

U.S. ECONOMIC OUTLOOK

# Economic weather report: Sunny growth, cloudy jobs, sticky showers

Our February 2026 U.S. economic outlook highlights an economy that ended 2025 with surprising resilience, even as underlying pressures continued to build. Real GDP accelerated through the middle of the year and is tracking close to a solid 3% annualized rate in Q4 – despite a policy environment shaped by shifting tariffs, tighter immigration constraints and fiscal uncertainty. Beneath the surface, however, the labor market has softened, with hiring constrained by limited labor force growth and firms adopting a cautious ‘low-hire, low-fire’ stance amid weakening job-perception metrics. Meanwhile, inflation is cooling only gradually, with price levels still elevated for essentials and firms planning to pass tariff-driven cost increases to consumers. These persistent cost headwinds support our expectation for slower consumption in 2026 and reinforce the Fed’s patient, data-dependent stance.

- **Growth:** With stronger late-2025 momentum and firmer incoming data, we now look for above-consensus real GDP growth of 2.7% on an annual-average basis (2.1% on a Q4/Q4 basis) – modestly higher than previously projected. Growth moderates as consumer spending cools, while fiscal-supported equipment investment and a gradual shift toward a more sustainable expansion help keep the overall outlook steady.
- **Labor market:** Despite cooler hiring and unemployment at 4.4% through December, labor conditions remain orderly, with limited layoffs and steady wage growth. We expect unemployment to move into the upper-4s by mid-2026, reflecting gradual normalization rather than sharp deterioration.
- **Inflation:** Core PCE is estimated to have risen 3.0% over the 12 months through December, with elevated readings driven largely by goods-sector price pressures linked to tariffs, while disinflation continues across most services categories. We expect core PCE to hover close to 3% through mid-2026 before gradually converging toward the Fed’s 2% target by late 2027.
- **Federal Reserve:** The Fed held rates steady in January and emphasized a patient, data-dependent approach, noting that policy is now near the upper end of ‘loosely neutral.’ With labor signals mixed but stable and inflation still above target but gradually easing, we continue to expect two cuts in 2026 – likely June and December – bringing the policy rate to 3.00–3.25%.
- **Risks:** Downside risks remain elevated, with our near-term recession probability now at 30%. Softer consumer sentiment – shaped by concerns around job stability and affordability – adds fragility, while uncertainty across fiscal, trade and immigration policy, along with the potential for a policy misstep by the Fed, continues to cloud the outlook.

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U.S. Bank Economics Research Group February 2026 Macro forecast summary

	Actual 2024	Forecast 2025	Forecast 2026	Forecast 2027
Real GDP	2.8	2.3	2.7	2.1
Consumer Spending	2.9	2.7	2.4	1.9
Investment	3.0	1.9	2.3	3.6
Housing Starts	1.37	1.36	1.36	1.39
Unemployment Rate	4.0	4.3	4.6	4.4
Consumer Price Index	3.0	2.7	2.9	2.4
Core PCE Price Index	2.9	2.8	2.9	2.3
Federal Funds (Upper Target)	5.3	4.4	3.6	3.2

Forecast as of: February 4, 2026. Sources: U.S. Bank Economics, Moody's Analytics, and Bloomberg. 1. Projections for real GDP are annual percentage change. Projections for housing starts are in millions, annualized. Projections for the unemployment rate represent annual averages. 2. Projections for the CPI and Core PCE are annual percent change; 3. Interest rate projections represent annual averages and are the views of the U.S. Bank Economics Group.

## From the desk of the Chief Economist: U.S. labor supply, from boom to bust

What is the most valuable resource in the world?

Is it land? Trees? Oil? Minerals? Water? How about labor?

From factory and office workers to scientists, labor is the most important resource in the world. Human input is essential for producing goods and services and utilizing natural resources. However, demographic shifts have caused a sharp decline in labor supply growth since the post-World War II baby boom. Without immigration, the Congressional Budget Office (CBO) projects the U.S. population to shrink starting in 2034.

The labor participation rate is now just 62.4%, which is 4.9% lower than its high of 67.3% when the baby boomers filled the workforce, and is destined to move lower as older workers continue to retire over the next decades and net migration saw huge [outflows in 2025](#). The U.S. birth rate has declined significantly below the replacement level, limiting younger worker availability. That pushed the U.S. age dependency ratio, defined as the population age 65 and over as a share of the workforce, to 28% in 2024 from 19% in 2010. It is expected to reach 38% by 2050. Fewer workers reduce government tax revenues, complicating funding for pensions and healthcare that is already at 46% of the federal budget.

There are some benefits for those workers remaining in the job market. A smaller labor force tightens the labor market, raises wages, lowers the unemployment rate and improves credit quality.

However, labor shortages increase business costs and skills gaps, as the quality of workers for the job shrinks. This reduces productivity, weakens business competitiveness and adds to inflationary pressures. Fewer consumers will reduce spending activity, weakening growth.

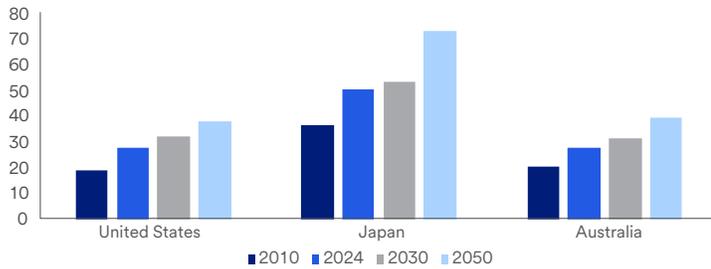
The U.S. is not alone in this problem. Other countries are aging with low birth rates.

Proposed solutions include incentivizing automation and workforce reskilling, alongside adjusting immigration policies to attract foreign workers. Comparisons with countries like Australia, which embraces open immigration and experiences economic growth, contrast with Japan's restrictive policies and economic stagnation

Japan and Australia also have an aging population and low birth rates. But Australia has an open immigration policy that has reduced its age dependency ratios, while Japan has tighter immigration policies, widening its age dependency ratio. Comparing economic conditions, Australia hasn't had a recession in 25 years, while Japan slowly recovers from its "Lost Decade." And with Japan's government debt to GDP ratio more than seven times larger than Australia, it seems that the former made the right decision.

**Age dependency ratio**

65+/15-64

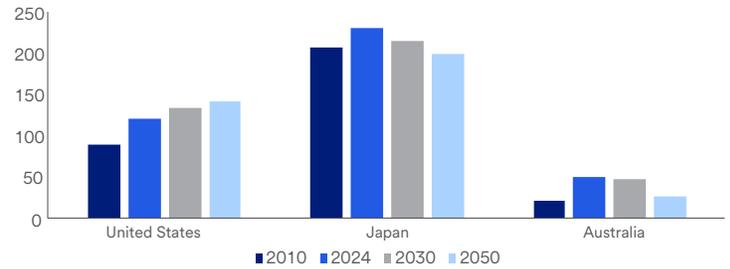


Source: U.S. Bank Economics; U.S. Bureau of Economic Analysis (BEA), Bloomberg

[Read the full commentary here >](#)

**General government debt to GDP ratio**

Yearly, percentage



**Economy: Solid footing on shifting ground**

The U.S. economy ended 2025 with considerably more momentum than we anticipated earlier in the year. After a soft first quarter, when real GDP dipped slightly amid shifts in trade, immigration and federal spending policies, growth rebounded meaningfully. The economy expanded at a 3.8% pace in the second quarter and an even stronger 4.4% in the third, with early data pointing to another solid reading near 3% in the fourth. All told, our growth expectation for 2025 is on track to reach about 2.6% on a fourth quarter-to-fourth quarter basis – an impressive outcome in a year marked by heightened, multi-layered policy uncertainty.

Consumers remained the centerpiece of economic resilience through late 2025. Household spending contributed about half of overall growth in the second and third quarters, even as higher import tariffs created a modest drag on purchasing power and raised prices on select goods. Moreover, updated data for October and November show that personal spending continued to hold up as the holiday season approached, with three-month annualized real consumption running at 3.1% annualized – consistent with signals from retail sales. Even as the labor market cooled gradually, households continued to spend, suggesting that consumer activity eased but did not lose steam at year-end.

**U.S. Consumer Spending**



Source: U.S. Bank Economics; U.S. Bureau of Economic Analysis (BEA), Bloomberg

That said, the income side of the household ledger presents a more restrained picture. Real disposable income was up just 1.0% year-over-year through November, as wage and salary growth decelerated alongside a normalization in hiring demand. In fact, income has grown more slowly than spending for seven straight months – the second longest such stretch on record. This gap has been financed by a drawdown in savings, with the personal saving rate slipping to 3.5% in November – down from 5.1% at the start of the year and the lowest level since late 2022.

So far, households have been able to sustain spending thanks to still-manageable debt service burdens and balance sheets supported by elevated home values and rising equity markets. But the cushion is thinning. Moreover, consumer sentiment surveys continue to show deepening concern about job stability and affordability – signals that have often preceded periods of weaker activity. As a result, despite the strong finish to 2025, we continue to expect both consumer spending and overall GDP growth to moderate in 2026.

### Labor market: Slower hiring, slower supply

Even as economic activity accelerated throughout 2025, the labor market lost momentum. Payroll growth has slipped toward stall speed – averaging a small decline over the past three months through December as federal employment fell sharply – while the unemployment rate has edged up modestly to 4.4%, from nearer 4% at the start of the year. The juxtaposition reflects a year shaped by both supply and demand shocks: tighter immigration policy weighing on labor supply and tariff-related uncertainty restraining labor demand. The practical result is a lower ‘breakeven’ pace of monthly hiring – now roughly 25,000 jobs – consistent with an unemployment rate that drifts higher but keeps the labor market near full employment.

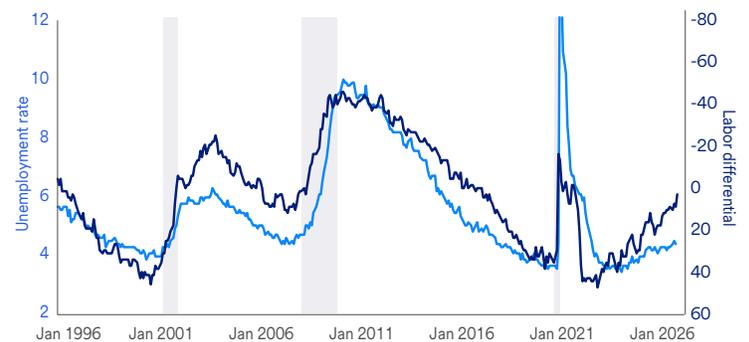
On the supply side, immigration restrictions have meaningfully slowed labor force growth, reducing the economy’s sustainable pace of job creation. With fewer new workers available, sectors that rely heavily on immigrant labor – construction, leisure/hospitality, manufacturing, agriculture and personal services – face tighter staffing conditions and localized wage pressure even as overall wage growth cools. A breakeven near ~25,000 means softer payroll prints can occur without signaling a sharp deterioration in labor slack. In short, today’s slower hiring pace ‘fits’ the available labor supply.

Demand for labor has also cooled, though in a distinctive pattern. Hiring has settled into a ‘*low-hire, low-fire*’ equilibrium: firms remain reluctant to expand headcount amid tariff and policy uncertainty, yet layoffs remain limited outside of federal cuts and trade-sensitive industries such as manufacturing, agriculture-related businesses and transportation/distribution. These dynamics are also visible in the data backdrop. Recent payroll gains have likely been overstated, consistent with labor demand running closer to flat. If realized, upcoming data revisions will validate what businesses have been signaling for months: caution rather than collapse.

Labor perceptions are catching up to these realities. The Conference Board’s consumer confidence measure deteriorated into January, as fewer consumers described jobs as “plentiful” and more said they were “hard to get.” We pay particular attention to its Labor Market Differential – the gap between “plentiful” and “hard to get” – because its inflection points have historically preceded recessions. Without getting overly technical, the takeaway is clear: the indicator has

narrowed sharply from its highs and is now near levels last seen in 2020, helping explain why job stability remains a top household concern despite strong GDP prints and buoyant financial markets.

### U.S. Job Insecurity



Source: U.S. Bank Economics; Bureau of Labor Statistics (BLS); Conference Board, Bloomberg

Our base case for 2026 is that monthly job gains hover around the zero-to-50,000 needed to keep unemployment in the mid-to-upper-4% range – still close to the Fed’s estimate of full employment. But risks remain tilted to the downside. Should immigration flows tighten further or policy uncertainty persist, hiring could stay below breakeven for longer, pushing joblessness higher and prompting already cost-conscious consumers to grow more cautious. In that scenario, economic growth risks slowing meaningfully. Practically, it remains prudent to prepare as if the labor market pessimists have the stronger case – even as we acknowledge that a soft-landing path is still possible if supply constraints ease and policy uncertainty fades.

### Inflation: Cooling, but affordability taking center stage

The past month’s inflation data have reinforced a familiar theme: price pressures are easing, but only gradually. Headline and core PCE inflation both held at 2.8% year-over-year through November, while recent Consumer Price Index (CPI), Producer Price Index (PPI), and Beige Book readings delivered a similar message – disinflation is progressing, but unevenly, and underlying price pressures remain above the Fed’s 2% target. Early tracking for December points to a somewhat firmer reading, likely nudging core Personal Consumption Expenditures (PCE) back toward 3.0% year-over-year and keeping shorter-term inflation trends hovering near that pace at the end of 2025.

Beneath the broader disinflation trend, the divide between goods and services continues to shape the inflation path. Goods prices have largely flattened in recent months, with limited early evidence of tariff-related pass-through, though both December CPI and the January Beige Book suggest that input-cost pressures may begin to put mild upward pressure on goods prices in the months ahead. In contrast, services inflation remains the stickier part of the basket – cooling, but still higher and more persistent than goods inflation – driven by categories such as healthcare and financial services. Housing remains the central wildcard. October’s disrupted data collection likely understated shelter inflation, a distortion that should unwind as reporting normalizes in early 2026. Taken together, services inflation is easing from earlier highs, goods inflation remains uneven, and there is still little sign of a renewed acceleration. Our outlook therefore remains mostly unchanged: core PCE should hover around 3% through mid-2026 before gradually gliding back toward 2% by late 2027.

At the same time, important developments are emerging outside the official inflation data, as a widening gap has opened between measured inflation and households’ lived experience. Even as price increases lessen to more moderate levels, consumer sentiment surveys show that affordability concerns continue to dominate, with many households expressing ongoing dissatisfaction with their financial situation. The underlying reason is straightforward: prices for essentials – food, housing and childcare – remain significantly higher than before the pandemic. Costs for these necessities are roughly 25–30% above early-2021 levels and have consistently outpaced earnings growth, placing the greatest strain on low- and middle-income households. In effect, even as inflation cools, the elevated price level continues to weigh heavily on day-to-day finances.

This divergence creates a central tension heading into 2026. Inflation is easing and real wages are improving, yet households remain uneasy because elevated prices – not the pace of price increases – now define their day-to-day reality. As a result, affordability is increasingly the lens through which consumers interpret economic conditions. With savings buffers thinning and a growing share of household budgets devoted to essentials, consumers have less flexibility to absorb rising costs elsewhere, leading discretionary purchases to slow as households prioritize core needs. This dynamic captures the ‘last-mile’ challenge of disinflation:

even as inflation gradually approaches target, the cumulative price reset of the past three years continues to shape how Americans feel – and how they’ll spend going forward.

## U.S. Inflation

Core PCE Price Index, Annualized Percent Change; Dec’25 estimated



Source: U.S. Bank Economics; U.S. Bureau of Economic Analysis (BEA)

## Monetary policy: A dovish hold, data first

The January Federal Open Market Committee (FOMC) meeting delivered what we view as a dovish hold, with the Committee leaving rates unchanged but underscoring that policy remains modestly restrictive – what Chair Jerome Powell described as “loosely neutral.” In the press conference, he emphasized that the economy is entering 2026 on solid footing, supported by resilient consumer spending and continued expansion in business investment, even as housing remains a notable weak spot. Despite firmer growth, Powell reiterated that the current stance continues to restrain activity appropriately as the Fed works to guide inflation back to target.

The message on the labor front emphasized early signs of stabilization in the unemployment rate but cautioned against placing too much weight on a limited number of data points. Powell pointed to mixed signals – continued cooling in labor demand alongside softer job-perception metrics – consistent with the removal of post-meeting language suggesting rising downside risks to employment. At the same time, although inflation remains somewhat above target, the Fed conveyed growing confidence that tariff-related goods inflation will ease as the year progresses, while disinflation in services continues to build – helping preserve the prospect of eventual policy loosening.

Against this backdrop, Powell emphasized a continued “meeting-by-meeting” approach, describing the current pause as deliberate and noting that the Committee is well positioned to wait before making further adjustments. With risks to both inflation and employment now diminished, the Fed signaled a clear lack of urgency to move rates in either direction. In effect, the central bank is keeping its options open – comfortable holding steady while monitoring whether inflation and labor market dynamics evolve in line with its objectives.

A key debate now threading through policy deliberations is the role of productivity. The widening gap between solid GDP growth and subdued job gains can theoretically be reconciled by rising productivity, with AI-related capital spending and process automation allowing firms to expand output with fewer workers. Powell acknowledged the historical pattern – technological waves can temporarily disrupt labor markets but ultimately raise productivity and wages – while expressing appropriate humility about whether recent gains reflect a persistent structural shift or a temporary cyclical lift. He also emphasized that higher productivity raises potential output and meaningfully shapes the Fed’s interpretation of inflation, slack and the policy stance, even if near-term readings remain noisy.

Finally, the leadership transition and evolving FOMC composition introduce additional uncertainty. Powell reiterated the importance of institutional independence and avoided signaling how policy might evolve under a new Chair, even as January’s decision again featured two dissents – from Governor Christopher Waller, a potential Chair contender, and Governor Stephen Miran, who has served in an advisory capacity to the White House – highlighting the cross-currents shaping internal deliberations. Despite these differences, broad support nevertheless coalesced around holding rates steady. Our base case remains that mid-year is the earliest likely window for the next adjustment, contingent on cleaner inflation readings as tariff effects fade and corroborating evidence from both labor market and activity data. With limited evidence that conditions warrant a materially easier stance, the scope for significant policy loosening remains narrow.

## U.S. Bank Economics Research Group February 2026 Macro forecast summary

	Actual	Forecast							Actual	Forecast		
	2025	2025		2026				2027				
	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	2024	2025	2026	
<b>Economic Data<sup>1</sup></b>												
Nominal GDP	8.3	6.0	5.5	5.0	3.9	4.1	4.0	4.1	5.3	5.1	5.6	
Real GDP	4.4	2.8	2.4	2.1	2.0	2.0	2.0	2.1	2.8	2.3	2.7	
Consumer Spending	3.5	2.8	2.2	2.0	1.8	1.8	1.9	2.0	2.9	2.7	2.4	
Investment	0.0	2.2	5.5	4.5	3.2	3.2	3.7	3.7	3.0	1.9	2.3	
Residential Structures	-7.1	-5.0	0.0	0.0	0.5	1.0	1.5	2.0	3.2	-2.4	-2.1	
Non-Residential Structures	-5.0	-3.0	2.0	2.0	2.0	2.0	2.0	2.0	1.1	-5.0	-0.5	
Intellectual Property	5.6	4.0	5.0	4.0	3.5	3.0	3.3	3.5	3.5	5.6	5.0	
Equipment	5.3	4.0	5.5	6.0	6.0	5.0	4.5	4.0	3.5	8.3	5.5	
Change in Inventory	-23.9	-15.0	2.0	10.0	5.0	5.0	10.0	15.0	43.5	28.7	5.5	
Government Spending	2.2	-0.9	1.8	0.8	0.8	0.8	0.8	0.8	3.8	1.4	0.8	
Federal	2.7	-4.0	3.0	0.6	0.6	0.6	0.6	0.6	3.8	-0.3	0.2	
State & Local	2.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	3.8	2.5	1.3	
Imports	-4.4	-2.7	3.5	3.0	2.0	2.0	2.5	2.5	5.8	2.6	-1.5	
Exports	9.6	1.6	1.0	2.0	3.0	3.0	2.5	2.5	3.6	1.9	2.5	
Housing Starts	1.34	1.34	1.34	1.36	1.36	1.37	1.37	1.38	1.37	1.36	1.36	
Unemployment Rate	4.3	4.5	4.6	4.6	4.6	4.5	4.4	4.4	4.0	4.3	4.6	
<b>Prices<sup>2</sup></b>												
Consumer Price Index	2.9	2.8	2.7	3.0	2.9	2.9	2.6	2.4	3.0	2.7	2.9	
Core PCE Price Index	2.9	2.8	2.9	3.1	3.0	2.8	2.6	2.4	2.9	2.8	2.9	
<b>Interest rates<sup>3</sup></b>												
Federal Funds (Upper Target)	4.46	4.02	3.72	3.66	3.45	3.39	3.20	3.20	5.31	4.37	3.56	
2-Yr Treasury Note	3.72	3.52	3.54	3.47	3.42	3.39	3.37	3.36	4.37	3.81	3.46	
10-Yr Treasury Note	4.26	4.10	4.22	4.26	4.28	4.29	4.29	4.30	4.21	4.29	4.26	
30-Yr Freddie Mac Mortgage	6.55	6.23	6.11	6.09	6.07	6.06	6.06	6.05	6.72	6.60	6.08	

Forecast as of: February 4, 2026. Sources: U.S. Bank Economics, Moody's Analytics, and Bloomberg.

1. Projections for real GDP are quarter-on-quarter percent change at annual rate. Projections for housing starts in millions, annualized. Projections for the unemployment rate represent quarterly/annual averages.

2. Projections for the CPI, GDP Deflator, and Core PCE are year-over-year percent change.

3. Interest rate projections represent quarterly/annual averages, and are the views of the U.S. Bank Economics Group.



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