



SPECIAL MID-QUARTER EDITION

Economic Commentary:

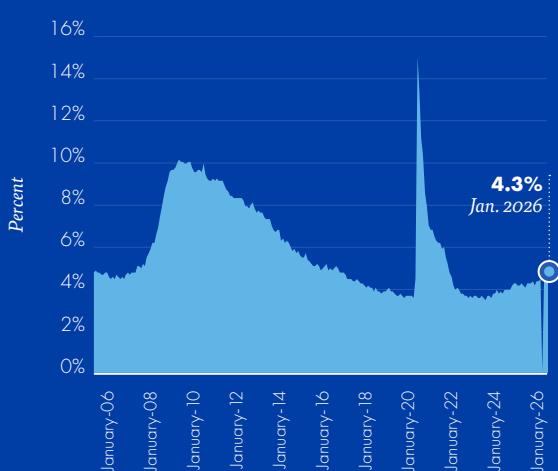
Consumer Spending Faces Sustainability Challenges

February 2026

GROSS DOMESTIC PRODUCT (GDP)



UNEMPLOYMENT RATE



RETAIL / FOOD SERVICE SALES



Source: Northmarg, U.S. Bureau of Economic Analysis,
U.S. Bureau of Labor Statistics, U.S. Bureau of the Census; Oct 2025 data not available

February 2026

We are still working through delays in the data following the October government shutdown. Even with incomplete information, the picture that is emerging points to an economy largely supported by higher-income households benefiting from the wealth effect of a strong equity market, while overall labor market growth remains minimal. That combination has left the consumer base bifurcated – an imbalance that does not support durable, long-term expansion. This divide may widen in the year ahead, as the OBBBA tax reductions primarily favor higher-income households, while reductions in social benefits weigh more heavily on lower-income families.

Moderating Inflation with Persistent Service-Sector Pressures

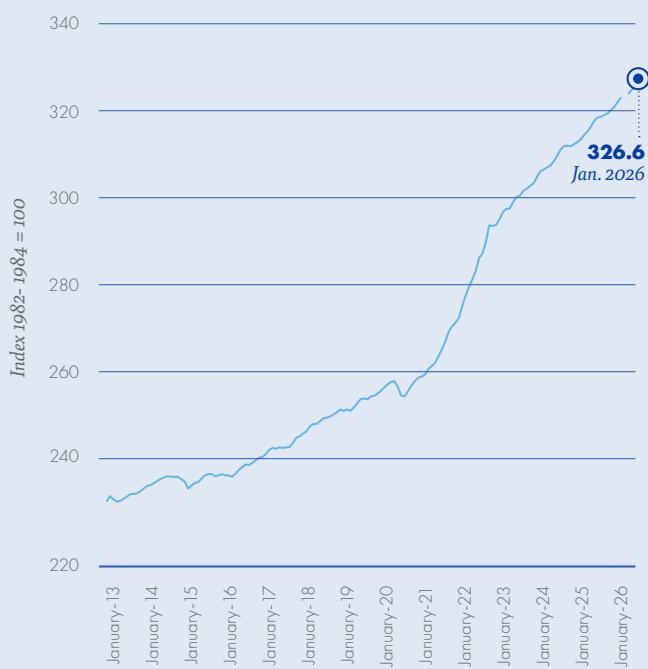
The January Consumer Price Index (CPI) increased 0.2%, bringing the year-over-year rate down from 2.7% to 2.4%. Core CPI rose 0.3%, with the annual rate easing to 2.5% from 2.6%, marking its lowest level since April 2021. Core goods prices were flat for the month and have risen at just a 0.4% annualized pace since September – an area where tariff effects might otherwise be expected to appear. In contrast, services inflation remains persistent, climbing 0.4% in January and 3.2% year over year.

Although the CPI report suggests continued moderation in inflation, the Federal Reserve will place greater weight on its preferred measure, the Core Personal Consumption Expenditures (Core PCE) Index, which is scheduled for release on March 13.

Consumer Spending Sustained by Savings, Not Income

Income and spending data continue to lag due to the shutdown, leaving November data as the most recent available. Real disposable personal income rose just 0.1% in November and has declined by \$102 billion at a -1.0% annualized rate since April. Despite this erosion in real income, consumer spending has held up. Real personal consumption expenditures increased 0.3% in November and have advanced \$269 billion at a 2.8% annualized rate since April. However, this resilience has been funded by savings rather than income growth. The personal saving rate dropped to 3.5%, a three-year low and roughly half its pre-pandemic level. Without the drawdown in savings from April through November, real consumer spending would have contracted at a -0.9% annualized rate instead of posting a 2.8% gain.

CONSUMER PRICE INDEX (CPI)



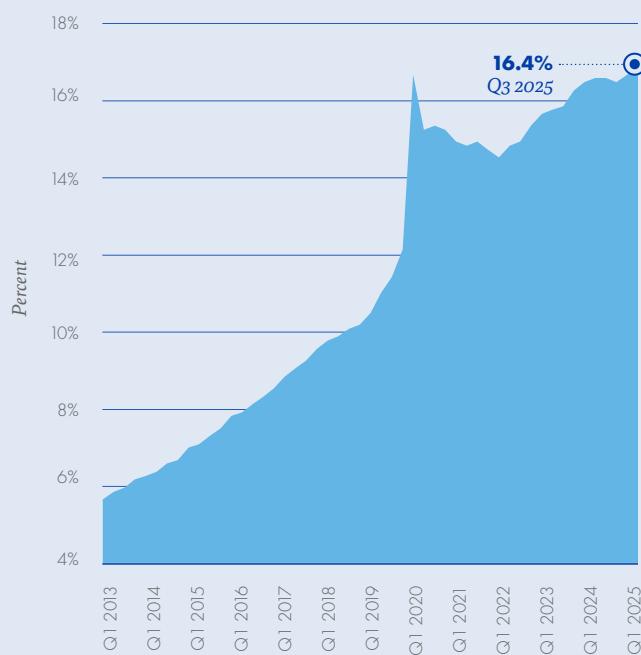
While consumers appear willing to tap into savings to sustain spending, that pattern may not be sustainable if labor market conditions deteriorate further or borrowing costs remain elevated. Household loan delinquencies, including mortgages and credit cards, rose to 4.8% of outstanding U.S. household debt in the fourth quarter of 2025 – the highest since 2017.

The initial estimate of fourth-quarter GDP will be released on February 20.

Manufacturing Rebounds but Sentiment Remains Cautious

The ISM Manufacturing Index surprised to the upside in January, rising to 52.6 and returning to expansion (above 50) for the first time in 12 months. New orders posted their strongest reading since February 2022, and export orders reached their highest level since last February. Production increased sharply from 50.7 to

E-COMMERCE RETAIL SALES (% OF TOTAL SALES)



55.9 in response to stronger demand. Even so, only 9 of 18 industries reported growth, and sentiment remained cautious. The employment sub-index stayed in contraction for the 28th straight month, reflecting ongoing staff reductions and restrained hiring.

The ISM Services Index held steady at 53.8, signaling continued expansion. While several demand-related sub-indices softened, though they remained above 50, business activity rose to a 13-month high of 57.4. The elevated prices-paid component indicates that services-related inflation pressures persist.

Labor Market Gains Mask Underlying Weakness

The January employment report showed a stronger-than-expected gain of 130,000 non-farm payroll jobs, the largest increase since December 2024. Private payrolls rose by 172,000, while government employment declined by 42,000. However, much of the gain was concentrated in education and health services, which added 137,000 jobs. Outside those sectors, employment declined. For full-year 2025, education and health services added 697,000 jobs, while total non-farm payrolls rose just 181,000, implying a net contraction of 516,000 jobs outside those two industries.



The unemployment rate edged down from 4.4% to 4.3%, as the household survey showed a 528,000 increase in employment, outpacing the 387,000 rise in the labor force.

Annual revisions to the 2025 data revealed that payrolls were overstated by 1 million jobs, reducing average monthly job gains to 15,000 from the previously reported 50,000.

There were some constructive signs in the January report: the number of workers employed part-time for economic reasons fell by 453,000, and multiple jobholders declined by 79,000. Average hourly earnings increased 0.4% for the month (3.7% year over year), while the average workweek ticked up from 34.2 to 34.3 hours.

Underscoring ongoing labor market fragility, the Challenger report showed 108,435 job cuts in January, up 118% from January 2025 and 205% from December levels, the highest January total since 2009. Announced hiring plans were the lowest for the month since tracking began in 2009.

The December Job Openings and Labor Turnover Survey (JOLTS) indicated that job openings have fallen 13.0% year over year to their lowest level since September 2020. There are now 15% more unemployed individuals than available job openings, signaling that labor supply has overtaken demand and should help contain wage pressures.

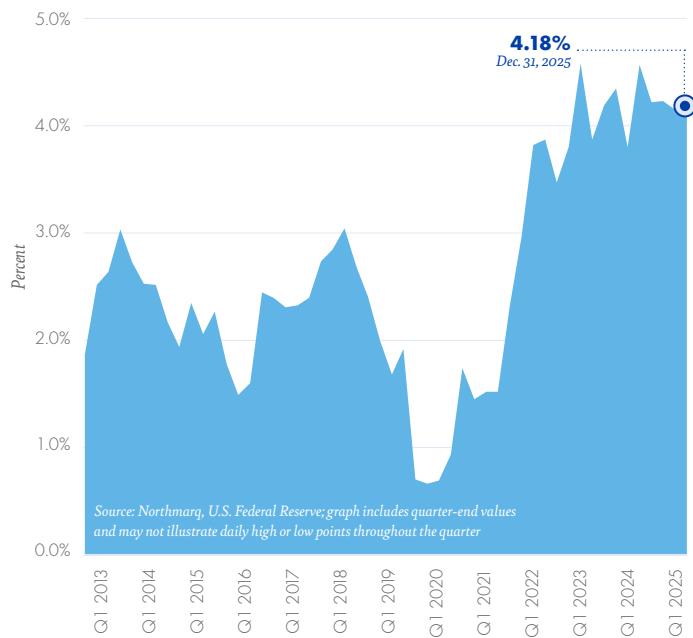


Fed Holds Rates, Monitors Growth and Labor Trends

At its January meeting, the Federal Open Market Committee (FOMC) left the federal funds target range unchanged at 3.50%–3.75%. Chair Powell emphasized that short-term inflation expectations have declined meaningfully and that longer-term expectations remain anchored near the Fed's 2.0% objective. Excluding tariff-related effects, core inflation is now close to target. The Fed believes inflation risks have diminished, and the labor market is stabilizing, but it stands ready to respond if employment weakens further.

Looking ahead, the Fed's next policy move will likely hinge on growth dynamics. Should labor market softness persist or intensify, consumer spending and GDP growth may slow, increasing the likelihood of a more forceful policy response. Financial markets are currently pricing in two rate cuts in the second half of the year.

10-YEAR TREASURY RATE



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