

## Holding Cash as a Tactical Move

In the course of managing investments, we get client enquiries on the level of cash in their portfolios. Interestingly, these views differ widely, with some clients asking why so much cash, and others asking why so little. To some clients, 10% cash holdings are too high and therefore too conservative; while to others, 30% cash holdings are too low and therefore risky. This dichotomy in views is not surprising. Investors have different risk appetites and they are influenced by their perceptions of the prevailing market conditions and the outlook for the future.

For us at PMA, the cash holding at any one time is the result of our active portfolio management style. We will tactically move assets from say, equities to cash equivalents and vice versa, depending on our reading of the market and its future direction. In investment parlance, it is termed market timing, a concept that is gaining increasing acceptance. In a speech to a group of institutional money managers of endowments and foundations, in 2003, Peter Bernstein, a respected investment professional, spoke of the need for market timing\*. He noted that investors need to be more flexible and opportunistic and asked, "What if moving around more frequently is now a necessity rather than a matter of choice?" We believe that markets are not perfectly efficient and active management, where market timing is a key decision, can exploit market anomalies.

With market timing, cash acts as a cushion in a market correction and provides an opportunistic reserve to buy into additional investments. Determining just how much cash to hold, however, is not easy as it is difficult to predict exactly when and to what extent a market will correct. It is more art than science. Holding too much cash also has risks, which is the opportunity costs of missing out on market rallies.

Under PMA active management approach, cash holdings can vary widely - as low as 5% in extremely oversold markets or market bottoms, or as high as 90% in extremely overbought markets or market tops. Baring such extreme conditions, our cash level has generally fluctuated between 10% and 40%.

We are not compelled to stay fully invested. In considering how much cash to hold, we weigh the downside risks against the upside potential in the markets. This is one of the key differences between PMA and unit trusts in general and allows us significant leeway to protect ourselves in market downturns.

Note: \* Bernstein's Shocking Words: Market Timing by Tom Lauricella, The Wall Street Journal Online, Aug 27,2003.