

0.59% ▲

-0.27% ▼

2.854% ▼

-2.56% ▼

-0.91% ▼

This copy is for your personal, non-commercial use only. To order presentation-ready copies for distribution to your colleagues, clients or customers visit <http://www.djreprints.com>.

<https://www.wsj.com/articles/the-surprising-good-news-about-demographics-and-the-stock-market-1517800441>

## JOURNAL REPORTS: FUNDS &amp; ETFS

# The Surprising Good News About Demographics and the Stock Market

Millennials could step in for the boomers in the stock market, defying the conventional wisdom—and boosting equities



Demographics will be a positive for stocks until 2035 (of course, with jarring market declines along the way). ILLUSTRATION: ROBERT NEUBECKER FOR THE WALL STREET JOURNAL

By Mark Hulbert

Feb. 4, 2018 10:14 p.m. ET

Everybody knows the conventional wisdom that the demographic trend these days is not a friend of the stock market. The baby-boom generation, we've been told, is moving into retirement, and selling stocks in the process.

The conventional wisdom, though, is no longer as accurate as it used to be.

---

## JOURNAL REPORT

- Insights from The Experts
- Read more at [WSJ.com/FundsETFs](http://WSJ.com/FundsETFs)

---

## MORE IN INVESTING IN FUNDS & ETFS

- Good Fund Managers Start in Kindergarten
- U.S.-Stock Funds Rose 4.4% in January
- Are Zero-Fee ETFs on the Horizon?
- Investor Quiz: The Fiduciary Rule
- College Finance Q&A

Credit the baby boomers' children, the so-called millennial generation born in the 1980s and 1990s. The millennials are entering the period of their lives in which they increasingly will be investing heavily in the stock market, and according to the leading economic model that relates demographic trends to the stock market, they are a big enough generation to overcome the bearish impact of the baby boomers' retirement. In fact, according to this model, demographics will be a positive for stocks until 2035 (of course, with jarring market declines along the way).

### Validity of the model

Some might question the validity of this model, put forth in a seminal study in 2002 by a handful of professors in finance and economics. But the model is consistent with the performance of stocks during periods that cover most of the 20th century. And it successfully predicted the relative weakness in stocks for the years from 2000 to 2016.

The performance of stocks from 2000 (when the demographic trends shifted to being bearish for equities) to 2016 (when they shifted back to being bullish) was well below average—recent all-time highs notwithstanding. Indeed, market strength in recent years only barely made up for the huge losses incurred during the financial crisis and, before that, the bursting of the internet-stock

bubble. On an inflation-adjusted and dividend-adjusted basis over that 16-plus-year period, the Nasdaq Composite lost ground. The S&P 500 produced just a 2.7% annualized return.

That S&P 500 return was less than half the stock market's long-term average of 6.9% annualized. There have been only two other times over the past 90 years in which the broad market's average return was this low: the period from 1929 through the mid- to late 1940s (encompassing the Great Depression), and the one between the mid-1960s and the early 1980s (encompassing the 1973-74 bear market and that era's hyperinflation). That is exactly what the demographic model would have forecast. (See chart.)

### The MY ratio

I wrote a newspaper article about the study soon after it was published, forecasting that the shift in demographics would cause the stock market on balance to struggle until 2016. The study's authors were John Geanakoplos, an economics professor at Yale University, Michael Magill, an economics professor at the University of Southern California, and Martine Quinzii, an economics professor at the University of California, Davis. Though their model is complex, its essence can be distilled to a single number: the ratio of those the authors label as middle-aged (ages 35-49) to those labeled young (ages 20-34).

The model's prediction is that stocks on balance should perform better when this so-called MY ratio is rising than when it is falling. It is this ratio that turned up at the beginning of last year and will continue rising until 2035.

To be sure, the MY ratio in 2035 won't be as high as it was at the height of the internet-stock bubble in early 2000. But Prof. Geanakoplos, in an interview, said that what's important to the model isn't the absolute level of the MY ratio but its trend. And it will be trending upward for the next 17 years.

### Fed hangover

One thing that could temper this otherwise rosy forecast is the hangover from the Fed's market-supporting bond-buying program, known as quantitative easing, or QE. Prof. Geanakoplos speculated that the stock market between 2000 and 2016 would have performed even more poorly than it did but for QE, which in effect "borrowed" some good performance from the future. If so, then average returns between now and 2035 may be somewhat less than they would have been otherwise.

Another unknown is the effect of international trade. The demographic model historically has worked best in countries for which trade represents a small share of GDP, such as Japan, and least well for countries for which trade represents a big share, such as those in Europe.

The U.S. in this regard is far closer to the Japan end of the spectrum than Europe, but nevertheless trade in recent decades has grown as a share of the U.S. economy.

These qualifications notwithstanding, however, Prof. Geanakoplos still puts stock in the demographic model's forecast that the stock market will perform better between now and 2035, on average, than it did between 2000 and 2016.

### No straight line?

He emphasized that the model's long-term bullishness doesn't imply that the market will rise in a straight line. There undoubtedly will be one or more bear markets along the way, after all. But it has to be welcome news to investors that demography can now even be considered as a bullish prop for equities.



One thing that could temper the rosy forecast is hangover from the Fed's market-supporting bond-buying program. PHOTO: ISTOCKPHOTO/GETTY IMAGES

Confirmation that the demographic model is worth paying attention to comes from its success in Japan, a country for which trade represents a small share of GDP and is therefore where the demographic model should be particularly accurate.

Japan's MY ratio has been rising since 2002, and sure enough, the Nikkei Stock Average is nearly triple today where it stood at its 2002 low.

According to Alejandra Grindal, senior international economist for Ned Davis Research, Japan's MY ratio is forecast to continue rising for five more years—until 2022—and then decline for more than a decade.

*Mr. Hulbert is the founder of the Hulbert Financial Digest and a senior columnist for MarketWatch. He can be reached at [reports@wsj.com](mailto:reports@wsj.com).*

*Appeared in the February 5, 2018, print edition as 'The Surprising Good News About Demographics and The Stock Market.'*

---

## JOURNAL REPORTS

---

- **College Rankings**
- **College Rankings Highlights**
- **Conferences**
- **Energy**
- **Funds/ETFs**
- **Health Care**
- **Leadership**
- **Retirement**
- **Small Business**
- **Tech Companies to Watch**
- **Wealth Management**

Copyright ©2017 Dow Jones & Company, Inc. All Rights Reserved

This copy is for your personal, non-commercial use only. To order presentation-ready copies for distribution to your colleagues, clients or customers visit <http://www.djreprints.com>.