



my. It could lead to a depression.

### **Boomers Driving the Market**

Some observers hope that foreign buyers will snap up boomers' stocks, and they may be right. But they haven't explained it in the context of aging populations in all developed countries and the tendency of national economies to become synchronized. Nor have they explained the effects of transferring equities outside of the country. If, for example, younger U.S. workers don't buy the boomers' stocks, they won't be able to use them to forward-fund their own retirements. There's also the control question—what if OPEC interests become dominant stockholders?

The conventional way to value and project the future of stock-based portfolios is misleading. In any other business, things that are bought for subsequent re-

sale are valued in inventories at their cost or market price, whichever is lower. They may have to be marked down but never up, and profits aren't recorded until the things have been sold.

When stock portfolios are marked up to current prices, profits are recorded that have not been and may never be made. If companies did this with business inventories, their earnings reports would be of little use for evaluating their stock prices or creditworthiness. Similarly, marking-to-market renders retirement plan projections meaningless.

The conventional approach is also misleading because it's intended to be used for portfolios whose transactions are too small to have major effects on the market. But when all boomers' retirement plans follow essentially the same strategy at about the same time, they can drive the market. We saw this in the front half of

the cycle, and should expect to see it again in the back half.

Because of the cycle, it's a mistake to use Monte Carlo techniques to project the future of portfolios. Boomers introduced a major wave into stock prices just as they did to school systems. As the wave passes, the future will be neither random nor unpredictable. If allowed to play itself out, it can be like the years 1982–2000 played backwards, but without the tech bubble.

### **Analysis Needed**

Population aging is more than a financial problem; it's a physical reality. Workers make the national pie of goods and services. Retirees are adults who consume slices of the pie without helping to make it. Nearly all financial retirement schemes, including Social Security and plans that will have to sell stocks, just transfer income from workers to retirees so they can consume slices of the pie they no longer help to make. What retirees get, workers do without.

There are limits to the amount of income workers will transfer to retirees, and if stocks are the vehicle for making the transfers, stock prices will be determined accordingly. Thus, true retired independence is an impossible dream for all but the wealthy few who can live on their interest and dividends without having to sell assets.

We know about the Social Security problem because of its 75-year projections. There would probably be no thought of privatization if there was a comparable projection of how the sum of all the country's stock-based retirement plans will function when the baby boomers retire.

It's important for professional organizations, business schools, companies, and others to do their own analyses of the stocks-for-retirement cycle and compare their findings. The analyses should treat all the stocks in retirement portfolios as a single national inventory of things to be sold by considering the size of the inventory, the timing of the sales, the prices

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needed to pay for retirements, and most important, the potential purchasing power available. This can be done as a rough cut that would not be expensive or time-consuming. Even accuracy of  $\pm 50$  percent would be revealing.

If the analyses show how the stocks-for-retirement cycle can work, that will be great news. But if they don't, boomers and their advisers must reconsider the retirement dream world. Regardless of one's car, the time it takes to drive into or out of a major city is largely determined by traffic. In addition to unpredictable tie-ups, there are patterns that change with time, weather, and seasons. The analyses can show the equivalent of traffic patterns to help actuaries advise their clients, who will have little choice but to go with the flow.

If the cycle does fail, it can have disastrous effects for actuaries and others who advise on investments and retirement planning. As shown by asbestos, auto, tire, tobacco, and other industries, what a company does after it learns of a product problem is critical to its future. Because articles like this one and related books have been published for at least eight years, the financial services industry is working toward the right-hand end of the could-have-known, should-have-known, surely-did-know scale. The significance of that should be obvious to those whose product is advice to clients.

But if the cycle is flawed, the full range of changes that may have to be made is less obvious. Clearly, many boomers who live longer will have to help make the national pie for more years. In addition to boomers whose retirement plans may fail, millions of others are not saving for their retirements and will have to work regardless of what stocks do. Just saying that suggests a few possibilities:

- Investments will be required to provide jobs for boomers whose skills may be obsolete or whose capabilities may be declining—just the types of investments and jobs public companies are eliminating to cut costs.

- Today, public companies are driven primarily to inflate their stocks. This will become impossible if boomers' retirement

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plan sales depress stocks for years.

- If companies can't inflate their stocks they'll need new goals. They may find that dependable pay and benefits are outputs to increase rather than costs to reduce.

- If stocks can't be inflated, capital will be harder to create so it will have to be used more wisely. Instead of investments being measured only by their rate of return, they may also be measured by the quality of their return, or what they contribute to society. This may require new intermediaries to manage capital in ways that are very different from today's pension and mutual funds.

- Following the Organization for Economic Cooperation and Development's concept of "active aging," retirement plans may help older people gradually shift from work to retirement at their own pace over extended periods.

- As people live longer, they decline at different rates. Retirement ages and income may have to be based more on individual needs than blanket eligibility. This will raise many questions about individual desires, freedoms, and responsibilities.

- Industries that expect well-to-do boomers to buy lavish homes and other amenities may instead find their customers are millions of older people with modest incomes.

There is, however, a bright side to all this. Unlike the costly changes the country will make as it emerges from its dream world and fights terrorism, the changes needed to provide for America's aging pop-

ulation can do a world of good—literally.

Few people understand the damage that has been caused by the massive buying of stocks for growth by pension and retirement funds. The managers of those funds passed the pressure for growth on to companies that responded by cutting costs, downsizing, laying off domestic workers, merging, and generally treating customers, employees, suppliers, communities, governments, and the environment as resources to be mined—all to inflate stock prices.

A fair amount of public discord can be traced to these actions. It's more than a coincidence, for example, that resistance to affirmative action grew as companies eliminated or exported semi-skilled jobs. Similarly, many issues raised in protests against the global economy are directed at large and often American companies.

It's both optimistic and realistic to say that if stock-based retirement plans are flawed, the changes that will have to be made offer huge opportunities to improve society. But it's only realistic to say that in order to enjoy the opportunities, the country must recognize the need and begin making changes in time to prevent a disaster. If we wait too long, as we did with terrorism, and a disaster happens, many opportunities will be lost forever.

The first step must be to analyze all stock-based retirement plans to see if they're realistic or just dreams. If they are dreams, America has more waking up to do. ●