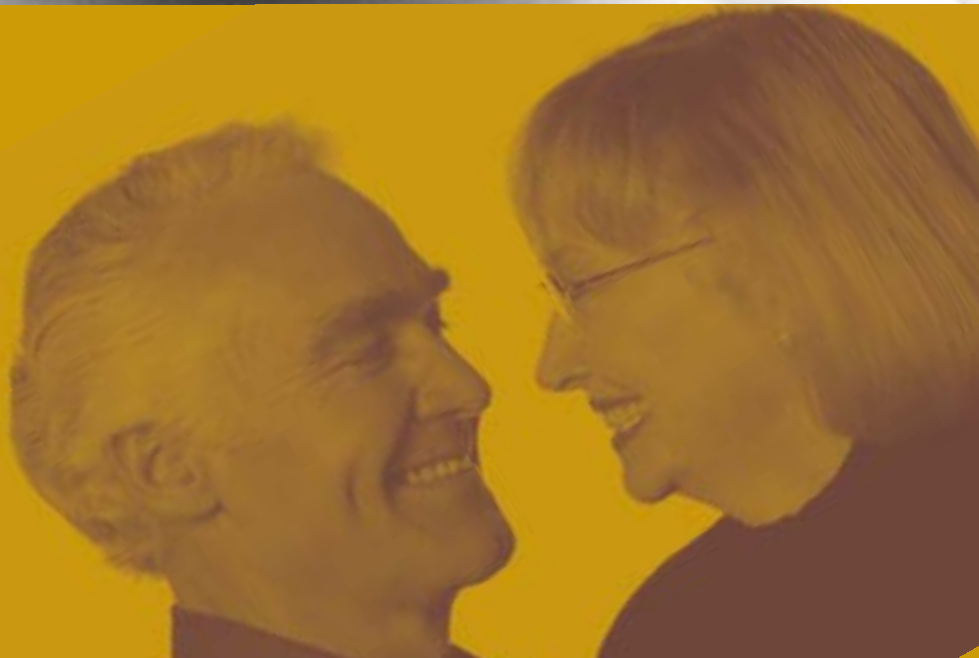


**WHEN BABY  
BOOMERS  
RETIRE...  
MARKETS  
TAKE NOTICE**

*By Jill Kerby*



In America, economists call the original post war babies the 'Baby Boomers'. Then there is the 'Baby Bust' or 'Xer Generation' which was born between 1964-84 and finally, the Echo Baby Boomers – the progeny of the two earlier generations, the ones who we hope will take care of us all in our old age.

The first group of boomers will start retiring soon, perhaps even next year when the oldest turn 60. I have a brother in Canada in this group, who owns his own travel and cruise business, but has transferred much of the day to day running of the business to his daughter so that he and his wife can travel more themselves. He will be funding his early semi-retirement, he says, by taking a smaller salary, but also by cashing in certain pension funds and retirement accounts.

#### HE ISN'T ALONE.

In the United States there were 79 million babies born between 1945 and 1964; in Canada, about six million. Millions of others were born in the UK, where higher income baby boomers also have substantial stock market related occupational and private pension funds. I too will begin contemplating my own retirement around 2016; the 'Bust' and 'Echo' babies will only start to retire between 2024 and 2030.

The questions that more and more people are beginning to ask is what impact the drawing down of retirement assets will have on the stock market and our respective economies. And will the Xer generation and the echo boomers be able to afford to retire at all in the wake of the original baby boomers?

The argument in the United States – led mainly in the halls of academia - and Wall Street about the impact of mass retirement between 2010 and 2024 goes something like this: demographic forces have always had an impact on the performance of the stock market indicated, for example by the fact that the decline in the stock markets in the 1960s and 70s may have had something to do with the fewer people born during the

years of the Great Depression. A demographic dip, they claim can cause a similar glitch in equities.

Relate this to the current demographic/stock market situation and a similar pattern has developed, say economic researchers Geanakoplos, McGill and Quinzil in their 2002 model "Demography and the Long-run Predictability of the Stock Market".

The fact that the Xer and baby bust generations have each produced 10 million plus fewer people suggests to them that there will be an impact on stock market investment, though it does not mean that "the market is going to suddenly get cut in half or something," Geanakoplos is quoted as saying. "But it does mean that that demography is going in a bad direction for the next 20 years or so."

It is the combination of fewer investors coming behind, baby boomers selling off their stocks, and our unsettled times that has Wall Street analysts and even a few of our own worried (see sidebar). Only a few are predicting a market 'meltdown'. Most, supported by economics like James M. Poterba, in his paper "Demographic Structure and Asset Returns," Review of Economics and Statistics, say that not only is the retirement period of the boomer generation spread out enough to have an insignificant impact on prices, but the evidence is already showing that the earliest boomers are not behaving as they were expected to: they are not selling assets, not even their homes. (Something previous generations have done in a down-sizing operation).

If anything, suggests Poterba, many are still buying shares and accumulating more wealth. When they do begin to retire, the ones who have accumulated substantial assets in wealth (and it is only a very small number of boomers who dominate the market) will do so in a way that probably protects their own portfolios. This is because they will want to protect themselves from encashment tax liabilities and to fully enjoy the fact that CGT tax changes in the US mean it makes more sense to keep a dividend stream flowing.

As for the demographic problem – fewer people around to continue investing in the market over the long boomer retirement period optimists say that higher birth rates from a still growing emigrant population, means economic growth will continue. Even if there are insufficient domestic buyers of the baby boomer's stocks, there should be eager buyers in countries that will be trading with the US in sufficient levels to afford to buy US securities.

The problem with that argument, say detractors like Jeremy Siegal, an economist at the University of Pennsylvania's Wharton School of Economics, is that such a massive shift of capital ownership would also cause "a huge shift in the global power structure." 'Uncertainty' is not a friend of the markets.

Economists agree that there will be some effect on US share and bond prices – with a knock-on effect on global assets – when the baby boomers begin to retire. It is the size of the price fall that is up for grabs, with the optimists saying it will be relatively slight, perhaps no more than a half percent.

It is the longer term effect of the demographic shift that has others more worried, specifically that the longer life expectancy of the boomers will worsen any downturn in security prices. The ratio of retirees to workers will soar over the next 50 years and this higher dependency ratio brings with it the risk of higher taxes as governments struggle to meet the costs of supporting a larger non-working population.

Already, the signs are there that the post boomer generations are not investing in the markets with the same zeal as the previous ones; typically for their generation they are more concerned with buying a property and, unlike the earliest boomers, with lifestyle spending. A combination of these different spending patterns, stock market volatility, the demographic shift, global political unrest and higher government debt suggests that there will be an impact on the markets.

Some prominent US financial analysts suggest that the consequences could mean a stagnation of the financial market for the next quarter century.

The impact of falling birth rates and greater longevity on the wealth of nations is in the public domain, but in a newly published report, "The Western World Past Its Prime - Sovereign Rating Perspectives in the Context of Aging Populations" the rating standards agency Standard & Poor's are predicting that the pressure of ageing populations in OECD countries will be so intense over the next 50 years that unless major structural reforms are adopted soon, "Sovereign ratings could come under strong pressure as early as the end of this decade".

According to the report, the debt ratio of the typical country would rise to 139% of GDP by 2050, from 47% in 2010, and fiscal deficits as a percentage of GDP would reach double-digit figures. Most of this deterioration is, however, to come only after 2020.

Continental European countries such as France, Germany, Portugal, Greece, Poland, and the Czech Republic will have debt burdens exceeding 200% of GDP by 2050 while Australia, Sweden, the U.K. and ourselves will manage better, even without significant further reform though in our own case our public debt burden will rise to 65% by 2050. Japan's debt burden could reach 718% of GDP.

S&P predict "that initially, at least, the pressure from age-related spending will remain very moderate. But starting around 2015 the burden will gradually rise, leading to worsening fiscal indicators." Assuming unchanged policies by governments to address this issue, sovereign ratings "could come under downward pressure as early as the end of this decade. This would continue until the mid-2030s, by which time the vast majority of countries would display fiscal characteristics that today are associated with non-investment-grade sovereigns."

The collapse of the credit ratings of whole countries is a very dark outlook indeed and presumably would have dire consequences for investment markets and the retirement prospects of more than just the post-war baby boomer generation. Standard & Poor's do not expect the sky to fall in however.

"It is unlikely that governments will allow debt and deficit burdens to spiral out of control in the manner outlined," the report concludes. "Nevertheless, the scenario indicates the dimension of the problem that governments face in pruning benefits granted by unfunded state-run social security systems and achieving further fiscal belt-tightening."

The baby boom/demographic argument could be seen as something of an academic exercise when observed from our island republic. We have one of the

youngest populations in Europe; our unusual demographic pattern of population stagnation and high emigration throughout the 20th century means there really is no 'baby boom' generation to rock the stock market. Most analysts agree that retirement of 60 year olds in the next few years will have no consequential impact on any market.

Our problems will come later, says consultant Jenny Logue of the forecasting consultants Amarach. Her research into the spending and lifestyle patterns of young to middle age consumers in Ireland confirm other studies which show that not only is retirement underfunded here but that the vast majority of AB and C income categories rely solely on not just a single salary but both salaries to meet their lifestyle costs. One in six already rely on their investments to supplement their current incomes.

"It is clear, that regardless of household income, most [middle age groups] are running hard to stand still," says Ms Logue. "For example the number of high earners is equivalent to those who have considerable outgoings in the form of higher than average mortgages, monthly grocery expenditure and / or childcare costs. Likewise over half agree that their outgoings just seem to keep rising faster than their income. This is reflective of the continued high cost of living in Ireland. In the context of younger age groups becoming more involved in the housing

Pramit Ghose may be too young to be a 'baby boomer', but Bloxham Stockbrokers' head of investment strategy reckons the impact of so many of them retiring in the US within a relatively short time-frame needs to be carefully considered by Irish trustees right now.

"The pattern of equity buying will change as the baby boomers turn from being net buyers of stocks to being either neutral at best, moving their portfolios into bonds and cash, or become outright sellers."

The generation coming behind them – the older ones at least - are buying shares now, he says, but the picture will be less rosy for the 20 and 30-somethings who are not only being forced to

spend higher amounts on property than their parents, but "they have already had a bad or worse experience of shares than their parents. I can hear them say, 'Shares? Go away. I had Hewlett Packard and Cisco a few years back and lost a bucket. I'll stick with property.' And yet I think these people are going to get a nasty surprise in the next few years as property returns prove to be very disappointing."

What Mr Ghose predicts will happen in the US market as the retirement boom gets underway - "and this is a favourite topic of mine - is that you will get more 'yield'. We're very successful at getting people to buy our high net fund on the percentage of yield it produces in dividend growth. I suspect you will get this change in the US investment psyche with people looking for more

market, and hence having mortgages considerably higher than the current average, coupled with lower salaries than their older counterparts, it is inevitable that this squeeze in terms of day to day living will become considerably more pressing."

Home ownership is high among Ireland's baby boomers, such as they are: eight out of 10 ABC/F1's in the 55-65 age group do not have a mortgage, say Amarach, but there are "still in excess of 40,000 ABCs / F1s spending more than €1,000 per month on their mortgage (or rent in a few cases) – most of which are skewed towards those under the age of 45."

We may not have the same share ownership track record as the Americans, but the same property ownership/spending patterns seem to be apparent here, with the older generation holding considerable more property asset wealth than the generation coming behind who are finding the financial burden of getting on the property ladder much heavier.

The Amarach study into our attitudes towards wealth also shows that aside from "obvious products such as insurance, regular savings accounts, SSIA's and mortgage protection (for those who have a mortgage), penetration of financial products is relatively low amongst ABCs / F1s." The main reasons could be "The financial savviness of Irish people in general is not as great as

financial institutions might otherwise believe, and based on net incomes and total outgoings there is strong evidence that little is left over for diverse financial commitments other than the very obvious (i.e. insurance), or the very simple (i.e.: regular savings accounts), or the very attractive (i.e. SSIA's). "

The study also found that "it is very much the minority who have shares, PIPs, investment funds and tracker bonds etc. with those who do have them tending to come from AB households."

As for our attitudes towards retirement, Amarach found that "there appears to be a general sense of confidence", however misplaced. Four in ten ABCs / F1s and six in ten 25-34 year olds do not have a pension plan.

"Of those who do not have a pension / pension plan," says Ms Logue, "the majority do not seem to have any intention of rectifying this situation anytime soon. When one considers the considerable amount of assets that this cohort possess (eight in ten own their houses outright) it is clear that a head in the sand attitude is fairly pervasive throughout."

Our lack of concern about what the future holds – for all ages – probably has a lot to do with our lack of participation in the global stock market adventure of the last two decades and the fact that traditionally, Irish people rely far more on property than

equities for any financial security they may have.

US economists, even the very pessimistic ones, at least share the view that no one working today should be putting all their investment eggs in a single basket. They predict that the great Baby Boom retirement experience, which will last for next 25 years, will undoubtedly be less serious if both the late boomers – those of us still in our 40s, and the Baby Bust generation coming behind - make an effort now to compensate for any lowering of share prices, a higher tax burden, and worsening government debt positions.

They suggest that stock portfolios – pension funds mainly – be well diversified in both the makeup of the assets as well as their sectoral and geographic distribution. We boomers need to own other assets like cash and property, to be more conscious of our health and to even consider more flexible careers and the idea of working a lot longer.

To paraphrase one US analyst: "The worst thing would be to open your [pension] statement when you're 65 or 70, and say, "I need to go back to work."

By that stage, it may be too late to make that kind of choice.

dividend yield growth. The markets will need to do something to keep people invested. I expect we'll see this shift over the next four or five years."

Irish pension trustees should be examining the diversification of their schemes' portfolios right now, says Pramit Ghose. Advisors and their clients who are retiring and investing in ARF's, are already looking carefully at higher yielding dividend shares, he says.

He is also concerned that there isn't enough understanding by Irish trustees of the implications of the retirement of the baby boom generation on share values or wider economies, including our own. What happens in American markets will have global repercussions, he says, and on that subject, diversification

should also take into account the global demographic shift, away from the old economies of the west towards the fast developing ones of the east which have growth, young populations and "underowned stocks where there is only one way traffic at the moment."

Irish trustees, whose members will inevitably feel the repercussions of whatever shift happens in the US markets between now and 2024, "need to look at other ways to add value and no longer blindly invest in equities because the Dow happens to be up," he says. "And they seriously have to look at alternative investments and markets."