Stages of life of an investor

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HUMAN capital along with financial capital comprises total wealth of an investor. The present value of future labour income is called human capital and financial capital is the stock, bond, FDR etc where an investor traditionally puts his wealth.

While making asset allocation to different financial assets, an investor usually not only forgets to consider his human capital which is a major portion of his total wealth; also exposes his total wealth to high volatility for not considering the correlation between his human capital and financial capital.

Composition of human capital and financial capital of an investor also considerably differs over the stages of an investor's life. So, understanding the different stages of life and taking human capital into consideration while making investment decision lead to sound wealth management and balancing risk factors associated with human and financial capital.

If we observe the life stage of an ordinary investor from the perspective of different phases, he passes through the chronological stage of foundation, accumulation, maintenance and sometimes distribution stage.

An investor starts his journey from the foundation stage. Acquiring the marketable skills, laying the foundation of business or taking educational degree and achieving different certifications can be regarded as the seed bed of an investor's foundation stage.

Where the basement of a building is used as ground block for building upper floors, here in foundation stage, an investor ploughs and weaves the seed bed for his future wealth creation in life.

The higher the amount of education, expertise or skills he has the greater human capital he possesses.

In this phase of life, an investor is usually young and has theoretically above average risk tolerance for having long remaining work life and higher expected income.

Different types of liquidity driven events like marriage, new born children, aspiration of better life create more willingness to take risk but the capacity to bear the risk remains usually low.

In this early earning stage of life, human capital remains highest and financial wealth is usually at low point. So increasing investment in financial capital such as stocks according to risk tolerance will make a better composition of total wealth in foundation stage.

In the meantime, education, skills, degrees and certifications already acquired and achieved by the investor start yielding return and help him accelerate his income, salary or wage level.

This stage is called the accumulation stage of human life. Size of financial wealth increases at this stage, when the investor's higher savings are converted to financial asset through different financial instruments like stock, bond, FDR or other saving instruments.

Return from those financial assets accumulates but ironically, power of human capital starts decreasing. Home purchase, health care, marriage and education of children increase the liquidity need at the first phase of accumulation stage and consequently the growth of financial capital remains slow; but coming to the second phase of accumulation stage, financial capital captures big portion of investor's total wealth.

As the investor is now at the pinnacle of his carrier, his saving naturally increases from lower expenditure need as dream home has already been bought and children has already been educated and got married. Risk tolerance is still very high for relatively long time horizon of career and higher income prospect.

Financial capital dominates total wealth and human capital starts rapidly decreasing. The investor can gradually decrease his exposure in risky financial assets like stocks in the later phase of accumulation stage and increase wealth exposure to fixed income assets like bonds and FDRs.

Third stage of life is the maintenance phase and the investor is now on the verge of retirement. As investor is approaching to his retirement, his risk tolerance capacity declines and preservation of his real value of wealth after adjusting the inflation and maintaining expenditure need becomes his prime concern.

As wage earning power or human capital of the investor gets largely depleted in this stage, now major portion of total wealth is financial capital accumulated over the years. As the time horizon is very short with high dependency on return from existing financial capital, it is very difficult for the retired investor to recover from the large financial loss.

The investor in this stage should substantially reduce his exposure from high risky financial assets like stocks and increase the allocation to low volatile fixed income instruments like bonds or FDRs.

We have already seen how an investor may change the composition of financial capital allocation based on the human capital in different stages of life. Apart from the role of human capital at different stages of life, correction of human capital with financial capital also dictates the investor's exposure to different financial assets.

Just because the investor belongs to the foundation stage of his life and has high willingness to take the risk do not necessarily mean that he should take very high exposure in the risky financial asset like stocks.

His capacity to bear the risk and other factors should be considered. To elucidate the concept; for example, consider two persons, Monir and Mujib who both are finance graduates and are now at the foundation stage of their carrier having same level of initial wealth and risk tolerance.

Monir is employed in a merchant bank as a senior executive where his responsibility is to supervise whole process of initial public offerings (IPOs). Monir's relative income and bonuses fluctuate substantially with the ups and downs of stockmarket as demand for and supply of new IPOs dry up in the cycle of bearish market which directly influences the profitability of the merchant bank.

On the other hand, Mujib is employed as a finance executive in a pharmaceutical company. Mujib faces very little fluctuation in his salary and yearly bonuses as sales and profit of pharmaceutical products experience very low volatility in any market conditions.

In the above case, though both professionals have same stage of life, same level of wealth and same risk tolerance; correlation between salary growth rate and stockmarket returns; and correlation between human capital and financial capital would largely determine how much they will invest in stocks or other less risky financial assets.

In case of Monir, as his employer's (the merchant bank's) income is highly influenced by stockmarket cycle and performance, Monir's salary and other monetary incentives like promotion and bonuses also hinge on the stockmarket's condition.

On the other hand, Mujib gets trend growth in his salary which has negligible link to financial market fluctuation. So, Mujib can take more exposure to equity as his salary has the nature of fixed income; but here Monir can reduce his allocation of financial capital from stocks and increase his investment in bonds and FDRs to diversify this financial capital.

The logic is that Monir has indirectly invested in the stocks because the human capital or labour income of Munir is directly influenced by the ups and downs of the stockmarket. As we know that total wealth of an investor is composed of both human capital and financial capital; so balancing human capital with financial capital at different stages of life and considering correlation of human capital with stockmarket will help an investor make better and diversified wealth management.

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Euro crisis is race against time

HUGO DIXON

SOLVING the euro crisis is a race against time. Can peripheral economies reform before the people buckle under the pressure of austerity and pull the rug from their politicians? After two months of optimism triggered by the European Central Bank's plans to buy government bonds, investors got a touch of jitters last week.

The best current fear gauge is the Spanish 10-year government bond yield. After peaking at 7.64 percent in late July, it fell to 5.65 percent in early September. It then poked its head above 6 percent in the middle of last week because there were large demonstrations against austerity; because Mariano Rajoy's government was dragging its heels over asking for help from the ECB; and because the prime minister of Catalonia, one of Spain's largest and richest regions, said he would call a referendum on independence.

But by the end of the week, the yield was just below 6 percent again. That's mainly because Rajoy came up with a new budget which contains further doses of austerity. The move prepares the way for Madrid to ask for the ECB to buy its bonds and so drive down its borrowing costs.

Rajoy didn't want to be seen to be told to do anything by his euro partners. Hence, this elaborate dance -- where he has now done what he knew he would have been told to do but can claim it was his choice. It's hard to believe that anybody is fooled by this subterfuge; indeed, from investors' perspective, it looks childish. But, at least the show is on the road again: the government has had the guts to press ahead with reform despite the immense unpopularity of the measures.

AFP

A woman enters a branch of the Emporiki Bank in Athens. Credit Agricole said it was in exclusive talks to offload its Greek subsidiary Emporiki to Greece's Alpha Bank, under terms which would see the French bank first pumping more funds into the ailing lender.

The question is whether Madrid and other governments in Lisbon, Dublin, Rome and Athens can keep up the reforms long enough to restore their economies to health. That, in turn, depends on three factors: how much farther they have to travel; how unruly their people are going to get; and how much help they will receive from their partners.

Economic health requires both that fiscal deficits are eliminated and that competitiveness is restored. The peripheral economies have made some progress on both fronts. But shrinking economies makes it hard to balance their budgets while fiscal squeezes undermine growth. The austerity vicious spiral is still whirring away.

That's why Spain is unlikely to hit its target of cutting its deficit to 4.5 percent of GDP next year. It can get there only on the optimistic assumption that the economy will shrink by just 0.5 percent in 2013. The same could be said of France, not yet a full member of the periphery, whose budget unveiled last Friday calls for a deficit of 3 percent of GDP next year. Paris is assuming 0.8 percent growth. The French prime minister describes the projection as "realistic and ambitious". Just ambitious would have been a more accurate description.

Meanwhile, restoring competitiveness is painful because it involves cutting people's pay. Ireland and Spain have made good progress, covering respectively 80 percent and 50 percent of what they needed to achieve by the end of last year, according to a report last week by Open Europe, a British think-tank. Portugal and Greece have done less well.

Current account deficits paint a similar picture. Spain's had shrunk to 3.5 percent of GDP last year while Ireland actually had a small surplus. Portugal, though, had a deficit of 6.4 percent of GDP and Greece was struggling with one of 9.8 percent.

Big falls in pay are forecast for the deficit countries over the next two years by Eurostat. It sees unit labour costs dropping 4.7 percent in Spain between end-2011 and end-2013; 3.8 percent in Portugal; and 9.5 percent in Greece. If that happens, competitiveness could be restored. Citigroup forecasts that Spain and Portugal will have current account surpluses next year while Greece's deficit will have shrunk to 2.8 percent.

The snag is that such pay cuts -- especially when combined with higher taxes and rising unemployment -- provoke howls of outrage from the population. Short of leaving the single currency and devaluing, the only other medicine for improving competitiveness is so-called fiscal devaluation. This involves cutting the social security contributions paid by employers and, in return, putting up other taxes.

Germany succeeded in pushing through such a fiscal devaluation in 2007. But that just made it more competitive vis-a-vis the weaker euro zone economies. More recently, Spain did a mini fiscal devaluation. But the most ambitious attempt, by Portugal, provoked such a massive backlash earlier this month that the government backed down.

Help from abroad is the main way of easing the pain of adjustment. The ECB's promised bond-buying plan is the most dramatic example. But solidarity has its limits. There has been a backlash in the German media over the central bank's plan. Meanwhile, Berlin has been trying to persuade Madrid not to ask for help. The German finance minister also clubbed together with his Dutch and Finnish counterparts last week, proposing rules that will make it harder for Spain to shift the cost of bailing out its banks onto the euro zone.

The consequences of a breakup of the euro zone would be so ghastly for both the periphery and the core that they will probably pull through what looks like it is going to be at least another year of hell. But the risks have certainly not vanished.

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Employee unrest hits flights at Kingfisher Airlines

REUTERS, *New Delhi*

LABOUR unrest forced ailing Kingfisher Airlines Ltd to cancel flights on Monday, the latest blow for a carrier scrambling to find an investor and sending its shares down by their daily limit of 5 percent.

Kingfisher said it was cancelling several flights, but a top official at the aviation regulator told Reuters that no Kingfisher flights were operating as of midday on Monday.

Kingfisher, controlled by liquor baron Vijay Mallya, had already grounded most of its fleet as of earlier this year.

"A section of employees of Kingfisher Airlines has not been reporting for work over the last fortnight and over the past two days, they have been threatening and even manhandling the other employees who are reporting for work," Kingfisher spokesman Prakash Mirpuri said in a statement on Monday.

All Kingfisher flights scheduled to depart from the Delhi airport until 4:30 p.m. (1100 GMT) had been cancelled, the airport's website showed.

"We are considering, examining the whole situation," Arun Mishra, the Director General of Civil Aviation, told Reuters.

Under Indian rules, an airline needs to operate at least five planes in order to maintain its licence.

Kingfisher, which has been months behind on salary payments, has seen its operations disrupted several times by fed-up employees, although until the recent incident there had not apparently been any reports of violence.

The Mint newspaper reported that the airline's ground staff had refused to attach an air bridge to a plane in Mumbai on Sunday, stranding passengers onboard, while some engineers "beat up" an executive, the newspaper said, citing two unnamed sources.

Mirpuri did not reply to phones calls and text messages.

Kingfisher is saddled with $1.4 billion debt and banks have refused to lend it more unless it can infuse fresh funds into the airline. The carrier, which has never turned a profit, has seen its domestic market share fall from second place last year to last among India's six main carriers.

"I must have been crazy to have booked tickets on Kingfisher. I don't know what to do now," Bilal Ahmed, 29, who is due to be married on Wednesday in Srinagar, told Reuters at Delhi airport, where his flight had been cancelled.

Last week, its banks held inconclusive talks about the carrier's turnaround plan and will meet again this month.