Second Quarter GDP Growth Slowed but Underlying Details Are Positive

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Headlines

- **Real GDP increased an annualized 1.5% in the second quarter in the initial print – down from 2.1% in the first quarter.**
- Investment, consumer spending, and exports were the main growth drivers, while government spending and imports weighed on growth.
- The PCE Price Index rose 5.1% in the second quarter, up from 4.6% in the first quarter. The core PCE Price Index, excluding food and energy, slowed to 3.4% from 4.4% in the previous quarter.
- **PNC's baseline forecast is for real GDP growth to remain near 2.0% in the second half of the year.**
- PNC expects the Federal Open Market Committee (FOMC) to hold the fed funds rate steady in the current range of 3.50%-3.75% into 2027.

Details

Economic growth slowed in the second quarter. Real GDP climbed an annualized 1.5% according to the initial estimate from the BEA (Figure 1), down from 2.1% in the first quarter. This was below PNC's forecast for an acceleration to 2.3%. Real GDP is up 2.1% from a year earlier, down from 2.7% in the first quarter (Figure 2).

Consumer spending accelerated sharply in the second quarter and contributed 2.12% to second quarter growth – up from 0.37% in the first quarter – with contributions of 1.08% from goods spending (up from 0.11%) and 1.04% from services spending (up from 0.26%).

Gross private domestic investment spending contributed 0.53% to second quarter growth, down from 1.35% in the second estimate. Fixed investment spending contributed 1.20% with nonresidential spending adding 1.15% and residential spending contributed 0.05%, the first positive contribution since the first quarter of 2024. Within the nonresidential fixed investment spending category, the three AI-related spending categories (information processing equipment, software, and research & development) contributed 0.67% to growth, down sharply from 1.50% in the first quarter and 0.97% in the fourth quarter of 2025.

Inventories reduced second quarter growth by 0.67% after boosting growth in the first quarter and last quarter of 2025. Net exports subtracted 1.01% from growth – the third consecutive decline – while government spending subtracted 0.14%. Federal

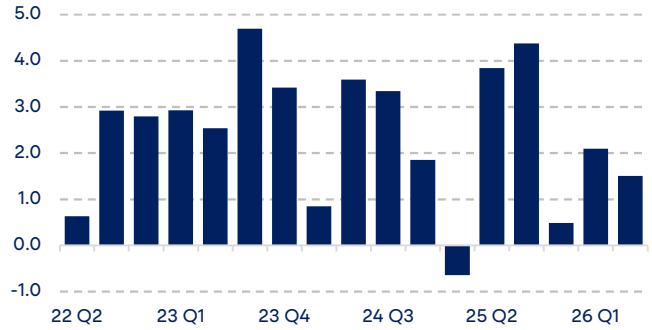
spending subtracted 0.26%, primarily reflecting nondefense consumption expenditures, specifically sales from the Strategic Petroleum Reserve which are deducted from government consumption and subtracted roughly 40 bps from headline growth. State and local spending lifted growth by 0.12%, down slightly from 0.17% in the previous quarter. Contributions from inventories and net exports have been volatile due to the various tariff regimes introduced by the Trump administration.

Final sales to private domestic purchasers – which excludes net exports, inventories and government spending and is a good measure of underlying demand – surged at a 3.9% annualized rate in the second quarter, more than double the 1.7% pace in the first quarter.

While topline real GDP growth unexpectedly cooled in the second quarter, it was partially due to federal government sales from the Strategic Petroleum Reserve which are subtracted from government expenditures. Notably, consumer spending growth accelerated to an annualized rate of 3.2% from just 0.5% in the first quarter. That was the strongest pace since the third quarter of 2025.

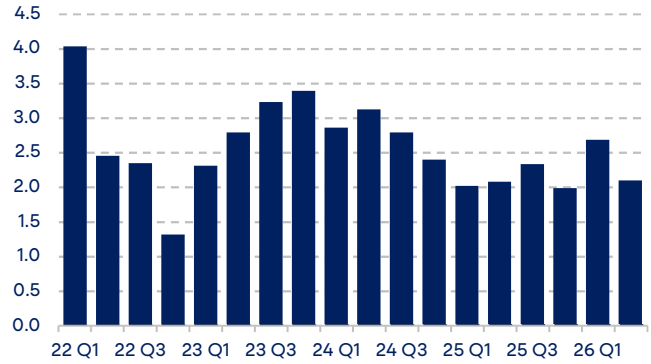
PNC's baseline forecast is for real GDP growth to remain near 2.0% in the second half of the year, partially due to a slowdown in consumer spending. Despite the second-half weakness, PNC expects the FOMC to hold the fed funds rate steady into 2027 amid still high inflation and elevated uncertainty with the conflict in the Middle East flaring up again.

Figure 1: Real GDP growth (% chg., q/q, SAAR)



Sources: BEA, PNC

Figure 2: Real GDP growth (% chg., y/y)



Sources: BEA, PNC

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