



National Economic Outlook

October 2025

Headlines

- **The government shut down on October 1st** with no clear end in sight. Each week of the shutdown could temporarily trim 15bps off of Q4 growth, creating additional uncertainty around this quarter's outlook.
- **The labor market continues to soften in 2025.** We see this driven by three main trends: sharply reduced net immigration, firms cutting labor costs in response to higher tariffs, and federal government job cuts. **We expect job growth to remain subdued through 2026, with the unemployment rate peaking at 4.7%.**
- **Despite labor market headwinds, economic activity has shown resilience.** AI-related capex and wealth effects have supported growth, but the gap between spending and income is unsustainable. **We expect growth to slow to 1.7% in 2026.**
- **Progress on inflation has stalled**, as tariff-related price pressures boost goods inflation. We expect core inflation to slow modestly next year but remain above the Fed's target, **increasing 2.6% in 2026.**
- **Risks to this outlook remain skewed to the downside.** Recent strength has hinged on two factors – robust consumer spending from equity-driven wealth effects and AI-related investment. Both rely on sustained AI optimism. **If sentiment fades and markets correct, these supports could reverse quickly, turning today's growth drivers into vulnerabilities.**

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Table 1: Baseline U.S economic outlook, summary table

Indicator	Quarterly								Annual (Q4/Q4)		
	25Q1	25Q2	25Q3f	25Q4f	26Q1f	26Q2f	26Q3f	26Q4f	2024	2025f	2026f
Output/Inflation											
Real GDP (Q/Q Ann. %)	-0.6	3.8	3.0	1.0	1.4	1.7	1.8	1.9	2.4	1.8	1.7
Core CPI (Q/Q Ann. %)	3.5	2.1	3.5	3.4	2.9	2.7	2.6	2.5	3.3	3.1	2.6
Labor Markets											
Payrolls (Avg. Monthly Change)	111k	55k	45k	-20k	30k	35k	40k	50k	168k	48k	39k
Unemployment Rate (%)	4.1	4.2	4.3	4.5	4.6	4.6	4.7	4.6	4.1	4.5	4.6
Interest Rates (%)											
Federal Funds	4.50	4.50	4.25	3.75	3.50	3.50	3.50	3.50	4.50	3.75	3.50
10-Year Treasury Note	4.27	4.50	4.50	4.17	4.21	4.24	4.25	4.25	4.40	4.17	4.25

p = preliminary, f = forecast, Please see the expanded table for more forecast series.

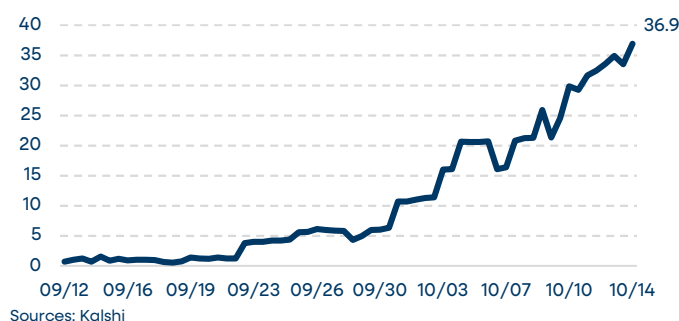


Shutdown limits data flow, adds uncertainty to the Q4 outlook

The government shutdown is now in its third week, which has limited the flow of official data releases and furloughed over 750k nondiscretionary federal workers. Historically, shutdowns have had modest and temporary effects on growth, **however the risk of more lasting effects on growth increases with the duration of the shutdown.**

By all indications, this shutdown will extend further into Q4 with no clear end in sight. President Trump secured temporary funding to ensure nearly 1.3 million active-duty military personnel continue to receive their paychecks, which in past shutdowns has been a political pressure point. **Betting markets now expect the shutdown to last nearly 40 days,** making it one of the longest shutdowns on record.

Figure 1: Prediction market expectations for length of government shutdown (# days)



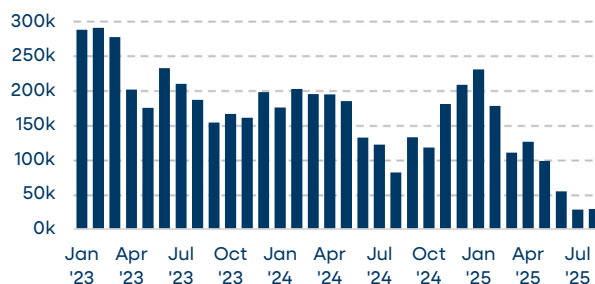
The data releases we have received since the shutdown have been mixed. Privately constructed measures of job growth show the labor market is in a similar place in September. Estimates of initial claims constructed from state-level releases show no material increase in layoffs since the shutdown began. Business sentiment surveys—such as the ISM Services and Manufacturing indices—have come in slightly weaker.

Low hire, low fire job market continues

In recent years, strong job creation has helped propel the economy forward despite high interest rates and high inflation. The labor market has cooled

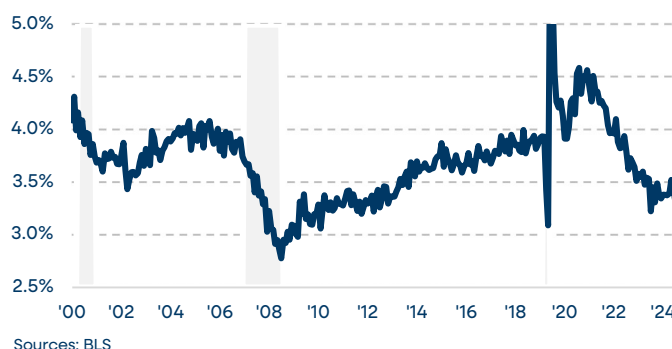
considerably in 2025, however, with net job growth falling to a 3-month moving average of 29k over the summer.

Figure 2: Nonfarm payroll job growth (3M MA)



As Chair Powell has said, this has become very much a **“low hire, low fire”** job market. **Firms have been reluctant to lay off workers** in 2025 – the pace of layoffs remains quite low by historical context. However, **firms have also been reluctant to add to headcount.** The pace of hiring has fallen to levels not seen since the depths of the pandemic or during the weak recovery from the 2007/09 recession.

Figure 3: Gross hiring rate has fallen to historically low levels



Why has job growth fallen so dramatically compared to a few years prior? We see two main reasons. First, the supply of workers into the labor market has fallen considerably through **weaker net immigration** in 2025. Second, it appears firms have **offset higher tariff costs** (and perhaps needs to build out AI capacity) **with weaker hiring.**

The combination of these two factors has created a very **“curious type of balance”** in the labor market. Despite net job growth falling to levels typically seen during the onset of recession, the unemployment



rate has barely moved in 2025, increasing from 4.1% at the end of last year to just 4.3% currently.

Figure 4: “Breakeven” pace of job growth¹ has fallen from 250k to under 50k over the past two years

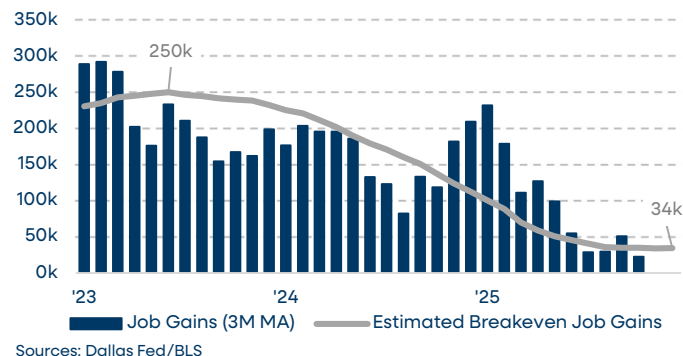


Figure 5: Factors influencing nonfinancial corporate profit margins between 25Q1 and 25Q2



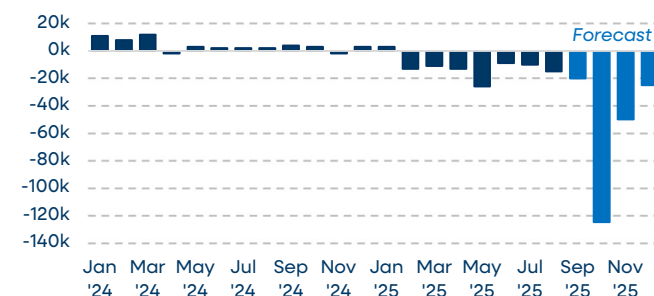
We expect these dynamics to carry into 2026. Job growth is likely to remain subdued at roughly 30k per month. However, weaker labor supply growth should help limit upward pressure on the unemployment rate. **We project the unemployment rate will continue rising through mid-2026, peaking at around 4.7% before easing in the latter half of the year.**

An additional factor shaping the outlook is federal employment. The Trump Administration has reiterated its goal of reducing the federal workforce by 300k positions in 2025. So far, approximately 100k jobs have been eliminated, on top of the 154k employees who accepted DOGE-related buyouts earlier this year and will officially leave government payrolls in Q4. **Taken together, these buyouts and**

¹ The “breakeven” pace of job growth is the level of job growth needed to keep the unemployment rate from rising. Job growth

ongoing workforce reductions are likely to lead to net payroll job losses in the fourth quarter.

Figure 6: Monthly change in federal payroll employment



Sources: BLS/PNC Estimates

Real GDP growth to slow to 1.7% in 2026

Despite softer job and income growth, the economy has remained surprisingly resilient through 2025. **We have revised our Q3 2025 real GDP forecast upward to 3.0%, following a similarly strong 3.8% gain in Q2.**

That said, the underlying growth trend has clearly slowed in 2025, and large swings in net trade and inventories – driven by tariff-related distortions – have obscured the signal to some degree. **Still, two developments have stood out this year.**

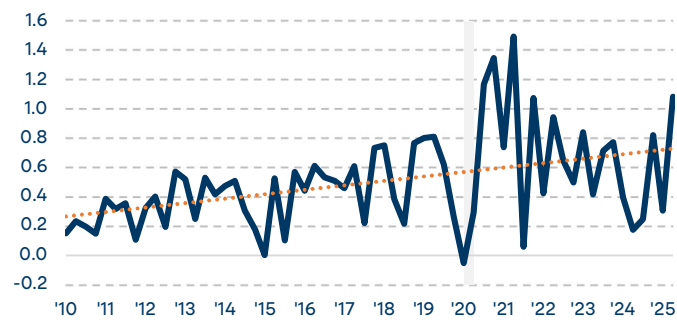
First, consumer spending has held up better than expected given muted labor income growth. Wealth effects from a surging equity market have supported spending, and households have reduced their saving to offset weaker income gains.

Second, business investment has been more resilient than anticipated, largely due to AI-related capital expenditures. Firms have poured resources into AI initiatives, even as non-AI investment has contracted. While we have a more conservative view on the economic impact of AI than some, it has **nonetheless provided a meaningful boost to growth in 2025.**

above the gray line indicates rising unemployment, below indicates falling

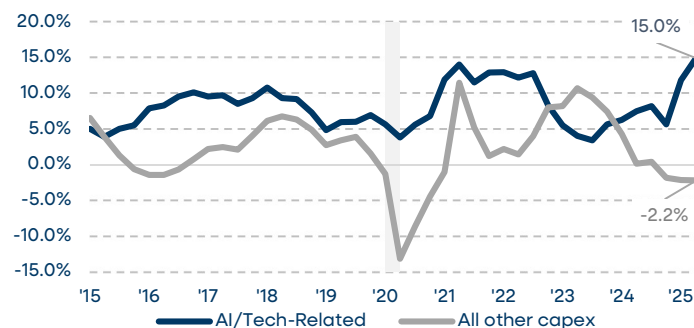


Figure 7: Contributions to Real GDP Growth from AI and Tech (Percentage Points)



Sources: BEA/PNC Estimates

Figure 8: Year-over-year growth in AI/tech-related capex vs. all other business capex



Sources: BEA/PNC Estimate

Looking ahead, we see this strength as unsustainable. Consumer spending growth is likely to slow in Q4 and into 2026, aligning more closely with labor market fundamentals. AI-driven investment should remain a tailwind next year, but broader capex plans outside of AI remain subdued. **Overall, we expect growth to decelerate to 1.7% in 2026 – closer to the economy’s underlying potential.**

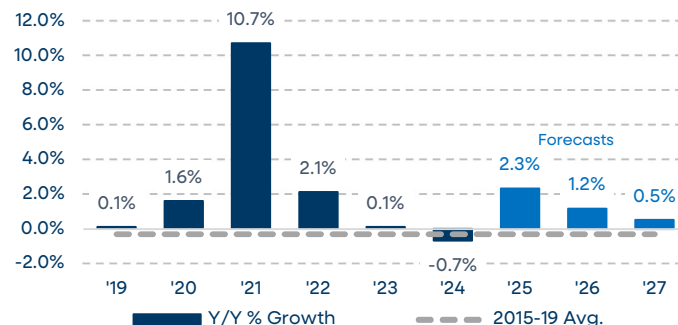
Risks to this outlook remain skewed to the downside. The better-than-expected performance in 2025 has been fueled by two forces: elevated consumer spending, supported by wealth effects from a booming equity market, and a surge in AI-related investment. **Both share a common root—optimism around AI.** If that sentiment fades and equity markets correct, the wealth effect could reverse quickly, pulling down consumption and capex. In short, the very drivers of recent strength could become vulnerabilities if the AI narrative loses momentum. There are also downside risks from tariffs and the government shutdown.

Inflation to remain elevated but slow to 2.6% in 2026

Progress on inflation stalled in 2025 as tariff-related price pressures pushed goods inflation higher, offsetting continued improvement in shelter costs. **PNC forecasts Core CPI to end 2025 at 3.1%, slowing to 2.6% in 2026.** We expect that gap between Core CPI and Core PCE – the Fed’s preferred inflation metric – to narrow further next year, also ending 2026 at 2.6% y/y.

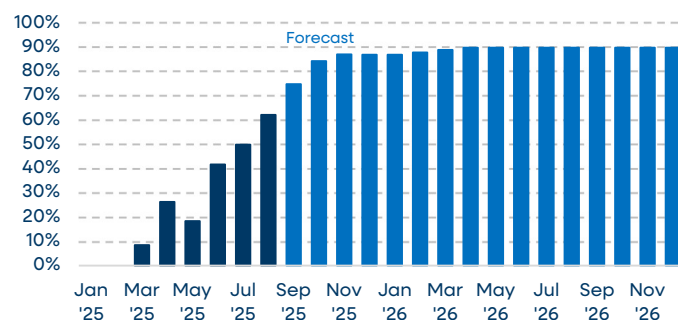
Tariffs are now clearly reflected in the inflation data, though their passthrough to consumer prices has been less severe than initially feared. The effective tariff rate on U.S. imports has risen to nearly 10% as of July, the latest available data. **We estimate roughly 60% of tariff costs have been passed on to consumers,** with the remainder absorbed by U.S. importers. Core goods inflation is expected to finish 2025 at 2.3% year-over-year, with tariff-related pressures persisting through at least Q2 2026.

Figure 9: Core Goods CPI Projections (Y/Y % Growth)



Sources: Dallas Fed/BLS

Figure 9: Estimated percentage of total tariff costs passed onto consumers

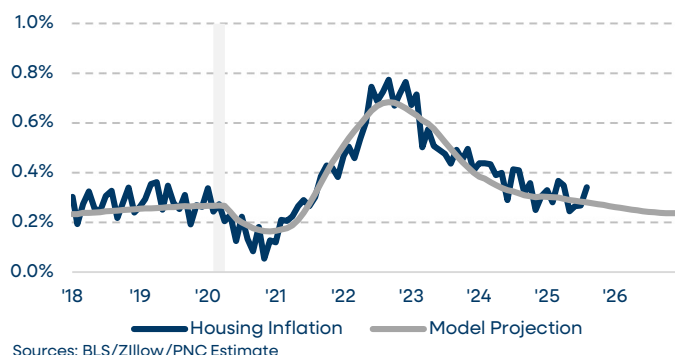


Sources: PNC Estimates

**The one bright spot in the inflation outlook is shelter.**

Rents surged during the post-pandemic reopening but have since slowed to below pre-pandemic levels. Market rents on newly listed apartments typically lead official measures by 12 to 18 months. By our estimates, CPI rents have now fully caught up to market trends and should continue moderating into 2026. **We expect shelter inflation to end 2025 at 3.5%, easing to 3.2% next year.**

Figure 8: CPI housing inflation: M/M % growth, actual vs. modeled projection



Outside of shelter, services inflation has remained stubbornly above pre-pandemic norms throughout 2025. Risks here are two-sided: a softer labor market and productivity gains could help pull services inflation lower, while weaker net immigration may put upward pressure on lower-skill service-sector wages. If the economy outperforms expectations, services inflation could even accelerate.

The Fed to cut until it sees improvements in the labor market

The minutes of the September FOMC meeting showed the Fed remains concerned and uncertain about the inflation outlook, but willing to look through that to support the employment side of its mandate. We agree with Chair Powell that there is no risk-free path for the Fed here. Cutting rates is likely needed to stabilize the employment side of its mandate, but risks reigniting inflationary pressures. Failing to cut rates risks recession, as the labor market clearly continues to weaken in 2025.

In our view, the Fed will likely cut by 25 bps at each of the next three FOMC meetings, reaching a terminal range of 3.25% to 3.50% after the January 2026 FOMC meeting. However, there are two-sided risks to this outlook. If inflation re-accelerates or proves more persistent than expected, the Fed may cut less; if growth falters or recession emerges, easing could be deeper and more prolonged.



Additional charts and tables

Table 2: Baseline U.S. Economic Outlook, Summary Table

Indicator	25Q2	25Q3f	25Q4f	26Q1f	26Q2f	26Q3f	26Q4f	2024	2025f	2026f	2027f
Output											
Nominal GDP (\$bn)	30,486	30,921	31,191	31,451	31,745	32,038	32,340	29,825	31,191	32,340	33,525
Percent Change Annualized	6.0	5.8	3.6	3.4	3.8	3.7	3.8	4.9	4.6	3.7	3.7
Real GDP (\$bn, '17 SAAR)	23,771	23,949	24,011	24,093	24,197	24,306	24,418	23,587	24,011	24,418	24,869
Percent Change Annualized	3.8	3.0	1.0	1.4	1.7	1.8	1.9	2.4	1.8	1.7	1.8
Consumer Spending	16,446	16,554	16,613	16,671	16,738	16,807	16,879	16,321	16,613	16,879	17,170
Percent Change Annualized	2.5	2.7	1.4	1.4	1.6	1.7	1.7	3.4	1.8	1.6	1.7
Business Fixed Investment	3,659	3,696	3,713	3,731	3,753	3,778	3,805	3,514	3,713	3,805	3,917
Percent Change Annualized	7.3	4.0	1.9	1.9	2.4	2.7	2.8	0.9	5.7	2.5	3.0
Residential Investment	779	769	764	765	770	775	782	791	764	782	810
Percent Change Annualized	-5.1	-5.0	-2.5	0.7	2.4	3.0	3.2	1.3	-3.4	2.3	3.6
Change in Private Inventories	-18	-18	-18	-6	13	27	36	17	-18	36	46
Net Exports	-1,058	-1,011	-1,003	-1,004	-1,017	-1,029	-1,040	-1,069	-1,003	-1,040	-1,071
Government Expenditures	3,993	3,989	3,971	3,964	3,969	3,976	3,986	4,004	3,971	3,986	4,027
Percent Change Annualized	-0.1	-0.4	-1.7	-0.7	0.5	0.7	1.0	3.6	-0.8	0.4	1.0
Industrial Production ('12 = 100)	104	104	105	105	106	106	107	102	105	107	110
Percent Change Annualized	1.6	2.0	1.4	1.5	1.9	2.2	2.3	-0.3	2.3	2.0	2.9
Capacity Utilization (Percent)	77.6	78.2	78.4	78.5	78.7	78.9	79.0	77.1	78.4	79.0	79.7
Prices											
CPI (% Change Ann.)	1.6	3.2	3.4	2.9	2.7	2.6	2.6	2.7	3.0	2.6	2.3
Core CPI Index (% Change Ann.)	2.1	3.5	3.4	2.9	2.7	2.6	2.5	3.3	3.1	2.6	2.3
PCE Price Index (% Change Ann.)	2.1	2.9	3.2	2.8	2.6	2.7	2.6	2.4	3.1	2.6	2.1
Core PCE Price (% Change Ann.)	2.6	3.5	3.3	2.8	2.6	2.6	2.5	3.0	3.2	2.6	2.1
GDP Price Index (% Change Ann.)	2.1	2.7	2.5	2.0	2.0	1.9	1.9	2.5	2.7	2.0	1.8
Crude Oil, WTI (\$/Barrel)	64.6	66.0	67.3	68.6	70.0	71.6	73.4	70.8	67.3	73.4	79.9
Labor Markets											
Payroll Jobs (Millions)	159.4	159.6	159.6	159.7	159.9	160.1	160.5	158.6	159.6	160.5	161.8
Percent Change Annualized	0.7	0.4	0.0	0.2	0.4	0.6	1.0	1.2	0.6	0.6	0.8
Unemployment Rate (Percent)	4.2	4.3	4.5	4.6	4.6	4.7	4.6	4.1	4.5	4.6	4.4
Avg. Wkly Hours, Prod. Works.	33.7	33.7	33.7	33.7	33.7	4.7	4.6	33.7	33.7	4.6	4.4
Personal Income											
Average Hourly Earnings (\$)	31.2	31.4	31.6	31.9	32.1	32.3	32.6	30.6	31.6	32.6	33.6
Percent Change Annualized	3.4	3.2	3.1	3.0	3.0	3.0	3.0	4.1	3.5	3.0	3.0
Real Disp. Income (2017 \$bn)	18,082	18,166	18,207	18,275	18,349	18,430	18,526	17,843	18,207	18,526	18,896
Percent Change Annualized	3.1	1.9	0.9	1.5	1.6	1.8	2.1	2.4	2.0	1.8	2.0
Interest Rates (%)											
Prime Rate	7.5	7.4	6.8	6.5	6.5	6.5	6.5	7.6	6.8	6.5	6.5
Federal Funds	4.3	4.2	3.7	3.4	3.4	3.4	3.4	4.5	3.7	3.4	3.4
3-Month Treasury Bill	4.3	4.0	3.6	3.4	3.4	3.4	3.4	4.3	3.6	3.4	3.4
10-Year Treasury Note	4.4	4.1	4.2	4.2	4.2	4.3	4.3	4.4	4.2	4.3	4.3
30-Year Fixed Mortgage	6.8	6.4	6.4	6.3	6.3	6.4	6.4	6.7	6.4	6.4	6.4



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