National Economic Outlook

September 2026

Headlines

- **Growth looks to have accelerated in the third quarter**, with strong spending growth and continued strength in business investment. Our preferred measure of "core" GDP is likely to have averaged 4.5% over the past two quarters, a more rapid pace of growth than 80% of two-quarter stretches since 1990.

- **The labor market is somewhere between stable and reaccelerating.** Job growth has averaged 71k over the past three months and the unemployment rate is 4.1% down from a peak of 4.5% last year. We're seeing early signs that wage growth may be picking up again, which could make it more difficult for the Fed to reduce inflation without raising rates.

- **Inflation is still too high, and the Fed has lost patience with waiting for it to return to target on its own**. Inflation is likely to look modestly better through the remainder of 2026 than it did earlier in the year, but the run-up in gas and diesel prices in recent months will make it difficult for the Fed to see the progress it needs anytime soon.

- Despite a solid economy, **affordability remains a major challenge** for many households as home prices, mortgage rates, vehicle costs, and borrowing costs have risen sharply since the pandemic. While this has not been enough to derail consumer spending, it helps explain why consumer sentiment remains so weak.

- **How much is AI boosting measured GDP growth**? We estimate the direct and indirect effects of AI-related capital spending and wealth effects are currently adding around 65 bps to annual real GDP growth.

- **Overall we expect real GDP growth of 2.4% in 2026** and the unemployment rate to stay near current levels. We think the Fed will hike twice more, once in December and again in March, but stress risks remain tilted to more, not fewer, hikes.

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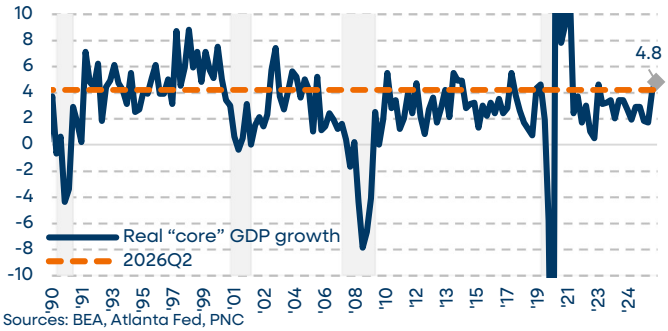
Growth accelerated in the middle of 2026

For now, the U.S. economy has largely shrugged off higher energy prices from the conflict with Iran and rising long-term interest rates, even appearing to accelerate through the second and third quarters of 2026. Q2 real GDP growth was revised up to 2.2% annualized, and the available data suggests Q3 growth should come in above 3%. Large swings in inventories and trade may obscure the true underlying trend in economic growth, which we believe is even stronger.

Our preferred measure of "core" GDP, which consists of consumer spending and non-inventory-related investment, is likely to have averaged 4.5% annualized over the past two quarters. That would be a faster pace of growth than 80% of two-quarter periods since 1990.

Figure 1: Core Real GDP (% chg., q/q annualized)



Sources: BEA, Atlanta Fed, PNC
Note: Note: Real "core" GDP is real personal consumption expenditures (PCE) plus private fixed investment. 2026Q3 is an Atlanta Fed GDPNow estimate; values capped at ±10%.

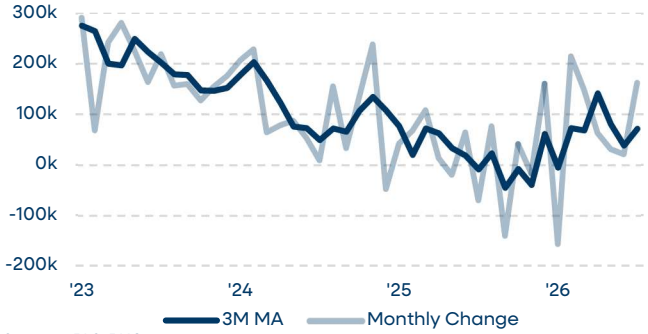
We are witnessing one of the largest capex booms of our lifetimes, while consumer balance sheets remain considerably healthier than most people give them credit for. That has been more than enough to keep the economy resilient in the face of rising interest rates, an energy price shock, a large tariff shock, and years of above-target inflation, and is likely enough to keep growth resilient in the near term.

We do expect growth to slow somewhat over the coming quarters as it moves closer to its underlying potential, but it will take time for the impact of higher rates to feed through to consumers and businesses. We expect Real GDP growth of 1.9% in 2027.

Labor market somewhere between stable and reaccelerating

Job growth rebounded in 2026 after coming to a stall last year, averaging 71k jobs added over the past three months. Given that labor force growth has slowed dramatically due to slowing net immigration and an aging population, this has been enough to drive the unemployment rate down to 4.1% from a peak of 4.5% last year.

Figure 2: Nonfarm payroll job growth



Sources: BLS, PNC

While it's probably not appropriate to call the labor market a source of inflation just yet, it has been trending in that direction, which has the Fed's attention. At a minimum, we don't think the Fed needs to worry about the labor market buckling in response to the rate hikes it is undertaking. However, at the other extreme, it is possible the Fed may need to hike further to prevent the labor market from becoming a source of inflation. Year-over-year growth in average hourly earning was just 3.1% in August, the slowest pace (outside of pandemic-caused distortions) since before the pandemic.

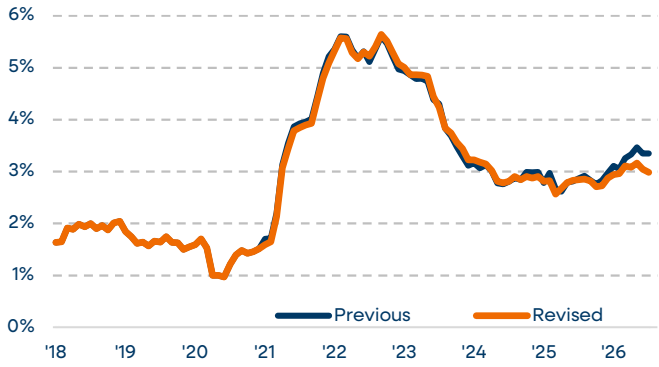
Inflation too high, Fed has lost patience waiting

Core PCE inflation increased 0.247% in August, which would translate to a 3.0% annualized pace if

sustained over the next twelve months. While inflation has clearly improved over the past three months from the torrid pace seen at the start of the year, it remains stuck well above the Fed's 2% objective, and we think whether the Fed raises the federal funds rate or not in October will come down to the September inflation print. Our baseline expectation remains that the Fed hikes twice more, 25 basis points each in December and again in March. This would leave the fed funds rate in a range of 4.25% to 4.50% by early spring, but risks remain tilted toward more, not fewer, hikes.

The August PCE release also included methodological revisions to a number of PCE components, which resulted in roughly a 30bp decline in the year-over-year inflation rate. This was primarily due to a reduction in the direct passthrough of equity price and home price changes into measured consumer inflation. Overall we expect "core" PCE inflation to end the year at 3.0% and to continue slowing through 2027.

Figure 3: Core PCE inflation (y/y % chg.)



Sources: BEA, PNC

Affordability isn't just inflation

Since the start of the pandemic in 2020, consumer prices have increased a cumulative 28%, according to the CPI, an average annual inflation rate of 4.3%. For many households, this is the first extended period of elevated inflation they have experienced. Not surprisingly, affordability has become a major political and economic issue.

Yet affordability concerns extend beyond the government's inflation measures. While the CPI is designed to track the cost of living, some of its methods may not fully capture the experience of consumers, particularly prospective homebuyers. Housing accounts for roughly one-quarter of the CPI, but the Bureau of Labor Statistics measures homeowner costs using "owners' equivalent rent" (OER), an estimate of what homeowners would pay to rent their own homes. While appropriate for measuring inflation, OER does not reflect the challenge of buying a home in today's market.

Figure 4: Housing affordability index (lower = less affordable)

Sources: NAR, PNC

Since early 2020, OER has risen 34%, but the median price of an existing single-family home has increased 49%, according to the National Association of Realtors. At the same time, the typical 30-year fixed mortgage rate has risen from below 3% to above 7%. As a result, housing affordability remains well below its long-run average despite some recent improvement.

A similar story exists in the auto market. New vehicle prices in the CPI are up 21% since the pandemic, but average monthly loan payments have risen 43% to $770 because of higher vehicle prices and borrowing costs.

There may be some relief coming on affordability, but in the near term the cost of living will continue to stress households. The Federal Reserve is committed to getting inflation under control, part of its task from Congress, although that process takes time. And the 21st Century ROAD to Housing Act took

effect over the summer; it has provisions designed to make homebuying more affordable, including efforts to increase the supply of new home construction, expand access to mortgages, and restrict home purchases by big investors. But it will take years before households start to feel better about affordability.

Figure 5: Average new vehicle loan payment ($)

Sources: Cox Automotive, Moody's Analytics, PNC

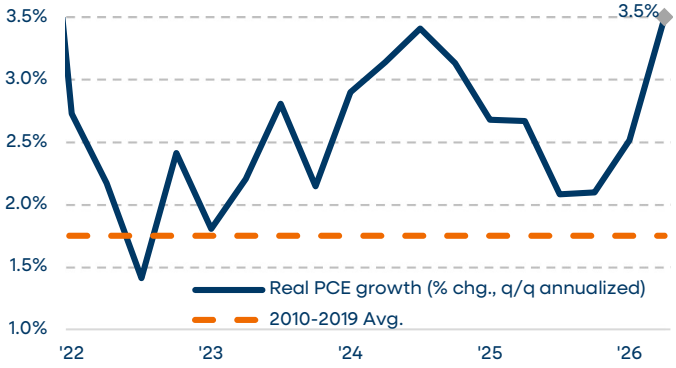
AI wealth gains power consumer spending – not 'dissaving'

A notable theme in recent years has been the resilience of consumer spending, despite slower income and job growth and negative shocks, such as tariffs and higher energy prices, weighing on sentiment and household purchasing power. Although we may still be waiting for the ultimate productivity payoff from the AI investment boom, its effects on household wealth, and as a result spending, are already visible.

Using standard estimates of the passthrough from equity wealth to consumption, we estimate that AI-driven wealth gains contributed an average of 24 bps to real GDP growth through stronger consumer spending in the first half of 2026, with a substantially larger contribution likely in the pipeline for the third quarter as earlier equity gains continue to pass through.

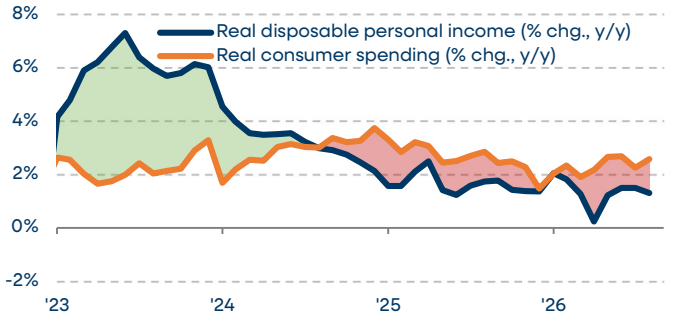
We expect wealth effects to provide a floor under consumption in the year ahead. We also find that AI-linked stocks have become relatively insensitive to hawkish monetary-policy surprises, suggesting that monetary-policy tightening could have a difficult time cooling aggregate demand; this could raise the risk of the Fed overtightening.

Figure 6: Consumption growth remains above its pre-pandemic average and is picking up



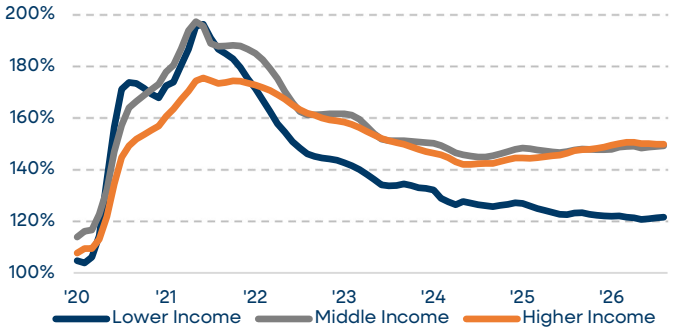
Sources: BEA, Atlanta Fed, PNC
Note: 2026Q3 is an Atlanta Fed GDPNow estimate.

Figure 7: Consumer spending growth has increasingly outpaced income growth



Sources: BEA, PNC
Note: Green shading indicates periods when income growth exceeded spending growth, while red shading indicates the opposite.

Figure 8: Median inflation-adjusted checking and savings deposit balances as a % of '19 levels (3M MA)

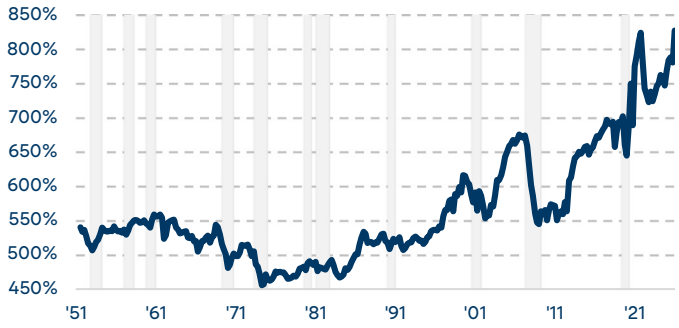


Source: PNC internal data
Note: Chart shows data seasonally adjusted by PNC and deflated using total consumer price index, 3-month moving average (3M MA).

Since mid-2024, consumer spending growth has been running ahead of personal income growth, and that differential has only widened. A standard explanation for what has sustained this spending is that households are spending down, or have already spent down, their pandemic-era buffers. We find limited support for this in PNC's internal data. Households have whittled down some of their pandemic-era liquid savings, but these buffers remain robust and have long since stopped declining. One positive is that there was a recent upward revision to the personal saving rate, indicating that households have not been running down their savings by as much as originally reported.

If not 'dissaving,' then what explains the resilience of both consumption and households' savings buffers? We find more credible support for households benefiting from rising equity prices and monetizing some of those gains to support consumption growth. A key reason equity prices have increased so much is enthusiasm around AI and expectations for significant future revenues from firms making AI investments. Household net worth has reached a record high of 830% of disposable income. At the same time, the market capitalization of publicly traded AI-linked stocks has reached 100% of GDP, up from 35% in 2022Q4, the quarter of ChatGPT's launch. In PNC's internal data, we also find that customers, particularly those in or approaching retirement, pulling increasing amounts of money from their brokerage accounts to support spending.

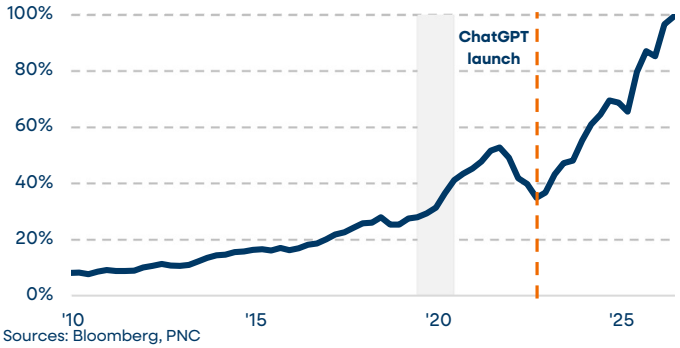
Figure 9: Household net worth (% of DPI)



Sources: Federal Reserve Board, PNC

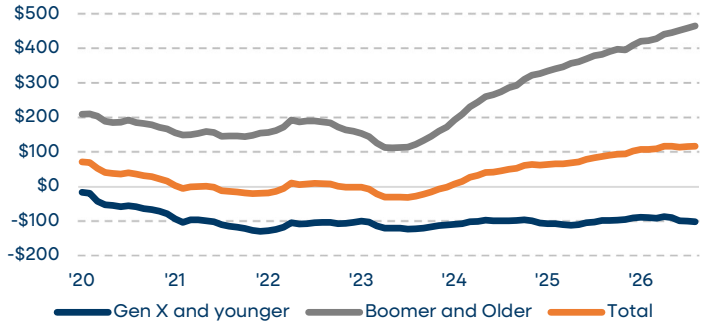
We estimate the consumption effect from AI-linked equities by applying a 3% annual marginal propensity to consume out of stock-market wealth.[1] The passthrough is not immediate. We assume it begins one quarter after the wealth shock and is largely phased in over the following two years. We estimate that AI wealth effects contributed an average of 24 bps to annualized real GDP growth in the first half of 2026. Because of the surge in stock prices in the second quarter, despite the Iran conflict, we estimate that wealth effects will contribute around 80 bps to growth in the third quarter, underpinning strong consumption growth. Because households do not realize the wealth effect all at once, recent wealth gains will continue to support consumption in the quarters ahead, even in the absence of further stock-price growth.

Figure 10: AI-linked stocks market cap (% nominal GDP)



Sources: Bloomberg, PNC

Figure 11: Net monthly inflows from brokerages into checking accounts per household

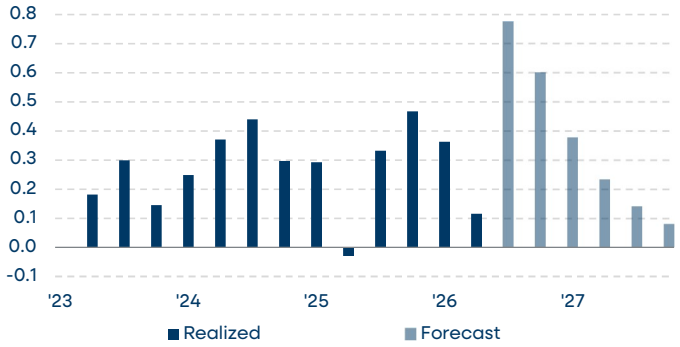


Source: PNC internal data

Note: Chart shows the average monthly net inflows from brokerages into our cohort's checking balances by broad generation category (twelve-month moving average)

[1] See Chodorow-Reich, Nenov, and Simsek (2021).

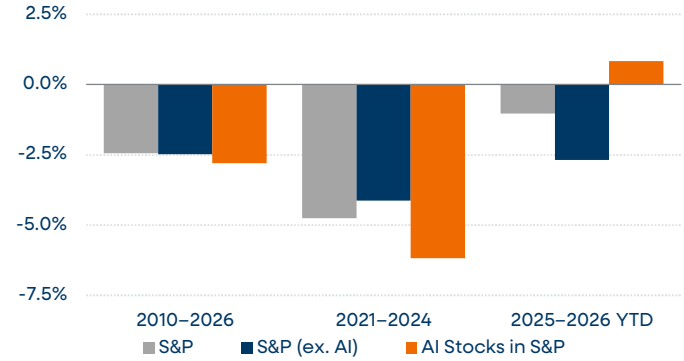
Figure 12: AI-linked equity wealth contribution to real GDP growth (percentage points, quarterly annualized)



Sources: BEA, Bloomberg, Federal Reserve Board, PNC
Note: Q3 nowcast and subsequent forecasts assume current-quarter equity gains are sustained, with no further gains through 2027.

Figure 13: AI-linked stocks show less sensitivity to hawkish monetary policy

Response to a +25 bp hawkish surprise, percent



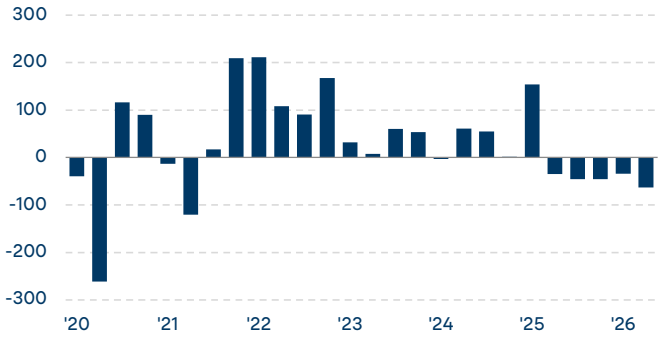
Sources: SF Fed, Bloomberg, PNC
Note: Estimates use monetary-event surprises from the San Francisco Fed's U.S. Monetary Policy Event-Study Database and measure the response of daily returns for the S&P 500, the S&P 500 excluding AI-linked stocks, and AI-linked S&P 500 stocks.

This poses a challenge for the Fed as it seeks to resume progress toward its inflation target. Historically, AI-linked stocks have not responded much differently to hawkish monetary-policy surprises compared to broader stock market indices or non-AI stocks. In fact, sensitivity of AI-related stocks to monetary-policy shocks increased in the immediate aftermath of the pandemic, consistent with AI and tech stocks being priced on more distant cash flows that are more sensitive to rising interest rates. However, since 2025, as the AI buildout has accelerated in earnest, AI-linked stocks have shown relatively little sensitivity to hawkish monetary-policy surprises, while non-AI stocks have remained sensitive. This suggests that AI and non-AI sectors of the economy could be affected differently by Fed tightening, leading to increasingly bifurcated outcomes. It also suggests that the Fed could have a difficult time slowing consumption if relatively rate-insensitive AI stocks continue to drive wealth effects, complicating progress toward its 2% inflation target. This insensitivity also creates the risk of Fed overtightening; if the economy and inflation do not respond initially to higher rates, the central bank may keep raising the fed funds rate until something "breaks."

Inventory rebuild should help drive growth in the coming quarters

Private inventories have declined in five consecutive quarters through the second quarter of 2026, a cumulative decline of $56 billion after adjustment for inflation, according to the Bureau of Economic Analysis. This is the first time inventories have declined for five quarters since the throes of the Great Recession, when the inventories fell for eight straight quarter, from 2008Q1 through 2010Q1.

Figure 14: Change in private inventories ($bn, 2017, SAAR)



Sources: BEA, PNC

Prior to that steep recession inventories hadn't fallen for five straight quarters since 1982, during the second leg of the U.S.'s double-dip recession. This suggests that big inventory declines are normally associated with steep recessions, but that has not been the case during the current period. Instead, the economy has been steadily expanding, with solid real GDP growth of 2.2% over the past year, even as inventories have been falling. Part of the drawdown in inventories came from a huge build in the first quarter of 2025, when they rose more than

$150 billion at an annualized pace, as businesses rushed to import ahead of higher tariffs from the Trump administration.

The inventories index from the Institute for Supply Management's Purchasing Managers Index was below the 50 level that indicates expansion from May 2025 to May 2026 but has moved into expansion territory for the past few months. The customer inventory index, another component of the ISM manufacturing report, has been below 50 every month since September 2024. The customers inventories index has moved higher in 2026, although it still remains in contraction. These measures suggest that businesses have been holding back on inventory accumulation despite solid demand. At least until recently businesses appear to have been concerned about holding on to too much inventory because of economic uncertainty.

As a result, the ratio of private inventories to final sales of domestic product—the inventory-to-sales ratio for the U.S. economy—was near a record low in the second quarter of 2026. This is true for both overall private inventories as well as non-farm inventories. For non-farm industries this ratio fell steadily in the last quarter of the 20th century as firms improved their inventory management techniques, but it has been much more stable over the past 25 years. With both the total and nonfarm ratios currently below their average over the past 25 years, inventories in the economy relative to sales are historically low. With demand continuing to expand, firms will likely need to add to inventories going forward, which should provide support to overall economy growth. This is apparent in the more recent ISM numbers.

In addition to the direct jobs created in manufacturing from an inventory build, greater investment in inventories would also drive job gains in industries like transportation and warehousing. Job growth has been inconsistent across manufacturing, transportation, and warehousing since the end of the bounce back in the economy from the disruptions caused by the COVID-19 pandemic. A period of inventory rebuilding could support job gains in these sectors, even as the Federal Reserve continues to tighten monetary policy in the near term. A higher fed funds rate that weighs on demand combined with an inventory build could help restore the balance between supply and demand, allowing for continued growth along with slower inflation.

Additional charts and tables

Table 1: Baseline U.S. Economic Outlook, Summary Table

Indicator	25Q4	26Q1	26Q2	26Q3f	26Q4f	27Q1f	27Q2f	2025	2026f	2027f	2028f
Output											
Nominal GDP ($bn)	31,423	31,866	32,486	33,031	33,386	33,755	34,111	31,423	33,386	34,825	36,321
Percent Change Annualized	**4.2**	**5.8**	**8.0**	**6.9**	**4.4**	**4.5**	**4.3**	**5.4**	**6.2**	**4.3**	**4.3**
Real GDP ($bn, '17 SAAR)	24,125	24,274	24,408	24,595	24,716	24,838	24,955	24,125	24,716	25,180	25,652
Percent Change Annualized	**0.2**	**2.5**	**2.2**	**3.1**	**2.0**	**2.0**	**1.9**	**2.0**	**2.4**	**1.9**	**1.9**
Consumer Spending	16,605	16,634	16,789	16,934	17,047	17,127	17,200	16,605	17,047	17,336	17,633
Percent Change Annualized	**1.9**	**0.7**	**3.8**	**3.5**	**2.7**	**1.9**	**1.7**	**2.1**	**2.7**	**1.7**	**1.7**
Business Fixed Investment	3,810	3,901	3,986	4,063	4,130	4,184	4,228	3,810	4,130	4,307	4,468
Percent Change Annualized	**2.1**	**9.9**	**9.0**	**8.0**	**6.8**	**5.3**	**4.3**	**6.0**	**8.4**	**4.3**	**3.7**
Residential Investment	756	741	746	740	736	736	736	756	736	741	760
Percent Change Annualized	**-1.8**	**-7.6**	**2.8**	**-3.5**	**-2.0**	**-0.1**	**0.5**	**-3.8**	**-2.6**	**0.7**	**2.6**
Change in Private Inventories	-46	-35	-63	15	6	10	13	-46	6	18	28
Net Exports	-1,006	-1,019	-1,099	-1,216	-1,274	-1,301	-1,315	-1,006	-1,274	-1,336	-1,382
Government Expenditures	4,041	4,087	4,087	4,096	4,108	4,118	4,129	4,041	4,108	4,150	4,181
Percent Change Annualized	**-5.7**	**4.7**	**-0.1**	**0.9**	**1.2**	**1.0**	**1.1**	**-0.6**	**1.7**	**1.0**	**0.8**
Industrial Production (*'12 = 100*)	101	102	103	104	104	105	106	101	104	107	110
Percent Change Annualized	**-1.9**	**1.3**	**4.2**	**4.5**	**2.6**	**2.4**	**2.4**	**1.6**	**3.1**	**2.5**	**2.4**
Capacity Utilization (*Percent*)	75.6	75.6	76.1	76.8	77.0	77.2	77.4	75.6	77.0	77.7	78.5
Prices											
CPI (% Change Ann.)	2.5	3.6	6.1	2.0	1.8	1.9	1.9	2.7	3.3	2.0	2.1
Core CPI Index (% Change Ann.)	2.0	2.8	2.9	2.3	2.4	2.3	2.4	2.7	2.6	2.3	2.2
PCE Price Index (% Change Ann.)	2.7	4.2	5.0	1.9	1.8	1.8	1.8	2.7	3.2	1.9	2.0
Core PCE Price (% Change Ann.)	2.5	3.9	3.3	2.3	2.4	2.3	2.2	2.8	3.0	2.2	2.1
GDP Price Index (% Change Ann.)	3.7	3.6	6.4	1.3	2.3	2.5	2.3	3.3	3.4	2.4	2.4
Crude Oil, WTI ($/Barrel)	59.6	72.7	95.6	87.6	81.8	79.2	77.1	59.6	81.8	75.6	75.9
Case-Shiller HPI (% Change Ann.)	3.3	2.3	-0.4	0.0	0.0	1.0	1.0	1.3	0.4	1.0	1.0
Labor Markets											
Payroll Jobs (*Millions*)	158.4	158.6	158.9	159.1	159.2	159.5	159.8	158.4	159.2	160.1	160.7
Percent Change Annualized	**-0.2**	**0.3**	**0.7**	**0.7**	**0.1**	**0.7**	**0.8**	**0.2**	**0.5**	**0.6**	**0.4**
Unemployment Rate (*Percent*)	4.5	4.3	4.3	4.2	4.3	4.3	4.3	4.5	4.3	4.3	4.2
Avg. Wkly Hours, Prod. Works.	33.7	33.8	33.8	33.8	33.8	33.8	33.8	33.7	33.8	33.8	33.8
Personal Income											
Average Hourly Earnings (*$*)	31.8	32.0	32.3	32.5	32.8	33.0	33.3	31.8	32.8	33.8	34.9
Percent Change Annualized	**3.8**	**3.3**	**3.5**	**2.8**	**3.1**	**3.1**	**3.1**	**3.9**	**3.2**	**3.1**	**3.2**
Real Disp. Income (*2017 $bn*)	18,193	18,303	18,294	18,395	18,502	18,610	18,731	18,193	18,502	18,960	19,379
Percent Change Annualized	**0.5**	**2.4**	**-0.2**	**2.2**	**2.3**	**2.4**	**2.6**	**1.4**	**1.7**	**2.5**	**2.2**
Interest Rates (%)											
Prime Rate	7.0	6.8	6.8	6.8	7.1	7.3	7.5	7.0	7.1	7.5	7.5
Federal Funds	4.00	3.75	3.75	3.75	4.00	4.25	4.50	4.00	4.00	4.50	4.50
3-Month Treasury Bill	3.8	3.7	3.7	3.8	4.1	4.3	4.4	3.8	4.1	4.4	4.4
10-Year Treasury Note	4.1	4.2	4.4	4.7	4.7	4.7	4.7	4.1	4.7	4.7	4.7
30-Year Fixed Mortgage	6.2	6.1	6.4	6.6	6.7	6.7	6.6	6.2	6.7	6.6	6.6

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