

# If you want to know why pension funds should invest in ...

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I have been [arguing for well over a decade](#) that pension funds should be focussing their investment efforts on long term bonds issued by local authorities, government and related organisations who use the capital entrusted to them to invest in long term infrastructure such as housing, transport, hospitals, schools and so on.

My logic has been twofold. The first is that there is a real, but unwritten, inter-generational contract regarding pensions as a result of which one generation agrees to leave enough real capital for use by the next generation in exchange for that next generation giving up part of its income to maintain those in retirement. Capital in this sense is real, tangible stuff that the next generation can use that means they can afford to give up current income to maintain the elderly - because that is exactly what we ask them to do via the pensions system.

We've forgotten this and so instead invest pension funds in what are largely intangible assets. Intangible assets are, as it says on the tin, by definition not real. That's because they represent the current value of the excess price that can be charged to future consumers as a result of the legally enforced premium that can be charged to them for the value of current inventions. In other words, intangible assets only have value because they represent the exploitation of future consumers.

The trouble is, those future consumers are the very people who those about to retire want to forego income to keep them in old age. So investing in intangible rather than tangible assets represents a double whammy on the young who need to support the next generation: we do not leave them the real capital they need if they are to forego income to keep us in old age and we also seek to reduce their future income by charging excess prices for the benefit of past economic activity, all at the same time. That's a recipe for pension disaster.

But there's a second reason why this is also guaranteed to fail. As [the FT noted yesterday](#), stock markets are dire at picking out which investments to pick. Just over 10% of all active stock market managers beat the market in 2014 in the USA. Randomly you would expect half to do so. That has not happened since 2009. And that's before

paying for the costs of these managers who get their judgement on which intangible assets to invest in (because that's what most company shares represent) so spectacularly wrong.

What is more, of the best 25% of fund managers in 2010 almost none remained in the top 25% in 2014. So getting this selection right once is no guarantee at all of doing it again.

In that case investing in intangible assets makes no sense at all for pension purposes.

But requiring pension funds to invest 25% of all their contributions in infrastructure that creates new jobs in exchange for the tax relief they get would not just be good for the economy - [which would be beyond dispute as it would give a £20 billion boost each year](#) - but would also be fantastic for the stability of pension fund returns whilst seriously cutting the costs of pension fund management. And it would also respect that fundamental pension contract between generations.

But the City will fight it tooth and nail. Which is why, no doubt, such a radical, and essential, pension reform is not on the political agenda right now. Feeding the myth of the City is more important, of course.