Why we raise our US forecast

The US economy is performing significantly better than expected. We explain the reasons for this and raise our growth forecast.

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US economy remains strong in the second half of the year ...

The US economy has been growing at a surprisingly strong rate for some time now (title chart) – despite President Trump's tariff capers. While the growth of almost 4% in the second quarter of 2025 could still be dismissed as a counter-movement to the weak first quarter, shortly before Christmas, growth of 4.3% was even reported for the third quarter. Although relatively little data is available for the fourth quarter due to the government shutdown, it once again points to strong growth. This strong performance in the second half of the year surprised even us, even though we had pointed out from the outset that tariffs would only dampen growth but were unlikely to trigger a slump. We see three main reasons for the robust growth.

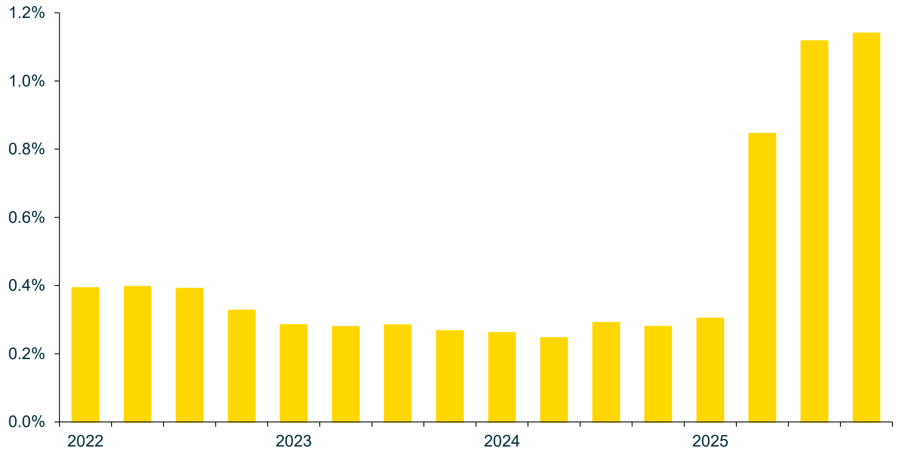
.. because tariffs are having less of an impact ...

Firstly, tariffs have had less of an impact on the economy than expected, at least so far. Companies imported a lot of goods before the tariffs came into force, so they did not have to raise their prices immediately and were able to spread the adjustment over time. Even more important was probably the fact that the tariffs actually paid were significantly lower than expected. Estimates based on the import structure of 2024 and the higher tariff rates had arrived at a new average rate of approximately 17% (Yale Budget Lab) or even 24% (**Gopinath/Neiman 2025**). However, if the tariffs paid are compared to the imports recorded – which better reflects the actual burden – the average rate is only just over 10%.

Many companies were granted exemptions and transitional rules for imports that are difficult to replace with US products. In addition, a larger proportion of imports from Mexico and Canada (around 27% of total imports) are now imported duty-free. This would have been possible earlier under the USMCA free trade agreement. However, this would have required documentation that the goods met certain requirements, in particular that a certain proportion of the value added was generated in the USMCA zone. Given the low tariff rates valid until the end of 2024, this bureaucratic effort was often not worthwhile. However, this changed with the high tariffs announced by Trump for non-USMCA-compatible imports from Canada and Mexico. Meanwhile, 80-90% of imports from these two countries are USMCA-compliant, twice as many as before 2025.

Compared to the average tariff rate of 2.3% that prevailed before Trump, the increase to a good 10% is still significant, but not as dramatic as feared. In relation to economic output, customs revenues rose from around 0.3% of gross domestic product (GDP) in 2023 and 2024 to 1.1% of GDP in the second half of 2025 (Chart 1). Since these tariffs have so far been borne almost entirely by the Americans and not by the supplier countries, this provides an estimate of the braking effect of the tariff increases. This amounted to around 0.8% of GDP. And this is too little to plunge the US economy into crisis. After all, it has recently grown at a nominal rate of over 5% per year.

Chart 1 - The "tariff tax" was not high enough to stop the economy in its tracks
Tariff revenue in % of GDP. For Q4.2025: Commerzbank estimate



Source: US Treasury, S&P Global, Commerzbank Research

... AI investments came at the right time ...

Secondly, Donald Trump was fortunate with the timing of his tariff increases. These coincided with a period of massive growth in investments related to artificial intelligence. This can be seen in private investments in IT equipment and software, which were probably driven primarily by the AI boom. In real terms, investment in IT rose by 18.6% in the third quarter compared with the same quarter of the previous year, while investment in software rose by 12.3%. Growth rates have thus doubled within a year. In the first three quarters of last year, these investments contributed 0.8 percentage points to average economic growth of 2.5%. In purely mathematical terms, this compensated for the braking effect of the tariff increases.

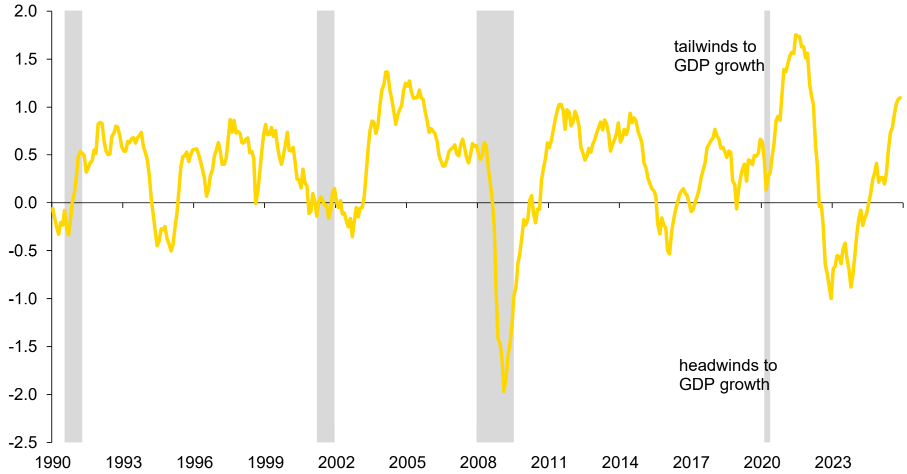
… and because financing conditions remain very favorable

A third reason for the sustained strength of the US economy is the significant improvement in financing conditions. Although key interest rates are still quite high, low risk premiums, rising stock prices, and the weaker dollar are boosting the economy. This is confirmed by an indicator from the Federal Reserve. This **FCIG** (Financial Conditions Impulse on Growth) shows the growth impulse resulting from financing conditions. Financing conditions, in turn, are constructed from the key interest rate and various market variables.[1] According to the FCIG, financing conditions are providing strong tailwinds for the US economy (Chart 2).

Given the improved starting position and the favorable financing conditions, which are likely to remain in place for some time to come, we are raising our growth forecast for this year significantly from 2.2% to 2.7%.

Chart 2 - Tailwinds from financial conditions

Financial Conditions Impulse on Growth (FCI-G), contribution to GDP growth over the next year in percentage points. Recessions shaded



Source: Fed, Commerzbank Research

Surprisingly low price pressure

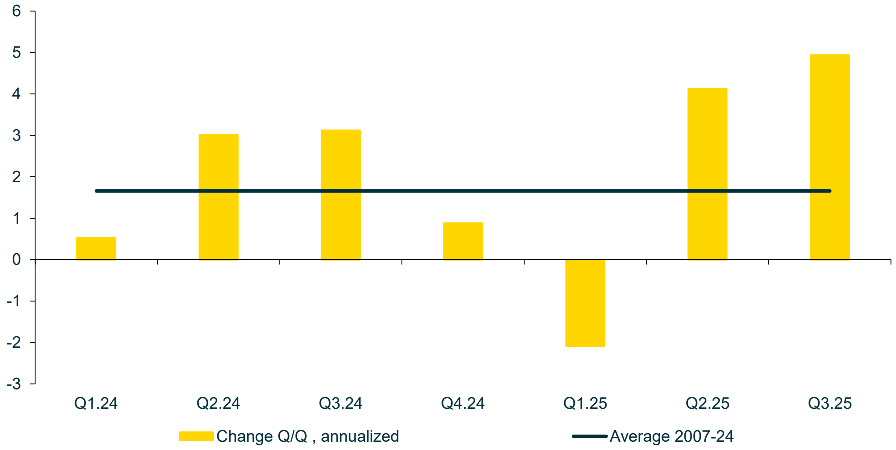
Given the strong growth, inflationary pressure has been surprisingly weak recently. The inflation rate based on the consumer price index was 2.7% in December, which was even slightly lower than the 2.9% recorded in December 2024, when tariffs had not yet been increased. This was partly because, as mentioned above, the tariffs were not that high, companies only gradually passed on their higher costs to final customers, and imported goods only account for about 10% of domestic demand anyway.

On the other hand, there are increasing signs that the US economy has entered a phase of higher productivity gains again. Labor productivity rose by 4.9% in the third quarter, following 4.1% in the second. This is significantly more than the just under 1.7% measured between 2007 and 2024 (Chart 3). Strong productivity growth is also on the cards for the fourth quarter.

This means that the improvement in productivity could continue. It is likely to be primarily the result of rationalization efforts in the wake of the labor shortage after 2019. It is probably still too early to see any effects of AI.

Chart 3 - US: Productivity is accelerating

Real output per hour worked, annualized quarterly rate of change in %



Source: BLS, S&P Global, Commerzbank Research

Another factor comes into play: rents and imputed rents for owner-occupied homes, the most important item of consumer expenditure, are rising much more slowly, and this weakness is likely to persist longer than expected. Rental inflation for new contracts, for which data from private providers such as Apartment List and Zillow are available, has turned down again (Chart 4). These rents are more than a year ahead of the overall market, as tightness in the housing market typically shows up more quickly in new contracts than in existing contracts.

In light of these factors, we are reducing our inflation forecast for 2026 from 3.2% to 2.8%.

Chart 4 - New contracts show that rent growth has turned lower again

rents, year-on-year change in %. New contracts (Apartment List, Zillow) and official data on overall market according to CPI

Source: Apartment List, Zillow, S&P Global, Commerzbank Research

No change for the Fed overall

Despite the significant revision to our growth forecast, we maintain our view that the Federal Reserve will continue to cut interest rates significantly in the course of 2026. Why?

- Part of the Fed's mandate is "full employment," so it focuses more on the labor market than on GDP growth. And the labor market has cooled gradually but steadily over the past year. Demand for new workers has declined, with an average of only 49,000 jobs created each month in 2025, down from just under 170,000 in 2024. Despite the sharp decline in immigration (i.e., a lower labor supply), the unemployment rate has risen slowly and stood at 4.4% in December, almost one percentage point higher than at its low in 2022/23. This puts the labor market at the top of the Fed's agenda. Interest rate cuts are intended to prevent the labor market from weakening further. The central bank is in a position to do so, partly because recent price data is likely to reinforce its assumption that the current inflationary pressure, which is still too high, is easing. This is because the labor market is less tight than before, and the effects of tariffs are only having a temporary impact on the inflation rate.
- The Fed is also coming under increasing pressure from the government to further loosen its monetary policy. The central bank is resisting this, however. Fed Chairman Powell has defended himself against this pressure in an unusual – and unusually clear – video message. Only cautious steps are therefore to be expected during his remaining term of office. However, we assume that the government will ultimately prevail once the new Fed leadership is in place in the spring. The Fed will then probably move towards

the government's line.

We therefore stand by our forecast that the Fed will lower its key interest rates to 2.5% over the course of the year, i.e., by a total of 125 basis points. This would mean that it would have reduced key interest rates by 300 basis points since their peak.

Market implications

We have not adjusted our financial market forecasts despite the changes in US growth and inflation. This is because the fact that the outlook for the Fed remains unchanged is more important for the financial markets. We therefore continue to expect the dollar to weaken to 1.22 against the euro by the end of the year due to the erosion of the Fed's independence. For ten-year government bond yields, we confirm our year-end targets of 4.4% (US Treasuries) and 3.0% (German Bunds).

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[1] The financing conditions are based on the yields of corporate bonds and Treasuries, mortgage interest rates, the external value of the dollar, a stock index, and a house price index. The approach also takes into account delays in impact of up to three years. (back to text)

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