

Economic Update

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On soft and shifting sands

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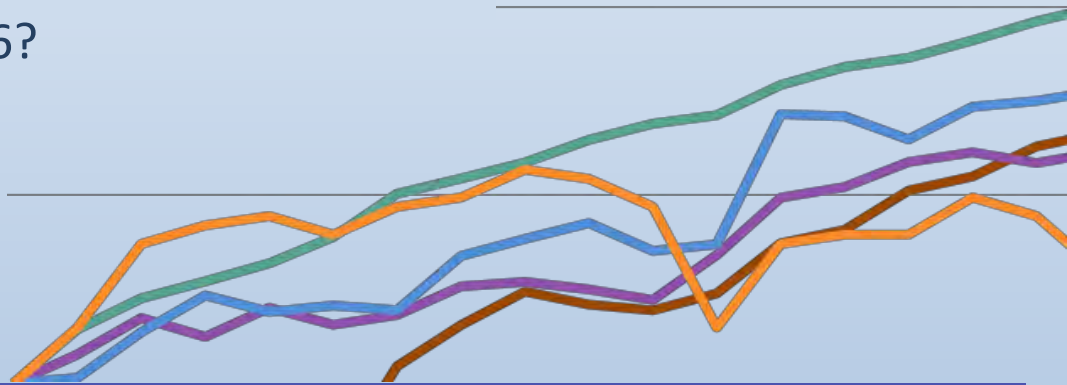


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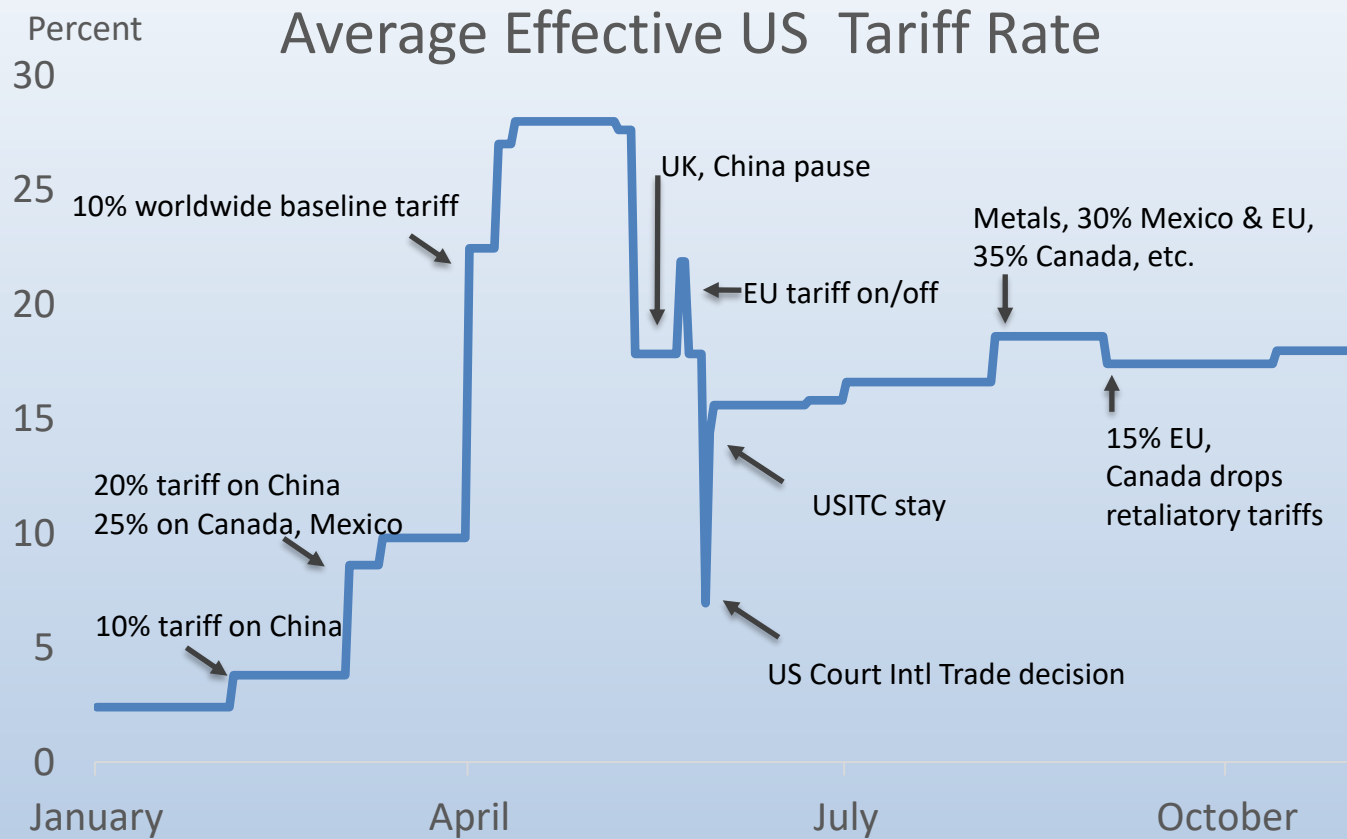
Volunteer Leadership Institute
Island of Kauai, January 14, 2026

Economy shuffling into 2026

- Last year saw gathering challenges
 - The labor market continued to soften
 - Tariffs and deportations raised prices and costs
 - Policy uncertainty weighed on investment
 - Only support came from Fed rate cuts and consumer resilience
- Will conditions improve in 2026?



The year of great uncertainty



Source: Yale Budget Lab as of Oct. 17, 2025

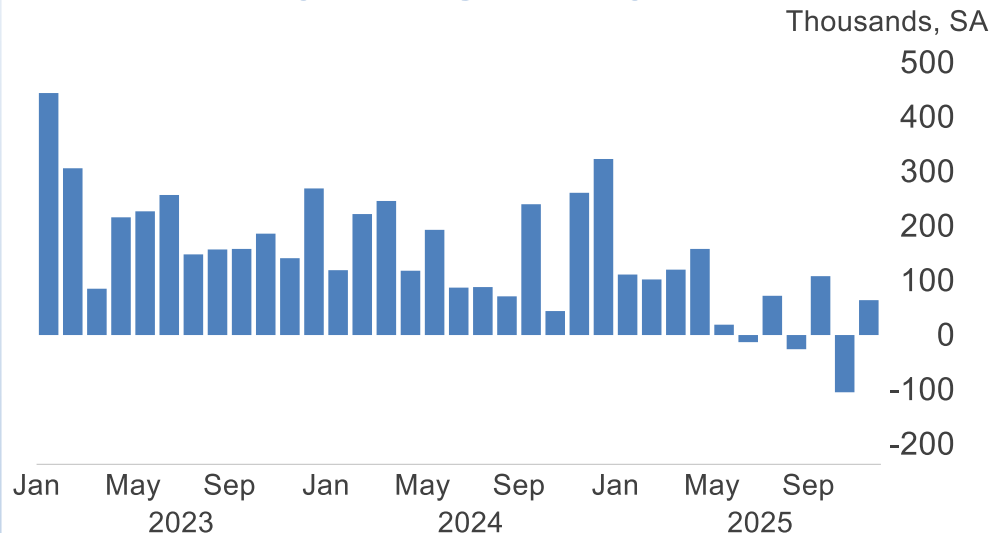
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The labor market has softened

- US labor market growth has stalled
 - Job growth effectively zero
 - Actually weaker than this in the 12 months ending in March
 - Openings & hires are low
 - Unemployment has risen to 4.6%

Monthly Change in Payroll Jobs

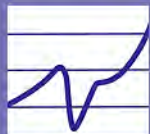
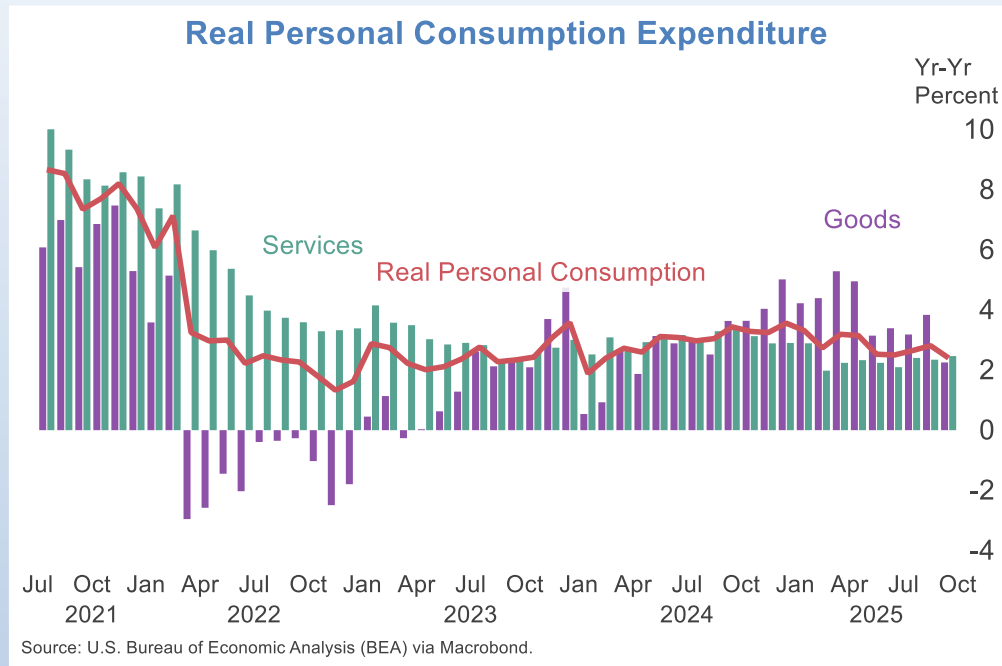


Source: U.S. Bureau of Labor Statistics (BLS) via Macrobond.



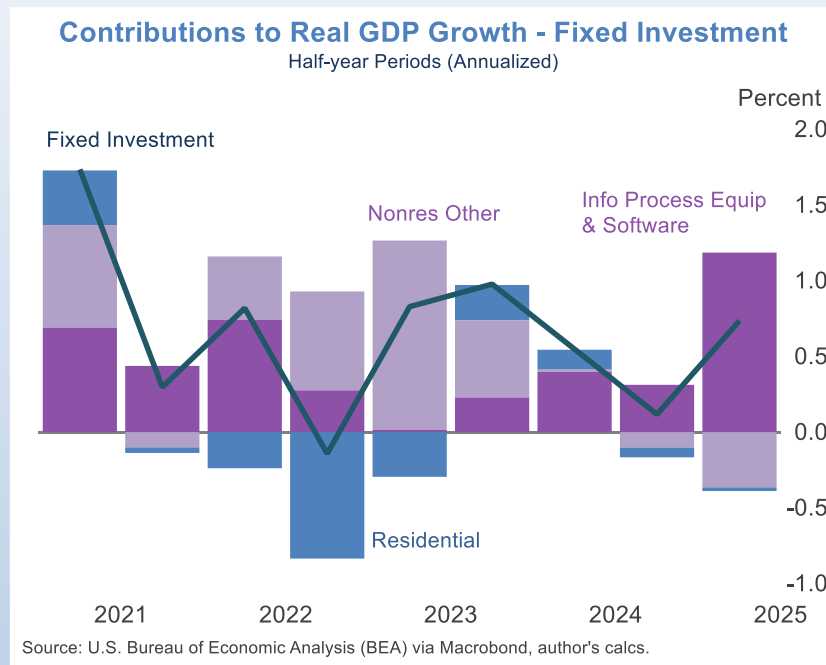
Consumer side of economy is slowing

- Consumer spending was firm in the year's first half
- Has been the biggest support of economy's resilience
- But spending has softened since mid-year



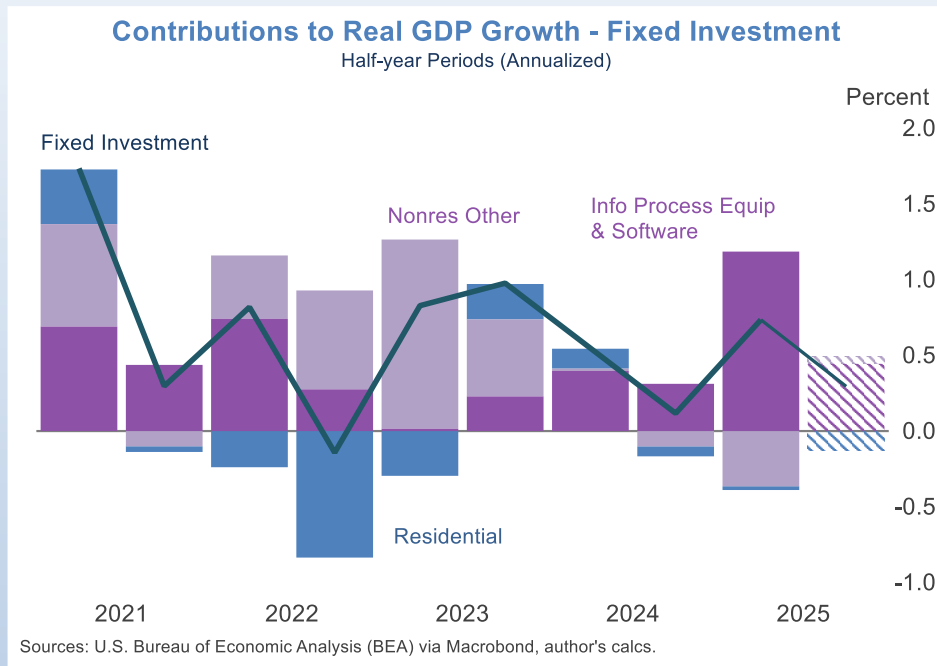
AI related investment is all there is

- Business fixed investment has been very weak
 - Residential small or negative
- First half of 2025, it was all AI



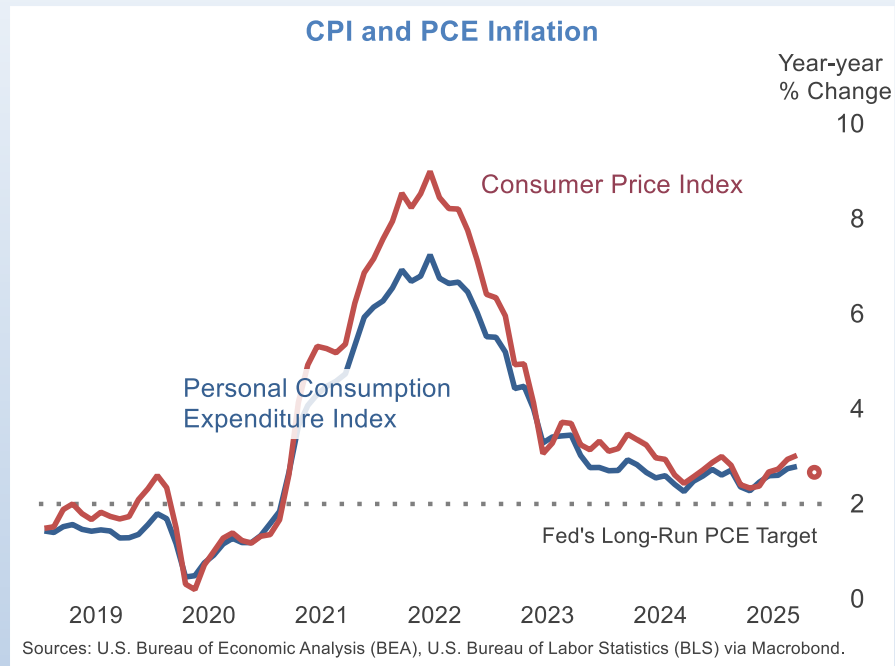
And even that has dropped off

- Business fixed investment has been very weak
 - Residential small or negative
- First half of 2025, it was all AI
- Even that dropped off in 3rd quarter

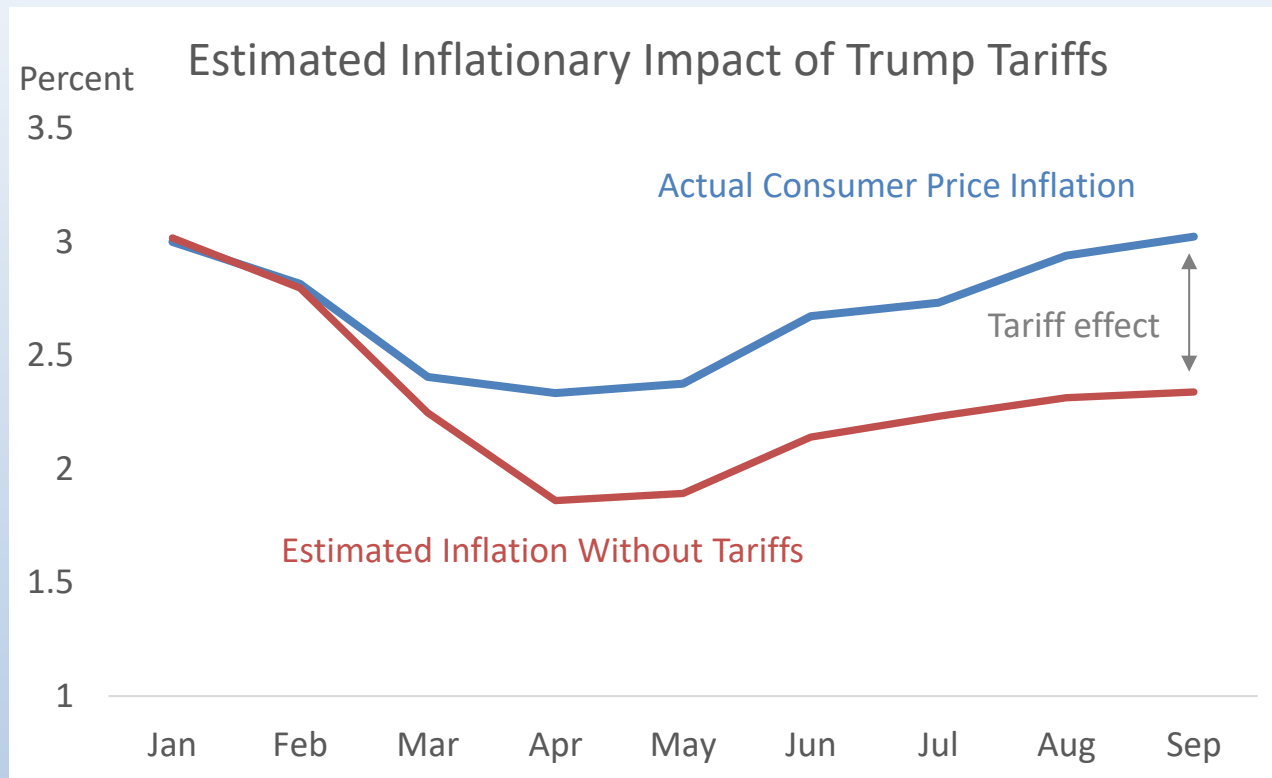


Inflation is moderate, but moving wrong way

- Headline measures of inflation are moving away from Fed's target
- Most recent PCE is September; No CPI survey for October
- November CPI data looks encouraging
 - But reasons to think this was an underestimate

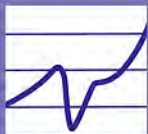
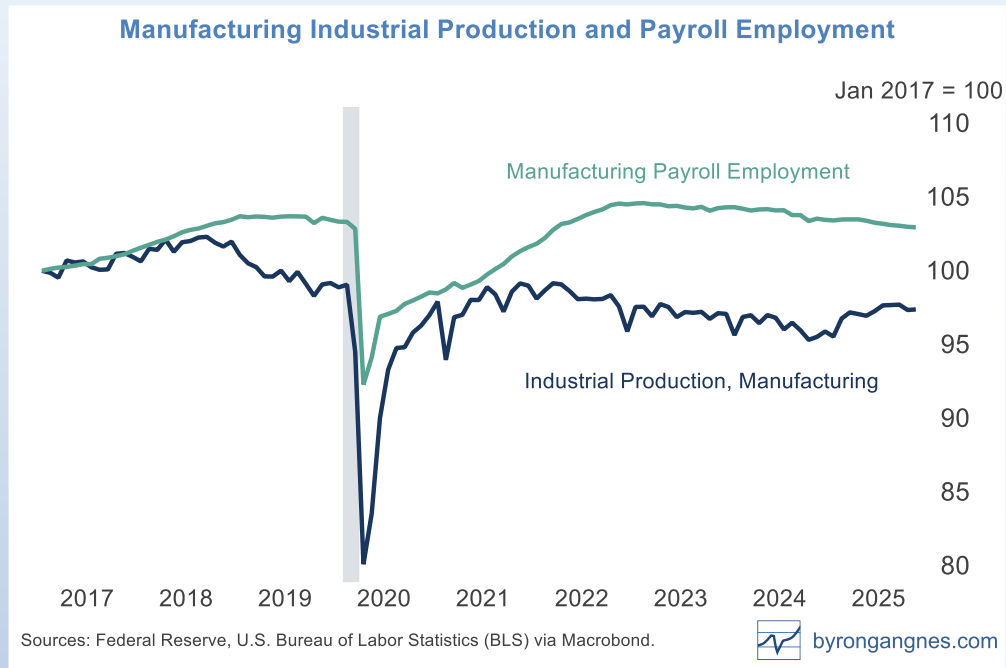


Tariffs are passing through into prices



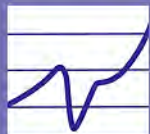
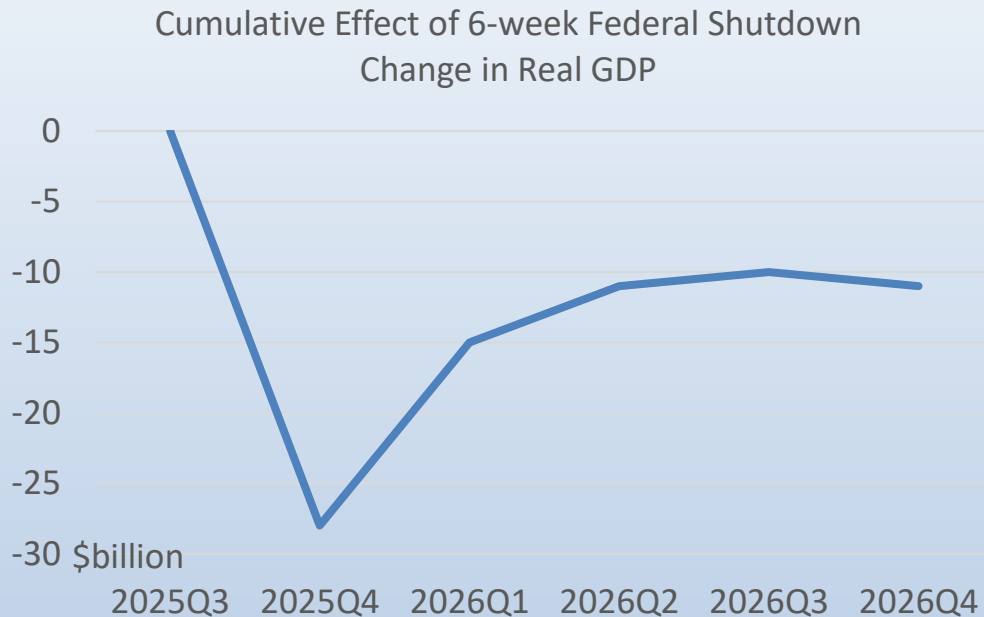
Manufacturing moving sideways

- Manufacturing activity remains flat
- New orders have barely budged
- Employment has been falling for three years



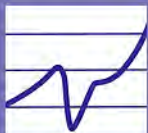
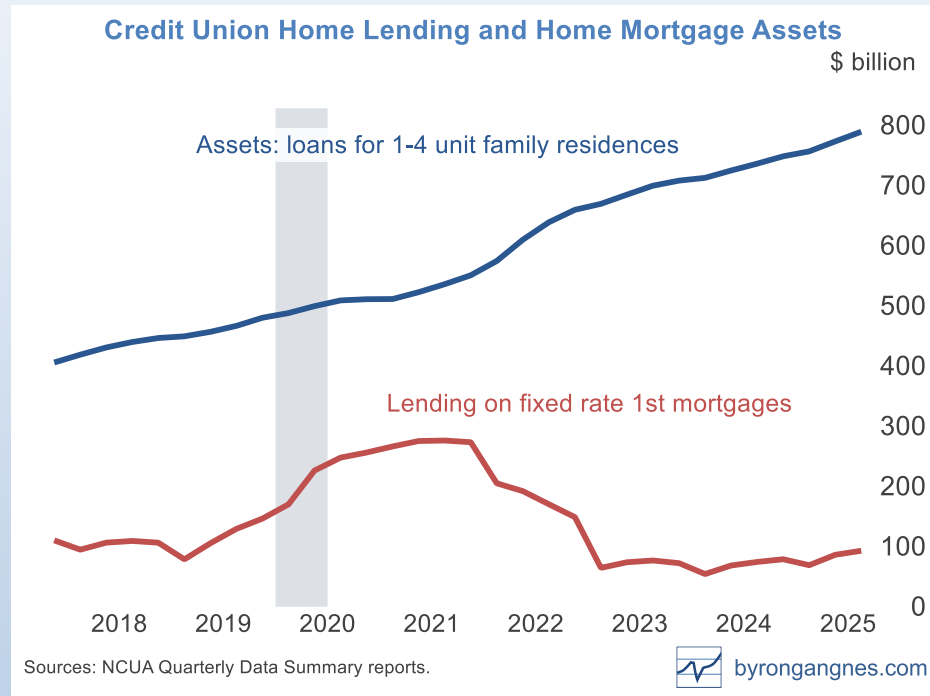
Shutdown economics

- Autumn federal shutdown reduced spending and growth
- Part of this will be made up
- Hardship impacts on many families were a bigger issue
- Delayed and lost data



Credit union conditions marginally better

- Credit union finances show some improvement
 - Return on assets turned the corner last year, on strength of net interest income
 - Delinquencies have stabilized
- But
 - Very low levels of mortgage lending
 - Flat fee income
 - Provisioning for loan losses 50% higher than in 2020



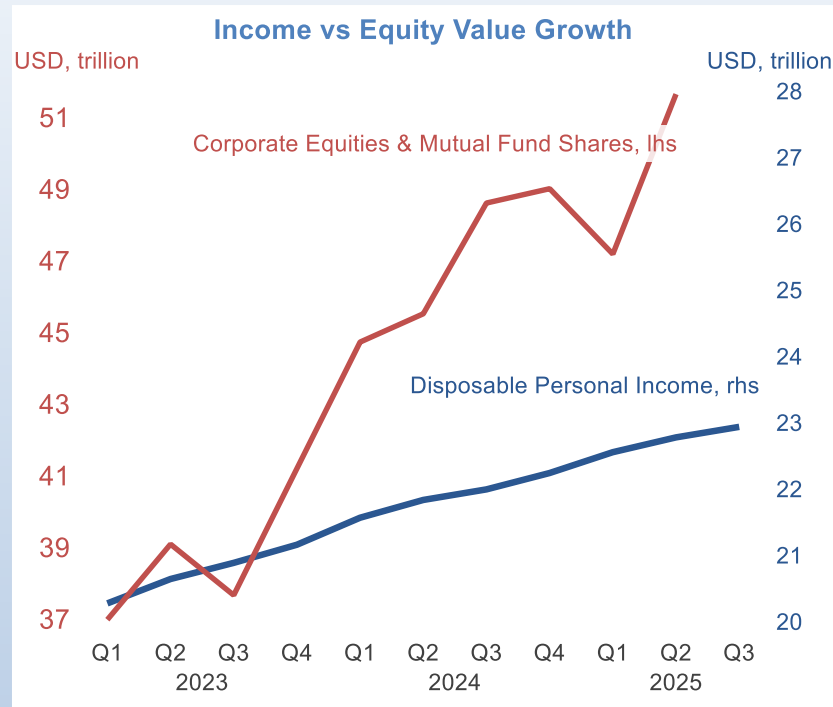
The balance of factors for 2026 is mixed

- Consumer in a more precarious position
 - Labor markets softer, spending already slower, tariffs biting
 - But income and wealth growing
- Macro policy may be more supportive
 - Monetary policy no longer restrictive
 - Tax cuts could offset drag
 - Tariff relief?
- Will business climate improve?
 - Reduced uncertainty could support investment
 - But tariffs & deportations will still weigh



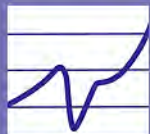
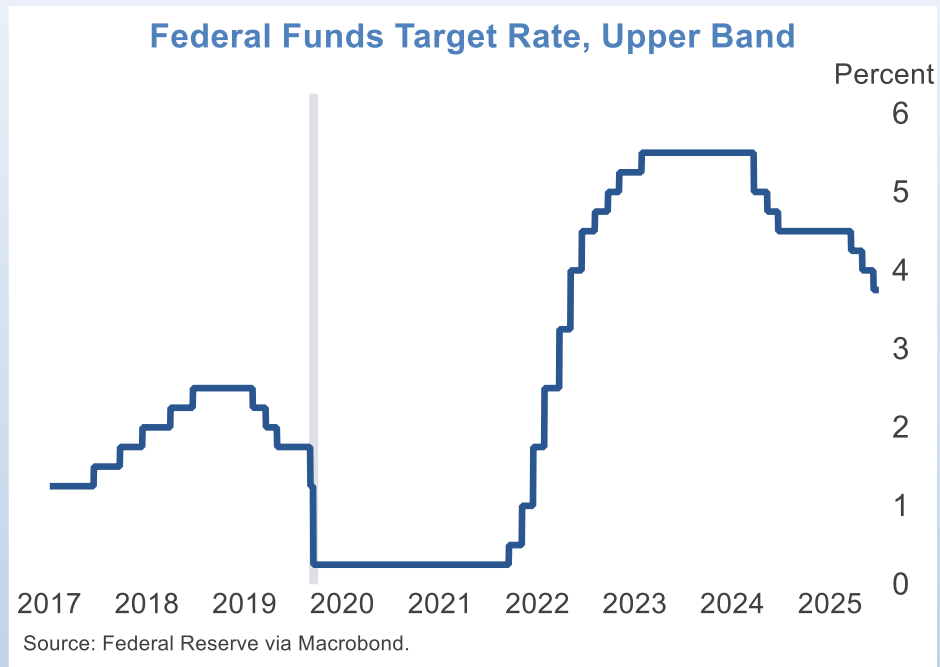
Stock gains are driving spending by some

- Incomes have grown
- But equity values have grown more
- Hard for spending by rich to offset weaker spending by poor
 - And bubble risks



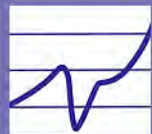
Fed policy no longer a drag

- The federal funds rate is now 0.75% lower than a year ago.
 - Close to a “neutral” rate
- The Fed’s dual mandate is more challenging
 - Labor market weakening
 - But inflation stubborn
- Long-term rates remain high
 - We’ll come back to this

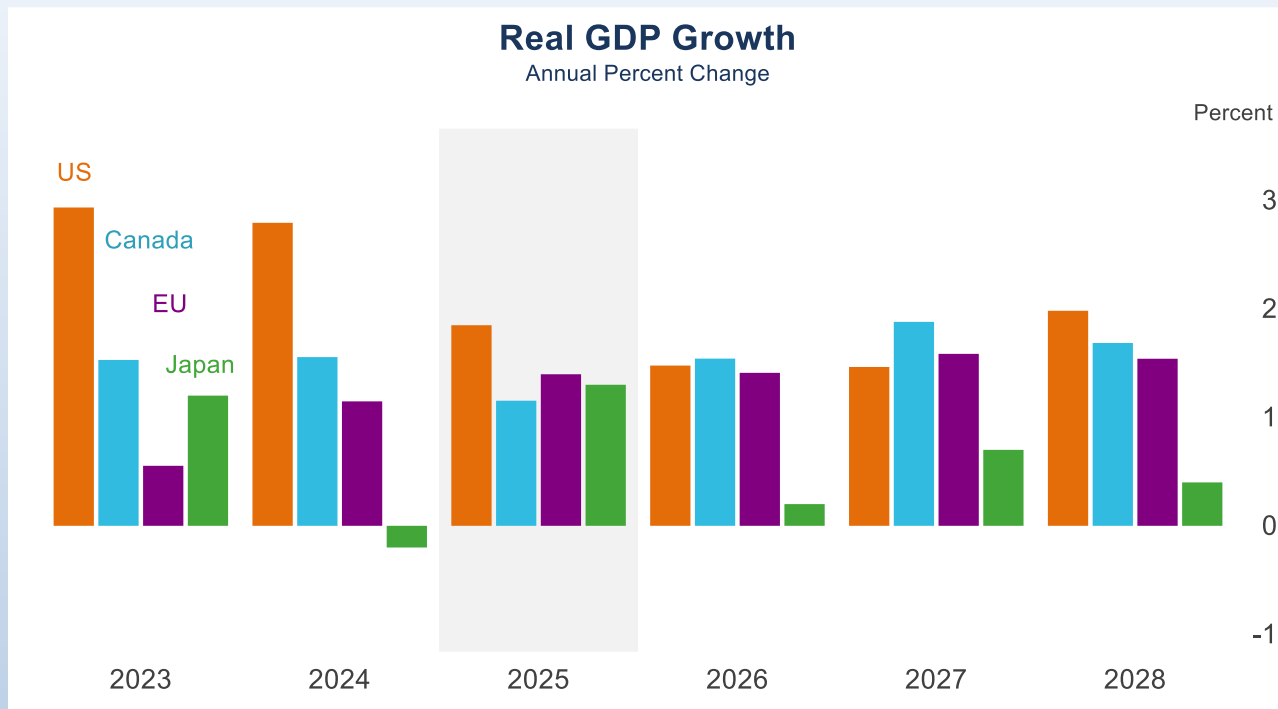


Short-term fiscal stimulus coming

- “One Big Beautiful Bill” will boost growth this year
 - Trump tax cuts extended, corporate taxes reduced, SALT ceiling raised, OT and tip exemption, bigger child tax credits
 - But cuts to social programs and end of health care subsidies will weigh on some households; end of clean energy credits on investment
 - GDP 0.2-0.4% higher this year and next than without it?
- Long-run effect is likely negative because of higher gov't debt and interest rates, poorer workforce health.

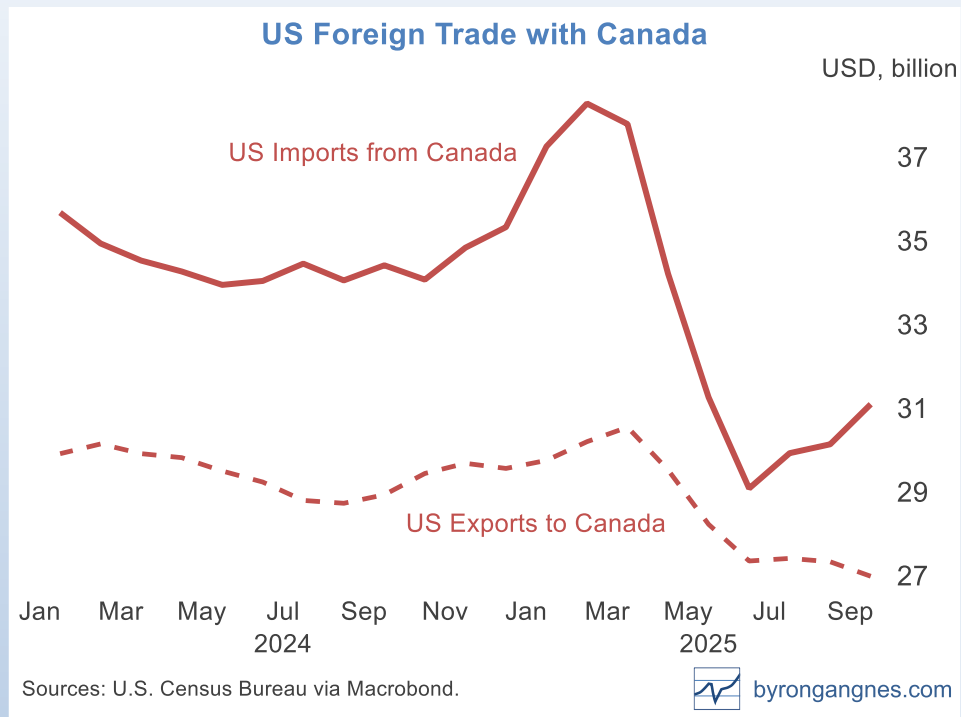


The outlook: Weakness before firming

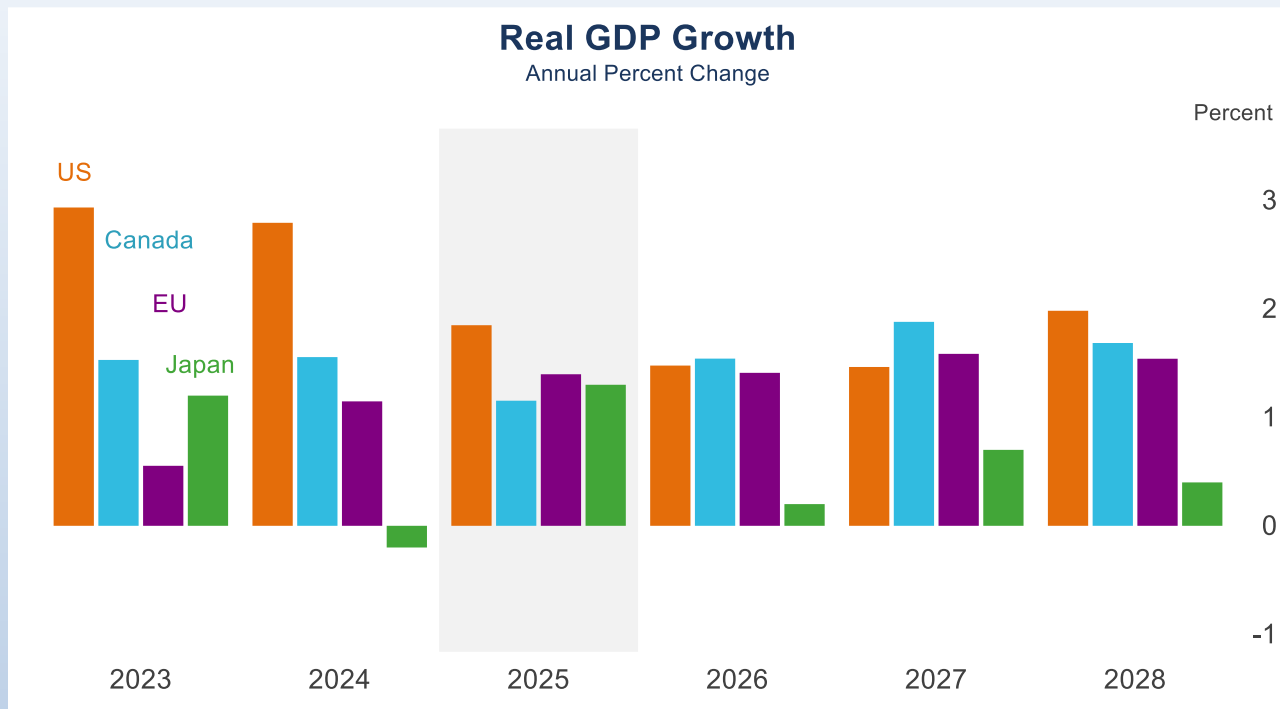


Trade war's international fallout (for some)

- Canadian exports took a tumble in the summer
 - Led to a very large decline in GDP
 - Intertwined NA auto market so hurt US producers too
- China was able to more than replace lost exports to the US
- US trade war contributes to an already weak global outlook

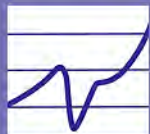


The outlook: Weakness before firming

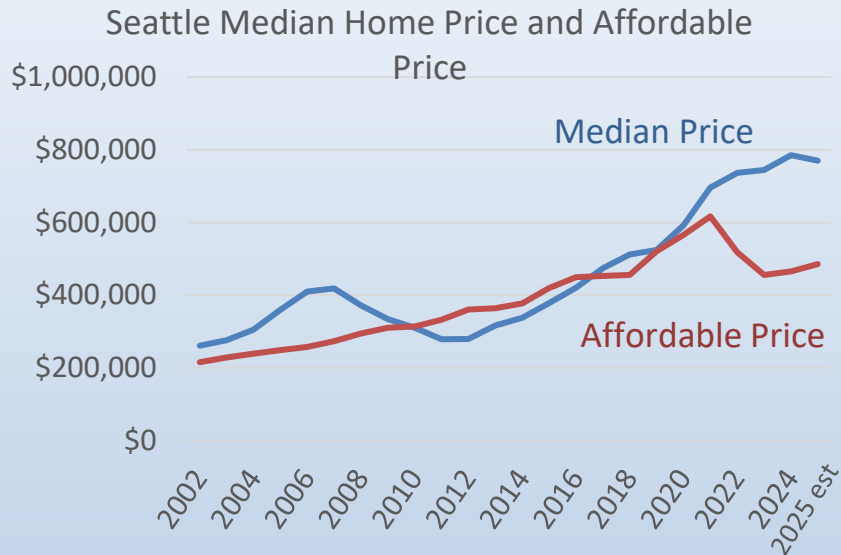


Big things to watch in 2026 and beyond

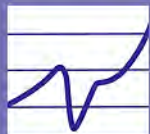
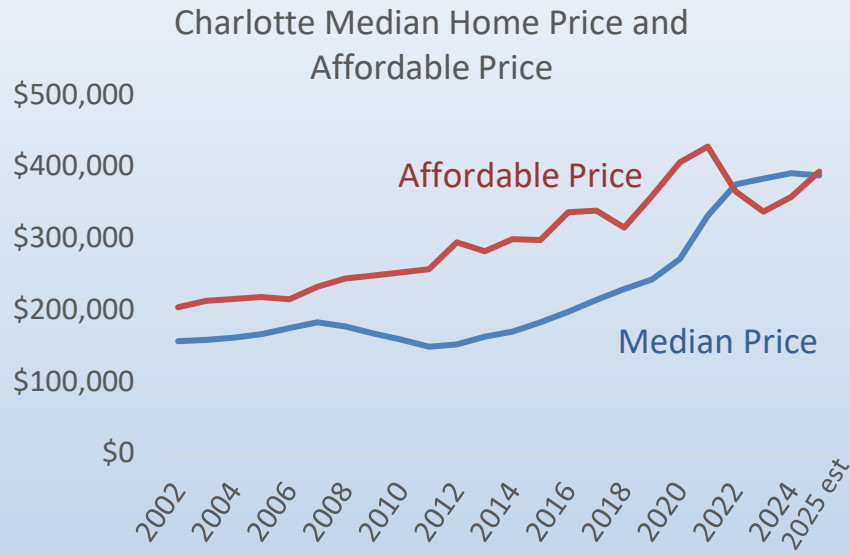
- Key longer-term issues
 - Housing affordability and prospects
 - Looming problem & promise



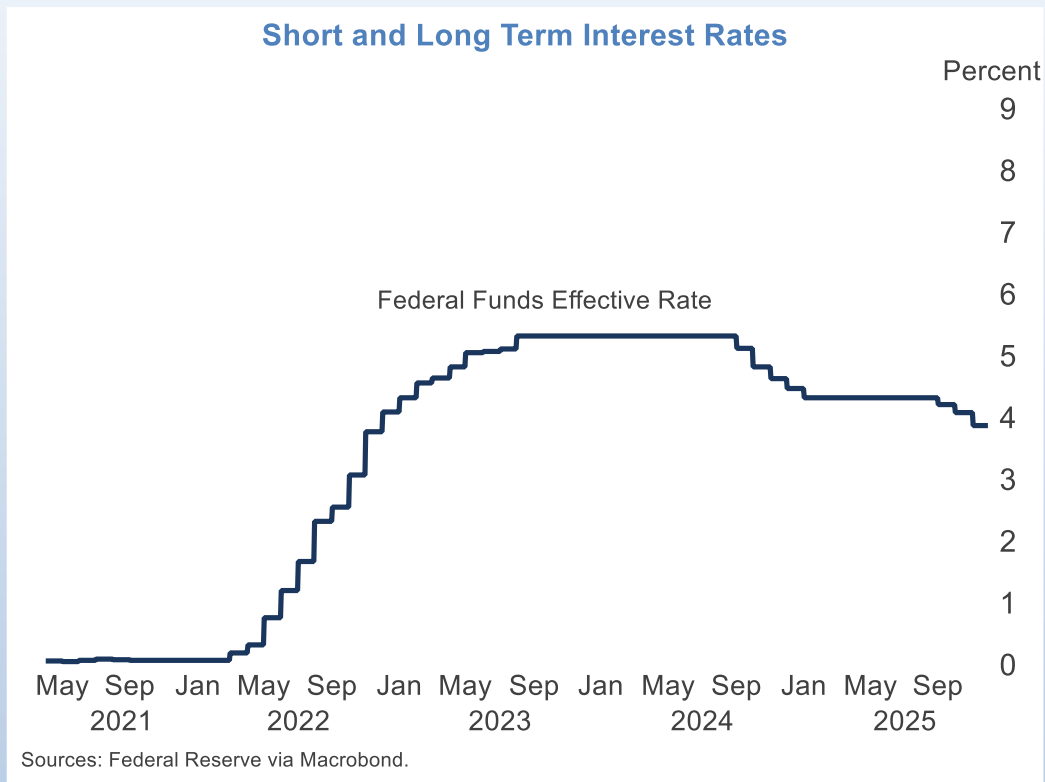
Home affordability is only a little better



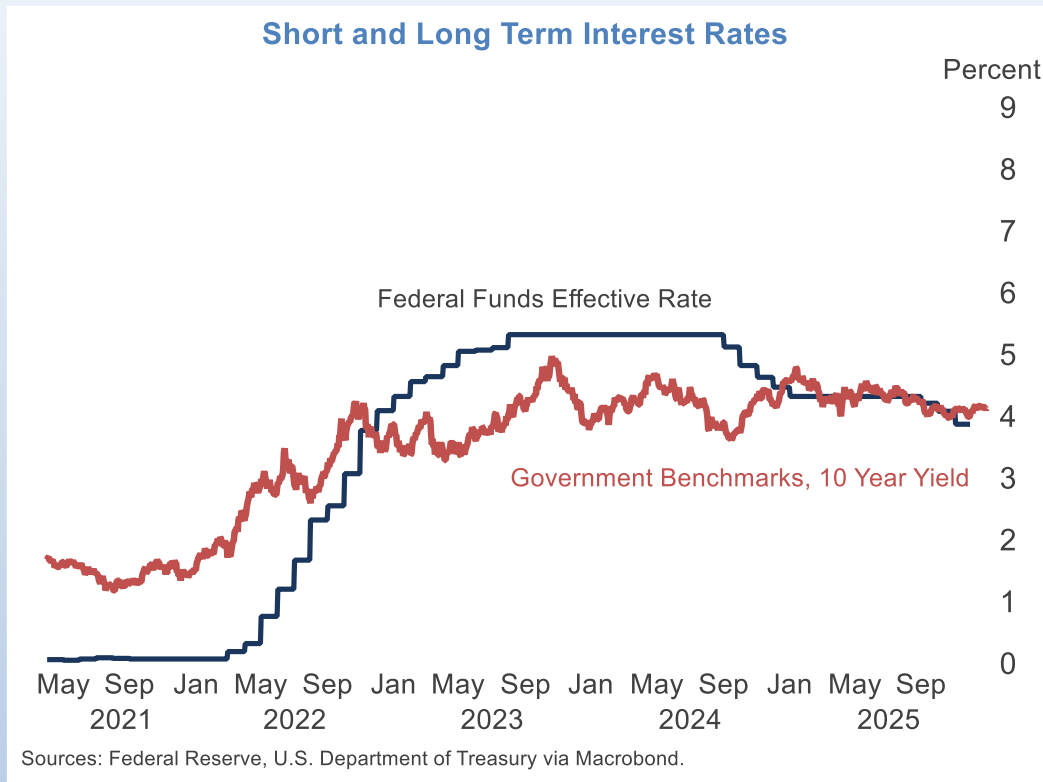
Some recent values are estimates.



Mortgage rates will remain high

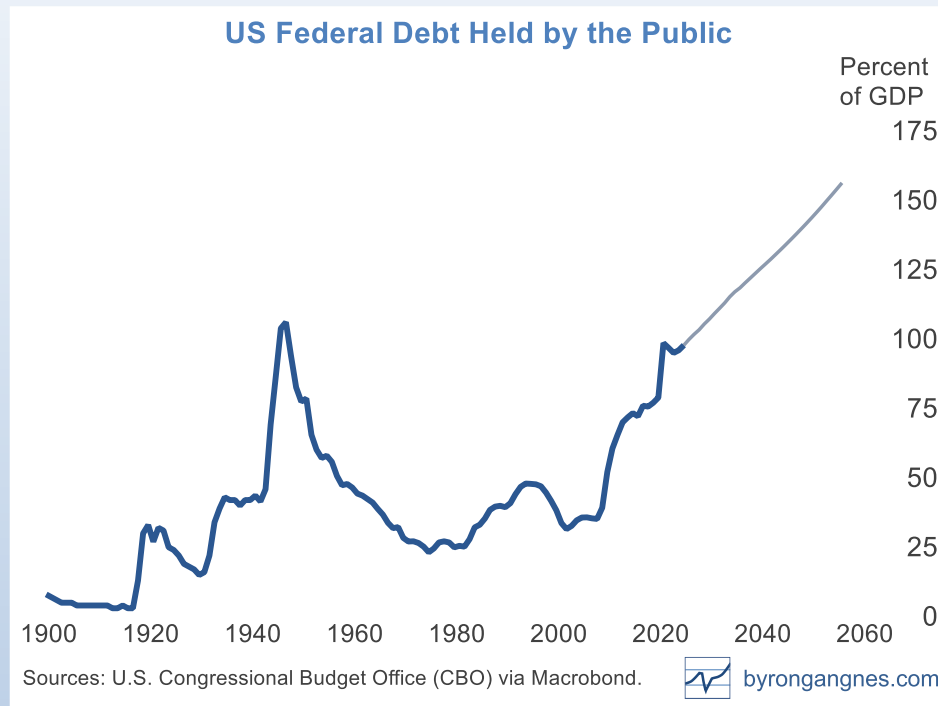


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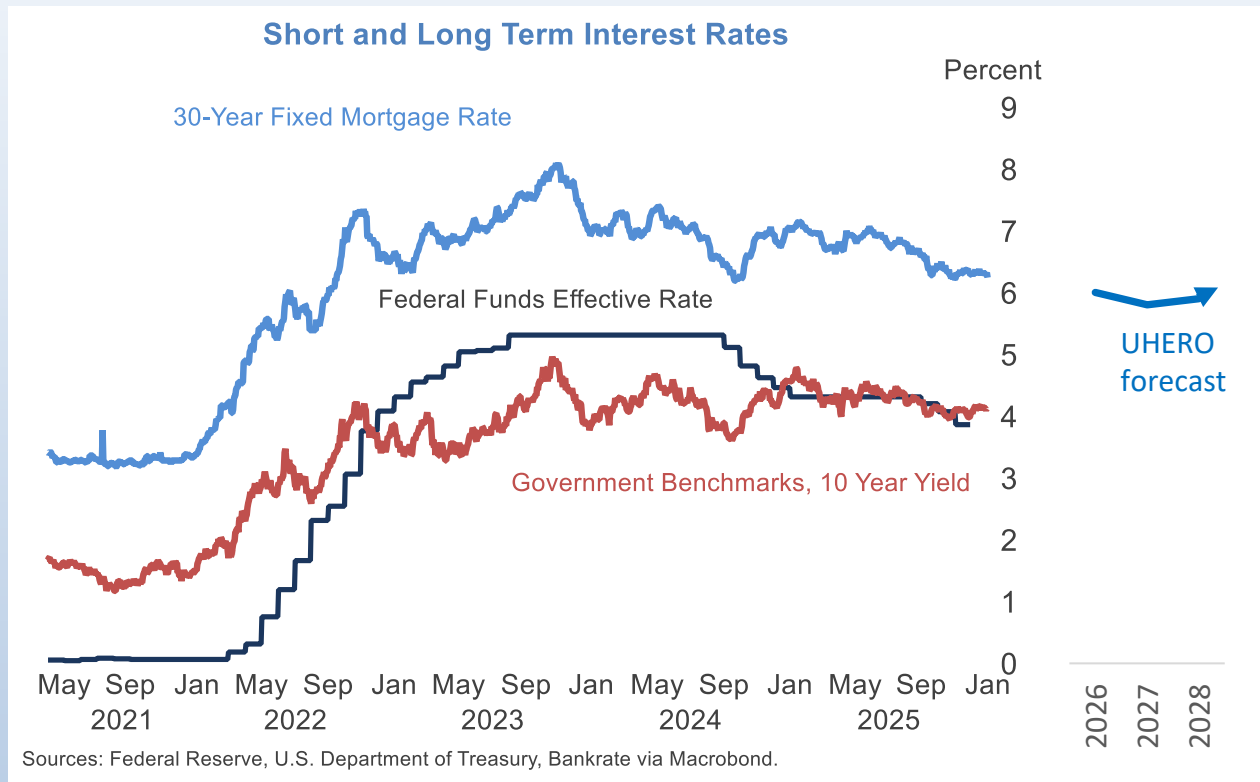


Why still high? Possibly public debt outlook

- Growth in outlays will exceed growth in revenues under current law
 - Driven by health care, net interest payments
- higher long-term interest rates may signal concerns about full faith and credit, inflation

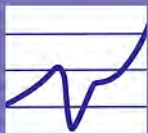


Mortgage rates likely to remain high

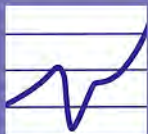
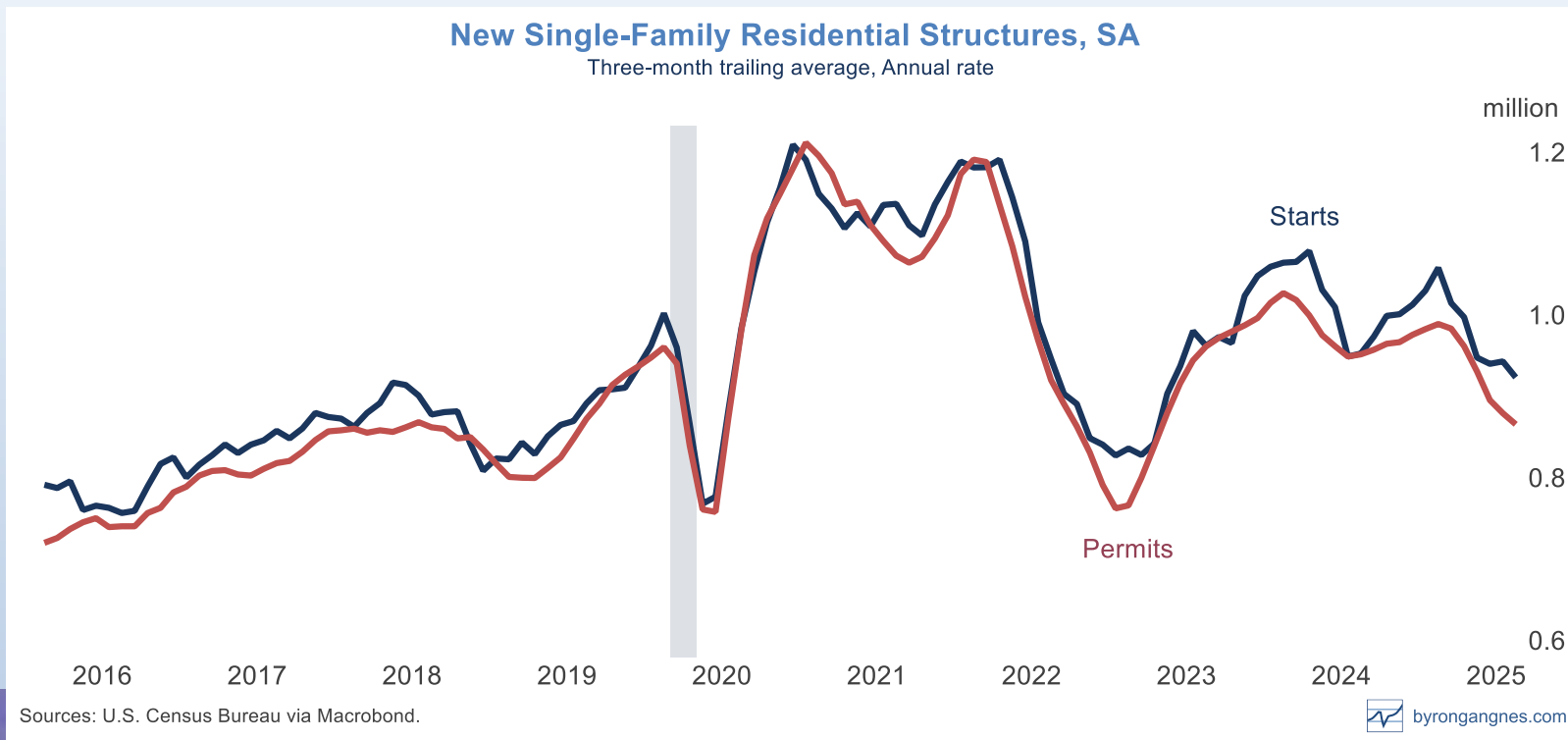


Source: Forecast is UHERO, December

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And new building is modest

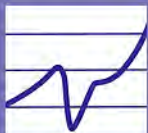


The aging problem

- We ain't getting any younger
 - Bigger burden on social programs
 - Pressure on government finances
 - Relatively smaller labor force but increased need
 - Possibly lower productivity



Photo by Annie Spratt on Unsplash



The AI promise

Key Pros

- **Productivity gains:** Automation and task augmentation raise output per worker
- **Faster innovation:** Accelerates R&D and discovery
- **New industries:** Enables new products, services
- **Economic growth despite aging:** Helps offset slower labor-force growth

Key Cons

- **Job displacement & worker disruption:** Especially for routine cognitive tasks
- **Adjustment frictions:** Slow diffusion, retraining costs, and transition unemployment
- **Rising inequality:** Across firm size, skill levels, and regions

Bottom Line: Consensus view is higher long-run growth, with distributional and transition risks.

Or so says ChatGPT!



BYRON GANGNES

Economic Insights



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Thank you!