash at a time with very low yield both in terms of Treasuries and bank deposits suggests that the motivation for taking risk-bearing investments, which equity investment is, should be very high. But the only thing that is holding it in check is sentiment. But as you know, sentiment is something non-numeric. And sentiment, like fashion, changes at the flick of a switch. So I won't want to be holding large amounts of cash when these people deploy this vast amount of cash back into equities.'**

Indeed.

In Singapore, in fact, the amount available for investments is far bigger than just deposits in the banks and finance companies. A huge chunk of our cash is also in the Central Provident Fund (CPF). According to the statistics digest, there was $154.7 billion in CPF due to members as at end-February 2009. Combined with bank deposits, the ratio of investable funds over Singapore's stock value is about 1.4 times!

So just how big is our cash hoard? Deposits and CPF combined, it's two times the country's gross domestic product (GDP) last year. So arguably, even if the whole economy were to shut down, there is still enough cash reserve for the country to survive for two years.

Meanwhile, the reduced holdings in domestic equities also shows up in the composition of banks' assets. From the third chart, you can see that as at February this year, domestic equities made up just under 1.2 per cent of banks' total assets. That's down from more than 1.8 per cent in 2005 and in 1997.

Of course, Singapore is a very open economy. Its cash can be invested anywhere in the world, not necessarily just in the Singapore market. Still, the last eight years' data of cash to market value ratios has shown that it is a good indicator of value in the market.

And as things stand today, it appears that there is still time for one to slowly deploy one's cash.

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