

# **The Merrill Perspectives Podcast**

## **At Home with the New Consumer**

With  
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**Candace Browning:**When we think about the impact the coronavirus is having on the economy and our lives, one of the most significant areas undergoing change is consumer spending. And it's not just in small or incidental ways. Just about everything we buy, from cars and bikes to gaming and entertainment, is undergoing a shift, and these shifts are likely to last even after we have a vaccine and life gradually returns to quote, unquote "normal."

So how might changes in what Americans are buying affect businesses large and small? What sectors could benefit and which ones could be hurt? And what does it all mean for overall economic growth and recovery?

**[THEME MUSIC]**

Hello and welcome to this market edition of the Merrill Perspectives podcast. I'm Candace Browning, Head of BofA Global Research. On these programs, we've been exploring the many ways our lives are being altered in the wake of the coronavirus.

On this episode, we're taking a deep dive into how it's transforming our consumer culture—from what we're buying to how we're buying it. We'll look at the ways new product innovations are helping us adapt to our more solitary lifestyles and whether these changes are temporary or perhaps more permanent. And we'll explore what it could all mean for potential investment opportunities.

Joining me for the conversation today is Chris Hyzy, Chief Investment Officer for Merrill and Bank of America Private Bank.

**Chris Hyzy:** Hello, Candace.

**Candace Browning:** And Robby Ohmes, Senior U.S. Consumer Analyst for BofA Global Research.

**Robby Ohmes:** Hi, Candace.

**Candace Browning:** Okay, so Robby, let's start with you. You've been following the consumer sector for quite a long time and I know you've seen a lot of changes in what people are buying and what they're not buying.

Could you give us a snapshot of the shifts you're seeing in consumer spending since the pandemic first hit the economy? And also, are there any particular areas that are being affected the most? For example, I hear that demand for bicycles is skyrocketing, along with pools and boats and all sorts of leisure solitary activities. Tell us what you're seeing.

**Robby Ohmes:** Yeah, that's right, Candace. We published our first solitary leisure notes back in late May highlighting what appeared to be an acceleration in consumer spending away from traditional entertainment, so away from amusement parks and movie theaters and tourist attractions and international travel and things like that, to solitary leisure activities, including some that you mentioned like golf and marine and hiking and camping and the staycation aspect of it as well.

And then we put out a note focusing on bicycles and our channel checks suggested a dramatic surge in the demand for bicycles and that was across price points and categories.

We've even looked at things like app downloads for Strava, which is a GPS tracking platform for cyclists. That was up 188% in May. So you have seen really interesting spending in solitary leisure categories, but most recently we've also heard from large retailers that apparel and sporting goods are doing incredibly well and there's been significant improvements in some of the general merchandise categories that weren't doing as well before.

One of the things that's changed dramatically is grocery e-commerce driven and supported by delivery is right now running about three to four years ahead of where anybody in that industry expected it to be. And we think that's likely going to be a permanent change and I think people are going to really have a much larger percentage of their goods including grocery delivered to them going forward and there may be industries that arise around that process.

**Candace Browning:** Okay. Well, Chris, let's put this in the context of the overall economy. We often talk about how the consumer is a huge driver of the U.S. economy. I think consumer spending accounts for about 70% of GDP and what Americans buy therefore and don't buy has a tremendous effect on the future direction of the economy.

Could the sort of pent-up demand that we're watching and seeing lead us into a whole new growth cycle? Or is there potentially a risk that many people end up saving as opposed to spending more?

**Chris Hyzy:**

Yeah, Candace, that's a decision that happens in a much more assertive way when you're dealing with good economic times. Generally speaking, as we all know, consumers just love to spend, and they do worry about retirement, yes, they do save, they do invest, but the majority of the consumer cohort likes to spend.

Now, coming out of recessions, particularly record recessions, despite the fact that it could just be two to three months, there's a changing, not only dialog, but there's a changing pattern that's going on as Robby already talked about that. You go into hunker-down mode in your first phase. You assess the broader situation. Most importantly, you assess your job, and the comfort level of your job and your income production is what ultimately drives how quick you re-spend and how much you spend. That is more or less going to be 2021's story.

Right now, many people have shifted current spending as disposable personal income in the broader economy has actually gone up because of the programs that were put in place. If those programs go away and DPI or disposable personal income begins to come down, the hunker-down mode is going to come in and some of the spending that we have all seen recently is likely to fade.

Our particular view is a little bit more bullish, which is as we get into 2021, unemployment begins to come down despite it being a bumpy recovery. We expect consumer spending trends to actually pick back up again coming out of the secondary outbreaks we're seeing right now.

And as Robby highlighted, Candace, the areas that are new to spending are more than likely not going to go away. They entrench themselves with or without a vaccine and you're likely to see what we call "individual leisure activities," ILAs, remain a core part of an individual consumer for the foreseeable future.

**Candace Browning:** Now, Robby, it sounds like many, if not all of the changes that you're seeing are a result of millions of Americans adapting to this new, much more solitary way of life we're in right now. Looking longer-term, do you think that these changes are temporary or could they have real staying power? In other words, are staycations here to stay?

**Robby Ohmes:** That's a great question. I think my initial answer is only time will tell, but I agree with Chris that some of these leisure habits that are being created now could have a very long tail, including the bicycle trend, also the uptick in golf that has happened. We've also written about the marine industry in our notes.

I think as consumers make investments in activities like boats and bikes, we would expect them to continue to use them over an extended period which implies a higher level of sustained spending in those types of industries. Staycations is a very interesting trend. You know, it may become more about the domestic leisure activities versus, say, international travel and leisure.

But the bottom line is I think that many of the solitary leisure activities that are seeing the increased demand now are going to remain at much higher consumption rates for the next several years versus

where they would've been if the current unfortunate environment had never happened.

**Candace Browning:** Okay, so, so far, we've mostly talked about industries that are benefiting from solitary leisure. But Chris, how important will it be for areas that have been most hurt during the pandemic, areas like travel, entertainment, to actually see a resumption of spending? Or will changing trends in technology just completely remake those industries?

**Chris Hyzy:** Yeah, we think it's a combination of both. The benefit to some crises is it forces change, whether it's the private sector changing their business model, better expense management, the use of new technology, accelerating trends that would not have happened prior to a something like a pandemic or even just a very difficult recession. And then when you come out on the other side, you maintain those business model adjustments, but yet expense management becomes number one.

So then you go into a second phase, Candace, in which new consumer activities begin to have that long tail that Robby discussed, but you still need those older industries to remake themselves in the new frontier. If you look at jet travel or you look at travel overall, business travel is likely to be very difficult for a variety of reasons as we've all already experienced.

Companies within the travel space are going to have to move even more investment towards the consumer, and potentially towards what we call as pod or network-like spending where you have a group of

friends, an extended family, a number of people in your network that you believe you can travel with and you remain in a physical distancing world, but yet travel does happen. Same thing with hotels, same thing with restaurants and pubs.

All of this is going to have to be re-made, but at the same time, that remake could potentially be additive to the broader economy because now new ventures and new networks are created, and the hope is that the previously harmed areas begin to climb back in a whole totally new way.

**Candace Browning:** Okay, well Chris, I want to follow up on that a little bit. I'm curious about the idea of E-everything and how that fits in with what we were just discussing. So with so many areas of our lives now happening remotely via the internet and other forms of technology, does that also have an impact on our buying patterns and on that tail that you were talking about? I mean effectively, could it mean a whole new wave of product innovation is really just around the corner?

**Chris Hyzy:** Yes, you've absolutely nailed it, Candace. This is the single biggest metamorphosis and transformation I think that we're living right now. It was E most things before or partial things, if you will, unless of course if you have a whole bunch of kids at your house, you think it's E-everything already. But when you go forward, think about businesses, think about schools, so E-education, E-learning, as we said before, gaming, sports management. All of that lends itself to a full satellite of businesses that surround it. The advancement of 5G, new ways to stream, information management, all of these areas could be accelerated from the E-everything world.



Think of schools, universities, colleges. What if schools create a much more hybrid culture where you have class lectures, many of which could be online, recorded, taped? What's likely to happen to cost management is to become much more efficient, so perhaps the cost of going to school could come down and you could reach more people.

Same thing as it relates to just sporting activities. So there's a number of different things that we believe will be accelerated and that will be additive overall to the broader economy.

**Candace Browning:** Okay. Well, Robby, let's switch gears a little bit and talk about demographics and the consumer. How much do millennials and the younger Generation Z affect what's being purchased? And do they have the power to determine which products ultimately make it in the marketplace?

**Robby Ohmes:** I think that millennials are extremely important to what's happening right now because they're obviously a very large demographic group and they're now entering their peak earning and spending years, as the oldest of that group is now over age 35. And they're forming households. So spending on the home could be one area where millennials could have a very big impact on which products make it. I think younger households also historically tend to be more budget-conscious, so that may impact what they buy, but also where they buy. And millennials also want convenience, especially delivery, so I think products and retailers that meet budget demands and their convenience demands are going to do better.

**Candace Browning:** Well, Chris, we can't really talk about consumer spending without actually talking about the housing market. So what trends are you seeing in the housing market?

**Chris Hyzy:** If we go back pre-pandemic, the statement used to be that the millennial apartment renter would never leave the city. They liked the small containment side of it, they like the social aspect of it. Now, what you're starting to see is, they're leaving that area, coming into the suburbs because of lower rates, greater affordability, a little bit bigger room. Even though they may not go into large homes, they certainly are purchasing them in some cases at a record rate.

And what we expect, quite frankly, is for that to continue. So the housing cycle to the broader economy is number one, it's got the greatest leverage to further jobs in terms of per dollar sold within the housing segment, and most importantly, as Robby mentioned, home furnishings. It doesn't just stop at a desk or a bed; it goes into electronics, and electronic purchases are up significantly. So you're going to create a social enterprise now within your home where you can invite your network into your home versus just going out like you used to most of the time, and that also lends itself to a consumer trend that is just beginning.

**Candace Browning:** So Robby, let's look at what all of these changes that we've been talking about could mean for how we invest. I know we can't talk about specific companies, but what areas and industries look most promising to you?

**Robby Ohmes:** Candace, that's a great question. What looks promising right now really includes anything that is outdoor leisure, independent leisure-related. So when this started, we first started hearing about golf up-ticking, and then it was home fitness. I think most recently it was bikes and then marine and outdoor activities including fishing and then camping. And then athletic and outdoor footwear and apparel that goes with these activities seems to have some momentum in it as well. But we do think there's probably many areas that we're missing right now that we're hoping to figure out.

**Candace Browning:** And Robby, are there any areas that you think may suffer in the long term?

**Robby Ohmes:** You know, I think there could be some lingering or longer tail pressures on the things that are suffering right now. So does in-home entertainment continue to do better than out-of-home entertainment? Do food retailers maintain higher levels of food consumption versus restaurants than they historically did? Do grocery stores maintain higher percentage of food going forward? We think they might, maybe not at the stock-up rate, but maybe at a higher rate again than they otherwise would have if this unfortunate situation had never happened.

**Candace Browning:** So Chris, is there anything you want to add to that in terms of sectors and industries that could benefit from or conversely be challenged by the changes that we've been seeing in consumer spending?

**Chris Hyzy:** Yes. One area that we've looked at very closely on top of the individual consumer spending areas is this concept of where science

and technology converge together, and we're seeing that in the wearables sector. That wearable product segment came out of the gates a little sluggish a few years back when it was really first introduced. But since we've been in a pod-like culture now for the past few months and we're doing leisure activities more and more and more, the convergence between healthcare and technology and the wearable segment, from our perspective, is likely to be one of the highest growth areas in the years ahead.

And I think we're in the early days of a very long outgrowth of bringing society into your home. The advancement of home electronics, creating the experience within your home or in outdoor activities. We are becoming a more productive society. I think the advancement of smart cities is going to have to happen sooner rather than later, both from a hygienic perspective, but also from a public transportation perspective and creating a safer environment.

And last but not least, if we were an experiential culture before, I think you're seeing an experiential culture being multiplied to the power of E now. We are humans at the end of the day. We enjoy interaction whether it happens out in public or it happens through a screen or through electronically or virtualization. That outgrowth is still very, very early and that's why I'm particularly excited about the years ahead.

**Candace Browning:** Well, that's a great note to end on. Chris and Robby, thank you again for joining me for this conversation. I know it's an area we'll continue to watch closely in the months and the years ahead.

And thank you all for listening to this market edition of the Merrill Perspectives podcast. My co-hosts have been Chris Hyzy, Chief Investment Officer for Merrill and Bank of America Private Bank, and Robby Ohmes, Senior U.S. Consumer Analyst for BofA Global Research. I'm Candace Browning, Head of BofA Global Research.

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Thanks again for listening.

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