

US Hispanization: Long/short strategies

The Trend Continues...

In November 2004, our report *The Hispanization of the United States* provided a context and investment framework to assess the growing influence of Hispanics in the US economy. Three years later, the theme retains its relevance, and we offer a long/short investment framework.

1. Demographic data remains compelling

The US population is expected to increase by 6 million people through 2010; Hispanics should account for 3 million, or 50% of total US population growth. Census Bureau expects Hispanics to grow from 14% of the US population in 2005 to 20% by 2030.

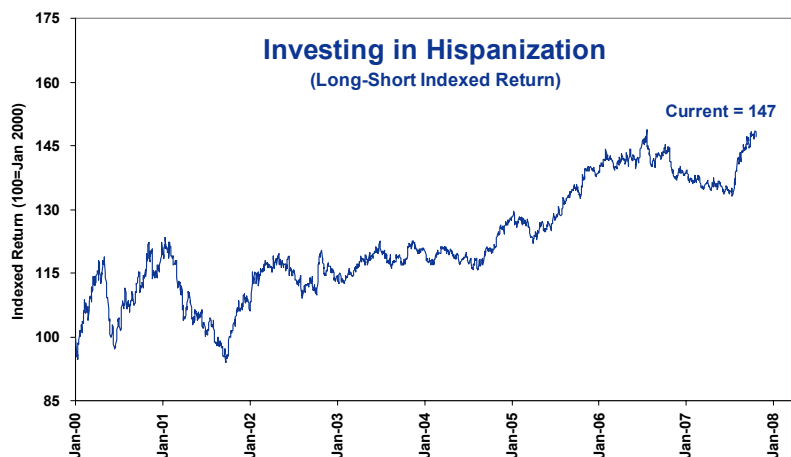
2. Where, on what, and how they spend money

We analyze patterns of Hispanic household expenditures to identify geographic areas **where** Hispanics spend, **what** products they purchase, and how they **will** spend in the future. We focus on Housing, Retail, Healthcare, and Financial Services.

3. Strategies to invest in Hispanization

Investors should consider three strategic angles to invest in this trend: the "Right States," the "Right Products" and the "Right Customers." We recommend buying a long/short basket of stocks most and least exposed to Hispanic trends (Bloomberg: <GSTHHPNL / GSTHHPNS>).

Investing in Hispanization: 34 long & 34 short stock ideas for next 3 years



Source: Goldman Sachs Research.

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Hispanization: Our investment framework to trade this theme

Long/short Hispanization investment strategies

This report focuses on long/short investment opportunities for portfolio managers to participate in the trend we refer to as the “Hispanization of the United States.”¹ US businesses across all industries have begun to focus on of the rapidly growing Hispanic/Latino market through targeted advertising spending and customized products. We believe this trend will continue. Firms taking the lead in these initiatives and in areas likely to benefit from the population growth of Hispanic/Latinos in the United States are likely to see their revenues grow faster than those of their competitors over the long term.

Demographic data remain compelling

The US Census Bureau predicts the total US population will reach 309 million by 2010, including 48 million Hispanics. This implies that roughly HALF of US population growth over the next three years will come from the growing Hispanic community. We believe this simple observation may come as a surprise to many investors and corporate managers.

Hispanics will represent 14% of aggregate US consumer spending growth over the next three years. We analyzed the “Consumer Expenditure Survey” released by the Bureau of Labor Statistics to forecast the increasing significance of Hispanic expenditures on the US economy.

The “Right” States: Where are Hispanics spending?

We analyzed the state-level Hispanic population data in the Geoscape® Intelligence System to identify regions most directly influenced by the Hispanization trend.

The “Right” Customers: What products are Hispanics buying?

We find that Hispanic households allocate expenditures differently from non-Hispanic US households, and we identify where companies may find opportunities in seeking growth.

The “Right” Products: How will Hispanics spend in the future?

Hispanic households changed their spending preferences between 2000 and 2005 and we expect further changes in the future. Although certain cultural differences may remain, we expect Hispanic households to converge to national means regarding other demographic areas such as income, family size and average age.

Framework for and Complications with Trading Hispanization

We believe the areas of opportunity lie within those categories in which Hispanics tend to allocate a large portion of household expenditures (Housing and Retail) as well as categories that should grow their share of Hispanic expenditures (Health Care and Financial Services). We recognize that timing, path of returns, isolating the Hispanization variable and determining what has already priced are the major complications of our trade.

¹ See *The Hispanization of the United States*, Goldman Sachs, November 2004.

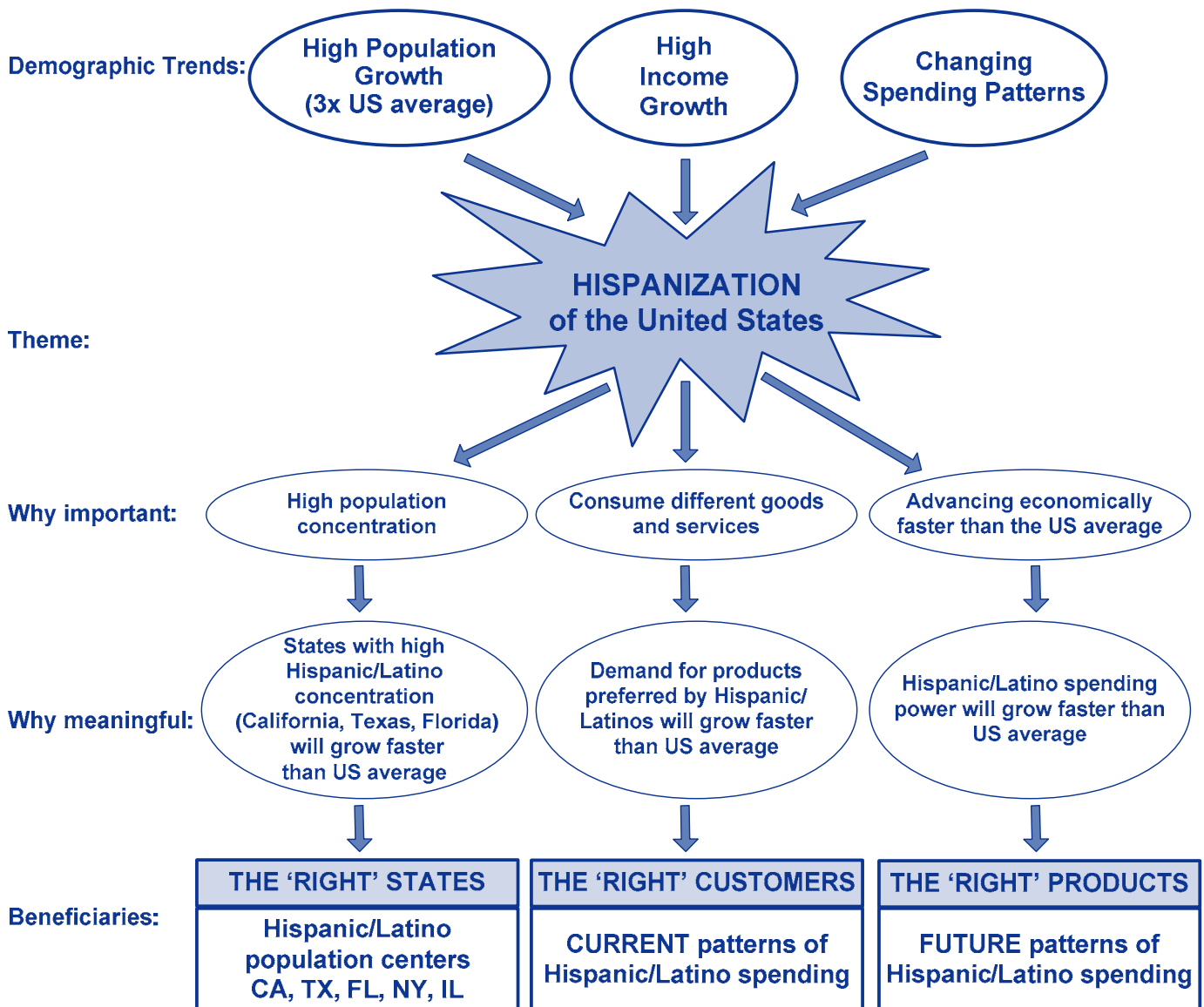
The Hispanization of the United States

What defines a Hispanic or Latino?

The Census Bureau considers people of Hispanic origin to be those who indicated that their origin was Mexican, Puerto Rican, Cuban, Central or South American, or some other Hispanic origin. People of Hispanic origin may be of any race. From an official perspective, the terms "Hispanic" and "Latino" may be used interchangeably to reflect the new terminology in the standards issued by the Office of Management and Budget in 1997 and implemented on January 1, 2003. We use the term "Hispanic" for purposes of this report.

High levels of immigration, above-average fertility rates, and a younger demographic community are driving dramatic population growth among Hispanic/Latinos relative to the US average. Hispanic/Latinos continue to advance economically, magnifying the effects of the increase in absolute population. Spending patterns are likely to change as incomes rise in this population segment.

Exhibit 1: The Hispanization of the United States



Source: Goldman Sachs Research.

1. Demographic data remains compelling

The US Census Bureau predicts that total US population will reach 309 million by 2010, including 48 million Hispanics. This implies that roughly HALF of US population growth over the next three years will come from the growing Hispanic community. We believe this simple observation may come as a surprise to investors and most corporate managers.

The *Hispanization* theme crosses multiple sectors and geographic regions and contains a number of investment implications. Although investing in macro trends is often difficult to implement and track given the lack of easily-identifiable catalysts, we believe the investment community will pay closer attention to Hispanization as companies allocate more resources in related efforts.

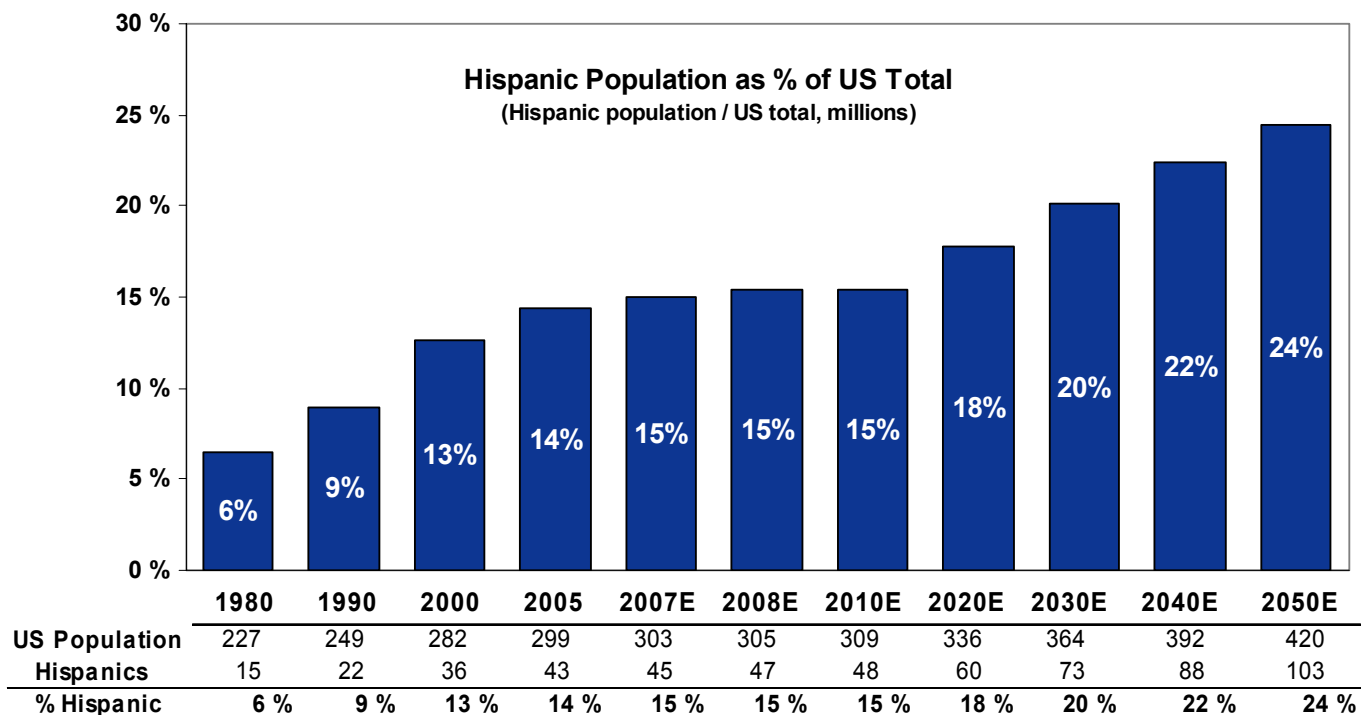
The quest for growth: Why invest in Hispanization now?

The growth in the Hispanic population is not a new phenomenon, nor is it expected to be short-lived. The Census Bureau estimates that Hispanics will represent a steadily increasing share of the US population through 2050 (see Exhibit 2).

Equity market participants are having an increasingly difficult time finding growth opportunities given a slowing US economy. For internationally-oriented investors, the rise of the BRICs (Brazil, Russia, India, and China) and other Emerging Markets offers a gateway to benefit from faster economic growth outside the US. **For domestically-focused investors and companies, gaining exposure to the rapidly growing US Hispanic population offers the best prospect for sales and earnings growth over the next three years.**

Exhibit 2: Total US and Hispanic population forecasts to 2050

Based on 2000 US Census projections

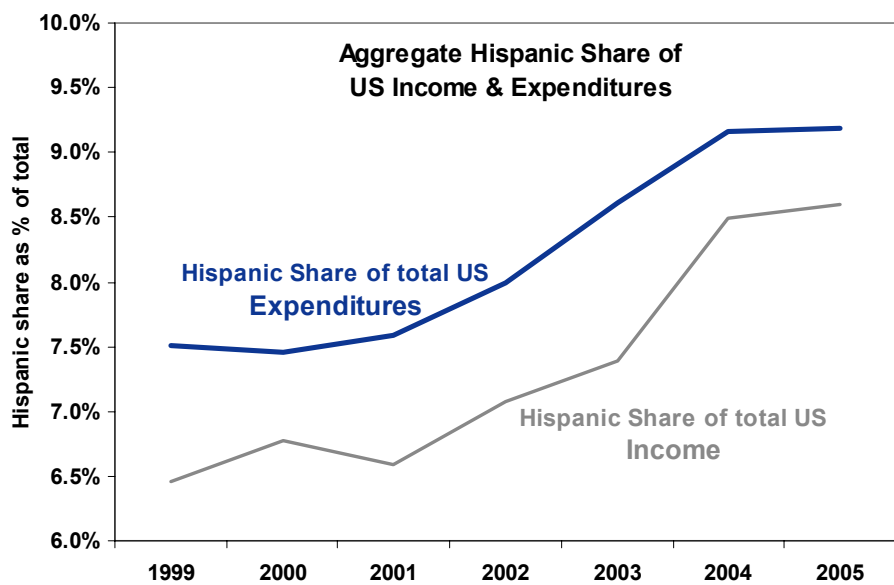


Source: US Census Bureau and Goldman Sachs Research.

Hispanics will represent 14% of aggregate US expenditure growth over the next three years. We analyzed the “Consumer Expenditure Surveys” released by the Bureau of Labor Statistics to forecast the increasing significance of Hispanic expenditures on the US economy. We believe Hispanic “consumer units” (as defined by the BLS), will increase expenditures from \$500 billion in 2005 to \$691 billion by 2010, a CAGR of 6.7%.

Currently, Hispanic spending accounts for roughly 9.2% of overall household expenditures. Combining the population estimates from the US Census Bureau with the household size and expenditure data from the BLS, we forecast Hispanic spending to account for 10% of US expenditures by 2010. This proportion should increase steadily through the 21st century, suggesting that both the corporate and investing worlds should incorporate the Hispanization theme into their growth strategies.

Exhibit 3: Hispanic share of income & expenditures and projections



| Consumer Expenditures (\$ bil) | | | | | | |
|--------------------------------|-------------------|---------|------|-----------------|----------|----------|
| | Historical Growth | | | Forecast Growth | | |
| Total Dollar | 2000 | 2005 | CAGR | 2010E | 2015E | 2020E |
| US Total | \$4,161 | \$5,446 | 6 % | \$6,855 | \$8,726 | \$11,088 |
| Hispanic | 310 | 500 | 10 | 691 | 953 | 1,537 |
| % of Total | 7 % | 9 % | | 10 % | 11 % | 14 % |
| Dollar Growth | 2000-'05 | | | 2005-'10 | 2005-'15 | 2005-'20 |
| US Total | \$1,286 | | | \$1,409 | \$3,280 | \$5,642 |
| Hispanic | 190 | | | 191 | 453 | 1,037 |
| Growth Attribution | 15 % | | | 14% | 14% | 18% |

Hispanic consumer expenditures represented 15% of total US consumer expenditure growth between 2003 and 2005. We estimate that Hispanics will represent 14% of consumer expenditure growth through 2010, and 18% through 2020.

Source: Bureau of Labor Statistics and Goldman Sachs Research.

2. Where, on what, and how will Hispanics spend?

The "Right" States: Where are Hispanics spending?

We analyzed the state-level Hispanic population data in the Geoscape® Intelligence System to identify regions most directly influenced by the Hispanization trend.

The Largest Markets: California, Texas, Florida, New York and Illinois boast the largest Hispanic populations in the country. In aggregate, these five states represent 66% of the national Hispanic population. Clearly, these are the largest markets in which companies exposed to Hispanic spending patterns may benefit. While the Hispanic populations of California, Texas and Florida are spread across the state, New York and Illinois Hispanics are mostly concentrated in New York City and Chicago, respectively. We would focus on large-cap companies in these states, where established Hispanic communities exist and where the largest amount of Hispanic expenditures may be found.

The Concentrated Markets: New Mexico, Arizona, Nevada, Colorado and New Jersey are the most "concentrated" states, measured by the ratio of Hispanics to total residents. These states tend not to be the most populous (with the exception of New Jersey), but nevertheless, the relative importance of the Hispanic populations remains a key factor. Within these states, we would expect to see a higher percentage of advertising, marketing and product placement budgets allocated towards the Hispanic markets.

The Growing Markets: We estimate that the Hispanic populations in South Carolina, Georgia, Tennessee, North Carolina and Maryland grew almost 7% per year from 2000 to 2007, the fastest rates in the country. The Hispanic populations in these states grew from a small base in 2000, but we expect continued rapid expansion, representing growth opportunities especially for small businesses concentrated in these states.

Exhibit 4: The geography of Hispanization
Current Hispanic population and growth by state

| | State | Current Population | | Population Growth | |
|---|----------------|---------------------------|------------------------|-------------------|------------|
| | | Hispanic Population (mil) | Hispanic as % of Total | 2000-08 CAGR | |
| | | | | Hispanic | Total |
| "LARGEST markets" States with the largest Hispanic Populations | California | 13.5 | 36 % | 3 % | 1 % |
| | Texas | 8.8 | 36 | 4 | 2 |
| | Florida | 3.8 | 20 | 5 | 2 |
| | New York | 3.1 | 16 | 1 | 0 |
| | Illinois | 2.0 | 15 | 3 | 1 |
| "CONCENTRATED markets" States with the highest concentration of Hispanics | New Mexico | 0.9 | 44 | 2 | 1 |
| | Arizona | 2.0 | 30 | 5 | 3 |
| | Nevada | 0.7 | 25 | 7 | 4 |
| | Colorado | 1.0 | 20 | 4 | 2 |
| | New Jersey | 1.4 | 16 | 2 | 1 |
| "GROWING markets" States with the fastest Hispanic population growth | Georgia | 0.8 | 8 | 8 | 2 |
| | Tennessee | 0.2 | 3 | 8 | 1 |
| | South Carolina | 0.2 | 4 | 7 | 1 |
| | North Carolina | 0.7 | 7 | 7 | 2 |
| | Maryland | 0.3 | 6 | 5 | 1 |
| US Total | | 47.2 | 15 % | 4 % | 1 % |

Source: US Census Bureau, Geoscape® American Marketcape DataStream™: 2008 Series; Latin Force Group LLC and Goldman Sachs Research.

The “Right” Customers: What products are Hispanics buying?

We analyzed the Consumer Expenditure Survey released by the Bureau of Labor Statistics to determine how Hispanic households allocate expenditures differently from non-Hispanic US households, and where companies have opportunities in seeking Hispanic spending.

The three major demographic factors differentiating Hispanic and non-Hispanic households in this regard are lower average income, larger family size and younger population.

Housing represents the largest spending allocation (36% of overall expenditures) as well as the category with the greatest allocation difference between Hispanics and non-Hispanics (see Exhibit 5). Lower income may partially explain this situation. However, we note that Hispanics are concentrated in what have been the country’s “hottest” real estate markets during the past five years (California, Florida and New York) which undoubtedly contributed to rising housing costs in those regions. Similarly, Hispanics tend to live within cities, which have higher costs than rural areas.

Retail & Entertainment account for roughly 24% of Hispanic household expenditures. Hispanics tend to allocate more on Apparel, Food and Personal Care, which we attribute primarily to larger family size. Within the Entertainment category, Hispanics tend to spend relatively less than non-Hispanics, perhaps a function of lower household income. These areas offer fertile avenues for investment in the Hispanization theme.

Health Care spending accounts for 6% of non-Hispanic household expenditures but just 4% for Hispanics. This discrepancy is concentrated in the drugs and medical supplies sub-categories, an indication of the younger Hispanic population (the elderly tend to spend more on prescriptions, etc).

Cash Contribution, Insurance and Pensions are categories in which Hispanics spend relatively less than non-Hispanics. Lower income and occupation distribution may explain most of the difference. Hispanics have less access to various financial services, which has limited spending in these areas as well.

Exhibit 5: Household expenditure allocation: Hispanic vs. Non-Hispanic
Share of household budget by expenditure category

| Household Expenditure Allocation | | | |
|----------------------------------|----------------|----------------|------------|
| Type | Hispanic | Non-Hispanic | Difference |
| Housing | 35.7 % | 32.4 % | 336 bp |
| Transportation | 19.7 | 17.8 | 188 |
| Apparel and Services | 5.5 | 3.9 | 155 |
| Food | 13.8 | 12.7 | 116 |
| Personal Care | 1.2 | 1.2 | 9 |
| Miscellaneous | 1.7 | 1.7 | (9) |
| Reading | 0.1 | 0.3 | (15) |
| Alcoholic Beverages | 0.7 | 0.9 | (23) |
| Tobacco Products | 0.4 | 0.7 | (32) |
| Education | 1.4 | 2.1 | (70) |
| Cash Contributions | 2.3 | 3.7 | (140) |
| Insurance and Pensions | 9.9 | 11.3 | (144) |
| Entertainment | 3.7 | 5.3 | (157) |
| Healthcare | 3.8 | 5.9 | (215) |
| Total | 100.0 % | 100.0 % | - |

MORE Hispanic spending
in these categories
(higher relative allocation)

LESS Hispanic spending
in these categories
(lower relative allocation)

Source: Bureau of Labor Statistics and Goldman Sachs Research.

The “Right” Products: How will Hispanics spend in the future?

Between 2000 and 2005, Hispanic households changed spending preferences, and we expect similar changes to continue in the future. Although certain cultural differences may remain, we expect Hispanic households to converge to national means regarding other demographic areas such as income, family size and average age.

MORE Spending: Housing again appears at the top of the list, although we believe the increased allocation in this category likely reflects the soaring house costs. **Cash Contributions, Insurance and Pensions** increased as well, a sign that Hispanics have modified expenditures as income has risen. We expect this trend to continue.

Insurance companies and retail banks stand to benefit, spanning from more openings of bank, pension and insurance accounts to increased use of other financial services, such as international money transfers. Similarly, we expect further gains in **Entertainment** (particularly within the fees and admissions sub-category) as income continues to rise.

LESS Spending: Hispanics decreased allocation in the **Food, Apparel and Services** categories the most. Family size and age demographics did not change significantly between 2000 and 2005, although average Hispanic income grew by 36% during the period, outpacing non-Hispanics (+31%). We expect further moderate declines in these areas due to additional income growth, but recognize that a significant portion of Hispanic expenditures will continue to fall in these categories.

Trend Reversal? Although Hispanic spending shifts between 2000 and 2005 appear consistent with demographics, we do not necessarily anticipate the same spending patterns to continue, most notably in the **Housing** and **Health Care** categories.

We believe Housing expenditures increased primarily due to soaring costs, not preference changes. Although we expect Housing to remain the largest category by allocation, we would not expect its share to increase further. We believe the mass inflow of immigrants, who spend less on Health Care, explains the decrease of expenditures in that category between 2000–2005. In the future, we expect Hispanics to increase Health Care expenditures, particularly in the health insurance sub-category.

Exhibit 6: Change in Household Expenditure Allocation

Share of household budget by expenditure category

| Change in Expenditure Allocation | | | |
|----------------------------------|---------------------|----------------|----------|
| Type | Hispanic Households | | |
| | 2000 | 2005 | Change |
| Housing | 33.1 % | 35.7 % | 259 bp |
| Insurance and Pensions | 8.0 | 9.9 | 194 |
| Cash Contributions | 2.0 | 2.3 | 34 |
| Education | 1.1 | 1.4 | 28 |
| Entertainment | 3.6 | 3.7 | 10 |
| Healthcare | 3.8 | 3.8 | (1) |
| Reading | 0.2 | 0.1 | (4) |
| Tobacco Products | 0.5 | 0.4 | (13) |
| Alcoholic Beverages | 0.9 | 0.7 | (16) |
| Miscellaneous | 1.8 | 1.7 | (18) |
| Personal Care | 1.7 | 1.2 | (47) |
| Transportation | 20.5 | 19.7 | (84) |
| Apparel and Services | 6.3 | 5.5 | (87) |
| Food | 16.4 | 13.8 | (255) |
| Total | 100.0 % | 100.0 % | - |

INCREASING Allocation

DECREASING Allocation

Source: Bureau of Labor Statistics and Goldman Sachs Research.

3. Strategies to invest in Hispanization

Framework for and Complications with Trading Hispanization

In the chart below, we lay out our basic framework for investing in Hispanization by sector (see Exhibit 7). Simply put, we believe the areas of opportunity lie within those categories in which Hispanics tend to allocate a large portion of household expenditures (Housing and Retail) as well as categories that should grow their share of Hispanic expenditures (Health Care and Financial Services).

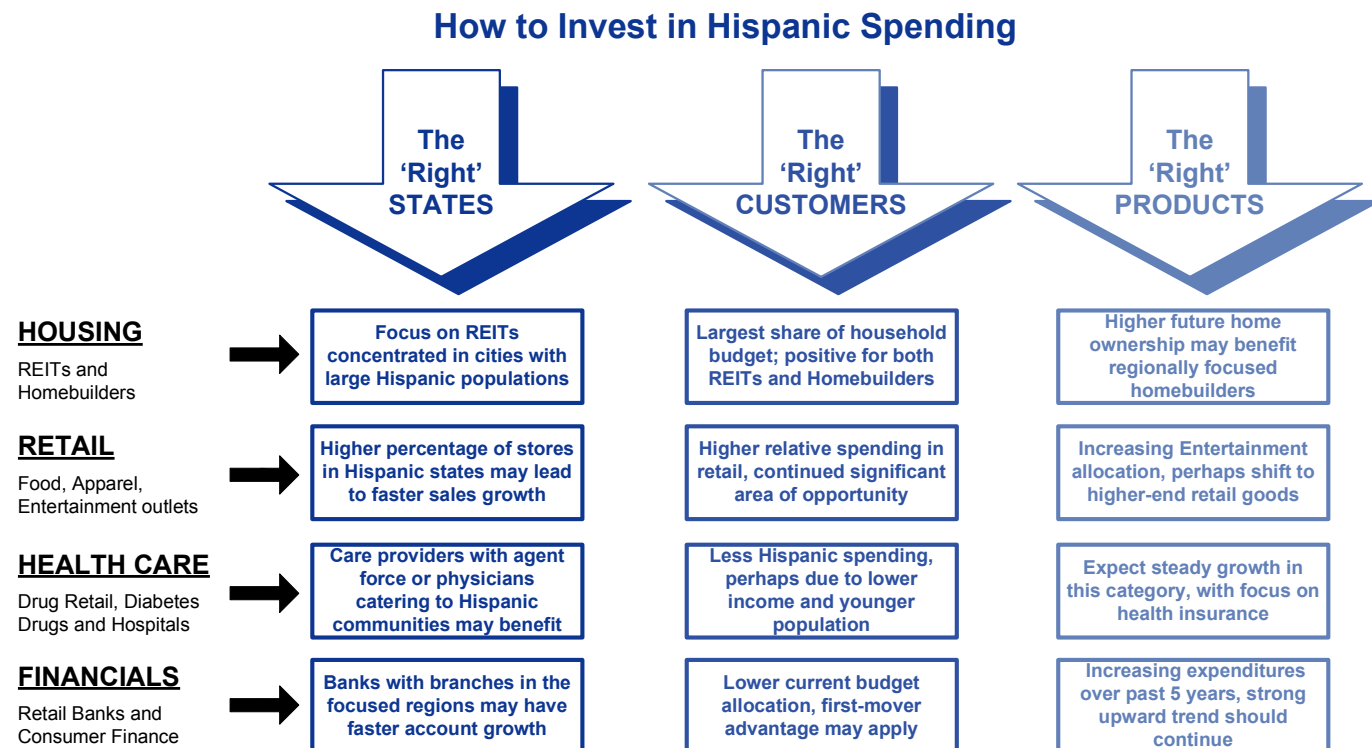
Timing: Macro trends may be slow to develop, but we are confident the theme will be realized over time. However, it is difficult to determine when shares will trade the theme.

Path: Although we believe Hispanization will affect the revenues, earnings and ultimately, the returns of stocks, the market may not trade this theme consistently, potentially resulting in large swings. We try to minimize risk by structuring sector neutral trades.

Isolating the variable: It is virtually impossible to identify public companies purely exposed or completely untouched by Hispanization. Trading the specific theme is difficult.

What is already priced: We are not sure to what extent analysts have factored Hispanic spending into earnings estimates. Consequently, we do not know how the market is discounting current and future Hispanic spending patterns.

Exhibit 7: Summary of investment implications based on Hispanic spending patterns



Source: Goldman Sachs Research.

How to invest in Hispanic Housing Expenditures

Hispanic home ownership rates are below the national average (47% vs. 68%), and we believe these two data points will converge over time. This shift should benefit Homebuilders that generate a high portion of revenue in Florida, California and Texas.

Hispanization should affect the US housing market. States that experience high inflows of immigrants should benefit, as should housing markets in states where large Hispanic populations already reside, given the above-average fertility rates.

We believe stock trading will be largely influenced by regional exposure, particularly in the REITs and Homebuilder industries, where land value plays a critical factor. Real estate booms occur in areas with fast growing populations and increasing population densities. Analyzing the US Census Bureau’s list of the fastest 100 growing counties in the United States, we find that 23 are in the states with the largest Hispanic populations (CA, FL, TX and IL). More interesting, however, Georgia alone encompasses 24 of the top 100 counties (see Appendix B). According the Geoscape® Intelligence System, Georgia has the fourth fastest growing Hispanic population across the US (see Exhibit 4).

The Consumer Expenditure Survey indicates that Hispanics allocate more than twice the allotment of non-Hispanics towards “Rented Dwellings”, a result of lower ownership rates. Accordingly, we screened for Apartment REITs that own and operate a high percentage of units in the Hispanic target states. As most REITs do not report tenancy by ethnicity, we cannot accurately determine which companies cater more directly to the Hispanic population. However, we believe that real estate companies concentrated in the relevant states will benefit regardless of their specific tenant composition compared with companies that have no presence at all.

The current housing downturn represents a serious risk to our thesis. Regardless of the merits of our Hispanization investment strategy, the near-term weak housing market will trump the long-term demographic fundamentals on most trading days. A number of market participants believe US housing market will remain weak into 2009. Interestingly, a case may be made that a weak single-family housing market can co-exist with a stable or improving multi-family market. Renters delay buying homes because of concern over falling home prices, job uncertainty, or the inability to obtain mortgage credit.

Exhibit 8: Long/Short recommendations within Homebuilders and REITs

| | Company | Ticker | Goldman Sachs Rating | Share of Units Owned / Built in Hispanic Target States | Revenue Growth | | | Valuation | | |
|------|-----------------------------------|--------|----------------------|--|----------------|-------------|-------------|-----------------|---------------|--------------|
| | | | | | 2000-'06 CAGR | 2007E | 2008E | MktCap (\$ bil) | P/E (a) (NTM) | Return YTD |
| Buy | Meritage Homes Corp. | MTH | Neutral | 93 % | 37 % | (35)% | (18)% | \$0.4 | NM | (71)% |
| | D.R. Horton Inc. | DHI | Buy | 76 | 26 | (24) | (10) | 4.0 | 109.7x | (51) |
| | Essex Property Trust Inc. | ESS | Neutral | 75 | 12 | 12 | 11 | 2.9 | 21.2x | (8) |
| | AvalonBay Communities Inc. | AVB | Buy | 74 | 4 | 9 | 10 | 9.1 | 23.2x | (10) |
| | Camden Property Trust | CPT | Neutral | 68 | 7 | 3 | 5 | 3.4 | 16.2x | (15) |
| Sell | KB Home | KBH | Neutral | 67 % | 17 % | (39)% | (20)% | \$2.0 | NM | (48)% |
| | Equity Residential | EQR | Neutral | 43 | (1) | 6 | 4 | 11.1 | 17.4 | (18) |
| | Mid-America Apartment Communities | MAA | NC | 40 | 6 | NA | NA | 1.3 | 13.9 | (8) |
| | Home Properties Inc. | HME | NC | 31 | 6 | 14 | 6 | 1.8 | 15.6 | (8) |
| | NVR Inc. | NVR | Neutral | 0 | 18 | (16) | (12) | 2.3 | 11.6 | (36) |
| | Long Stocks - average | | | 77 % | 17 % | (7)% | (0)% | \$4.0 | 42.6x | (31)% |
| | Short Stocks - average | | | 36 | 9 | (9) | (6) | 3.7 | 14.6 | (24) |

Note: Some homebuilders report geographical breakdown by states, others by region. Share of units in Hispanic target states makes certain assumptions.

Source: Company Filings, Compustat, FirstCall via FactSet, and Goldman Sachs Research.

How to invest in Retailers exposed to Hispanic trends

Retail expenditures (Food, Apparel and Personal Care) represent three of the five categories in which Hispanics tend to spend relatively more than non-Hispanics.

Although allocation has decreased in these categories, we believe expenditures in these areas will remain close to 20% of Hispanic household budgets.

Similar to the real estate market, we believe trading this theme primarily hinges on geographic exposure. We would invest predominantly in mid-cap companies with exposure to the California, Texas, Florida, New York and Illinois (specifically Chicago) markets, and trade against similar retailers in other areas. In this sector, we also consider price points and product types. Within Food Retail, we do not find many liquid stocks that are regionally focused, so we focus on discount names.

Demographic concerns also influence investing in the retail space. Hispanics tend to live in households of larger families than non-Hispanics (3.4 persons vs. 2.4), and typically have twice the number of children under 18 years old (1.2 vs. 0.6). The combination of a larger household and more children perhaps explains the higher allocation of Food expenditures among Hispanics and implies that investors should look to Apparel Retailers that target children's and teen clothing. Finally, we note that the retail industry relies heavily upon brand equity. A strong image is important to larger retailers trying to gain market share in states with large Hispanic communities.

Our trade outlined below features nine retailers to buy and nine to sell based on exposure to Hispanic markets. We note that the companies on the long side of the trade have grown sales at an annual rate 2 percentage points faster than the short stocks (8% vs. 6%), perhaps in part due to increasing Hispanic population. Analysts expect these stocks to continue outpacing the non-exposed stocks in 2007 (15% vs. 8%) and in 2008 (10% vs. 8%).

Exhibit 9: Long/Short recommendations within Retailers

| | Company | Ticker | Goldman Sachs Rating | Share of Stores in Hispanic Target States | Revenue Growth | | | Valuation | | |
|-------------------------------|-----------------------------|--------|----------------------|---|----------------|-------------|-------------|-----------------|---------------|-------------|
| | | | | | 2000-'06 CAGR | 2007E | 2008E | MktCap (\$ bil) | P/E (a) (NTM) | Return YTD |
| Buy | Winn-Dixie Stores Inc. | WINN | NC | 69 % | (10)% | 1 % | 2 % | \$0.9 | 109.0x | 29 % |
| | Ross Stores Inc. | ROST | Neutral | 55 | 13 | 12 | 10 | 3.6 | 13.0 | (10) |
| | Costco Wholesale Corp. | COST | Buy | 54 | 11 | 9 | 10 | 28.9 | 22.0 | 25 |
| | Whole Foods Market Inc. | WFMI | NC | 51 | 20 | 17 | 21 | 6.6 | 32.6 | 2 |
| | Tween Brands Inc. | TWB | NC | 47 | 9 | 18 | 16 | 0.9 | 14.1 | (27) |
| | Wet Seal Inc. | WTSLA | NC | 47 | (0) | 13 | 13 | 0.3 | 12.5 | (59) |
| | SUPERVALU Inc. | SVU | Neutral | 43 | 5 | 35 | 4 | 7.9 | 12.6 | 6 |
| | Best Buy Co. Inc. | BBY | Neutral | 40 | 16 | 16 | 9 | 19.6 | 14.2 | (4) |
| | Herbalife Ltd. | HLF | Buy | NA | 10 | 11 | 9 | 3.0 | 15.8 | 11 |
| Sell | Cato Corp. | CTR | NC | 30 % | 5 % | 1 % | 7 % | \$0.6 | 12.2x | (20)% |
| | J. Crew Group Inc. | JCG | NC | 29 | 5 | 22 | 14 | 2.4 | 24.4 | 1 |
| | Sherwin-Williams Co. | SHW | NC | 25 | 7 | 4 | 5 | 8.3 | 13.0 | 1 |
| | Cabela's Inc. | CAB | NC | 22 | 14 | 15 | 23 | 1.3 | 14.0 | (19) |
| | Casey's General Stores Inc. | CASY | NC | 11 | 12 | 19 | 13 | 1.4 | 18.1 | 17 |
| | RadioShack Corp. | RSH | Neutral | 10 | (0) | (10) | (1) | 2.7 | 12.3 | 15 |
| | Buckle Inc. | BKE | NC | 10 | 5 | NA | 2 | 1.2 | NA | 23 |
| | Weis Markets Inc. | WMK | Sell | 3 | 1 | 5 | 2 | 1.1 | NA | 7 |
| | Ruddick Corp. | RDK | NC | 2 | 3 | 12 | NA | 1.5 | NA | 16 |
| Long Stocks - average | | | | 51 % | 8 % | 15 % | 10 % | \$8.0 | 27.3x | (3)% |
| Short Stocks - average | | | | 16 | 6 | 8 | 8 | 2.3 | 15.7 | 5 |

Source: Company filings, Compustat, FirstCall via FactSet, and Goldman Sachs Research.

How to invest in future Hispanic Health Care spending

Hispanics have consistently allocated less on Health Care spending than non-Hispanics, and we believe this sector presents a growth investment opportunity.

The lower allotment is apparent in all sub-categories, namely Insurance, Medical Services, Drugs and Supplies.

According to the US Census Bureau, roughly 33% of the Hispanics population does not have health insurance, compared with just 11% for non-Hispanic whites.² We expect the rate of uninsured Hispanics to converge with the national average, as Hispanics have climbed the economic ladder faster than non-Hispanics (based on median household income growth between 2000 and 2005). We believe insurance companies that market to Hispanics and retain agents in the 'Right' states are best poised to benefit from this demographic shift. Furthermore, we believe that customer bases in the insurance industry are "sticky" (brand loyal), indicating that first-mover advantages are significant.

The Centers for Disease Control and Prevention (CDC) reports that Hispanic adults aged 18 to 44 are roughly 2.5 times likelier than non-Hispanics to be diagnosed with diabetes.³ We expect that companies focused on diabetes drugs and self-testing supplies have a significant market for growth. Similarly, we believe the growth in generic drugs will likely benefit Drug Retailers.

The last Health Care sub-sector in which we find investment opportunities is among the Health Care Facilities stocks. Companies that operate a high percentage of hospitals or retain a large portion of physicians in Hispanization target states are likely to benefit from the rapidly growing populations.

About 17% of Americans are more than 60 years old, yet just 7% of Hispanics are in this age cohort. From a customer standpoint, senior living facilities do not penetrate the bulk of the Hispanic market. We prefer to focus on general hospitals located in the right areas.

Exhibit 10: Long/Short recommendations within Health Care

| | Company | Ticker | Goldman Sachs Rating | Share of Facilities/Beds in Hispanic Target States | Revenue Growth | | | Valuation | | |
|------|-------------------------------|--------|----------------------|--|----------------|-------------|-------------|-----------------|---------------|-------------|
| | | | | | 2000-'06 CAGR | 2007E | 2008E | MktCap (\$ bil) | P/E (a) (NTM) | Return YTD |
| Buy | PolyMedica Corp. | PLMD | NC | 81 % | 21 % | 23 % | 19 % | \$1.2 | 23.7x | 32 % |
| | AMERIGROUP Corp. | AGP | Buy | 78 | 28 | 36 | 11 | 1.8 | 15.9 | (5) |
| | Health Net Inc. | HNT | Neutral | 77 | 6 | 9 | 9 | 5.8 | 13.3 | 6 |
| | Humana Inc. | HUM | Buy | 49 | 12 | 17 | 8 | 12.6 | 15.5 | 35 |
| | CVS Caremark Corp. | CVS | Buy | 39 | 14 | 74 | 17 | 59.0 | 19.3 | 31 |
| | Medco Health Solutions Inc. | MHS | Buy | NA | 7 | 5 | 11 | 24.6 | 24.3 | 69 |
| Sell | Brookdale Senior Living Inc. | BKD | Neutral | 53 % | 12 % | 42 % | 7 % | \$4.0 | NA | (16)% |
| | Rite Aid Corp. | RAD | Sell | 37 | 4 | 33 | 17 | 3.2 | NA | (26) |
| | Centene Corp. | CNC | Neutral | 36 | 47 | 28 | 19 | 1.0 | 14.2x | (4) |
| | Kindred Healthcare Inc. | KND | NC | 29 | 5 | 0 | (2) | 0.8 | 15.9 | (1) |
| | Lifepoint Hospitals Inc. | LPNT | Neutral | 17 | 28 | 9 | 6 | 1.7 | 12.3 | (15) |
| | UnitedHealth Group Inc. | UNH | Neutral | NA | 23 | 6 | 7 | 63.4 | 12.7 | (10) |
| | Long Stocks - average | | | 65 % | 14 % | 27 % | 12 % | \$17.5 | 18.7x | 28 % |
| | Short Stocks - average | | | 34 | 20 | 20 | 9 | 12.3 | 13.8 | (12) |

Source: Company Filings, Compustat, FirstCall via FactSet, and Goldman Sachs Research.

² http://www.census.gov/Press-Release/www/releases/archives/income_wealth/005647.html

³ <http://www.cdc.gov/od/oc/media/presskits/hhd/diabetes.htm>

How to invest in Financial Services catering to Hispanics

The Consumer Expenditure Survey indicates that Hispanics tend allocate less than non-Hispanics to Insurance, Pensions and Cash Contributions. However, allocations are rising in all three categories.

These expenditures relate to financial services through account handling, premium payments and other service fees. According to the Federal Reserve, roughly 8.7% of the US population does not have a bank account, a fraction primarily comprised of Hispanics and African Americans. Similarly, roughly half of Hispanics in the US do not have a checking account.

We expect many Hispanics to open banking accounts going forward, converging to national averages. Even Bank of America (BAC, Buy), the sixth largest company in the US by equity capitalization, has been recognized by the press as a leading financial institution that markets specifically toward the Hispanic community. However, when trading Hispanization, we do not recommend investors look toward the larger companies, rather, we suggest investing in smaller, Regional Banks that are primarily centered in areas with large Hispanic populations.

Exhibit 11: Long/Short recommendations within Regional Banks and Consumer Finance

| | Company | Ticker | Goldman Sachs Rating | Share of Branches/Agents in Hispanic Target Areas | Revenue Growth | | | Valuation | | |
|--------------------------------|---------------------------------------|--------|----------------------|---|----------------|--------------|------------|-----------------|---------------|--------------|
| | | | | | 2000-'06 CAGR | 2007E | 2008E | MktCap (\$ bil) | P/E (a) (NTM) | Return YTD |
| | | | | | | | | | | |
| Buy | Pacific Capital Bancorp | PCBC | NC | 100 % | 13 % | 4 % | (25)% | \$1.3 | 11.7x | (19)% |
| | City National Corp. | CYN | Neutral | 100 | 6 | (14) | 6 | 3.3 | 13.5 | (3) |
| | Cullen/Frost Bankers Inc. | CFR | NC | 100 | 5 | (15) | 7 | 2.9 | 13.1 | (10) |
| | East West Bancorp Inc. | EWBC | NC | 100 | 23 | (36) | 9 | 2.2 | 13.4 | 4 |
| | First Community Bancorp Inc. | FCBP | NC | 100 | 47 | (4) | 2 | 1.6 | 15.2 | 1 |
| | International Bancshares Corp. | IBOC | NC | 100 | 9 | NA | NA | 1.5 | NM | (23) |
| | Westamerica Bancorp | WABC | NC | 100 | (0) | (20) | 1 | 1.4 | 15.7 | (4) |
| | Prosperity Bancshares Inc. | PRSP | NC | 100 | 23 | (3) | 9 | 1.4 | 14.5 | (6) |
| | CVB Financial Corp. | CVBF | NC | 100 | 13 | (44) | 7 | 0.9 | 13.8 | (15) |
| | Sterling Bancshares Inc. | SBIB | NC | 100 | 5 | (22) | 9 | 0.8 | 14.8 | (13) |
| | FirstFed Financial Corp. | FED | NC | 100 | 15 | (61) | (6) | 0.7 | 7.5 | (31) |
| | First Cash Financial Services Inc. | FCFS | NC | 71 | 17 | 47 | 17 | 0.7 | 14.2 | (19) |
| | Cash America International Inc. | CSH | NC | 54 | 12 | 37 | 13 | 1.0 | 12.7 | (28) |
| First Bancorp Of Puerto Rico | FBP | NC | NA | 17 | NA | NA | 0.8 | NM | (2) | |
| Sell | TCF Financial Corp. | TCB | NC | 44 % | 3 % | (21)% | 3 % | \$3.2 | 12.8x | (5)% |
| | South Financial Group Inc. | TSFG | NC | 40 | 15 | (48) | 7 | 1.6 | 15.1 | (15) |
| | Washington Federal Inc. | WFSL | NC | 21 | 1 | (48) | NA | 2.2 | 14.1 | 8 |
| | UMB Financial Corp. | UMBF | NC | 10 | (0) | (16) | 7 | 1.8 | 22.4 | 20 |
| | Old National Bancorp | ONB | NC | 8 | (3) | (36) | 4 | 1.1 | 13.3 | (11) |
| | Commerce Bancshares Inc. | CBSH | NC | 2 | 2 | (23) | 4 | 3.1 | 13.8 | (4) |
| | Wilmington Trust Corp. | WL | NC | 0 | 6 | (25) | 6 | 2.5 | 13.0 | (9) |
| | Fulton Financial Corp. | FULT | NC | 0 | 9 | (36) | 3 | 2.2 | 13.2 | (23) |
| | Chittenden Corp. | CHZ | NC | 0 | 5 | (31) | 17 | 1.6 | 16.7 | 16 |
| | NewAlliance Bancshares Inc. | NAL | NC | 0 | 46 | (44) | 17 | 1.6 | 27.9 | (15) |
| | First Niagara Financial Group Inc. | FNFG | NC | 0 | 21 | (33) | 7 | 1.4 | 15.5 | (3) |
| | Susquehanna Bancshares Inc. | SUSQ | NC | 0 | 6 | (36) | 43 | 1.0 | 13.0 | (26) |
| | Sterling Financial Corp. (Washington) | STSA | NC | 0 | 19 | (23) | 24 | 1.3 | 10.4 | (25) |
| Citizens Republic Bancorp Inc. | CRBC | NC | 0 | (4) | (19) | 3 | 1.2 | 9.3 | (37) | |
| Long Stocks - average | | | | 94 % | 15 % | (11)% | 4 % | \$1.5 | 13.3x | (12)% |
| Short Stocks - average | | | | 9 | 9 | (31) | 11 | 1.8 | 15.0 | (9) |

Source: Company Filings, Compustat, FirstCall via FactSet, and Goldman Sachs Research.

Backtesting offers no proof, yet history corroborates our thesis

We backtested our basket of 34 long and 34 short stock ideas to determine the relative performance of the recommended trade (see Exhibit 12).

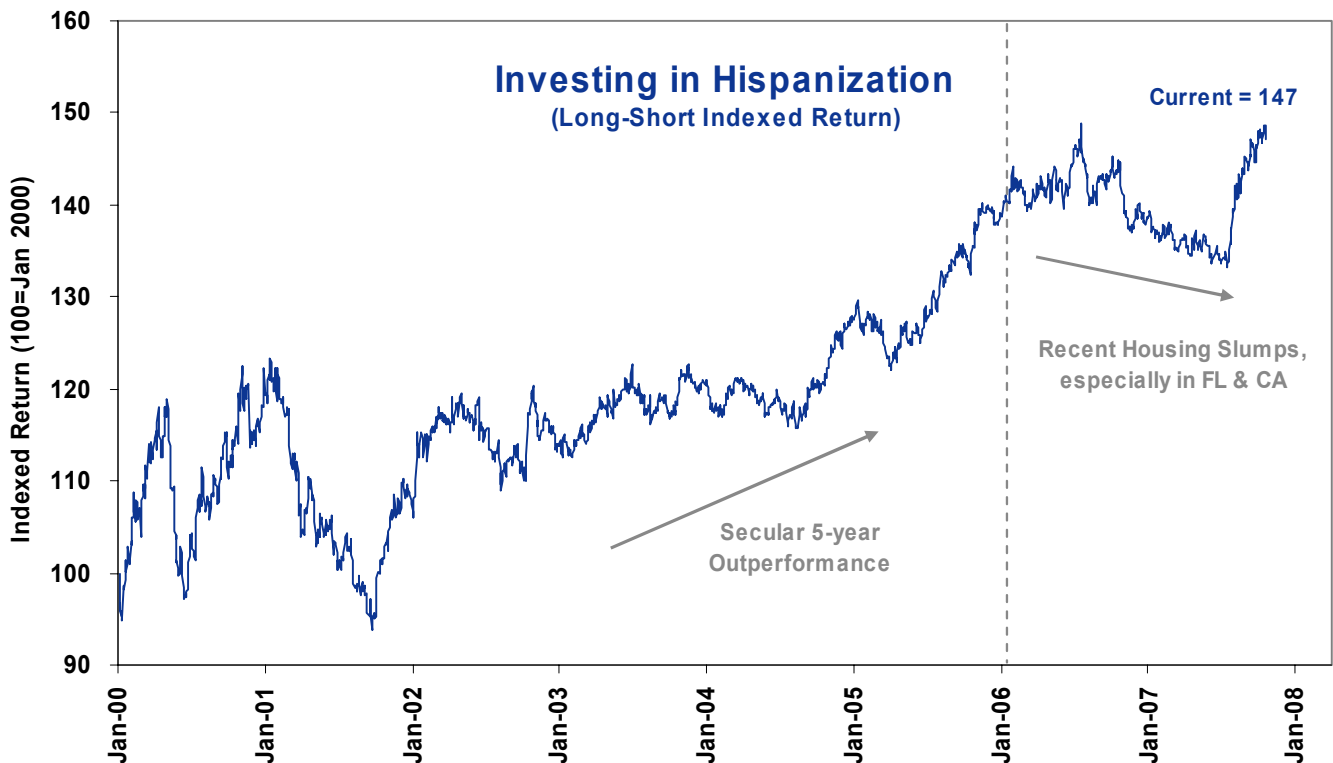
Initiating the trade in January 2000 would have earned 47% over the past 7 ¾ years. We believe this outperformance is partly due to Hispanization, although calculating the specific impact is not possible. During the same period, the S&P 500 returned just 16.5%, suggesting our trade would have outperformed by 3100 bp. The long/short strategy offers protection against market corrections while typically constraining upside potential (the Hispanization trade returned +7.8% in 2002 when the market dropped 22.1%). We conclude that the regionally and demographically exposed Housing, Retail, Health Care and Financial Services stocks have secularly outperformed.

Are we just trading regional economics?

High Mortgage Equity Withdrawal (MEW) in the “Right” states, as opposed to Hispanization, may have fueled local economies over the past decade (see Appendix A). Although this phenomenon may certainly have helped our trade to outperform historically, we believe the gains would be primarily concentrated in the Retail sector. When we analyze each leg of the trade individually, we find that the outperformance was spread across our four sectors. Therefore, we believe our strategy is a veritable demographic investment play, not simply a regional economics trade.

Exhibit 12: Back-testing our Hispanization long/short trade recommendation

Return of long/short Hispanization trade, 2000 to present



Source: Compustat and Goldman Sachs Research.

Hispanization Long Basket: Bloomberg ticker <GSTHHPNL>

We recommend investors buy these stocks, as they are poised to benefit from the Hispanization of the US.

Exhibit 13: Valuation of Hispanization Long Stock Ideas

as of October 22, 2007

Hispanization of the US - LONG Basket (Bloomberg <GSTHHPNL>)

| Company | Ticker | Sub-Sector | Rating | Price 23-Oct | MktCap (\$ mil) | P/E (NTM) | Return YTD | Div. Yield |
|------------------------------------|--------|-------------------------------|---------|-----------------|--------------------|--------------|---------------|---------------|
| Housing | | | | | | | | |
| D.R. Horton Inc. | DHI | Homebuilding | Buy | \$12.71 | \$4,018 | 111.0x | (50.8)% | 4.7 % |
| Meritage Homes Corp. | MTH | Homebuilding | Neutral | 14.62 | 370 | NA | (70.5) | 0.0 |
| AvalonBay Communities Inc. | AVB | Residential REITs | Buy | 115.77 | 8,916 | 22.8 | (12.2) | 3.0 |
| Camden Property Trust | CPT | Residential REITs | Neutral | 60.13 | 3,287 | 15.6 | (18.2) | 4.7 |
| Essex Property Trust Inc. | ESS | Residential REITs | Neutral | 117.86 | 2,882 | 20.8 | (9.3) | 3.2 |
| Retail | | | | | | | | |
| Ross Stores Inc. | ROST | Apparel Retail | Neutral | 26.24 | 3,702 | 13.5 | (7.2) | 1.1 |
| Tween Brands Inc. | TWB | Apparel Retail | NC | 30.55 | 916 | 14.4 | (25.5) | 0.0 |
| Wet Seal Inc. | WTSLA | Apparel Retail | NC | 2.58 | 253 | 12.3 | (59.4) | 0.0 |
| Best Buy Co. Inc. | BBY | Computer & Electronics Retail | Neutral | 47.31 | 19,644 | 14.2 | (3.8) | 1.1 |
| SUPERVALU Inc. | SVU | Food Retail | Neutral | 38.47 | 8,109 | 13.0 | 8.8 | 1.8 |
| Whole Foods Market Inc. | WFMI | Food Retail | Neutral | 48.05 | 6,655 | 33.0 | 3.7 | 1.5 |
| Winn-Dixie Stores Inc. | WINN | Food Retail | NC | 17.51 | 937 | 108.7 | 28.8 | 0.0 |
| Costco Wholesale Corp. | COST | Hypermarkets & Super Centers | Buy | 66.19 | 29,517 | 22.4 | 27.8 | 0.9 |
| Herbalife Ltd. | HLF | Personal Products | Buy | 43.08 | 3,032 | 15.8 | 10.9 | 1.8 |
| Health Care | | | | | | | | |
| CVS Caremark Corp. | CVS | Drug Retail | Buy | 40.12 | 58,384 | 19.1 | 29.3 | 0.6 |
| Medco Health Solutions Inc. | MHS | Health Care Services | Buy | 90.10 | 24,203 | 24.0 | 66.4 | 0.0 |
| PolyMedica Corp. | PLMD | Health Care Supplies | NC | 52.90 | 1,206 | 23.8 | 32.2 | 1.1 |
| Humana Inc. | HUM | Managed Health Care | Buy | 76.18 | 12,592 | 15.5 | 35.1 | 0.0 |
| Health Net Inc. | HNT | Managed Health Care | Neutral | 51.67 | 5,747 | 13.2 | 5.2 | 0.0 |
| AMERIGROUP Corp. | AGP | Managed Health Care | Buy | 35.22 | 1,780 | 15.9 | (5.7) | 0.0 |
| Financial Services | | | | | | | | |
| Cash America International Inc. | CSH | Consumer Finance | NC | 33.87 | 1,005 | 12.9 | (27.3) | 0.4 |
| First Cash Financial Services Inc. | FCFS | Consumer Finance | NC | 19.56 | 638 | 13.3 | (23.2) | 0.0 |
| City National Corp. | CYN | Regional Banks | Neutral | 66.90 | 3,217 | 13.2 | (6.5) | 2.8 |
| Cullen/Frost Bankers Inc. | CFR | Regional Banks | NC | 48.84 | 2,886 | 13.1 | (10.6) | 3.3 |
| East West Bancorp Inc. | EWBC | Regional Banks | NC | 34.59 | 2,104 | 12.9 | (1.6) | 1.2 |
| International Bancshares Corp. | IBOC | Regional Banks | NC | 21.18 | 1,463 | NA | (22.5) | 3.1 |
| First Community Bancorp Inc. | FCBP | Regional Banks | NC | 48.80 | 1,456 | 14.6 | (6.2) | 2.7 |
| Prosperity Bancshares Inc. | PRSP | Regional Banks | NC | 30.84 | 1,382 | 13.8 | (8.0) | 1.4 |
| Westamerica Bancorp | WABC | Regional Banks | NC | 46.69 | 1,381 | 15.5 | (5.1) | 2.9 |
| Pacific Capital Bancorp | PCBC | Regional Banks | NC | 25.28 | 1,185 | 11.1 | (22.6) | 3.5 |
| CVB Financial Corp. | CVBF | Regional Banks | NC | 11.57 | 970 | 14.3 | (10.2) | 3.0 |
| Sterling Bancshares Inc. | SBIB | Regional Banks | NC | 11.29 | 799 | 14.2 | (14.9) | 1.9 |
| First Bancorp Of Puerto Rico | FBP | Regional Banks | NC | 9.06 | 748 | NA | (4.0) | 3.1 |
| FirstFed Financial Corp. | FED | Thriffs & Mortgage Finance | NC | 42.41 | 691 | 7.7 | (35.5) | 0.0 |
| GSTHHPNL Basket (median) | | | | | \$1,942 | 14.4x | (6.8)% | 1.3 % |

Source: Compustat, FirstCall via FactSet, and Goldman Sachs Research.

Hispanization Short Basket: Bloomberg ticker <GSTHHPNS>

We recommend investors short sell these stocks, as they should underperform the shares of companies that are better positioned to benefit from Hispanization.

Exhibit 14: Valuation of Hispanization Short stock ideas

as of October 22, 2007

Hispanization of the US - SHORT Basket (Bloomberg <GSTHHPNS>)

| Company | Ticker | Sub-Sector | Rating | Price 23-Oct | MktCap (\$ mil) | P/E (NTM) | Return YTD | Div. Yield |
|------------------------------------|--------|-------------------------------|---------|-----------------|--------------------|--------------|----------------|---------------|
| Housing | | | | | | | | |
| NVR Inc. | NVR | Homebuilding | Neutral | \$468.00 | 2,670 | 13.6x | (26.2)% | 0.0 % |
| KB Home | KBH | Homebuilding | Neutral | 27.19 | 2,107 | NA | (45.9) | 3.7 |
| Equity Residential | EQR | Residential REITs | Neutral | 40.43 | 10,994 | 17.1 | (19.4) | 4.7 |
| Home Properties Inc. | HME | Residential REITs | NC | 50.52 | 1,686 | 14.9 | (12.1) | 5.2 |
| Mid-America Apt. Communities Inc. | MAA | Residential REITs | NC | 51.59 | 1,294 | 13.9 | (7.5) | 4.8 |
| Retail | | | | | | | | |
| J. Crew Group Inc. | JCG | Apparel Retail | Neutral | 37.69 | 2,416 | 24.6 | 2.1 | 0.0 |
| Buckle Inc. | BKE | Apparel Retail | NC | 40.75 | 1,230 | 17.9 | 22.9 | 2.5 |
| Cato Corp. | CTR | Apparel Retail | NC | 18.67 | 616 | 12.9 | (15.6) | 3.5 |
| RadioShack Corp. | RSH | Computer & Electronics Retail | Neutral | 19.82 | 2,680 | 12.3 | 15.9 | 1.3 |
| Ruddick Corp. | RDK | Food Retail | NC | 32.89 | 1,567 | NA | 18.8 | 1.3 |
| Casey's General Stores Inc. | CASY | Food Retail | NC | 28.22 | 1,418 | 18.5 | 19.6 | 0.9 |
| Weis Markets Inc. | WMK | Food Retail | Sell | 42.63 | 1,142 | NA | 7.6 | 2.7 |
| Sherwin-Williams Co. | SHW | Home Improvement Retail | NC | 66.12 | 8,557 | 13.4 | 4.3 | 1.9 |
| Cabela's Inc. | CAB | Specialty Stores | NC | 20.10 | 1,309 | 14.2 | (17.5) | 0.0 |
| Health Care | | | | | | | | |
| Rite Aid Corp. | RAD | Drug Retail | Sell | 4.02 | 3,198 | NA | (26.1) | 0.0 |
| Brookdale Senior Living Inc. | BKD | Health Care Facilities | Neutral | 38.21 | 3,838 | NA | (18.6) | 5.3 |
| Lifepoint Hospitals Inc. | LPNT | Health Care Facilities | Neutral | 29.29 | 1,666 | 12.3 | (14.9) | 0.0 |
| Kindred Healthcare Inc. | KND | Health Care Facilities | NC | 19.49 | 789 | 15.9 | (0.9) | 0.0 |
| UnitedHealth Group Inc. | UNH | Managed Health Care | Neutral | 48.84 | 63,483 | 12.7 | (10.4) | 0.1 |
| Centene Corp. | CNC | Managed Health Care | Neutral | 25.37 | 1,028 | 13.2 | (4.2) | 0.0 |
| Financial Services | | | | | | | | |
| Commerce Bancshares Inc. | CBSH | Regional Banks | NC | 45.47 | 3,094 | 13.7 | (5.2) | 2.2 |
| TCF Financial Corp. | TCB | Regional Banks | NC | 23.86 | 3,025 | 11.8 | (10.6) | 4.1 |
| Wilmington Trust Corp. | WL | Regional Banks | NC | 35.84 | 2,460 | 13.4 | (12.1) | 3.7 |
| Fulton Financial Corp. | FULT | Regional Banks | NC | 12.59 | 2,201 | 13.7 | (21.7) | 4.7 |
| UMB Financial Corp. | UMBF | Regional Banks | NC | 43.11 | 1,827 | 21.5 | 20.1 | 1.3 |
| Chittenden Corp. | CHZ | Regional Banks | NC | 36.19 | 1,669 | 17.2 | 18.4 | 2.5 |
| South Financial Group Inc. | TSFG | Regional Banks | NC | 20.24 | 1,499 | 14.1 | (21.4) | 3.6 |
| Sterling Financial Corp. | STSA | Regional Banks | NC | 23.42 | 1,200 | 9.8 | (30.3) | 1.5 |
| Citizens Republic Bancorp Inc. | CRBC | Regional Banks | NC | 15.37 | 1,163 | 9.4 | (39.4) | 7.5 |
| Old National Bancorp | ONB | Regional Banks | NC | 16.39 | 1,088 | 13.5 | (9.8) | 5.4 |
| Susquehanna Bancshares Inc. | SUSQ | Regional Banks | NC | 19.80 | 1,006 | 12.6 | (25.7) | 5.4 |
| Washington Federal Inc. | WFSL | Thrifts & Mortgage Finance | NC | 24.70 | 2,164 | 14.2 | 8.0 | 3.4 |
| NewAlliance Bancshares Inc. | NAL | Thrifts & Mortgage Finance | NC | 13.60 | 1,532 | 27.4 | (16.2) | 1.9 |
| First Niagara Financial Group Inc. | FNFG | Thrifts & Mortgage Finance | NC | 13.86 | 1,414 | 15.3 | (4.6) | 4.1 |
| GSTHHPNS Basket (median) | | | | | \$1,667 | 13.7x | (10.5)% | 2.5 % |

Source: Compustat, FirstCall via FactSet, and Goldman Sachs Research.

Appendix A: Leveraging the Geoscape® Intelligence System

We utilized the analytical tools offered by the Geoscape® Intelligence System to calculate the impact of the growing Hispanic population within each of the fastest 100 growing counties in the US.

Georgia alone contains 24 of the Top 100 list, and Hispanics typically represent 5% of the total population in these counties. We note that Georgia screens as the state with the fastest growing Hispanic population, and we do not find it a coincidence that the state happens to encompass the highest number of counties in the Top 100 list.

Hispanics typically make up 9% of the population in the fastest growing counties. Because Hispanics represent 15% of the total US population, it may appear as though they are underrepresented in the fast growing areas. However, we maintain that Hispanics are driving the expansion, growing from a relatively smaller base. In regards to spending, Hispanics tend to represent just 5% of household expenditures in the fast growing counties. We believe faster income growth among Hispanics will lead to a higher share of aggregate expenditures.

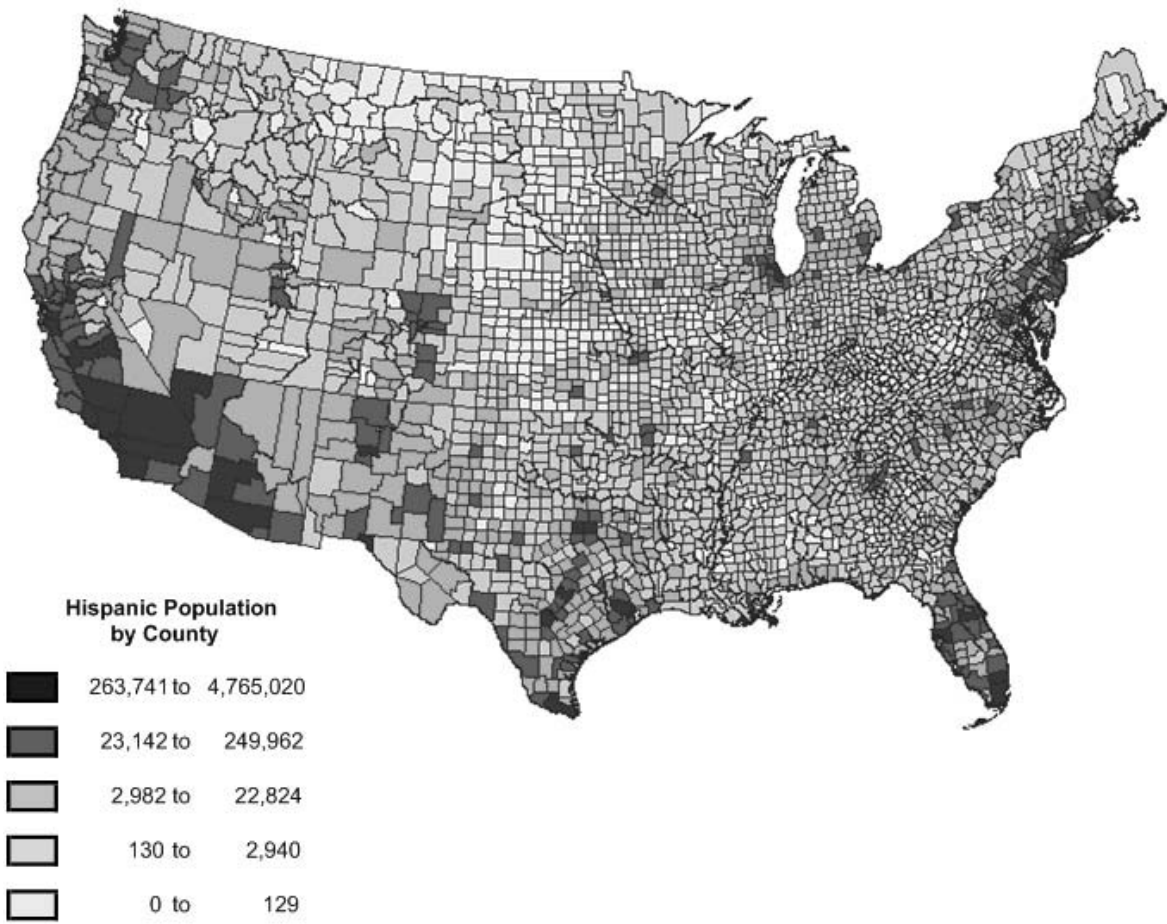
Although our analysis and investment framework draws primarily upon aggregated statistics, we recognize the importance of detailed information when assessing single-stock opportunities. We recommend that investors seeking focused investments utilize tools offered by Geoscape® to assess investment opportunities in greater detail.

Exhibit 15: 100 Fastest Growing Counties by State; Hispanic share of population and expenditures

| US Census Bureau - Fastest 100 Growing Counties | | | | | | |
|---|----|----------------------------------|--|--------------|---------------------------|--|
| State | | No. of Counties in Top 100 | Hispanic as % of Total (average county) | | Target Hispan State | |
| | | | Population | Expenditures | | |
| Georgia | GA | 24 | 5 | 3 | Growing Markets | |
| Florida | FL | 12 | 13 | 8 | Largest Markets | |
| Virginia | VA | 11 | 6 | 4 | NA | |
| Texas | TX | 8 | 20 | 12 | Largest Markets | |
| Colorado | CO | 5 | 13 | 9 | Concentrated Markets | |
| Minnesota | MN | 5 | 3 | 1 | NA | |
| North Carolina | NC | 4 | 7 | 4 | Growing Markets | |
| Illinois | IL | 2 | 16 | 11 | Largest Markets | |
| South Carolina | SC | 2 | 7 | 3 | Growing Markets | |
| Tennessee | TN | 2 | 5 | 3 | Growing Markets | |
| Arizona | AZ | 1 | 30 | 19 | Concentrated Markets | |
| California | CA | 1 | 11 | 7 | Largest Markets | |
| Nevada | NV | 1 | 29 | 17 | Concentrated Markets | |
| Total | | 100 | 9 | 5 | | |

Source: Geoscape® American Marketscape DataStream™: 2008 Series; Latin Force Group LLC, US Census Bureau, and Goldman Sachs Research.

Exhibit 16: Hispanic population by county



Source: Geoscape@ American Marketscape DataStream™: 2008 Series; Latin Force Group LLC.

Exhibit 17: Housing prices have appreciated dramatically in the "Right" states
 Median One-Family Home Price Change, 2000 to 2007

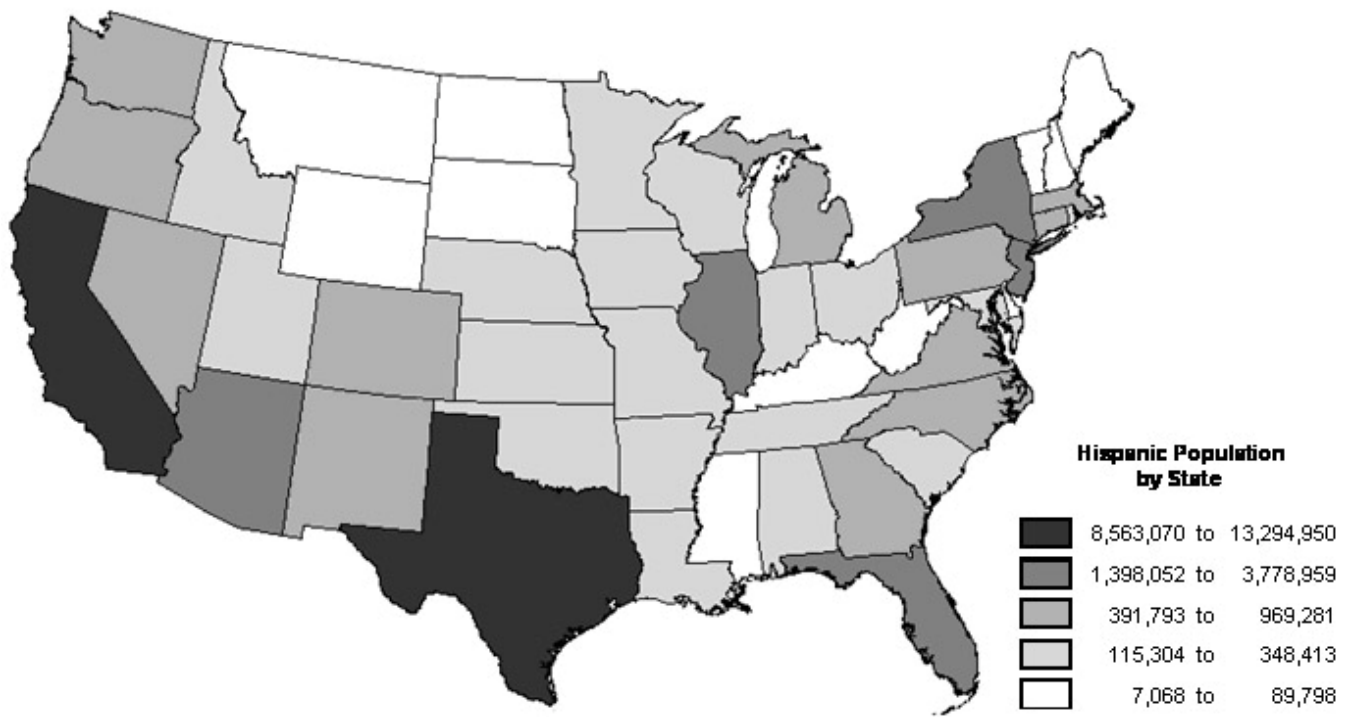
| Metro Area | States | Median Home Price Change |
|--------------------------------|--------|--------------------------|
| | | 2000-'07 CAGR |
| Los Angeles | CA | 16.6 |
| Miami | FL | 15.9 |
| Washington | DC | 15.4 |
| San Diego | CA | 13.1 |
| Baltimore | MD | 13.1 |
| Las Vegas | NV | 12.7 |
| Seattle | WA | 11.7 |
| New York | NY | 11.4 |
| Phoenix | AZ | 10.5 |
| Philadelphia | PA | 10.3 |
| San Francisco | CA | 8.6 |
| United States (average) | | 8.2 |
| Boston | MA | 7.7 |
| San Antonio | TX | 7.4 |
| Salt Lake City | UT | 6.8 |
| Minneapolis | MN | 6.7 |
| Houston | TX | 4.8 |
| Atlanta | GA | 4.5 |
| Denver | CO | 3.9 |
| Pittsburgh | PA | 3.1 |
| Kansas City | MO | 2.9 |
| Dallas | TX | 2.8 |
| Cincinnati | OH | 1.4 |
| Detroit | MI | 1.2 |
| Cleveland | OH | 0.2 |

Home Prices rose the fastest among Metropolitan areas in the 'Right' states.

Perhaps higher levels of Mortgage Equity Withdrawal, rather than Hispanization, fueled the local economies, causing our trade strategy to outperform.

Source: National Association of Realtors, Office of Federal Housing Enterprise Oversight, and Goldman Sachs Research.

Exhibit 18: Hispanic population by state



Source: Geoscape@ American Marketscape DataStream™: 2008 Series; Latin Force Group LLC.

Appendix B: The Hispanization trend in context ⁴

The rapid growth of the Hispanic/Latino population represents one of the most important demographic trends taking place in the United States. It will have dramatic social, political, economic, and market influences on the country during the next 25 years.

High levels of immigration, above-average fertility rates, and a younger demographic community are driving dramatic population growth among Hispanic/Latinos relative to the US average. Hispanic/Latinos continue to advance economically, magnifying the effects of the increase in absolute population. Spending patterns are likely to change as incomes rise in this population segment.

US businesses across all industries have begun to focus on of the rapidly growing Hispanic/Latino market through targeted advertising spending and customized products. We believe this trend will continue. Firms taking the lead in these initiatives are likely to see their revenues grow faster than those of their competitors over the long term.

This report focuses on what we believe are some of the best long/short investment opportunities for portfolio managers to participate in the trend we refer to as the “Hispanization of the United States.” We do not directly address other important aspects of this theme (such as the increased political influence of Latinos or the societal consequences of the shift in demographics), several recently published books highlight these issues.⁵ These studies put the emerging demographic shift into context.

What defines a Hispanic or Latino?

Nearly 13% of the US population classified themselves as Hispanic or Latino in the 2000 Census. Specifically, question five on the survey form asked “Is this person Spanish/Hispanic/Latino?” Possible answers included “(a) No, not Spanish/Hispanic/Latino, (b) Yes, Mexican, Mexican American, Chicano, (c) Yes, Puerto Rican, (d) Yes, Cuban, or (e) Yes, other Spanish/Hispanic/Latino (print group).”

The Census Bureau considers people of Hispanic origin to be those who indicated that their origin was Mexican, Puerto Rican, Cuban, Central or South American, or some other Hispanic origin. People of Hispanic origin may be of any race.

- **From an official perspective,** the terms “Hispanic” and “Latino” may be used interchangeably to reflect the new terminology in the standards issued by the Office of Management and Budget in 1997 and implemented on January 1, 2003.
- **From a practical perspective,** consider how veteran Univision anchorman and author Jorge Ramos describes a Hispanic/Latino person:

I use the terms “Hispanic” and “Latino” interchangeably. In California and Chicago, people generally prefer “Latino”. In Florida and Texas, “Hispanic” usually takes priority. But when it

⁴ See *The Hispanization of the United States*, Goldman Sachs & Co., November 22, 2004 and *Revisiting Hispanization*, Goldman, Sachs & Co., October 7, 2005.

⁵ See, for example, *The Latino Wave: How Hispanics Will Elect the Next American President*, Jorge Ramos, HarperCollins, 2004; *Who We Are Now: The Changing Face of America in the Twenty-First Century*, Sam Roberts, Henry Holt & Co., 2004; *Who Are We? The Challenges to America’s National Identity*, Samuel P. Huntington, Simon & Schuster, 2004; and *National Survey of Latinos*, Pew Hispanic Center, 2002.

comes down to it, most of the people I know don't use either of these terms to describe themselves. They say, "I'm Mexican," "I'm Cuban," "I'm Puerto Rican," "I'm Colombian," or "Mexican American." What they don't say is "I'm Latino" or "I'm Hispanic." ...

...while a small percentage of the population does prefer to define themselves as such, the terms "Hispanic" or "Latino" have been invaluable in their ability to quantify a growing segment of the population and give it a single categorization. By grouping together under one name (or two), we can present a united front, on both political and economic matters as well as in defense of our civil rights and education. If an official, unifying category did not exist, our incipient political power would be much more diluted.⁶

Spanish language is the common thread among the diverse Latino population

The National Survey of Latinos conducted and published in 2002 by the Pew Hispanic Center notes that Latinos come from many different countries of origin and have different degrees of language assimilation. The Latino population is comprised of recent immigrants, children of immigrants, and those whose families have been in the United States for multiple generations.⁷

In 2000, for the first time, the majority of Americans born abroad were from Latin America. Mexicans alone accounted for 25% of all foreign-born residents.

Language skills varied greatly based on birthplace. Foreign-born Latinos in the Pew Survey were found to be much more likely than native-born Latinos to be Spanish-dominant in their primary language (72% versus 4%). In contrast, native-born Latinos were English dominant (61% versus 4%) or bilingual (35% versus 24%).

As Sam Roberts notes in *Who Are We Now: The Changing Face of America in the Twenty-First Century*, **"In California, for the first time since the late 1850s, shortly after the territory was seized from Mexico, the majority of babies born in the state are Hispanic.** Non-Hispanic whites now constitute a minority of the population in California and New Mexico – *again* – and are close to becoming a minority in Texas, too. In the late 1990s, Hispanics, propelled by both immigration and higher birth rates, achieved numerical parity with blacks or African Americans (the Census uses the terms interchangeably)."⁸

Mexican Immigration and the Hispanization of America

Harvard University professor Samuel Huntington points out many ways in which the contemporary Mexican immigration trend is unique in American history. We note four of these observations below and highlight implications of the Hispanic/Latino immigration wave on US society.

⁶ See *The Latino Wave*, Jorge Ramos, page 97.

⁷ See *Who We Are Now: The Changing Face of America in the Twenty-First Century*, Sam Roberts, page 122. Our boldface.

⁸ See *Who Are We? The Challenges of America's National Identity*, Samuel P. Huntington, pages 221-256. Our boldface.

1. Linguistic concentration

Previous immigration surges included a diversity of foreign-born locations and mother tongues. Such variety facilitated assimilation. However, almost half of the immigrants arriving in the United States over the past 40 years speak a single non-English language: Spanish. The domination of the immigrant flow by a single language is unprecedented.

Such concentration reduces the need for assimilation.

2. Regional concentration

More than 69% of the US Hispanic/Latinos population is concentrated in the Southwest: California, Nevada, New Mexico, as well as Texas, Florida, and New York. **This concentration allows language usage and traditional culture to persist for long periods, even indefinitely.**

3. Immigrant volume

Hispanic/Latinos comprise 52% of annual immigrants into the United States. Each year over 700,000 thousand Hispanic/Latinos enter the United States, with roughly 40% entering illegally. **The constant supply of first-generation immigrants will ensure the Hispanic/Latino population retains culture, language, and behavioral patterns longer than other immigrant groups.**

4. Contiguous border

The United States is unique among developed world nations in that it shares a long, contiguous border with an economically emerging nation. Japan, Australia and New Zealand are islands. Canada is bordered only by the United States. The closest European countries come to the emerging world is across the Strait of Gibraltar between Spain and Morocco and the Straits of Otranto between Italy and Albania. This US-Mexico border will likely continue to serve as a unique gateway from the emerging world to the developed world – a gateway that has been and will be impossible to fully control. **This all but ensures the massive immigrant inflow will continue until the economic gap between the United States and Central and South American countries closes significantly.**

A supply-side view of the labor market

The growth in the US labor force is slowing. During the past four years, the growth rate of the US labor force has slowed by half, falling to 0.8% per year from about 1.6% in the late 1990s, as the Goldman Sachs Economics Group noted in a report published earlier this year.⁹ Three basic factors affect the supply of labor: (1) natural population growth, (2) immigrants and temporary workers, and (3) labor force participation. **The flow of foreign labor, including temporary workers, permanent legal immigrants, and undocumented immigrants, has become increasingly important to the US labor supply.** Official data show that immigration has added nearly half a percentage point to annual labor force growth in the United States over the past 40 years (roughly 20% of the total labor force growth over this period).

⁹ See *A Supply-Side View of the Labor Market*, US Economics Analyst, Goldman Sachs Research, April 23, 2004.

The New Colossus: Why immigration is good for America

Although immigrants no longer arrive via Ellis Island, in a sense things have never changed. The stirring lines of Emma Lazarus' poem still ring true: "Give me your tired, your poor, your huddled masses yearning to breathe free . . . I lift my lamp beside the golden door!" Immigrants typically arrive poorer and less educated than native-born Americans. But the sense of economic opportunity that attracted them here in the first place serves as a powerful inspiration for each wave of immigrants to pursue upward economic mobility.

Do immigrants cost Americans money or contribute to the nation's economy?

Sam Roberts answers the question by citing a 1997 study by the National Research Council. "**Age and education** are the variables that appear most likely to determine the difference between how much an immigrant costs society in services provided over his lifetime and what the government gains in taxes. An adult arriving with less than a high school education costs about \$89,000 (in 1996 dollars) over his lifetime. An adult who graduated from high school would cost \$31,000. An adult with more than a high school degree would contribute \$105,000."¹⁰

Purchasing patterns: Will Hispanics start buying Starbucks coffee?

Hispanic/Latinos spend 93% of their current discretionary income versus the US average of 82%. In addition, they follow buying patterns characteristic of lower-income groups and direct a greater share of income directed towards: (1) rental expense, (2) food, and (3) transportation. As Hispanic/Latinos advance economically, we anticipate a higher savings rate and an "upmarket" spending shift towards areas such as health care and insurance.

Immigration would blur the shift in spending patterns. Continued high immigration volumes are expected to have the same effect on spending patterns as on income levels for Hispanic/Latinos. As second-generation immigrants advance economically, they are likely to shift spending towards health care and insurance. However, while this is happening first-generation immigrants, with lower incomes, would continue to spend according to necessity, favoring food, housing, and transportation.

Over the long term the generation effect will rule the day. As second-generation and above immigrants make up a greater share of the population, the "upmarket" spending shift becomes more profound. Currently Hispanic/Latinos have the lowest: (1) health care insurance coverage rates, and (2) home ownership rates and (3) savings rates of the large ethnic groups in the United States. Higher incomes will likely lead to higher insurance coverage, home ownership, and savings rates.

¹⁰ *Who Are We Now? The Changing Face of America in the Twenty-First Century*, Sam Roberts, page 130.

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