

High Income Consumers and AI Investments Fuel Growth

This report is excerpted from the Fourth Quarter 2025 Fixed-Income Sector Views.

Housing, labor market, and lower income households face challenges.

U.S. economic growth found its footing after decelerating earlier this year, supported by a recovery in consumption and robust investment in AI. Reduced uncertainty and a rebound in financial markets helped consumption recover, particularly for high income households. AI-related investment has been a significant contributor to real GDP growth, even with official data likely understating the gains. Recent data looks relatively robust, prompting upward revisions to third-quarter GDP estimates.

That said, the labor market remains a key risk, as job creation has slowed from a three-month average of 176,000 in January 2024 to just 29,000 by August 2025, with gains narrowly concentrated in healthcare and government sectors. Slower immigration and increased retirements have tempered the impact of weaker job growth, resulting in just a modest rise in the unemployment rate to 4.3 percent in August. We expect it to continue rising gradually to around 4.5 percent by year end, driven mainly by labor force entrants struggling to find jobs rather than widespread layoffs. Risks are skewed toward a sharper rise in unemployment, particularly as the conclusion of the government’s deferred resignation program at the end of September could add up to 150,000 federal layoffs.

Looking ahead, we expect growth to stabilize at around 1.7 percent in 2025 and maintain a similar pace in 2026, supported by fiscal measures under the One Big Beautiful Bill Act (OBBBA), which

includes retroactive tax cuts that should lift personal tax refunds and provisions to broaden business investment. AI optimism and elevated asset prices are likely to sustain high income household consumption, though the economy remains bifurcated. Housing and lower income households continue to face challenges, with depressed home sales, subdued housing investment, and rising credit card and student loan delinquencies.

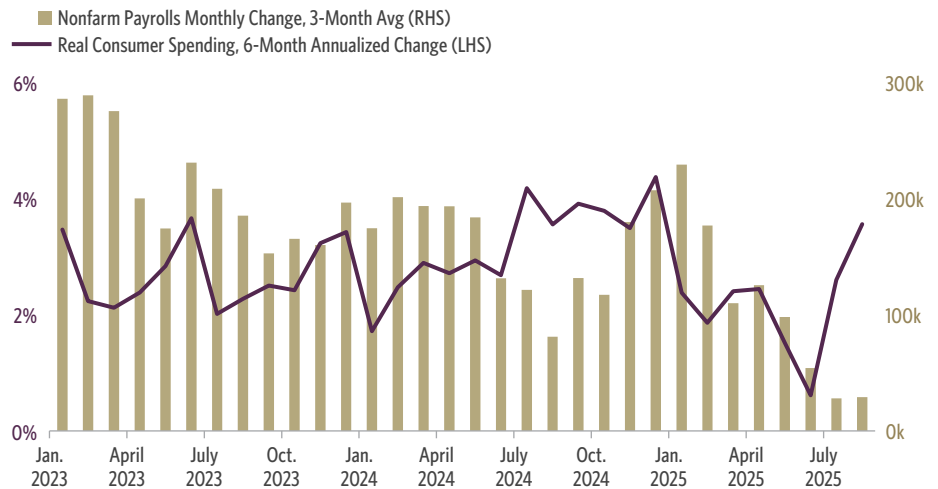
Inflation is expected to remain above target through early 2026, driven by tariff passthrough effects, before resuming a disinflationary trajectory. While actual tariff collections have lagged tariff rates due to delayed implementation and corporate mitigation measures, the administration is closing loopholes. We expect continued gradual tariff pass-through into consumer prices but see these as one-time price adjustments rather than persistent inflation.

The Fed is back in easing mode, implementing a “risk management” rate cut in September. While the prospect of above-target inflation remains a risk, Fed policymakers largely expect slower growth to weigh on inflation, and tariff passthrough to be temporary. Meanwhile, slightly higher unemployment has tilted risks to its dual mandate toward a softer labor market. We see the September rate cut as part of a recalibration, with two more cuts this year, and easing to neutral over the course of 2026.

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Consumer Spending Has Recovered but Job Creation Remains Weak



Source: Guggenheim Investments, Bloomberg. Data as of 8.31.2025.

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