

Competitive position and cash holdings

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This paper investigates a negative relationship between the firm's competitive position and cash holdings. Because firms with low competitive position have a lower expected cash flow, therefore such firms save cash out of cash flow to avoid default. I empirically analyze the relationship between firm's competitive position and cash holdings. We find that firms with lower competitive position rely more on cash hoarding. The competitive position effect on cash is stronger when firm face financial constraints or when firms in more competitive industries.

First of all, we introduce product market interaction into Acharya, Davydenko and Strebulaev (2012), and explain the probable theoretical hypothesis. In the first set of empirical results, we explore whether the effect of competitive competition on cash holdings is consistent with our theoretical hypothesis. After controlling for firm's financial channels, various firm features and internal factors of firms, we find that over 2005-2014 period, increasing the measure of competitive position one standard deviations at mean increase the cash-to-net-assets ratio of Japanese manufacturing firms by 0.11 at mean. We also find that main bank dependence has a significant impact on the relationship between competitive position and cash holdings. When firms are more connected with main banks, the effect of competitive position on cash decreased significantly.

In the second set of empirical results, we find that financial constraints have an important effect on the relationship between competitive position and cash holdings. We find that negative relationship between competitive position and cash holdings is significant among firms with financial constraints.

In the third set of empirical results, the firms in more competitive industries hold more cash from low competitive position than do firms in less competitive industries. The empirical result suggest that the relation between the measure of competitive position and cash holdings is negative and significant in the highest competitive industries, and this relation is monotonously decreasing across less competitive industries.

Our empirical result help explain the trend of the increase in cash holdings of Japanese firms in recent years.