

U.S. ECONOMIC OUTLOOK

# Mostly unchanged despite shutdown fog

- **Summary:** Our November 2025 U.S. economic outlook highlights the growing economic toll of the federal government shutdown. Fortunately, Congress may be nearing an agreement. Until then, however, the absence of key data clouds visibility, while direct and indirect costs continue to mount. Despite resilient consumer spending and a stable, if fragile, labor market, downside risks remain heightened. Inflation remains elevated, the Fed is shifting toward neutral, and sector-specific vulnerabilities are emerging. The path forward hinges on resolving fiscal gridlock and restoring confidence.
- **Growth:** Economic activity remains broadly intact, supported by resilient consumer spending and stable business investment. Our Q3 GDP tracking estimate sits at 2.9% (quarter-over-quarter, annualized), up from 1.6% on average in the first half amid tariff-driven swings in trade and inventories. Despite limited data updates due to the shutdown, we expect 2025 growth to remain at 1.9%. As uncertainty fades and fiscal support builds, we still anticipate modest but sustained expansion, with our 2026 forecast revised up to 1.8%.
- **Labor market:** Conditions remain stable but increasingly fragile. Hiring has slowed, layoffs remain low, and the unemployment rate was at 4.3% in August. We expect it to rise to 4.5% by year-end and remain elevated through mid-2026. Shocks to both labor supply (immigration restrictions) and demand (tariffs, AI, DOGE) have reduced market dynamism. With job creation running at or below breakeven, even modest disruptions could push unemployment higher and test the soft-landing narrative.
- **Inflation:** Price pressures remain elevated. Tariff-related inflation persists, particularly in goods, while non-housing services remain firm. We estimate core PCE inflation at 2.8% year-over-year, with underlying trends closer to 2.3–2.4%, excluding tariffs. Our baseline has core PCE peaking near 3.2% in early 2026 before easing toward the Fed's 2% target.
- **Fed:** The Federal Reserve cut rates by another 25-basis points (bps) in October, bringing the policy rate just below 4% – a level closer to estimates of neutrality. Policymakers have signaled a shift toward a more balanced stance, citing softer labor demand and persistent inflation. We expect the Fed to continue aligning policy with a long-run neutral rate of 3.25% over the next year. This gradual adjustment reflects growing confidence in a soft landing, albeit risks remain.
- **Risks:** The risk to our baseline outlook remains skewed to the downside (at 35% near-term recession probability), driven by the rapid change in policies across several dimensions: fiscal, immigration and trade – including the Supreme Court's review of presidential tariff authority. These factors will keep general uncertainty about the future path of economic activity elevated.

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U.S. Bank Economics Research Group November 2025 Macro forecast summary

	Actual 2024	Forecast 2025	Forecast 2026	Forecast 2027
Real GDP	2.8	1.9	1.8	2.0
Consumer Spending	2.9	2.5	1.7	2.0
Investment	3.0	2.1	1.4	2.7
Housing Starts	1.37	1.36	1.36	1.39
Unemployment Rate	4.0	4.3	4.5	4.4
Consumer Price Index	3.0	2.8	3.0	2.2
Core PCE Price Index	2.9	2.9	2.9	2.1
Federal Funds (Upper Target)	5.3	4.4	3.6	3.2

Forecast as of November 3, 2025. Sources: U.S. Bank Economics, Moody's Analytics, and Bloomberg. 1. Projections for real GDP are annual percent change. Projections for housing starts 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 Research Group.

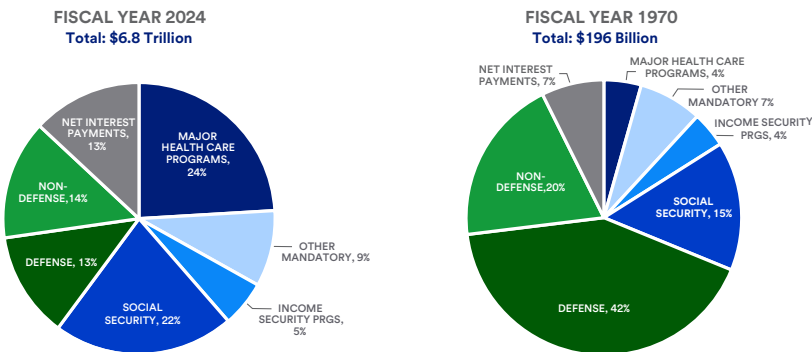
From the desk of the Chief Economist:  
Government debt: mind the gap

As lawmakers remain at an impasse, the government shutdown – now the longest in U.S. history – continues. If the compromise wins approval, our estimates suggest it has shaved about 0.7% off Q4 GDP growth. Indirect costs, such as postponed or cancelled contract work and vacations, make it worse. While some of that loss may be recouped later in Q4 and Q1 as delayed contracts and vacations resume, productivity lost from furloughed workers is gone for good. The compromise ensures backpay and an unwind of some federal layoffs, but it’s not a done deal. The impact could be worse if workers are denied backpay or laid off, as the White House has warned. Compounding the issue, the Fed has lacked critical economic data to guide interest rate decisions. With its dual mandate – price stability and maximum employment – under strain for the first time since the Volcker era, the risk of a policy misstep is rising.

The shutdown, driven by disputes over Affordable Care Act (ACA) premium tax credits, obscures a larger concern: the unsustainable trajectory of U.S. government debt. Historically, the U.S. has benefitted from its status as the world’s reserve currency, allowing it to carry higher debt levels. But with federal debt now at 100% of GDP and projected to reach 123% by 2034 (per CBO estimates factoring in the 2025 “One Big Beautiful Bill Act”), questions about fiscal limits are mounting. That legislation alone adds \$3.4 trillion to the primary deficit through 2024 – \$4.1 trillion when interest costs are included.

Finding room in the budget is increasingly difficult. Mandatory spending – Medicare, Social Security, military pensions – now consumes 55% of federal outlays, up from 26% in 1970. Defense spending is politically untouchable amid global tensions. Non-defense discretionary spending has shrunk from 20% to just 14%. And interest payments alone now account for 13% of spending, double the share in 1970.

U.S. Federal Government spending – Share of total



Source: U.S. Bank Economics Research Group calculations, CBO

Yet the U.S. is not alone. Government debt is rising globally. Japan leads with debt at 134% of GDP, with other trading partners close behind. The common driver? Aging populations. In the U.S., those over 65 made up 13% of the population in 2010; by 2050, that figure will reach 22%. Japan's elderly share will grow from 23% to 36% over the same period. As lifespans increase, so do costs for retirement and healthcare. Medicare and Social Security already account for 46% of U.S. federal spending – and that will rise.

Attempts to curb these costs have largely failed. Raising the retirement age has seen limited success. Although the full retirement age is officially 67 for those born after 1960, average life expectancy now exceeds 80, meaning retirees still draw benefits for over a decade. Proposals to switch to a chained CPI for cost-of-living adjustments, raise the Social Security wage cap (currently \$176,100), or reform immigration to boost taxable income have all stalled.

Bottom line: While a resolution to reopen the government may come soon, the deeper fiscal challenges remain unresolved – and increasingly urgent.

[Read the earlier commentary here >](#)

### **Gone furlough: the price of political stalemate**

The longest federal government shutdown U.S. history has exerted a growing drag on economic activity. The impasse stems from a political standoff over expiring health insurance subsidies and demands for a stopgap funding bill, leaving negotiations stalled and many agencies shuttered. Beyond the political brinksmanship, the absence of key economic data – such as employment and inflation reports – has compounded uncertainty for businesses, investors and policymakers. This data blackout limits visibility into current economic conditions and complicates decision-making.

The economic costs of the shutdown are both direct and indirect. Directly, the furlough of roughly 650,000 federal employees is estimated to reduce GDP by over 0.1 percentage points per week. Indirect effects – including delayed federal contracts, suspended public services and disruptions to tourism at national parks and monuments – pushed the total to around 0.2 percentage points per week if the shutdown persists and spillover effects intensify. While some lost output may be recovered once operations resume, productivity lost during the shutdown is permanent.

Broader risks are beginning to emerge. Thus far, financial markets have shown limited signs of risk aversion, and consumer confidence remains relatively stable. While less likely to happen given the Senate compromise, prolonged gridlock could erode sentiment and investment plans, particularly if uncertainty extends into December. Sector-specific vulnerabilities – such as housing, defense contracting and travel – are already evident. A tipping point could occur if businesses begin to adjust hiring or capital expenditure plans, amplifying the slowdown beyond what is typically a temporary setback.

Structural risks are also appearing. Prior to the shutdown, the White House directed agencies to prepare for potential Reduction in Force (RIF) notices for programs misaligned with administration priorities. That guidance led to over 4,000 federal workers being terminated within the first 10 days of the shutdown. However, a federal judge's order in late October halted further layoffs and prohibited new RIF notices for the duration of the shutdown. The Senate compromise, if approved, also will bring back some of those laid off workers. Still, the episode underscores the fragility of federal employment and the heightened risk of permanent displacement.

### **Consumers keep calm while jobs stand still**

The ongoing government shutdown has disrupted access to key federal data, including the October employment report originally scheduled for release on November 7. In its absence, we are relying on alternative indicators – such as state level unemployment claims, the Beige Book and private-sector surveys – to assess labor market conditions. These sources suggest that while momentum remains intact, it is fragile.

We do not see evidence of accelerating weakness in the labor market. October's ADP report showed a modest gain of 42,000 private sector jobs, marking the first increase since July. Hiring was concentrated among large firms and in sectors such as trade, transportation and education, while small businesses and more cyclical industries continued to shed jobs. Here, the overall picture remains one of stability – neither robust nor deteriorating.

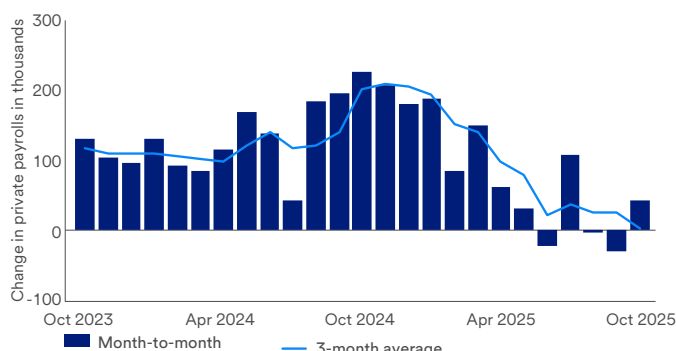
Labor market dynamics continue to reflect a delicate equilibrium. A slowdown in the supply of new workers – driven primarily by declining immigration and, to a lesser extent, lower labor force participation – has coincided with softening demand. This has resulted in subdued job

creation and a low job-finding rate for the unemployed, yet the unemployment rate remains low, holding at 4.3% in August with no clear signs of further deterioration since. The persistence of this balance suggests that the labor market is steady, but what Powell dubs “pretty curious.”

Stability at low levels of hiring leaves little cushion against adverse shocks. The current equilibrium depends on layoffs remaining subdued – a firewall that could prove thin. Even a modest rise in separations could push unemployment higher, particularly if displaced workers face prolonged job searches. We continue to expect a soft landing, supported by stable layoffs, moderating wage pressures and watchful monetary policy. But the labor market’s lack of dynamism limits its ability to absorb disruptions. If the Senate compromise is not approved, a prolonged government shutdown or a broader confidence shock could tip the balance, and the absence of comprehensive federal employment data increases the risk of delayed recognition of deterioration.

On the consumer side, spending remains healthy, particularly among higher income households. Our U.S. Bank Economics U.S. Consumer Card Transactions indicator continues to show growth. And the Conference Board’s October survey revealed a rebound in consumer intentions to purchase big ticket items, including used cars and major appliances, while vacation plans reached their highest level since January. However, the divergence by income is notable: confidence fell among lower income households but rose sharply among those earning over \$200,000, who continue to drive aggregate spending growth.

### U.S. Labor market



Source: U.S. Bank Economics; Automatic Data Processing, Inc.

### Inflation: the price is mostly right (unless you count tariffs)

Inflation pressures remain elevated. Despite delays caused by the extended federal government shutdown, the September Consumer Price Index (CPI) report was ultimately released – with an exception made due to its critical role in determining the annual cost-of-living adjustment (COLA) for Social Security recipients. Headline inflation moderated, but core CPI rose at a 3.6% annualized rate over the prior three months (3.0% year-over-year), still well above the Fed’s 2% target. Housing inflation is cooling, but goods prices remain elevated, driven in part by tariffs. Non-housing services inflation also continues to run firm, suggesting that while some price pressures are easing, others remain stubbornly persistent.

The September Producer Price Index (PPI) was not published, leaving a gap in translating CPI trends into the Fed’s preferred inflation gauge – the core PCE price index. Based on CPI data alone, we estimate that core PCE rose 2.8% year-over-year through September. Excluding the effects of tariffs, we believe inflation may be closer to 2.3–2.4%, indicating that underlying inflation – though still above target – is not dramatically far from the Fed’s goal. As Chair Jerome Powell recently noted, and we agree, once the full impact of tariffs is absorbed, their inflationary effect is likely to fade, resulting in a one-time price level adjustment rather than a sustained inflation impulse. Looking ahead, we expect year-over-year core PCE inflation to rise another three or four tenths into early 2026 – peaking around 3.2% – before gradually returning to the non-tariff inflation trend, which is already hovering not far from 2%.

### U.S. Inflation



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

**Neutral ground: where Fed policy meets the future**

Interest rates are beginning to reflect a shift toward a more neutral policy stance. With the 25-basis point cut at the October Federal Open Market Committee (FOMC) meeting, the Fed's overnight rate now sits just under 4% – within the range where most policymakers estimate the neutral rate to reside (typically between 3% and 4%, according to the latest 'dot plot'). Our view is that a nominal neutral rate of 3.25% makes sense over the long run, based on a real neutral rate ( $r^*$ ) of roughly 1.25% – a level consistent with model estimates from the New York Fed – and long-run inflation expectations anchored near 2%. In other words, when the economy is operating at its full potential and inflation is stable, a 3.25% fed funds rate should neither stimulate nor restrict growth.

This framework helps explain why the current 2-year Treasury yield, hovering near 3.60%, is broadly aligned with market expectations. One simple way to think about shorter term interest rates is through the lens of the term structure of policy expectations. The 2-year spot rate, for instance, reflects the market's estimate of the average fed funds rate over the next two years – currently around 3.4–3.5% – plus a modest term premium, which compensates investors for uncertainty around inflation, monetary policy and broader macroeconomic risks. Taken together, the current 2-year yield is consistent with a market that expects the Fed to gradually settle into a neutral stance.

The term premium is making a comeback – and it's reshaping the yield curve. For much of the past decade, the term premium – the extra yield investors demand for holding longer-term bonds – was near zero or even negative. That was largely due to subdued inflation, strong foreign demand for U.S. Treasuries, and aggressive Fed bond-buying. But that dynamic appears to be changing. Recent estimates place the 10-year term premium between 0.50% and 0.75%, likely reflecting growing concerns about inflation persistence, rising fiscal deficits, heavier Treasury issuance and reduced foreign appetite for U.S. debt.

Understanding the term premium is key to interpreting longer-term interest rates. Unlike short-term yields, which mostly reflect expectations for the Fed's policy rate, longer-term yields also embed compensation for uncertainty – about inflation, fiscal sustainability and geopolitical risks. We expect the 10-year term premium to continue to rise gradually. That

would imply a breakeven yield on the 10-year Treasury above 4% (based on a long-run expected policy rate of 3.25% plus a >0.75% average term premium). Therefore, with the current 10-year yield still near 4.10%, that seems to be adequately pricing long-term risks, particularly around inflation volatility and fiscal stress.

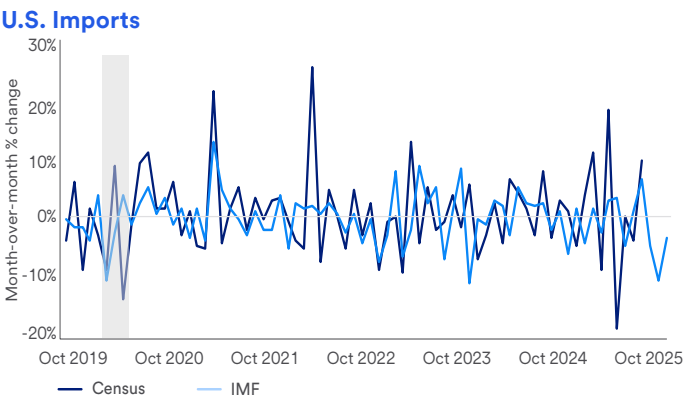
We expect the yield curve to steepen meaningfully over the next year. With the Fed moving toward neutral, the 2-year Treasury yield is likely to trend even lower – we think reaching 3.35% by the end of 2026. Meanwhile, the 10-year yield is expected to drift back up to around 4.30%. That would push the 2s-10s spread to nearly 100 basis points, up from the current 50 bps. While still below the steep curves seen in past expansions, this shift reflects a rebalancing of Fed expectations and a more realistic pricing of long-term risks.

**Trade update: tariffs, truces and tensions**

Trade policy remains a source of economic uncertainty, with recent developments offering both temporary relief and renewed friction. The U.S. maintained a high tariff regime on Chinese imports, with the effective rate hovering around 40% throughout October. President Trump threatened an additional 100% tariff on Chinese goods in response to China's export restrictions on rare earth minerals. However, a tentative trade agreement reached ahead of a summit with President Xi Jinping averted new tariffs and extended the existing trade truce through November 10. As part of the deal, China agreed to delay its rare earth export controls and increase purchases of U.S. agricultural products, including soybeans.

Despite this diplomatic progress, tariff uncertainty continues to contribute to inflationary pressures and supply chain disruptions – particularly in sectors reliant on global manufacturing. In a separate move, the administration announced a 10% tariff on Canadian imports, raising the total tariff on non-USMCA goods to 45%. This followed a dispute over an anti-tariff advertisement in Ontario referencing Ronald Reagan's trade views. Meanwhile, the U.S. and Mexico agreed to maintain current tariff levels while enhancing cooperation on supply chain security and trade facilitation, aiming to prevent further escalation. According to U.S. Census Bureau data from July 2025, Canada accounted for 12.5% of U.S. trade – second behind Mexico at 15.9% and ahead of China at 7.6%.

Although official government data was not available due to the shutdown, import volume indicators from the International Monetary Fund (IMF) suggest that businesses are beginning to slow their import activity – likely in response to rising costs and policy uncertainty. Legal uncertainty also looms, as the Supreme Court heard arguments this week on whether the International Emergency Economic Powers Act (IEEPA) authorizes the president to impose sweeping tariffs – potentially reshaping the future of U.S. trade policy.



Source: U.S. Bank Economics; IMF Port Monitor; Census Bureau

## U.S. Bank Economics Research Group November 2025 Macro forecast summary

	Actual		Forecast						Actual	Forecast	
	2025		2025		2026						
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	2024	2025	2026
<b>Economic Data<sup>1</sup></b>											
Nominal GDP	2.9	6.0	6.1	3.3	4.5	3.4	3.9	4.0	5.3	4.7	4.2
Real GDP	-0.6	3.8	2.9	0.8	1.6	1.8	1.8	1.9	2.8	1.9	1.8
Consumer Spending	0.6	2.5	3.2	0.8	1.3	1.6	1.8	2.0	2.9	2.5	1.7
Investment	23.3	-13.8	2.5	0.3	2.4	4.1	3.5	3.3	3.0	2.1	1.4
Residential Structures	-1.0	-5.1	-3.4	-1.0	0.2	1.0	2.5	2.5	3.2	-1.7	-0.2
Non-Residential Structures	-3.1	-7.5	-2.5	-2.0	0.7	2.2	2.2	2.2	1.1	-4.7	-0.2
Intellectual Property	6.5	15.0	5.0	3.0	2.0	2.5	2.5	2.8	3.5	5.4	3.5
Equipment	21.4	8.5	3.0	0.5	3.0	3.0	2.7	2.5	3.5	7.8	2.8
Change in Inventory	172.0	-18.3	-10.0	-15.4	-9.2	9.6	20.0	27.2	43.5	32.1	11.9
Government Spending	-1.0	-0.1	0.7	0.5	0.3	0.2	0.2	0.6	3.8	1.3	0.3
Federal	-5.6	-5.3	-2.9	-1.7	0.0	0.0	0.0	0.1	3.8	-0.8	-1.0
State & Local	1.9	3.1	3.0	1.8	0.5	0.3	0.3	0.9	3.8	2.7	1.2
Imports	38.0	-29.3	-0.5	-1.0	-1.0	0.6	2.0	3.0	5.8	3.2	-2.2
Exports	0.2	-1.8	-0.5	0.0	0.6	0.7	2.0	2.5	3.6	0.6	0.5
Housing Starts	1.40	1.35	1.34	1.35	1.35	1.36	1.36	1.37	1.37	1.36	1.36
Unemployment Rate	4.1	4.2	4.3	4.5	4.5	4.5	4.5	4.4	4.0	4.3	4.5
<b>Prices<sup>2</sup></b>											
Consumer Price Index	2.7	2.5	2.9	3.1	3.2	3.1	3.0	2.7	3.0	2.9	3.0
Core PCE Price Index	2.8	2.7	2.9	3.0	3.2	3.1	2.9	2.6	2.9	2.9	2.9
<b>Interest rates<sup>3</sup></b>											
Federal Funds (Upper Target)	4.5	4.5	4.5	4.0	3.7	3.7	3.5	3.4	5.3	4.4	3.6
2-Yr Treasury Note	4.1	3.9	3.7	3.5	3.5	3.4	3.4	3.4	4.4	3.8	3.4
10-Yr Treasury Note	4.5	4.4	4.3	4.1	4.2	4.2	4.3	4.3	4.2	4.3	4.2
30-Yr Freddie Mac Mortgage	6.8	6.8	6.6	6.2	6.2	6.1	6.1	6.1	6.7	6.6	6.1

Forecast as of: November 3, 2025. 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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