

# Economics

## ECONOMIC FLASH!

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December 23, 2025

### US Q3 GDP: Good news, but nothing we didn't already know

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Annualized Qtrly Chg.	25 Q3	25 Q2	25 Q1	24 Q4	24 Q3	24 Q2
Real GDP	4.3%	3.8%	-0.6%	1.9%	3.3%	3.6%
Personal consumption	3.5%	2.5%	0.6%	3.9%	4.0%	3.9%
• Goods	3.1%	2.2%	0.2%	6.9%	6.1%	5.5%
• Durable goods	1.6%	2.3%	-3.4%	13.0%	8.6%	7.7%
• Nondurable goods	3.9%	2.2%	2.2%	3.8%	4.8%	4.3%
• Services	3.7%	2.6%	0.8%	2.5%	3.0%	3.2%
Gross private investment	-0.3%	-13.7%	23.3%	-6.8%	0.9%	8.2%
• Fixed investment	1.0%	4.4%	7.1%	-1.9%	1.5%	1.4%
• Nonresidential	2.8%	7.3%	9.5%	-3.7%	3.5%	2.5%
• Structures	-6.3%	-7.5%	-3.1%	-8.0%	-2.2%	-3.9%
• Equipment	5.4%	8.5%	21.3%	-4.2%	8.2%	8.9%
• Intellectual Property	5.4%	15.0%	6.5%	-0.6%	2.6%	0.7%
• Residential	-5.1%	-5.1%	-1.0%	4.3%	-4.8%	-2.0%
Exports	8.8%	-1.8%	0.2%	-0.9%	8.9%	0.7%
• Goods	7.4%	-4.7%	6.3%	-3.9%	8.4%	0.4%
• Services	11.2%	3.5%	-9.7%	4.6%	9.8%	1.2%
Imports	-4.7%	-29.3%	38.0%	-0.2%	10.1%	8.4%
• Goods	-7.5%	-35.0%	52.0%	-3.1%	8.9%	9.0%
• Services	6.3%	-1.2%	-5.8%	11.5%	15.4%	5.9%
Government	2.2%	-0.1%	-1.0%	3.3%	5.4%	3.3%
• Federal	2.9%	-5.3%	-5.6%	4.4%	8.6%	4.3%
• National defense	5.8%	0.9%	-6.9%	4.5%	13.5%	7.0%
• Nondefense	-1.1%	-13.0%	-3.8%	4.0%	2.4%	0.9%
• State and local	1.8%	3.1%	1.9%	2.7%	3.6%	2.8%

Source: Haver Analytics.

- The Q3 GDP numbers were good news, but confirm what we already know: investments in AI and robust consumer spending continue to propel the economy forward, despite tariff headwinds and tight immigration policies. GDP growth came in strong once again in Q3 at 4.3% Q/Q SAAR, a full percentage point above consensus expectations of 3.3%. Private final domestic demand posted a stellar 3% pace in the quarter, with consumption growth clocking in at 3.5% and contributing more than half of overall growth. Beyond consumption, net exports were a major contributor to growth, driven by both strong exports and soft import growth in the quarter. Direct AI-related investment was less eye-popping than the prior quarter, but still about 10% of Q3 growth came from software, R&D, and information-processing equipment, where AI spending is likely most concentrated. The core PCE price deflator came in at 2.9%,

in line with expectations. This release combined elements of a typical advanced and secondary release and so GDI came with this report, showing growth of just 2.4%. That's far below the pace of GDP, but GDI has a history of being revised closer to GDP as of late.

- This is a good report, and better than expected. But what does it mean for the Fed? Likely not much. Besides being a bit dated, the Fed prioritizes the job market over activity data as a leading indicator of where the economy is headed, and the labor market has moved further in the wrong direction in the fourth quarter, albeit with more limited data. The worry may be that consumer spending is not generating the normal level of labor demand. Firms continue to be cautious about hiring more workers in an environment where policy continues to whipsaw, and the Fed is likely to provide more insurance in the new year if the job market continues to soften. We expect two more rate cuts in the first half of next year.
- Looking under the hood of today's report, consumer spending on services was likely the single biggest surprise in the report. Services spending jumped to 3.7% from 2.6% in the prior quarter, and most of that was due to a sharp increase in spending on medical care services, up about 2%-points to 6.8% in the quarter. With ACA subsidies expiring at year-end, Americans may be hurrying to take advantage of elective procedures that might either not be covered or come at far greater cost next year. Services spending could look robust again in Q4 for the same reason. Goods consumption was also strong, but now the consumer is tilting away from durables towards nondurable goods, and there was a noticeable bump in off-premises food and beverage consumption.
- Business investment moderated from 7.3% to 2.8% in Q3 as both equipment and intellectual property products (IPP) capital spending moderated. Equipment peaked in Q1 on tariff-front running but AI-related spending on computers and other hardware components, as well as airplane purchases have kept investment healthy. But the AI-related boom is more visible in IPP, which has surged since late 2024. Growth was 5.4% in IPP in Q3, but that follows an eye-popping 15% in Q2. R&D investment is still growing at a healthy 8% pace.
- Overall, the dent from the trade war on the economy has been modest, with the most serious impacts being firms' caution in adding labor at the same time that they must pass on higher prices gradually. The consumer appears mostly unbothered by modestly higher prices, while investments in AI technology, transportation, and tariff front-running have all conspired to keep the economy growing at an underlying pace of around 3%. Fed easing has helped with that process; nonetheless, the economy's performance amid significant uncertainty is impressive and far stronger than we thought at the start of the year. With the Supreme Court likely to throw a wrench into the administration's tariff plans next year, and more Fed cuts coming next year to help the job market, the economy should stay on a solid growth path and weather the storm of potential policy changes, including lower tariffs and slower immigration.

## Implications & actions

**Re: Economic forecast** — GDP came in above expectations, but with the job market still likely on a cooling trajectory, we expect the Fed to ease twice next year in the first half of the year.

**Re: Markets** — Bond yields and the dollar rose as headline GDP exceeded expectations.

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