Dead money

Cash has been piling up on companies' balance-sheets since before the crisis

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Monetary stimulus gets you only so far. In America, third-quarter profits and revenues for companies in the S&P 500 index appear to have fallen year on year for the first time since 2009, according to Thomson Reuters. Profits for roughly half the firms in the European Stoxx 600 have fallen short of expectations so far.

Companies in search of a culprit may want to glance in the mirror. Firms are trimming their budgets for everything from technology-consulting services to semiconductor equipment in the face of what Sir Martin Sorrell of WPP, a British advertising and marketing giant, calls four "grey swans" (unlike black swans, people know about grey ones). The four worries unnerving business are: the euro-zone crisis; upheaval in the Middle East; a possible recession in China; and America's economic health and "fiscal cliff"—the combination of tax increases and spending cuts scheduled to occur at the end of this year.

This is not a new problem. Investment has steadily risen since the recession ended, but not as vigorously as profits. In America, for example, nominal capital expenditure this year (on an annualised basis) has risen by 6% compared with 2007; internal cash flow is up by 32%. Companies have been net suppliers, instead of users, of funds to the rest of the economy since 2008. Firms in the S&P 500 held roughly $900 billion of cash at the end of June, according to Thomson Reuters, down a bit from a year earlier but still 40% up on 2008.

Business leaders and conservative critics cite that cash mountain as proof that meddlesome federal regulations and America's high corporate-tax rate is locking up cash and depressing investment. But that cannot explain why the same phenomenon prevails worldwide. Japanese companies' liquid assets have soared by around 75% since 2007, to $2.8 trillion, according to ISI Group, a broker. Cash stockpiles have continued to grow in Britain and Canada, too, to the immense frustration of policymakers there. "Dead money" is how Mark Carney, the Bank of Canada's governor, has described the nearly $300 billion in cash Canadian companies now hold, 25% more than in 2008. Mr Carney admonished them to "put money to work and if they can't think of what to do with it, they should give it back to their shareholders."

No single factor seems to explain companies' high savings. The Bank of England notes that natural-resource companies account for a disproportionate share of the cash build-up. That may reflect the boom in commodities prices and the paucity of promising new sources of supply.

Low interest rates have reduced borrowing costs, adding roughly a percentage point to American profit margins, according to BCA Research. (Yet rock-bottom interest rates also make it less attractive to hold cash.) The financial crisis has made firms more skittish about relying on banks or securities markets for funds. Since questions were raised in 2008 about the ability of General Electric's finance arm to fund itself, the company has been stockpiling cash: $85 billion at the end of the third quarter, the most in the S&P 500.

A rapid reversal is unlikely. That's because rising corporate saving has deeper roots than the crisis, the commodities boom or this interest-rate cycle. In a recent study Loukas Karabarbounis and Brent Neiman at the University of Chicago found that across 51 countries they examined between 1975 and 2007, companies' share of private saving rose in aggregate by 20 percentage points. In countries where corporate saving rose, labour's share of GDP in the corporate sector shrank, by five percentage points in aggregate.

Mr Karabarbounis and Mr Neiman link both rising corporate saving and labour's shrinking share of GDP to a fall in the relative price of investment goods that began in the early 1980s. That drop may be down to the plunging cost of computing, or to the shift in capital-goods production towards lower-wage developing countries, or both.

Whatever the reason, firms have responded by substituting away from labour and towards capital, and by more than textbook economic models imply. And to finance this investment companies have steadily boosted saving over time. (Just as households can save each year and take out a mortgage, that does not mean firms stopped borrowing: indeed, American businesses have by some measures become more indebted in recent decades.)

The authors do not have comparable data for all 51 countries since 2007. But they do have numbers for the four largest economies (see chart). The data there show that the corporate share of private savings has since dipped a bit, in part because household savings have risen, although it remains high in absolute terms. (Labour's share of GDP has stabilised at a low level.) The urge to save may be lessening. Japanese firms, with few growth prospects at home, have been making foreign deals. Marc Zenner of JPMorgan Chase notes that in the past 18 months firms that announce acquisitions have been rewarded with higher share prices.

Yet even if they are loosening the purse strings a bit, companies are unlikely to abandon their frugal ways in the near future. Falling corporate-tax rates have increased the appeal of capital over labour; heightened uncertainty and capricious funding markets seem a recurring part of the landscape. That should make firms all the more determined to fund growth internally. Between now and 2016, GE expects to generate $100 billion in cash, enough to finance investment, acquisitions and dividends, and to buy back enough stock that shares outstanding will be lower than before the crisis. Asked recently if GE was tempted to spend more of its cash pile on acquisitions, Jeffrey Immelt, the chief executive, replied: "It's not burning a hole in our pocket."