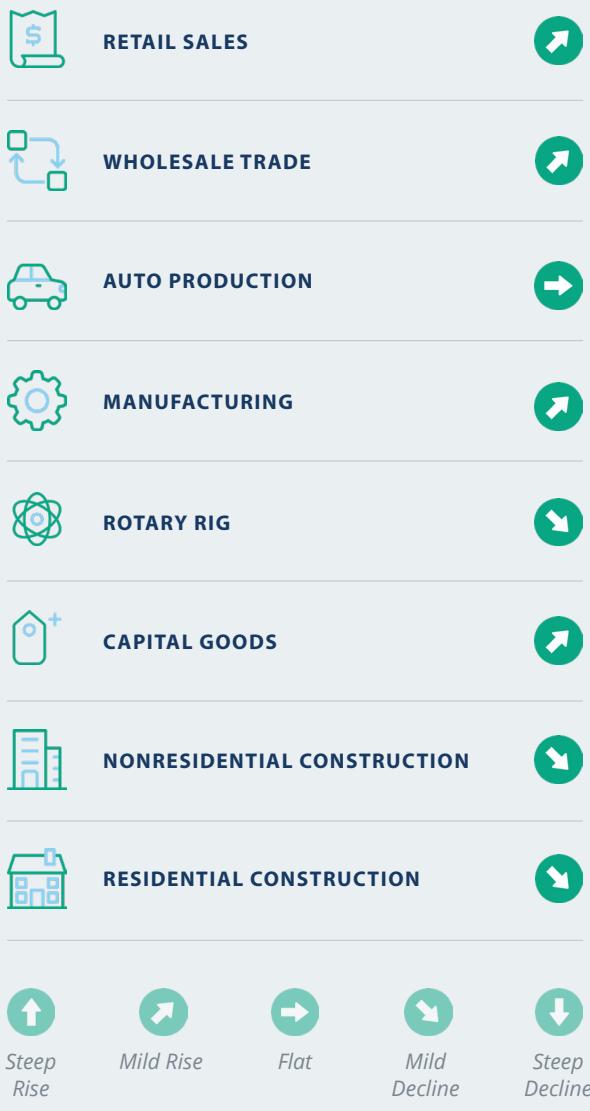


Industry Snapshots

Arrow denotes 12-month moving total/average direction.



Macroeconomic Outlook

We are entering the new year with generally well-positioned consumers, rising business-to-business spending, and an expanding industrial sector. Data-driven signals of resilience underpin our expectations for the macroeconomy to continue to grow, albeit at a mild pace, in 2026. Still, there are headwinds. Recent developments in the indictment of the Federal Reserve chair pose a threat to the rate-setting body's independence, a potential upside risk to already rising inflation. We are monitoring this unprecedented development.

US Real Gross Domestic Product is rising, driven primarily by consumer spending. Despite some uncertainty and weak metrics of consumer confidence, Personal Consumption Expenditures are rising on both a volume basis and dollars basis. Consumer balance sheets, in aggregate, are being boosted by rising real incomes. However, the "K-shaped economy" discourse posits that widening economic outcomes between income brackets are positioning higher-income consumers to drive much of the upcoming growth. Those higher-income individuals are benefiting from a multitude of factors that support spending, including a bullish stock market and elevated home values. This is something to keep in mind for your business as you target demographics and implement pricing strategies.

US Real Gross Domestic Product is rising

On the business side, capex spending is rising at an accelerating pace. Further business-to-business spending is supported by elevated, though slowing in growth, corporate profits and corporate cash levels. Unlike consumer sentiment, US Small Business Optimism has been generally positive, and US Small Business Capital Expenditures are gaining momentum, an encouraging sign given that smaller firms typically invest more cautiously due to tighter financial and operational constraints. Elevated borrowing costs will continue to temper overall B2B spending to some extent, however.

The nonresidential side of construction is mildly declining. We recently revised our outlook for US Private Nonresidential Construction due in part to weakness in the residential market. We expect mild rise for much of 2026 and 2027, but growth rates will be in the low single digits. Despite recent cuts to the federal funds target rate, long-term interest rates are elevated. With construction more closely tied to long-term rates, this will dampen some nonresidential activity.

The economic backdrop entering 2026 is one of cautious optimism: consumers are healthy in aggregate, and their spending remains the primary engine of growth. Keep the K-shaped economy in mind and consider diversifying your business where possible to maximize exposure to demographics or markets that are poised for growth.

Make Your Move

Despite recent geopolitical and domestic developments, the data continues to support our outlook for growth, though there will be disparities by market. In addition to watching macro trends, drill down to market-level data and forecasts.

Investor Update

The S&P 500 posted a double-digit rate of growth for 2025 as a whole, the third straight year this has occurred. Tech (quarterly rate-of-change at +28.3% in December), Communications (+22.7%), and Industrials (+15.3%) led the market in 2025. As 2026 unfolds we may see some of these sectors soften, especially in the latter half of the year. Four straight years of double-digit increases would be a historical rarity, and our softer 2027 expectations point to more muted 2026 returns.

ITR Economics Long-Term View

2026

GROWTH

2027

GDP GROWTH; MANUF. FLAT

2028

GROWTH

Leading Indicator Snapshot

	1Q2026	2Q2026	3Q2026
ITR Leading Indicator™	●	●	●
ITR Retail Sales Leading Indicator™	●	●	●
US OECD Leading Indicator	●	●	●
US ISM PMI (Purchasing Managers Index)	●	●	●
US Total Industry Capacity Utilization Rate	●	●	●

● Denotes that the indicator signals cyclical rise for the economy in the given quarter.

● Denotes that the indicator signals cyclical decline for the economy in the given quarter.

● N/A

KEY TAKEAWAYS

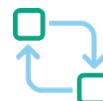
- Leading indicator signals remain somewhat mixed; however, economic evidence is pointing toward mild rise.
- The US Total Industry Capacity Utilization Rate is in a general, shallow rising trend, supporting our outlook for mild industrial sector expansion.
- Relatively resilient consumer and business balance sheets will drive spending and growth in the coming year for many, but not all, markets. Ensure your business is positioned to capture broad, muted growth, and look for ways to preserve margins.

Industry Analysis



RETAIL SALES

- US Total Retail Sales in the 12 months through November were 3.8% above the year-ago level
- Consumers are managing their debt effectively, boding well for future spending
- Retail Sales are poised for further rise, likely driven largely by upper-income consumers



WHOLESALE TRADE

- Annual US Total Wholesale Trade in October came in at \$8.4 trillion, 4.3% higher than the year-ago level
- The nondurables component is 2.4% above the year-ago level and accelerating in growth; durables are 6.5% above the year-ago level
- Inflation trends will drive some of the expected growth in Wholesale Trade



AUTO PRODUCTION

- Annual North America Light Vehicle Production totaled 15.2 million units in November, 3.2% below the year-ago level
- Auto loan delinquencies suggest some consumers are struggling, but this market has the "K-shaped" trend, with higher-income households driving much of the growth
- Electric vehicles are likely to face additional headwinds due to the expiration of EV tax credits and subsidies



MANUFACTURING

- Annual US Total Manufacturing Production in December was 1.2% above the year-ago level
- Given the prevalence of policies designed to boost domestic production, more industrial capacity will likely come online
- Dollar-denominated annual US Total Manufacturing New Orders, at 2.5% above year-ago levels, are growing faster than volume activity, highlighting rising prices



ROTARY RIG

- The US Rotary Rig Count in the final quarter of 2025 averaged 548 units, 6.5% below the 4Q24 level
- The Dallas Fed's fourth quarter energy survey signals a cautious capex environment in this market
- Still, a growing industrial sector is likely to exert some upward pressure on the Rig Count



CAPITAL GOODS NEW ORDERS

- US Nondefense Capital Goods New Orders (excluding aircraft) in the 12 months through October were 2.6% above the year-ago level
- US Defense Capital Goods New Orders for the same time period were 13.8% above the year-ago level
- The defense sector is likely to benefit from geopolitical volatility



TOTAL NONRESIDENTIAL CONSTRUCTION

- US Total Nonresidential Construction is below year-ago levels
- Commercial delinquency rates are elevated relative to the past decade, which could hamper some future Construction activity
- Weak architecture billings suggest muted Construction in at least the near term



TOTAL RESIDENTIAL CONSTRUCTION

- Annual US Housing Starts are declining and 6.6% below the year-ago level
- The multi-unit sector, however, is showing some resilience; annual US Multi-Unit Housing Starts are 11.2% above the year-ago level
- Mortgage rates are lower than their recent peak but still elevated, a notable hurdle to housing affordability

A Closer Look: The US Economy

Understanding Interest Rates: What the Bond Market Is Telling Us

DAVID FAIRCHILD

While the Fed can influence short-term rates, long-term rates show signs of stickiness due to bond market expectations.

Interest rates are often discussed as if they are a single number. In reality, rates represent a signaling system — a complex one at that — about risk, growth, inflation, and economic confidence. For business leaders, understanding how those signals interact is critical.

At the most basic level, an interest rate is the price of money over time. It compensates the lender for delaying consumption and for taking on risk. Lenders evaluate inflation, economic growth, and creditworthiness. When uncertainty about those factors rises, lenders demand higher rates to offset that risk. The inverse is also true: when confidence improves, rates tend to fall.

The Federal Reserve has a dual mandate: maximizing employment and keeping inflation around 2%. One policy tool is the federal funds rate, which is the short-term interest rate targeted by the Fed. It sets the overnight lending rate between banks or, in other words, how much banks charge each other to lend money. When the Fed raises or lowers the fed funds rate, it is attempting to influence borrowing, spending, and inflation by tightening or loosening financial conditions. It is important to note that it reflects the Fed's intent, not the market's long-term outlook.

That distinction becomes clear when examining long-term interest rates, such as the 10-year yield, which are determined primarily by the bond market. The Treasury yield is determined largely by what the market expects about future inflation and economic growth, government borrowing, and institutional credibility. While the Fed can influence long-term rates indirectly, it does not control them.

The 10-year Treasury has been notably “sticky” in recent years, remaining elevated even as the Fed has cut the fed funds rate and inflation has cooled significantly from its pandemic-induced highs. 10-year Treasurys averaged a 4.14% yield in December. This is little changed from the prior few months and nearly identical to the 4.15% average over 2023–25 despite 175 basis points of fed funds rate cuts from late 2024 to now. As of January 20th, the yield on the 10-year Treasury is 4.27%.

This persistence suggests the bond market is not fully convinced that inflation risks have been permanently resolved, nor that long-term government fiscal imbalances will be meaningfully addressed — concerns that ITR Economics shares. From ITR Economics' perspective, the list of inflationary drivers is long: not enough workers, not enough houses, not enough electricity in an AI/electrification era, unsustainable deficit spending, and nationalism/tariffs leading to increases in the price of goods. Sticky long-term rates signal that investors are demanding a higher risk premium. Diminished confidence that inflation will be subdued translates directly into higher borrowing costs across the economy.

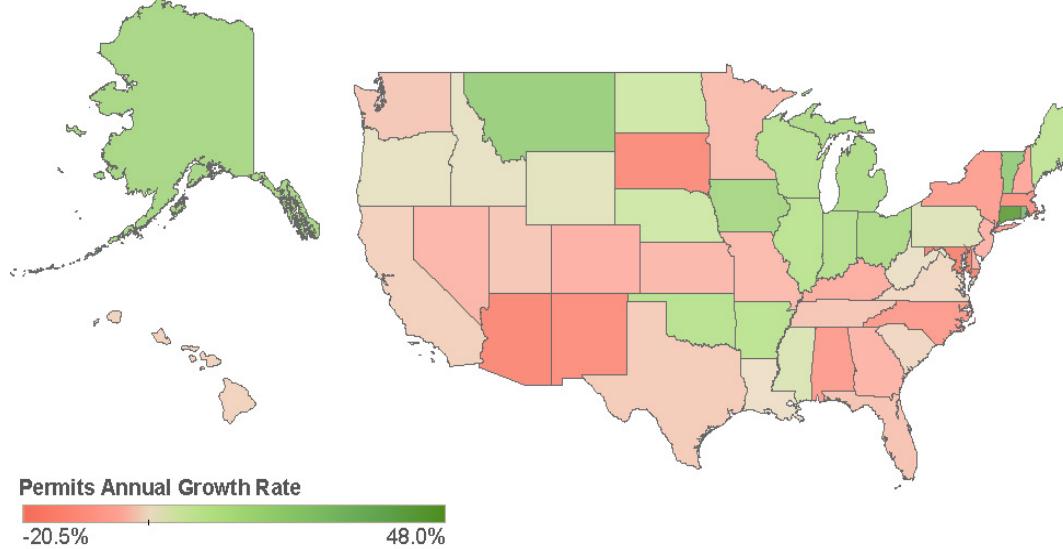
This is why the Fed's independence is critical. The Fed was designed to operate independently of short-term political pressures to maintain its credibility all while fighting inflation, promoting maximum employment, and preserving the purchasing power of the dollar. That independence reassures bond investors that monetary policy decisions are driven by economic data, not election cycles. The US economy has benefited heavily from that independence.

If that credibility is undermined, markets may begin to believe the Fed is subordinated to political priorities. Investors could demand higher yields to compensate for the increased risk of inflationary policy mistakes, and we could see further decoupling of the fed funds rate and longer-term rates like 10-year Treasurys. ITR Economics' forecast is for 10-year Treasury yields to be moving generally higher for the rest of this decade.

Do not assume that fed rate cuts equate to one-for-one reductions in long-term interest rates. Capital investments — physical or technological — that you can make today to increase your existing labor force's efficiency and productivity will help protect your bottom line in the coming years. For most firms, our long-term interest rate expectations suggest that it is best to time investments according to when you want to realize the ROI before the 2030s rather than holding out for better rates.



onDemand



- Annual US Housing Permits in October were 2.4% below the year-ago level. Permits have been in a general declining trend since the pandemic-era surge; in terms of volume, they are currently trending at about where they were five years ago.
- In terms of regional trends, only the Midwest has overall annual housing permits above year-ago levels, with strength concentrated in Great Lakes states. While the Northeast as a whole is not above year-ago levels, the strongest individual states are there, with Connecticut, Rhode Island, and Vermont posting annual growth rates of 48.0%, 31.7%, and 24.3%, respectively.
- Housing permits for the South and West regions, both of which had robust building activity in prior years, are below year-ago levels.
- Housing starts are also below year-ago levels for the US as a whole, dampened in part by affordability challenges.

Readers' Forum

Will the weakening labor market lead to a recession?

Haley Sienkiewicz, Economist at ITR Economics™, answers:

While some metrics suggest softening, a look at historical trends indicates that the labor market is relatively sound. On an annual basis, US Total Nonfarm Employment is at record highs and rising, though the pace of rise is slowing. The US Unemployment Rate is generally rising, but it is historically low, and the upward slope is much gentler than what has typically correlated with recessionary periods.

These are high-level metrics, so dynamics will vary by industry and geographic location. However, from a macroeconomic perspective, the labor market will be able to support upcoming macroeconomic growth. It is also important to remember that the labor market is not a leading indicator for the economy; rather, it lags, as hiring decisions are often reactionary. The softer jobs numbers we are seeing are in the wake of prior trends rather than a harbinger of future weakness.

Please send questions to: questions@itreconomics.com

Strategic Shifts for Resiliency in the 2030s Great Depression



The changes coming up for the economy, and by extension our markets and businesses, are going to be tectonic given the trends coming to a nexus in the early 2030s. Going into the downturn with a “we will just sell more” attitude is using hope as a strategy. We have seen that hope dashed repeatedly in every major recession, and the 2030s downturn will be the worst that any of us has experienced. The good news is that we can prepare our businesses and position our wealth to not simply survive the coming depression but come out stronger on the other side.

Discover the critical insights you need for the next decade in our December webinar. Insider members receive \$25 off with code INSIDER2025!

RECORDING AVAILABLE