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Commentary

BY FRENCH HILL

The Good News Is ...

IN HIS 1993 BEST-SELLER *THE Great Boom Ahead*, Harry Dent correctly predicted a "rosy" stock market during the 1990s, based primarily on demographic trends and the spending cycle of the baby boom generation. However, Dent's book also called for a 15-year depression to begin in 2008. The premise for this gloomy prognostication is his belief that the financial markets will be thrown into disarray as baby boomers begin liquidating their financial assets to generate the funds necessary to maintain their lifestyles.

A baby boomer is any American born between 1946 and 1964. The boom in births following World War II produced 78 million Americans who today account for 25 percent of the U.S. population. Many are on the verge of retirement. Authors such as Dent have stirred up a lot of investment commentary as to whether the market will face a dramatic sell-off as the boomers retire. This debate has generated so much attention that the federal General Accountability Office released a report in July analyzing the future economic impact of the baby boomers as they reach retirement age.

The GAO report is more upbeat and contradicts many of Dent's doomsday claims. First, the baby boomers will not all retire at once. The generation's entry into retirement will be stretched across almost 20 years, and the effect of this shift could be further mitigated by the fact that many anticipate working past the age of 65. A 2004 study prepared for the AARP found that approximately 79 percent of boomers intended to "work for pay" during retirement.

Next, the GAO research determined that baby boomers control only 20 percent of our country's financial assets, and nearly 70 percent of these assets are controlled by the generation's wealthiest 10 percent. The report noted that the top 10 percent of boomers own over two-thirds of the $7.6 trillion in U.S. investment and IRA accounts. This wealthy group owns an average of $1.2 million in financial assets and over $2 million in other assets, including home equity. It is likely that the majority of baby boomers will pay for retirement the same way previous generations have — with income generated by, not the liquidation of, their financial assets. The GAO sampled retirees born before 1946 and found that only 16 percent spend more than the annual income generated by their savings and investments. Furthermore, an analysis of 1994-2004 found that 57 percent of retirees who owned financial assets outside of an IRA or other retirement account purchased stocks during the decade. The GAO's analysis did not support the premise that retirees had begun liquidating their equity holdings and reallocating the proceeds to fixed-income investments. According to the GAO, roughly 60 percent of the investments of households over the age of 70 remained in stocks.

The most shocking aspect of the GAO report is how many baby boomers have little or no retirement savings. The fact that the wealthiest 10 percent of baby boomers control the vast majority of the generation's assets may relieve worries about a massive sell-off, but knowing that the remaining 90 percent of boomers control just 30 percent of the assets should comfort no one. It appears that many baby boomers will work — some willingly, others not — well into their retirement years.

This reality carries two important implications. This group is vulnerable to an adverse lifestyle change due to a major illness and the subsequent loss of income. According to the GAO study, only 8 percent of today's 65-year-olds have long-term care insurance, although 35 percent are projected to need nursing home services. Additionally, boomers who are "house rich but cash poor" may be excellent candidates for reverse mortgages that effectively annuitize home equity in the form of a lump-sum or monthly payment.

The bottom line? Baby boomers may lower annual market returns by a fraction of a percent over a 20-year period. The larger lesson, however, is to have a financial plan in place and to take advantage of innovative financial products to protect yourself and your family in the long run. ■

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