U.S. ECONOMIC OUTLOOK

Economy keeps on keeping on

Summary: Our November 2026 U.S. economic outlook continues to point to an economy with considerable underlying momentum, even as that strength has become more concentrated and costly. Domestic demand remains strong, supported by resilient consumer spending and robust AI-related business investment. At the same time, resilience is becoming less evenly distributed. Financially stronger households continue to spend, while higher price levels, weaker real purchasing-power growth, and thinner savings cushions create greater strain elsewhere. Likewise, inflation remains elevated, while persistently high long-term borrowing costs are raising financing costs across the economy.

Looking ahead, our baseline forecast continues to call for growth near its long-run potential pace, but its composition and cost have become more important. AI-related investment should remain a key driver, although its growing role also creates concentration risk. Consumer spending should benefit from low layoffs and continued income growth, but its durability will depend on household purchasing power. Meanwhile, the final stretch toward price stability is proving more complicated, with some inflation pressures less responsive to higher interest rates. We continue to expect two additional 25-basis-point Fed rate increases by early 2027, bringing the cumulative increase to 75 basis points since September. The challenge is no longer whether inflation warrants continued restraint, but how much additional tightening is appropriate when borrowing costs are already elevated and monetary policy may be less effective against the inflation that remains.

- **Growth:** Real GDP growth is forecast at 2.5% Q4-over-Q4 in 2026 (2.4% annual average) and 2.0% in 2027 (2.2% annual average). Momentum remains solid, supported by resilient consumers and robust business investment, although growth is increasingly concentrated around AI-related spending.
- **Labor market:** We expect unemployment to average 4.2% in both 2026 and 2027. Slower hiring should be offset by historically low layoffs and slower labor-force growth, keeping the labor market broadly stable and supportive of household income and spending.
- **Inflation:** The final stretch toward price stability is proving more complicated, as energy and other supply-related pressures offset improvement in some underlying components. We expect core personal consumption expenditures (PCE) inflation to average 3.2% year-over-year in Q4 2026 before moderating to 2.5% by the end of 2027, keeping inflation above the Fed's 2% objective for longer.
- **Federal Reserve:** Resilient demand and persistent inflation continue to argue for additional restraint. We expect 25-basis-point rate increases in December and March, bringing the federal funds rate to 4.25%–4.50%, with risks increasingly tilted toward a longer tightening cycle.
- **Risks:** We maintain a 25% probability of recession over the next 12 months. Persistent inflation, additional monetary tightening, and elevated borrowing costs remain key risks, while growing reliance on AI-related investment and financial-market strength leaves the economy increasingly exposed to a reversal in either.

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U.S. Bank Economic Research Group November 2026 Macro Forecast Summary

	Actual 2025	Forecast 2026	Forecast 2027	Forecast 2028
Real GDP	2.4	2.4	2.2	2.1
Consumer Spending	2.4	2.4	2.4	1.9
Investment	4.8	4.8	6.2	3.7
Housing Starts	1.34	1.34	1.35	1.37
Unemployment Rate	4.2	4.2	4.2	4.2
Consumer Price Index	3.5	3.5	3.2	2.3
Core PCE Price Index	3.1	3.1	2.7	2.2
Federal Funds (Upper Target)	3.8	3.8	4.4	4.5

Forecast as of: November 2, 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 Economic Research Group.

From the desk of the Chief Economist:
Who's really setting interest rates?

Fear of persistently high inflation has caused investors to demand more yield to hold longer duration. One big driver is the heavy Treasury issuance to finance persistent deficits. Large-scale AI investment is also drawing on the same pool of capital to a lesser degree, adding to overall financing demand.

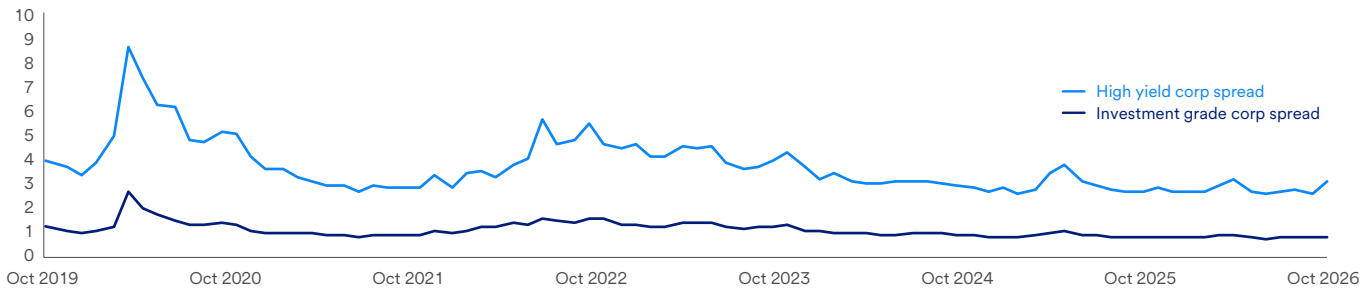
Because corporate borrowing costs are built on top of Treasury rates, higher government yields raise the cost of capital across the economy. So far, credit investors are not demanding extra compensation for holding corporate bonds over Treasuries. Default risk, refinancing risk, and liquidity risk are all still being priced benignly.

In theory, both forces could crowd out private borrowers and push corporate borrowing costs higher. In private credit markets, there are some signs of it (direct lending capital that might have gone to another option is increasingly being diverted to AI-related products). But private credit assets under management have grown fast enough to not yet produce visible stress for non-AI borrowers.

As of October 2026, high-yield option-adjusted spreads (OAS) were 323 basis points and investment-grade spreads were 84 basis points, both near post-Global Financial Crisis lows.

Bottom line: Government borrowing and AI investment have pushed up the absolute cost of capital, but not the relative cost of corporate borrowing. Corporate credit spreads remain near a historic low, despite Treasury rates lifting borrowing costs across the economy. While market-driven higher rates may support the Fed's quest to cool the economy this time, the Fed doesn't want the help.

Corporate spreads still near post-pandemic lows



Source: Bloomberg, U.S. Economic Research Group calculations

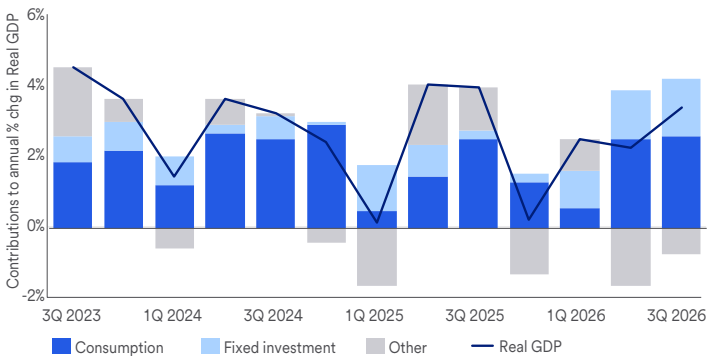
Read the full commentary here >

Growth: Strong beneath the headline, but increasingly investment-driven

The U.S. economy carried considerable momentum into the third quarter. Real GDP grew at a 3.4% annualized rate, up from 2.2% in the second quarter and leaving output 2.1% above a year earlier – roughly in line with its longer-run trend. More importantly, underlying domestic demand was even stronger. Real final sales to private domestic purchasers, a cleaner measure of demand from U.S. consumers and businesses, rose 4.9% following an already-strong 4.6% increase in the second quarter. Those back-to-back readings point to exceptionally strong domestic momentum despite elevated interest rates and persistent inflation.

Business investment has become an important source of that strength. Nonresidential investment rose 12.7% annualized in the third quarter, extending the strong gains recorded over the first half of the year, while rate-sensitive residential investment declined and has posted growth in just one quarter since 2024. The AI investment cycle is also extending beyond computing equipment and software into data centers, specialized industrial machinery, power generation, and grid infrastructure, with recent gains in capital-goods orders and manufacturing activity suggesting the benefits are spreading more broadly.

U.S. Economic Growth



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

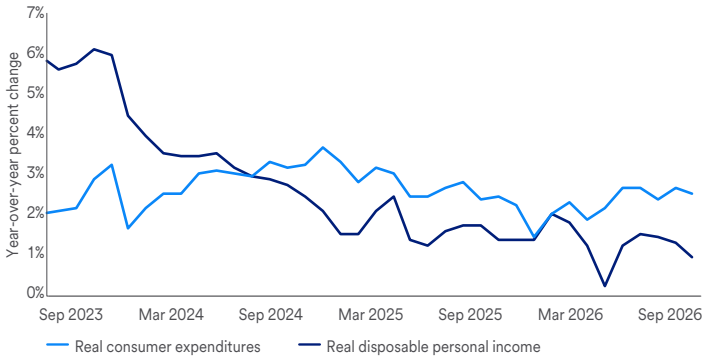
How broadly and durably those gains spread will be critical to the outlook. For now, much of the AI boom remains concentrated among a relatively small group of companies, magnifying its influence well beyond business investment. Rising earnings expectations have supported equity valuations and household wealth, creating a reinforcing cycle in which AI investment can bolster financial conditions and consumer spending. But that cycle works in both directions. Weaker expected returns, infrastructure constraints, or a meaningful market correction could simultaneously weigh on investment and household demand. AI is therefore becoming both a larger source of growth and a more consequential source of concentration risk. Going forward, with slower labor-force growth providing less support, sustaining the economy near its long-run potential pace will increasingly depend on whether AI-related investment delivers broader productivity gains.

Consumer: Resilient, but increasingly costly

Consumer spending remains a key source of economic resilience. Real consumption increased at a 3.8% annualized rate in the third quarter, matching the strong second-quarter pace despite elevated energy prices and borrowing costs. These back-to-back gains have helped drive the economy's stronger-than-expected performance this year, although that pace of spending growth is unlikely to be sustained.

September, however, offered a less comfortable picture of the consumer's underlying position. Nominal spending continued to rise, but higher prices absorbed those gains, leaving real consumption essentially unchanged. At the same time, real disposable income declined and the saving rate slipped below 4% as households continued to spend faster than their incomes grew. The figures do not yet signal a broad pullback, but they suggest households entered the fourth quarter with less purchasing-power momentum and thinner cushions against continued price pressures.

U.S. Personal Income and Spending



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

Stable employment and rising household wealth help explain why spending has remained resilient. Layoffs remain historically low and unemployment continues to hover near 4.2%, preserving income security even as hiring has cooled. Moreover, financial-market gains have provided an additional

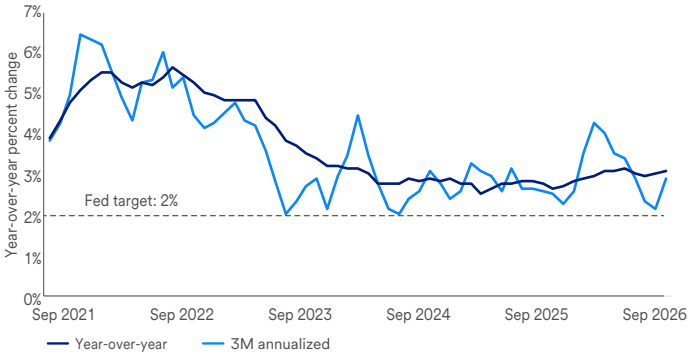
source of spending capacity not captured in income measures – which helps explain why expenditures have run hotter than income gains without a commensurate increase in debt – although that support is unevenly distributed. Higher-income households generally have greater exposure to appreciating financial assets and more capacity to absorb elevated prices and borrowing costs, while lower-income households remain more vulnerable to essential expenses and high-cost credit.

We maintain a constructive outlook for consumer spending but expect growth to moderate toward a trend-like pace of roughly 2% through 2027. A stable labor market should continue to support household income, while elevated borrowing costs, higher energy prices, and reduced saving capacity limit the scope for another extended period of above-trend consumption. Household purchasing power is therefore becoming the key test of consumer durability, with continued spending growth increasingly dependent on whether income can keep pace with prices without requiring further declines in saving or continued appreciation in financial assets.

Inflation & interest rates: A more complicated final mile

Progress toward price stability became more uneven at the end of the third quarter. Headline PCE inflation rose 0.5% month-over-month in September and 3.6% from a year earlier, reflecting the continued effects of elevated energy prices. Core PCE inflation also increased 0.3% over the month and edged up to 3.1% from a year ago, with price pressures extending across both goods and services. Although the September increase does not necessarily mark a renewed inflationary surge, it reinforces that the path back to the Federal Reserve's 2% objective is unlikely to be smooth or rapid.

U.S. Inflation

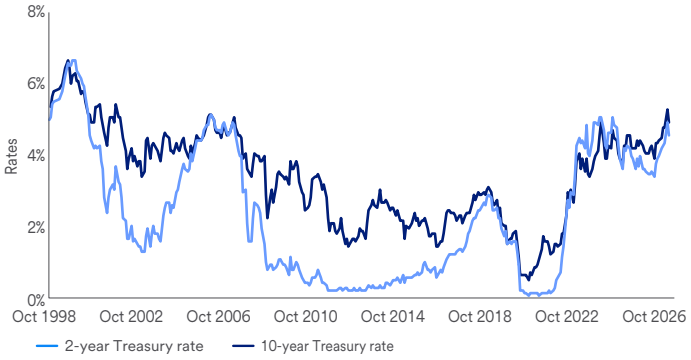


Source: U.S. Bank Economics, U.S. Bureau of Economic Analysis (BEA), Bloomberg

The composition of inflation has also become more complicated. Higher energy and transportation costs are beginning to pass through supply chains and into selected consumer prices, while strong demand gives businesses more room to pass along those increases. At the same time, some of the forces that drove the earlier inflation cycle continue to improve. Wage growth has moderated, housing price pressures have generally eased, and longer-run inflation expectations remain comparatively stable. Trimmed-mean measures, which strip out the largest price increases and declines, also suggest underlying inflation remains less pronounced than the headline core PCE reading implies. Together, these trends suggest inflation should continue to moderate, but energy, goods, and other supply-related pressures are likely to make the final stretch toward price stability slower and less predictable.

A slower and less predictable path back to price stability is also contributing to a broader repricing of long-term interest rates. The 10-year Treasury yield recently reached levels last seen in the early 2000s, but the increase reflects more than elevated inflation or expectations for additional Fed tightening. Higher real rates and term premiums suggest investors are demanding greater compensation for holding longer-duration securities amid heavy Treasury borrowing, fiscal uncertainty, and inflation risk. Strong economic growth and substantial private capital demand, including investment in AI and energy infrastructure, are adding further pressure. In our view, long-term borrowing costs may therefore remain elevated even as inflation gradually improves and the Fed approaches the end of its tightening cycle.

U.S. Treasury Rates



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

The result is a higher and increasingly consequential cost of capital across the economy. Elevated Treasury yields flow through to mortgage rates and corporate borrowing costs, making some investments less attractive even without another increase in the Fed's policy rate. The effects are also uneven. Housing and other rate-sensitive sectors are already under considerable pressure, while AI-related and other strategically important investments continue to move forward because expected returns remain high. Sticky inflation and a higher term premium are therefore putting a higher floor under borrowing costs, making financing conditions an increasingly important constraint on households, businesses, and the broader outlook.

Federal Reserve: Restrictive for longer, but how much tighter?

The Federal Reserve paused at its October meeting, leaving the federal funds rate unchanged at 3.75%–4.00% following September's 25-basis-point increase. Yet the decision did little to suggest the inflation fight is over. The Federal Open Market Committee (FOMC) upgraded its assessment of economic activity from expanding at a 'solid' pace to a 'strong' pace, while continuing to characterize inflation as elevated and labor-market conditions as stable. The 10–2 vote also revealed support for moving more quickly, with Governor Cook and Cleveland President Hammack favoring another quarter-point increase. Importantly, Fed Chair Warsh characterized the pause as an opportunity to gather more information rather than a retreat from the Fed's price-stability objective, suggesting the decision was more about the timing than the direction of policy.

The challenge is that persistent strong growth gives the Fed room to tighten but does not necessarily establish the need for an aggressive cycle. Robust capital investment and productivity growth may be expanding the economy's capacity, allowing activity to remain firm without creating a high degree of inflation pressure. Wage growth has also moderated, while energy and other supply-related forces account for more of the inflation that remains. Those pressures cannot be resolved directly through a higher policy rate, although the Fed must prevent them from spreading into expectations and broader pricing behavior. At the same time, elevated long-term borrowing costs and tighter credit conditions are already delivering additional restraint. The question is therefore not whether inflation warrants continued restraint, but how much additional tightening is appropriate and how effective it will be against the inflation that remains.

We continue to expect additional 25-basis-point increases in December 2026 and March 2027, bringing the federal funds rate to a peak range of 4.25%–4.50%. The risks around that forecast are increasingly tilted toward additional tightening. If economic activity continues to absorb higher borrowing costs while inflation fails to make meaningful progress toward 2%, policymakers may conclude that a higher policy rate is necessary to prevent persistent supply shocks from becoming embedded in broader prices and expectations. For now, however, the Fed appears likely to move gradually, allowing time to assess the cumulative effects of higher short- and long-term rates while keeping further tightening on the table if inflation remains stubborn.

U.S. Bank Economic Research Group November 2026 Macro forecast summary

	Actual			Forecast					Actual	Forecast		
	2026				2027							
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	2025	2026	2027	2028
Economic Data[1]												
Nominal GDP	5.8	8.5	5.6	5.8	4.8	4.7	4.5	4.4	5.0	6.1	5.2	4.3
Real GDP	2.5	2.2	3.4	2.1	1.9	2.1	2.0	2.0	2.3	2.4	2.2	2.1
Consumer Spending	0.7	3.8	3.8	2.3	1.9	2.0	1.9	1.9	2.6	2.4	2.4	1.9
Investment	7.2	4.6	19.4	6.5	4.3	3.5	3.6	3.7	3.1	4.8	6.2	3.7
Residential Structures	-7.6	2.8	-3.3	0.0	0.3	0.8	1.9	1.8	-2.7	-3.3	0.3	1.9
Non-Residential Structures	-9.4	0.1	5.4	1.5	1.7	2.0	2.0	2.0	-2.2	-4.9	2.1	2.0
Intellectual Property	15.6	9.2	7.0	6.5	5.0	5.0	4.8	4.7	6.8	9.5	5.9	4.5
Equipment	15.5	13.4	20.9	8.9	6.0	4.3	4.0	4.0	8.8	12.4	8.0	3.6
Change in Inventory	-35	-63	20	29	30	27	25	25	7	-12	27	34
Government Spending	4.7	-0.1	5.3	0.9	0.8	1.6	1.3	1.0	1.6	1.1	1.5	1.1
Federal	10.9	-2.4	15.8	1.7	0.8	2.9	2.0	1.4	-1.3	0.9	3.1	1.7
State & Local	1.4	1.2	-0.1	0.5	0.7	0.8	0.8	0.8	3.3	1.2	0.6	0.8
Imports	11.5	12.6	19.7	8.2	4.0	3.0	3.0	3.0	3.6	5.5	6.7	3.0
Exports	13.9	5.0	-5.7	3.5	2.0	2.5	2.7	3.0	2.1	3.9	1.7	3.2
Housing Starts	1.42	1.35	1.29	1.32	1.34	1.35	1.36	1.37	1.36	1.34	1.35	1.37
Unemployment Rate	4.3	4.3	4.1	4.2	4.2	4.3	4.3	4.2	4.3	4.2	4.2	4.2
Prices[2]												
Consumer Price Index	2.7	3.8	3.5	4.0	3.9	3.1	3.3	2.7	2.7	3.5	3.2	2.3
Core PCE Price Index	3.0	3.1	3.1	3.2	2.9	2.7	2.7	2.5	2.8	3.1	2.7	2.2
Interest rates[3]												
Federal Funds (Upper Target)	3.75	3.75	3.79	4.06	4.28	4.50	4.50	4.50	4.37	3.84	4.44	4.51
2-Yr Treasury Note	3.58	3.97	4.36	4.69	4.62	4.61	4.60	4.60	3.81	4.15	4.61	4.60
10-Yr Treasury Note	4.20	4.42	4.76	5.04	4.99	5.00	5.00	5.00	4.29	4.60	5.00	5.00
30-Yr Freddie Mac Mortgage	6.11	6.42	6.69	7.11	6.84	6.78	6.76	6.75	6.60	6.58	6.78	6.75

Forecast as of November 2, 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 Economic Research Group.



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