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ARGUS ECONOMIC COMMENTARY

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Cracks in the Foundation: Our Monthly Survey of the Economy, Interest Rates, and Stocks

November was a mixed month, with a deep dive after mid-month and a rally at the finish, this as the stock market moved on shifting expectations for a Fed rate cut at the mid-December FOMC meeting. Investors began November unsettled by the late-October FOMC meeting, at which the Fed cut rates but warned that a December rate cut was no sure thing. The S&P 500 reached its November low on 11/20/25, at which point the index was down 4.7%; that was also lowest closing level since September. The November low point coincided with upbeat jobs data that appeared to increase the likelihood of the Fed standing pat in December. The CME FedWatch tool fell from 50% to a 25% on the likelihood of a December cut. The stock market rallied out of that hole, however, on weak retail sales and softer-than-expected wholesale inflation, sending the CME FedWatch tool probability for December above 85%.

When all was said and done, November ended up just 0.1% on the S&P 500, down on the Nasdaq, and with uncertainty ahead. The three-year rally in stocks has been built on an AI foundation. In November, that foundation showed some cracks.

The Economy, Interest Rates, and Earnings

The federal government is back up and running, but the 40-plus day shutdown has complicated and delayed release of multiple key economic reports. The Bureau of Economic Analysis (BEA) will not issue an advance GDP report for the third quarter, and preliminary 3Q25 GDP will not be released until December 23. There are also delays in non-farm payrolls, personal income and outlays, industrial production, and other reports.

In the absence of hard data, the Atlanta Fed's GDPNow model continues to estimate that third-quarter GDP grew by 3.9%. That estimate has been stable for the past several weeks and has risen from preliminary expectations in the 2% range a month ago.

The third (final) report of second-quarter 2025 GDP indicated growth of 3.8%, representing sharp recovery from a 0.5% decline for 1Q25. Both first and second-quarter GDP featured distortions in the imports and private inventory categories due to trade positioning ahead of the August implementation of tariffs. The third quarter of 2025 was expected to feature the first "clean" GDP report in which those two categories did not distort the underlying trend in consumer and business spending.

Argus Chief Economist Chris Graja, CFA, has been encouraged by the economy's resilience and believes that solid GDP growth continued in the third quarter of 2025. The Argus model estimates 3Q25 GDP growth at 2.6%, below the Atlanta Fed estimate but within the broad 1.7%-3.8% economists' consensus estimate.

Argus is modeling that 3Q25 personal consumption expenditures (PCE) may have risen in the 2% range. In 2Q25, PCE rose by 2.5%. The widely discussed K-shaped economy is resulting in solid spending by the middle- and upper-income consumers, but a slower pace of spending and a shift to bargain goods by lower-income consumers. Services, which is the biggest category in PCE, is being impacted by this trend. Restaurants are reporting fewer visits by younger consumers and families on the bottom leg of the "K," as these folks are redirecting spending away from discretionary items and to necessities.

Argus is forecasting that non-residential fixed investment, the proxy for corporate capital spending, will grow at a 4.5% rate in 3Q25. Non-residential fixed investment rose by 7.3% in 2Q25; that is a step-down from 9.5% in 1Q25, but

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still very solid. We note that the old economy drivers of the business cycle, housing and manufacturing, are sluggish. Amid the AI boom, we estimate that business investments in intellectual property and equipment may have added seven-tenths of a point to 3Q GDP growth.

PCE and non-residential fixed investment normally constitute 80%-85% of GDP. With the pre-tariff positioning and trade distortions of 1Q and 2Q now behind, these two categories may have contributed 2.0-to-2.5 percentage points to 3Q25 GDP growth.

Government spending was down 0.1% in 2Q25 after being down 1.0% in the final 1Q25 GDP report. Argus is modeling a 0.2% decline in 3Q25 government spending, with state and local still positive and federal trending down. Imports and exports are tough to model without government input, given that tariffs were not fully settled at quarter's end. We are modeling exports and imports as having an overall net neutral effect on GDP growth.

Finally, we are modeling 3.0% growth in the core PCE price index (excluding food and energy). This number is close to the 3.1% annual rise in core PPI in September and the 3.0% range in July and August.

Outside the GDP accounts, the government shutdown compromised access to the most widely watched economic release in any month, non-farm payrolls. The government has issued the September report, while also announcing it will not issue a stand-alone October report. The November non-farm payrolls report, slated for release on December 16, will include some October data but not an October unemployment rate.

According to the BLS, the U.S. economy generated 119,000 new non-farm jobs in September. That was much better than forecasts of 50,000 by consensus and 56,000 by Argus. Although both July and August tallies were revised lower, the strong September result pushed three-month average jobs growth to 62,00 from a prior 29,000 as of the end of August.

The unemployment ticked up to 4.4% for September, above the 4.3% consensus call and extending the steady progression upward from 4.3% for August, 4.2% for July, and 4.1% for June. Average hourly earnings grew 3.8% annually for September, up a tick from August and keeping wage growth running ahead of inflation growth.

As stated, the October non-farm payrolls report has been cancelled, and the November report is delayed until 12/16/25. We had been modeling October non-farm payrolls up in the 25,000 range. ADP private payrolls increased 42,000 in October after declining by 29,000 in September. The consensus expectation for November non-farm payrolls is a gain of about 28,000.

The breakeven level of jobs growth, required to hold the unemployment rate steady, is now lower than 150,000 range in recent years because of trends in population growth. Due to sharply reduced immigration and secular decline in native-born birth rates, the St. Louis Fed now estimates breakeven employment growth of 32,000-82,000 per month. Thus, job gains in the neighborhood of consensus estimates would likely keep unemployment stable.

Other reports delayed by the shutdown are now trickling in. Real average weekly earnings, usually released with non-farm payrolls but delayed by a day due to the shutdown, were unchanged for September as monthly inflation offset an increase in hourly earnings. The September producer price index (PPI) rose 0.3% month over month, up from a 0.1% dip in August. The annual change of 2.7%, however, was a tick better than consensus and appeared to give the Fed room to cut rates in December. More delayed data will be released in December, and it could take a month or more to get back on schedule.

Based on sentiment surveys and diffusion indices, the business community appears guardedly optimistic, while consumers are worried about new jobs scarcity. The ISM's manufacturing purchasing managers' index (PMI) edged slipped to 48.7% from October from 49.1% in September. ISM's services PMI rebounded to 52.4% for October from 50.0% for September.

The Conference Board's Consumer Confidence Index fell to 88.7% in November from 94.2 for September and from 97.4 for August. Within this series, the expectations index reading of 63.2% fell 8.6 points and remained below the 80 threshold that some investors believe signals a recession ahead. The University of Michigan's consumer sentiment survey fell to 51.0% for November from a downwardly revised 53.6% for October. The reading was 71.8% a year earlier in November 2024.

In the absence of 3Q25 GDP data and despite no payrolls report scheduled for October, Argus Economics believes the U.S. economy remains on a growth trajectory. We are reiterating our 2025 GDP growth forecast of 1.9%. We believe GDP is likely to remain fairly steady next year, and the current 2026 GDP growth forecast is also 1.9%.

The U.S. Federal Reserve is tasked with the dual mandate of optimizing employment while keeping inflation in check. After raising rates aggressively throughout 2022 and early 2023, the Fed maintained its policy rate at 5.25%-5.50% from September 2023 until August 2024. Beginning in August 2024, the Fed cut rates by a cumulative 100 bps over the next three FOMC meetings. It then moved to the sidelines for the first nine months of 2025.

The central bank cut the fed funds rate in September 2025 for the first time in nine months. It then cut rates again by a quarter point at the end of October. The Fed in September broadly hinted at two additional rate-cuts by year-end. But after the October meeting, Fed Chair Powell stated that a widely anticipated rate cut in December was "not a foregone conclusion." Commentary following the October cut reminded investors again that any further monetary easing will be data-dependent.

Assessing the delicate balance act between jobs growth and pricing pressures, the Fed appears to have determined that the balance of risks had shifted away from rising prices and toward weakness in the employment economy. The latest CPI data signals that inflation remains elevated. But the recent trend in monthly non-farm payrolls growth, along with downward revisions to most of 2024 and early 2025 jobs data, signals softness in the employment situation.

U.S. Treasury yields were little changed in September and October. But rates moved lower into November-end, given the increasing likelihood of a December rate cut by the Fed. The 10-year Treasury yield was 4.00% as of the end of November 2025, compared with 4.11% as of the end of October. Yields are back near their 2025 lows from April; the cycle peak for the 10-year yield was 4.9% in October 2023. The two-year Treasury yield was 3.45% as of the end of November 2025, versus 3.61% as of the end of October 2025. The cycle peak for the two-year yield was 5.2% as of October 2023.

Over time, Argus expects short-term yields to move lower from current levels. Long yields over time are expected to widen their relative premium to short yields.

Notwithstanding Fed Chair Powell's ambiguity about any further policy action in 2026, Argus Fixed Income Strategist Kevin Heal continues to model one remaining rate cut in 2025 following the reductions in September and October. According to the CME FedWatch tool, the probability of a rate cut at the December FOMC meeting was about 85% at the end of November. Fed watchers are now turning their focus to 2026. Argus is currently modeling just one quarter-point cut in 2026, which is in line with consensus.

With the dearth of government data, calendar 3Q25 earnings season had an outsized and largely positive impact on stocks. The busiest weeks are now behind, with just a few retail and technology stragglers set to report early in December. Expectations heading into earnings season, for high-single-digit to low-double-digit growth, were the most positive in at least four quarters. Third-quarter 2025 earnings season still managed to play out better than anticipated.

The annual growth rate for calendar 3Q25 earnings is at the high end of the 12%-14% range, with different agencies reporting slightly different rates. More than 82% of companies have reported earnings above the pre-reporting consensus, which is higher than the long-term 75% average. The magnitude of the EPS beat against expectations, in the high-single-digit range, is above the midpoint of the long-term range of 5%-9%.

The best growth in 3Q25 earnings season came from the Technology, Financial, Utilities, Materials, and Industrial sectors. The weakest sectors included Staples, Healthcare, and Energy. The single-digit decline in Energy earnings is actually the most moderate of any quarter in the past year. Nearly all sectors are growing revenue, which is partly a reflection of still-present inflation.

An analysis of earnings-call transcripts suggest that while tariffs are still a topic, they are no longer an all-consuming topic. Companies also disclosed actual and potential impacts from the government shutdown. The overall message was positive, with earnings for calendar 4Q25 forecast to rise in high-single-digit percentages.

Third-quarter earnings season also featured expansion in non-GAAP operating margins to the 12.4% range, which is up about 50 basis points (bps) year over year. Companies have learned to live with or at least navigate around tariffs -- sourcing locally to end markets and flexing variable costs whenever possible. Assuming the S&P 500 can sustain recent revenue growth exceeding 5% annually, we see room for further margin expansion ahead as volume leverage supersedes higher costs and tariffs.

We are reiterating our forecasts for S&P 500 earnings from continuing operations of $270 for 2025 and $300 for 2026.

Domestic and Global Markets

The AI trade showed some cracks in the foundation during November. Nvidia released its highest-ever revenue and adjusted EPS for its fiscal 3Q26 (ended October 2025). Despite beating the 3Q26 revenue consensus by billions and guiding fiscal 4Q6 billions of dollars above consensus, the NVDA stock fell post-earnings, dragging the AI trade down with it. Although NVDA recovered a bit into November end, the damage was done, and Nasdaq finished down for the eleventh month.

As of the end of November, the S&P 500 was up 17.8% year to date (YTD), just two ticks above where it ended October. The Nasdaq was up 21.7% year to date at the end of November after being up 23.5% at the end of October. The Dow Jones Industrial Average had the best monthly showing of the big three and finished November up 13.9% YTD after being up 13.2% at the end of October.

Wilshire Large Cap Growth was up 22.6% YTD as of the end of November, while Wilshire Large Cap Value was up 13.5% at the end of the month. The growth-to-value premium narrowed to 9.1% at the end of November from 13.9% at the end of October. The Russell 2000 was up 13.5% for the year at the end of November, versus 12.0% at the end of October.

The Barclays Bloomberg U.S. Bond Index was up 7.2% year to date at the end of November 2025, its highest level of the year. Bond returns could continue higher if the fed cuts rates again in December 2025.

AI winnings are being redeployed into other sectors -- some of which are seen as beneficiaries as AI expands from the hyperscale data center and into diverse enterprise-use cases. Fourth-quarter stock performance at the sector level shows where some of those AI winnings are going, while analysis of full-year performance suggests that investors are not giving up on the AI trade altogether.

For 4Q25 to date, the best sector performer by far is Healthcare (IYH), which was up 13.6% as of the end of November. The S&P 500, by contrast, eked out a fractional gain for the two months of the quarter to date. Healthcare has done so well in the fourth quarter that it has rescued what had been a terrible performance as of the nine-month mark.

Healthcare has benefited from the perception that the sector was oversold based on difficult trends being reported by a single niche, the healthcare insurers. The Healthcare sector overall has certainly been helped by President Trump's intervention to lower the monthly price of GLP-1 drugs. While that may depress profit margins in the near term for Lilly and Novo Nordisk, it could potentially lead to enough volume leverage to offset pricing pressures. The clock is ticking toward the calendar 2025 year-end expiration of Affordable Care Act subsidies, the issue that caused the longest government shutdown in history. If the Democrats and Republicans can't agree on a compromise and millions of families elect not to maintain their health insurance, the sector may look a lot different to investors in 2026.

Based on a Thanksgiving week sprint into the finish, four other sectors are positive in 4Q25 to date. The best of the bunch is Utilities; the rate-sensitive sector has been lifted by the two rate cuts in September and October and potential for a third cut in December. Other sectors in the green in 4Q25 to date include Consumer Staples, Energy, Information Technology, Materials, and Real Estate.

All this action in 4Q25 has had the effect of smoothing the overall sector map for full-year 2025. As of November end, Consumer Staples has pushed into positive territory, and that means all sectors are positive year to date. Sectors that are up in single-digit percentages for 2025 to date include (in ascending order) Consumer Staples, Real Estate, Energy, Consumer Discretionary, and Industrials. Sectors that are up in double-digit percentage for 2025 to date include (in ascending order) Financial, Materials, Healthcare, Communication Services, Utilities, and Information Technology.

The rise of generative AI is sort of turning every company into a technology company. But there are still a few sectors that sell the digital pick-axes to the AI gold rush. Information Technology is the chief beneficiary of the AI economy. It includes companies in computing, software, semiconductor, data storage, communications equipment, and related areas that are increasingly benefiting from increased spending to support AI. The Information Technology sector as of the end of November 2025 exceeded 36% of overall S&P 500 market capitalization, up 4.8 percentage points in just a year. Even without adjusting to exclude the social media giants (META, GOOGL) spun into newly formed Communication Services in 2018 or the fintech giants (V, MA) that moved into the financial sector in 2023, the Information Technology is now at its highest sector weight ever within the S&P 500.

Two other sectors have been major beneficiaries of the AI revolution. These two sectors each include two of the so-called "Magnificent 7" stocks. Communication Services has steadily grown since inception, even though the stock prices and market caps of the big telecom names (VZ, T) have not changed much in the past few years. The two Mag 7 names, Alphabet and Meta Platforms, are seen as leaders in AI areas including LLMs, model training, inference, and more-recent growth opportunities including multi-modal models, agentic AI, and physical AI. Communication Services is pushing toward 11% of total S&P 500 market capitalization, after being below 9% a year ago.

Consumer Discretionary is a multi-industry sector. Retailers and restaurants are suffering loss of business from lower-tier consumers in a K-shaped economy. Builders and automakers are being impacted by high financing costs and affordability issues. Discretionary houses two of the Mag 7 giants, however, in TSLA and AMAZN. Discretionary has held its own over the past year at about 10.5% of S&P 500 sector weight, as the giants just keep getting bigger while retail, restaurants, lodging & gaming, auto OEM & parts, and homebuilders & builders supply keep getting smaller.

Like the US market, global stocks did better in 2023 than they did in 2022; and most carried that momentum across 2024. In 2025, overseas markets have generally been doing better than the U.S. market. Tariffs have both scared foreign investors out of U.S. equities and realigned leadership around the world. All nine global bourses in our tally are positive for 2025 as of the end of November, but leadership has changed since early in the year.

Most global markets strengthened in November as trade-related tensions continued to wind down. Some of the worst markets in 2024, such as Mexico, are near the top of the leaderboard in 2025. Conversely, some of 2024's winners such as India are relatively underperforming in 2025. India alone is lagging the U.S. market (S&P 500) for the year to date.

In terms of our themes, Resources economies are up in the 32% range as of November, while Asian markets are 24%; these two groups were level at up-28% at the end of October. Americas markets are up 28% YTD, fueled by recovery in Mexico and Canada. Mature economies, which led in 2024 and 2023, are up 22%. BRICs-minus-Russia are up 19% year to date.

Conclusion

After a three-year rally, are the cracks in the AI foundation superficial? Or do they run deeper? The tentpole of the AI revolution, Nvidia, reported its fiscal 3Q26 results after the market close on 11/19/25. What transpired in the following 24 hours encapsulates all the excitement, astonishment, skepticism, and fear that has characterized the three years since ChatGPT was made widely available in November 2022.

Pushing back against fears that AI was in a bubble phase, Nvidia co-founder and CEO Jensen Huang doubled down on claims made at the company's GTC event in October in Washington D.C. The CEO reiterated that the company is on track for cumulative Blackwell, Blackwell Ultra, and Rubin GPU and related revenue of $500 billion by the end of calendar 2026. Given the many deals announced since GTC Washington, Nvidia said it will likely be raising that $500 billion goal. The company also stands by its mind-blowing forecast that the global annual spend on AI infrastructure will be $3-$4 trillion by approximately 2030.

CEO Huang could make such a claim because the market for AI technology is changing rapidly and broadening dramatically. In the months leading up to Nvidia's quarterly results release, Nvidia announced multiple new AI partnership deals -- not with the hyperscalers that dominated earlier GPU demand, but with multiple neoclouds, large global enterprises, and sovereign clients.

NVDA and other AI leaders rallied across Thanksgiving week, reversing most of their mid-month losses. As investors cashed out of these names, AI winnings were redeployed into other sectors -- some of which are seen as beneficiaries as AI expands from the hyperscale data center and out into diverse enterprise use cases. That rotation is healthy for near-term stability in the stock market.

We expect the AI trade to be bumpy going forward. And like other transformational technology trades before it, including cloud, internet, semiconductors, and PCs, we expect the AI trade to be long and fruitful.

Jim Kelleher, CFA,
Director of Research

No Releases this Week

Previous Week's Releases and Next Week's Releases on next page.

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
1-Dec	ISM Manufacturing	November	48.7	49.4	49.0	**48.2**
	ISM New Orders	November	49.4	49.2	NA	**47.4**
3-Dec	ISM Services Index	November	52.4	52.0	51.5	NA
	Industrial Production	September	0.8%	0.9%	NA	NA
	Capacity Utilization	September	75.8%	75.7%	77.3%	NA
	Import Price Index	September	0.0%	0.1%	0.4%	NA
5-Dec	PCE Deflator	September	2.7%	2.8%	2.8%	NA
	PCE Core Deflator	September	2.9%	2.9%	2.9%	NA
	Personal Income	September	5.1%	5.0%	NA	NA
	Personal Spending	September	5.6%	4.8%	NA	NA
	U. Michigan Sentiment	December	51.0	52.0	51.2	NA

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
16-Dec	Nonfarm Payrolls	November	119K	NA	NA	NA
	Unemployment Rate	November	4.4%	NA	NA	NA
	Average Weekly Hours	November	34.2	NA	NA	NA
	Average Hourly Earnings	November	3.8%	NA	NA	NA
18-Dec	Consumer Price Index	November	3.0%	NA	NA	NA
	CPI ex-Food & Energy	November	3.0%	NA	NA	NA

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