Strategic: Put cash to work

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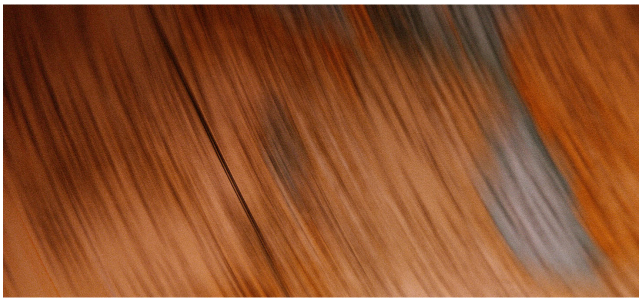
Why? 1) Recent all-time highs in major stock markets should not deter long-term investors from committing to markets, given US stocks have beaten cash in 97% of cases between 1945 and July of this year. 2) Balanced investing by maintaining a diversified 60/40 portfolio (60% equities, 40% bonds) has proven resilient across market cycles and a consistent outperformer versus cash. 3) Having an intentional plan for both cash and investing can help overcome emotional biases and the false allure of market timing.



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For some investors, especially those who hold substantial wealth in their private businesses, cash is synonymous with "rainy day fund" or "safety net." Holding large amounts of cash relative to financial assets as a counterbalance to a business may seem appropriate as a fallback plan.

But for some investors, cash is what is left over after other investments have been committed. Or cash is a general fund for potential spending or opportunistic investments as yet unknown. In short, cash is held unintentionally, an afterthought.

In an uncertain world and yet one where we identify multiple compelling investment opportunities across asset classes, we believe treating cash as a residual may be a mistake.

Instead, we outline a three-step approach for prudent cash management, one that can both maximize the chances of having funds on hand when needed, while also supporting long-term financial goals to protect, preserve, and grow wealth.

Step 1: Ascertain how much cash to hold, and invest the excess

CIO recommends that investors maintain enough cash to cover 2-5 years of net expected portfolio withdrawals. This range is based on historical recovery periods for balanced portfolios (stocks and bonds) following their worst drawdowns. If an investor holds more than this, their excess cash may not be working efficiently toward long-term financial goals.

Excess cash often sits idle, earning little or no real return, and is vulnerable to inflation erosion. In this context, holding large cash balances can result in negative after-inflation returns, eroding purchasing power over time.

History shows that phasing excess cash into diversified portfolios can deliver more robust long-term outcomes. Over 10- and 20-year holding periods, US stocks have beaten cash in 97% and 100% of cases, respectively, between 1945 and July of this year, based on our analysis. By gradually investing excess cash into a mix of stocks, bonds, commodities, and alternatives, investors can reduce the risk of poor market timing and benefit from market dips and rebounds.

Balanced investing by contrast, such as maintaining a diversified 60/40 portfolio (60% equities, 40% bonds), has proven resilient across market cycles and a consistent outperformer versus cash. Looking at data from 1992 to July of this year, USD 100 investing in such a combination of stocks (S&P 500) and bonds (Intermediate Treasuries) would be worth roughly six times the value of the same USD 100 kept in US 1-3 month T-bills.

Some investors fear drawdowns, a technical term for peak-to-trough losses, and the time for their portfolio to recover. We analyzed a series of US stock and bond portfolios ranging from all equities to all bonds, including adding to stocks by 10% increments. One way to measure investor discomfort after a market decline is the longest time it would have taken for a portfolio to not just recover but take out a fresh high. We discover that while an all-bond portfolio's longest recovery time was 4 years and an all-equity portfolio's around 6 years, mixing 40% stocks and 60% bonds yields the fastest recovery of 2.5 years.

Step 2: Don’t just look at headline rates, consider reinvestment risk

While markets still expect US interest rates to rise this year, we think the Federal Reserve is more likely to stay on hold. What’s more, mechanically rolling over very short-term deposits exposes investors to potentially significant reinvestment risk.

Instead of rolling over short-term deposits, investors should consider locking in currently elevated yields with longer-term fixed-term deposits or high-grade (HG) bonds. This strategy may outperform cash in adverse growth scenarios where rates fall and bonds have potential for capital gains. With yields elevated, we believe short- and medium-maturity high-quality government bonds offer an appealing risk-return profile.

Step 3: Explore alternative ways to put cash to work through a cash management framework

A thoughtful cash management strategy involves segmenting liquidity into three categories: everyday cash, core liquidity, and investment cash. It is crucial to optimize diversification, liquidity, and returns within each.

Everyday cash (6-12 months). Everyday cash should prioritize access and safety over yield. This tier is designed for daily expenses, taxes, emergency needs, and liabilities due within roughly six to 12 months. We note that returns will generally be low, but the priority is immediate access and safety, avoiding market, credit, or currency risk.

Current accounts, checking accounts, savings accounts, and very short-dated money market approaches can provide flexibility, while money market funds may offer diversification across short-term instruments.

However, money-market funds are investments rather than bank deposits: Their value can fluctuate, they are not guaranteed to maintain a stable value, and access may involve settlement time. Investors should also consider the credit strength of the bank or fund holdings and avoid concentrating too much cash with a single institution.

Core liquidity (1-3 years). For known expenses or emergency needs further out, investors may have more flexibility.

Deposits and short-duration fixed income can serve known expenses over the next one to three years. Fixed-term deposits can provide a defined interest rate and maturity, making them of interest when the amount and timing of a future expense are relatively clear. The trade-off is reduced access, with early withdrawal potentially unavailable or costly.

Call or notice deposits may offer more flexibility, although withdrawals can require advance notice. Short-duration investment grade bond funds, Treasury bills, and short-dated government or corporate bonds can provide diversification and potentially higher income, but their prices may fall before maturity as interest rates or credit spreads change.

A bond ladder may also provide structure for predictable withdrawals while reducing reinvestment risk. A ladder combines bonds or fixed-term solutions with staggered maturities, so that a portion of the portfolio becomes available at regular intervals. Investors can align each holding’s size and maturity with a planned withdrawal, creating predictable cash flows without relying entirely on an on-demand account.

Investment cash (up to 5 years):

For longer-term needs, focus on maximizing returns by accepting some price fluctuation and limited liquidity.

Medium-term government or investment grade bonds, diversified across countries, sectors, and currencies, can provide higher returns than cash.

Equally, investors may consider certain structured strategies with capital preservation features, in an effort to generate returns that keep pace with inflation while limiting the risks of the investment being impaired by market declines by the time it is needed.

Managing cash is not risk-free. Investors must weigh counterparty, credit, liquidity, and reinvestment risks, as well as the potential for negative real returns in low or negative rate environments. Matching risk to time horizon, diversifying across instruments, and regularly reviewing allocations are essential to preserving and growing wealth in today’s uncertain world.

While the phrase “time in the market beats timing the market” is overused, it may also be worth recalling given the statistical merits of investing rather than waiting for a correction.

Market timing—the attempt to sell before downturns and buy before recoveries—may seem appealing during periods of lofty stock markets or heightened uncertainty. However, statistics show that the best market days often follow the worst.

This arises because many markets' strongest days frequently occur within weeks of their sharpest declines, underscoring the danger of being out of the market at the wrong time. Selling in response to immediate uncertainty locks in temporary losses and reduces the ability to participate in recoveries.

Market timing is closely linked to emotional decision-making. During crises, investors often succumb to "action bias"—the urge to take action simply to feel in control. This can lead to selling at market lows and buying at highs, a pattern that erodes wealth over time. Equally, waiting for market highs to fade before adding to stocks assumes that peaks are fleeting.

Behavioral finance studies show that investors who react emotionally tend to underperform those who stay invested. Strategies like rebalancing can help "scratch the itch" of action bias while keeping long-term plans intact.

Attempting to time the market also requires constant monitoring, rapid decision-making, and a deep understanding of global events, policy shifts, and market dynamics. This is extremely time and resource intensive, and even professional investors struggle to consistently predict market turning points.

By contrast, relying on professionals who construct balanced portfolios may yield positive results in most instances, assuming proper diversification and risk management. Professional managers may have access to tools including active strategies to rebalance portfolios while adjusting exposures to changing conditions, all under the umbrella of a disciplined approach that avoids emotional pitfalls.

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Attractive: We consider this asset class to be attractive. Consider opportunities in this asset class.
Neutral: We do not expect outsized returns or losses. Hold longer-term exposure.
Unattractive: We consider this asset class to be unattractive. Consider alternative opportunities
Note: For equities, we have a five-tier rating system with two additional preferences
Most Attractive: We consider this asset class to be among the most attractive. Investors should seek opportunities to add exposure.
Least Attractive: We consider this asset class to be among the least attractive. Seek more favorable alternatives opportunities.
When equities are included with the other asset classes in the three-tier rating system, we collapse "Most Attractive" with "Attractive" and "Least Attractive" with "Unattractive."

Appendix

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