SHOULD YOU SIT ON CASH IN YOUR ACCOUNT?

By: Kathleen L. Springer, Senior Vice President, Private Banking Team Leader

Cash strategies are as unique as each individual—there is no "one size fits all." If you find yourself in a situation where you have excess cash on hand as the result of a bonus, inheritance, windfall, or investment transaction, a cash flow plan will be helpful in implementing your overall investment strategy.

Consider the following suggestions if you need to develop or tweak your cash flow plan.

IS IT TIME TO PUT YOUR CASH TO WORK?

Cash on the sidelines isn't necessarily a bad thing. However, cash that isn't working for you could be working against you when you consider the effects of inflation. Keep in mind your approach to cash management depends on three factors: your appetite for risk, short- and long-term goals, and current financial obligations.

FUND AN EMERGENCY ACCOUNT

The first step in creating or updating a cash flow plan is to review your monthly budget. It's important to set aside four to six months of living expenses in a separate emergency account (do not combine these funds with existing checking, savings, certificates of deposit (CDs), and money market assets).

Deposit enough cash in the emergency account to cover your day-to-day expenses such as food, clothing, medical, and transportation. Put in adequate funds to cover regular monthly payments such as your mortgage and utilities. Also, you might want to have ample cash in the account to cover deductibles for insurance—car, health, and homeowners—should you need to file a claim.

Keep in mind the amount of cash in the emergency account should be tailored to your needs—and your family's—based on your lifestyle. For example, a cash flow plan would be quite different for a retired couple with limited expenses, a single salesperson on commission, and a married couple with children still living in their home.

KEEP YOUR OVERALL WEALTH STRATEGY INTACT

Investors should consider keeping their emergency fund cash separate from the cash kept in their portfolio to take advantage of new investment opportunities without having to sell existing investments and potentially create a taxable event.*

Without proper planning for an emergency situation, you might have to gather all your available cash or liquidate a long-term investment, which could disrupt your existing investment plan. For example, if you take a non-qualified distribution from your retirement account prior to retirement, those assets could be subject to tax penalties. It might be better to keep your overall wealth strategy intact by keeping those assets invested to potentially generate a long-term return.

ESTABLISH A LINE OF CREDIT

One way to access cash and take advantage of today's lower interest rates is to establish a line of credit that can be utilized as needed for large or unplanned purchases. Borrowing against the equity in your home or non-retirement investments can provide for short-term cash needs if your emergency fund doesn't stretch to meet your expenses.

Many consumers are familiar with home equity lines of credit and credit cards, but investors often have an additional option—borrowing against their securities portfolio. With securities-based lending, you retain ownership of your investment while borrowing against the value of it, similar to a home equity line of credit.

Securities-based lending can be a great source of funding for a short-term loan, such as a bridge loan, for example, if you need to buy a new home prior to selling your current one. This is a common borrowing strategy among investors because it provides flexibility, a sense of control, and preserves emergency cash.

CASH-OUT MORTGAGE REFINANCE

If you're able to refinance your home at a lower rate, that's generally a prudent strategy to either reduce your monthly payment or pull out equity currently in your home to fund an emergency account or other investment objective. However, be aware of the overall costs and make sure it supports your long-term goals. For instance, if you are planning to sell your home and move in the near future, reducing your mortgage rate by 0.5% and paying closing costs may not reap the long-term savings you envisioned.

PAY OFF DEBT OR INVEST

Paying off debt vs. investing excess cash is a personal choice based on your unique situation. If you're debt averse, it may give you peace of mind to reduce debt even when your finances could benefit more from investing the cash. However, if you can earn more by investing the money than you would pay in interest on the debt, it's better to invest. Likewise, if the interest on your debt is more than you would earn through investing, you should consider paying off the debt.

FINANCE OR PAY CASH

The old adage that "cash is king" may not hold true in a low interest rate environment. If you're able to invest your cash and earn 8% while borrowing for a car or home loan at a lower percentage rate, it's more advantageous to borrow for the purchase and invest the cash, earning a higher interest rate. Even a small difference between borrowing rates and interest on earnings can benefit your portfolio.

These considerations are just a few of the many ways to maximize and manage your excess cash within a cash flow plan. Contact Commerce Trust Company today. Together we can explore a variety of options for cash management solutions and help you make educated decisions based on your goals and unique financial situation.

*Consult your tax advisor

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Kathleen is a relationship manager team leader with Commerce Trust Company. As a member of the private client team and an experienced, tenured private banker, she and her dedicated client support staff are responsible for ensuring each client's experience with Commerce Trust exceeds expectations. Kathleen's specific responsibilities include management of our clients' day-to-day banking, cash management, and credit needs, while also helping them navigate the wide array of our financial services to find the solutions that best fit their needs. Before joining Commerce Bank in 1996, she was a private banker with Boatmen's National Bank as well as a commercial lender at South Side National Bank and has 27 years of private banking experience. She received her undergraduate degree from University of Missouri and her master of business administration degree from Webster University.

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