KeyBank

EOY Economic Outlook

2025

Economic growth is slowing — but not stopping.

Inflation, labor market shifts, and policy uncertainty are reshaping the landscape. Here's what you need to know to stay ahead.

Introduction and overview

The U.S. economy continues to navigate a complex landscape of cautious stability. Modest growth persists, fueled by resilient consumer spending and an improving trade balance, but the path forward is anything but smooth. Several headwinds — including persistent inflation, a cooling labor market, and ongoing policy uncertainty — pose significant risks. For investors and business leaders, understanding these pressure points is essential.

Overview:

U.S. economic growth slowing, resilience tested by persistent risks

After a rebound in Q2, growth is expected to remain weak but avoid recession in the near term.

The U.S. economy rebounded strongly in the second quarter.

Consumer spending is steady but losing momentum.

The underlying pace of growth has slowed and is likely to slow further, but growth has not ended, at least not yet.

Uncertainty surrounding tariffs has generated buying ahead of feared price increases, both by consumers and businesses, especially importers. This will likely weigh on growth in the final months of the year. But while consumers are still contributing to growth, they are doing so at a slower pace.

Spending among upper-income groups remains resilient, while middle- and lower-income households remain cautious, and some are showing signs of financial stress.

Consumers feel very pessimistic. There are many reasons for this. Inflation is inching higher, moving many goods' prices to levels above those consumers were already uncomfortable with. The federal government shutdown extended through much of the survey period, reducing services and adding to the already-high uncertainty. The labor market is weakening, with job openings scarce. There is little for consumers to like at present other than the strength of the stock market and stable gasoline prices.

Tariffs raising pressure

Tariffs continue to ripple through the economy, raising costs for imported goods and certain domestic products.

For policymakers and businesses, this underscores a key challenge: tariff-related inflation is less responsive to interest rate cuts and will likely remain until trade terms improve. For consumers, the result is sustained higher prices in tariff-sensitive categories, shaping spending patterns well into 2026.

While some firms have temporarily shielded buyers from price hikes, sectors such as autos and electronics are already seeing upward pressure.

Beyond domestic tariff considerations, the global trade environment is currently characterized by a complex interplay of factors, including ongoing geopolitical tensions and efforts to diversify supply chains.

Conclusion

Looking ahead, the baseline economic forecast shows weakening real GDP growth in the near term, though a full-blown recession is expected to be averted.

Traders have become less confident that the easing cycle will extend into 2026, given still-elevated inflation and persistent divisions among policymakers, and at December's meeting, the median FOMC participant sees just one quarter-point rate cut in 2026. A more significant rebound is not expected until 2027, and even then, the strengthening will be modest, constrained by limited federal support, a drag from trade, and slow employment growth.

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About Benjamin E. Demko

Ben Demko manages the economic research and analytics team focused on macroeconomic, industry, and market risks that impact KeyBank's varied loan portfolios. He is responsible for proprietary, forward-looking perspectives on the economy and real estate markets that are used across the bank for stress testing, loss estimation, asset management, resource allocation, and profit planning. Ben joined KeyBank in 2005 and has nearly 20 years of business analytics, economic research, and risk management experience.

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