



LET'S TALK ABOUT...

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Liquidity trap

The term was coined by the renowned British economist – as well as speculative investor - John Maynard Keynes in the 30's. It denotes a condition in which the monetary policy, however loose, and other public interventions, are unable to stimulate a depressed economy. That is the current case for many Western growth-less scenarios: interest rates have been cut down to historical lows, near zero, all other measures have been implemented, including some non-conventional ones, as the so called “quantitative easings”, so injecting huge amounts of cash into the system, without succeeding in fuelling significant and sustainable growths.

The reasons are many: low interest rates do not stimulate investments and many assets are held in cash, also because deflationary environment points to lower prices and values ahead. Moreover households restrain consumption, not just only because prices are expected to get down, but mainly because of gloomy expectations in terms of jobs, retirement provision, general uncertainty, not to say of the losses many families have suffered in their financial and property investments. Indeed the impoverishment process of middle classes, both in Europe and the United States, has been massive through the past years. Neither companies are tempted to invest, as consumption is slack. Well, the “liquidity trap” recalls the famous Arab saying according to which you can take your camel to the water well, but you can not force him to drink. Thus, most of the liquidity that central banks inject into the market, does not take the way of the real economy, but rather is used by banks to “arrange” their internal situations, or is invested in more rewarding ways, e.g. in fast-growing emerging markets or other assets, such as commodities and currencies. After the 30's and the 40's, with the many disputes about the Keynesian theories, the “trap” was back in the limelight during the Japan's “lost decade” in the 90's, when the zero-rate policy was unable to avoid a long period of deflation and stagnation after the previous equity and property bubbles had gone burst. - *GLT*

The views expressed are not necessarily those of the Swiss Association of Asset Managers
