

R&I Blog
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What Is The Liquidity Premium for Cash?

One can divide that vast majority of investors today into three groups:

- The first group believes that central banks and governments will continue to successfully keep liquidity flowing and will do so long term, and will succeed in establishing a sustainable recovery in the next year or so.
- The second group believes that central banks and governments will continue to successfully keep liquidity flowing and will do so long term, and will succeed in establishing a sustainable recovery but it will take a long time (the “New Normal” as PIMCO says).
- The third group, the bears, believes that central banks and governments will continue to successfully keep liquidity flowing and will do so long term, but will fail to produce a sustainable recovery, because they’re out of fiscal and monetary stimulus ammunition.

I think they’re all wrong, because there is no basis for the near universal belief in adequate liquidity as far as the eye can foresee. The one-time “success” of the Fed in the recent crisis, in preventing a long-term liquidity crunch, has given rise to a near-religious faith that central banks will always be able to maintain liquidity. If, as I believe, the Fed does not possess an infinite capacity to liquidify the United States, let alone the world, then **the liquidity premium for cash, even at interest rates below 1%, is grossly undervalued.**