RSM Global Economics Team

U.S. Macroeconomic Outlook

2025

Economic outlook summary

- The Fed has begun its interest rate pivot, cutting by 50 basis points in Sept. and 25 basis points in Nov. to 4.50-4.75%; we except another 25 basis-point cut Dec.
- US economy continuing to outperform in growth and employment, growing 3% in Q3 despite concerns about higher rates
- Combination of growth and likely expansionary fiscal policy will support a solid pace of growth and higher interest rates at the long end of the curve (higher for longer)
- Rising productivity and support from fiscal policies will be key tailwinds for growth but will result in inflation above Fed’s 2% target

Outlook scenarios for 2025

Scenario probability	GDP growth	Unemployment rate	PCE inflation	Fed Funds rate	10-year yield
Baseline (55%)	2.5%	4.2%	2.2%	3.5%	4.5%
Alternative (30%)	3% or higher	3.5% to 4%	2.5% to 3.5%	4.0%	5% or higher
Recession (15%)	Below 1% or negative	5% or higher	High if stagflation; low, otherwise	High if stagflation; near zero, otherwise	High if stagflation; low, otherwise

US growth outlook: The best economy in a generation that everyone still hates

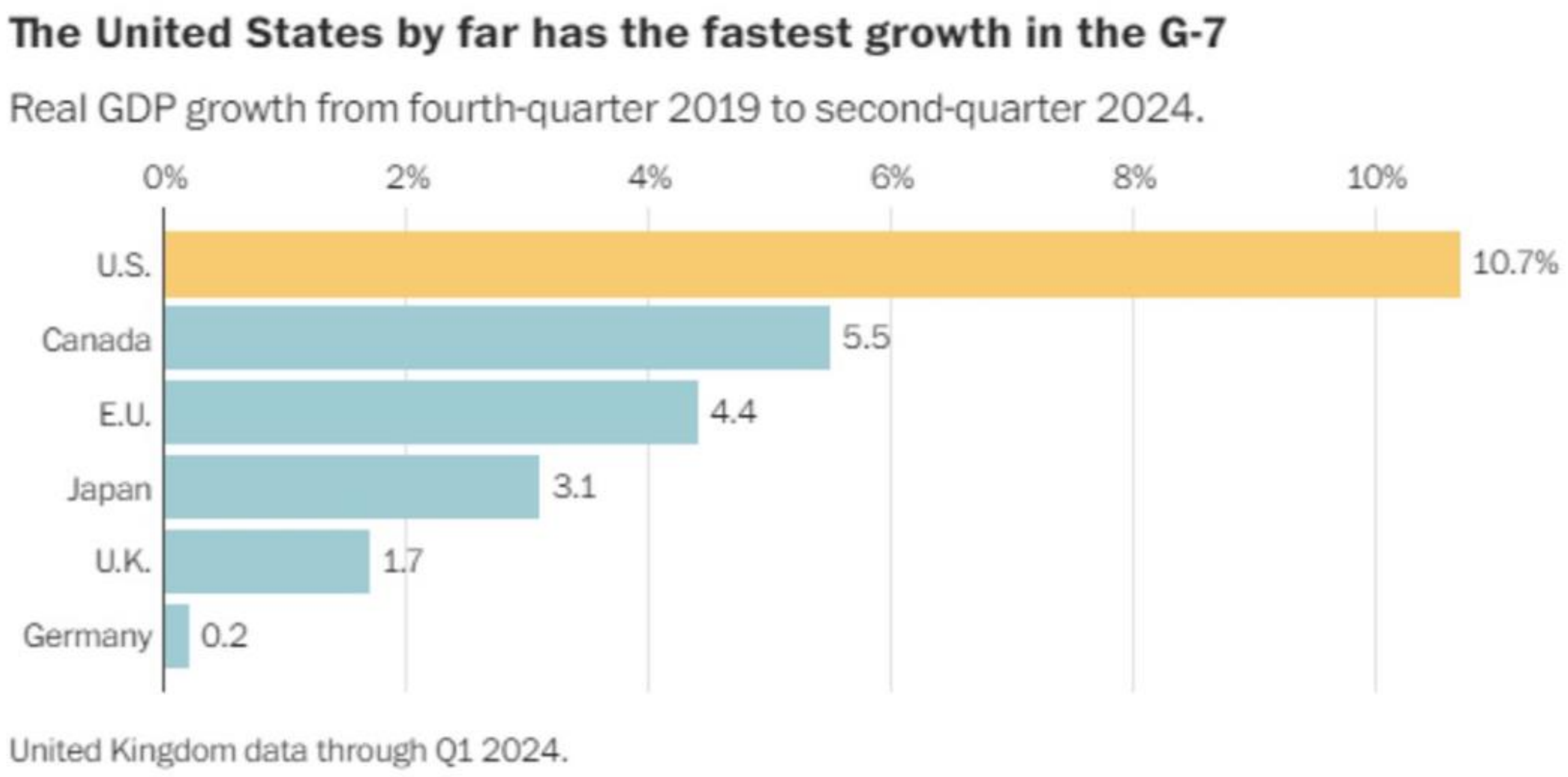
01 GDP remained strong in Q3, up 2.8% overall, driven by robust household spending, private investment, inventory accumulation

02 Q3 featured very strong 11.1% rise in spending on productivity-enhancing investment

03 Since Q3 2022, nine consecutive quarters of 2.9% growth, well above long-term trend of 1.8%

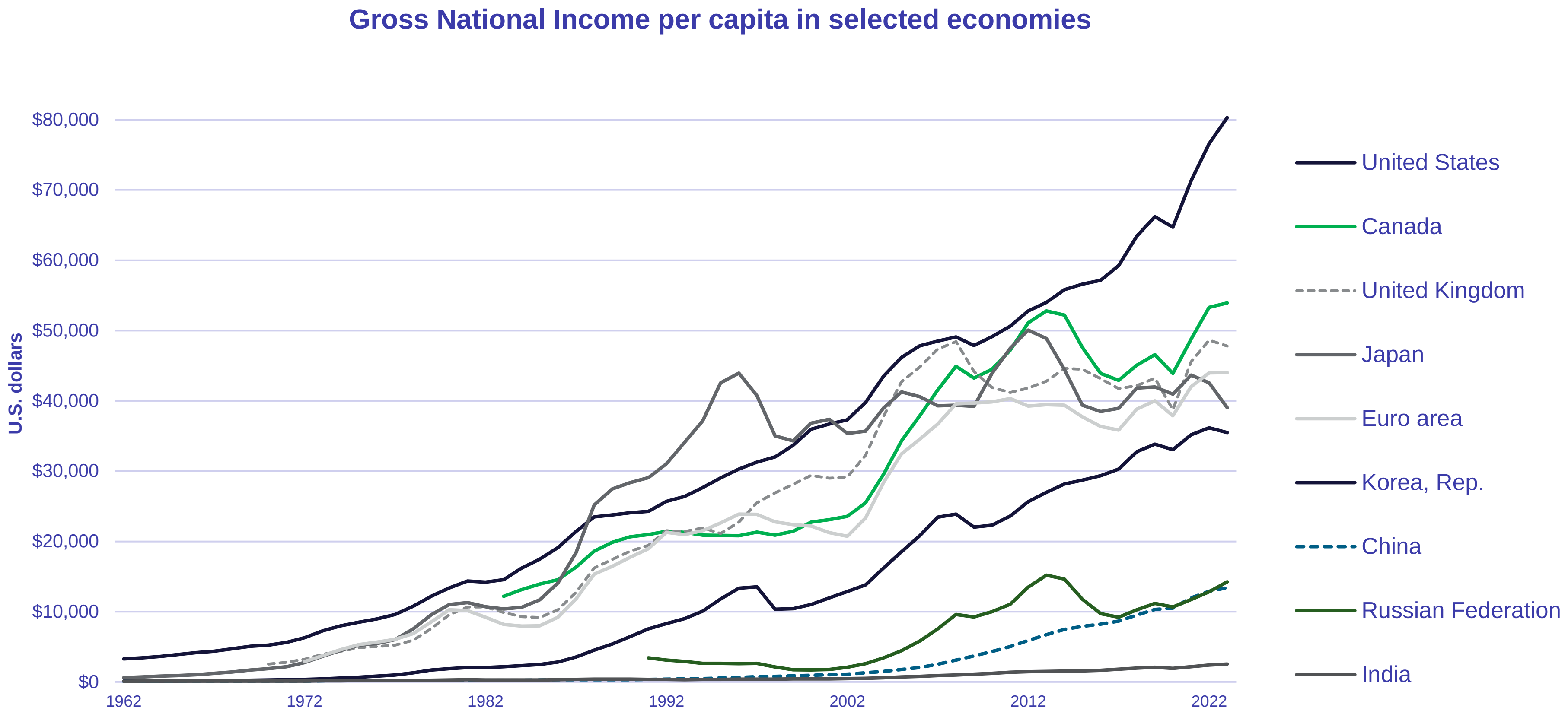
04 Growth in Q4 will be tempered by hurricanes, resulting in a deceleration to 2-2.5%

US best in class



Source: BEA, RSM US

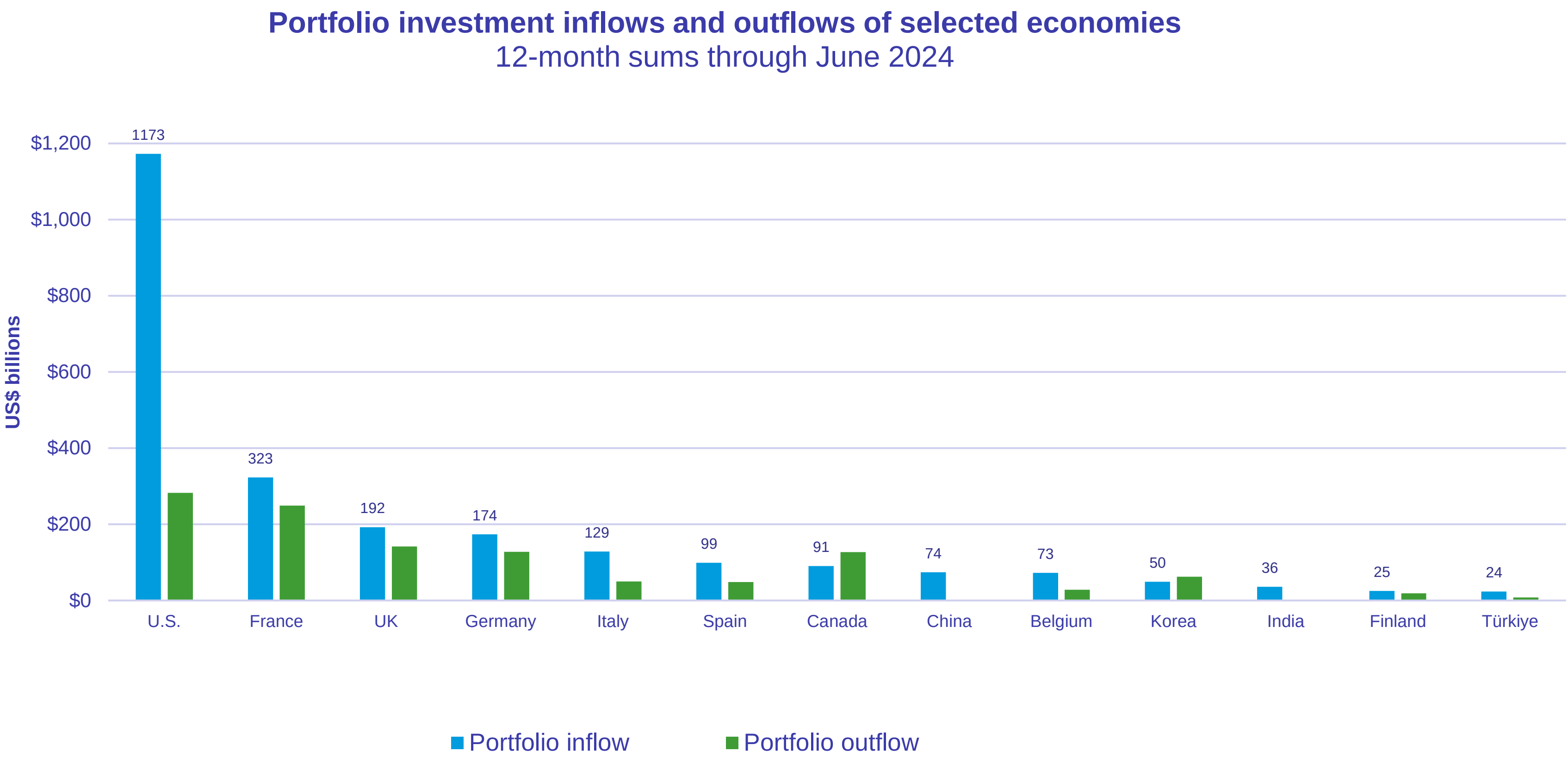
US best in class



Source: World Bank; RSM US LLP

Source: BEA, RSM US

Capital flows



Source: All except UK: OECD Monthly Capital Flow Dataset ; UK: RSM US LLP estimate

Source: BEA, RSM US

Employment outlook

01 Adjusting for downward revision of 112,000 jobs for Aug. and Sept., and modest 12,000 gain in Oct., there was a decline in total employment of 100,000

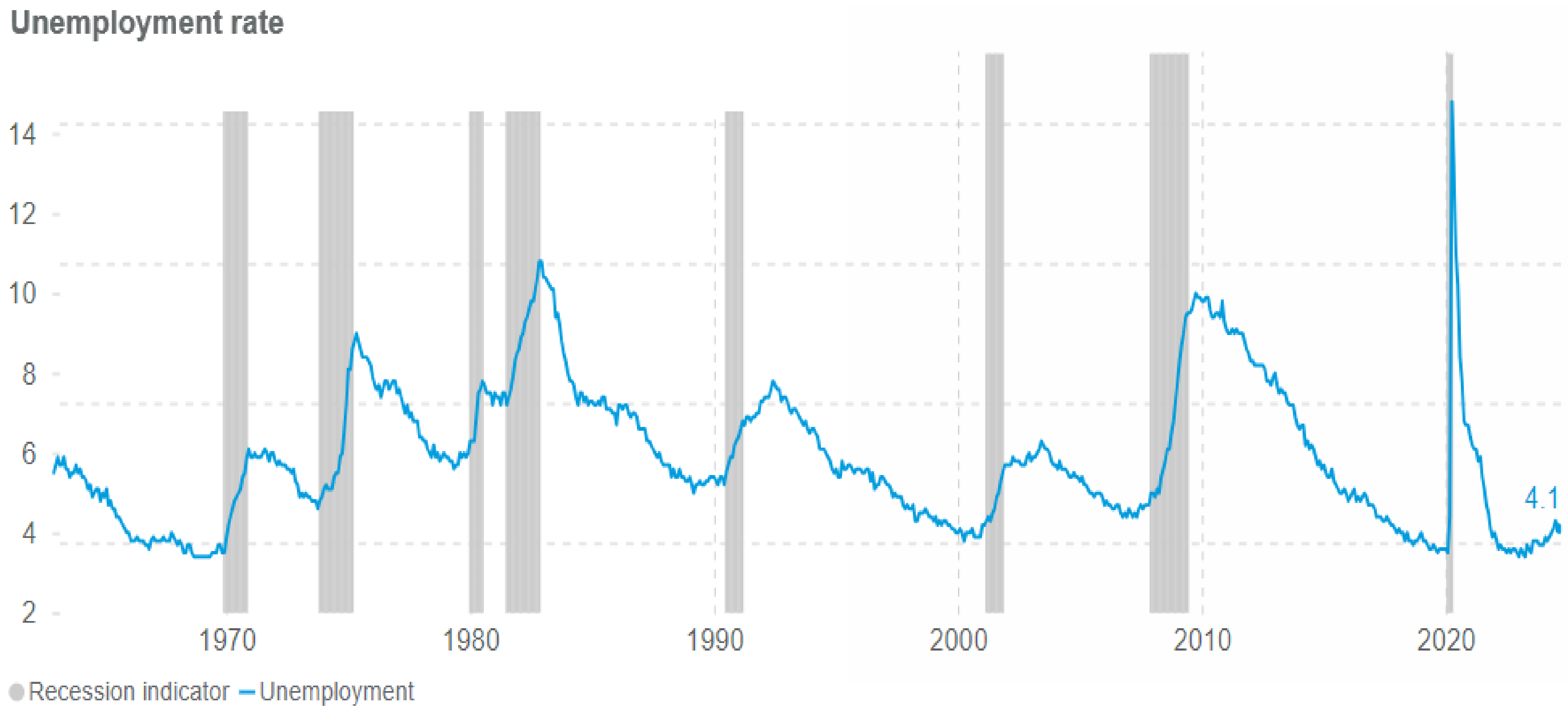
02 Do <u>not</u> over-interpret temporary factors driving top-line decline—two hurricanes and the Boeing strike

03 It will be early next year before we get a “clean” look at real condition of labor market

04 Will likely see strong rebound in November hiring post-hurricane; strong but still a slowdown and moderation from trend

Unemployment rate at 4.1% up from recent low of 3.4%

Driven by labor market normalization and the increase in labor supply



Source: BLS, RSM US

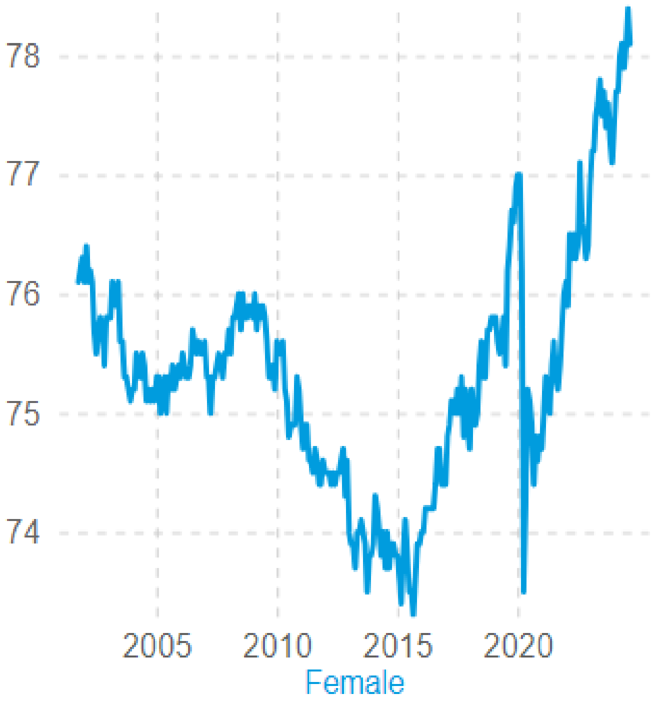
Prime-age participation rate at multidecade high

Driven mostly by female workers due to childcare improvement and hybrid work environment

Prime-age participation rate

Male workers

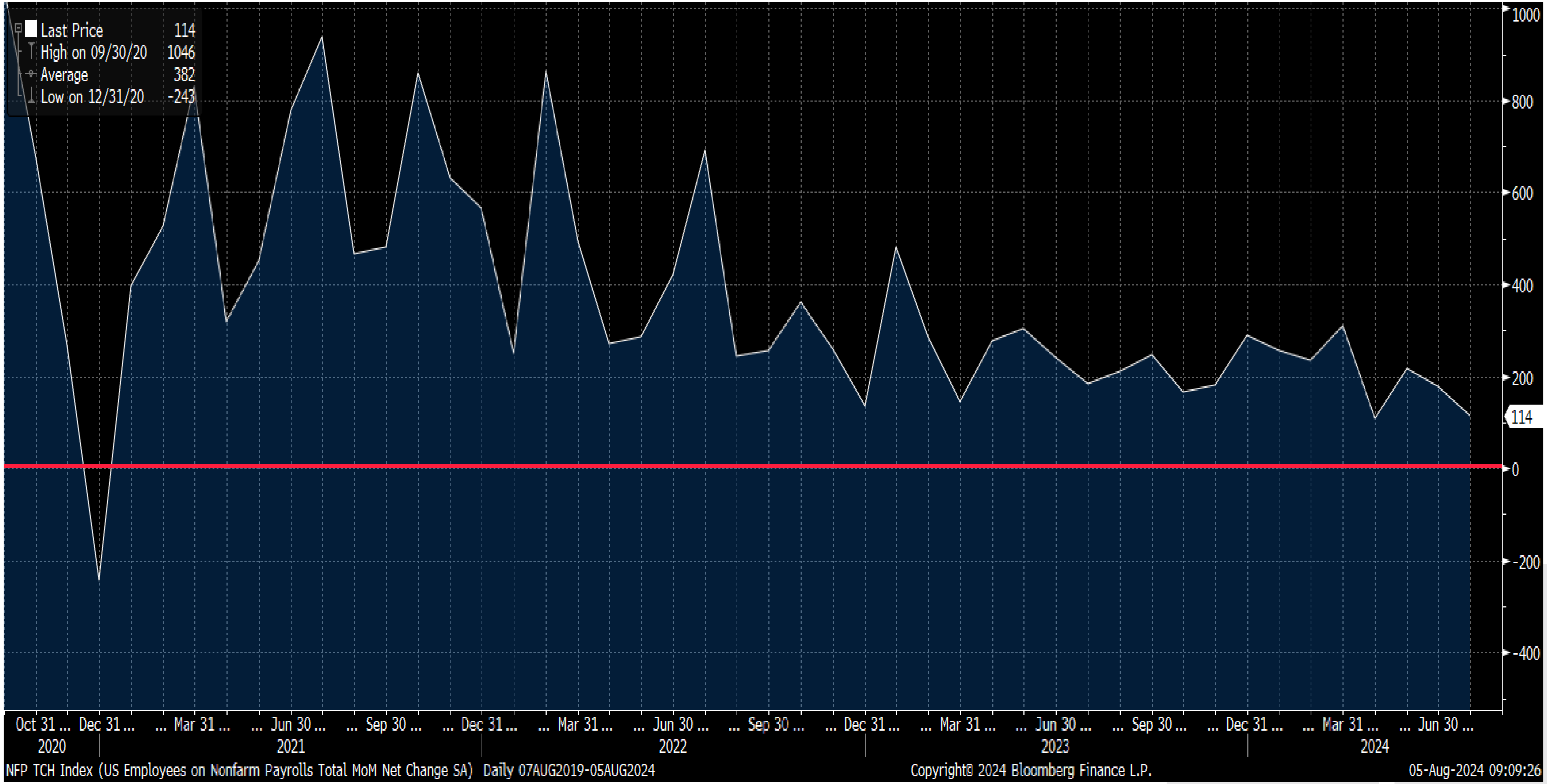
Female workers



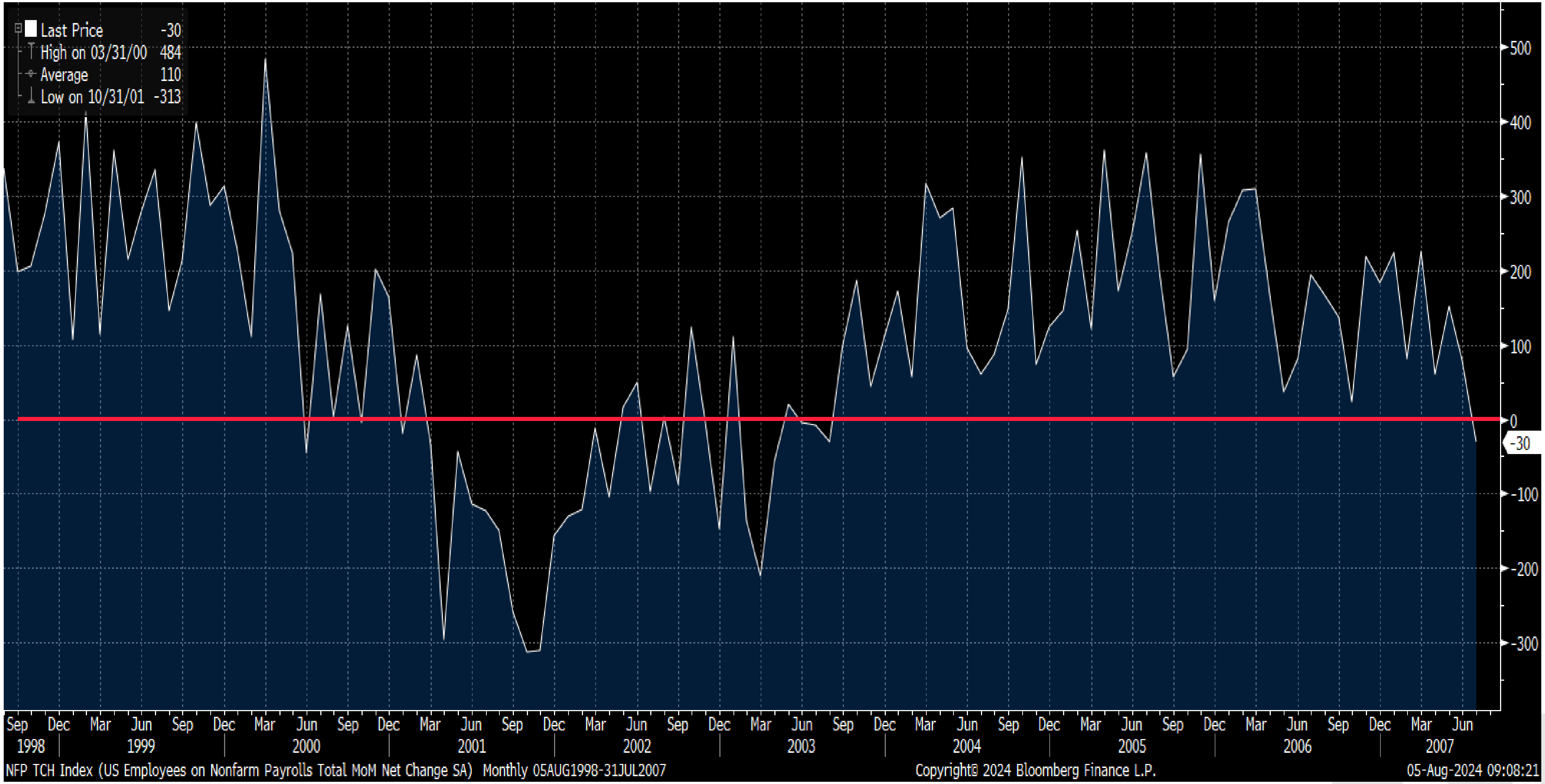
Source: BLS, RSM US

But we’re in a recession, right?

Monthly non-farm payrolls show moderating job *gains*



March 2001 to May 2002: 14 consecutive months of job *losses*



Inflation outlook: Price stability = Investment visibility

01 Fed's preferred inflation measure (Core PCE) will average around 2.2%, allowing for gradual interest rate cuts

02 Strong productivity gains should dampen inflationary pressures

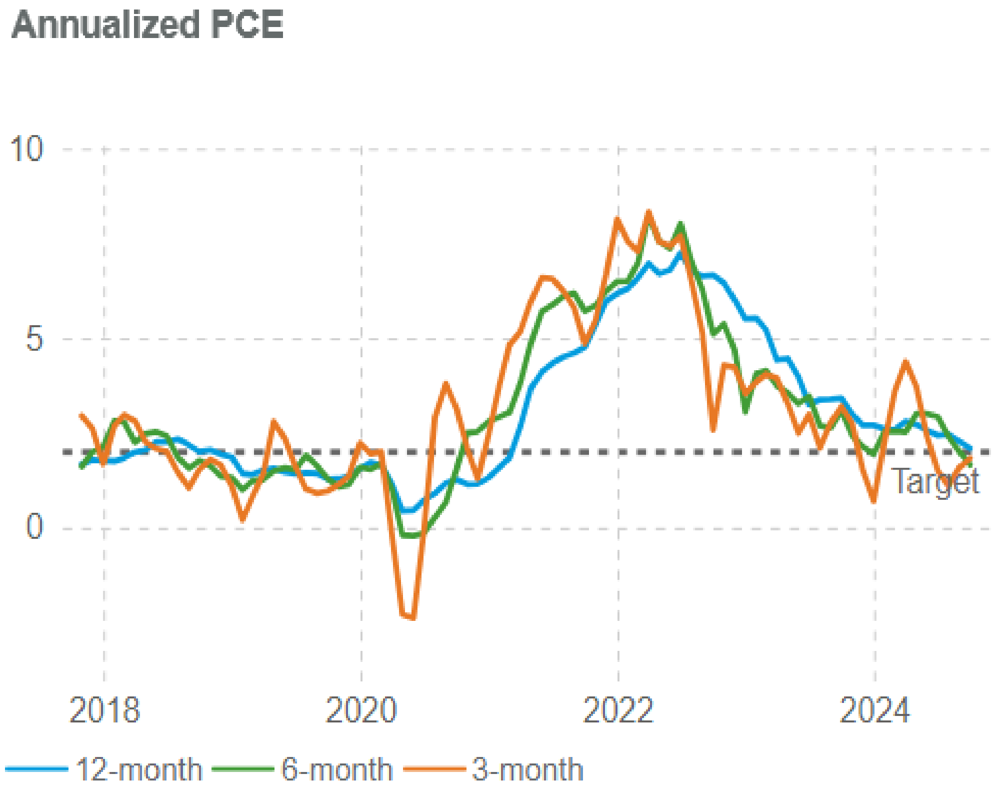
03 Wage growth solid: 3.9% employment cost index—the Fed's key gauge; demographics, immigration policy tilt risks higher

04 Overall inflation risks now balanced versus growth risks as Fed continues to cut rates

05 Trade and industrial policies will keep inflation 2.5% to 3% over the medium to long term

Annualized PCE

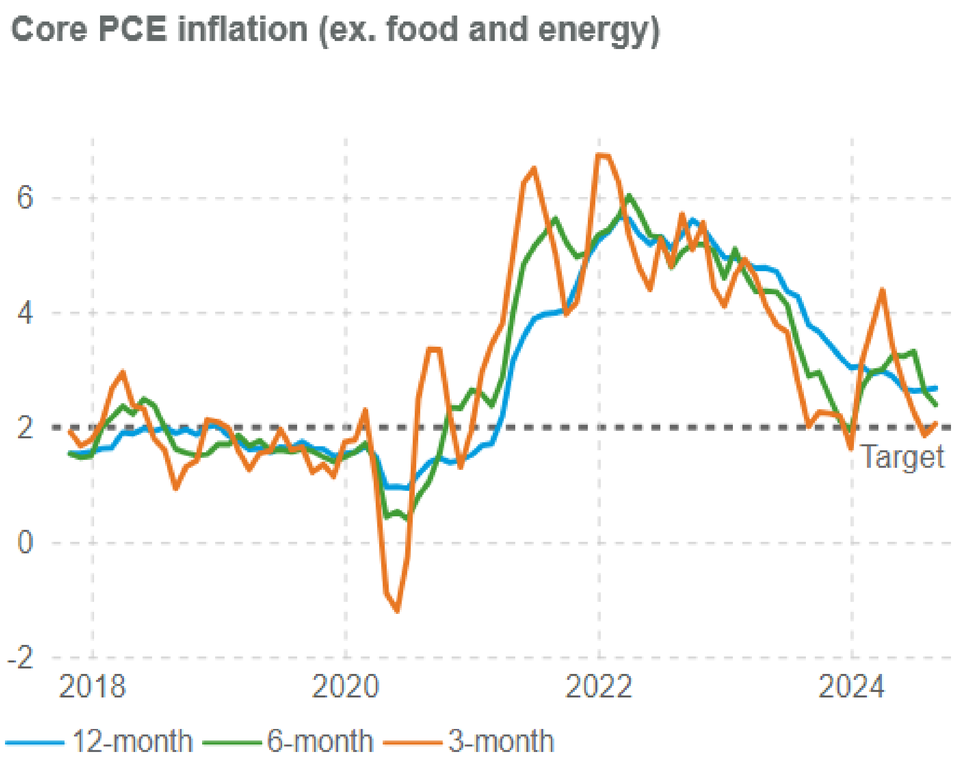
Short-term inflation is back at 2% target… for now

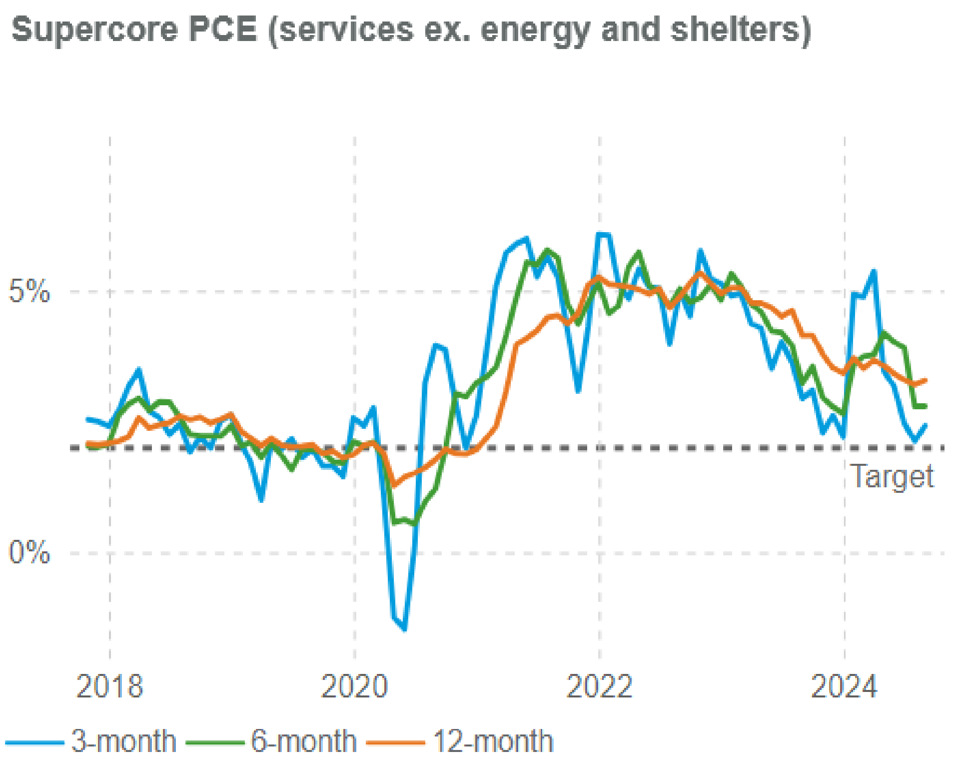


Source: BEA, RSM US

Underlying inflation remains higher than target

More aligned with our estimate that post-pandemic inflation should be between 2 to 2.5% due to structural changes



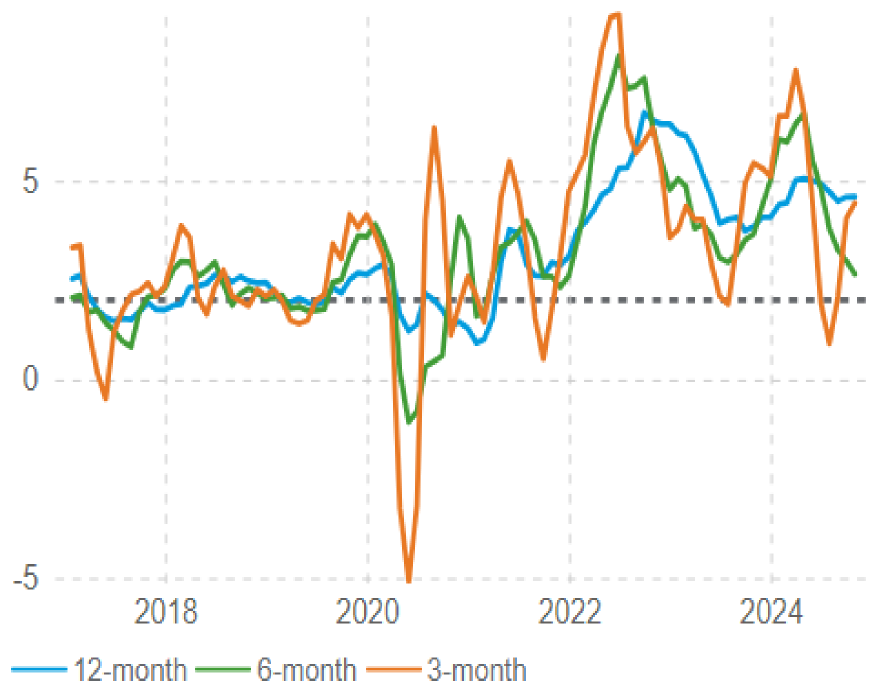


Source: BEA, RSM US

Super core inflation is back to target

Improvements are broad-based, with transportation services leading the declines

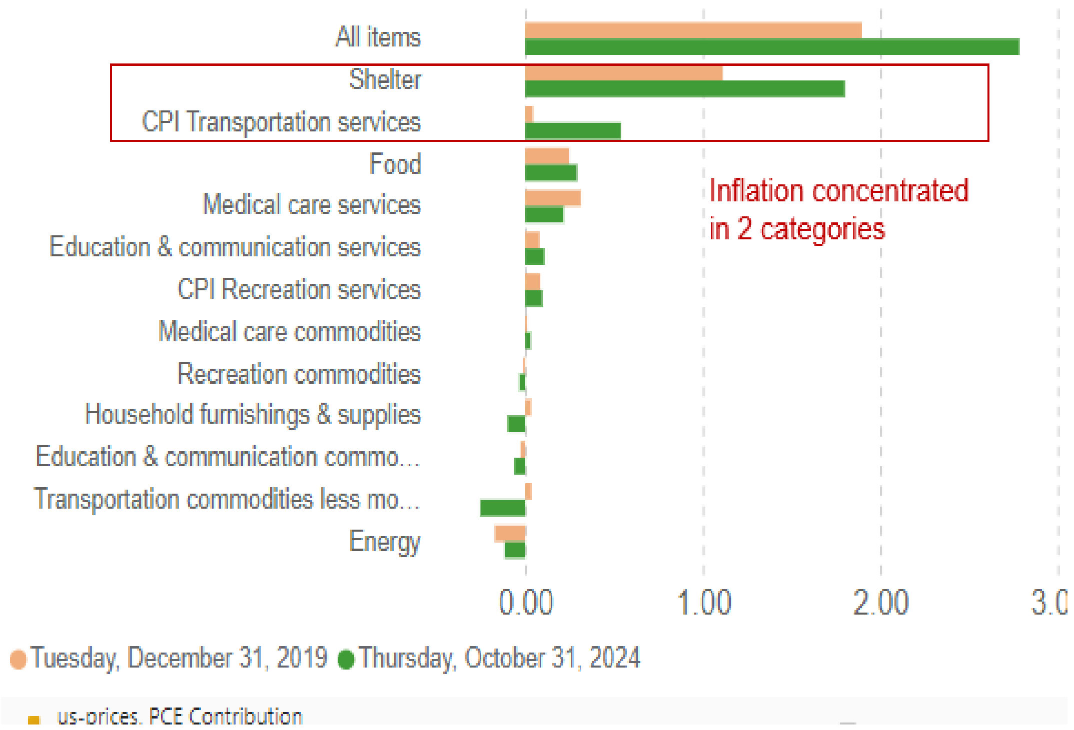
CPI inflation: Supercore



Source: BLS, RSM US

Component contribution to 12-month inflation

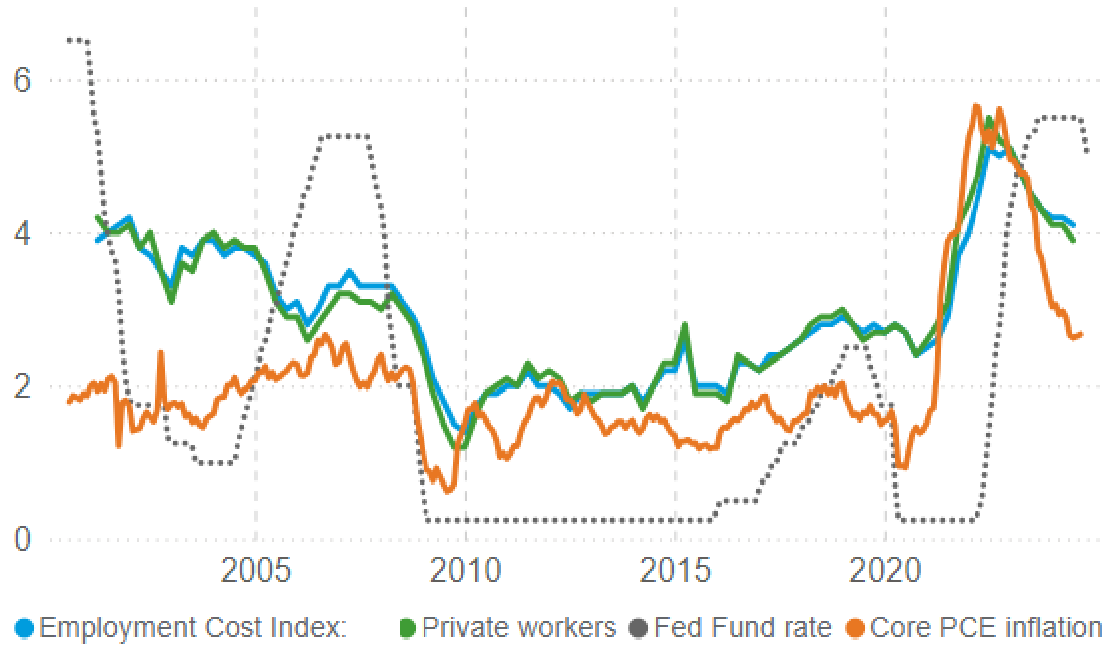
6-month moving average



Wage growth remains elevated due to tight labor market

Real wage turns positive as inflation comes down; support stronger spending

Employment cost index



Source: BLS, BEA, Federal Reserve, RSM US

Hourly wage growth, 12-month

Personal spending and income outlook

01 Consumers more resilient than expected, supported by strong labor market and rising real wages

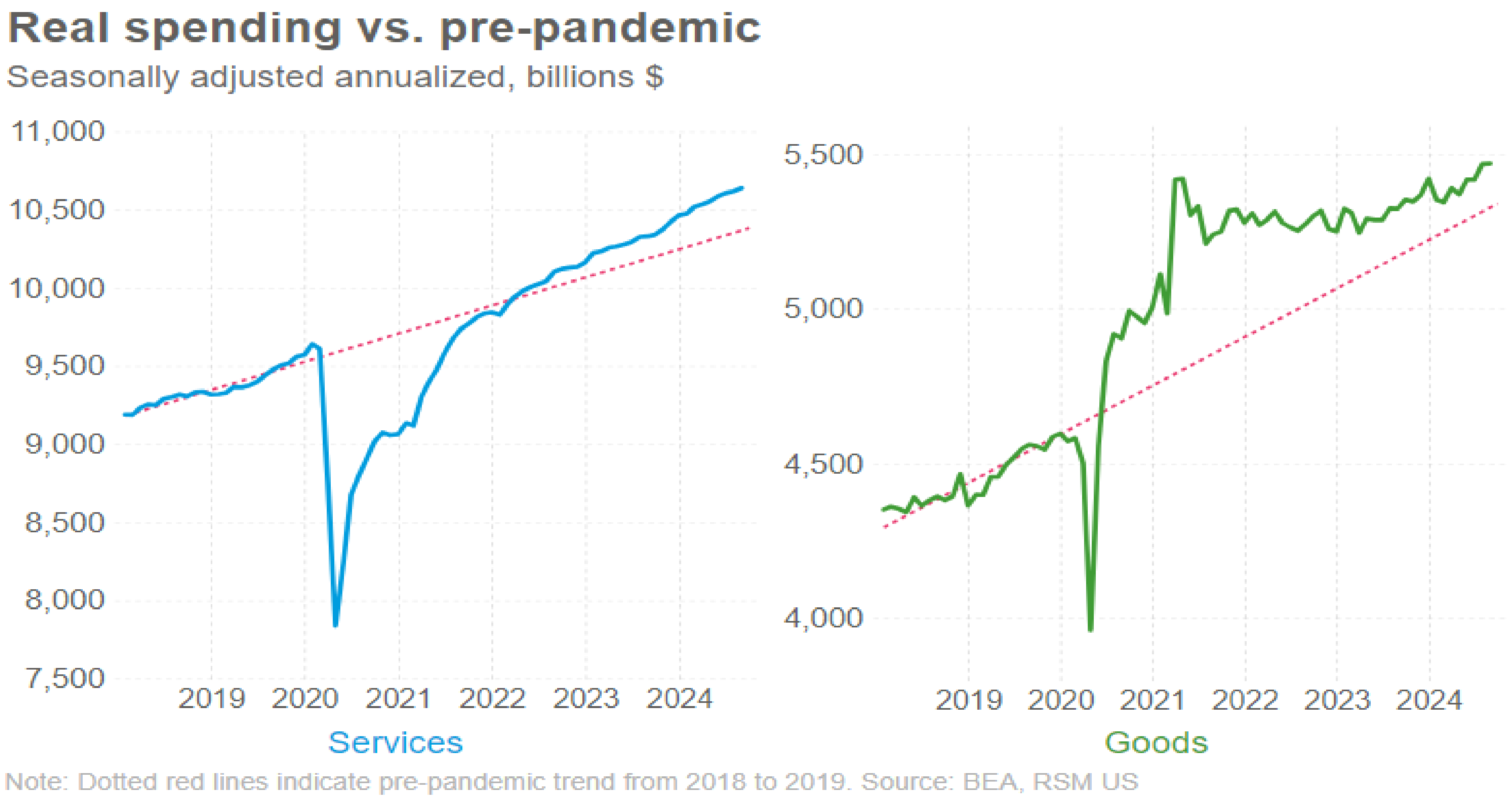
02 Personal spending on three-month average annualized basis increased at a 5.2% pace while savings rate eased to 4.6% from 4.8%

03 Beware of “The Consumer is Dead” mantra; there is no such thing as a monolithic The Consumer

04 Consumer confidence has picked up in last 6 months as inflation eases, slowly catching up with hard data on demand

Service spending back to trend, support overall spending

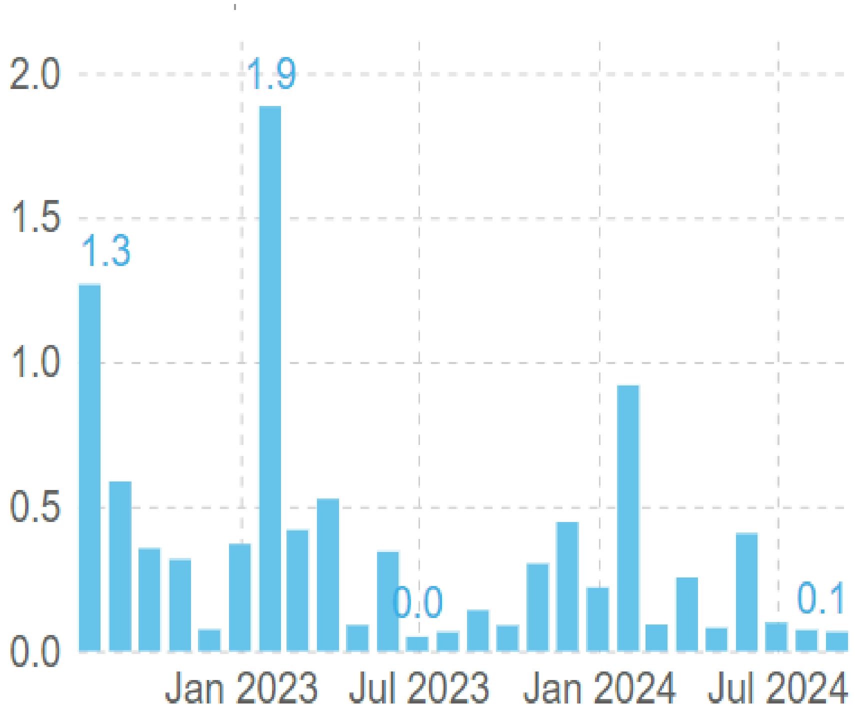
Pent-up demand for goods especially durable goods has been a drag



Income stays solid due to strong labor market

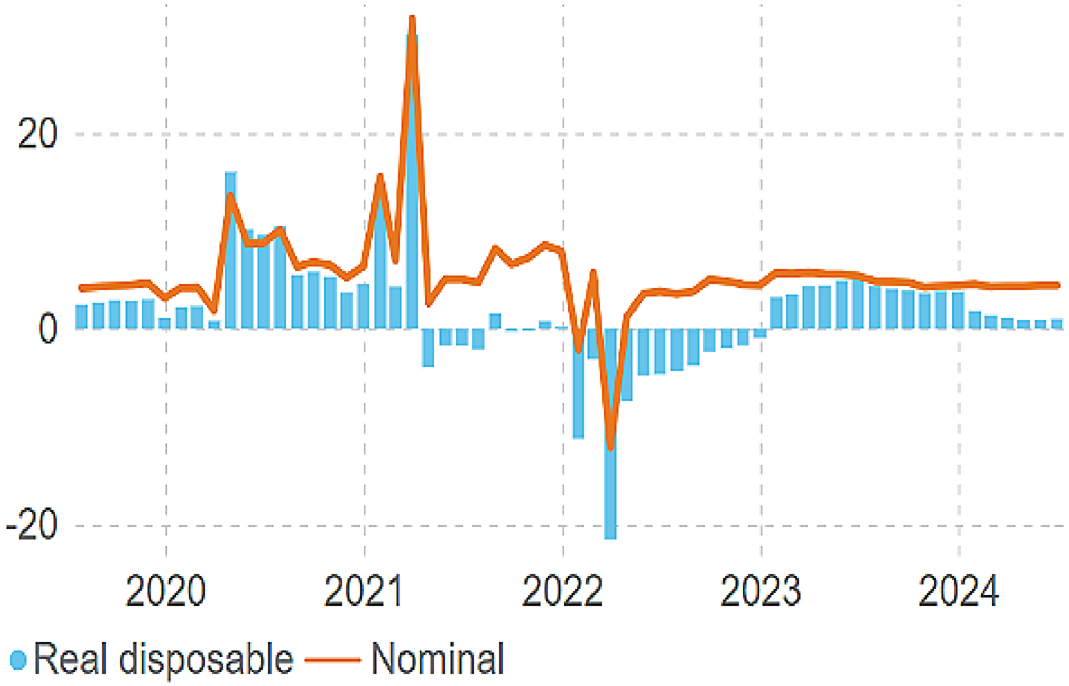
Income outgrows prices as inflation subsides

Real disposable income monthly change



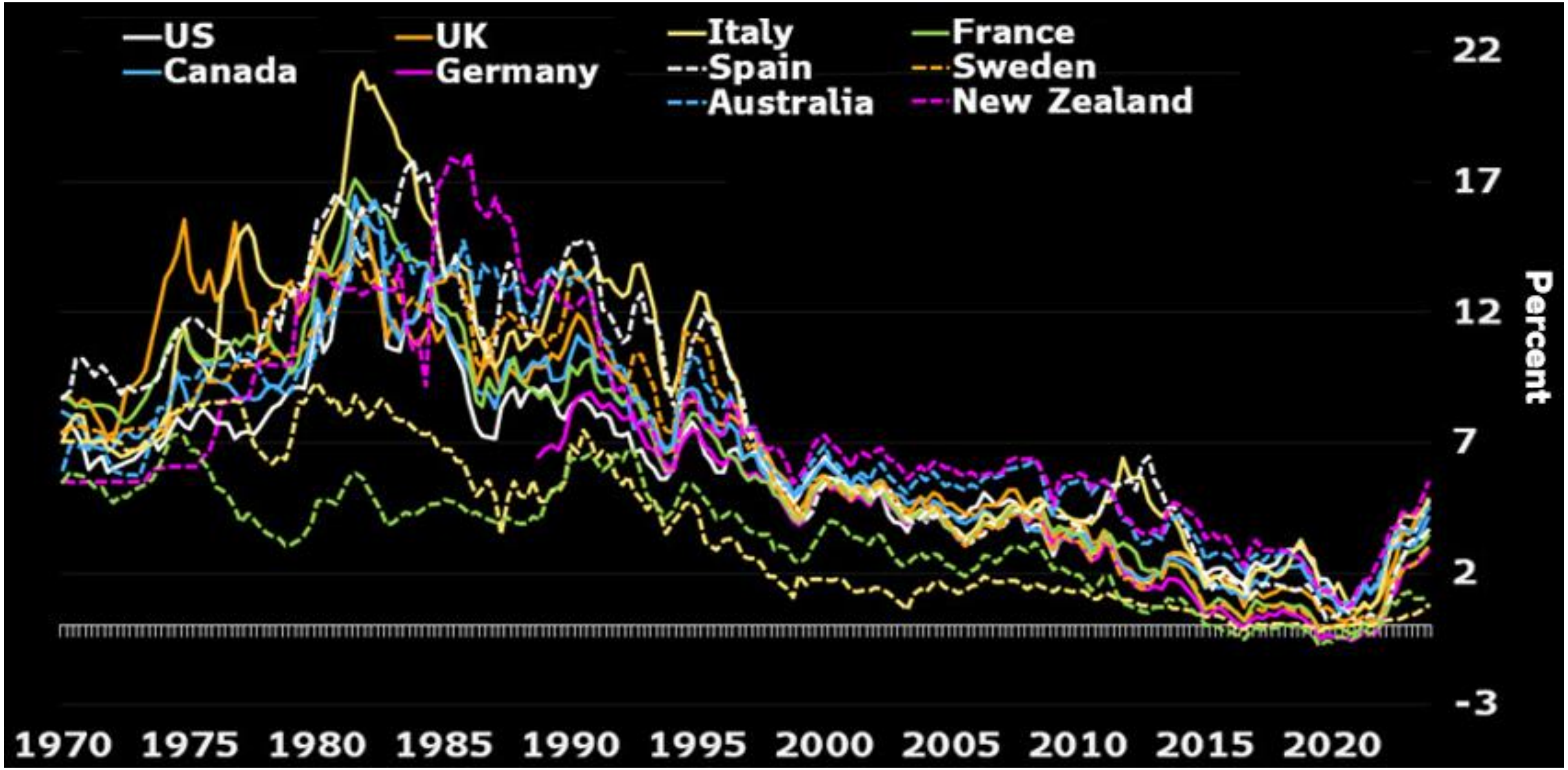
Source: BEA, RSM US

Year-over-year change in income



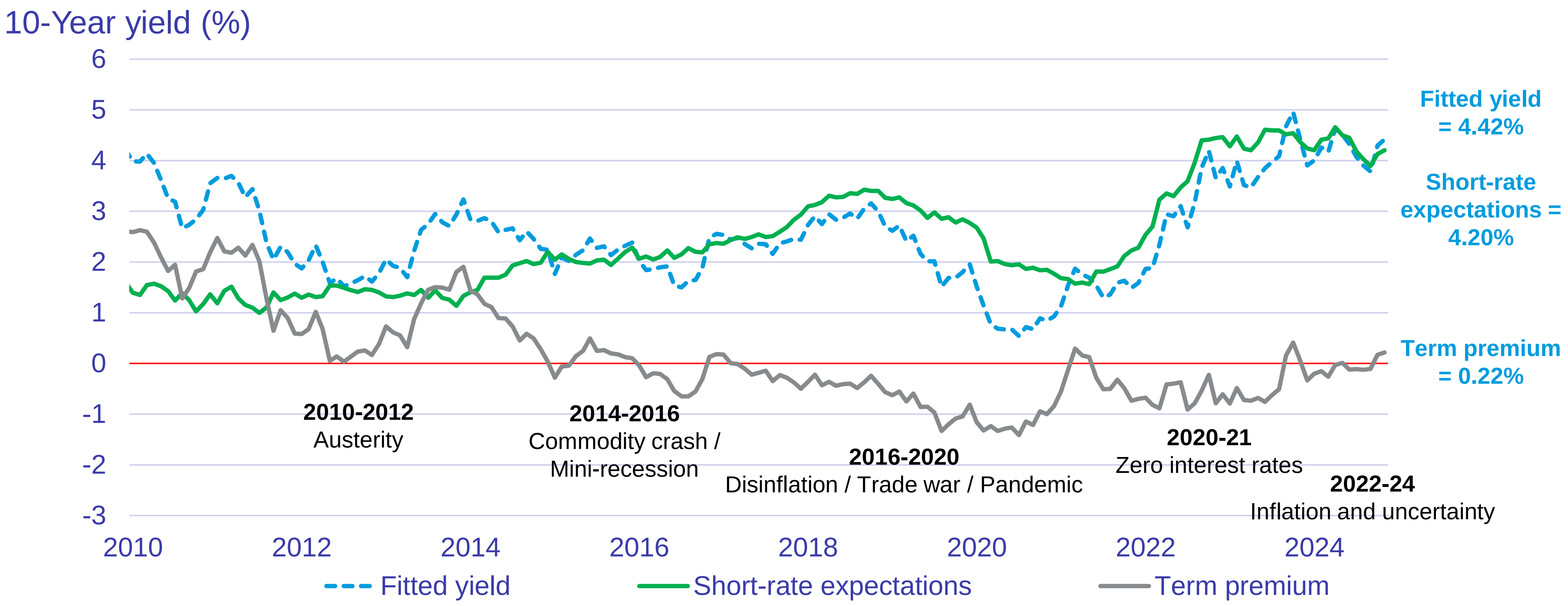
What does “higher for longer” mean?

Why no one really believes “higher for longer”



Signs of return to normalcy: A positive term premium

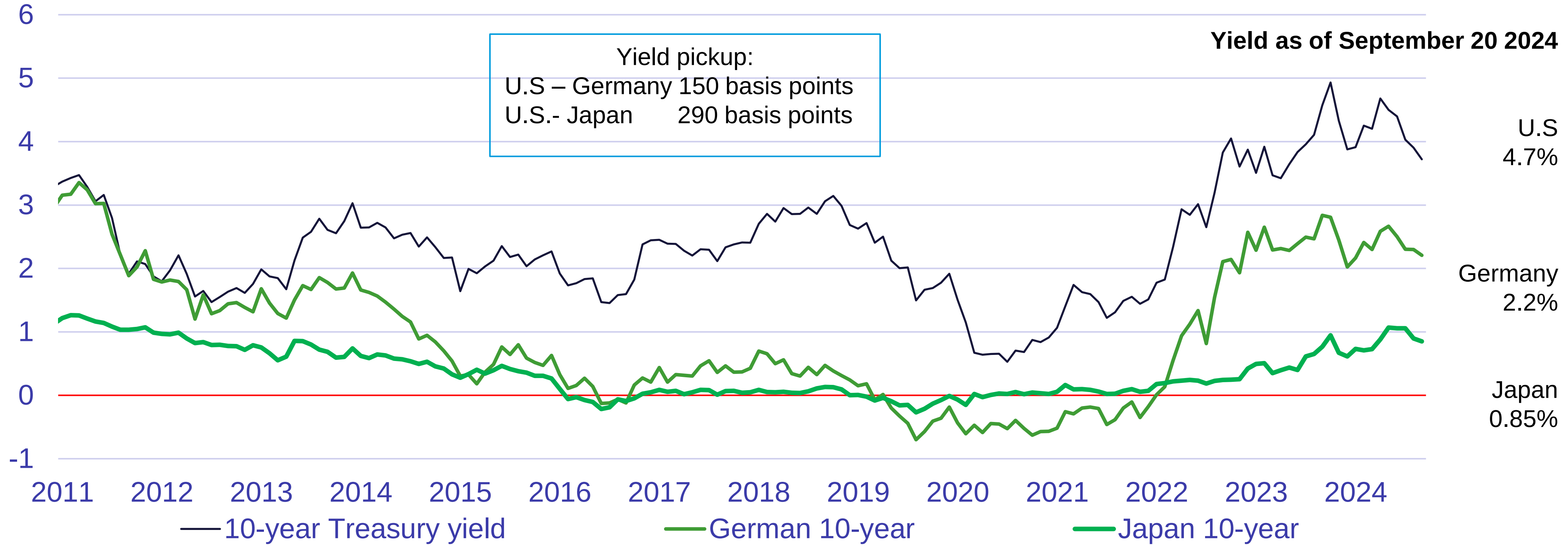
10-year yields determined as the sum of expectations for the Fed funds rate plus a term premium for holding a bond over its maturity



Source: Adrian, Crunch and Moench; NY Fed; Bloomberg; RSM US LLP

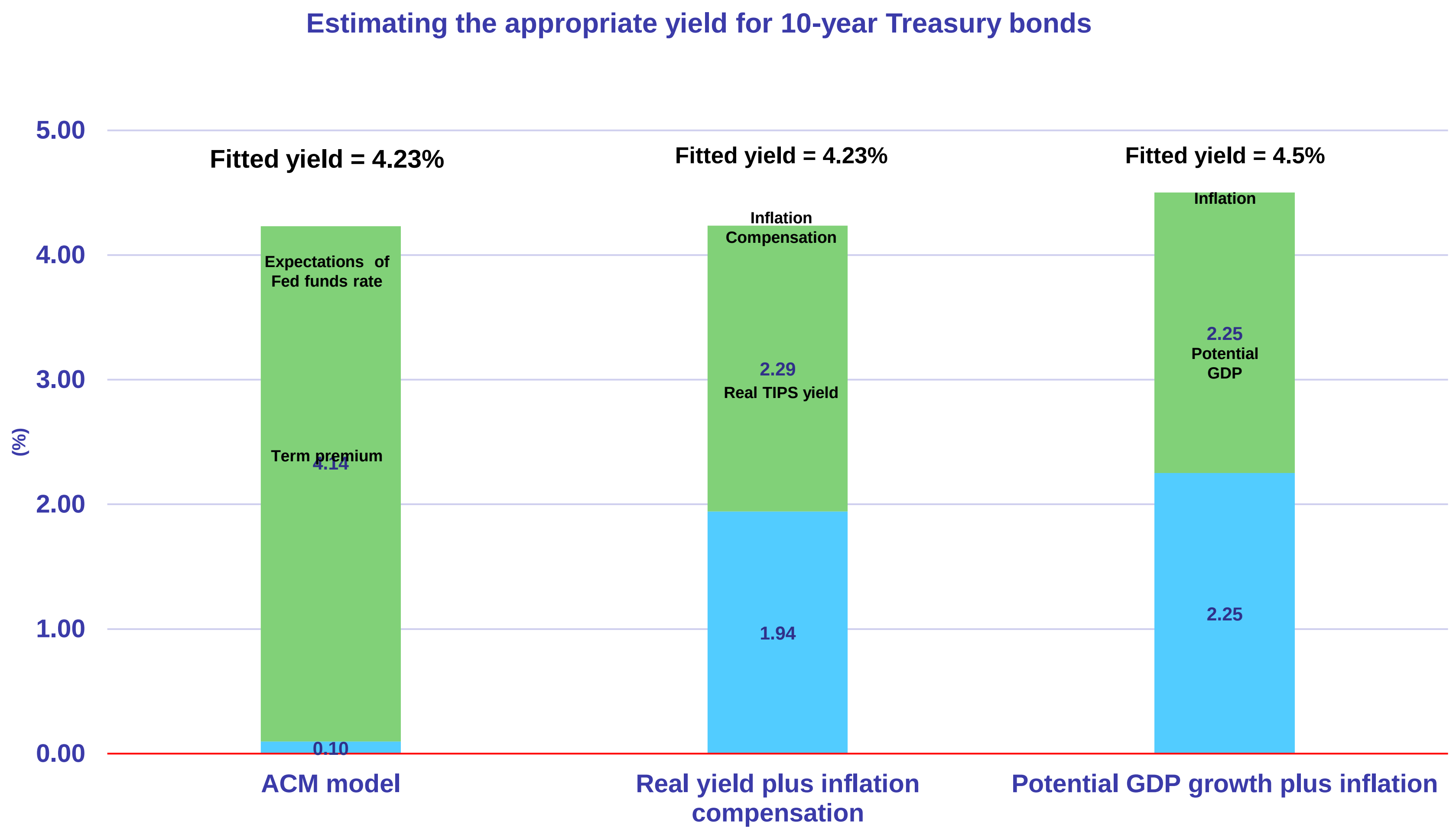
U.S. 10-year Treasuries continue to be attractive relative to government bond in other financial centers.

10-year government bond yields in the U.S., Germany and Japan (%)



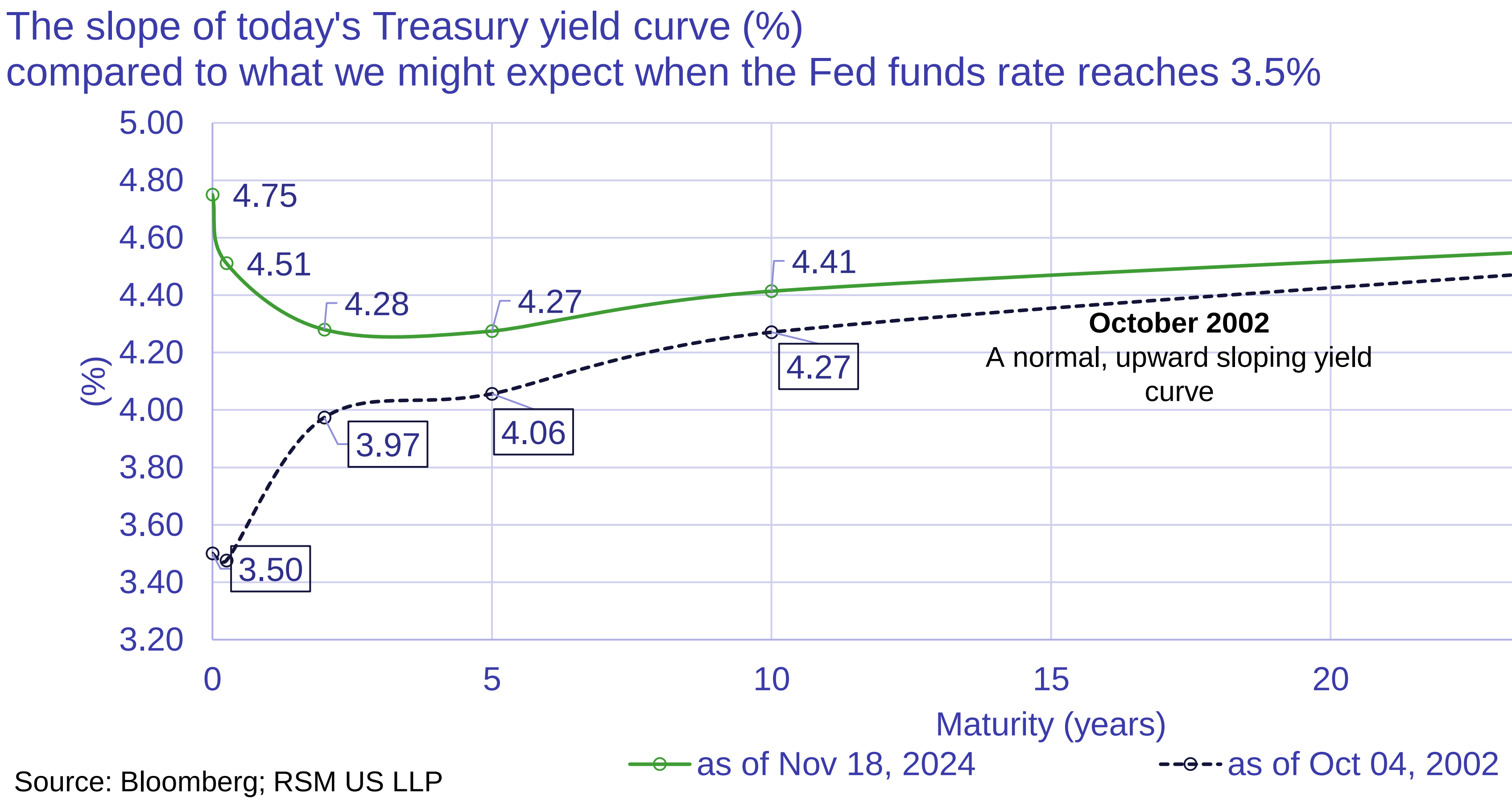
Source: Bloomberg; RSM US LLP

Estimating term premium: Three models



Source: Bloomberg; RSM US LLP calculations

Today's yield curve and what we might expect as the Fed funds rate moves toward a terminal rate of 3.5%

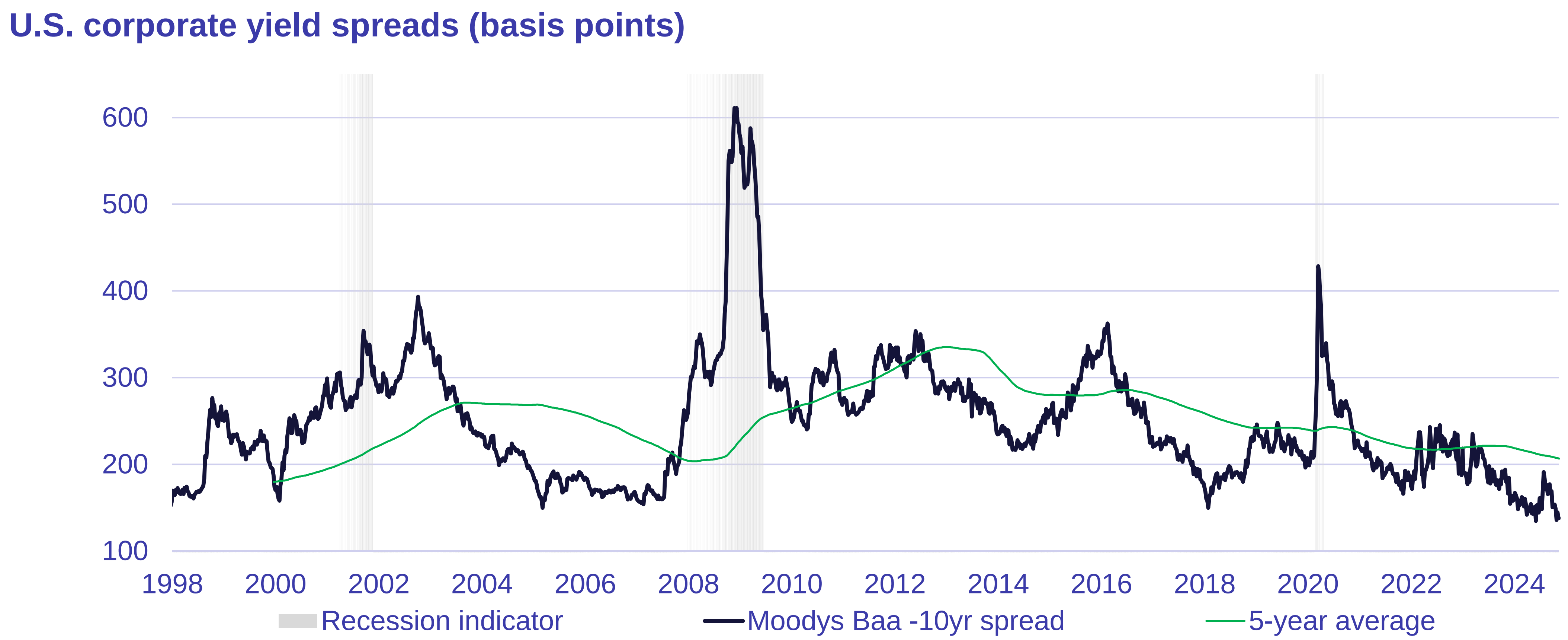


Source: Bloomberg; RSM US LLP

Corporate bond market

- 2024 will end as a banner year for issuance of corporate debt
- Foreign and domestic investors continue to find corporate debt attractive

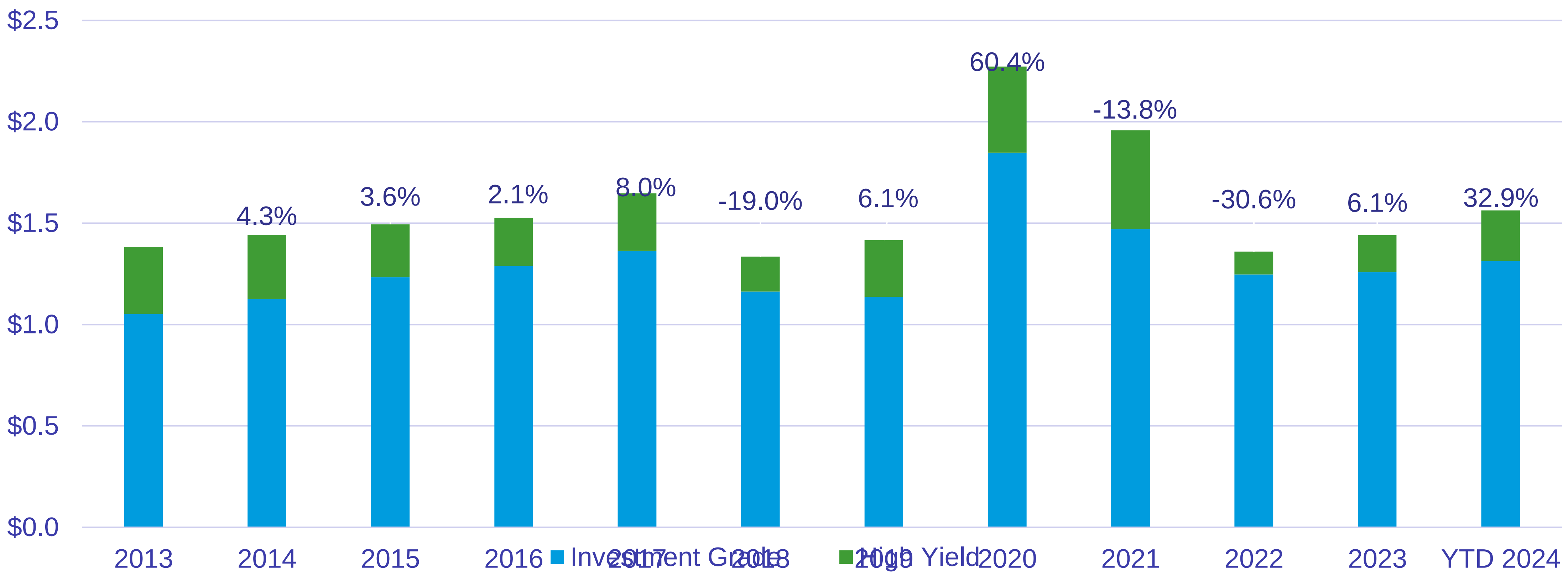
Long-term decline in credit spreads



Source: Bloomberg; RSM US LLP

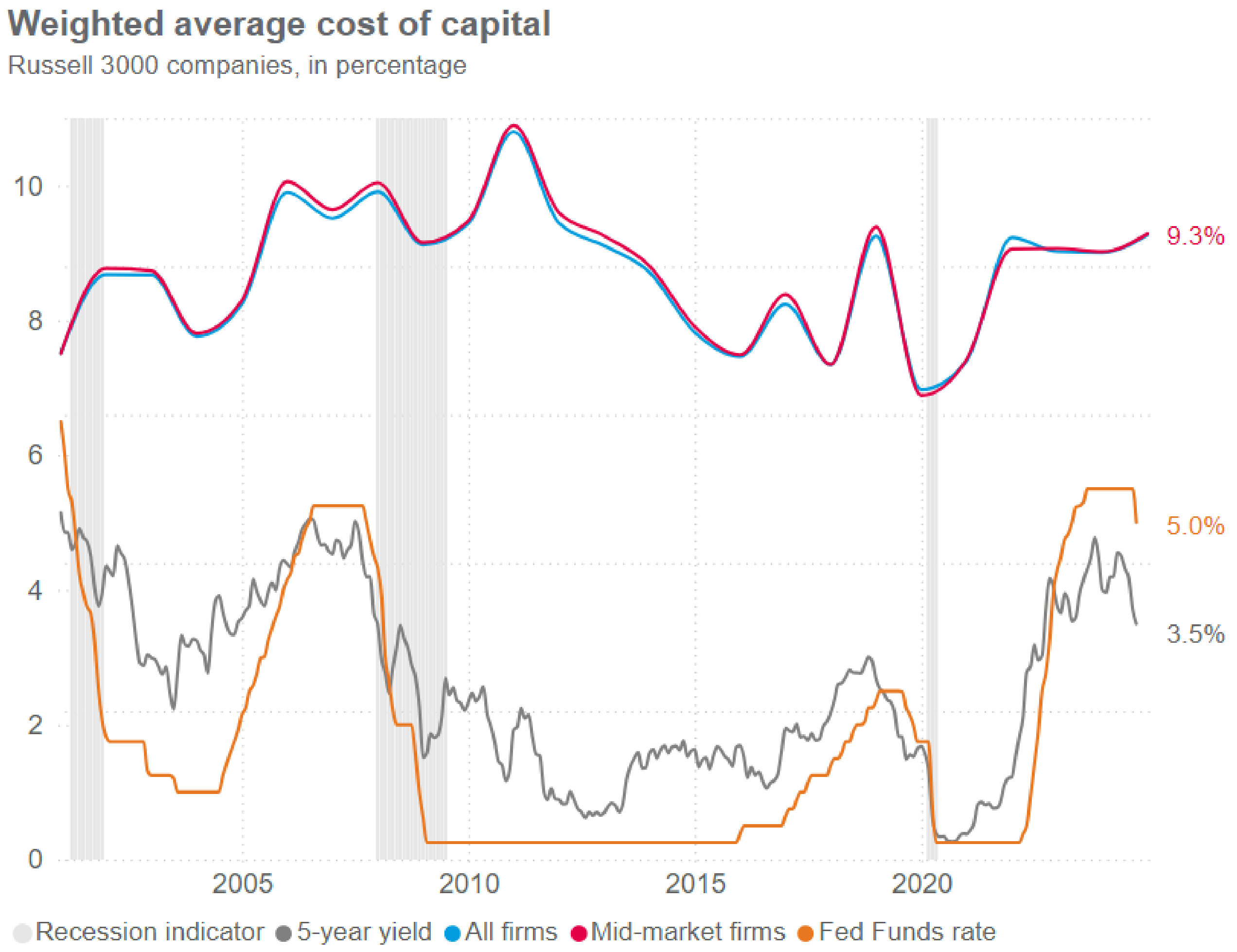
2024 looks to be a banner year for corporate issuance

Issuance of U.S. corporate debt and increase from prior year (US$ trillions)



Source: SIFMA; RSM US LLP

Middle Market Weighted Average Cost of Capital

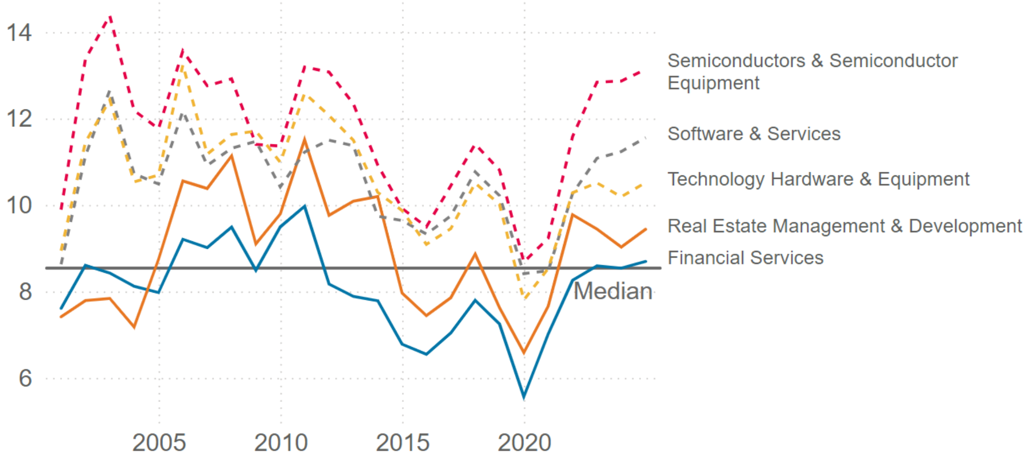


Source: Bloomberg, RSM US

Middle Market Weighted Average Cost of Capitals

Weighted average cost of capital, middle market

Russell 3000 companies with revenue from $1 to $10 billions; in percentage



Note: The median line indicates the median level for all industries. Source: Bloomberg, RSM US

Changes in weighted average cost of capital, middle market

Russell 3000 companies with revenue from $1 to $10 billions

Rank	Industry	Pct change 16-24	Pct change 20-24	Pct point change 16-24	Pct point change 20-24
1	Semiconductors & Semiconductor Equipment	25.77%	42.29%	2.69	3.90
2	Financial Services	23.47%	23.89%	1.65	1.68
3	Real Estate Management & Development	20.16%	23.19%	1.58	1.78
4	Health Care Equipment & Services	19.98%	23.42%	1.63	1.86
5	Utilities	19.80%	23.70%	1.12	1.30
6	Software & Services	18.56%	36.27%	1.81	3.08
7	Consumer Durables & Apparel	17.63%	0.64%	1.42	0.06
8	Telecommunication Services	16.20%	48.57%	1.10	2.57
9	Consumer Discretionary Distribution & Retail	15.06%	14.31%	1.17	1.12
10	Automobiles & Components	13.07%	20.46%	1.13	1.66
11	Media & Entertainment	11.98%	34.43%	0.99	2.37
12	Technology Hardware & Equipment	11.28%	23.27%	1.07	1.99
13	Consumer Services	9.16%	7.08%	0.71	0.56
14	Capital Goods	8.92%	20.79%	0.79	1.67
15	Banks	6.33%	11.24%	0.44	0.75
16	Transportation	6.18%	31.90%	0.50	2.09
17	Materials	6.03%	15.55%	0.51	1.20
18	Commercial & Professional Services	4.81%	18.36%	0.40	1.37
19	Household & Personal Products	3.21%	5.46%	0.24	0.41
20	Insurance	2.75%	3.57%	0.21	0.27
21	Food, Beverage & Tobacco	2.08%	19.56%	0.14	1.15
22	Pharmaceuticals, Biotechnology & Life Sciences	1.76%	43.08%	0.19	3.36
23	Energy	-3.94%	30.68%	-0.34	1.97
24	Consumer Staples Distribution & Retail	-6.75%	150.66%	-0.53	4.37
25	Equity Real Estate Investment Trusts (REITs)	-7.38%	17.29%	-0.61	1.13

Source: Bloomberg, RSM US

What could go wrong?

Negative risks to the outlook

01 Inflation re-accelerates, keeping Fed hawkish

02 Geopolitical tensions causing oil prices to move much higher

03 Maturity wall of debt in corporate sector and commercial real estate

04 Small and regional banks nonperforming debt

05 Tariffs and trade wars; policy uncertainty

What could go right?

Take everything from 2009 to 2019 and turn it upside down

Positive risks to the outlook

01 Price stability = investment visibility

02 Fiscal stimulus through tax cuts and reduced regulations

03 Consumer spending remains robust

04 Capex and productivity gains accelerate

Quarterly forecasts

Averages	1Q 2024	2Q 2024	3Q 2024	4Q 2024	1Q 2025	2Q 2025	3Q 2025	4Q 2025	Avg. 2024	Avg. 2025	Avg. 2026
Real GDP SAAR%	1.4%	3.0%	2.8%	2.5%	2.2%	2.5%	2.6%	2.7%	2.7%	2.5%	2.5%
Consumer Spending SAAR%	1.5%	2.9%	3.7%	2.8%	2.5%	2.7%	3.0%	3.2%	2.8%	3.0%	2.6%
PCE Price Index YOY%	2.6%	2.6%	2.3%	2.3%	2.2%	2.2%	2.2%	2.2%	2.4%	2.2%	2.2%
PCE Core Price Index YOY%	2.9%	2.7%	2.7%	2.5%	2.5%	2.4%	2.3%	2.3%	2.7%	2.4%	2.3%
Private Investment SAAR%	4.4%	7.5%	0.3%	1.5%	2.0%	2.5%	3.0%	3.7%	1.7%	2.5%	2.5%
Unemployment Rate	3.8%	4.0%	4.2%	4.2%	4.3%	4.2%	4.1%	4.1%	4.2%	4.2%	4.0%
Avg Monthly Payrolls (,000)	267	147	185	120	120	120	120	120	140	120	
CPI (Year-Over-Year Ago %)	3.3%	3.2%	2.6%	2.3%	2.3%	2.3%	2.3%		2.7%	2.3%	2.3%
Industrial Production YoY%	-0.5%	0.1%	-0.4%	1.00%					0.50%		
Fed. Fund Rate, upper bound	5.5%	5.5%	5.0%	4.5%	4.25%	4.0%	3.75%	3.5%			
10-year Note	4.20%	4.40%	3.8%	4.4%	4.5%	4.5%	4.5%	4.5%	4.1%	4.5%	4.5%

**Red indicated actual data*