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“Demography and the Long-Run Predictability of the Stock Market”  
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We examine whether demographic fluctuations—baby booms and busts—can provide a unified explanation of the alternating twenty-year bull and bear markets in postwar U.S. equities. We construct a stylized, nonstochastic life-cycle model that recognizes the different income and consumption behavior of households of different ages and assumes that the population age structure follows a twenty-year cycle. In this base model, fluctuations in population age structure similar to those observed in the United States can account for large fluctuations in asset prices. The model’s qualitative behavior is not significantly changed when enriched to accommodate more realistic features such as children, Social Security, and bequests, or when uncertainty in wages and dividends is introduced. In the latter case, the model predicts an equity premium that is larger when stock prices are low, which, unlike the predictions of some rational expectations models, is consistent with the historical record.

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