ECONOMIC INDICATORS

5 forces could stimulate the U.S. economy

Cheryl Frank, Damien McCann, Brittain Ezzes and Mark Casey

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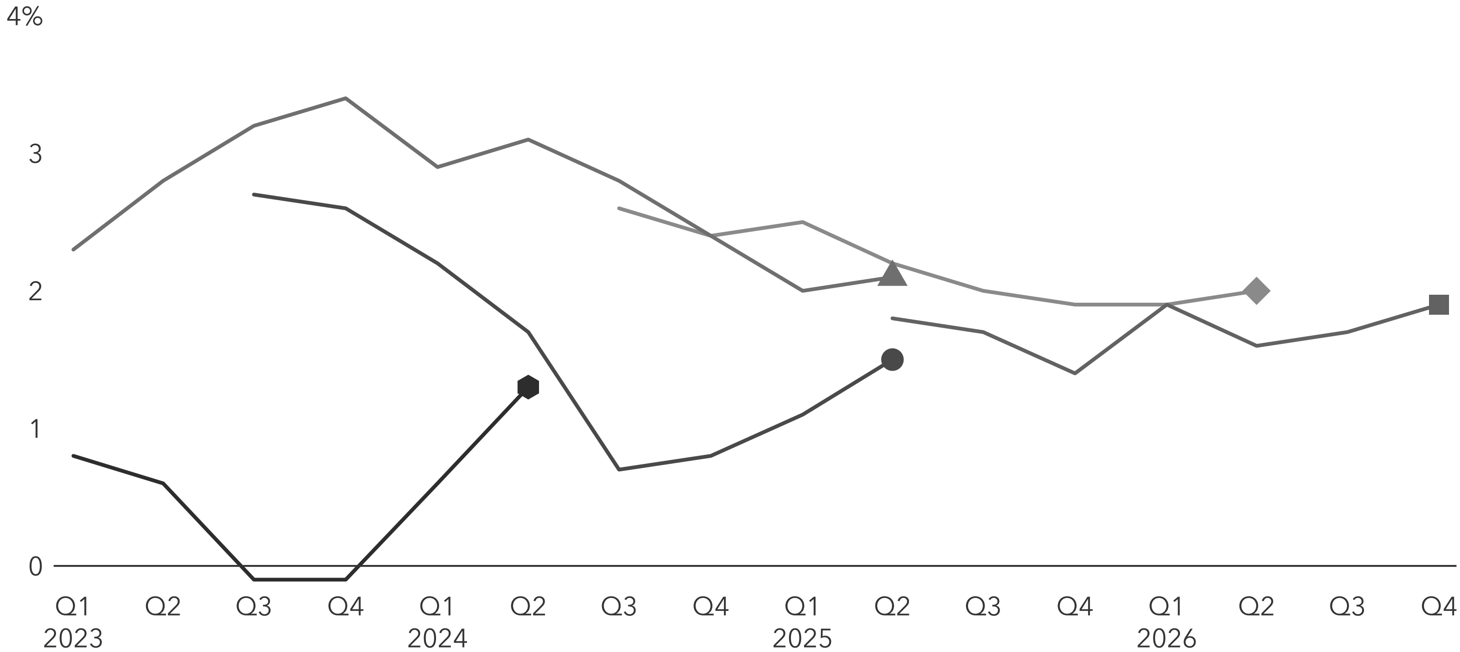
The U.S. economy has demonstrated surprising resilience in the six months since President Trump unveiled a long list of tariffs against virtually every trading partner. In the aftermath of "Liberation Day," fears of an imminent recession have eased as investors have started to envision a future without a tariff-induced trade war.

"Tariff uncertainty hasn't fully abated but the administration has moved away from brinkmanship in favor of negotiations," says Cheryl Frank, portfolio manager for CGCV – Capital Group Conservative Equity ETF.

Slowing job growth and consumer spending patterns suggest the economy is weakening. However, there are reasons for optimism, Frank notes. From the passage of the tax bill to declining interest rates, there is less uncertainty on many fronts compared to earlier this year. Below are five forces that could pave the way for continued economic expansion.

U.S. economic growth has continuously surprised to the upside

- Consensus (12/31/2022)
- Consensus (12/31/2023)
- Consensus (12/31/2024)
- Consensus (9/30/2025)
- Real GDP Y/Y



Sources: Capital Group, Bloomberg. Consensus reflects sell-side U.S. Real GDP year-over-year growth estimates. Real GDP (gross domestic product) is the inflation-adjusted value of the goods and services produced by labor and property located in the United States.

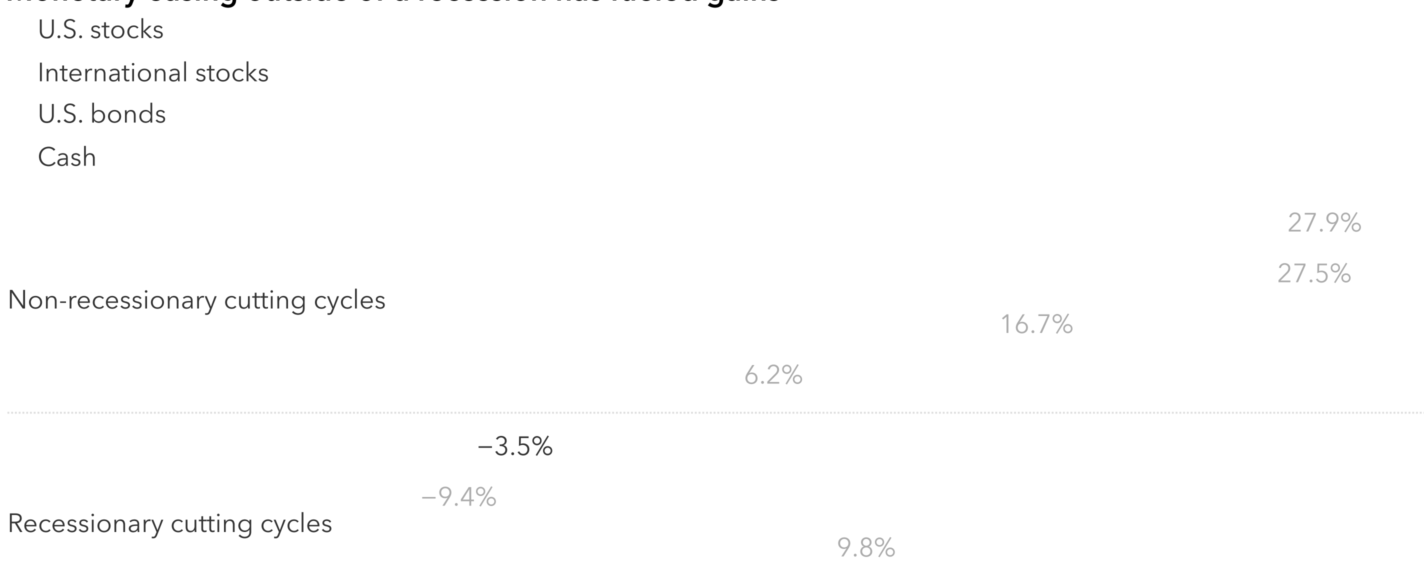
1. A dovish Fed starts rate-cutting cycle

The Federal Reserve's latest rate cut arrived at a moment of economic softness — namely sluggish job growth. Officials guided additional cuts through 2028, signifying a dovish stance.

Rate cuts usually lead to higher company spending and hiring, and more sales of big-ticket items such as cars and homes. "There's a long list of companies waiting for rates to drop, especially those tied to the housing market," Frank notes. Potential beneficiaries include retailers such as Home Depot, heating and cooling system manufacturers such as Carrier Global and paint companies such as Sherwin-Williams.

Markets have rewarded investors when rate cuts happen outside of a recession. On average, the S&P 500 Index returned 27.9%, while the Bloomberg U.S. Aggregate Index returned 16.7%.

Monetary easing outside of a recession has fueled gains



Sources: Capital Group, Bloomberg Index Services Ltd., Morningstar, Standard & Poor's. Return calculations reflect annualized total returns over periods in which the U.S. Federal Reserve had stopped raising rates and began to actively cut rates, measured from the peak federal funds rate target to the lowest federal funds rate target for each cycle. Specific easing cycles include August 1984 to August 1986 (non-recessionary), May 1989 to September 1992 (recessionary), February 1995 to January 1996 (non-recessionary), March 1997 to November 1998 (non-recessionary), May 2000 to June 2003 (recessionary), June 2006 to December 2008 (recessionary) and December 2018 to March 2020 (recessionary). Benchmarks used are the S&P 500 Index (U.S. stocks), MSCI World ex USA Index (international stocks), Bloomberg U.S. Aggregate Index (U.S. bonds) and the average investment rate of 3-month U.S. Treasury Bills (cash). As of December 31, 2024.

Still, there are concerns borrowing costs may not decline to levels that rekindle spending. After all, the Fed cut interest rates in September 2024, only to see the benchmark 10-year U.S. Treasury, which underpins borrowing costs, rise instead. The culprit? A string of unexpectedly strong economic data prompted investors to recalibrate policy expectations, pushing rates higher.

So far this year, the 10-year Treasury has declined over half a point to 4.13% on October 8, from a level of 4.79% in January. A more amiable Fed, particularly if the administration has more sway with rate setters, could explore unconventional tools to suppress long-term yields, says Damien McCann, portfolio manager for CGMS – Capital Group U.S. Multi-Sector Income ETF and American Funds® Multi-Sector Income Fund. "It's not a prediction, but a possibility worth considering."

2. Tax bill functions as a "massive stimulus check"

A notable feature of the One Big Beautiful Bill Act is the inclusion of retroactive tax cuts for 2025, with refunds to taxpayers expected in early 2026.

Other aspects of the bill, such as exemptions for overtime and tips, translate to unusually large tax refunds totaling over $200 billion in early 2026. "It could function as a massive stimulus check," Frank says. The one-time cash infusion may serve as a powerful psychological boost to consumer confidence and provide some relief to tariff-related inflation.

The bill also favors companies that invest in the U.S. by lowering their taxable income. Specifically, companies can quickly expense spending on research and development, capital investments and new factories. As a result, technology and defense companies may see a boost in free cash flow.

Not all sectors are winners, as the bill rolls back some prior subsidies for clean energy and health insurance. Moreover, the plan increases the national debt significantly over the long run, which could fan inflation and weigh on growth.

3. Deregulation can spur growth outside of AI

A deregulatory environment could benefit some companies, including those left out of the artificial intelligence boom.

"Many businesses not on the cutting edge of technology have been left behind," says Brittain Ezzes, portfolio manager for CGVV – Capital Group U.S. Large Value ETF. "Broadly speaking, companies in the energy, industrials and telecommunications sectors could be helped by deregulation."

Investors are also closely tracking bank deregulation since it could increase lending activity across industries — a potential tailwind for the economy. Wells Fargo Bank, for example, has faced years of regulatory scrutiny and was limited in its ability to grow revenue. But Ezzes sees potential: The bank hired a new management team in 2019 that worked to restore its reputation. The removal of its asset growth restriction coupled with a more favorable regulatory climate could expand the company's lending base and earnings potential.

"With the deregulation push by the U.S. administration, companies may feel less constrained in making investment decisions," McCann adds.

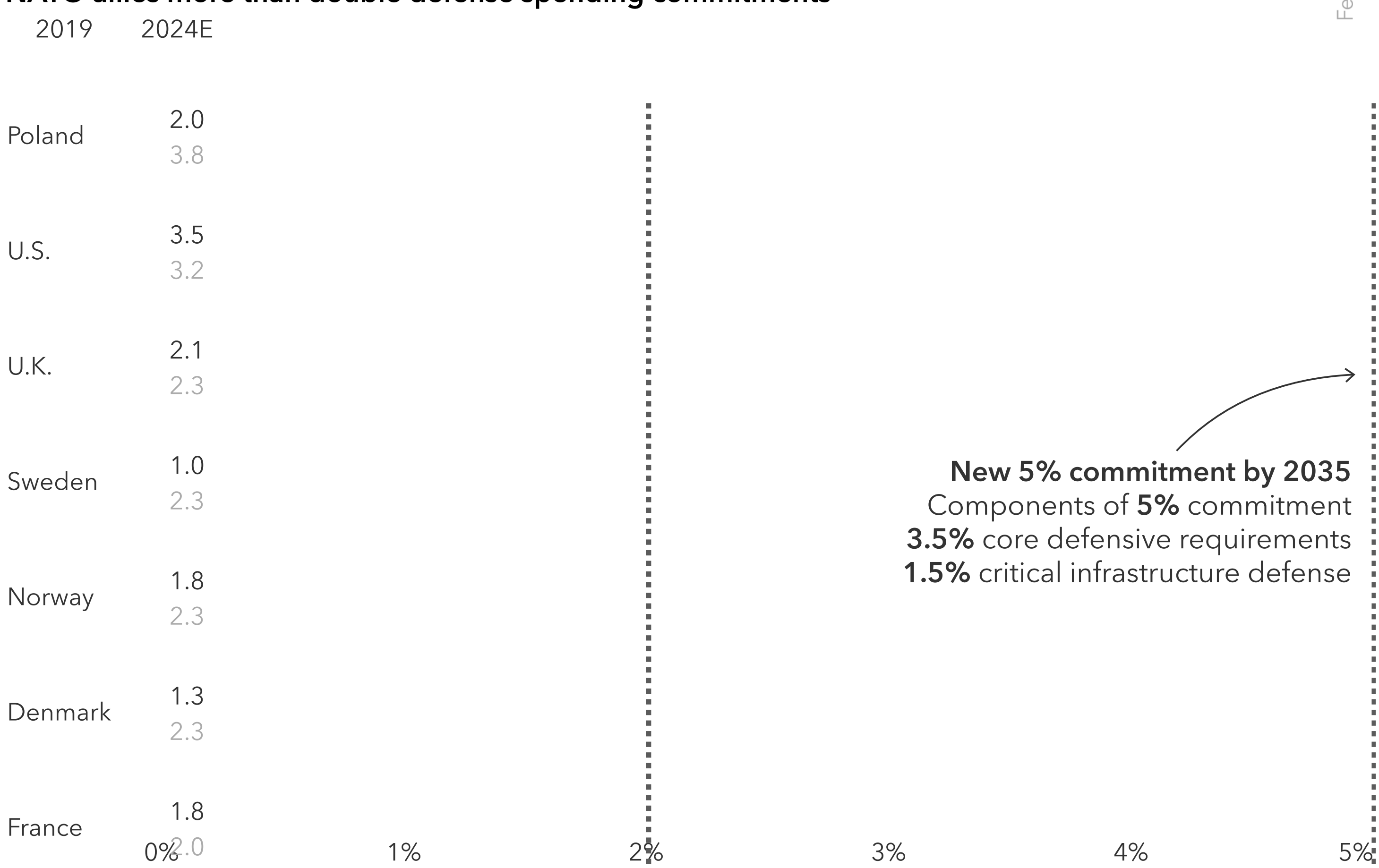
So far this year, cable giants Charter Communications and Cox Communications are set to merge, and Union Pacific aims to forge a coast-to-coast rail system via its acquisition of Norfolk Southern. Both deals underscore a broader wave of consolidation that may test the boundaries of antitrust concerns. On the flip side, McCann notes, fewer regulatory eyes mean investors need to be vigilant of potential risks.

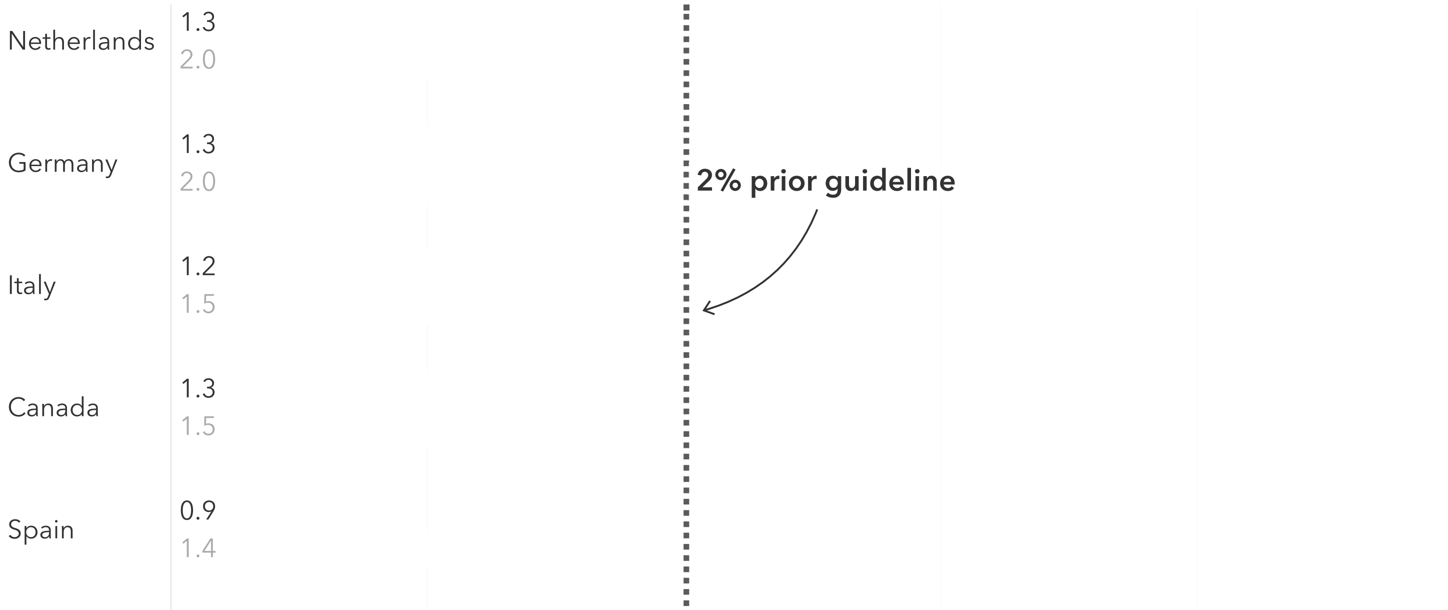
4. Rising defense budgets are a long-term tailwind

As NATO partners boost defense budgets, demand for products across a range of industries should jump, according to Frank.

In June, NATO allies committed to increasing defense spending from 2% to 5% of GDP by 2035 — a dramatic shift that's reflective of mounting geopolitical tensions as tariffs threaten supply chains and strain alliances. Germany, in particular, has taken the lead. It previously disclosed aggressive fiscal stimulus focused primarily on defense and infrastructure.

NATO allies more than double defense spending commitments





Sources: Capital Group, NATO. Figures for 2024 are estimates based on most recently available data, as of August 28, 2025. New 5% commitment was announced June 27, 2025. Percentage of GDP is based on constant prices and exchange rates, indexed to 2021. NATO defines defense expenditure as payments made by a national government specifically to meet the needs of its armed forces, those of Allies or of the Alliance. Critical infrastructure defense consists of investments to protect critical infrastructure, defend networks, fund innovation and strengthen the defense industrial base.

Rising defense budgets represent a long-term tailwind for many U.S. companies, since the majority of advanced defense systems are made in America. U.S. contractor RTX, known for its sophisticated radar and missile systems, has seen demand climb as European and Middle Eastern nations pursue modernization. The growing adoption of drone technology is also expected to benefit companies like U.S.-based Northrop Grumman as well as U.K.-based BAE Systems.

In Germany, defense backlogs are mounting. Rheinmetall, a leading manufacturer of advanced systems, reported a backlog increase of 29.9% to €63.2 billion as of June 30, 2025.

5. AI investments continue to climb

Spurred by the arrival of ChatGPT, the AI economy has become a powerful engine of U.S. growth. As of June 30, 2025, technology spending — which includes research and development and data centers — accounted for roughly 7.5% of U.S. GDP, surpassing the dot-com era peak and poised to rise further.

"AI systems have made remarkable progress, but we're still very early innings of the AI deployment over the next decade," says Mark Casey, portfolio manager for CGGR – Capital Group Growth ETF and The Growth Fund of America®. He expects widespread adoption of AI across industries, which could drive productivity gains and innovation.

However, the economic impact will be uneven, with some companies benefiting greatly while others face disruption or decline. Over the next decade, Casey anticipates the AI ecosystem will grow but also exhibit cyclicality, with periods of optimism followed by occasional setbacks when expectations outpace reality.

An economy on the move

The U.S. economy is vulnerable. Typical forces that propel growth — job creation, consumer confidence and business investments — have stalled. New potential tailwinds are untested, with long-term ramifications to the nation's fiscal health and geopolitical alliances. Inflation remains elevated, with the full impact of tariffs yet to come. Meanwhile, AI's influence on stock markets and GDP complicates the picture.

Still, there are reasons for optimism as the U.S. economy and stock market have proven naysayers wrong time and again. Over the long run, investors who remained fully invested during periods of heightened uncertainty and market volatility have often emerged stronger. "I believe in staying invested," Frank explains. "Even when markets get a little too excited or fearful, discipline and a focus on fundamentals help me navigate the volatility."

Read important disclosures

***Cheryl Frank** is an equity portfolio manager with 27 years of investment industry experience (as of 12/31/2024). She holds an MBA from Stanford and a bachelor's degree from Harvard.*

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GDP (gross domestic product) is the value of the goods and services produced by labor and property located in the United States.

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Bloomberg U.S. Aggregate Index represents the U.S. investment-grade fixed-rate bond market.

MSCI World ex USA Index is designed to measure equity market results of developed markets. The index consists of more than 20 developed market country indexes, excluding the United States.

S&P 500 Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks.

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