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Corporate Asset Allocation under Economic Policy Uncertainty: Avoidance Behaviour and the Conditional Value of Digital Economic Assets

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Abstract

Economic policy uncertainty has become an important factor affecting firms' investment decisions in recent years. When uncertainty increases, firms may become more cautious about long-term investment and prefer to hold safer assets with higher liquidity. This paper studies how economic policy uncertainty influences firms' allocation between traditional safe assets and digital economic assets. It also examines whether this allocation affects firms' short-term performance differently under uncertain conditions. Using panel data from Chinese A-share listed companies between 2014 and 2023, this study applies fixed-effects regression models for empirical analysis. The results suggest that firms tend to increase traditional safe asset holdings and reduce digital asset investment when economic policy uncertainty rises. In addition, digital economic assets are negatively related to short-term return on assets (ROA) on average. However, the interaction results show that the negative effect becomes weaker under higher levels of uncertainty. These results may indicate that firms become more conservative during uncertain periods, but reducing digital investment too much could also weaken firms' ability to adapt to changing environments in the long run.

Keywords

economic policy uncertainty, digital economic assets, traditional safe assets, asset allocation, firm performance

1. Introduction

Economic policy uncertainty (EPU) has become an important factor influencing corporate decision-making in recent years. Changes in government policy, international trade conditions and macroeconomic expectations may affect firms' investment behavior and risk preferences. Existing studies show that higher uncertainty often causes firms to become more cautious in investment and financing activities, especially when future returns are difficult to predict [1,2].

At the same time, digital transformation has gradually become an important development strategy for many firms in China. Investment in digital technologies, digital infrastructure and related research and development may improve firms' operational efficiency and long-term competitiveness. However, compared with traditional safe assets such as cash and low-risk financial holdings, digital economic assets usually involve higher initial costs and longer return cycles.

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Under conditions of economic policy uncertainty, firms may therefore face a trade-off between maintaining liquidity and continuing digital investment. Although previous studies have separately examined precautionary asset holdings and digital transformation, relatively few studies discuss how firms adjust the allocation between these two types of assets under uncertainty. In addition, limited attention has been paid to whether the value of digital investment changes when the external environment becomes more uncertain.

Based on these issues, this paper investigates how economic policy uncertainty affects firms' allocation between traditional safe assets and digital economic assets, and further analyses the impact of such allocation on firm performance.

This paper draws on precautionary savings theory and the risk-return trade-off as the theoretical foundation. Firm-level panel data on Chinese A-share listed companies from 2014 to 2023 are obtained from the CSMAR database, and the China Economic Policy Uncertainty index is publicly accessible [1,3]. Fixed effects models with interaction terms are applied to identify how macro-level uncertainty conditions firm-level allocation decisions and their returns [3].

The marginal contributions of this paper are as follows. First, from the perspective of asset allocation, this paper reveals the inhibiting effect of economic policy uncertainty on firms' digital asset investment. Second, this paper shows that economic policy uncertainty can alleviate the negative effect of digital assets on short-term firm performance, which reveals the conditional value of digital assets.

2. Literature Review and Theoretical Foundation

2.1 Literature Review

Existing research generally suggests that economic uncertainty changes firms' investment preferences and increases their demand for liquid assets. Studies based on the China Economic Policy Uncertainty index find that firms tend to reduce investment expenditure when uncertainty rises, while precautionary financial holdings become more important [3,4]. Some studies also show that firms become more cautious in dividend distribution and reserve management under uncertain policy environments [5]. Further evidence from Chinese listed firms confirms that monetary and economic policy uncertainty raises corporate cash reserves and shapes corporate financialization [6,7]. However, most existing studies mainly focus on cash holdings or financial assets separately, and relatively few studies examine how firms balance traditional safe assets and long-term digital investment simultaneously.

Research on digital investment presents more nuanced conclusions. The information-technology literature emphasises that the benefits of IT investment are often intangible, organisationally mediated and difficult to measure, so that returns frequently emerge only after a substantial lag [3]. Evidence from Chinese listed firms shows that digital transformation can improve market valuation, stock liquidity, financial stability and broader corporate outcomes such as ESG performance [8,9]. Yet other firm-level studies report that digital transformation initially reduces profitability because of large upfront costs and organisational friction, with a profitability rebound emerging only years after adoption [6].

Previous studies show that the effects of digital investment are not always reflected immediately and may vary under different economic conditions. Compared with traditional safe assets, digital economic assets usually require more long-term investment and involve higher initial costs. Because of this, firms may treat digital investment differently from safe assets when economic policy uncertainty increases.

Under uncertain conditions, some firms may prefer to hold more liquid and lower-risk assets instead of continuing large-scale digital investment. However, digital technologies may also help firms improve operational flexibility and deal with changing market conditions more effectively. Based on this perspective, this paper further examines whether the role of digital economic assets changes under different levels of economic policy uncertainty.

2.2 Theoretical Foundation and Hypotheses

This study mainly relates to precautionary savings theory and the risk-return relationship. Under higher levels of external uncertainty, firms are usually more concerned about potential risks and may prefer to hold

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assets with higher liquidity and lower risk in order to reduce possible losses. This idea is consistent with precautionary savings theory.

At the same time, assets with higher risk may also provide higher potential returns. Because digital economic assets often involve larger investment costs and longer return periods, firms may adjust the balance between digital investment and traditional safe assets when economic policy uncertainty changes.

The information-technology productivity-lag perspective holds that the returns to digital and IT investment are realised with a delay, because they require complementary organisational adjustment before their value materialises [3].

When external uncertainty rises, firms tend to reduce high-risk and long-cycle investments and shift more resources to low-risk and liquid assets. Prior evidence shows that uncertainty depresses corporate investment [2,5]. Other evidence indicates that uncertainty increases financial and cash holdings [10,11]. Digital economic assets, which involve higher risk, larger upfront outlays and longer payback periods, are therefore likely to be reduced, while traditional safe assets, which are more liquid and stable, are likely to be increased. This logic is consistent with the core idea of precautionary savings theory, namely that rising uncertainty strengthens firms' risk-aversion motive.

H1: Economic policy uncertainty has a significant negative impact on corporate digital economic asset allocation, and a significant positive impact on corporate traditional safe asset allocation.

The return implications of digital assets are more subtle. According to the productivity-lag perspective, digital investment imposes large upfront costs that compress short-term profitability, even though it may enhance long-term value, and firm-level evidence confirms an initial decline in profitability followed by a delayed rebound [3,6]. In the short run, therefore, digital economic assets are expected to depress return on assets. However, the value of flexible, technology-intensive assets may be greater when the external environment is more uncertain because such assets enhance a firm's ability to adapt and process information. Digital transformation has been linked to improved information environments, innovation and financial stability [8,9]. In uncertain periods, firms may rely more heavily on digital technologies to improve information processing, operational flexibility and risk response capability. As a result, the short-term negative effect of digital assets on profitability may gradually weaken when uncertainty increases.

H2: Corporate digital economic asset allocation has a significant negative impact on short-term return on assets; however, the interaction between digital economic asset allocation and economic policy uncertainty is significantly positive, so that the negative short-term effect weakens as economic policy uncertainty increases.

3. Research Design

3.1 Sample, Data Sources and Variables

This paper takes Chinese A-share listed companies from 2014 to 2023 as the research sample. Following standard practice in corporate finance research, financial firms, ST and *ST firms, and firm-year observations with missing key variables are excluded, and all continuous variables are winsorised at the 1% and 99% levels to mitigate the influence of outliers. Data on traditional safe assets, digital economic assets, financial indicators and control variables are obtained from the CSMAR database. After cleaning and matching, the final sample contains 4,332 firm-year observations.

The explanatory variable is the Economic Policy Uncertainty index (EPU), measured at the country-year level [1,10]. The dependent variables are the corporate digital economic asset allocation ratio (DEI) and the traditional safe asset allocation ratio (TRA) when testing H1, and return on assets (ROA) when testing H2. To test the conditional effect in H2, two interaction terms, EPU×DEI and EPU×TRA, are constructed. The control variables include firm size (size, the natural logarithm of total assets), leverage (lev) and growth opportunity (grow, revenue growth rate). All firm-level variables are constructed at the firm-year level.

3.2 Model Specification

Because the Economic Policy Uncertainty index (EPU) is an annual macro-level variable, it is perfectly collinear with year fixed effects and cannot be identified once year fixed effects are included. Following the

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interaction-based identification strategy used in this literature, Model 1 is therefore estimated with firm fixed effects only, and Model 2 also uses firm fixed effects in combination with EPU interaction terms to identify the conditional effect [10]. Standard errors are clustered at the firm level throughout.

Model 1, corresponding to H1, examines the effect of economic policy uncertainty on the allocation of the two asset categories:

$$DEI_{it} = \alpha_0 + \alpha_1 EPU_t + \Sigma\, \alpha_j Control_{it} + \mu_i + \varepsilon_{it} \quad (1)$$

$$TRA_{it} = \beta_0 + \beta_1 EPU_t + \Sigma\, \beta_j Control_{it} + \mu_i + \varepsilon_{it} \quad (2)$$

Model 2, corresponding to H2, examines the effect of the two asset categories on corporate return, and whether this effect is conditional on economic policy uncertainty:

$$ROA_{it} = \gamma_0 + \gamma_1 DEI_{it} + \gamma_2 TRA_{it} + \gamma_3 (EPU_t \times DEI_{it}) + \gamma_4 (EPU_t \times TRA_{it}) + \Sigma\, \gamma_j Control_{it} + \mu_i + \varepsilon_{it} \quad (3)$$

In all models, μ_i denotes firm fixed effects and ε_{it} is the random error term. A baseline ROA model without interaction terms (controlling for both firm and year fixed effects) is also reported for comparison.

4. Empirical Results

4.1 Descriptive Statistics

Descriptive statistics show that the mean, standard deviation, minimum, maximum and median values of the main variables fall within reasonable ranges, with no extreme outliers observed after winsorisation. The distributions of DEI, TRA and ROA are consistent with prior studies on Chinese listed firms, indicating that the data quality meets the requirements for subsequent regression analysis.

4.2 Baseline Regression

Table 1 reports the regression results. Columns (1) and (2) test H1 with firm fixed effects; column (3) reports the baseline ROA model with firm and year fixed effects; and column (4) reports the ROA model with EPU interaction terms, which is the core test of the conditional effect in H2. Robust standard errors clustered at the firm level are used throughout.

Table 1: Baseline and Interaction Regression Results

Variable	(1) DEI	(2) TRA	(3) ROA	(4) ROA
EPU	-0.0000810***	0.000171***	—	—
	(0.0000280)	(0.0000289)		
DEI	—	—	-0.0816***	-0.0786***
			(0.0157)	(0.0160)
TRA	—	—	0.0205*	0.0146
			(0.0121)	(0.0116)
EPU×DEI	—	—	—	0.0194***
				(0.0071)
EPU×TRA	—	—	—	0.0031
				(0.0108)
size	-0.0285***	0.0077	0.0071*	-0.0070**
	(0.0081)	(0.0063)	(0.0038)	(0.0029)
lev	0.0407	-0.2226***	-0.1410***	-0.1318***
	(0.0333)	(0.0333)	(0.0131)	(0.0135)
grow	-0.0016	-0.0025	0.0096***	0.0097***
	(0.0019)	(0.0019)	(0.0011)	(0.0011)
Firm FE	Yes	Yes	Yes	Yes
Year FE	No	No	Yes	No
N	4332	4332	4332	4332
Within R^2	0.0735	0.0951	0.1706	0.1612

*Note: Robust standard errors clustered at the firm level are in parentheses. EPU is a national year-level variable and is therefore identified with firm (not year) fixed effects in columns (1), (2) and (4). *** p < 0.01, ** p < 0.05, * p < 0.1.*

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The regression results in Columns (1) and (2) show that economic policy uncertainty is negatively related to digital economic asset allocation and positively related to traditional safe asset allocation. In other words, firms appear to reduce digital investment and hold more safe assets when the external environment becomes more uncertain. This may reflect a tendency to prioritize liquidity and short-term stability under uncertain conditions.

For firm performance, the results in Column (3) suggest that a higher level of digital economic assets is associated with lower short-term ROA. A possible explanation is that digital investment usually involves relatively high costs at the early stage, while the benefits may take time to appear. Compared with digital assets, traditional safe assets show a relatively weak positive relationship with ROA.

After adding the interaction terms in Column (4), the coefficient of the interaction between EPU and DEI becomes positive and statistically significant. This suggests that the negative relationship between digital assets and short-term profitability becomes weaker when economic policy uncertainty is higher. One possible reason is that firms may rely more on digital technologies during uncertain periods to improve efficiency, flexibility and information management.

By contrast, the interaction term between EPU and traditional safe assets is not statistically significant. This means that the relationship between traditional safe assets and firm performance does not appear to change much under different levels of uncertainty.

Overall, the findings suggest that firms become more conservative when uncertainty increases, although digital investment may still play an important role in helping firms respond to unstable environments.

5. Recommendations

5.1 Firms Should Avoid Over-Cutting Digital Assets under Uncertainty

Firms should adopt a dual-track asset allocation strategy that combines digital economic assets with traditional safe assets, and adjust the proportions according to the level of economic policy uncertainty. While moderately increasing traditional safe assets during turbulent periods is reasonable for liquidity protection, the evidence that the drag of digital assets on returns weakens as uncertainty rises implies that firms should avoid excessive reductions in digital investment when uncertainty is high. Maintaining digital R&D and digital infrastructure preserves the flexibility and information advantages that are most valuable precisely in uncertain environments.

5.2 Policy Should Support Digital Investment in Uncertain Times

Because firms tend to retreat from digital assets when uncertainty rises, even though such assets become relatively more valuable, there is a role for policy in counteracting this short-sighted retreat. Policymakers may consider targeted tax incentives, R&D subsidies and risk-sharing mechanisms for digital investment, particularly for financially constrained and high-tech firms, and should improve the institutional environment for digital asset recognition, valuation and disclosure so as to reduce the policy-related uncertainty surrounding digital investment.

5.3 Markets Should Strengthen Information Disclosure

Capital markets and regulators should strengthen disclosure and risk-warning mechanisms regarding economic policy uncertainty and firm-level asset composition. Encouraging listed firms to disclose more granular information on their digital and traditional safe asset holdings would allow investors to better evaluate firms' allocation strategies and to recognise the conditional value of digital assets, reducing the likelihood that markets penalise firms for digital investment that is costly in the short run but valuable under uncertainty.

6. Conclusion

This study examines how economic policy uncertainty influences firms' allocation between digital economic assets and traditional safe assets using data from Chinese A-share listed firms from 2014 to 2023.

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The empirical results show that firms become more conservative when uncertainty rises, increasing traditional safe asset holdings while reducing digital investment. At the same time, although digital economic assets negatively affect short-term ROA on average, this negative effect becomes weaker under higher levels of uncertainty.

Overall, the findings suggest that firms may underestimate the strategic value of digital investment during uncertain periods. While maintaining liquidity is important, excessive cuts in digital investment could weaken firms' long-term flexibility and competitiveness.

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Conflicts of Interest

The authors declare no conflict of interest.

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