Opinion **Corporate bonds**

Tech companies are the new investment banks

The much-lauded overseas ‘cash’ pile is actually a giant bond portfolio

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A few years ago, while trawling for information about financial risk and where it might be held, I had a fascinating conversation with an economist at the US Treasury’s Office of Financial Research.

She told me to look at the debt offerings and corporate bond purchases being made by the largest, richest corporations, such as Apple or Google. In a low interest rate environment, with billions of dollars in yearly earnings, these high-grade firms were issuing their own very cheap debt and using it to buy up the higher-yielding corporate debt of other firms.

In the search for both higher returns and for something to do with all their money, they were, in a way, acting like banks, taking large anchor positions in new corporate debt offerings and essentially underwriting them the way that JPMorgan or Goldman Sachs might. Since such companies were not regulated like banks, it was difficult to see exactly what they were buying, how much they were buying, and what the market implications might be. Still, the idea that cash-rich tech companies might be the new systemically important institutions was compelling.

That is why I have been poring over a new Credit Suisse report that both confirms and quantifies this idea. Economist Zoltan Pozsar has forensically analysed the $1tn in corporate offshore savings parked in liquid assets, a fortune that he likens to China's foreign exchange reserves, not only because of its market-moving size, but the idea that both fortunes were created by a macroeconomic "crime" — mercantilism in the case of China, and tax arbitrage for the corporate hoard.

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The largest and most intellectual-property-rich 10 per cent of companies — Apple, Microsoft, Cisco, Oracle, Alphabet — control 80 per cent of this hoard. Their earnings come mainly from IP that can be easily moved across borders. Their offshore savings went from around $100bn in 2008 to $700bn by 2016. And according to Mr Pozsar's calculations, most of that money is held not in cash but in bonds. Indeed, half of it is in corporate bonds.

The much-lauded overseas "cash" pile held by the richest American companies, a treasure that Republicans cited as the key reason they passed their ill-advised tax "reform" plan, is actually a giant bond portfolio.

What does this mean? Many significant things. But let us start with the obvious, which is that bonds are not cash. If companies are to bring back those overseas earnings and invest them in growth-enhancing projects in the US, as Donald Trump keeps promising us they will, they would have to sell their bond stash.

This has serious implications for interest rates. Consider that the Federal Reserve is starting to deleverage its own balance sheet. Now, add in the corporate "echo-taper", as the Credit Suisse report puts it, and you have got a heck of a lot of bonds on the market, which is bound to move the interest rate needle up, perhaps more quickly than is currently expected. We saw last week the effect that even a mild change in interest rate expectations can have.

Another point to consider: the real economic growth impact of this spending scenario would be minimal. Corporate treasurers have already said that the bulk of repatriated funds will be used for mergers and acquisitions, dividends and share buybacks, not building factories or raising wages.

"That will be good for whoever owns those stocks, but not much else," says Mr Pozsar. "The $1tn offshore is the manifestation of a lot of what [Thomas] Piketty [author of *Capital in the Twenty-First Century*] says."

Financial fortunes will be made and lost as this cycle plays out over the next couple of years — most of the dealmaking would probably be done by 2020, when the next presidential election could shift rules yet again. Yet nothing in the real economic growth picture would change. We are still in the last stages of a recovery cycle, with flat productivity and demographics, and due for slower, not faster, growth in the next few years. The Wall Street-Main Street divide remains as stark as ever.

In fact, the new Republican tax plan is likely to exacerbate that divide, by making it even easier for big companies to move money around. The shift to the territorial system means that US businesses won't have to play the game of issuing debt to buy debt any more. They will just move money where they like. In the context of more trade protectionism and pushback against immigration, this could lead to further discontent with globalisation, if you define it as the free movement of goods, people and capital. As Mr Pozsar writes, "the US is embracing protectionism on the one hand, and tearing down liquidity silos on the other". If people continue to feel the game of globalisation is rigged against the little guy, you can bet on more political populism.

This time around, the target of voter rage will not be the big banks, but the world's largest and richest corporations. Just as, say, the Rothschilds went from being merchants to merchant bankers when they had enough cash on hand, so rich corporations — especially tech firms — have become the financial engineers of our day. Let us hope the companies' boards are thinking about all that comes with it.

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