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3 Questions: Cash is an asset class again

Liquidity products offer access, stability and, now, return.

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"3 Questions" delves into the investment approach used by Federated Investors strategists. This installment features Debbie Cunningham, chief investment officer, Global Money Markets.

1. **Why should investors think of liquidity as an asset class?** One word: yield. Cash is no longer just a place to store operating funds until something better shows up or to pay bills and expenses. It's again an important part of a strategic allocation of investor assets. In 2018, government, tax-free and prime money market fund categories all had positive returns, while the lion's share of the investment world fared ... well ... you know. But this is not about liquidity versus equities/fixed-income/etc.; it's about how cash can now be a productive part of a diversified portfolio. Many prime money funds currently earn more than inflation, and government and muni funds are not far behind, and they all bring a stable counterbalance to risk assets and even bonds.

2. **How is liquidity performing in the current volatile market environment?** Quite well. Liquidity is generally a flight-to-quality asset class, and the turbulence of the last few months has been no exception. The tax-free, government and prime institutional iMoneyNet money market fund categories had strong returns in 2018 (1.21%, 1.53% and 1.79%, respectively) and industry assets grew nearly $150 billion in the fourth quarter alone. But liquidity also is filling its traditional role of meeting investor needs for regular withdrawals, such as for payrolls or mortgage payments, accessible on a same-day basis. Many clients need some form of a steady stream of income, so why not have it come from a broadened portfolio's liquidity position? You likely are going to earn more than you would from a non-interest-earning checking account or the like. And, while obviously not as risk-free as U.S. Treasuries or federally insured accounts, for the better part of 50 years, money markets mutual funds have been stable products.

3. **What is the outlook and positioning for liquidity strategies over the next 3 to 6 months?** We are looking for a data-dependent Federal Reserve to hike rates twice in 2019, with the first most likely coming in June. We think an upward-sloping yield curve will continue to anticipate these moves. That means liquidity strategies should be best positioned to capture those market changes by focusing on variable-rate securities and by shortening weighted average maturity targets. The industry will be closely watching how many of the inflows that came because of volatility stick around simply based on the return now being offered. But everything depends on the need of the client. Cash is, if nothing else, extremely flexible and can be a small or a large component of a portfolio, and configured in many ways. It remains a go-to class when people need access and stability—and now return, too.

Thanks, Debbie.

TAGS

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