The Next Greatest Generation: Big Problems Will Require Bold Solutions

By Michael Arone, CFA, Chief Investment Strategist
US SPDR Business

“I don’t believe in any greatest generation. I believe in great events. They sweep ordinary people up, expose them to extremes of human behavior and unimaginable tests of integrity and courage, and then deposit them back on the home front.”

— Phil Klay

Hey, Big Spender

Shameful. On July 22, White House and Congressional negotiators agreed to increase federal spending and raise the government’s borrowing limit. This deal for more than $2.7 trillion in spending over two years would suspend the debt ceiling until the end of July 2021. Increasing spending by nearly $50 billion for the next fiscal year, the agreement provides for $320 billion in spending over two years, beyond the limits set in 2011’s sequester that established automatic spending cuts.¹

This deal, which still must pass both chambers of Congress and be signed by President Trump, avoids a fiscal crisis by splashing more red ink on a deficit that has already surged to more than $1 trillion. While it might not be possible to determine exactly when this irresponsible behavior will wreak havoc on the world, some fascinating research about generations may provide insight into which generation will most likely solve what might be our nation’s greatest future challenge.

Keep the Voters Happy, but Debt Matters

Predictably, all the tough talk about significant government spending cuts from the Trump administration and Republican fiscal hawks has been tossed out the window in advance of what is sure to be a brutal election year. Go figure, wasteful spending that will burden future generations with mountains of debt and further fuel the deficit is the one thing that Republicans and Democrats can agree on.

Figure 1: The US Budget Deficit has Historically Fluctuated, but It Is Set to Remain Consistently High in the Next Decade

Source: Congressional Budget Office. 2019 Long-Term Budget Outlook, June 2019.
The Next Greatest Generation: Big Problems Will Require Bold Solutions

The nonpartisan Committee for a Responsible Federal Budget estimates that the deal will add roughly $1.7 trillion to projected debt levels over the next decade. Folks, we already have a form of Modern Monetary Theory (MMT). Conveniently, politicians from both sides of the aisle choose not to use that controversial label to describe their reckless fiscal policies.

DC’s general acceptance for operating under massive deficits can be traced back to 2002, when the Bush administration’s economic team met to discuss a second round of tax reductions to follow Bush’s 2001 cuts. When then-Treasury Secretary Paul O’Neill raised concerns that additional tax cuts could cause the US government — already running a $158 billion deficit — to spiral toward a fiscal crisis, Vice President Dick Cheney famously alleged that “Reagan proved deficits don’t matter.” It was as if Cheney’s words were delivered on two stone tablets, granting all future governments permission to spend well beyond the nation’s means.

At the risk of sounding like Chicken Little, I’ll declare that debt and the deficit matter right now — more than ever. In the aftermath of the Global Financial Crisis, the US and global economies are suffering from much slower than normal growth rates. Deflation, not inflation, has been the greater threat during the past decade. And, finally, last year’s fourth quarter meltdown shockingly demonstrated that the world economy and financial markets can’t even tolerate modestly positive real interest rates.

These permanent consequences exist despite the best efforts of world governments and global central bankers that have implemented unprecedented fiscal and monetary stimulus in recent years. Yet economic growth rates remain stubbornly below trend and inflation dormant. Still, investors have little choice but to own risky assets. Positioning for an economic collapse in the face of massive amounts of fiscal stimulus and against central banks’ easy monetary policies hasn’t been a winning investment formula.

If you believe that debt and deficits don’t matter, I’m sorry, but you are wrong. They may not seem to matter because nothing terrible has happened yet as both debt and deficits have ballooned in recent years. However, just because a person is lucky enough to not blow his brains out in a game of Russian roulette doesn’t mean that the game isn’t dangerous — potentially fatal.

Talkin’ ‘bout the Generations

Thinking about how massive debt and huge deficits will impact future generations reminds me of one of the most thought-provoking books I have ever read — The Fourth Turning: An American Prophecy — What the Cycles of History Tell us About America’s Next Rendezvous with Destiny by William Strauss and Neil Howe. The authors apply their generational theories to the cycles of history to conclude that the United States may be on the brink of a crisis period they define as the “Fourth Turning.” Strauss and Howe suggest that US history moves in predictable cycles that last roughly 80 years, where different generations (i.e., Baby Boomers, Generation X and Millennials) move through roughly 20-year periods of influence called “turnings.”

Each of the four turnings comes with a mood shift that catches people by surprise. For example, the rapid breakdown of globalization in concert with rising nationalist sentiment and the surge in populist leaders around the world has shocked many people in recent years. The turnings follow a familiar rhythm of growth, maturity, decay and — ultimately — destruction. It’s easy to connect them to the four seasons — spring, summer, fall and winter. When the book was published in 1997, Strauss and Howe were forecasting that winter was due to arrive early in the 21st century. Followers of their work have cited such events as 9/11 and the Great Recession as evidence that the Fourth Turning was beginning as predicted. The massive national debt and increasing deficits have become symptoms of this crisis period.

Strauss and Howe stress that each generation will navigate the Fourth Turning in a different way. Their classic example is the G.I. Generation, or as journalist Tom Brokaw called them, the Greatest Generation. These heroes were born from roughly 1901 to 1924 and came of age during the last Fourth Turning in America — the Great Depression era through World War II (1929–1946). As children, they experienced the sharpest rise in schooling ever recorded. As young adults, their uniformed corps patiently endured depression and — ultimately — destruction. It’s easy to connect them to the four seasons — spring, summer, fall and winter.

Figure 2: The Federal Debt Has Outpaced GDP Since 2012, Growing at an Annual Pace of 7.3% Since 2000, While GDP Has Moderated to a 2–3% Growth Rate

![Figure 2: The Federal Debt Has Outpaced GDP Since 2012, Growing at an Annual Pace of 7.3% Since 2000, While GDP Has Moderated to a 2–3% Growth Rate](source)


State Street Global Advisors
Admittedly, to hold up Strauss and Howe’s research as absolute truth would be a major stretch. But to dismiss it entirely as pseudoscience would be a mistake of equal proportion. Being a skeptic, I have often wondered if they simply looked back at historical periods and laid a creative story on top of them. Everything fits so perfectly. Perhaps too perfectly? Strauss and Howe’s research is well thought out, extensive and makes tremendous intuitive sense. For proponents of their work, that is the attraction. And in what might be the only true test of their theories, there are plausible signs to suggest that America has been either in or on the brink of a Fourth Turning crisis period in the first two decades of this century. Exactly as the authors predicted.

So, Ya Wanna be a Hero, Kid?

Take that leap with me for a minute. If we extend Strauss and Howe’s research to its next logical step, it would imply that the Millennial Generation, like the G.I. Generation before them, will likely be the heroes of a Fourth Turning. This may strike fear into some of you, while for others, it may confirm your confidence in the Millennials to solve the nation’s toughest challenges. I suppose your reaction will largely depend on your own generational alignment — or your children’s.

Generational affiliations aside, human nature dictates that tough problems won’t be addressed until we are staring into the abyss. That’s why today’s global leaders get away with continuing to kick the can down the road. When we do reach the frightening precipice, Strauss and Howe’s work suggests that the Millennials will have the attributes and the good sense to make the tough decisions required to solve the nation’s most challenging problems.

And why not? Millennials came of age during 9/11, the second Gulf War and the Great Recession. They believe in global community. They are self-confident, entrepreneurial, racially diverse, accepting, and technologically savvy. And while they are highly collaborative, they also value autonomy and individualism.

Second-Level Summer Fun

With all the summer heat, it’s been refreshing to push our thinking beyond ordinary market topics to what Howard Marks in The Most Important Thing defines as second-level thinking. Deliberate second-level thinking considers interactions and time, understanding that despite our good intentions, our interventions often cause harm. Second-level thinkers ask themselves the important question, “And then what?”

Meanwhile, DC remains trapped in the fast and easy first-level thinking that solves problems without considering the consequences of the solutions. Yes, we’ll avoid a fiscal crisis this year because the White House and Congress raised the debt ceiling and agreed on a spending plan. But there are long-term consequences to this reckless spending — more debt and widening deficits. Our government needs to move beyond first-level thinking, where everyone reaches the same conclusion — that massive debt and deficits don’t matter.

Strauss and Howe certainly have created a fascinating and intuitive second-level framework for us to view history and make forecasts. And extraordinary insight can be gained by looking at our nation’s problems through a new lens.

It’s unclear whether America is in the midst of or close to entering the Fourth Turning crisis period. Only time will tell. But wherever we are in the cycle, a fiscal crisis could create more conflict. That might be the push that Millennials need to take charge and bring us back from the brink to a new First Turning high. Something to think about during these long summer days.

The Next Greatest Generation: Big Problems Will Require Bold Solutions

Important Risk Information
The views expressed in this material are the views of Michael Arone through the period ended July 25, 2019 and are subject to change based on market and other conditions. This document contains certain statements that may be deemed forward looking statements. Please note that any such statements are not guarantees of any future performance and actual results or developments may differ materially from those projected. Investing involves risk including the risk of loss of principal.
Past performance is no guarantee of future results.
The information provided does not constitute investment advice and it should not be relied on as such. It should not be considered a solicitation to buy or an offer to sell a security. It does not take into account any investor’s particular investment objectives, strategies, tax status or investment horizon. You should consult your tax and financial advisor. All material has been obtained from sources believed to be reliable. There is no representation or warranty as to the accuracy of the information and State Street shall have no liability for decisions based on such information.
The whole or any part of this work may not be reproduced, copied or transmitted or any of its contents disclosed to third parties without State Street Global Advisors’ express written consent.
Standard & Poor’s®, S&P® and SPDR® are registered trademarks of Standard & Poor’s Financial Services LLC, a division of S&P Global (S&P); Dow Jones is a registered trademark of Dow Jones Trademark Holdings LLC (Dow Jones); and these trademarks have been licensed for use by S&P Dow Jones Indices LLC (SPDJI) and sub licensed for certain purposes by State Street Corporation. State Street Corporation’s financial products are not sponsored, endorsed, sold or promoted by SPDJI, Dow Jones, S&P, their respective affiliates and third party licensors and none of such parties make any representation regarding the advisability of investing in such product(s) nor do they have any liability in relation thereto, including for any errors, omissions, or interruptions of any index.
State Street Global Advisors Funds Distributors, LLC, member FINRA, SIPC.

© 2019 State Street Corporation. All Rights Reserved.
ID17028-2655191.1.1.AM.RTL 0719 Exp. Date: 07/31/2020