A mad dash for cash

- The release of the Q1 Financial Accounts from the Federal Reserve confirmed the mad dash for cash last quarter. The degree of cash hoarding by households (which include hedge funds, private equity and personal trusts) and nonfinancial corporates businesses was unprecedented. Holdings of cash and cash-like instruments rose by $939 billion and $397 billion for households and nonfinancial corporates, respectively, lifting the relative shares of these instruments in financial assets to 16.7% and 12.1%. These rises in cash holdings far exceeded previous records.

- The damage to household balance sheets was particularly acute as household net worth plunged by nearly $6.6 trillion (5.6%), the largest drop on record. At the same time, the corporate scramble for cash in the first quarter coincided with record increases in bank loans and debt.

- For households, redeployment of cash partly explains the swift rebound in asset markets, which will boost household net worth given its high correlation with the equity market. However, net worth may not fully recover near term, and the recent volatility may result in more cautious behavior beyond the initial surge as the economy reopens. As we noted previously (see "Are US households still scarred by the financial crisis?") household economic decisions showed signs of scarring years after the Great Financial Crisis. While corporates are now flush with cash to stave off liquidity concerns, balance sheet leverage is historically high, potentially depressing the pace of hiring and investment.

### Figure 1: Cash was king in Q1

![Cash was king in Q1](source: FRB, Haver Analytics, Deutsche Bank)
A mad dash for cash

The Z.1 accounts compiled by the Federal Reserve provide data on transactions and levels of financial assets and liabilities, by sector and financial instrument, as well as full balance sheets, including net worth, for households and nonprofit organizations, nonfinancial corporate businesses, and nonfinancial noncorporate businesses. It is important to remember that the household sector includes domestic hedge funds, private equity and personal trusts.

The latest release for Q1 reveals what we largely already knew in terms of the sharp decline in risk assets and subsequent move to cash. However, the magnitude of these moves was unprecedented. We define cash as the sum of foreign deposits, checkable deposits and currency, time and savings deposits, and money market fund shares (for corporates we also include securities repurchase agreements). Regarding household balance sheets, the cash and cash-like share of financial assets surged from 14.5% to 16.7% (Figure 2). With respect to nonfinancial corporate balance sheets, cash and cash-like instruments jumped from 10.4% to 12.1% of total financial assets. For both sectors, the increase in the cash share of financial assets was the largest one-quarter gain on record.

To be sure, the increases in these shares of financial assets on the balance sheet also reflects the decline in the market value of other financial assets such as corporate equities and bonds. However, when we turn to the transaction level data, which measure the net acquisition of assets, corporates acquired on net $397 billion of cash and cash-like instruments, far exceeding the next largest increase of $216 billion in Q3 2019. Moreover, corporate demand for cash was dwarfed by the $939 billion in net cash acquisitions from households, which was more than double the previous record of $424 billion in Q1 2008 (Figure 3). The extreme de-risking by households and corporates began to severely impair market functioning, which was one reason why the Fed was forced to intervene so aggressively as the crisis began to unfold, swiftly cutting interest rates by 150bps, ramping up its offerings of repo liquidity and increasing its holdings of Treasury securities by a record $650 billion in the first quarter. Indeed, the Fed has bought another $1 trillion of Treasury securities thus far in the current quarter, along with $500 billion in agency MBS.

Figure 2: Cash as a share of assets surged

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Source: FRB, Haver Analytics, Deutsche Bank

Figure 3: Cash was king in Q1

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Source: FRB, Haver Analytics, Deutsche Bank
**Balance sheet triage**

The increase in cash on the part of households can partly be explained by a massive $358 billion liquidation of treasury securities, possibly due to hedge fund deleveraging (Figure 4). At the same time, “other loans and advances”, which includes cash accounts at brokers and dealers as well as syndicated loans to nonfinancial corporate business by nonprofits and domestic hedge funds surged by a record $146 billion (Figure 5). This is not surprising given that mutual fund shares saw the largest net outflows since Q4 2018 (Figure 6). However, it is interesting to note that households were net buyers of corporate equities and corporate bonds in Q1. Not surprisingly, the move to cash and selling of mutual fund shares often coincides with large movements in equity prices (Figure 7).

Within the corporate world, debt and loans exploded by $656 billion combined, by far the largest increase on record (Figure 8). This was driven mainly by bank loans ($326 billion) as companies drew down lines of credit and corporate bond issuance.
($171 billion), which also increased at a record pace despite the freezing up of issuance markets toward the end of the quarter (Figure 9). The current quarter is likely to see an even larger increase in corporate debt given the record pace of issuance over the past couple of months.

With respect to the overall balance sheet picture, household net worth plunged by nearly $6.6 trillion (5.6%), the largest drop on record, largely due to a drop in equity prices (Figure 10). In addition, corporate leverage has increased, with corporate debt as share of GDP rising 3.2 ppts to a new record high of 48.7% (Figure 11). It will likely breach 50% in the current quarter given our expectations for a 38.4% decline in Q2 inflation-adjusted output.

While some of the decline in net worth may be made up in the current quarter barring further material declines in equity prices, household balance sheets have been left somewhat dented and given elevated unemployment expected in the quarters ahead, they may be less willing to resume spending as quickly as they
otherwise may have. As Figure 12 illustrates, the relationship between net worth and the savings rate has changed meaningfully since the financial crisis (see "Are US households still scarred by the financial crisis?"), suggesting a shift toward greater savings. Additionally, changes in household net worth have historically led the trend in retail sales by a quarter (Figure 14). Regarding the corporate sector, the massive rise in debt, while going a long way in terms of addressing liquidity needs and bankruptcy risk, may leave companies wary of quickly resuming investment and hiring given the uncertain demand environment.
Appendix 1

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