PLAINSCAPITAL BANK

ECONOMIC HIGHLIGHTS

Economic Commentary
October 2025

By Jerrod Dawson, CFA

Executive Summary

- U.S. economic growth stays positive, with upward revisions to Q2 GDP and expectations for ongoing expansion in Q3, though momentum is slowing due to weak manufacturing and small business sentiment.
- The government shutdown has delayed key data releases, reducing visibility into real-time conditions, but private data sources indicate minimal long-term economic impact.
- Inflation continues to slow despite tariff worries, with the Fed projecting PCE inflation at 2.5% (headline) and 2.8% (core) for 2025.
- Manufacturing shows early signs of recovery, with the PMI stabilizing near the expansion threshold, indicating possible improvement.
- Labor market conditions are mixed, with limited hiring and few layoffs; younger men experience higher unemployment due to sectoral shifts driven by AI.
- Consumer spending stays strong, fueled by high-income households and supported by healthy balance sheets and wealth effects, although sentiment is softening.
- A $150 billion stimulus from the recent tax bill is expected to boost consumer activity in 2026, supporting retail sales and discretionary sectors.
- The Federal Reserve is expected to conclude its Quantitative Tightening program soon, maintaining $265 billion in bank reserves annually and aligning with market expectations for further rate cuts.
- Fiscal policy is moving toward expansive tax cuts, deregulation, and strategic reshoring, with $100 billion in business tax relief and $150 billion in consumer aid planned.
- Domestic US Liquidity conditions have tightened due to significant October tax payments, especially from high capital gains areas, affecting bank reserves.
- The impact of the government shutdown on the economy is expected to be limited, as bipartisan efforts are underway to resolve budget issues.
- S&P 500 earnings are expected to grow 7.74% in Q3 2025 and surpass 10% by early 2026, led by financials and technology.
- Analysts' estimates have increased during earnings season, driven by stronger-than-expected results and rising optimism across sectors.
- The Guidance Index and Citi Global Earnings Revision Index both signal increasing confidence from corporate management despite broader economic uncertainties.
- Healthcare faces challenges with expected earnings declines, while the technology sector remains robust but is sensitive to AI-related capital spending trends.

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US Economic Cycle Drivers:

Growth	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Citi Economic Surprise - United States	11.1	4.7	↑	↓
Bloomberg Economics US GDP Nowcast	1.5	4.7	↓	↓
Concensus USA Growth Forecast Survey	-23.6	-34.2	↑	↓

Inflation	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Citi Inflation Surprise Index - United States	-15.7	-33.5	↑	↓
Bloomberg Economics US CPI Nowcast	3.0	2.8	↑	↑
Concensus USA Inflation Forecast Survey	66.3	64.3	↑	↑

Employment	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Unemployment Rate	4.3	4.2	↑	↑
Conference Board Employment Trend	106.4	107.7	↓	↓

Consumer Spending	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Johnson Redbook Retail Sales y/y	5.4	5.2	↑	↑
Adjusted Retail & Food Service Sales	5.0	3.4	↑	↑
Conference Board Consumer Confidence	94.2	95.2	↑	↓

Corporate Profitability	NTM (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
S&P 500 Est. Sales Growth Rate	6.4	2.8	↑	↑
S&P 500 Est. EPS Growth Rate	13.0	8.3	↑	↑
NFIB Small Business Optimism	100.8	98.6	↑	↑

Government Policy	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Budget/ GDP	-5.8	-7.0	↑	↑
USD Real Effective Exchange Rate	108.7	109.3	↓	↓

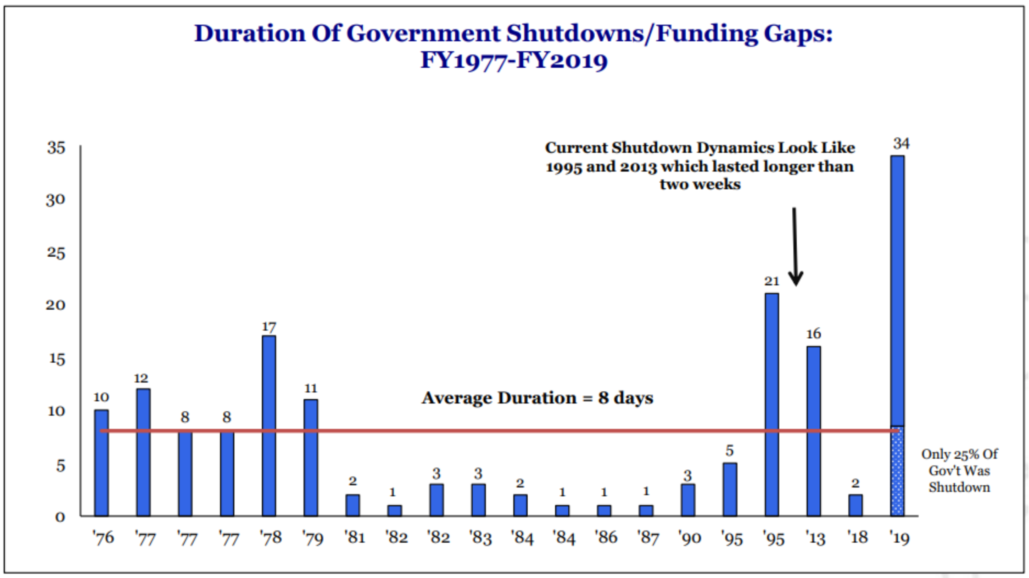
Central Bank Policy Rate	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
U.S. Federal Funds Rate Upper Bound	4.3	4.5	↓	↓
U.S. Market Implied Policy Rate 1Y Fwd	2.9	3.1	↓	↓

Liquidity	3mo Δ (%)	12mo Δ (%)	Trend q/q	Trend y/y
U.S. Domestic Liquidity	-0.1	1.5	↓	↑
Global Liquidity Index	0.3	12.1	↑	↑

Data source: Bloomberg

US & Global Economic Highlights

The U.S. economy continues to navigate a complex landscape as it enters the final quarter of the year. Recent data shows a mixed picture of economic growth, with upward revisions to second-quarter GDP and expectations for continued expansion in the third quarter. However, momentum appears to be slowing, as indicated by regional manufacturing surveys and subdued small business optimism. The ongoing government shutdown has delayed key data releases, limiting visibility into current conditions and increasing the risk of market overreactions. Overall, economic data in September was positive, but the federal government shutdown has postponed several critical reports, including CPI and some employment data. These delays will temporarily restrict insight into real-time conditions. Nonetheless, several private market data providers have stepped in to offer a snapshot of the current situation. Assessing the impact and duration of the government shutdown remains challenging, but if history is any guide, long-term economic and market effects are likely to be minimal.



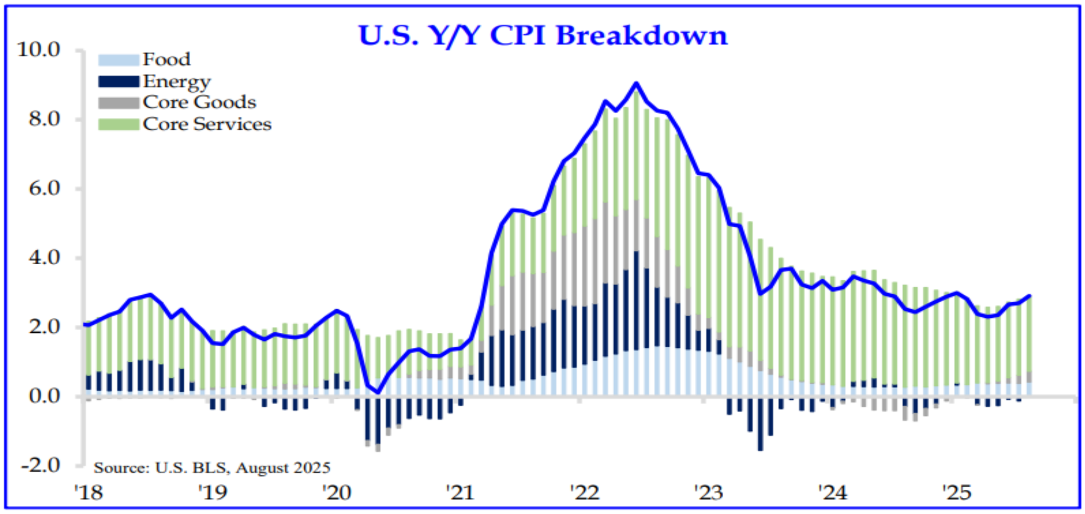
Duration Of Government Shutdowns/Funding Gaps: FY1977-FY2019

Despite these challenges, industries like technology, healthcare, and gig work remain resilient, supported by structural factors such as AI-driven productivity gains and demographic shifts.

Inflation continues to undermine the tariff scare with surprises to the downside. Supporting the positive data, at the September 16-17 FOMC meeting, Fed officials projected PCE inflation at 2.5% for 2025 (headline) and 2.8% (core), with broader ranges reflecting balanced risks around the 2% target.

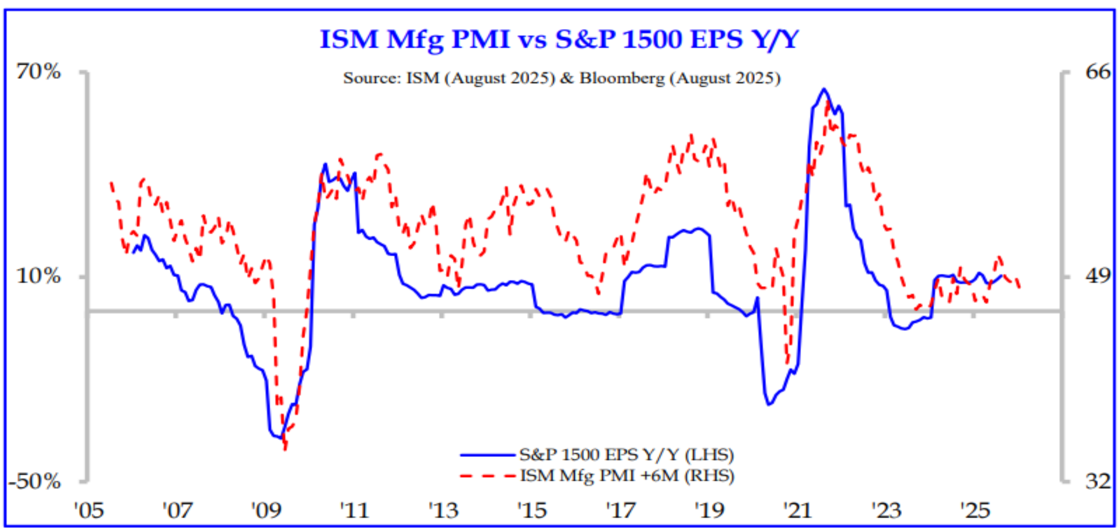
Critical points for the economy

- U.S. economic growth stays positive, with upward revisions to Q2 GDP and expectations for ongoing expansion in Q3, though momentum is slowing due to weak manufacturing and small business sentiment.
- The government shutdown has delayed key data releases, reducing visibility into real-time conditions, but private data sources indicate minimal long-term economic impact.
- Inflation continues to slow despite tariff worries, with the Fed projecting PCE inflation at 2.5% (headline) and 2.8% (core) for 2025.
- Manufacturing shows early signs of recovery, with the PMI stabilizing near the expansion threshold, indicating possible improvement.
- Labor market conditions are mixed, with limited hiring and few layoffs; younger men experience higher unemployment due to sectoral shifts driven by AI.
- Consumer spending stays strong, fueled by high-income households and supported by healthy balance sheets and wealth effects, although sentiment is softening.
- A $150 billion stimulus from the recent tax bill is expected to boost consumer activity in 2026, supporting retail sales and discretionary sectors.

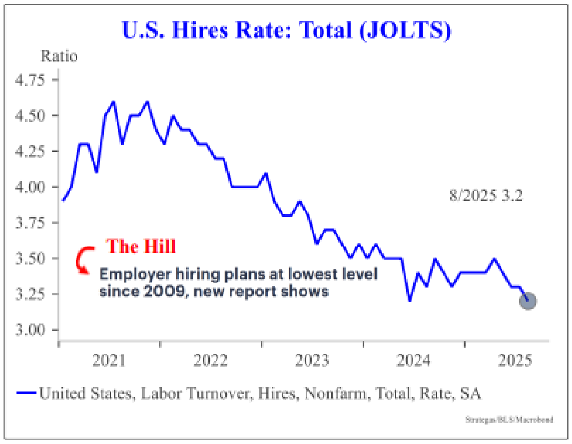


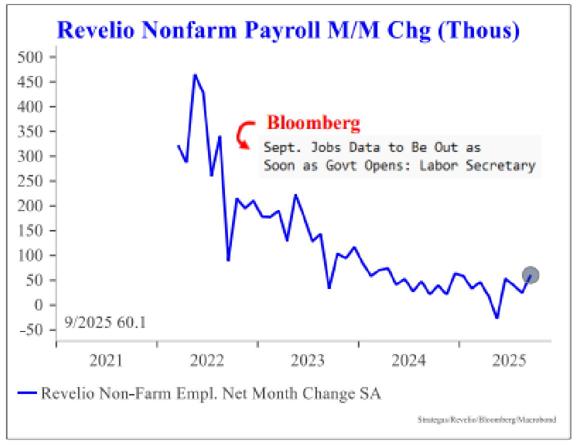
Tariff rhetoric continues to spread through financial media, but inflation pressures and supply chain issues have been well contained so far. Inflation is still declining, and supply chain pressures remain mild.

Since the exhaustion of the COVID stimulus, manufacturing has been in a sharp decline. However, this trend appears to be reversing. Although it is still technically below the elusive 50 expansion line, at 49, the manufacturing PMI (manufacturing index) remains stable and has shown early signs of upward movement.

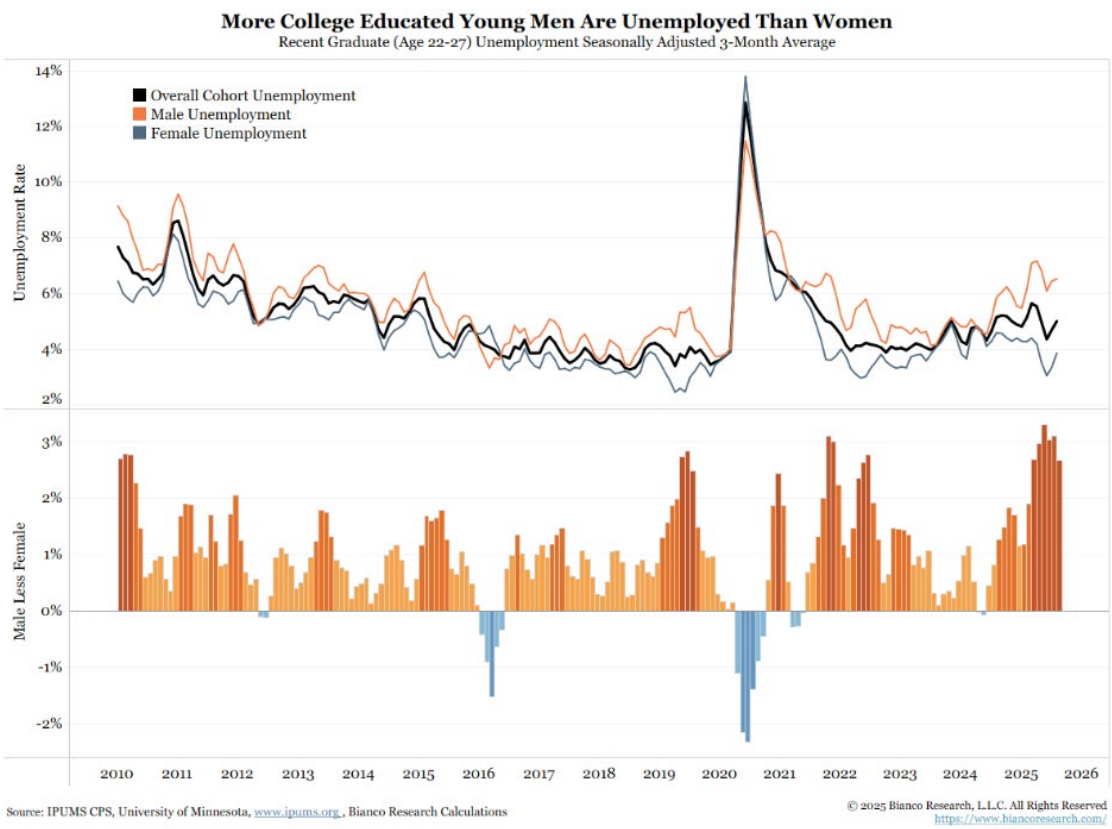


Labor market conditions are complex. While hiring remains limited, layoffs are few, and job seekers find it hard to secure new roles. Private-sector surveys indicate stability, but government data has been delayed. The Jolts Report, which tracks job openings, increased slightly, but the main point is a slow churn with low firing and hiring rates.



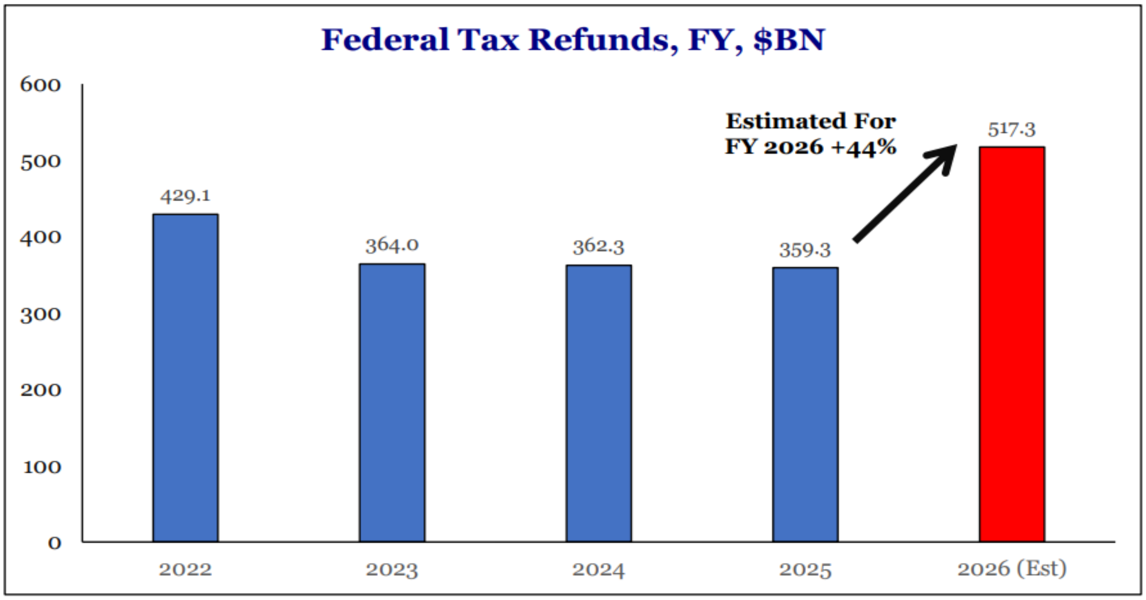


Younger men are experiencing higher unemployment rates than women, a trend connected to sectoral shifts caused by AI adoption in more male-dominated industries such as tech, finance, and law. Immigration has contributed to GDP growth, although its growth rate has slowed.

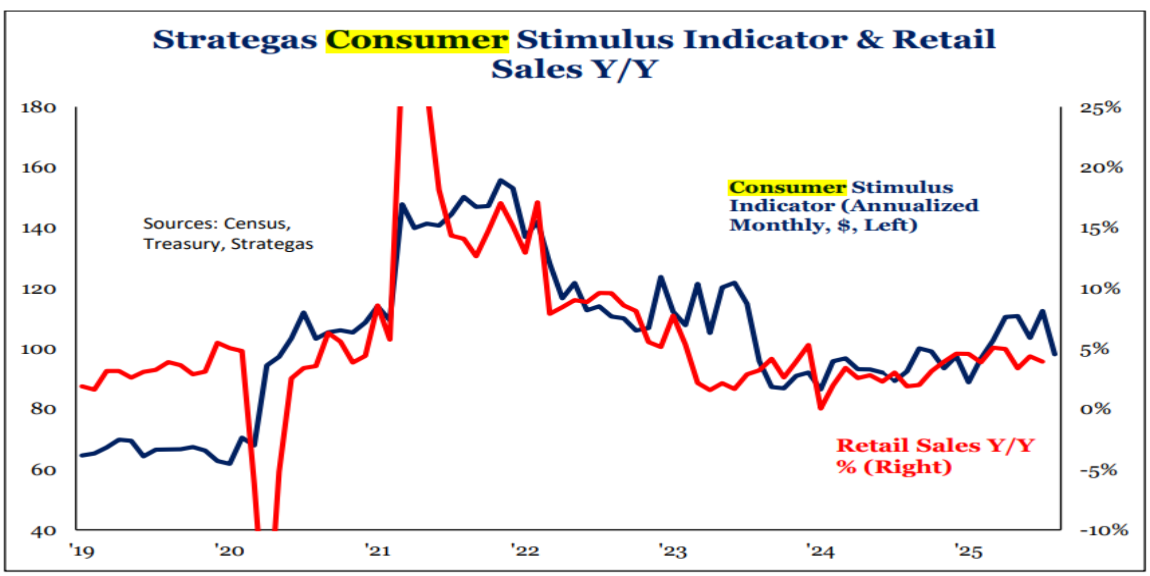


This naturally raises the question of how the government shutdown might further impact the labor market. The same concerning reports we've seen on inflation over the past eight months have appeared here, with many grim predictions. Of course, no one knows precisely what will happen, but if history is any guide, the actual effects are likely minimal. Past episodes have shown little lasting impact on the economy or markets. To put it in perspective: only about 25% of government spending will be affected, since 75% is considered essential and will continue as usual. One caveat this time is that the Trump administration has indicated they are seeking opportunities to continue reducing government staff to shrink the size of government.

Consumer behavior remains a crucial factor in economic resilience. High-income households continue to drive spending, supported by strong balance sheets and positive wealth effects. Sentiment has weakened, and resistance to price increases is growing, especially among lower-income groups facing disproportionate inflation pressures. Looking ahead, provisions in the recently passed tax bill are expected to inject over $150 billion into consumer accounts in 2026, potentially boosting retail sales and supporting discretionary sectors.



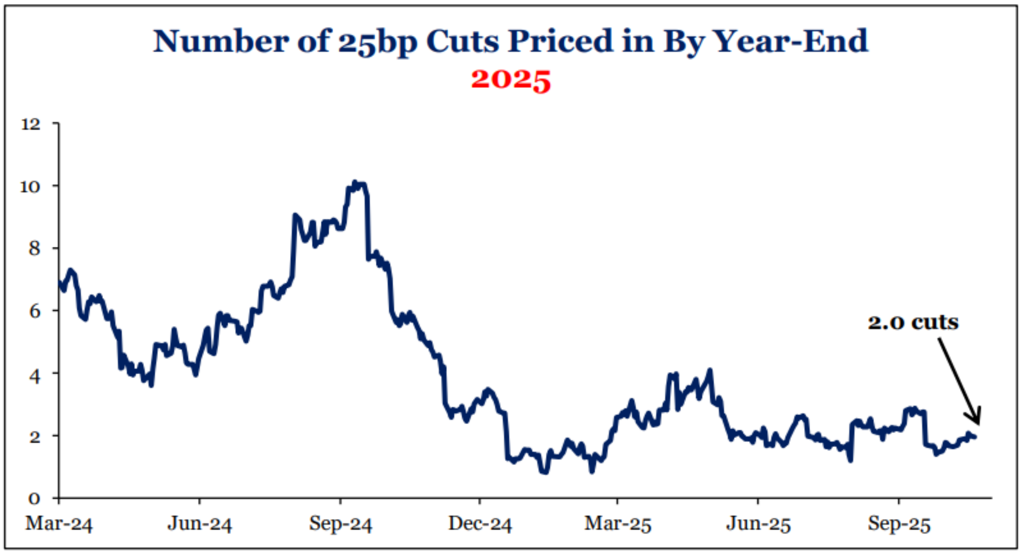
This stimulus will start reaching consumer accounts in 2026 and is likely to boost retail sales rapidly. This should bolster overall economic growth and act as a tailwind for consumer discretionary stocks.



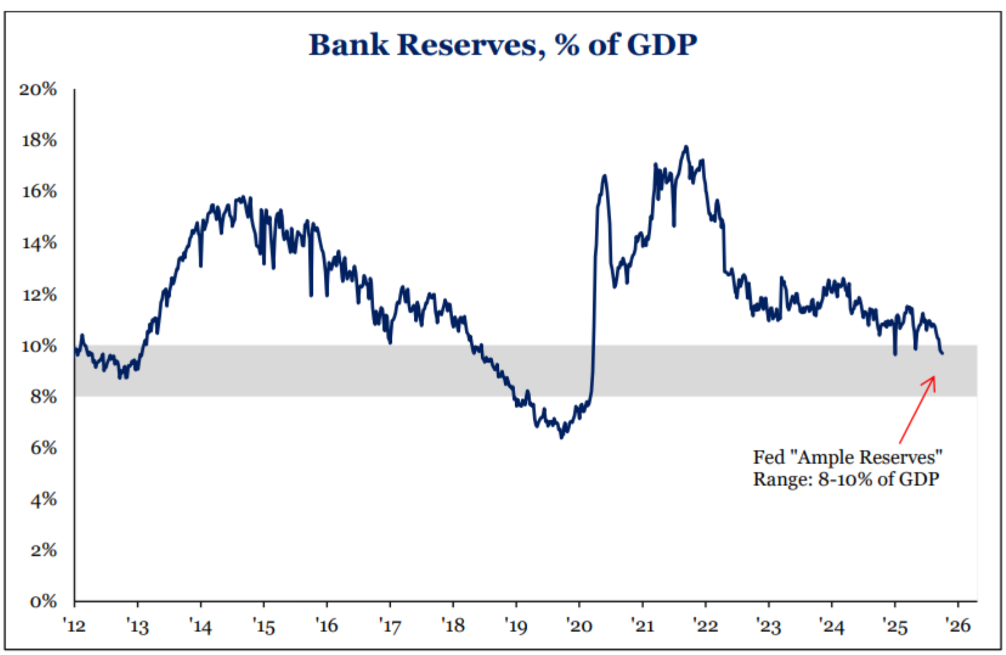
In summary, key recurring themes in the report on the US economy include the uneven distribution of resilience, the transformative impact of AI on labor dynamics, and the importance of productivity gains for sustaining growth. While short-term risks remain, structural supports and policy measures offer a pathway toward stabilization and gradual improvement.

Monetary Policy & Fed Outlook Highlights

Recent developments in U.S. policy indicate a significant change in monetary, fiscal, and liquidity dynamics. The Federal Reserve is likely to end its Quantitative Tightening program soon, which could save $265 billion in bank reserves each year. This adjustment is roughly equivalent to a quarter-point rate cut and aligns with market expectations for further rate cuts.



Chairman Powell's comments before liquidity-draining events such as tax payments and Treasury settlements underscore the need for this policy change. The Treasury's questions about reinvestment strategies further indicate a shift in monetary operations.



Critical points for policy

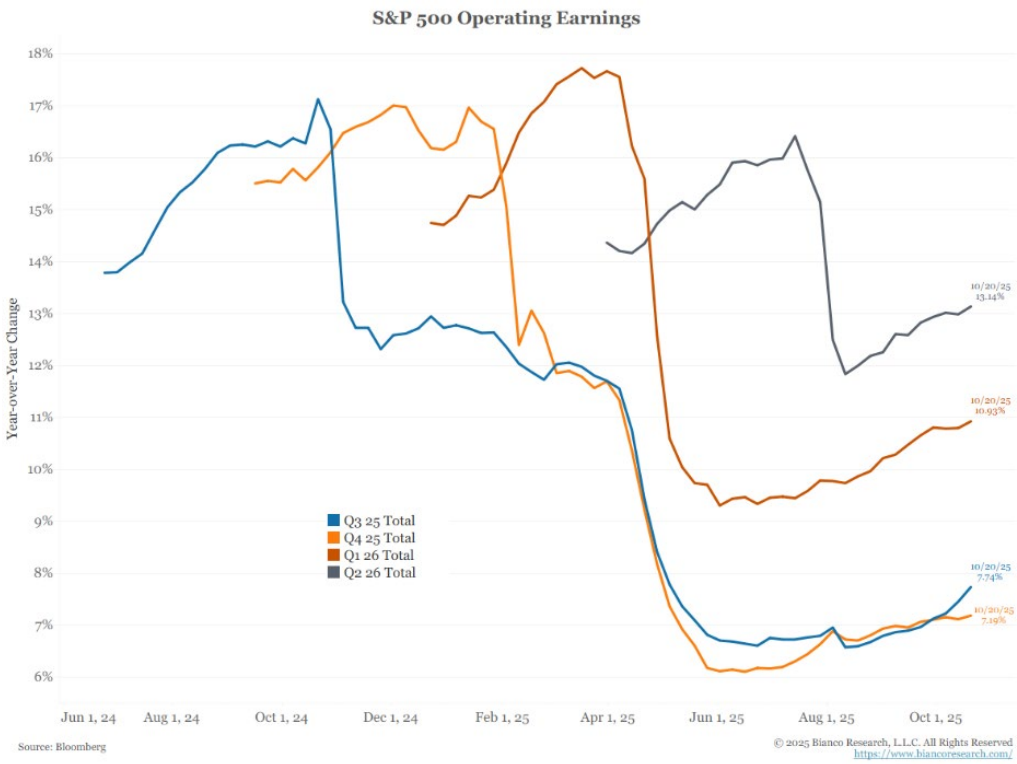
- The Federal Reserve is expected to conclude its Quantitative Tightening program soon, maintaining $265 billion in bank reserves annually and aligning with market expectations for further rate cuts.
- Fiscal policy is moving toward expansive tax cuts, deregulation, and strategic reshoring, with $100 billion in business tax relief and $150 billion in consumer aid planned.
- Liquidity conditions have tightened due to significant October tax payments, especially from high capital gains areas, affecting bank reserves.
- The government shutdown is expected to have a limited economic impact, as bipartisan efforts are underway to resolve budget issues.

On the fiscal front, the administration is moving toward a policy framework characterized by significant tax cuts, deregulation, and strategic reshoring. This strategy implies a multi-year positive shock to economic growth. The bipartisan support for fiscal stimulus requires monetary support, including possible yield curve control and targeted balance sheet expansion. Recent and expected measures—such as $100 billion in business tax cuts and $150 billion in consumer aid—highlight the scale of fiscal support.

Domestically, U.S. liquidity conditions have tightened due to large October tax payments, especially in areas with high capital gains. These payments decrease bank reserves by moving funds to the Treasury General Account, affecting market liquidity.

Corporate Profitability Highlights

Corporate profitability in the U.S. continues to demonstrate resilience amid shifting economic conditions. S&P 500 earnings growth is projected to reach 7.74% in the third quarter of 2025 and exceed 10% in early 2026.



Financials rose significantly with nearly 19.4% growth. Still, Technology remains a key driver, with earnings growth estimated at 22.2%. However, any disruption to AI-related capital spending could affect this outlook. Healthcare, on the other hand, faces challenges, with earnings expected to decline by 4.6%. Analysts' estimates, which are usually conservative before earnings season, have been revised upward as companies report stronger-than-expected results.

Critical points for profitability

- S&P 500 earnings are expected to grow 7.74% in Q3 2025 and surpass 10% by early 2026, led by financials and technology.
- Analysts' estimates have increased during earnings season, driven by stronger-than-expected results and rising optimism across sectors.
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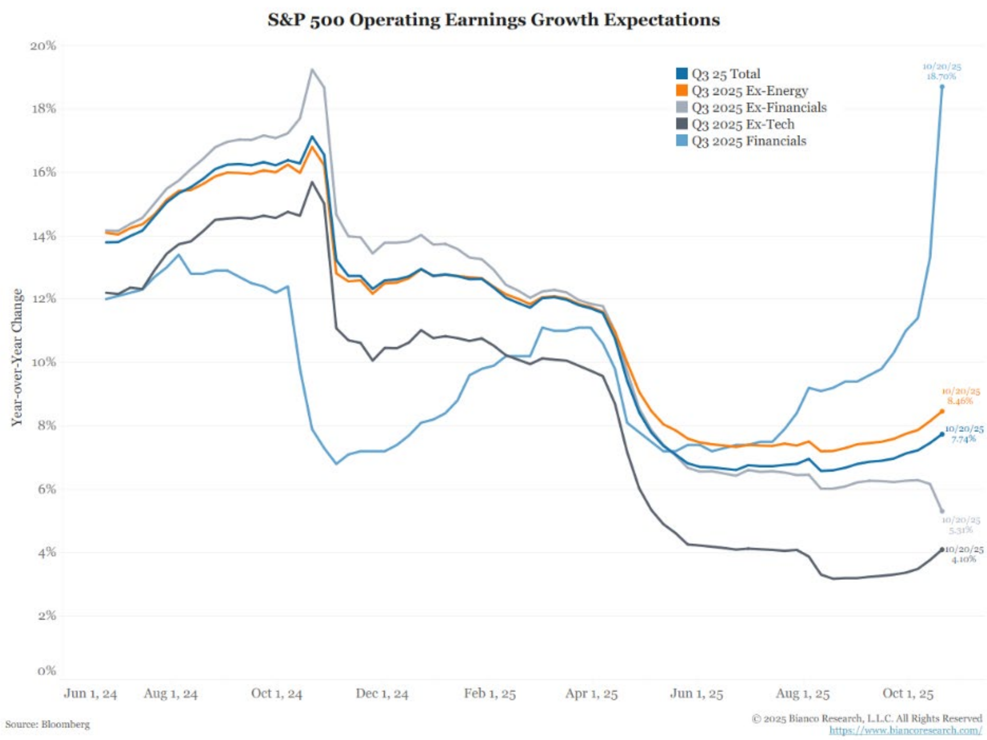
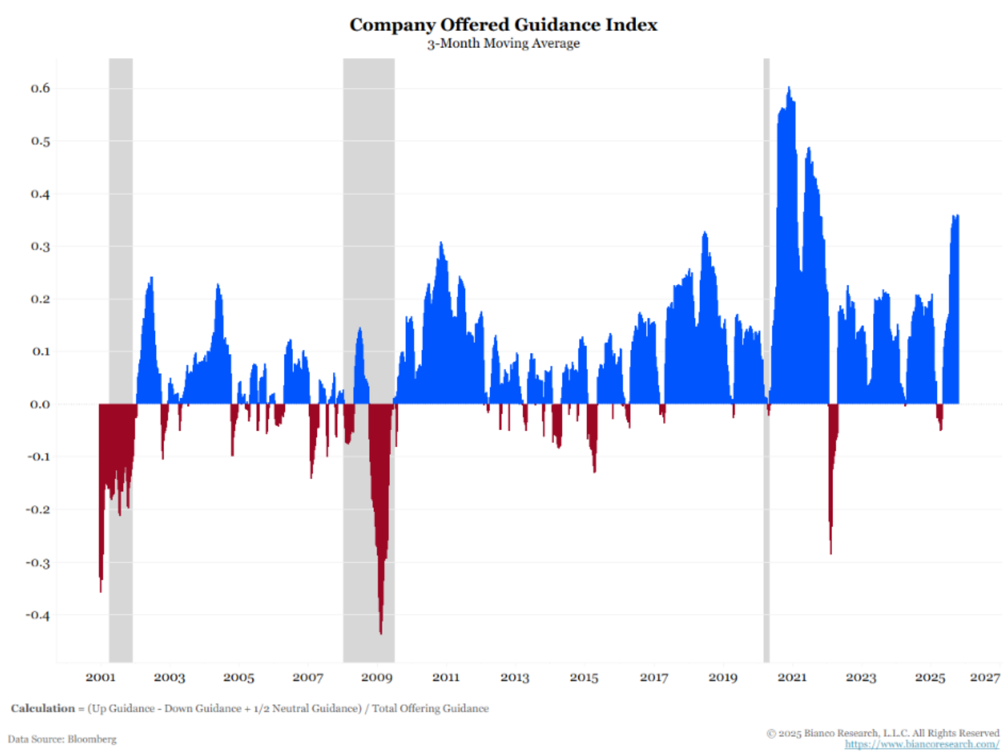
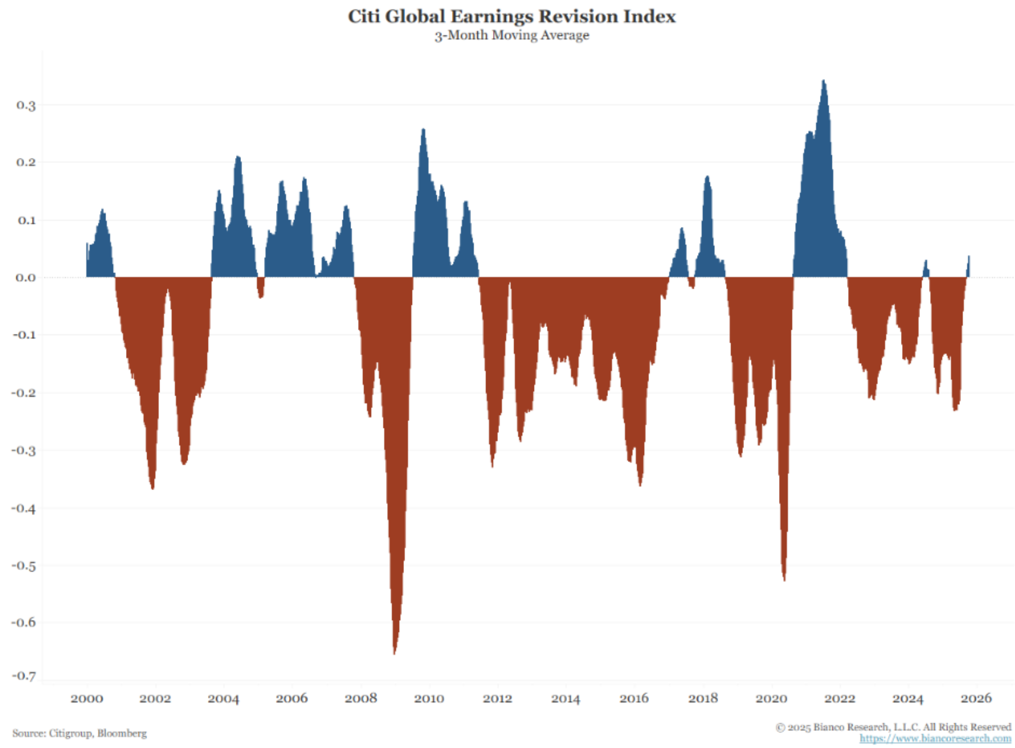


The Guidance Index reflects an essentially optimistic view from corporate management, showing confidence in year-end results despite broader uncertainties. This optimism aligns with the larger economic picture, where GDP growth has been revised upward, and consumer sentiment remains strong. Even with ongoing worries about the business outlook through 2025, companies still expect a positive year-end.



Over a 3-month rolling period, analysts had been lowering their expectations until recently. Still, now they seem to be growing more optimistic and are raising them, according to the Citi Global Earnings Revision Index. Why might they be boosting their forecasts if everyone is predicting an economic slowdown? The main reason could be that company management has remained very optimistic.



Recurrent themes in the U.S. corporate profitability report include the stabilizing effect of corporate earnings in the broader economy and the importance of sector-specific performance, especially in financials and technology. Corporate profits serve as a buffer against macroeconomic volatility, and the overall growth trend, while slow, is improving. Looking ahead, stimulus measures like the OBBB bill are expected to support consumer spending, which could further boost corporate performance. As companies continue to update their guidance, maintaining a balanced view will be essential for interpreting trends and managing investor expectations.