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Beyond Today's Financial Headlines

A Lost Generation? Young Families after the Great Recession

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Federal Reserve Bank of St. Louis

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Ray Boshara, director, Center for Household Financial Stability

Federal Reserve Bank of St. Louis

SETTING THE STAGE

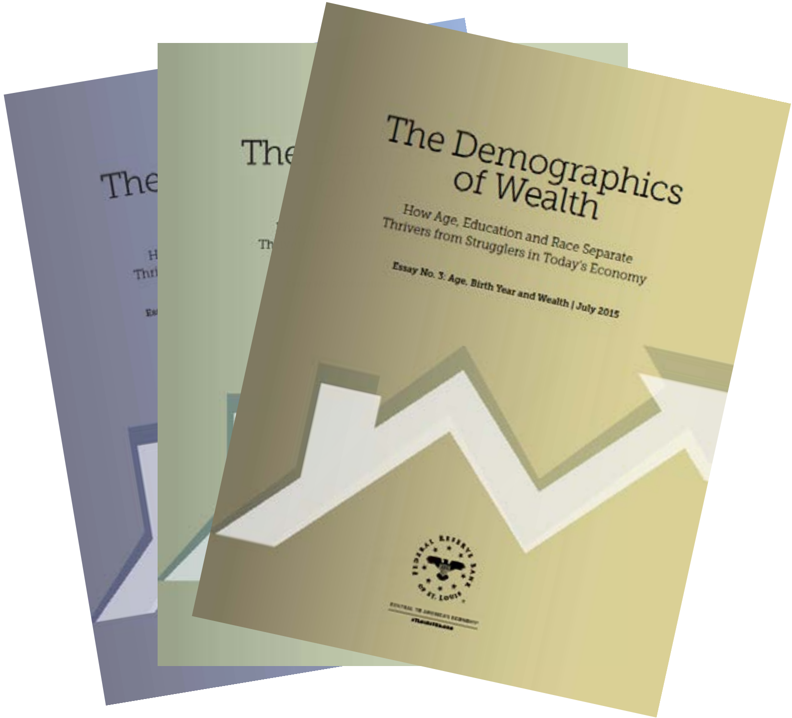
Lowell R. Ricketts, lead analyst, Center for Household Financial Stability
Federal Reserve Bank of St. Louis

PRESENTATION

Overview

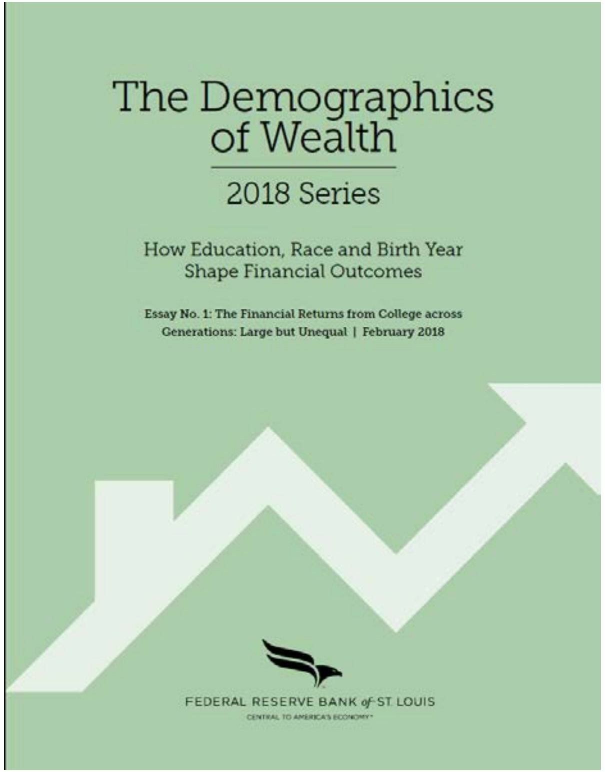
- Introducing the *Demographics of Wealth*
- The Lasting Impact of the Great Recession
- Exploring the Life Cycle of Wealth
- When You Were Born Matters: Wealth Outcomes of Generations
- Why Were Young Families Hit So Hard?
- Will the 1980s Cohort Become a “Lost Generation”?

The Demographics of Wealth



- Three essays written by Center staff in 2015.
- The series explores the connection between wealth and a person's race/ethnicity, education and age.
- These three factors increasingly predict which families struggle and thrive.

The Demographics of Wealth Redux

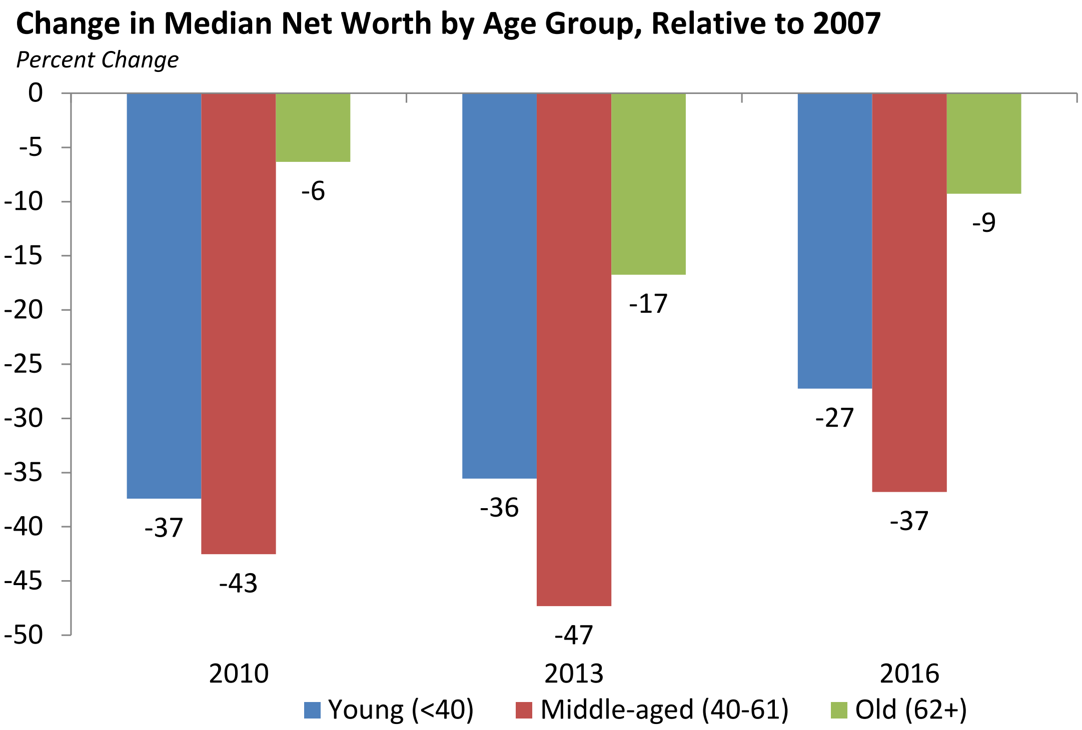


- The new series uses 2016 data from the Survey of Consumer Finances (SCF).
- It explores connection between financial outcomes and the education of both a family and their parents.

The Lasting Impact of the Great Recession

- The Great Recession of 2007-09 inflicted deep and widespread losses to wealth across American families.
- While wealth losses occurred across the age spectrum, the extent of the damage has been unequal.
- Younger families suffered the most and have rebounded slowly.

Wealth Losses Unevenly Distributed



Source: Federal Reserve Board's Survey of Consumer Finances.

- The decline in median wealth among older families (62+) was milder.
- The median wealth among middle-aged (40-61) & young (<40) families remains well below pre-recession values.

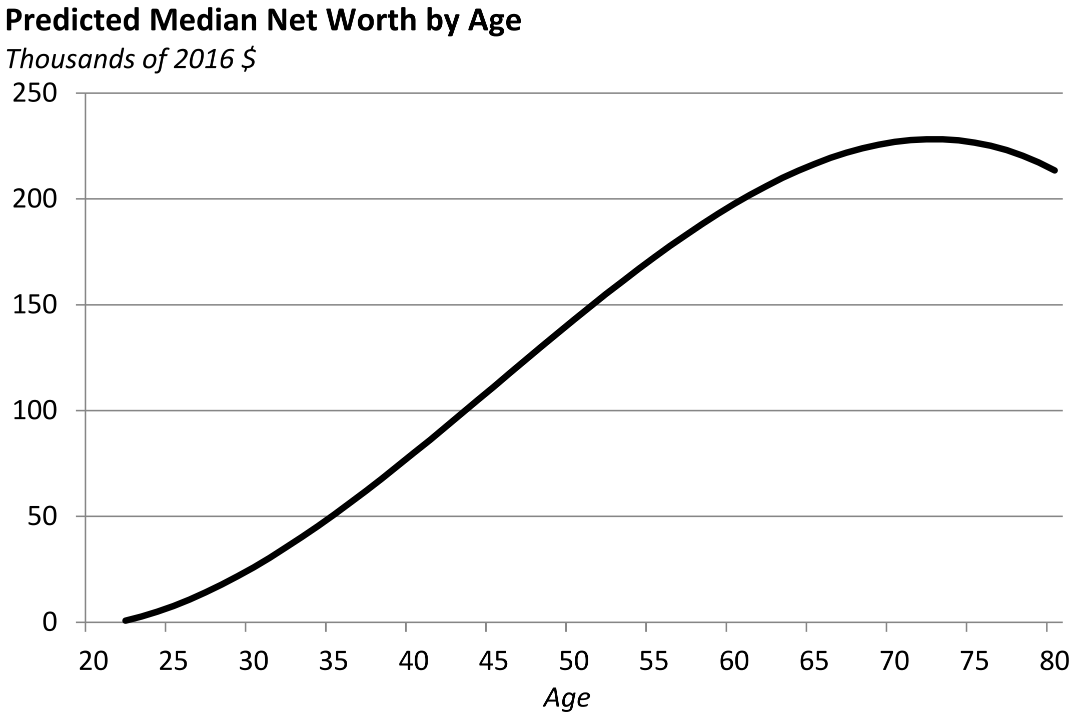
Can Families Recover What They Lost?

- For the families that lost the most wealth, how likely are they to recover in time for major goals?
  - First home purchase
  - College tuition for their children
  - Retirement
- Will young or middle-aged families at the advent of the recession become part of a “lost generation” that struggles to achieve life’s financial milestones?

The Life Cycle of Wealth

- The life cycle of wealth sounds complicated but you may find it pretty intuitive.
- When you’re young, your earnings are typically at their lowest, and you haven’t had much time to save.
- By middle age, your income is close to its maximum and you (hopefully) start to build a sizable savings.
- As you reach your elder years, you eventually retire and draw down your savings in the form of income.

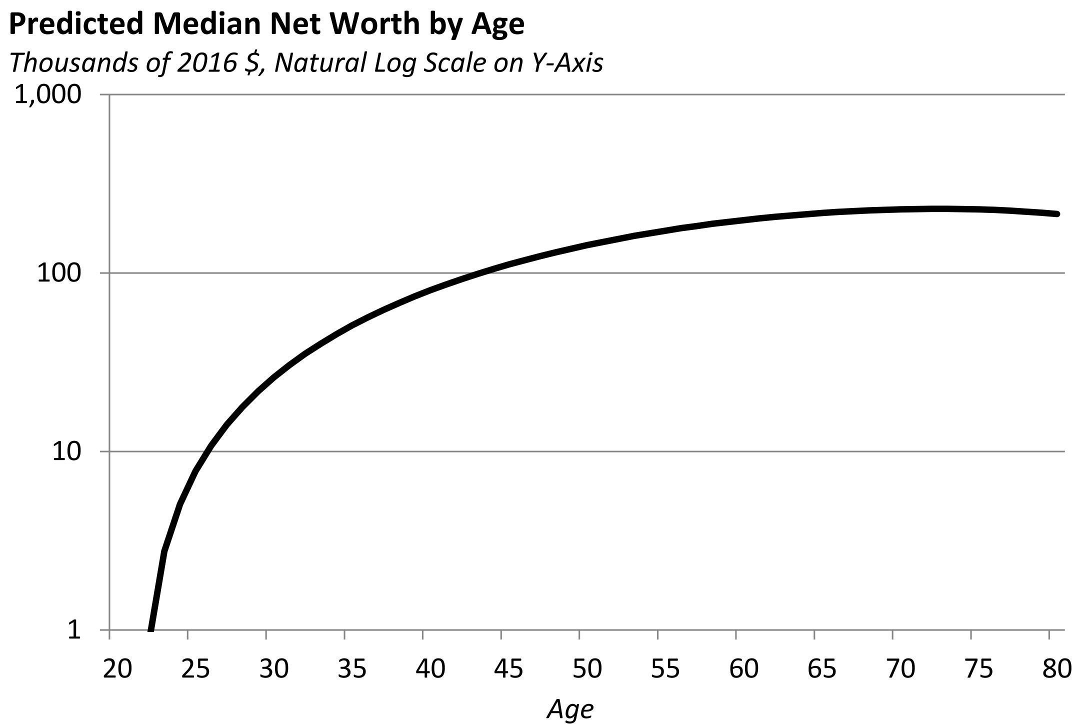
The Life Cycle of Wealth



Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- The classical life cycle is represented as a hump shaped trend.
- This trend line is estimated from responses from 47,776 families in the SCF between 1989 and 2016.

The Life Cycle of Wealth (Transformed)



Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- We transform the scale because wealth accumulation is a compounding process.
- Using this approach, equal vertical distances represent equal percentage differences.

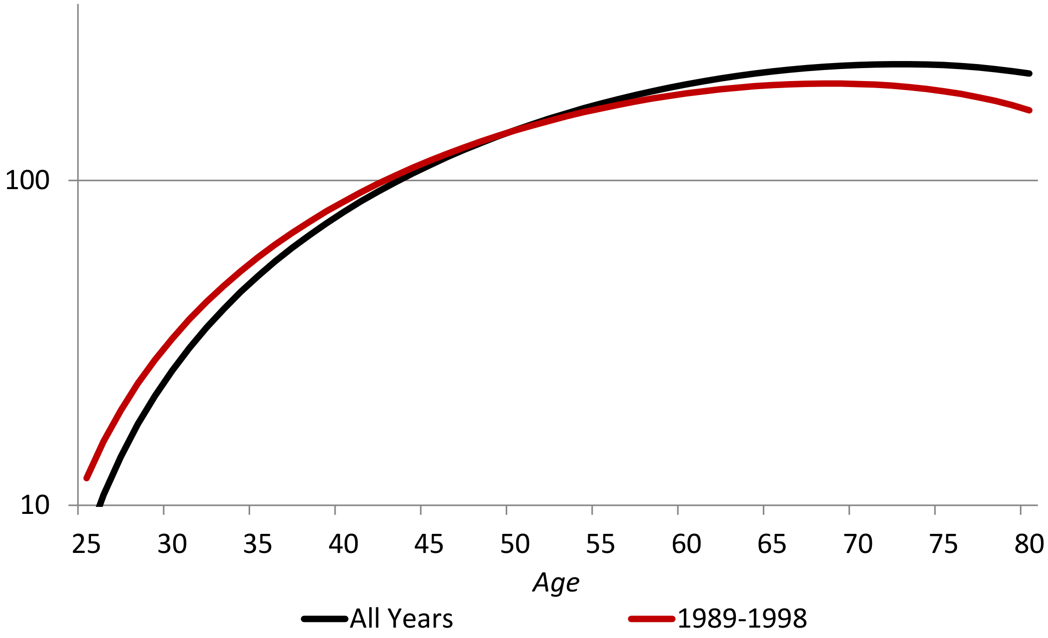
Estimating The Life Cycle of Wealth

- The life cycle that we estimate removes the effects that are associated with taking the survey in a specific year.
- Having removed these effects, we capture the underlying relationship between wealth and age.
- In other words, time-specific factors can increase (or decrease) predicted wealth.
- Comparing the underlying trend to those estimated for specific years helps to illustrate these effects.

The Pre-Housing Bubble Period

Predicted Median Net Worth by Age and Survey Year

Thousands of 2016 $, Natural Log Scale on Y-Axis

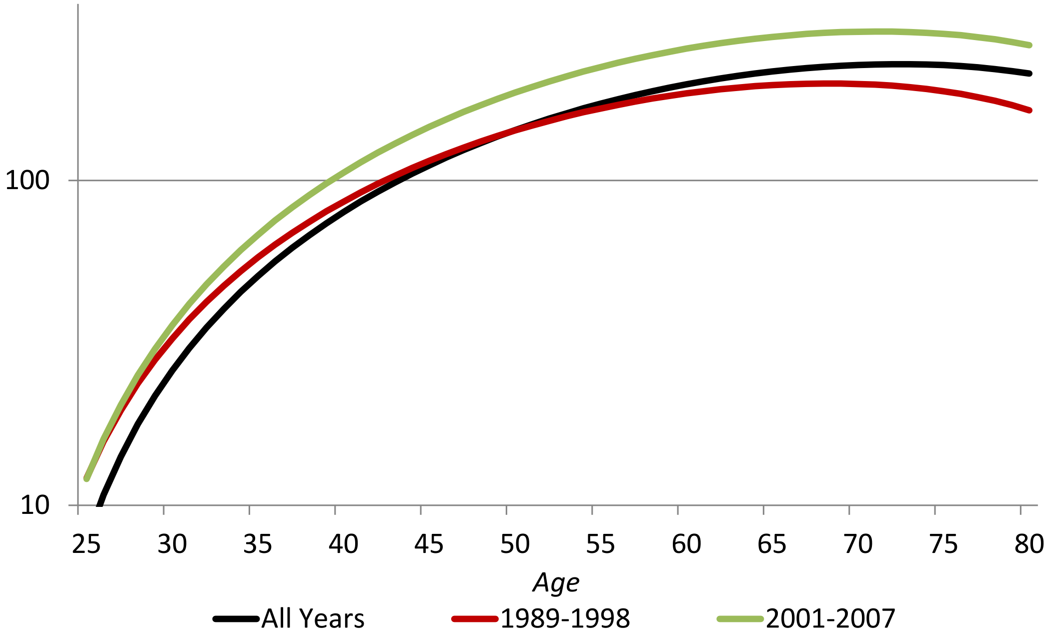


Sources: Federal Reserve Board's Survey of Consumer Finances,and authors' calculations.

- As compared to the long-run life cycle, the 1990s featured…
- Greater predicted wealth among families under 45: +$6,600 at age 30.
- Lower predicted wealth among those over 55: -$28,600 at age 70.

The Housing Bubble Period

Predicted Median Net Worth by Age and Survey Year
Thousands of 2016 $, Natural Log Scale on Y-Axis



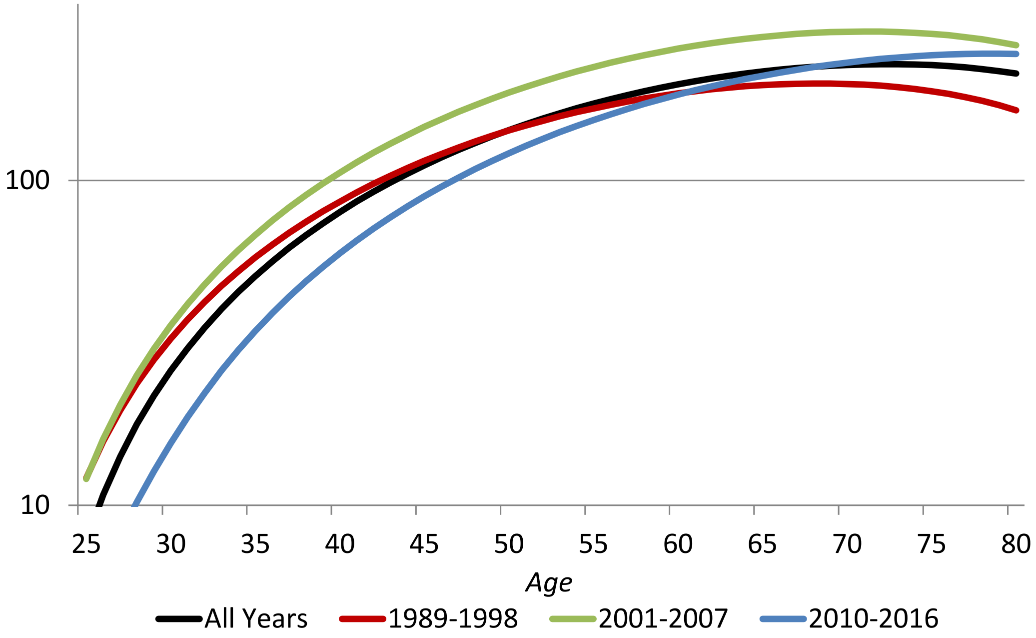
Sources: Federal Reserve Board's Survey of Consumer Finances,and authors' calculations.

- Early to mid-2000s had greater predicted wealth for families of all ages: +$60,300 at age 70.
- Further gains for predicted wealth among young families: +$9,800 at age 30.
- Some of this wealth effect was illusory.

The Post-Great Recession Period

Predicted Median Net Worth by Age and Survey Year

Thousands of 2016 $, Natural Log Scale on Y-Axis



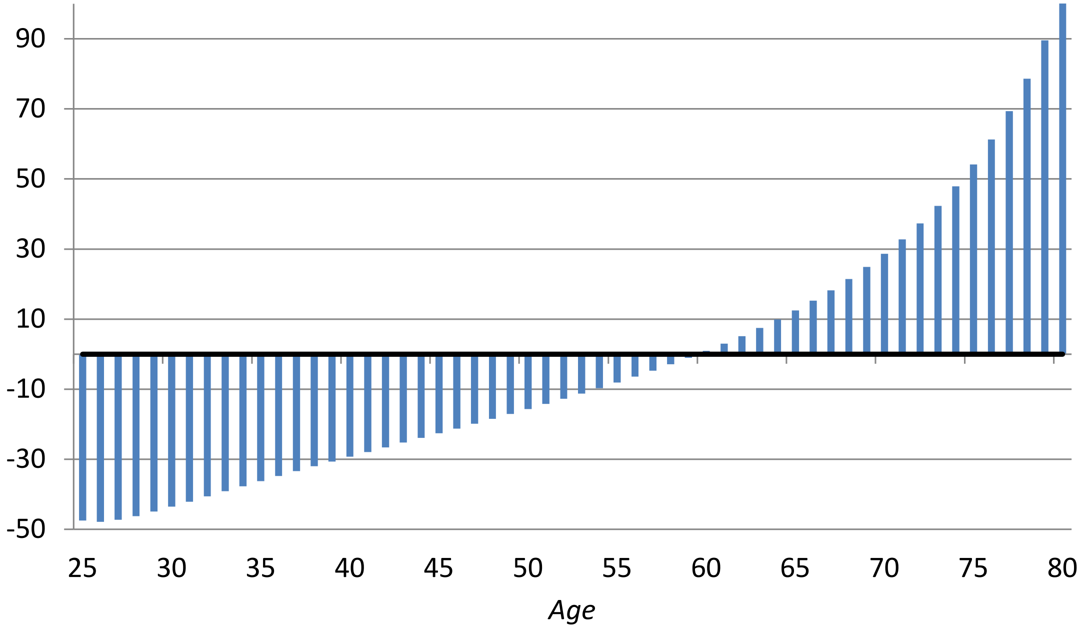
Sources: Federal Reserve Board's Survey of Consumer Finances,and authors' calculations.

- The late 2000s and early 2010s featured a reduction in *almost* all levels of predicted wealth.
- The fall was particularly severe for young families: -$10,500 at age 30.
- Families typically in retirement were still over trend: +$3,800 at age 70.

The Changing Fortunes of Age

Change Between 1989 and 2016 in Predicted Wealth

Percentage Difference



Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- The age of 60 marks a turning point in predicted wealth.
- Since 1989, all families younger than 60 have lower predicted wealth; all families older than 60 have greater predicted wealth.

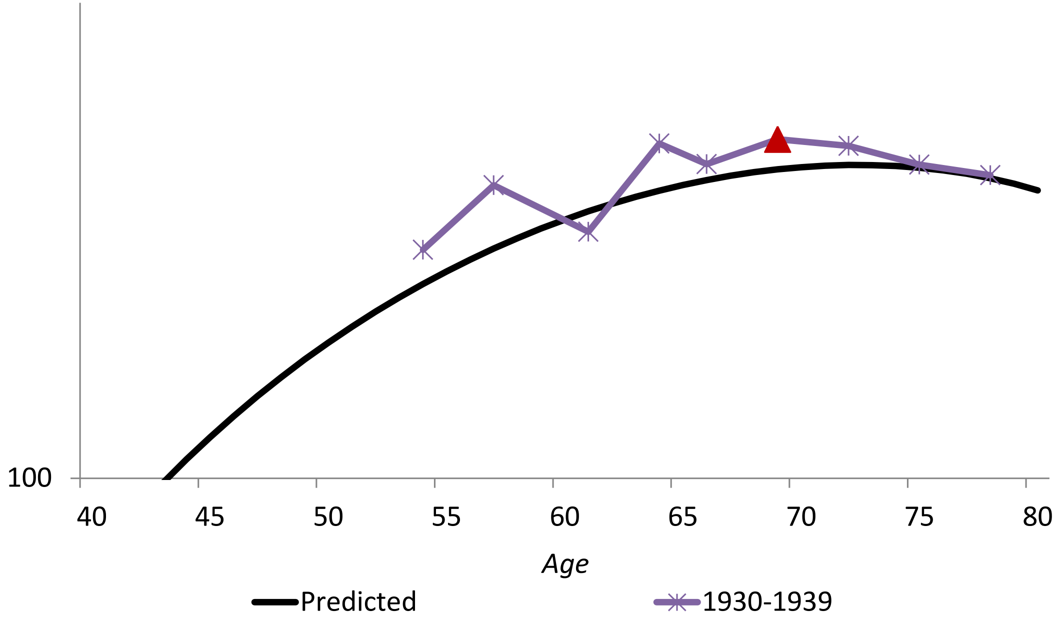
When You Were Born Matters

- Given substantial shifts in predicted wealth by age, when you reach age milestones is important.
- To understand how members of particular birth years have fared, we track six decade-long cohorts over time:
  - Family heads born in the 1930s, 1940s, 1950s, 1960s, 1970s and 1980s.
- To be clear, we don’t track individual families across time; instead, we use “quasi-panels” of families.

Born in the 1930s

Median Net Worth, Predicted vs. Actual, by Age and Birth Cohorts

Thousands of 2016 $, Natural Log Scale on Y-Axis



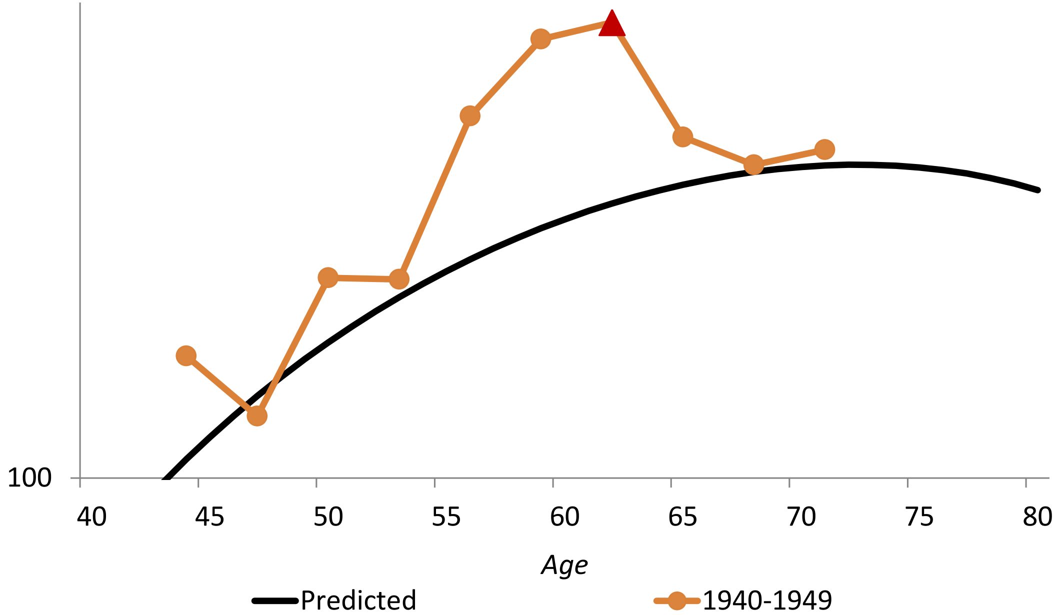
Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- Over the course of the SCF, these families have exceeded predictions.
- This cohort lost wealth after 2007 but remained above their age-specific benchmark.
- Observed wealth in 2016 is roughly as predicted.

Born in the 1940s

Median Net Worth, Predicted vs. Actual, by Age and Birth Cohorts

Thousands of 2016 $, Natural Log Scale on Y-Axis



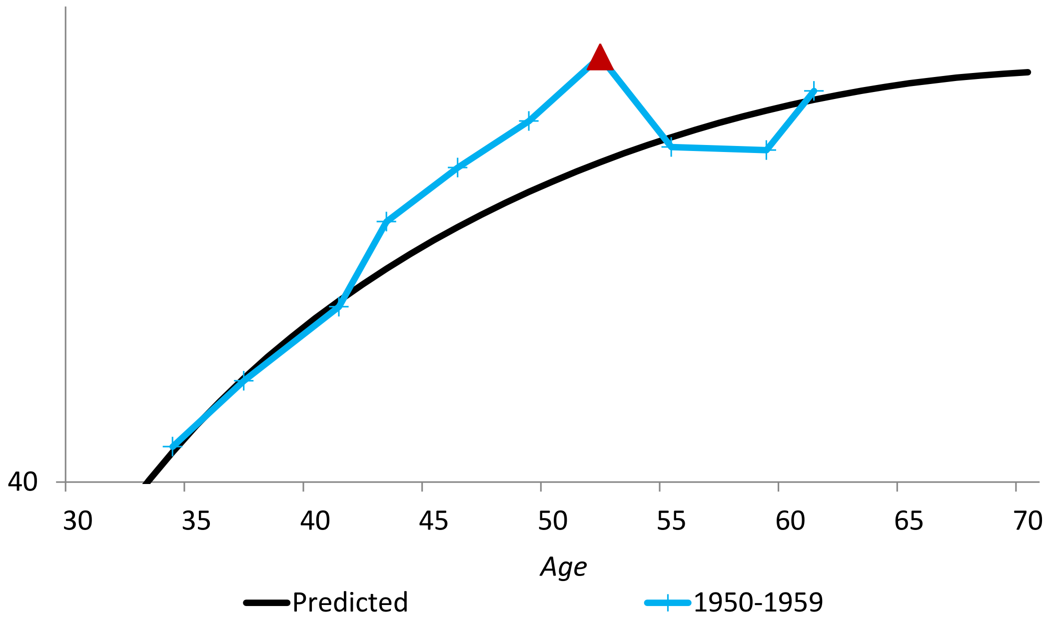
Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- The Great Recession reined in an impressive wealth advantage for this cohort.
- However, like the 1930s cohort, wealth levels remain at the benchmark.

Born in the 1950s

Median Net Worth, Predicted vs. Actual, by Age and Birth Cohorts

Thousands of 2016 $, Natural Log Scale on Y-Axis



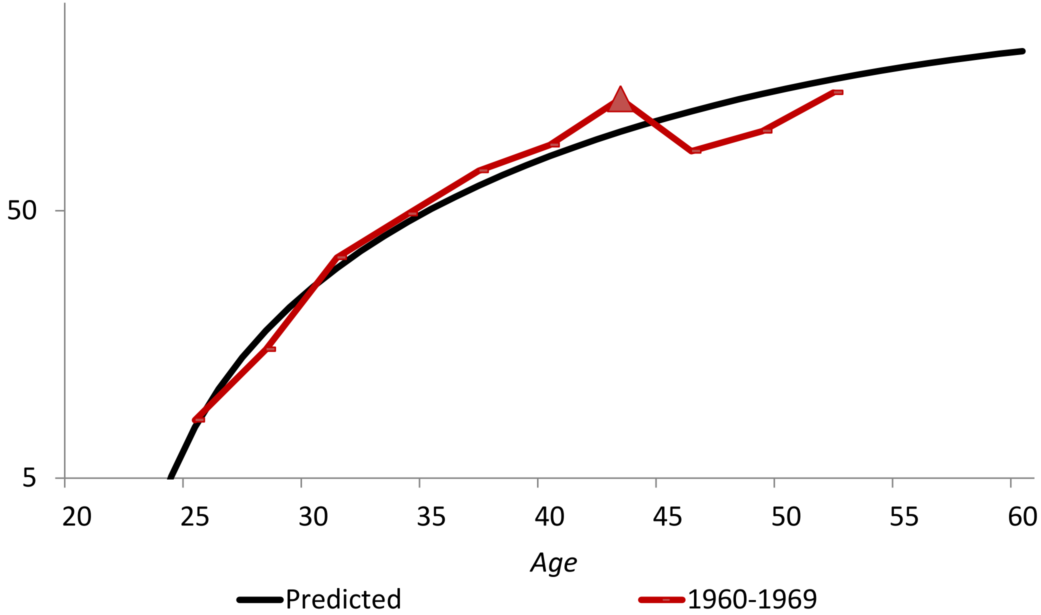
Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- The typical family in the 1950s cohort saw their wealth fall below predicted levels in 2010 and 2013.
- However, their median wealth rebounded in 2016 and again is exceeding the benchmark.

Born in the 1960s

Median Net Worth, Predicted vs. Actual, by Age and Birth Cohorts

Thousands of 2016 $, Natural Log Scale on Y-Axis



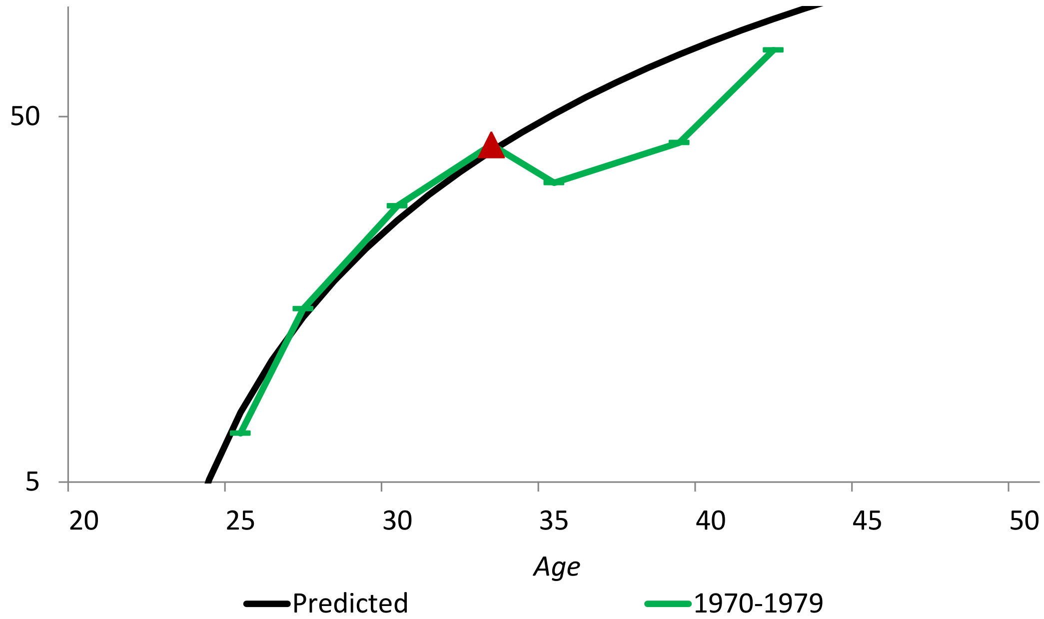
Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- The 1960s cohort was knocked well below benchmark levels by the recession and remained below them through 2016.
- The 1960s cohort was, on average, 52 years old in 2016.
- Recall the earlier split seen at age 60.

Born in the 1970s

Median Net Worth, Predicted vs. Actual, by Age and Birth Cohorts

Thousands of 2016 $, Natural Log Scale on Y-Axis



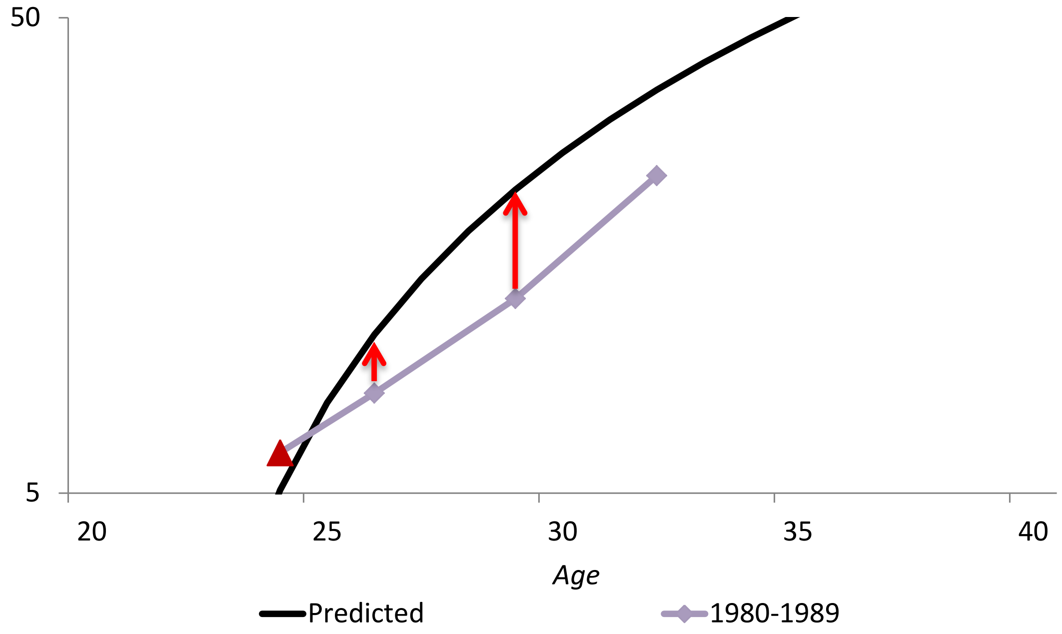
Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- The 1970s cohort also experienced a severe deviation from predicted wealth levels following the recession.
- The typical family within this cohort recovered a sizable amount of wealth in 2016 but remains below predicted values.

Born in the 1980s

Median Net Worth, Predicted vs. Actual, by Age and Birth Cohorts

Thousands of 2016 $, Natural Log Scale on Y-Axis



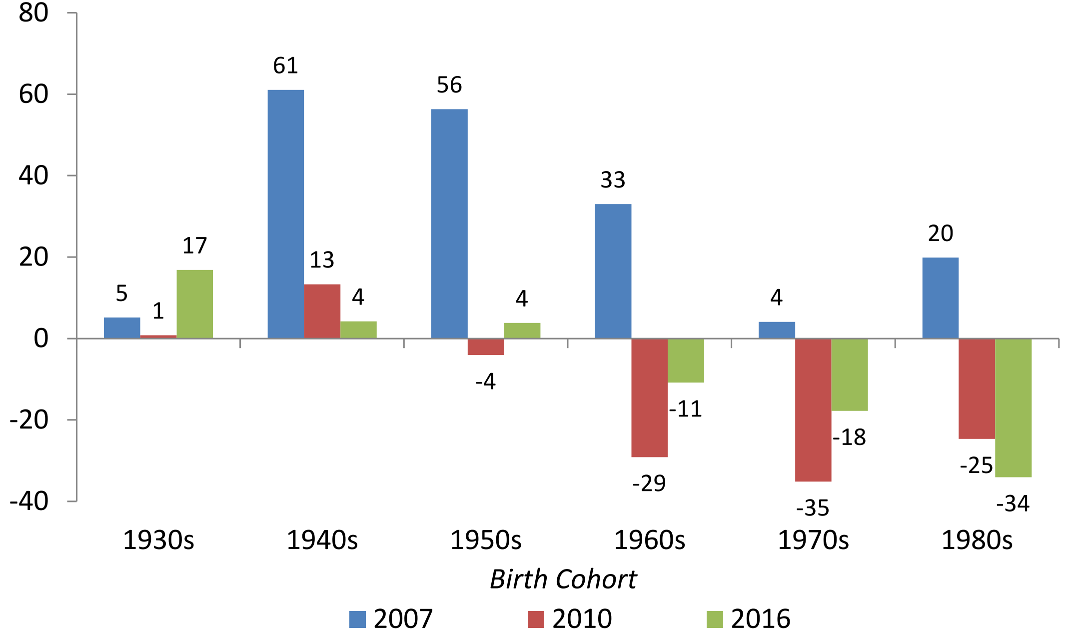
Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- The 1980s cohort not only suffered a severe setback from the recession but drifted further from predicted values between 2010 and 2013.
- Joining the 1960s and 1970s cohort, the typical family born in the 1980s has yet to regain their predicted wealth.

Which Generations Are Back on Track?

Deviation of Birth Cohort Median Wealth from Predicted Value

Percentage Points



Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- Cohorts born before 1960 were above benchmark levels in 2016.
- Cohorts born in 1960 or later were below predicted wealth levels.
- The 1980s cohort slipped noticeably further behind between 2010 and 2016.

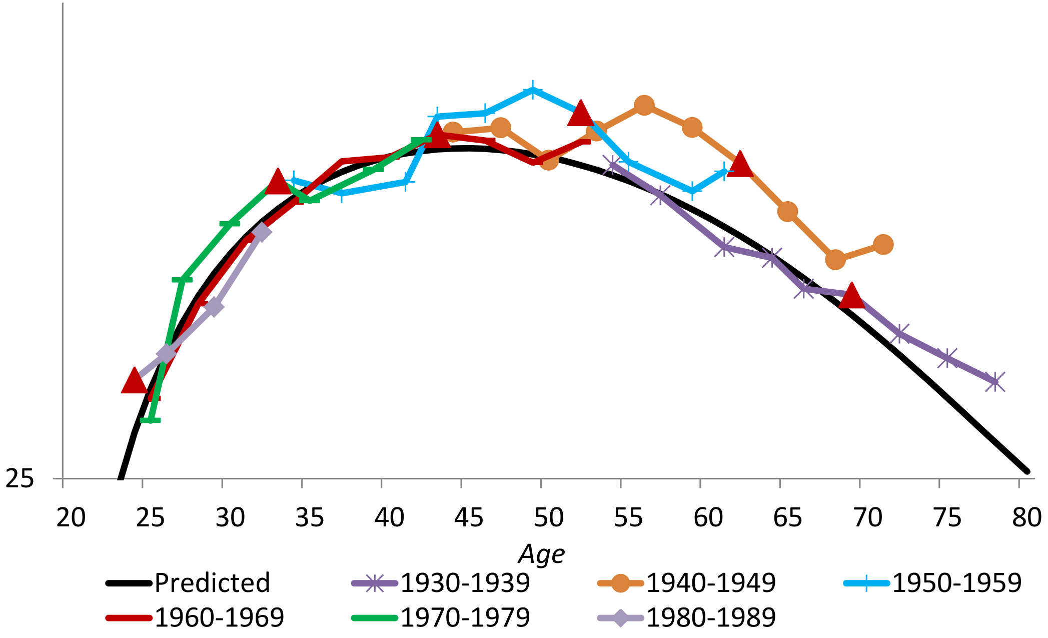
Why Were Young Families Hit So Hard?

- To shed more light on this question—and to gauge their potential to recover—we look at trends in income, saving and several financial indicators.
- Perhaps surprisingly, income and saving trends appear to be relatively unimportant.
- At the same time, other indicators—debt and homeownership—may have had an important role.

Income Gaps? Not Readily Apparent

Median Income, Predicted vs. Actual, by Age and Birth Cohorts

Thousands of 2016 $, Natural Log Scale on Y-Axis

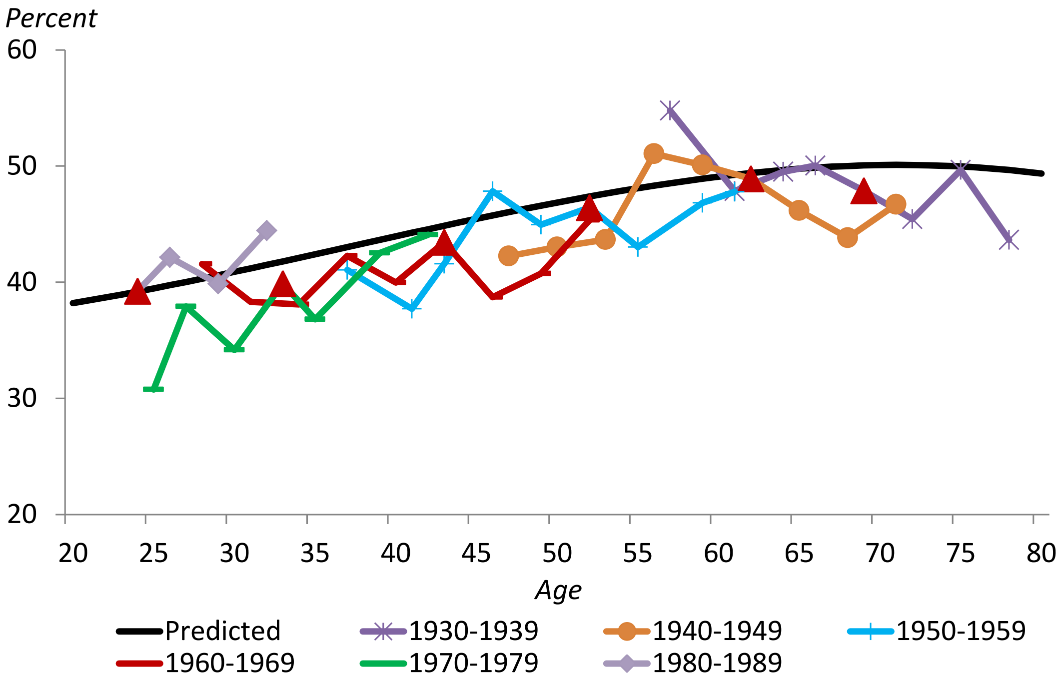


Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- Relative to the income life cycle, the typical family born in the 1960s, 1970s and 1980s fared well.
- Families born before 1960 did even better.
- Income gaps, before or after the recession, don't appear to be an important source of wealth shortfalls.

Different Saving Shares? Not Likely

Saving Share, Predicted vs. Actual, by Age and Birth Cohorts

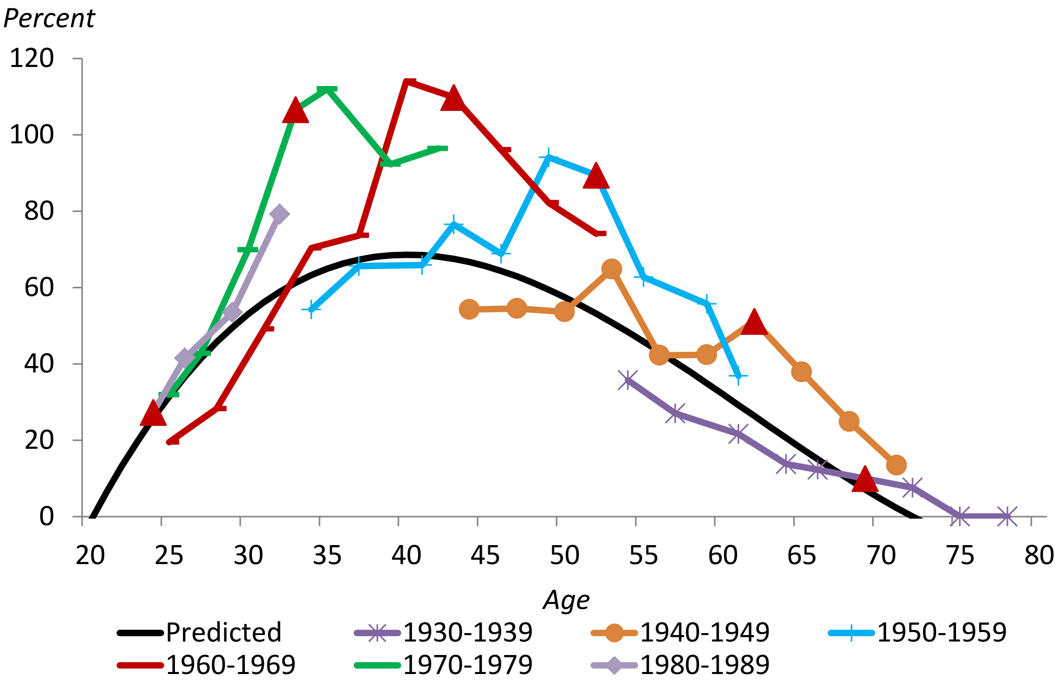


Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- As with income, there is nothing unusual about saving habits of younger cohorts.
- Despite a larger wealth shortfall, the 1980s cohort has a notably higher saving rate than the 1970s cohort.

Debt Burdens? They Certainly Stand Out

Median Debt/Income, Predicted vs. Actual, by Age and Birth Cohorts

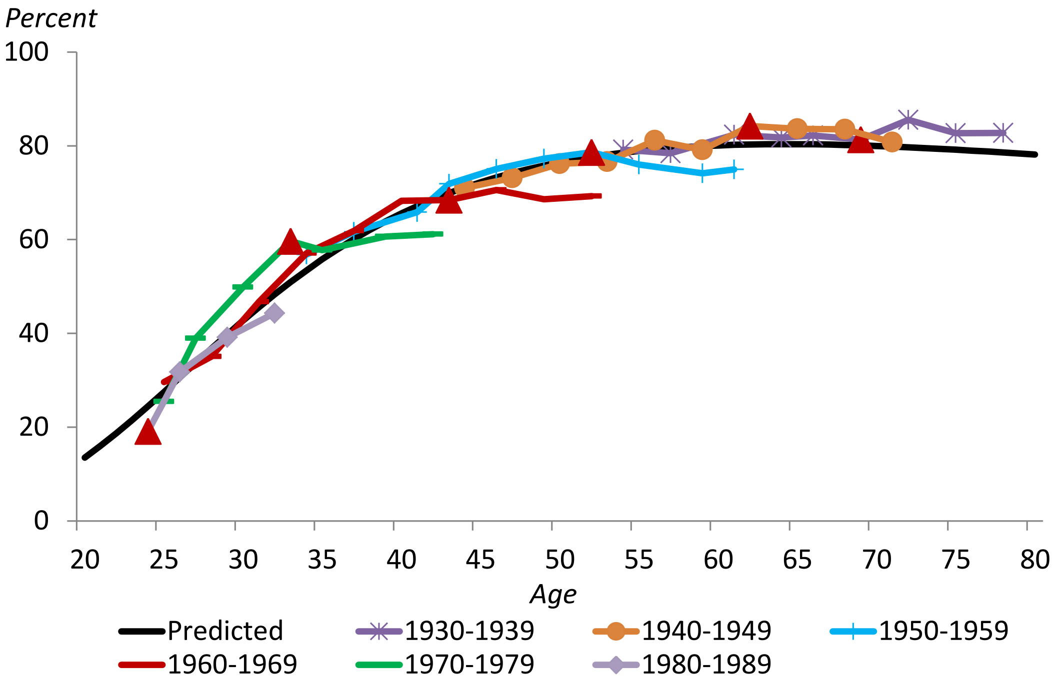


Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- Starting with families born in the 1930s, each successive cohort generally has held more debt relative to income.
- Although 1980s families were very young during the bubble, they also look highly debt-burdened.

Housing Crisis? Looks Plausible

Homeownership Rate, Predicted vs. Actual, by Age and Birth Cohorts

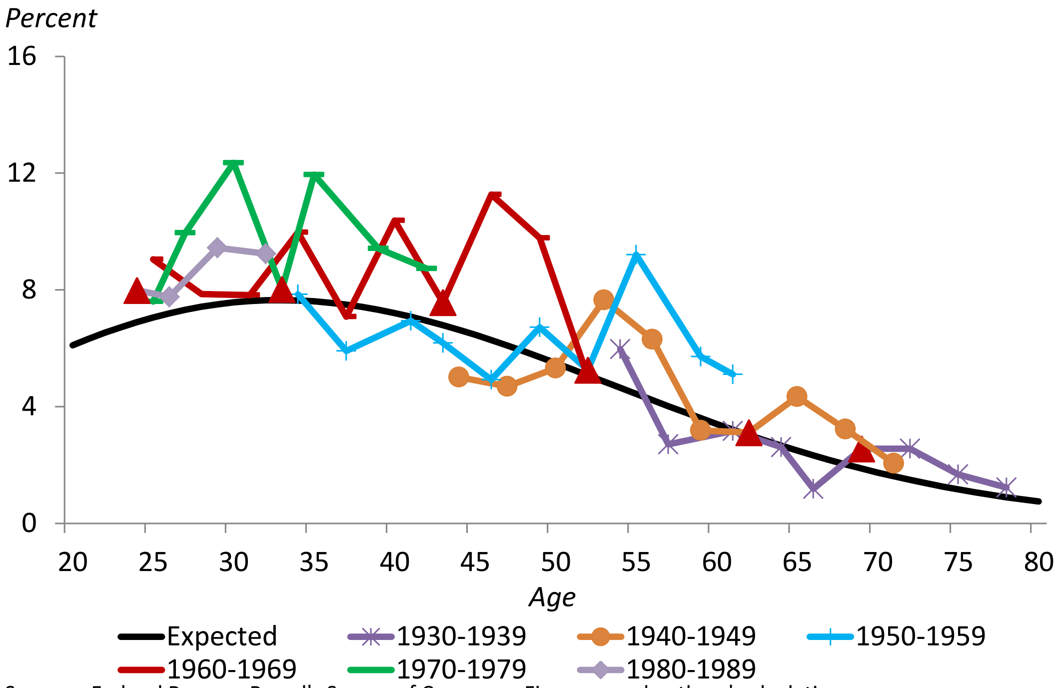


Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- Families born in the 1960s and 1970s had high homeownership rates prior to the Great Recession.
- By 2016, those groups' homeownership rates had fallen significantly below predicted levels.
- This does not explain lower wealth for the 1980s cohort.

Financial Hardship? Looks Elevated

Delinquency Rate, Predicted vs. Actual, by Age and Birth Cohorts



Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- Debt delinquency rates have been high for all cohorts born in 1960 and later, a sign of burdensome debt.
- Both the 1970s and 1980s cohorts have always exceeded the delinquency benchmark.

Housing Was Key for 1960s, 1970s Cohorts

- Together, high debt ratios, high homeownership rates and high delinquency rates spelled trouble for families born in the 1960s and 1970s.
- Housing and mortgage debt likely played a role in the wealth losses seen during the Great Recession.
- Conversely, as home values recovered in recent years, many of these homeowners benefited, as evidenced by closing gaps between actual and predicted wealth.

Families Born in the 1980s Are Different

- In 2007, only 19 percent of 1980s families were homeowners.
- Instead of mortgages, student loans, credit card debt, and auto loans were a key source of leverage.
- Unlike stocks and real estate, these debt-financed assets haven’t rapidly appreciated in the last few years.
- Recall that the 1980s cohort was unusual in falling further behind wealth benchmarks from 2010-2016.

Is the 1980s a “Lost Generation”?

- The high returns on housing and financial assets in recent years are unlikely to continue in future years.
- Thus, catching up to the wealth benchmarks set by earlier generations is possible − but no simple feat.
- Income and homeownership trends have been unexceptional for the 1980s cohort so far.
- The challenge faced by the typical 1980s family should not be underestimated.

A Case for Optimism

- Two key factors on the side of 1980s-born families are time and education.
- These families have many more years to earn, save and accumulate wealth.
- This is the most highly educated generation; it’s possible that their income and wealth trajectories will be steeper.
- It’s far too soon to know whether families born in the 1980s will catch up; we will have to wait and see.

If You Were Born in the 1980s…

- Build wealth—start saving early, and diversify assets and risks.
- Keep debts low and tied to appreciating or income-generating assets.
- Build education and skills early and throughout life.
- Avoid over-investing in housing; a home purchase shouldn't deplete your liquid savings buffer.

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