THE Weekly View

RIVERFRONT INVESTMENT GROUP

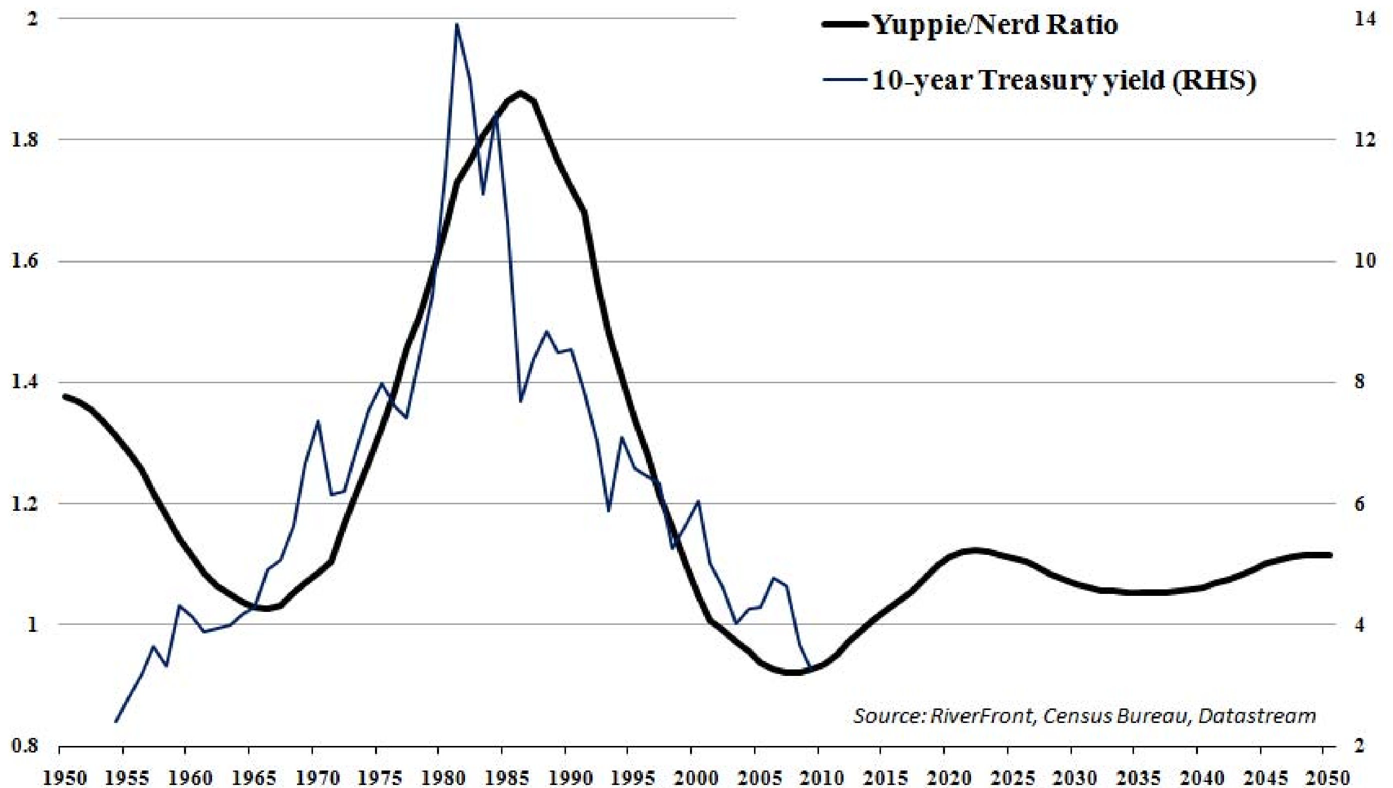
Asset Management • Investment Strategy • Advice

Rod Smyth • Bill Ryder, CFA, CMT • Ken Liu

April 12, 2010

Demographics and Destiny: Boomers Need Yield

- Remember the yuppie/nerd ratio? A client reminded us of it at a meeting last week. It is the ratio of 25- to 34-year olds ('yuppies') to 45- to 54-year olds ('nerds') and was made popular as the baby boomers moved through these two demographic phases. As they formed households, hitting their peak spending years, inflation surged and interest rates consequently rose. Demographers attribute some of that inflation to the spending power of the group bidding up prices. The peaks in bond yields coincided with the boomers entering their maximum earning and investing years – the nerd phase (see chart below). A small resurgence of 25- to 34-year olds – the echo boomers – over the next ten years might imply higher yields. However, with the boomers moving from high-earning savers to retirees needing investment income, we believe the yuppie/nerd ratio is becoming less relevant (see chart on page 2).

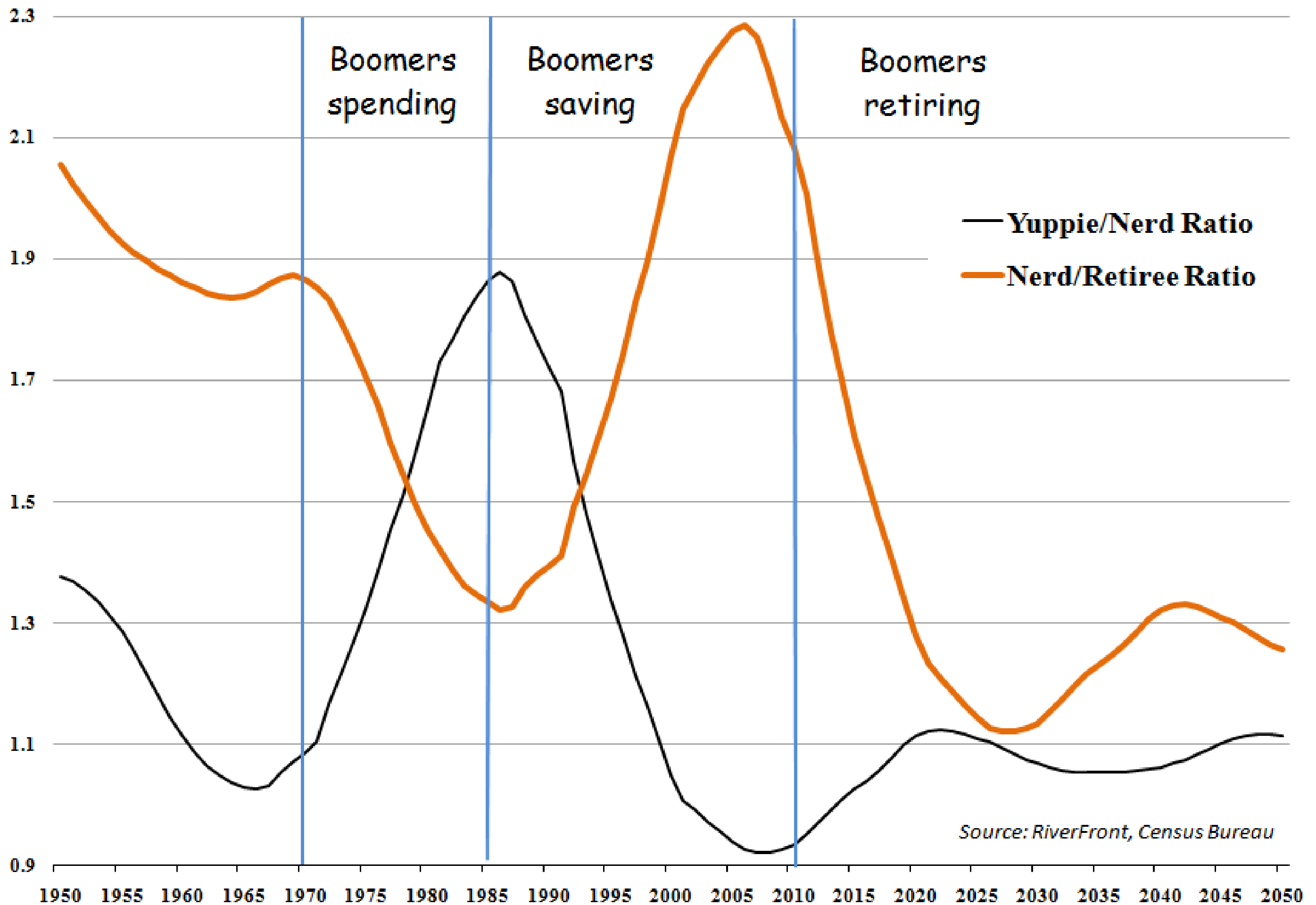


Past performance is no guarantee of future results

- It seems that boomers can usually be relied on to overpay for everything. Thus, between 1982 and 2010 the boomers overpaid for assets: growth stocks during the late 1990s and second homes in the sun during the mid-2000s. Over the next ten years, we think the boomers will overpay for investments with reliable yields, bidding up corporate bond prices and gradually rediscovering the benefits of dividends. Naturally, in retirement, spending and investing habits change as salaries decrease. Leading up to retirement, investors become more focused on capital preservation and the necessity of income streams. Furthermore, given the two major bear markets over the last ten years, many boomers have become disillusioned with stock investing and are attracted to the perceived safety and superior 10-year track record of bonds and even cash.

- Cash has been a dependable haven of capital preservation, but has been a fickle and volatile source of income; yields for 3-month FDIC-guaranteed Certificates of Deposit averaged 5.3% in 2007 but are now less than than 0.5%. Low returns on cash have driven record investment flows from money market funds into bond funds. In our judgment, the buying boom in Treasury bonds is over. Investors are now reaching for the higher yields offered by corporate bonds, but we believe baby boomers will soon recognize the importance of income *growth* to a retirement horizon that will likely span 20 to 30 years. This will cause them to overpay for the stocks of high quality, global franchise, dividend- paying companies, in our view, where earnings can grow along with the world economy and dividend growth will offer protection against inflation. *Dividends are not guaranteed and are subject to change or elimination.*

The Weekly Chart: Boomers moving from accumulation to distribution



Past performance is no guarantee of future results

Our chart shows the ratio of 45- to 54-year olds (nerds) to 65- to 74-year olds (retirees) along with the yuppie/nerd ratio. The rise of 25- to 34-year olds – the echo boomers – relative to nerds over the next ten years might suggest a rise in interest rates. However we think this is unlikely due to the surging number of boomers retiring, which is causing the nerd/retiree ratio to plunge over the next ten years. These retirees will likely overpay for fixed income securities in their search for income; thus helping to offset some of the upward pressure on interest rates, in our view.

Rod Smyth, Bill Ryder, CFA, CMT & Ken Liu • 804-549-4800 • www.riverfrontig.com
RiverFront Investment Group, 9011 Arboretum Parkway, Suite 110, Richmond, VA 23236

Information provided in this report is for educational and illustrative purposes only and should not be construed as individualized investment advice. The investment or strategy discussed may not be suitable for all investors. Investors must make their own decisions based on their specific investment objectives and financial circumstances.