Money Matters: What to do with cash

By Rick Gross

Cash has a role to play in a diversified portfolio for long-term investors in any market situation, particularly when interest rates and volatility are on the rise. If you have a portion of your portfolio in cash, or if it's been awhile since you've reviewed your cash position, read on.

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The role of cash

For many investors, cash helps protect a portion of income against market volatility and provides the ability to generate a competitive return. Cash is also important to maintaining a degree of liquidity in case of a financial emergency. This is particularly true for retirees and those preparing to retire. Sustaining several months or even a year or two of easily accessible income provides cash flow to meet daily essential and lifestyle expenses.

The environment changes for cash

With short-term interest rates hovering near zero percent, investors have become accustomed to very limited returns on money put to work in cash. This environment is progressively changing. Since December 2015, the Federal Reserve (the Fed), which has notable influence in the fixed income marketplace, has steadily raised short-term interest rates. Many investors believe rising rates may be a turning point that signals better returns ahead for cash savings.

For example, the yield on three-month U.S. Treasury Bills was as low as 0.20 percent at the end of March 2016. Two years later, the rate stands above 1.7 percent.1 Other forms of short-term savings are also generating higher rates as the market changes.

As the environment for rates changes, it’s important to note another persistent trend in the market: increased volatility in stocks. Investors with a diversified portfolio likely have experienced market swings as they position a portion of their assets toward growth. While market swings are a normal occurrence for the investor, having a chunk of assets in cash equivalent vehicles can help cushion the impact of market volatility on your portfolio.

Ways to seek yields on your cash

Amid these environmental changes, you may be tempted to tuck your cash in a bank savings account and accept that you may earn a less-than-competitive interest rate. Yet, the potential for better returns means it’s worth evaluating other options. While there are a variety of cash solutions, the following are three common vehicles that could work as an alternative or supplement to your current strategy:

· **U.S. Treasury Securities.** There are a variety of securities available that are backed by the full faith and credit of the U.S. government. In recent months, yields on shorter-term securities (Treasuries with maturities of less than one year) have been rising faster than those for longer-term Treasury bonds, such as 10- and 30-year bonds. This creates a modest opportunity for cash investors to get more bang for their buck while providing access to the money in short order.

· **Certificates.** These are short-term, guaranteed investments from private institutions that typically offer competitive yields and flexible solutions that can be structured to suit your needs. Many investors choose certificates using a laddering strategy, which means owning certificates with different maturity dates. As each certificate matures, the proceeds are reinvested into new certificates. Since a portion of the laddered savings continues to mature periodically, the investor maintains a degree of liquidity while generating yields.

· **Money market mutual funds.** Money market funds are a portfolio of short-term, highly-liquid securities that offer investors a stable and diverse place for their cash. Funds may include U.S. Treasury or municipal securities, and certificates, among other options. Many funds provide tax-advantaged gains, because they invest in municipal securities at are exempt from tax at the federal and/or state level.

As you evaluate these and other cash strategies, remember to keep your overall portfolio in mind. How your savings are allocated between cash and cash-equivalent vehicles should align with your unique goals, risk tolerance, and investment time horizon. Talk to a financial advisor about how to most effectively position your cash assets in today’s market.

1 “Daily Treasury yield curve rates,” U.S. Department of the Treasury.

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