VIEWPOINT

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Economic Commentary:

Business Investment Leads a Slow-Growth Economy

September 2026

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Economic data received over the past month continues to show an economy growing below potential, but at a slow and steady pace. The outlook remains complicated by uncertainty surrounding the U.S.-Iran conflict, monetary policy, expanding fiscal deficits and the competition for capital created by the AI investment boom. With no formal meeting of the Federal Open Market Committee (FOMC) in August, attention turned to Kevin Warsh's inaugural address at Jackson Hole late in the month. He left little doubt that the Fed remains firmly focused on bringing inflation down to its 2% target.

Inflation improves but risk remains

Inflation data provided some encouragement. July headline Consumer Price Index (CPI) rose just 0.1%, lowering the year-over-year rate to 3.4% from 3.5% in June. The three-month annualized trend is now just 0.5%. Core CPI increased 0.2%, with the year-over-year rate falling to 2.5%, matching the five-year low reached in February. Core inflation is running at just a 1.6% annualized rate over the past three months, while services inflation is running at 2.1%. The Fed's preferred measure, core personal consumption expenditures (PCE), rose 0.2% in July, leaving its year-over-year increase unchanged at 3.3%.

The inflation outlook, however, remains vulnerable to energy prices and fiscal pressures. If second-round inflation effects from higher oil prices remain limited, underlying inflation pressures will depend largely on broader economic conditions and the health of the labor market. Services inflation is particularly sensitive to domestic economic conditions, making it one of the components policymakers can influence most directly and one that warrants close attention.

Along with inflation concerns, long-term Treasury yields face pressure from the enormous borrowing requirements of the federal government and the growing demand for capital from the technology sector. U.S. corporate debt issuance has reached $1.68 trillion this year, up 27% from the same point in 2025. AI-related borrowing has become a significant additional source of competition for capital.

Household purchasing power under pressure

The consumer remains the softer side of the economy. Real disposable personal income exceeded real consumer spending in July for the first time since January, resulting in an increase in the personal savings rate to 3.0% from 2.6% in June. Nevertheless, the savings rate remains well below the 4.5% level recorded last July. The continued squeeze on household purchasing power is also evident in corporate earnings reports. Walmart provides perhaps the clearest window into the U.S. consumer and reported its smallest comparable-sales gain in six years in its second quarter results. While transactions remained positive, the average ticket was weak, suggesting that consumers are trading down and purchasing less on each trip.

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John Beuerlein
Chief Economist, Pohlad Companies

Record margins support business investment

The second estimate of second-quarter GDP growth was unchanged at a 1.5% annualized rate. Consumer spending was revised higher, but stronger imports offset some of that improvement. Corporate profitability, by contrast, remains exceptionally strong. Corporate profits grew at an annualized rate of more than 40% in the second quarter and more than 20% year over year. Profit margins for non-financial corporations are now at their highest level since World War II. Record margins should provide support for continued business investment.

AI remains a major driver of that investment. Total construction spending declined 0.5% in July and 3.8% year over year, but data center construction increased 6% for the month and 57% year over year. Excluding data centers, non-residential construction spending was down 1.3% year over year. Encouragingly, investment appears to be broadening beyond AI, with non-AI business investment rising at its fastest pace in three years.

Business surveys remain consistent with continued, albeit moderate, economic expansion. The two Institute of Supply Management (ISM) indexes point to third-quarter GDP growth slightly above 2% annualized. Manufacturing appears to have considerable momentum, with depleted inventories and strong new orders supporting continued expansion in production. At the same time, higher oil prices, shifting tariffs and AI-related demand are pushing input costs higher.

The ISM services survey showed a similar pattern, with its price index rising to its highest level since August 2022. The simultaneous increase in order backlogs suggests that broader supply-chain pressures and elevated energy prices are contributing to renewed price pressures.

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Labor market stabilizes and rebalances

The August employment report was stronger than expected. Nonfarm payrolls increased by 162,000, while the July decline in employment was revised to show a small increase. Even so, the underlying pace of job creation remains only modestly above the level needed to keep the unemployment rate stable. The unemployment rate held at 4.1%, while wage growth eased to 3.1% year over year from 3.2%. With productivity increasing by more than 2% annually, wage growth near 3% is consistent with continued moderation in core inflation. The slowing pace of wage growth suggests that the labor market is currently contributing to disinflation rather than adding to inflationary pressure.

More importantly, the labor force expanded by 683,000, reversing much of the decline seen earlier in the year. Other labor indicators, including the Job Openings and Labor Turnover Survey (JOLTS) and the Automatic Data Processing (ADP) National Employment Report , point to a relatively stable "no-hire, no-fire" environment rather than a rapidly weakening labor market.

Rate outlook constrained by capital demand

The September 15–16 FOMC meeting will therefore be driven primarily by the inflation data. With the labor market showing greater stability, the August CPI report on September 11 has become the key near-term indicator for monetary policy. Markets are currently showing a 60% probability of a 25-basis-point rate increase. With inflation still above target, strong corporate investment and substantial government and AI-related borrowing competing for capital, the case for significantly lower interest rates remains difficult to establish.

The broader picture is one of an economy expanding at a modest pace, supported increasingly by business investment and AI, while consumers face continued pressure on purchasing power. Inflation is moving in the right direction but remains above the Fed's target. For investors, the combination of persistent fiscal borrowing, heavy corporate issuance and AI-driven demand for capital suggests that even as inflation moderates, long-term interest rates may remain higher than they were in the pre-pandemic environment.

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