n-linked bonds still best option for pension savers

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But what about the familiar argument that the volatility of past equity returns shows the probability that equities will earn less than the risk-free rate decreases with time, so that long-term pension savers should hold equities, not inflation-protected bonds?

The proper measure of equity risk is the cost of buying insurance against underperformance versus the risk-free return – a "put option" on a stock market index. If risk reduces over time the cost of equity put options against any shortfall should reduce. But the cost increases the longer the option period, reflecting increasing not decreasing risk.

The theoretical price, based on a standard option pricing model and actual prices charged by banks, is about 25 per cent for 10 years and 30 per cent for 20 years.

If holding equities for the long run leads to higher average returns, with negligible risk, why don't investment banks provide guaranteed equity outperformance, for a modest fee reflecting the (supposedly) modest risk?

The optimal equity/bond split for the pension saver should be driven not by age or time to retirement, but by an individual's "risk aversion" and the desire to lock in a minimum level of pension, which can only be done by holding inflation-protected bonds. We face many risks in old age which we can do nothing about, why add one we can eliminate?

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Fellow of the Faculty of Actuaries,
St Albans, Herts, UK

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(Letters, January
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Brand designs: Tesco has replicated its success into banking Bloomberg

Winners need a clear channel strategy

From Prof Robert Shaw.

Sir, Your report "Brand damage by association" (Business Life, February 3) is one more piece of evidence foretelling a mass extinction of brands. Brand advertising is fading away; social media are "outing" fabricated brand identities; many consumer brands are too weak to survive, except in niches.

I get groceries from Amazon and insurance and banking from Tesco. Yesterday's winners had a clear brand strategy; tomorrow's winners need a clear channel strategy; yet few except Tesco or Amazon have one.

Robert Shaw,
Honorary Professor of Marketing Metrics,
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Productivity in a competitive world

From Mr Martin Beresford.

Sir, Clive Crook correctly states that "if US productivity rises, so will US living standards" ("Economic growth is not a race to the moon", Comment, January 31). But it is not so clear that there is "no reason at all" why growth in India or China should affect US productivity, or that international competitiveness is not to at least some extent a zero-sum game.

Raising productivity in the US or any country entails both capital deepening (building capital stock per person) and capital upgrading – a process of continually exiting or upgrading sectors with low productivity and redeploying assets to sectors where productivity is higher. If the US loses market share of such high productivity sectors then its ability to continue upgrading its industrial structure – thus raising its average productivity – will be surely impaired.

Martin Beresford,
San Francisco, CA, US

Temptation to cut legal corners is a threat to markets

From Mr Roger McCormick.

Sir, Gillian Tett's thought-provoking article "Geopolitics is final piece in the tormenting jigsaw of risk" (Global Insight, February 3) does not mention one of the more important risks requiring management in the financial markets – legal risk.

This has three principal facets: change in law risk; adverse claims risk; and documentation risk, the risk of failing to appreciate the impact of what you are signing. It is a risk that has generally been overlooked and underappreciated by the regulators and the regulated, which is surprising – given its close relationship with reputational risk and political risk.

Management of legal risk should, one might think, be straightforward. But experience keeps providing extraordinary case studies of failure.

To take just one example, the crisis has shown that even the chief executives of major investment banks seemed to have only a tentative grasp (if any) of the significance of rehypothecation rights and "rights of use" in prime brokerage and comparable documentation.

Only when "client assets" started to disappear into the maw of the Lehman administration did the awful consequences of such provisions start to become apparent. Now, the consequences of such risk management failures include regulatory proposals that make significant inroads into the old mythology that in these "sophisticated" markets the professionals can be trusted to know what they are doing.

The temptation to cut corners, to seek out only "convenient" legal advice when a dubious course of action is contemplated, can have overwhelming appeal – in a variety of contexts. It is time legal risk management was given more prominence in the lexicon of bank corporate governance.

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mob finds it hard to migrate