



## Guidelines For Investing Excess Business Cash

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Depending on their cash flow cycle, businesses often find that there is excess cash in their checking or operating account. Savvy CEOs and CFOs should strive to manage this excess cash for maximum return while minimizing risk and maintaining adequate liquidity.

There are three main objectives you should strive for when it comes to managing excess business cash:

1. Invest the money relatively safely.
2. Keep the funds as liquid as possible so they can be accessed to meet operating expenses, if necessary.
3. Within these parameters, generate the highest possible return on the funds.

### Is It Really Excess Cash?

The first thing to do, though, is to make sure that what looks like excess cash is, indeed, excess cash. This is where the cash flow cycle comes into play.

Sometimes, businesses end up collecting payment from clients early, before they have paid for the raw materials, inventory and labor that will be needed to produce a product or deliver a service. In this case, the extra money in the operating account isn't excess cash at all—it's just a temporary bump in the account balance until payables for cost-of-goods sold are disbursed later. This money should usually be kept safely in the operating account to pay expenses when they are due.

Given the overall ebbs and flows of your cash flow cycle, decide what is the minimum balance that you're comfortable maintaining in your operating account. To do this, you need to determine how much working capital is necessary to meet your company's ongoing operating expenses. A simple calculation is to divide the past year's total operating expenses by 12. This will give you a monthly average, which would be your minimum account balance.

Then, you can consider any balances above this minimum level to be excess cash. Investment options for this cash may include the following:

**Business mutual funds and money market accounts** — These are offered by most banks and are usually insured up to \$250,000 per depositor by the Federal Deposit Insurance Corporation (FDIC). They pay market interest rates—which, admittedly, are at historic lows right now—but more importantly, offer maximum liquidity.

**Business certificates of deposit (CDs)** — Also sometimes called jumbo CDs, these may be a good option if you have a relatively large sum of excess cash that you know you won't need for at least three to six months. You may earn a higher rate of interest than on a business mutual fund or money market

account, but you'll also sacrifice some liquidity—so make sure you won't need the money to meet operating expenses before the CD matures.

**Business sweep accounts** — As the name implies, these are bank accounts that automatically “sweep” excess funds above a target minimum balance that you specify into short-term or overnight investment vehicles at the end of the day. Funds are then swept back into your checking account as needed to cover operating expenses. The beauty of a sweep account is that all of this is done automatically, enabling you to easily maximize your return on excess funds.

**Short-term Treasury bonds and bond mutual funds** — These may be appropriate if you have a longer-term time frame for your excess cash—typically, at least two or three years. They may offer a higher yield than business CDs due to the longer timeframe, but again, you have to consider your company's potential liquidity needs. And if interest rates rise in the future, as some are predicting, the value of your bond will fall.

### **Concluding Thoughts**

In today's environment of ongoing economic and business uncertainty, Los Angeles and Southern California CEOs and CFOs should carefully balance the three primary objectives noted here when it comes to investing excess business cash. For more guidance and assistance, you may want to talk to an outsourced CFO services provider, who can help you analyze your cash flow cycle, determine an appropriate minimum balance for your operating account, and choose the right investment vehicle for excess cash.

### **About CFO Edge**

CFO Edge, LLC is a leading Southern California provider of outsourced CFO services. Based in Los Angeles, we are a group of experienced chief financial officers who engage with CEOs and CFOs on demand to address strategic planning, business management, and day-to-day financial operations challenges. Our seasoned professionals deliver services as interim CFOs, part-time CFOs, project-based CFOs, recruitment-to-permanent CFOs and interim-to-permanent CFOs. At CFO Edge, we're passionate about helping our clients create, grow and sustain value. For more information, visit [www.cfoedge.com](http://www.cfoedge.com) or call 626.683.8840.

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