

## US Outlook: growth revised up, but downside risks remain

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Our Focal Point series explores topical issues on macro, markets and investment

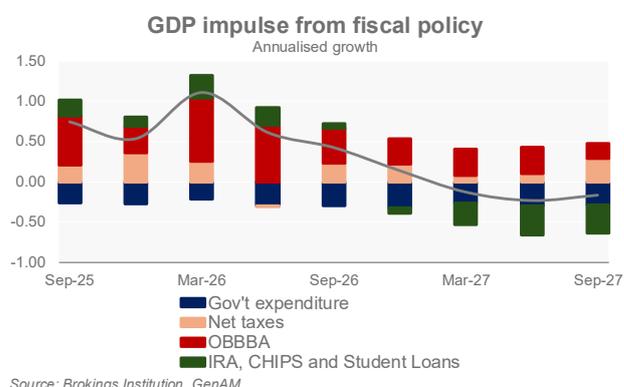
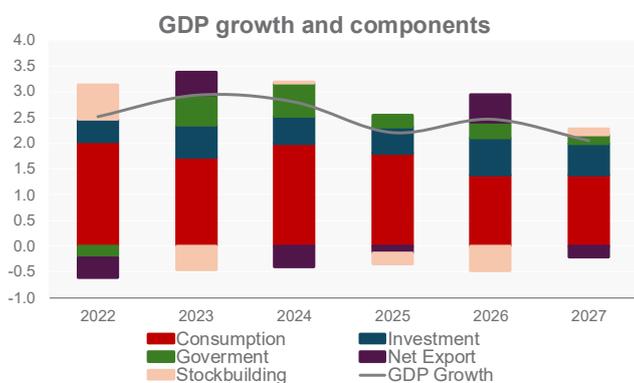
- We revise up to 2.5% our US growth forecast this year. Non-residential investment is going to play a leading role as non-AI-related capex will catch up thanks to tax cuts. Policy uncertainty remains a source of downside risk, and the contribution from easing financial conditions will be marginal as long rates remain high.
- Steady productivity growth will induce a retreat in inflation, but it is the mirror image of the “jobless growth” that will represent a liability for the Republicans in the November mid-term election.
- Consumption growth will moderate and become even more reliant on high income household and wealth effects. The unemployment rate will remain at around 4.5%.
- With annual inflation still at around 2.5% by year end and nonnegligible upward risks, the Fed will remain constrained on policy easing. We still see only one rate cut, likely delayed to June. Threats to its independence (and the volatility they create) will loom but the institutional safeguards remain strong.

Our forecast for US growth of 2.5% this year stands above the current consensus of 2.3%. This resilience is rooted in robust business investment, underpinned by favourable tax incentives. Strong productivity could lead to an even better performance, but downside risks are relevant. The K-shaped expansion evident in 2025 is set to continue, and overall growth will remain unusually fragile. The disconnect between strong GDP growth and sluggish job gains will keep unemployment at elevated levels. In this environment, higher-income households stand to benefit from strong—though potentially volatile—equity-driven wealth effects, which are now propelling much of consumer spending.

## Easing Headwinds...

The start of the year has seen a spike in policy uncertainty originating from the US administration, but several of the headwinds that characterised 2025 are expected to turn neutral or even positive in 2026:

- **Tariffs:** The disruptive tariff hikes are now behind us. Risks remain, as shown by the recent temporary threat of tariff on European countries over US' Greenland claims. But in our base case we expect some relief, particularly as the administration recognises that higher prices on prominent goods could become a political liability with the November mid-term election approaching. Additionally, an upcoming Supreme Court decision is expected to reduce certain restrictions and limit future presidential tariff powers, which should promote supply chain stability, reduce uncertainty, and ease import costs.
- **Fiscal Policy:** The fiscal stance is shifting decisively towards stimulus. The “One Big Beautiful Bill” tax package, effective January 2026, reduces individual taxes—particularly for higher-income households—and introduces new tax incentives, especially for capital expenditure. This represents a significant fiscal impulse, likely to be frontloaded in the first half of the year, potentially adding up to 0.8 percentage points to annualised GDP.
- **Financial Conditions:** Conditions have improved, with interest rates retreating from their peaks, credit spreads remaining low, and a positive outlook for the stock market. However, the impact on economic growth is expected to be limited. As inflation flattens out, the Federal Reserve is likely to implement only one further rate cut, and ongoing concerns about fiscal imbalances and erratic policymaking will be reflected in risk premiums. Recent government efforts to reduce mortgage rates through increased purchases of mortgage-backed securities are unlikely to have a substantial effect; our model simulations suggest that even a 100-basis point drop in the 30-year mortgage rate would boost GDP by just 0.1%.



### ...matched by visible productivity gains

Recent data suggest the US economy has entered a period of higher productivity growth, with nonfarm business output per hour rising by about 2.1% annualized over 2023–2025—a rate not seen since the late 1990s. While it is too early to attribute this entirely to AI, it likely reflects a persistent cyclical response to post-pandemic labour shortages and wage pressures, bolstered by low borrowing costs and fiscal support. Firms have invested in labour-saving technology, and improvements in work organisation (such as remote work) and faster business creation have also contributed. The combination of tax-driven investment and rapid AI adoption will make these productivity gains more persistent, and this constitutes a key upside risk to our growth outlook. However, policy headwinds—such as trade fragmentation, immigration restrictions, and crowding out of private investment by expanding deficits—will offset some of the benefits. As a result, we expect growth to revert quickly to a roughly 2% trend after 2026.

### Strong Business Investment, Led by AI...

Capital expenditure will remain the key growth driver in 2026, expanding by just over 4%. While AI-related investment led private non-residential investment growth in 2025, we anticipate a more balanced expansion this year, as non-AI investment rebounds with reduced policy headwinds and greater supply chain clarity encouraging manufacturers to invest. Fiscal incentives from the “OBDDA” bill, which allows full expensing of investments from 2026, will be a major factor. However, the concentration of investment in AI and other labour-saving technologies will mean that capital expansion will not be accompanied by significant increases in payrolls.

As a result, 2026 will likely see 2.5% GDP growth but only around 50,000 new jobs created per month. This is not due to higher productivity alone; the workforce is not growing rapidly—due to ongoing immigration curbs (which reduced the US population by 600,000–1.1 million in 2025, [according to the Dallas Fed](#)) and a [declining native-born participation rate](#). Reversing these trends would require substantial investment in retraining and reskilling, which is not aligned with current government labour policy. Additionally, firms that hired heavily in 2021–22 and retained staff through the 2023–25 slowdown may now increase output by utilising previously underused employees rather than making new hires. As such, low employment growth will be the norm in 2026. The unemployment rate, constrained by limited labour supply, is expected to peak at around 4.6% in H1 and to remain near that level throughout the year.

### ... capping employment growth and making consumption more fragile

Consumption growth is expected to slow to around 2.2% in 2026, down from 2.6% in 2025. The expansion in consumption will not be broad-based; wealthier households will benefit most from the tax cuts, while lower-income households will face weaker real wage growth, sluggish employment, and dwindling savings. Household wealth gains—mainly from a robust equity market—have supported consumption and are expected to continue doing so. However, since equity ownership is concentrated among older, wealthier households, and much of this spending is discretionary, consumption growth will be narrower in base and more sensitive to market volatility. For example, our model estimation shows that an 8% fall in the stock market would lower GDP by nearly 0.4%, with the actual impact likely larger given the current outsized role of wealth effects.

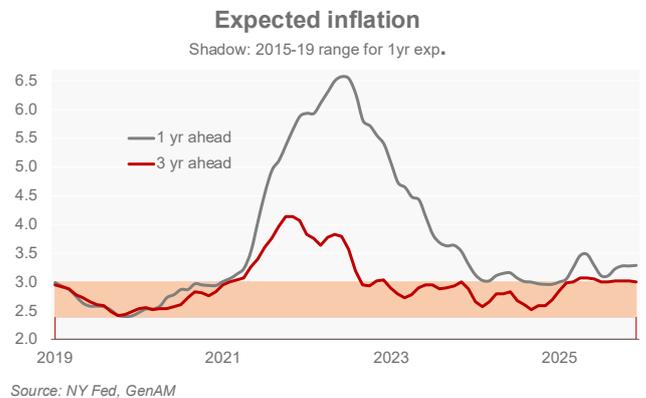
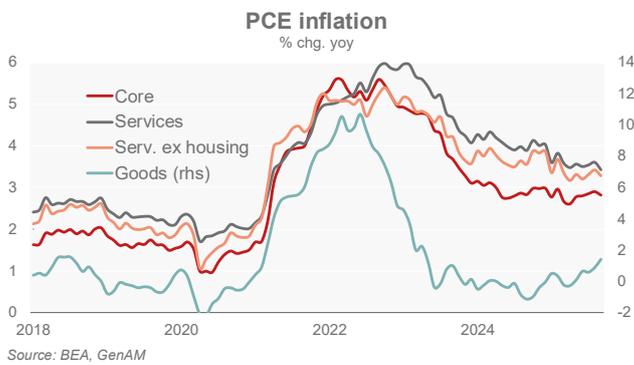
Real income and employment prospects will be pivotal in the November mid-term elections. Republican chances of retaining both houses depend heavily on a material

improvement in consumer sentiment and assessments of the administration's economic performance. While fiscal levers will be deployed, their current form offers little benefit to most voters and could even worsen conditions for some, especially if social security spending is cut. Rising health insurance premiums and the potential withdrawal of Obamacare financial support would further erode purchasing power among lower-income households.

### Slow disinflation, with upside risks

We anticipate core PCE inflation will finish 2026 at about 2.5% year on year, a reduction of 0.4 percentage points from our estimate for December 2025. Most inflation pressure is concentrated in ex-housing services, with two main factors at play in 2026. Weaker labour demand should continue to restrain wage growth in service sectors, where productivity gains are relatively slow. However, wealthier households' continued demand for services will allow firms to maintain pricing power, slowing the pace of disinflation. Overall, the risks to inflation are skewed to the upside. The fiscal stimulus, which benefits mainly richer households, may have a larger than expected effect on demand, especially given ongoing constraints on labour supply. While tariffs were almost completely borne by US importers their modest impact so far is largely attributable to retailers absorbing costs; if profitability comes under pressure, price increases may accelerate. Finally, inflation expectations may remain elevated following the sharp increases of 2021–22.

The administration has begun implementing measures to contain the rise in prices for certain critical goods, such as cutting tariffs on agricultural imports and announcing steps to reduce electricity bills—though these details remain unclear as well as the effective relief they will deliver.

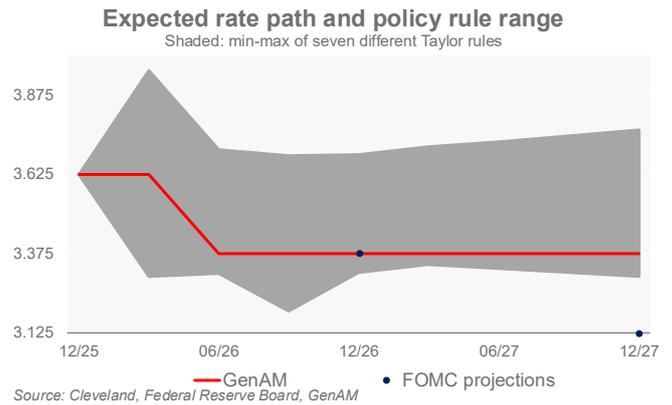
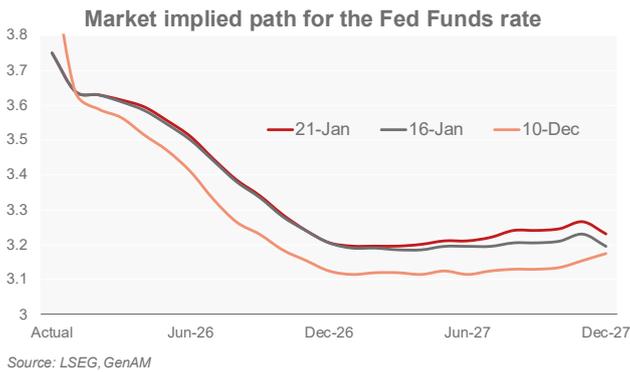


### The Fed remains independent and cautious

Our constructive growth outlook is consistent with the expectation of only one rate cut by the Federal Reserve in 2026, bringing the policy rate to the 3.25–3.5% range. The strength of GDP growth in the first quarter suggests this cut will not occur before June. Markets have already begun adjusting to a higher terminal rate, shifting their expectations of the year end level from 3% to 3.2%. Our projection is at the lower end of policy rules, indicating that monetary policy will not be particularly restrictive, especially given the slow pace of disinflation and only a modest rise in unemployment.

Questions remain about the extent to which political pressure will influence the Fed's actions. Developments such as the Department of Justice's inquiry into Chair Powell have prompted market pushback and resistance from some Republican legislators. Powell is set to step down as FOMC Chair in April, but it is not clear who will succeed him. Market turbulence has reduced the likelihood of appointing a candidate seen as too responsive to the administration's calls for lower rates. Powell could remain on the Board until 2028, and given the threats to the Fed's independence, he may choose to stay. There is currently a solid majority of FOMC members—including those appointed by President Trump in his first term—committed to a cautious stance, so the new chair would likely be outvoted.

The most critical test for the Fed's independence will be the Supreme Court's decision on the attempt by the administration to dismiss Governor Lisa Cook. There is no set date for the ruling, but initial statements following the 21 January hearing suggest the dismissal will likely be deemed illegal, shielding the Fed from the President's discretionary dismissals. Should the decision favour the government, it would enable a rapid and complete reshuffle of the FOMC, shifting the balance towards lower policy rates and significantly undermining the Fed's credibility, with potential for major impacts on the US dollar and long-term Treasury yields.



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