Fortnightly Thoughts

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Issue 107

Why you need to know more about Gen-X

In this edition of Fortnightly Thoughts we shine a light on the sometimes overlooked, but economically important cohort known as Gen-X. We interview demographics expert Neil Howe and have contributions from our analysts on how the differences of the Xers impacts autos, asset managers, retailers, advertisers and elections.

The generation that is rarely discussed, but accounts for over 25% of consumption in the US, is Gen-X (those between the ages of 36 and 51 in 2016). It sits right in the center of the consumption sweet spot and therefore matters to DM economies.

But it is different from the Boomers. It is smaller and less well off. It has only seen average real income growth of 1.8% pa between ages 34-43 vs. the Boomers at 3% pa for the same age group, and it hasn't benefitted in the way that the Boomers did from asset price inflation. As the average Xer now resides in their mid-40s, time is running out to build up savings.

All of this implies that they won't consume in the same way as the Boomers, partly because they can't and partly because their preferences and attitudes are different. They prioritize spending on their families (children, housing etc.) and are faced with higher costs for things like education, healthcare and property, but they are under-indexing on things like autos.

This generation is also seen as resilient and pragmatic which matters not just for consumption, but also for their impact on the world given that Xers are moving into leadership positons, both within companies and countries.

***EXCERPT*: This report is a modified version of Goldman Sachs Research's original published July 13, 2016.**

What's inside

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Why you need to know more about Gen-X

It could be you

If you are a member of Gen-X then you might want to look away now as here are words typically used to describe a generation that attracts little attention between the might of the Boomers and the sparkle of the Millennials: Xers are described in a 2011 Journal of Behavioral Studies in Business article as " pessimistic, skeptical and disillusioned" and there are numerous observations coalescing around this theme. But on the other side of the equation they are also seen as resilient, self-starting and bottom-line focussed.

So why write about this rather overlooked cohort? Because Gen-X represents approximately 25% of current consumption in the US. The mid-point of the Xers in developed markets is about 44 years old which is right in the sweet spot of consumption i.e. when people spend the most. But that is only part of the picture as they have lower household wealth and savings rates and haven't benefitted from the asset inflation the Boomers saw. Plus they have less time ahead of them than the millennials to build up sufficient savings. Thus what they spend, how they spend it and their likely inability to fully seize the consumption baton from the Boomers are all very important for the levels and components of consumption.

X marks the spot

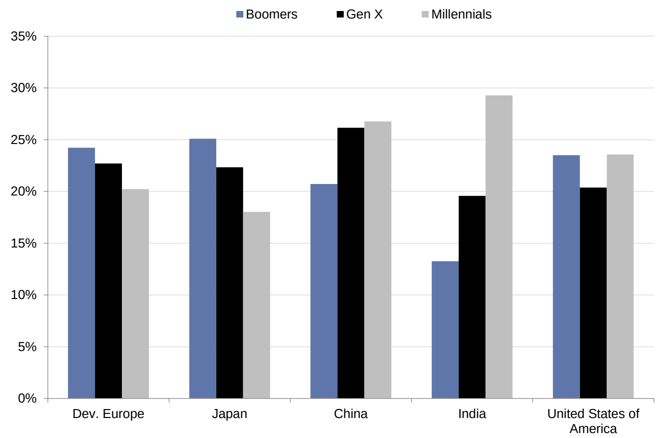
Generational definitions are not set in stone (our definitions are in the box below). This is an important point as these are just somewhat arbitrary definitions and what we are really discussing is the early-middle aged and middle-aged population who have a different outlook on life and financial situation than late-middle aged and older people. It is likely that an older Gen-Xer has more in common with a young Boomer than he or she does with a younger Xer who in turn has more in common with an older Millennial.

Who is who?

	Silent	Baby Boomers	Gen X	Millennials
Birth year	1928-1945	1946-1964	1965-1980	1981-2004
Age	71 - 88	52 - 70	36 - 51	19 - 35
US	9%	24%	20%	24%
Europe	13%	24%	23%	20%

Source: Pew Research.

Distribution of population by generation, 2015



Source: UN.

Smaller but important

The Xers are a smaller cohort than the Boomers or the Millennials at 62 mn members versus 73 mn and 75 mn in the US, whereas Europe is slightly different in that Xers are smaller than the Boomers, but actually bigger than the Millennials. The reasons for Gen-X's smaller size is partly definitional, but also because fertility rates fell in the US with annual births falling from around 4.2 mn in 1960 to 3.2 mn in 1970.

A tough beginning…

Although Xers are in the zone where earnings peak, their spending power is less than that implies. Why so? Firstly their disposable income hasn't grown in the way that the Boomers' did because their real income growth has been sluggish at best. If we take the average Gen-X and the average Boomer in the US and the average annual growth in real income for ages 34-43 years for each generation, it has been materially different: 3% pa vs. 1.8% pa. It's a similar story when you look at the real GDP growth both cohorts have either enjoyed in the case of the Boomers or experienced in the case of Gen-X: 3.3% pa vs. 1.7% pa for both between ages 34-43. And unfortunately for Gen-X the same story plays out in asset price inflation which was a transformative tailwind for the Boomers.

Not your father's housing market

The picture darkens if you consider when Gen-X was likely to make its first home purchase or when had it built up enough savings to invest in equity markets. If the average Xer bought a house when they were 30, then in the US that meant buying in 2003, only 4 years ahead of the fall in US house prices. Rather than just the change in house prices between the mid-2000s and today, it is the far greater oscillation in prices than the previous generations experienced that may have scarred Xers. This is notable especially given that when they were buying houses, the average loan-to-value ratios were higher, implying higher debt levels.

Pew Research estimates that Xers lost approximately 45% of their net wealth between 2007 and 2009. Millennials have no doubt been impacted by observing these asset price falls, but they typically have much less invested (home ownership is markedly lower) and have cautious attitudes towards debt (63% of US Millennials don't have a credit card). And they, unlike Gen-X, still have a long time left to build wealth. The midpoint of Gen-X only has 20 years left if you assume retirement at 65.

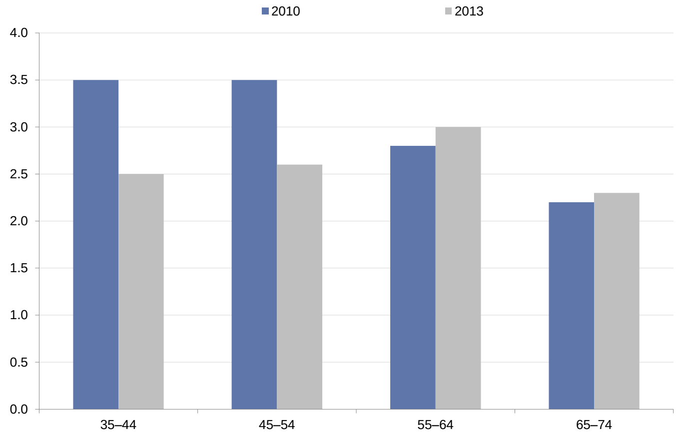
Some help could arrive for the younger Xers from their Boomer parents in the form of inheritance. Using ICI data for those who invest in mutual funds in the US 43% of those over 70 years old have investments excluding their main residence worth more than $500,000. For Gen-X it is only 22%. Therefore it is likely that there will be an inheritance benefit for older Xers, but it is hard to precisely calculate what that would be given assumptions on tax rates and whether it passes through a generation to the children of the Xers. The average family net worth for 65+ in the US is c.48% greater than the average family net worth for all age groups in the US.

… a tough end

As consumption growth in the US has historically been in part fuelled by borrowing, looking at changes in credit card debt by age groups is fascinating. What stands out in the next chart is that the amount of credit card debt for 34-54 year olds has fallen by 29% from 2010 to 2013. But for older generations it actually grew by 5-7% which suggests a rosier consumption picture for Boomers vs. Gen-X.

Older borrowers

Median value of credit card debt for households in the US by age groups (thousands of dollars)

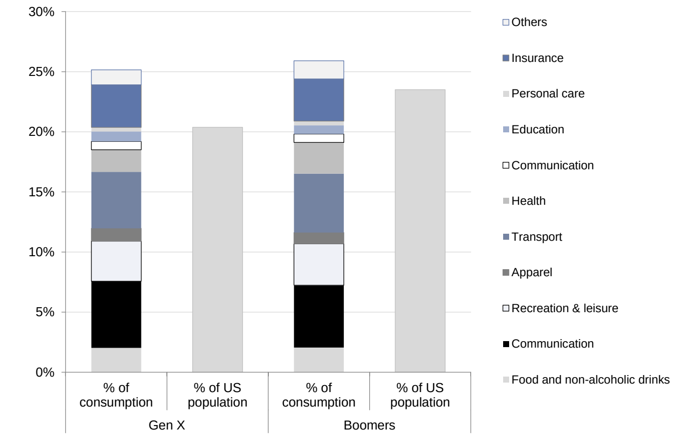


Source: Federal Reserve.

Given that Xers will have greater responsibility for their own retirements, they need to increase their savings rate. It also seems likely that retirement will be delayed as is happening now for the Boomers (65+ participation rates in the US have gone up from 14.4% in 2004 to 18.6% in 2014. The US Bureau of Labor Statistics also projects that it will go up to 21.7% by 2024). To add to this, the age dependency ratio, which is the number of people over the age of 64 compared to the working age population, was as low as 15% in 1960 and is now at 22% in the US, implying that Xers will receive less from the government during their retirement (net of their taxes) versus the Baby Boomers.

Boomers vs. Xers

Share of total consumer expenditure in 2015 and % of US population, by generation



Source: BLS.

The consumption sweet spot

The reason that this matters is that peak consumption by an individual is in the band of 45-54 years old in the US and is higher in the UK at 30-49 years old. We estimate that Gen-X is responsible for over 25% of US consumption currently. That shows their disproportionate economic importance. Therefore they really matter. So, even though they are smaller than the Boomers they are still a key demographic to target or sell to, but as see Drew Borst's piece on advertising argues Madison Avenue dedicates little of its collective time to them.

Taste shifts

Where Xers are spending more relative to Boomers is the following: eating out, mortgages and other housing costs, personal services, education and apparel. Why this is so is a mixture of tastes and priority shifts e.g. the importance they attach to their children and also eating out as an experience, but also some of it is imposed by price inflation which applies to things like property and education costs. For instance, education costs in the US have risen by 3.8% pa over the last 10 years and by 5% pa over the last 20 years. This enforced shift leaves less for other things and there is evidence that Gen-X is shying away from some Boomer status symbols.

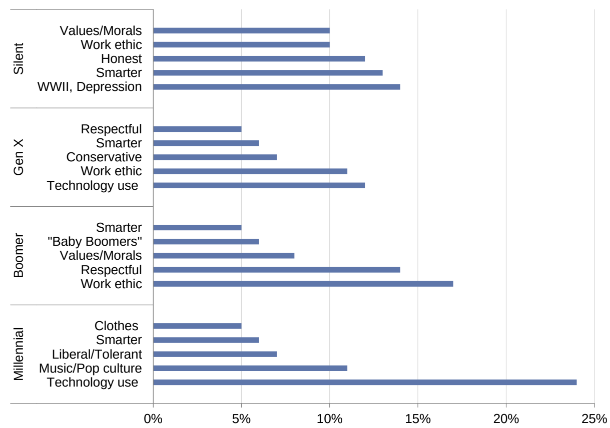
Social media usage

Xers are a hybrid of Millennials and Boomers when it comes to social media. Today's Gen-X have the same social media penetration rates as Millennials did 5 years ago, with the catch-up being fastest for older Gen-X (see chart on page 5). This has implications for how to communicate with Xers as they still use traditional media e.g. TV, but are increasingly active in social media as well.

Pragmatism and resilience

The next chart shows some of the key attitudes of Gen-X compared to other generations. In our interview with Neil Howe on page 6 we discuss his theory of generational turnings; how each generation is shaped by the prevailing economic conditions and social attitudes, but also by what's gone before and in particular their parents. The increase in spending on their children by Gen-Xers' parents can be seen as a reflexive response to the relatively little time and money Gen-X had spent on them. The attitudes of resilience and pragmatism with a lack of idealism that Gen-X displays is not surprising in Neil's generational context but it does have implications for what sort of leaders Xers are and will be. His answer? Xers will make good leaders for the challenges of the world they find themselves living in (spoiler alert he believes we are in a crisis phase where Xers' pragmatism will be critical). And if not as leaders then they are clearly important in choosing leaders. Also, Alec Phillips explores the role of Xers in the forthcoming US election on page 14.

Pew survey: What makes your own generation unique?

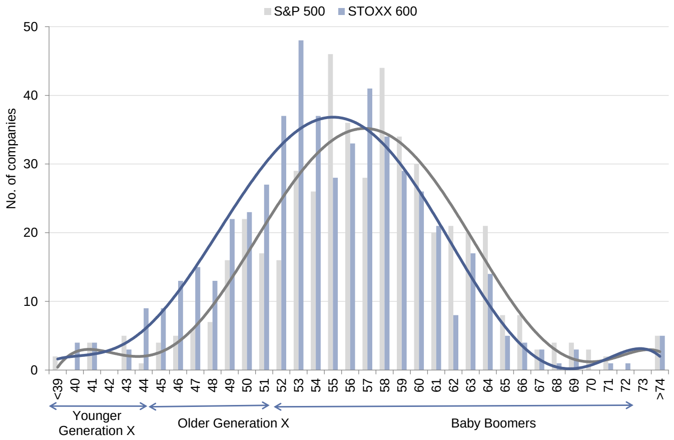


Source: Pew Research.

Surprisingly, when we look at the distribution of European and US CEOs by age, European CEOs are slightly younger. The median age for the US is 57 meaning that Gen-X isn't running the C-suite yet, but will be soon. What their more parsimonious proclivities will mean for capex, M&A and cost cutting remains to be seen.

Boomers run the C-Suite

Age distribution of S&P500 and STOXX600 CEOs



Source: Bloomberg.

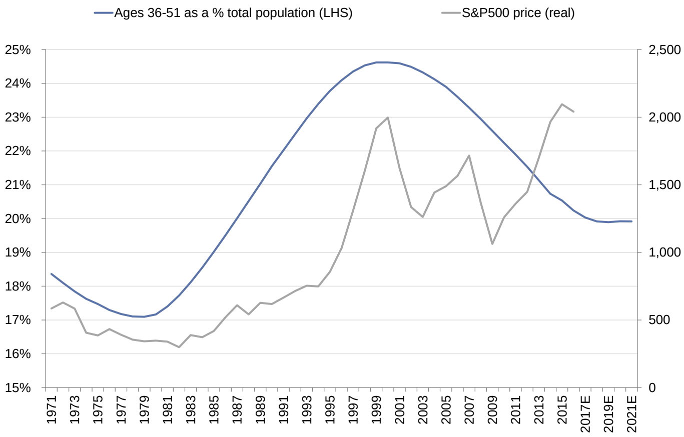
Gen-X and investment implications

Gen-X is not usually a generation that is specifically targeted by brands and it is a difficult generation to sell to as they are a mix between analog and digital. This is why Drew Borst highlights that TV advertising is still effective with this cohort on page 13. They are also a more conservative, frugal generation, reflecting our US analysts' argument that they spend less on cars versus their Boomer parents (page 12). Focusing on what they spend on, either more or less relative to the Baby Boomer generation reveals both the differences in priorities and economic conditions; many of the things they consume disproportionately more revolves around the family – children, housing, appliances, apparel and travel. Therefore the outlook for Gen-X matters most to sub-sectors like home improvement, autos, consumer durables, apparel and leisure. It is particularly important to understand where their tastes, and the value they place on brands, have and could change. There is a history of companies launching brands targeting this age group that didn't last long e.g. American Eagle Outfitters and its Martin + Osa store chain, Gap with Forth & Towne and Abercrombie & Fitch with Ruehl No. 925. The Millennial disdain for established brands is often debated, but it's a similar story with Gen-X, raising risks to companies supplying high-ticket consumer goods.

One final thought around the Xers is the broader demographic backdrop. When working age populations as a percentage of the total shrink it has typically been seen as a headwind for economic growth and growth in savings. As countries age they typically experience lower growth and lower risk appetites which can have implications for how much and how people invest.

Extrapolating?

Share of 36-51 population in the US vs. real S&P 500 performance



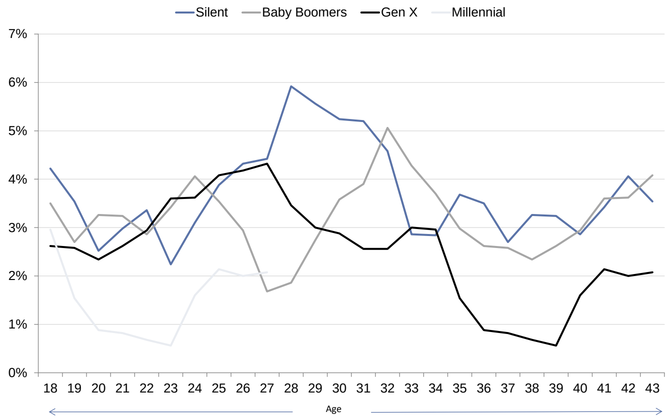
Source: Robert Schiller, UN.

Six generational charts

The first four charts depict economic conditions in the US and the UK when the different generations entered their formative years

Unexceptional growth

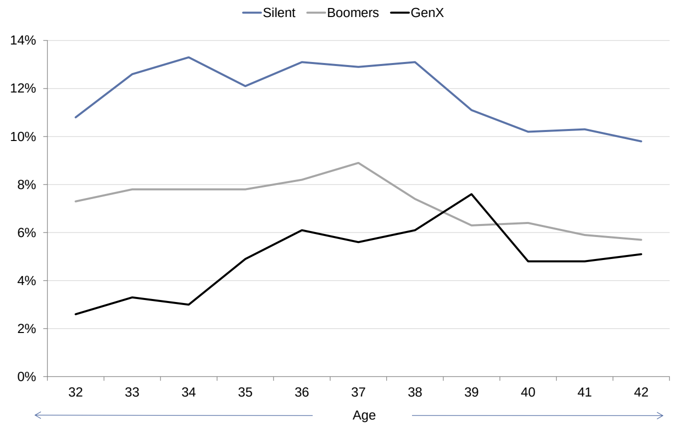
US real GDP growth yoy



Source: Federal Reserve.

Hard to save

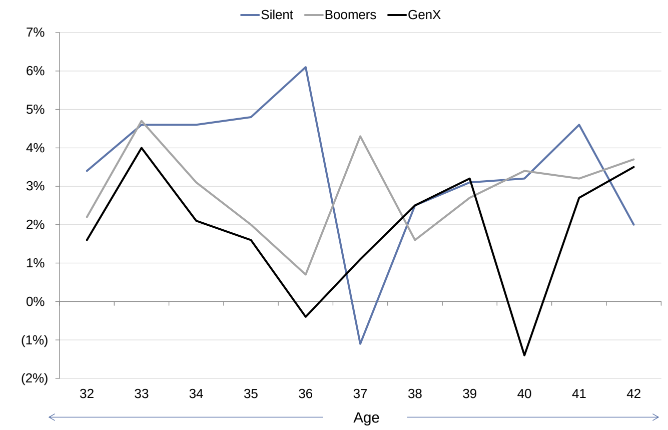
US savings as a percentage of real disposable income



Source: Federal Reserve.

More downs than ups

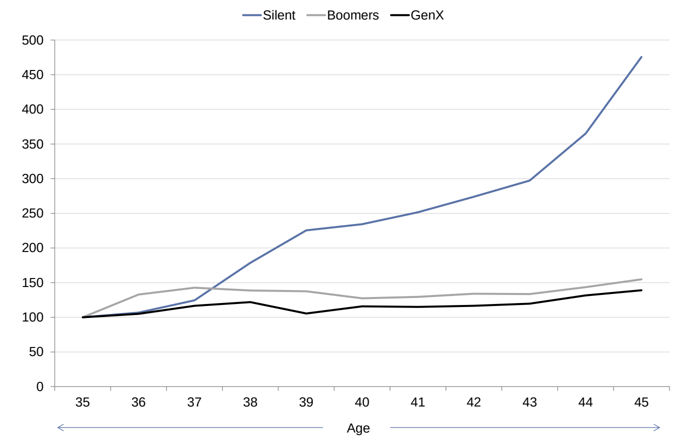
US real disposable income growth yoy



Source: Federal Reserve.

Being there

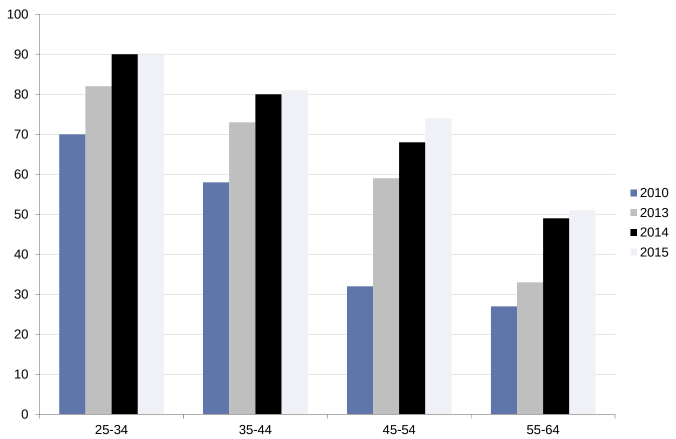
UK house prices, indexed



Source: ONS.

The hybrid generation

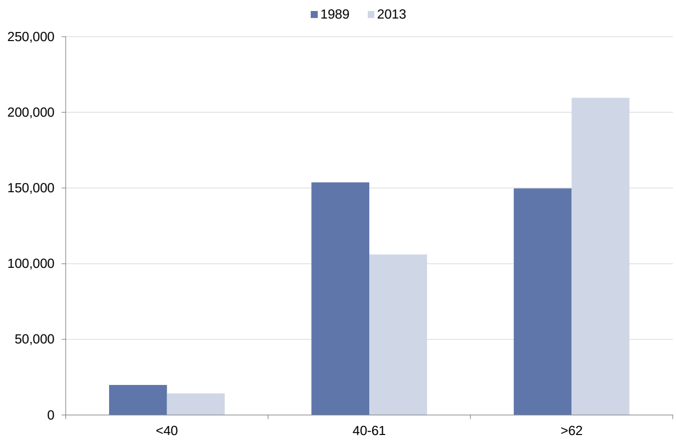
% of people having a social media profile by age group



Source: Pew Research.

A step down

Median wealth of US families, US$



Source: Federal Reserve.

Interview with...Neil Howe

Neil Howe is a renowned author and speaker on economic, demographic, and social change in America. He is the nation's leading authority on today's generations: who they are, what motivates them, and how they will shape America's future. Howe coined the term "Millennial Generation" and has written over a dozen books on generations, many of them with William Strauss, including Generations and Millennials in the Workplace. Howe is currently a senior associate at the Center for Strategic and International Studies and the Global Aging Institute.

Can you give an overview of your generational theory and the place of Gen-X within that?

First, let's define what a generation is. It's a group of people born over a span of about 20 years or so, who share common beliefs, attitudes and behaviours. They also share a common age location in history. For example, the G.I. Generation came of age during the Great Depression and World War II, while Boomers (roughly half of whom were literally children of the G.I. Generation), came of age during the mid-'60s to the early '80s, a time of tremendous turmoil and upheaval in societal conventions. The G.I.s were shaped by D-Day and one of the major national crises in American history. Boomers were shaped by Woodstock and one of major awakening eras of American history. Small wonder they turned out so differently.

Gen-Xers were the children of that awakening period, which is instrumental in understanding their behaviour. Throughout history, generations born during Awakenings, we call them "Nomads", grow up amid social and cultural upheaval. They are generally left on their own by adults who are busy trashing old norms and exploring new values. Xers started coming of age themselves as adults after the Awakening ended in the early Reagan years.

The generation following Xers was Millennials, who benefited from a large-scale shift toward child protection in early-'80s America. This was a far cry from Xers' childhood as latchkey kids. In fact, hands-off childrearing, the sort that Xers experienced, is one aspect of being raised in an Awakening era, something that Nomadic generations typically experience as children.

Let's also take a look at the other kinds of generations. Apart from Nomads, we define three other archetypes in our theory: Heroes, Artists, and Prophets. Hero archetypes are born after Awakenings and are raised at a time of increasing protectiveness toward children, for example the G.I. Generation, The Silent Generation is of the Artist type, which is raised during a Crisis era. Prophets, like the Boomers, are raised just after the end of a Crisis era, when child rearing becomes more indulgent.

A generation can also be defined based on what it missed. Even the oldest of the Silent missed any memory of the Roaring Twenties; their earliest childhood experiences were of the Great Depression. Boomers just missed World War II. Gen-X missed the American High and cannot recall the watershed moment of Kennedy's assassination. Finally, even the oldest Millennials can't recall any of the social and family experimentation of the Consciousness Revolution, nothing before "Baby on Board" bumper stickers and new "family values" moral panic over the welfare of children.

Can you talk about some of the factors that have shaped behaviour for Gen-X?

Consider the childhood environment when Gen-X first arrived in the early '60s. It was a time when divorce rates accelerated, fertility rates plummeted and schools no longer seemed to work. The old joke is that Xers are the first generation people took pills not to have children. There was a society-wide hostility to children during this period, they were an annoyance and, well, we all knew (from reading the "Population Bomb") that there were way too many of them, anyway. Many of the most popular movies of the time, like Rosemary's Baby, The Exorcist, and The Omen depicted evil children.

While their parents were busy trying to discover themselves, Xer children were left with latchkey guides to take care of themselves. Ebbing confidence in institutions meant that kids trusted nothing and nobody, giving rise to this generation's trademark cynicism and resilience. From early on, they understood that focusing on the bottom line was more important in life than ideals. This materialistic focus shows up in the pop culture of the Xer teen era with songs like Madonna's "Material Girl."

Likewise, a UCLA college freshman survey running since 1967 has asked fresh students around the country whether it is more important to develop a meaningful philosophy of life or to be financially well off. The ratio of responses in favour of a meaningful philosophy of life had been around 3:1 to 4:1 until the late '60s, when Boomers were still freshmen, but in the mid- to late '70s shifted in favour of being financially well off by a ratio of about 2:1.

Of course, since every generation spans roughly 20 years, there are differences between "first waves" and "last waves" of the same generation.

For example, the first wave of Xers born in the '60s came of age during the Reagan years. They prioritize self-sufficiency, the bottom line, and a scathing (anti-Boomer) scepticism toward grand ideals. They are also very attached to individualism, free agency, and deregulation. In fact, people born in the '60s are actually among the most partisan birth decade born in the 20th century. Fully 63% of all Americans who are born between 1961 and 1971 and who have ever served as a U.S. governor or a member of Congress are Republican. (This imbalance is outmatched only by people born in the 1910s, who came of age at the height of the Great Depression and who later leaned very heavily Democratic.)

But as we move to the last-wave Xers born in the '70s, we see a clear shift toward being more Democrat-aligned. And so, even within the same generation, we meet contrasts like we see with Xers: the Reagan versus the Clinton wave; or the Atari versus Nintendo wave.

Today, first-wave Xers are reaching (belatedly) the age of national leadership. And just look at the 2016 primary race. While on the Republican side, we saw many prominent Gen-X names, including Paul Ryan, Chris Christy, Marco Rubio, Nikki Haley, Bobby Jindal, and Scott Walker, there were barely any Gen-X candidates on the Democratic side. The average age of Republicans in Congress has also been declining substantially over the past few years as Xers move into leadership positions, while on the Democratic side, the average age continues to rise.

Given the socio-economic circumstances that they have faced, do you think Xers consume differently versus previous generations?

To understand the effects of generational shifts on consumption, we need to consider three factors: the demographic volume or density of their birth cohorts, their spending power, and their attitudes.

Population density increases as we go from first-wave to last-wave Boomers, born in the late 1950s. It decreases rapidly again in the mid-1960s, which gave rise to the term "baby bust" to describe most of Generation X.

To be sure, some of the population decrease attributable to the fertility decline was made up for by heavy immigration. In fact, Gen-X is the largest immigrant generation (not just in absolute numbers, but per capita) of any generation born in the 20th century. Yet overall, the population pyramid today still shows a huge bulge at the top made up of Boomers, an inward Gen-X bust crescent further down, then a second bulge of Millennials in young adulthood. The peak Millennial birth years are 1990 and 1991, which forms another outward protruding bulge.

Over the next fifteen years, the crescent indentation comprised of mid- to late-wave Xers will be moving up as they get into their 50s and 60s, causing sizable declines in the number of people in this age group. On the other hand, we will get a lot more people in their late 30s and early 40s. Implications? Keep in mind that the mid-life age bracket historically constitutes a large chunk of all consumers of the highest profit-margin goods and services, be it cars, houses, boats, appliances, or vacation homes. This is the "luxury" bracket. Declining numbers per cohort in this high-margin age bracket will put plenty of stress on corporate income statements, whose margins right now are already eroding.

But that's not all. Not only will numbers decline in this age bracket, but per-capita ability to spend as well. As Xers move into midlife, we're going to see in this age bracket a sizable drop in median household net worth. Their incomes will be constrained, and their purchases will be further constrained by their desperate need to save more before they retire. In short, we're going to see, finally and at the prime of life, that much-heralded reversal in upward generational economic mobility that economists have for so long talked about.

So it is true, then, that Gen-Xers represent the first downwardly mobile generation in the economy?

Almost. It's more accurate to say they are the first full generation to experience a significant decline in real median household net worth when compared to the prior generation at the same age.

Cohort by cohort, when you look at the data, the downturn actually started a bit earlier. It started with late-wave Boomers, those born in the mid- to late-1950s. Compared to first-wave Boomers, they were hit much younger by the turmoil of the '60s and came of age at an unluckier economic moment, not the go-go late '60s, but the stagflation late '70s. They were more numerous, which bid down entry-level wages. And they were less well educated by almost every measure. College completion rates declined, particularly for males born in the late '50s. From first wave to last, Boomer SAT scores fell for 17 consecutive years, reaching an all-time low for the birth cohorts of 1960-61.

By the time Xers came along, the '80s recovery had brought new job growth, but also rising interest rates for student loans and mortgages. Further, when the Rust Belt was being disbanded or outsourced in the '80s, we saw the introduction of two-tier wages where only older workers would have their wages preserved. This too was unprecedented, and the only way Xers could get ahead was by spurning institutions that protected older incumbents and relying instead on themselves. These circumstances really shaped their collective persona. Unlike Boomers, they didn't bemoan the injustice of their fate or hide behind a toney yuppie façade. Xers got to work, took chances, and never assumed that anyone was there to look after them.

Along the way, Gen-X has become the most spread-out generation in terms of income and wealth distribution. The combination of eroding youth safety nets, a disappearing middle class, high immigration, a tough childhood, and free agency has shaped the Gen-X mindset. They were considered hopeless slackers, and many Xers took this to heart. They knew that they would never be admired as a group by older people. They also knew (and were constantly told) that most of them would never inherit the American Dream. So naturally, few of them had much interest in identifying with their generation. They embraced a maverick outsider role, and cultivated their individuality. Each Xer hoped to be the exception, the one who broke the odds and turned out a winner. All this stands in stark contrast with Millennials. While young Millennials have the collective confidence that they're all somehow going to get ahead, that wasn't the case with young Xers, who always suspected (to use the Wayne's World line) that "we are unworthy."

Two other watershed events that shaped Generation X were the big market crashes: the dot.com bubble burst and the crisis of 2008. The latter was a real call of reckoning for this generation. The drop in median household net worth from 2007 to 2010 in the Gen-X age bracket far exceeds that of any other generation. Young-adult Xers bought late into the stock market and late into the real-estate market. And in real estate they typically bought into exurban locations where the prices fell the fastest. So yes they were the biggest losers. By 2010-11, Xers were far more likely than other generations to be underwater on their mortgages, which remains true today. To some extent, Xers still remain trapped in houses that cost too much, in student loans they're still paying off, and in an income-asset-debt vice that is hard to escape in the absence of significant inflation. In the wake of the Great Recession, we have seen the emergence among Gen-Xers of what I call the "new frugality." Millennials, traumatized by seeing what debt had done to Xers, have become so averse to debt for this very reason. Apart from student debt (here Millennials feel they have no choice) every other form of debt (credit card, auto, and housing) has been declining swiftly for Americans under age 30 over the past decade.

The debt burden of Xers also means they're less likely to be able to "catch up" and save for retirement than Boomers with higher net worth. Indeed, Xers are the ones we have to worry about when it comes to long-term economic prospects. Most Boomers are old enough and financially healthy enough to retire with sufficient accumulated wealth, while Millennials are still young with time left to increase net worth. Xers, on the other hand, are much less prepared for retirement today than their parents were 25 years ago. A key statistic from the Fed's Survey of Current Finances: For households age 40-49, the median net worth in 2013 was roughly US$100k; in 1989, it was slightly over US$150k (in 2013 dollars).

How different are Xers from other generations in their attitude toward work and family?

A remarkable thing about Xers is how they're behaving as parents. Being afterthoughts when they themselves were kids, they are diligently trying to compensate, some might say overcompensate, in raising their own kids. With their titanium-alloy baby carriages and their GPS tracking devices sown into their kids' clothing, Xers have in fact become the most protective generation of parents in living memory. They're raising their kids (late-wave Millennials and now post-Millennials) very differently to how they were raised.

Also, Xers are beginning to move into positions of power in the corporate sphere. Many founded, and now lead, some of Silicon Valley's biggest companies. Their general lack of confidence in the future of the global economy makes them focus more on the bottom line than the top line. They are pragmatic deal-makers and a ruthless generation of cost cutters.

Xers are also big on DIY employment, with a much higher propensity than other generations to stay home with kids and participate in the gig economy instead of the conventional labour market. They are often willing to move to Sun Belt states that are taxed less, and to piece together their own living wherever they go. The result is that, while Boomers past age 60 are working more than ever, the employment-to-population ratio between ages 25 and 54 remains well below its earlier 2007 high-water mark.

This adaptability also allows Xers to depend more, without stigma, on help from their extended family. Today's renaissance in extended-family living is indeed a profound social trend in America, and it is being manifested most clearly by Millennials, who have always been on pretty good terms with their parents. The share of 25- to 34-year-olds living with parents or older family members has increased from 11% in 1980 to 24% in 2014.

Many Xers have parents still better off financially than they are; the net voluntary subsidy flow between generations is now hugely from old to young, the opposite of what it was doing 40 years ago. The Silent Generation, who constitute the parents of most first-wave Xers, are so well off financially that we are seeing an unprecedented aging of wealth in the United States today. In 2013, the median net worth of households over age 65 was more than double that of all younger families.

I digress, but this is why the Silent Generation is often called "the lucky generation" by demographers like Richard Easterlin and Elwood Carlson. When the Silent were young adults, America's elderly were so destitute they were deemed to be a major target of JFK's and LBJ's "war on poverty." It's nice to go through life always doing well relative to people who are older and younger than you. It seems so effortless. As Woody Allen once put it, "Eighty percent of life is just showing up", a joke that leaves Xers shaking their heads in incomprehension.

So even as first-wave Xers approach retirement age, many remain dependent on their parents for direct subsidy to keep their mortgages going and to send their children to college. I tell financial service companies, by the way, to spend less time marketing to the parents of nuclear families and more time marketing to the grandparents of extended families, where many of the real decisions are still being made.

So what lies ahead for Gen-X?

In our generational theory, we outline a recurring cycle of four turnings or seasons of history, a High (era of strong institutions), an Awakening (when institutions are attacked), an Unravelling (when institutions are weak) and a Crisis (when old institutions die and new ones are born). We identify the period in America beginning around 2008 as a new Crisis era. This is a period in which the pace of history quickens, economic and political institutions are torn down and rebuilt, and the very survival of the nation ultimately feels under urgent threat.

On average in recent history a turning lasts around 22 years, so we're only a part of the way into the current Crisis era. We expect enormous financial turbulence and political upheaval in the years ahead. This uncertainty makes the November elections even more important. People want security and for leaders to assert authority during a Crisis era. The current mood is remarkably similar to what we saw in the '30s.

One of the positive aspects of Fourth Turnings, which we have seen throughout American history, is that families become stronger and generations work together in the face of danger. Unlike the G.I. generation, which in its maturity built up America's infrastructure but remained culturally alienated from their own kids, Boomers are prioritizing family solidarity. Millennials know that Boomers have zero reputation for building anything (they're better known for demolishing things), but they admire Boomers' vision and values. So most Millennials remain personally close to their parents.

In a Crisis era, young people tend to turn away from personal risk taking. So while young Boomers were clearly a generation willing to take staggering risks (not just sex, drugs, and rock 'n roll, but crime, suicide, cigarettes, booze, and self-inflicted accidents), Millennials are reversing most of those trends. They are turning out to be remarkably cautious in their lifestyle choices. Bars and nightclubs are closing across America today. Why? Millennials aren't going there. They're too dark and dangerous, and besides, you can't even take a good selfie in them!

This backdrop should lead to a really interesting era ahead, and I think Xers are a key linchpin in deciding its fate.

In a famous Time magazine cover from the fall of 1990, Xers were shown as glum-looking kids dressed in black, all looking in different directions. That image reflected the fact that few Xers really thought of themselves as a generation at the time. In fact, at the time when we coined the term "Millennial" in our book on generations, Gen-X didn't even have a name yet. They were the thirteenth generation since the era of America's founding fathers, and so we just called them "13ers." Doug Coupland's novel Generation X, which named the generation, came out a year or two later.

Think of that: Millennials were actually named before Xers were. That's how overlooked this generation has been. If we rank generational names by the frequency with which they are mentioned in the recent earnings calls of S&P 500 companies, the highest number of mentions is for Boomers, closely followed by Millennials. Generation X? A distant third.

But increasingly, Xers are going to become leaders with power as Boomers age further into elderhood and Millennials start to climb the managerial ladder. Being pushed to the curb so many times has given Xers a real sense of how life works. They are good at navigating risks, and their grit should serve them well as they make white-knuckle decisions. I think history will show that Xers will demonstrate common sense and good judgement as they take the helm of our country at a critical time.

Demographic change in UK retail?

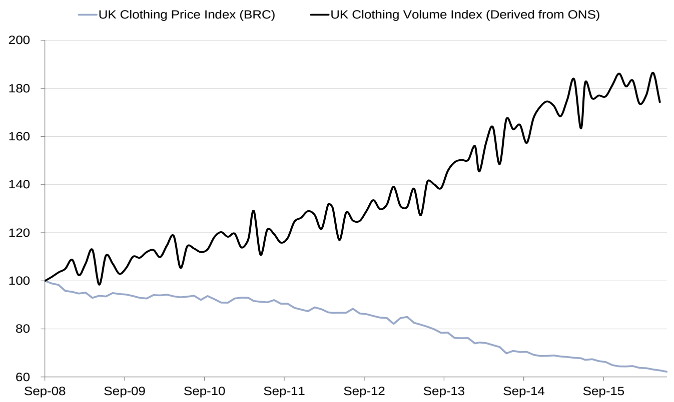
Richard Edwards, our European Retail analyst, explains the weakness in UK apparel retail

An evolution in UK consumer behaviour?

Over the last 12-18 months, the UK apparel market growth rate (+2.5% pa 2006-15) has moved into decline as average selling prices (ASPs) have continued to fade (c.-5% 2006-15 CAGR) but volume growth trends have slowed. In overview, the ASP declines over the last decade have been primarily driven by consumer trade-down activity to lower priced apparel, leading to an acceleration in clothing market volume growth trends, notably benefiting the discount clothing retailers.

UK apparel market has seen trading-down activity drive strong volume growth trends…

UK clothing market ASP vs. volumes growth trends, 2008-16



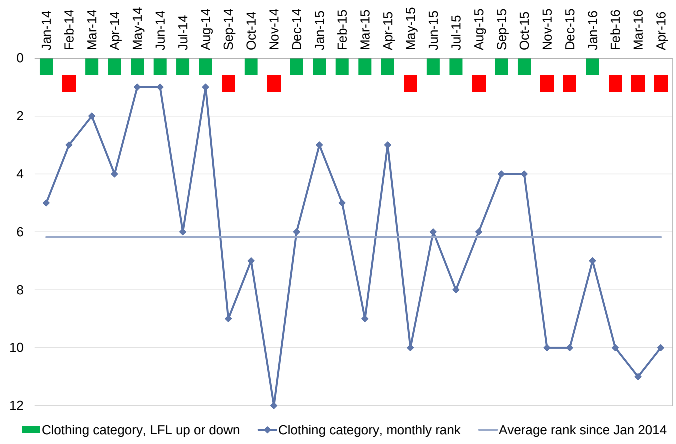
Source: ONS, BRC.

However, despite recent moderate disposable income growth trends, the UK clothing market has unusually underperformed the broader non-food retail sector over the last 18 months. This could be explained simply by a prolonged period of adverse weather, albeit the clothing sector's underperformance has been reasonably consistent since September 2014. We argue that while weather patterns have not helped, 21 months seems too long a period for clothing underperformance to be explained by weather alone. Other explanations used by the industry are that consumers have got 'enough stuff' (so called stuffication) and buying ever greater volumes of clothing is getting harder / undesirable.

Alternatively, there is the Millennial consumer explanation, which suggests that consumers are more interested in experiences, family and the home, than collecting ever more clothing and shoe options. The latter seems to fit the data (see below) to the extent that the strongest performing non-food retail categories over the last 18 months have been home-related (and in particular furniture), while clothing performance has been deteriorating.

However, stalled volumes have driven clothing market underperformance for the last 21 months…

UK clothing market growth ranking (1 = low, 12 = high)

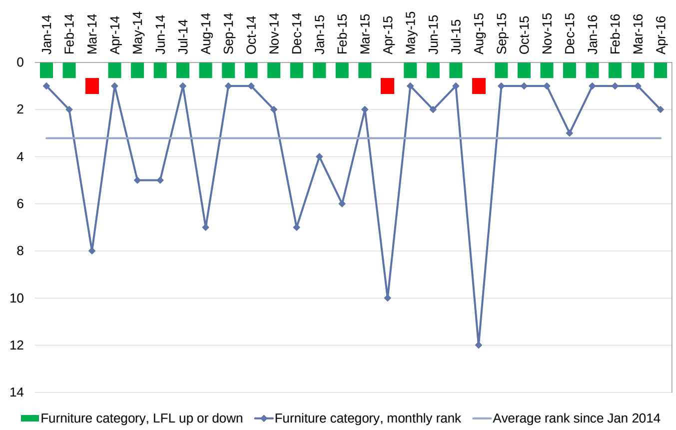


Source: BRC.

In conclusion, while an explanation for the recent decline in the UK clothing market may in part be weather-related, the declining growth pattern now appears sufficiently consistent to suggest that consumer behaviour is also evolving. Taken in combination with the current online channel shift, and related store-based sales cannibalisation, we argue that the outlook for European apparel retailers is getting more demanding by the day, especially for the less differentiated formats.

…with stronger consumer spending in experience and home-related retail categories

UK furniture market growth ranking (1 = low, 12 = high)



Source: BRC.

Richard Edwards

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Investing in a more risk-averse generation

Alexander Blostein, our US Asset Managers analyst, discusses the implications of Gen-X for his sector's growth profile

Overview

Generation X looks to be positioned at a marked savings / wealth disadvantage to the Baby Boomers and Silent / GI Generations. According to the Investment Company Institute, there is a US$3 tn gap in mutual fund assets and 50% less in the median account between Generation X and Baby Boomers. We attribute this divergence to weaker market performance and fewer years to compound returns for the majority of Generation X investors. We believe that Gen-X will have to increase its savings rate over time to compensate this delta, while low interest rates and rich equity valuations may compound this problem near term. In terms of asset allocation, Generation X portfolios favour ETFs and balanced funds, primarily Target Date funds, more than other demographics, which we believe will lead to organic growth divergence across the asset management industry.

Background

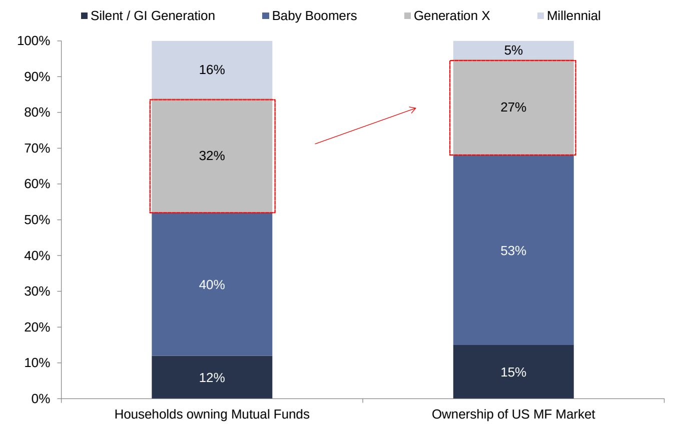
For background on the data below, we utilized the Investment Company Institute's 2016 Factbook to analyze mutual fund ownership across the US. The Factbook defines the four major demographic groups as:

1. The Silent /GI Generation (born 1904 to 1945)
2. Baby Boomers (born 1946 to 1964)
3. Generation X (born 1965 to 1980), and
4. Millennials (born 1981 to 2004).

From an age perspective, the Silent / GI Generation comprises ages 71 and older, Baby Boomers range from 70 to 52, Generation X from 51 to 36 and Millennials from 35 to 12 (however ICI data only includes responses from individuals over 18 years of age).

Gen-X owns c.27% (US$3.3 tn) of US mutual fund assets despite having a 32% share of households that own funds

Ownership of US mutual funds by household and AUM



Source: ICI.

Weaker markets and fewer years = US$3 tn gap between Boomers and Gen-X

According to the Investment Company Institute (ICI), US households own 89% of the US mutual fund market, or roughly US$12.3 tn at the end of 2015. Generation X households own c.27%, or US$3.3 tn of US mutual fund assets, despite accounting for roughly 32% or 17 mn of the 54 mn US households that invest in mutual funds. That compares to the Baby Boomers, which own the largest share of the US mutual fund market (c.53%/US$6.5 tn). Overall, Baby Boomers have a 13% share advantage or c.US$3.2 tn in AUM over Generation X, despite only having 8% more households.

We attribute the lower level of AUM compared with the Baby Boomers to two main drivers: (1) shorter investment periods; and (2) lower market returns. On average, Generation X investors purchased their first mutual fund shares in 1998, or roughly 18 years ago, compared to Baby Boomers who purchased their initial funds in 1991 or roughly 25 years ago. Put simply, Baby Boomers have had seven additional years to compound returns. Additionally, market returns have not been as favourable to Generation X as for Baby Boomers. Using a blended index of 60% S&P 500 and 40% Barclays Aggregate as a performance proxy, we estimate that the annualized return for Gen-X portfolios is 6.2% since 1998, versus 8.6% annualized for Baby Boomers, since 1991. On a cumulative basis, this translates into roughly a 3x return for Gen-X versus 8x return on their initial investment for Baby Boomers.

Bear markets such as the technology bubble and Global Financial Crisis certainly played a role in the reduced returns, and looking ahead, the lower for longer rate environment may also compound Gen-X's problems, forcing higher savings rates or increased equity allocations.

Obviously, differences in savings rates, reinvestment rates and asset allocation decisions over these years can dramatically alter the performance of individual investors, but in aggregate, the data suggests that Boomers enjoyed a much more robust beta environment than Gen-X, further solidified by seven additional years of compounding.

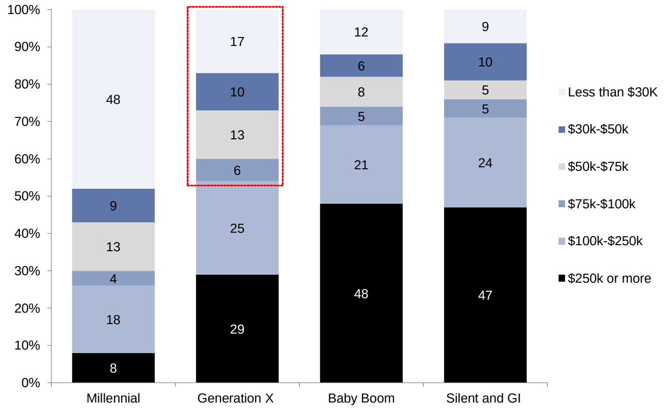
Increased savings needed to remedy low account balances

According to ICI, 46% of Generation X households have less than US$100k invested in mutual fund assets. When we look across the entire distribution, the median Gen-X household has roughly US$100k invested in mutual funds, 50% less than the median Baby Boomer and Silent / GI Generation. Furthermore, 17% of Gen-X households hold less than US$50k in mutual fund assets vs. 18%/19% for Baby Boomers and Silent / GI Generation respectively. On the high-end, only 29% of Gen-X households have more than US$250k in mutual funds vs. 48%/47% for Baby Boomers and the Silent / GI Generation respectively. We believe that Gen-X investors will be forced to either save more or lower their retirement spending / lifestyle as a result of lower wealth accumulation. Although many individuals may inherit wealth from Baby Boomer and/or Silent / GI Generation family members, the uncertainty of amounts and timing will likely force higher savings in the near term. Rising consumption patterns and uncertainty surrounding healthcare spending may exacerbate the need for Gen-X members to start saving more in the near term. While household wealth is much higher than these balances, owing to other assets such as housing, CDs, etc., we believe this represents the vast majority of liquid savings earmarked for retirement, largely held in tax deferred plans such as IRAs and 401(k)s. That said, low interest rates and the fact that Generation X members have lived though volatile equity markets might make them reluctant to invest more in the capital markets, which makes achieving higher real asset balances more challenging.

For the asset management industry, we believe smaller client accounts among Gen-X investors will likely require increased distribution and investor education efforts to reach the broad market. Additionally, shelf space in 401(k) markets and IRA distribution will be critical to success as we anticipate that Generation X members will likely increase savings primarily through tax- pre-tax income being diverted into tax-deferred accounts.

As a result, 46% of Generation X households have less than US$100k invested in mutual funds

Household mutual fund assets



Source: ICI.

ETFs, Target Date funds favoured by Gen-X

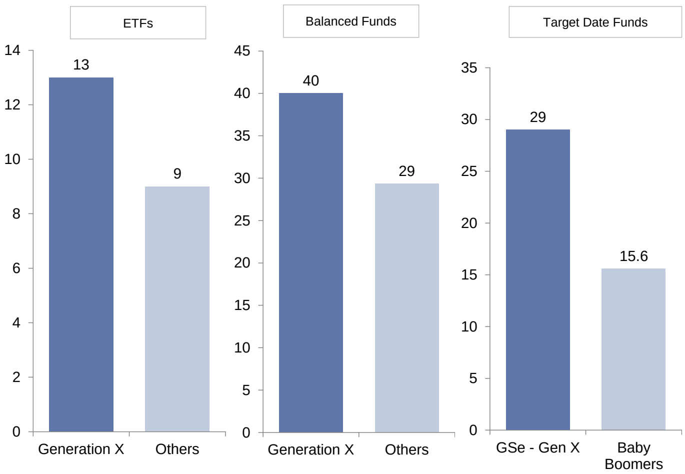
Across the different generations, asset allocation differences exist where one might expect: Baby Boomers and Silent / GI Generation households hold more bonds / less equity investments than younger generations. **But putting that aside, we highlight two major differences between Generation X investors and other demographics (both young and old). First, Gen-X households have the highest utilisation rate of ETFs, with 13% of households owning ETFs vs. a 9% average for other generations.** Given that the average Gen-X investor started investing in 1998, it makes sense that their allocations somewhat match the rise in popularity of ETFs over the past 20 years. Additionally, weak active equity performance since the Global Financial Crisis likely also contributed to higher demand for ETFs as cheap beta exposure produced similar returns.

Secondly, Generation X favours balanced/multi-asset funds more than other demographics, specifically Target Date funds. For balanced funds broadly, ICI data shows that 40% of Gen-X households own balanced funds vs. 29% for other demographics. Further, we utilise ICI's 401(k) allocation data which shows that Gen-X accounts have an average allocation of 29% to Target Date funds vs. 15% for Baby Boomers. Monetary policy uncertainty, search for yield and high equity valuations have all likely contributed to increased demand for multi-asset / Target Date strategies which will likely continue for the foreseeable future.

For the asset management industry, investor preference for ETFs and balanced funds, particularly Target Date funds, is a trend that will likely lead to further growth divergence given few firms have scale in both businesses. Specifically, the top-3 ETF providers have 70% global market share, making it difficult for other firms to access the growing demand. On the Target Date side, we estimate that the top-3 providers in the US have 76% market share. Overall, we believe the rising popularity of ETFs and balanced strategies, particularly Target Date funds will lead to greater growth divergence across the industry with fewer firms being able to grow organically.

Generation X investors favour ETFs and balanced funds more than peers, particularly target date funds vs. Boomers

Household ownership (%) of ETFs and balanced funds; GSe 401(k) Target Date allocation %: Gen-X & Baby Boomers



Source: ICI, Goldman Sachs Global Investment Research.

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Gen-X: The pragmatic auto consumer

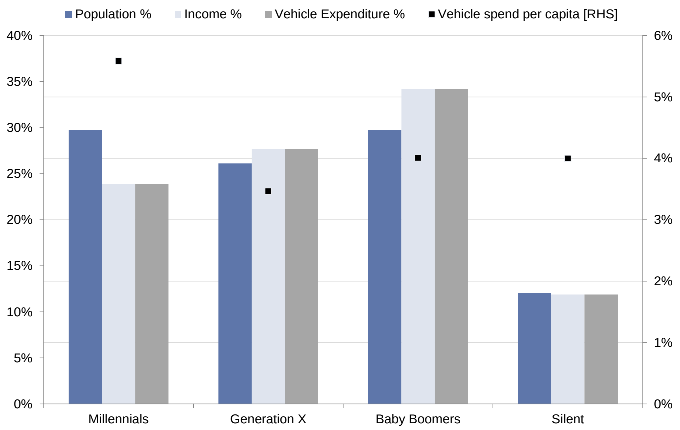
Our US Autos analysts highlight the under-indexing of Gen-X autos spending

Digitally naturalized, not native

Bookended by Baby Boomers and Millennials, Generation X suffers not only from definitional limitations impacting size, but also from a bifurcated history with technology. Marked by self-reliance and independence, this group grew up to appreciate technology as it progressed whereas the Baby Boomers had to work to acquire it and Millennials were effectively born with tech integrated into their lives; as a result, Gen-X lies as a digitally inclined segment, but blends traditional media channels with the more modern digital channels. So while they have adapted to the increasing digital economy as tech progressed, with one foot in the past and one in the future, marketing organizations see a more complex equation to solve when targeting this group. And considering the smaller relative size to their predecessors and the digital natives behind them, and a lack of extroversion relative to other generations, Gen-X offers little in the way of upside to target, given the need for multiple platforms – pushing marketers (auto companies among them) to focus on the larger demographic groups that can be easier targets (Millennials through digital media and Baby Boomer's through traditional outlets –radio, print, and TV). This has effectively helped drive the tag-line of the forgotten generation.

Statistically small population size drives under-indexed auto sales for Gen-X

Mix of population, income, and expenditure on new vehicles across generations (2014)



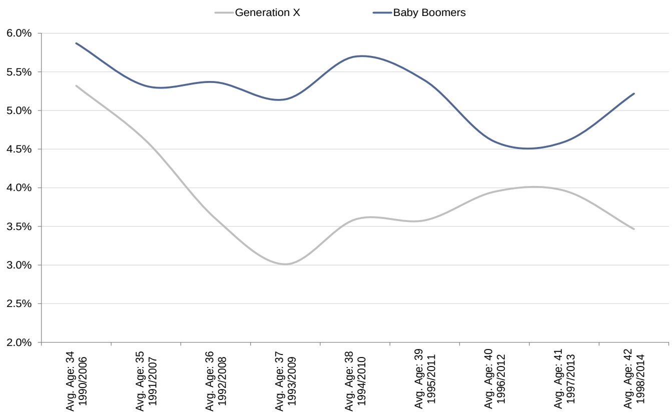
Source: US Census Bureau, Goldman Sachs Global Investment Research.

A closer look at the specifics –smaller population equals smaller relative auto purchases.

At 26% of the US population, Generation X under-indexes to both Baby Boomers and Millennials at 30% each (as above). In fact, over the past decade Gen-X has represented an average 27% of the US population, relative to Baby Boomers at 31%. And once the Millennial population picked up in 2010, both cohorts have overshadowed Gen-X in terms of significance. The smaller relative size in turn drives lower demand for new vehicle purchases, with Gen-X representing only 28% of total US sales, lower than the 34% of the Baby Boomers, but higher than the Millennials at 24%. This is a trend that has held for the past decade, with Gen-X averaging 27% of new vehicle sales, Baby Boomers averaging 33%, and Millennials averaging 24%. Interestingly, Millennials did overtake Gen-X back in 2012, making up 30% of new vehicle purchases vs. Gen-X at 25%. Even so, the larger sized Baby Boomers with a much higher share of income have continued to carry the US auto industry for the past two decades.

Across the same age range, Gen-X has underspent its Baby Boomer predecessors

Share of per capita income spent on new vehicles by Gen-X and Baby Boomers



Source: US Census Bureau, Goldman Sachs Global Investment Research.

Punching below their weight: Gen-X pragmatic when it comes to their wheels

The other interesting trend for Gen-X is the proportion of their income that is spent on new vehicles. As shown in the first chart, vehicle spend as a percentage of income lags Baby Boomer peers and even the Silent generation. This is partially due to Gen-X's higher average income levels more recently (Gen-X per capita income surpassed Baby Boomers for the first time in 2014). However, as automobile purchasing patterns vary over a person's life cycle, we compare similar age groups across the Baby Boomers (1990-1998) and Gen-X (2006-2014) on a per capita basis over time. This effectively captures and compares purchasing patterns by the two groups during average ages from 34 to 42. We find that while spending as a percentage of income did go down over time for both age cohorts (as incomes rose), Gen-X underspent the Baby Boomer generation by an average 130 bp during similar average ages in their life cycle (as above).

So, even as Gen-X has aged, it has not been spending as much as its predecessors on new vehicles. We believe this reflects the nature of the economic cycle experienced by Gen-X, which has left much deeper financial scars and a tougher job market from 2006 to 2014, relative to Baby Boomer peers during the 1990s. As a result, we believe Gen-X displays a more pragmatic buying behaviour when it comes to new vehicle purchases, allocating a higher percentage of income to other priorities. Extrapolating this to future demand, we do not expect to see a material positive inflection in new vehicle buying behaviour from Gen-X.

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Selling to Gen-X

Drew Borst, our US Media analyst, pays attention to the neglected generation

"I don't get no respect!"

Gen-X is the Rodney Dangerfield of generations: "I don't get no respect!" Demographers sometimes refer to Gen-X as the lost generation or transitional generation. The Pew Research Center called Gen-X, "America's neglected middle child." This starts with its size, or lack thereof. Gen-X, totalling 62 mn, is dwarfed by its two siblings, with the Millennials at 75 mn and Baby Boomers at 73 mn.

But it goes beyond mere population size. Demographers consider Gen-X less distinctive, less interesting and less dynamic than Millennials or Boomers. Gen-X is not easily categorized and, unlike its two siblings, Gen-X was never galvanized by a single social or political issue. Boomers were defined by the civil rights and women's movements, and by questioning authority. Millennials are the digitally-native generation that harnessed technology and social media to drive a socially progressive agenda, like ushering in gay marriage. Millennials are also a supremely self-confident bunch, undoubtedly aided by the ceaseless research and media attention.

In many ways, Gen-X is the mirror image of Millennials. Gen-X suffers from an inferiority complex. While Millennials are heaped with praise, Gen-X is slapped with a multitude of negative labels, like slackers, baby busters, the latch-key generation, and the "Why-me" generation.

Gen-X came of age amid a multitude of negative trends and events. For starters, there was the rising divorce rate, which begot the "latch-key" generation label. The divorce rate peaked in 1980, when many Xers were moving into the formative teens. The crime rate was also on the rise in the 1980s and 1990s, peaking in 1992 when Xers were in their mid-teens to mid-20s. There was the 1980s AIDS spurt, the 1987 stock market crash and the 1990 Persian Gulf War. All of this weighs on the psyche of Gen-X and it should come as no surprise that Gen-X is generally a cynical group.

And given this profile, maybe it is no wonder that Madison Avenue gives Gen-X no respect, even though Gen-X, at 37-51 years of age currently, is squarely in Madison Avenue's vaunted adult 18-49 (A18-49) target demographic. Here, Gen-X is once again disadvantaged by its comparative size. Within the A18-49 demo, the Millennials actually comprise the majority of the population, at 61%, versus Gen-X at 39%.

In addition to size, Millennials command so much attention from Madison Avenue because their media habits are changing rapidly and differ from the rest of the US population.

For starters, Millennials under-index on traditional pay TV services offered by cable, satellite and telco providers.

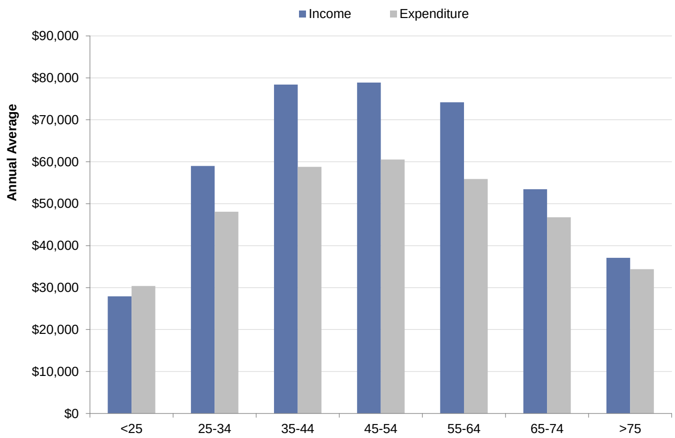
Next, Millennials over-index on "new" technology that, in many cases, is a substitute for traditional TV. From subscription VOD services (e.g., Netflix) to smart TVs to tablets and smartphones, penetration of these devices and services is consistently higher among Millennials compared to the total population.

As a consequence of these two trends, the Millennials consume much less live TV than the rest of the population. Needless to say, live TV is still the bedrock of TV advertising. Millennials consume an average of 2.5 hours of live TV per day, which is 53% less than the average for the rest of the adult population of 5.35 hours. Compared to Gen-X, Millennials watch 35% less live TV. Gen-X falls right in the middle of Millennials and Boomers.

It is surprising that marketers give Gen-X short shrift because this generation is now peaking in terms of income and spending. According to the Bureau of Labor Statistics, Gen-X (35-54) has the highest income and consumer expenditure of any age cohort (below). Gen-X average income is 33% higher than Millennial and expenditures are 24% higher. Gen-X accounts for 31% of total consumer spending vs. its 20% share of the US population.

At the top

Income versus expenditure for US by age group



Source: BLS.

Maybe there is hope yet for Gen-X to get some respect from Madison Avenue. The advertising industry's obsession with age and gender demos is fading in favour of behavioural targeting. With behavioural targeting the data, like purchasing power, trumps axioms and stereotypes like A18-49. Demographic targeting is imprecise and wasteful next to behavioural targeting, where online publishers use web-browsing behaviour to increase advertising effectiveness. TV advertising must develop the tools to compete against online behavioural targeting or TV advertising itself runs the risk of become an anachronism.

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The generational gap in politics

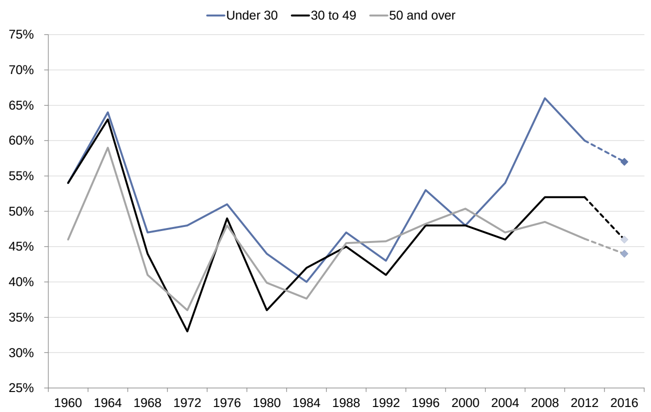
Alec Phillips discusses the impact of demographics on US politics

The return of the generational gap in US politics

Not long ago, political preferences did not vary much by age. However, differences across generations have become more prominent, with a modest gap in political preferences between the old and young appearing in 2004, and growing significantly wider in 2008. The gap narrowed slightly in 2012, but recent polling suggests that the pattern may hold once again this year, with voters under 30 supporting Democrats in much stronger numbers than older voters, including Gen-X (shown, along with the oldest portion of Millennials, in the middle age group in the exhibit below).

Voting share

Democratic vote share by age group



Source: New York Times, Roper Center, Gallup, Public Policy Polling.

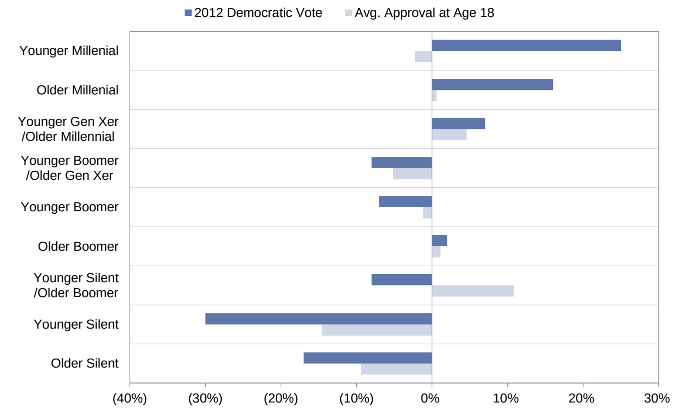
The transition of Generation X from youth to middle age may be one piece of the puzzle. When Gen-Xers began to reach voting age, they were more Republican-leaning than the Baby Boomers who came before them, or the Millennials who followed. A common potential explanation is that the period during which Gen-Xers came of age included two fairly popular Republican presidents (Reagan, 1981-1989; Bush, 1989-1993). Recent academic research has attempted to link these two factors more directly, by using the president's approval rating during a cohort's formative years to predict partisan leanings. The formative years are subject to interpretation, though one analysis finds that ages 14-24 are most important, with age 18 the single most important year; not surprisingly, political developments after age 45 are demonstrated to have little effect.

Of course, generations are not monolithic. Public opinion polling from the Pew Research Center that breaks down voting intentions in the 2012 and 2014 elections by birth year suggests that older Gen-Xers had more in common with younger Baby Boomers in the last few elections than they did with younger Gen-Xers, who were more Democratic leaning and whose politics more closely resemble Millennials.

The next exhibit breaks down each generation into two or three pieces, organized by the presidential term in which they reached age 18, and the approval rating of that President organized by Democratic advantage (for example, a popular Democratic president produces a positive score; an unpopular Republican president would also produce a positive score, while a popular Republican would produce a negative score). The oldest Gen-Xers came of age during the Reagan/Bush years and have tended to lean Republican since then. By contrast, the youngest Gen-Xers did not reach age 18 until later in the Clinton administration, along with the oldest Millennials. In both cases, the political sentiment during their formative years is in line with their recent political preferences.

Political preferences

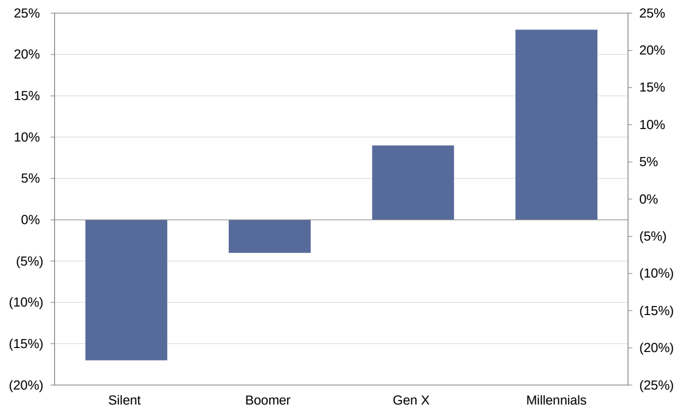
Approval rating of the President by Democratic advantage for an average 18 year old vs. all ages



Source: Pew Research Center. The American Presidency Project at University of California Santa Barbara. Goldman Sachs Global Investment Research.

Election polling

June 2016; Clinton minus Trump



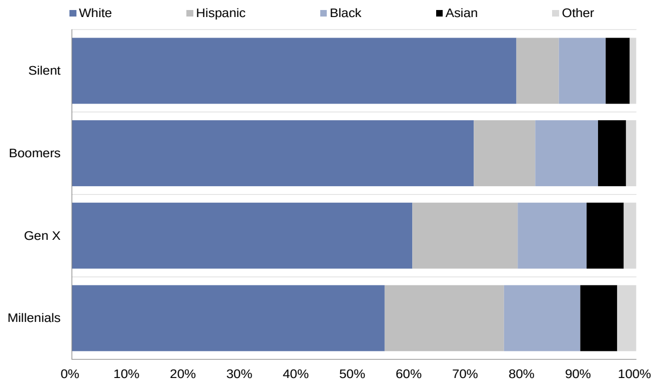
Source: Quinnipiac Poll, June 29, 2016.

However, taken together Generation X appears to lean Democratic (exhibit above) in recent polling, perhaps slightly more than might be expected given their prior voting behavior, and looks likely to support Sec. Clinton over Mr. Trump in November's Presidential election.

There are likely a variety of factors at play behind Gen-X's previous Republican leanings and their current net Democratic support, but we note three considerations: first, Generation X is much more racially and ethnically diverse than prior generations (following exhibit). In the last several elections, non-white voters have been strong supporters of Democratic candidates, on average; this pattern may be obscuring some of the generational influence.

Population diversity

Racial and ethnic distribution of population by generations



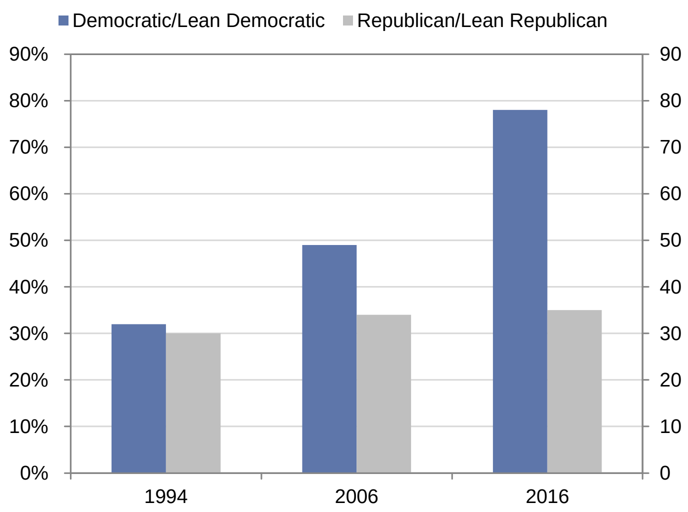
Source: Current Population Survey, May 2016.

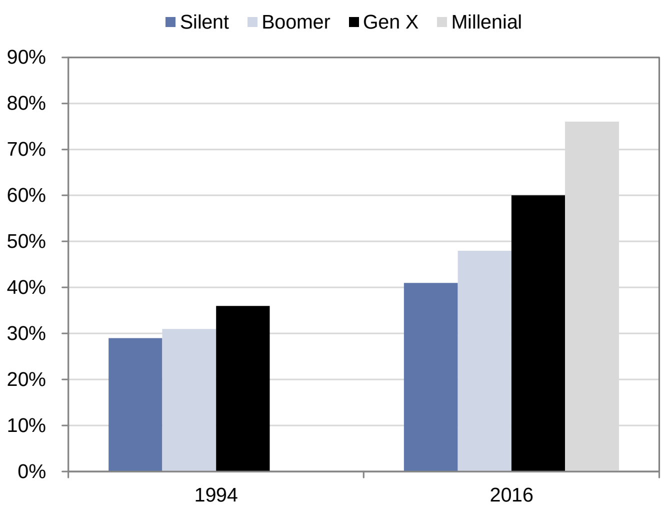
Second, Gen-Xers might have less in common with Mr. Trump on policy than they have had with prior Republican presidential candidates. For example, Gen-Xers have been more focused on the budget deficit and the fiscal situation than any other generation (Mr. Trump's plans would be costly, according to most independent analyses), and they have generally supported a more internationalist approach, including greater support for the wars in Iraq and Afghanistan than any other generation and net support for free trade agreements. On immigration, a key issue for Mr. Trump, Gen-Xers see more benefits to immigration than prior generations, though not as much as Millennials. However, a significant partisan divide has opened up on the issue, where none really existed when Gen-Xers started voting a quarter-century ago (final exhibit). The divergence on issues like this one might explain why Gen-Xers seem to be supporting Democrats to a greater degree than they did in the past.

Third, and perhaps most importantly, the partisan differences between Gen-X and other generations have faded somewhat since Gen-Xers first began to vote. In 1992, Generation X was split roughly equally between Republican-leaning voters and Democratic-leaning voters; older generations were all more heavily Democratic-leaning. However, while the older generations have become more conservative, Xers have become more Democratic leaning: 49% identified as Democratic-leaning in 2014, compared with 38% Republican-leaning. This may partly reflect the fact that older Xers were more conservative than the young end of the generation, so the generation as a whole shifted Democratic as its voting age population grew. It may also reflect national sentiment, since some similarities are seen across generations; for instance, all generations leaned a bit more Democratic around the time of the financial crisis. Regardless, it suggests that Generation X might help the Republicans a bit less this year than they have in some previous elections.

Survey conducted by Pew Research

Percent who say immigrants strengthen the country due to their hard work and talents





Source: Pew Research Center.

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Disclosure Appendix

Reg AC

We, Hugo Scott-Gall, Sumana Manohar, Richard Edwards, Alexander Blostein, Bernard Grayson, Patrick Archaumbault, David Tamberrino and Drew Borst, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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