APOLLON

Market Recap

January 2026

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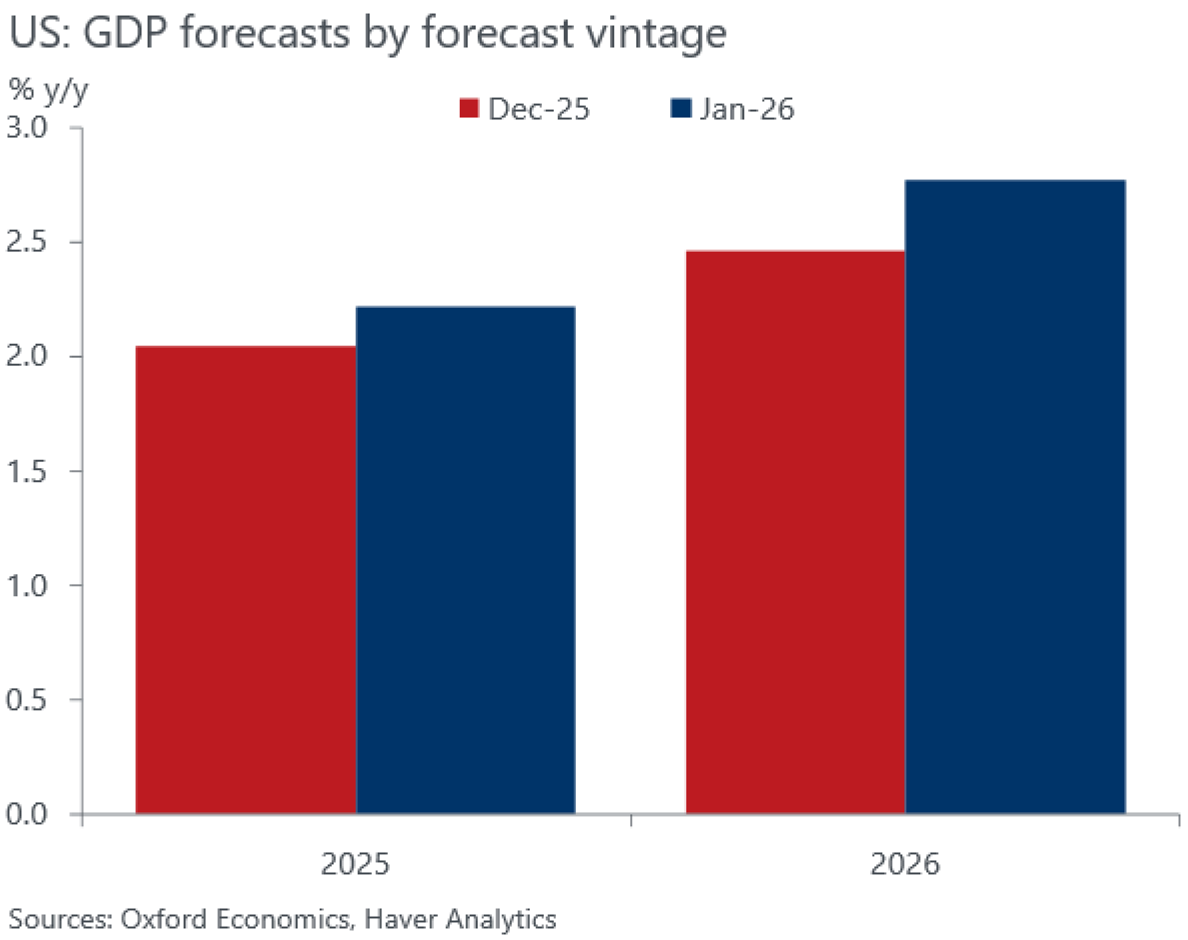
Growth outlook upgraded for this year

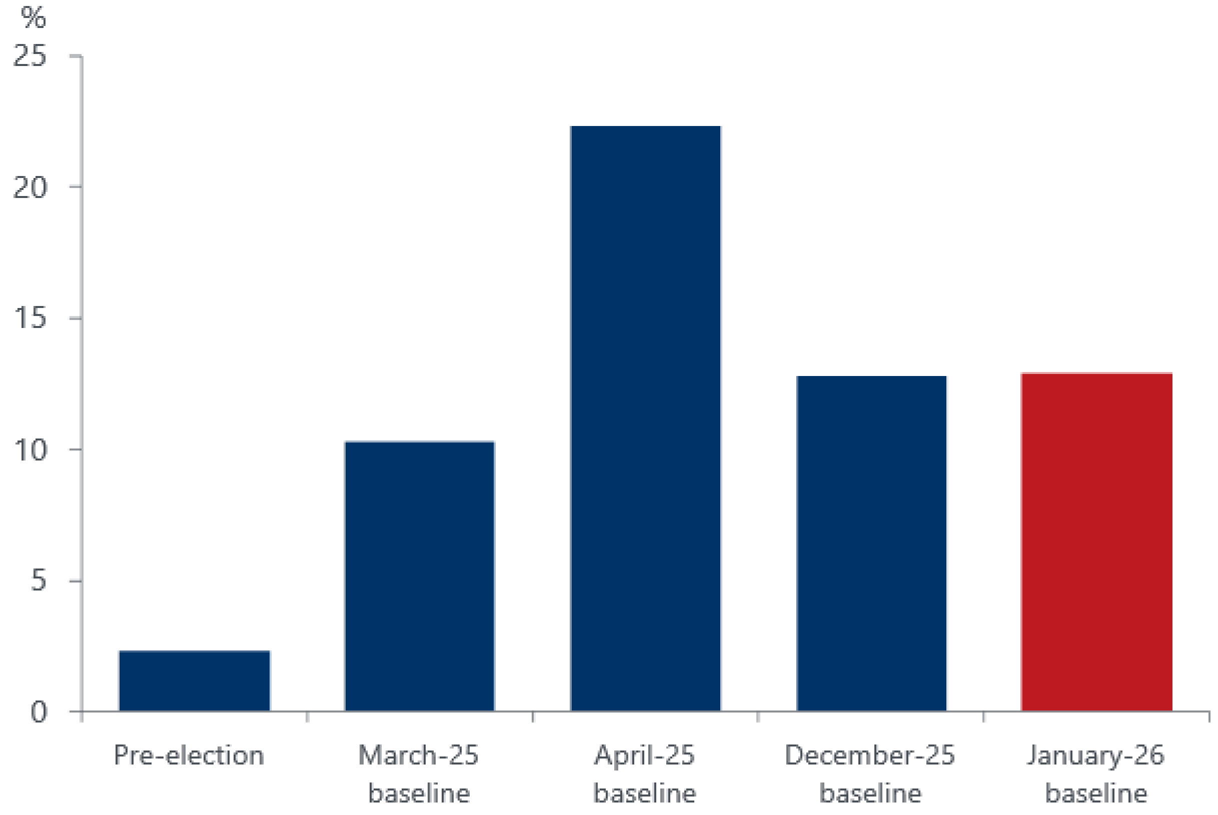


Key takeaways

- We've raised our forecast for real GDP growth in the US in 2026 by 0.3ppt to 2.8% to reflect updated assumptions around the AI boom.
- Investment incentives under the Republican spending bill and the decline in business borrowing costs will support business equipment spending outside of AI next year.
- Consumer spending will continue to get a boost from the wealth effect, especially among older, richer households. It will also be supported by a rebound in real disposable income growth, as inflation fades this year.

Effective tariff rate steady around 13%

US: Effective tariff rate by forecast vintage



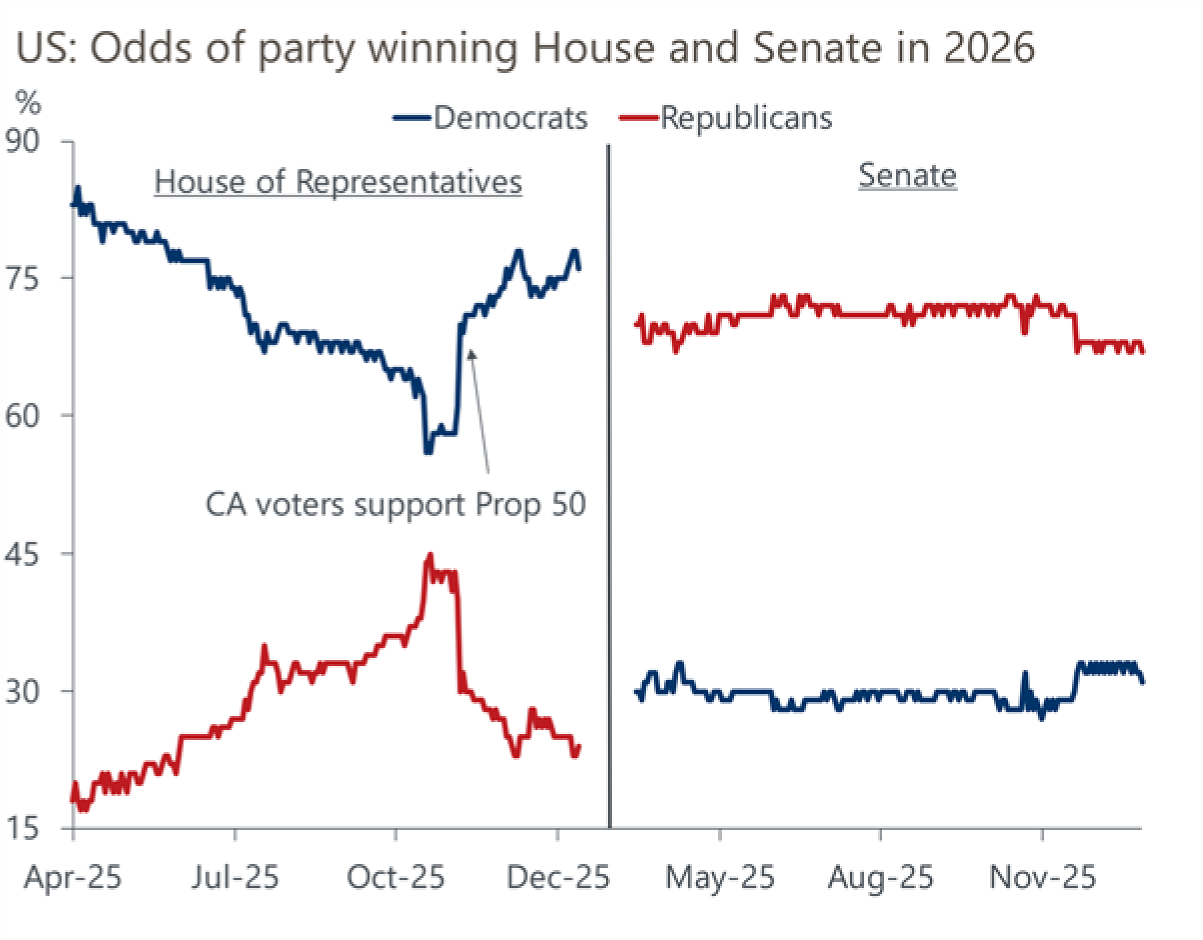
Sources: Oxford Economics, Haver Analytics

Key takeaways

- The effective US tariff rate remains close to 13%. Our January baseline included a reduction in tariffs on Taiwan, from 20% to 15%. New tariffs on semiconductors are very narrow in scope and won't boost the overall tariff burden.
- We have not included any assumptions about the outcome of Supreme Court's ruling on the legality of IEEPA tariffs in our forecast. There are several other legal channels by which tariffs could be raised again.
- The biggest threats still in the pipeline comes from sectoral tariff investigations, and the potential for USMCA negotiations to fail.

Focus: 2026 midterms add to uncertainty

Midterms will likely yield divided Congress

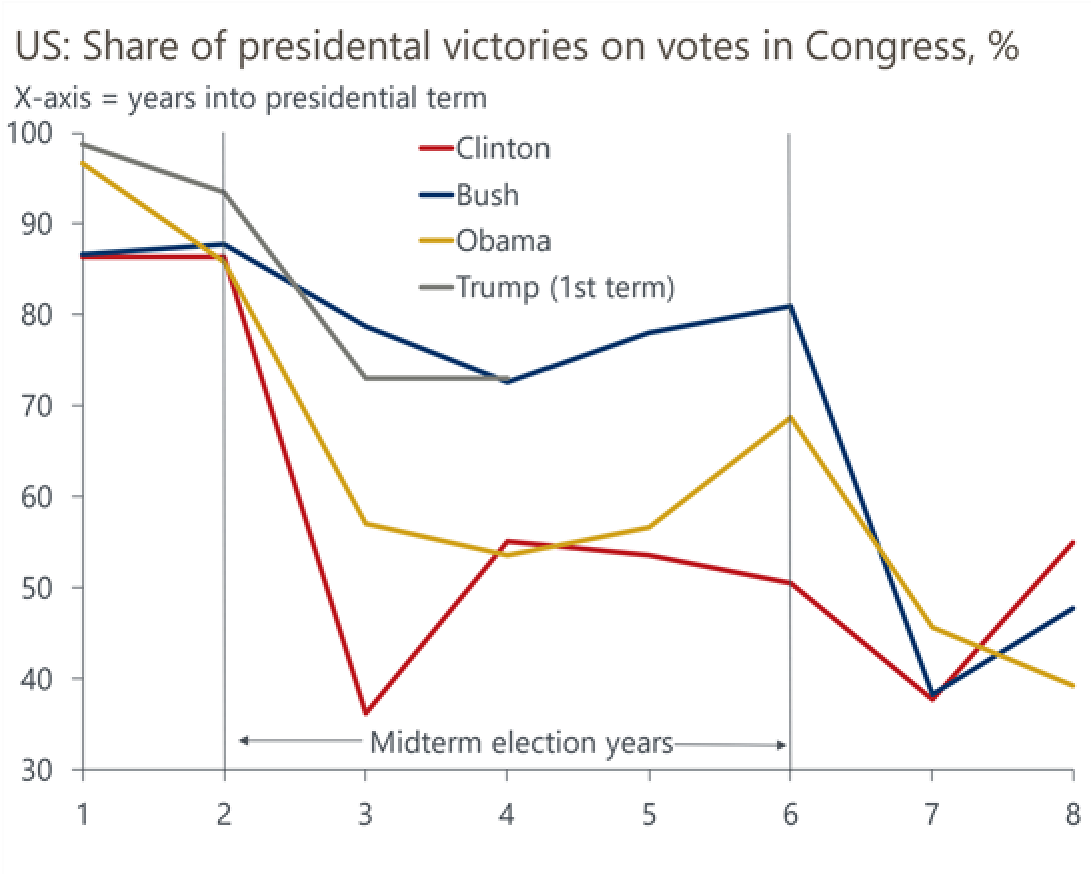


Sources: Oxford Economics, Haver Analytics

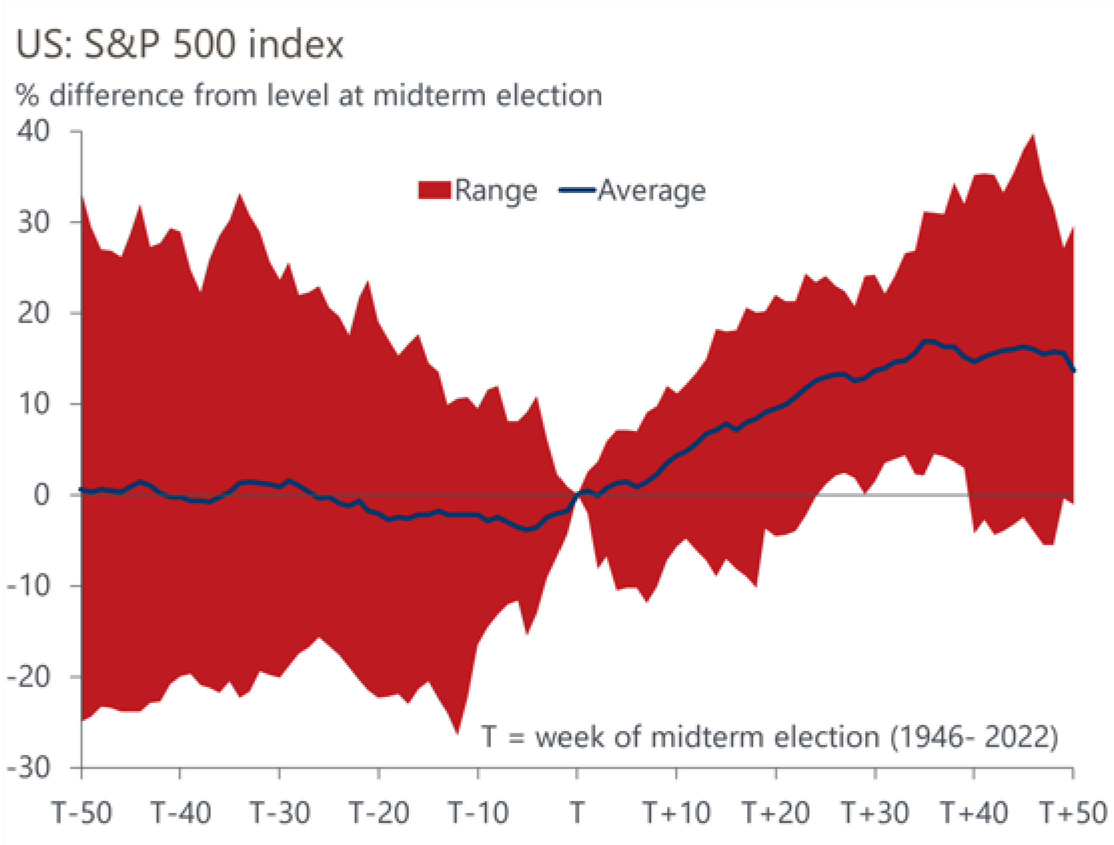
Key takeaways

- Divided government is the most likely outcome of the 2026 midterm elections. Generic ballot polling currently indicates Republicans will fall 13 seats short of the minimum 218 seats necessary to maintain their House majority.
- Without unified Republican control in Congress, President Trump would struggle to enact additional major changes to taxes and spending. Another run up against the debt limit in 2027 would also be contentious.
- Stock market performance tends to improve following midterm elections, as uncertainty subsides. Historically, equities perform best under divided governments.

Usually after, presidents have less sway and equities improve



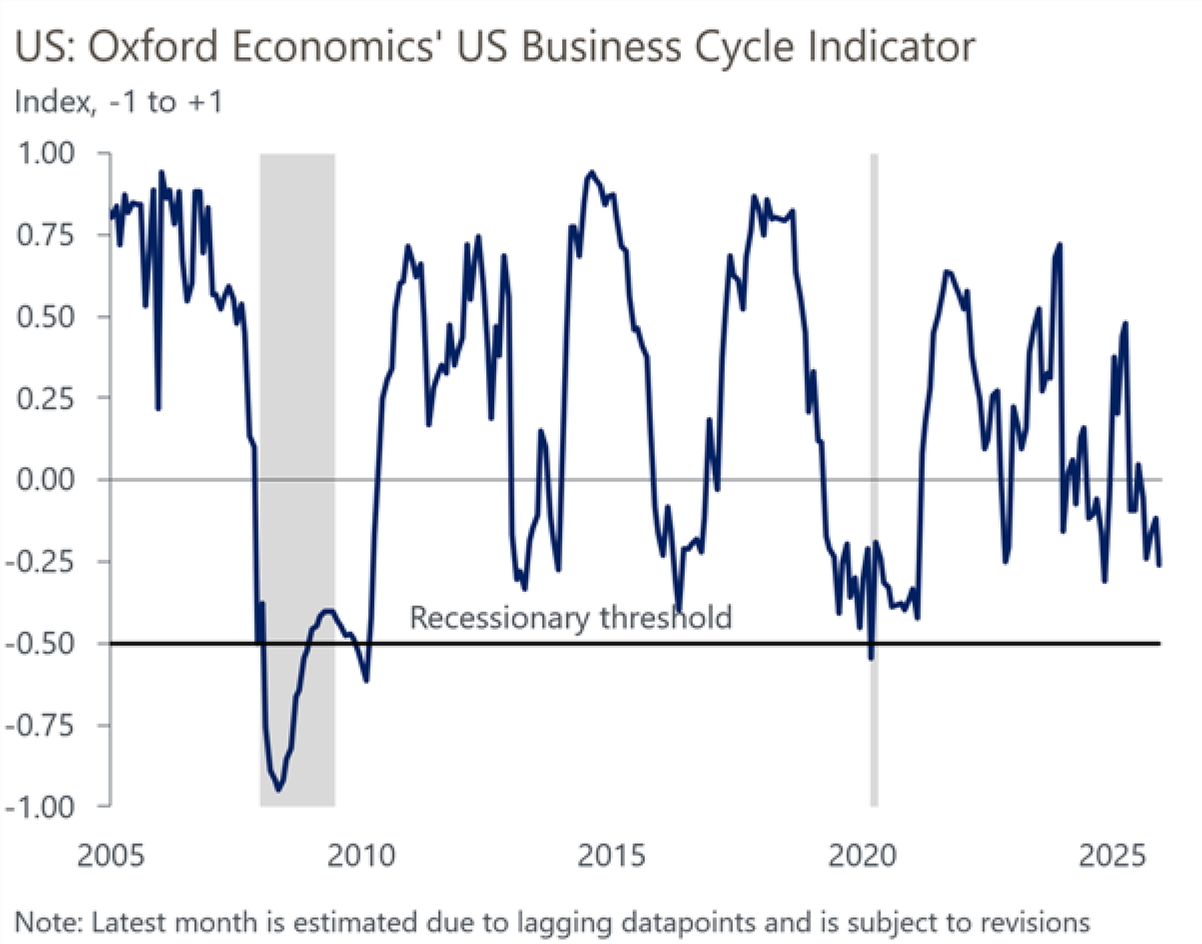
Sources: Oxford Economics, Bloomberg



Sources: Oxford Economics, Haver Analytics

Health check on the economy

Economy resilient outside labor market

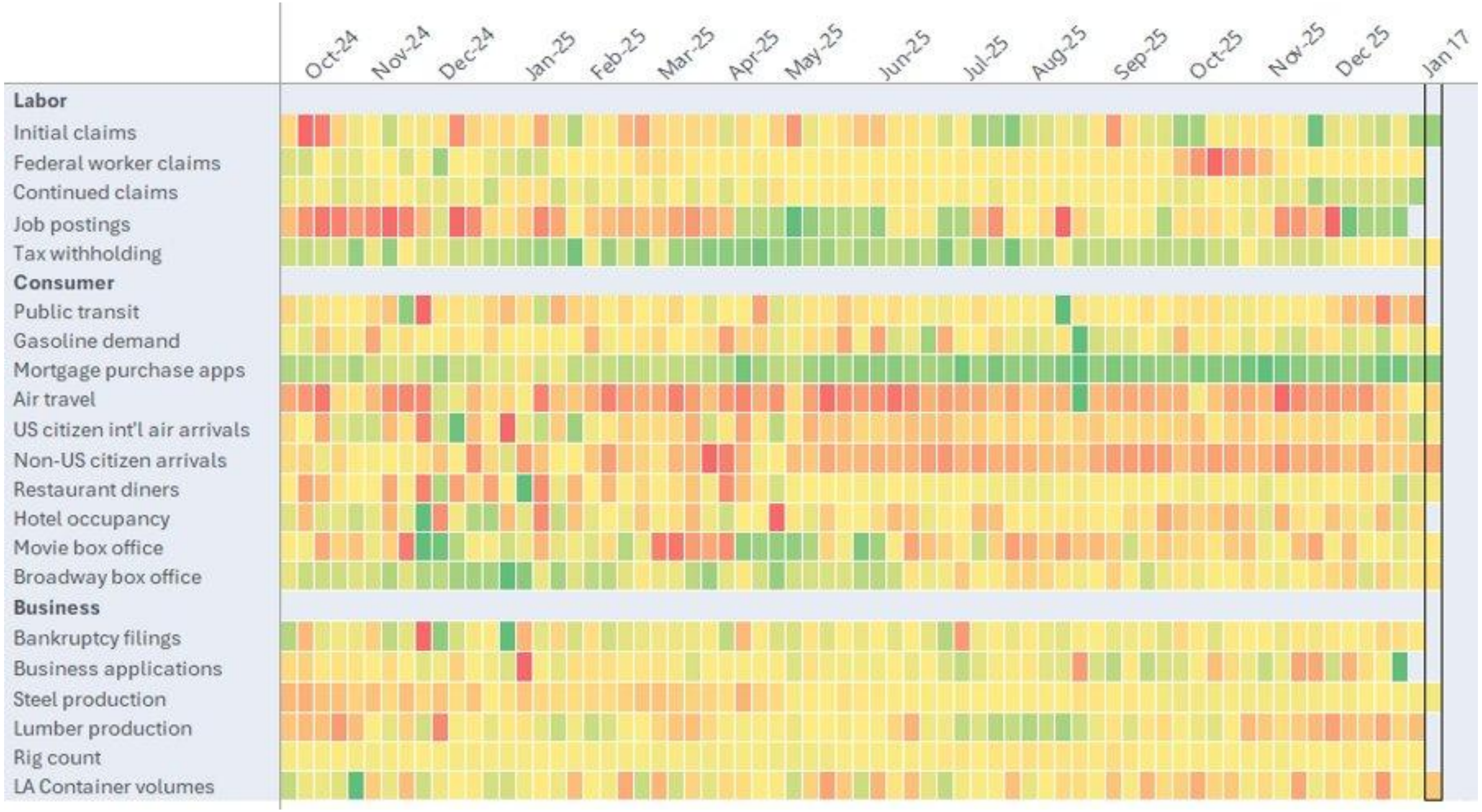


Source: Oxford Economics

Key takeaways

- Our business cycle indicator softened at year-end, but a productivity upswing, improving manufacturing activity, and strong consumer spending point to faster growth in 2026.
- Federal job cuts played an outsize role in last year's unemployment rise. Slower immigration and an aging population, means the economy will require modest job gains to hold unemployment steady.
- Strong productivity growth is lifting corporate profits. Healthy cash flows support business investment, which will be amplified by fiscal incentives and lower interest rates.

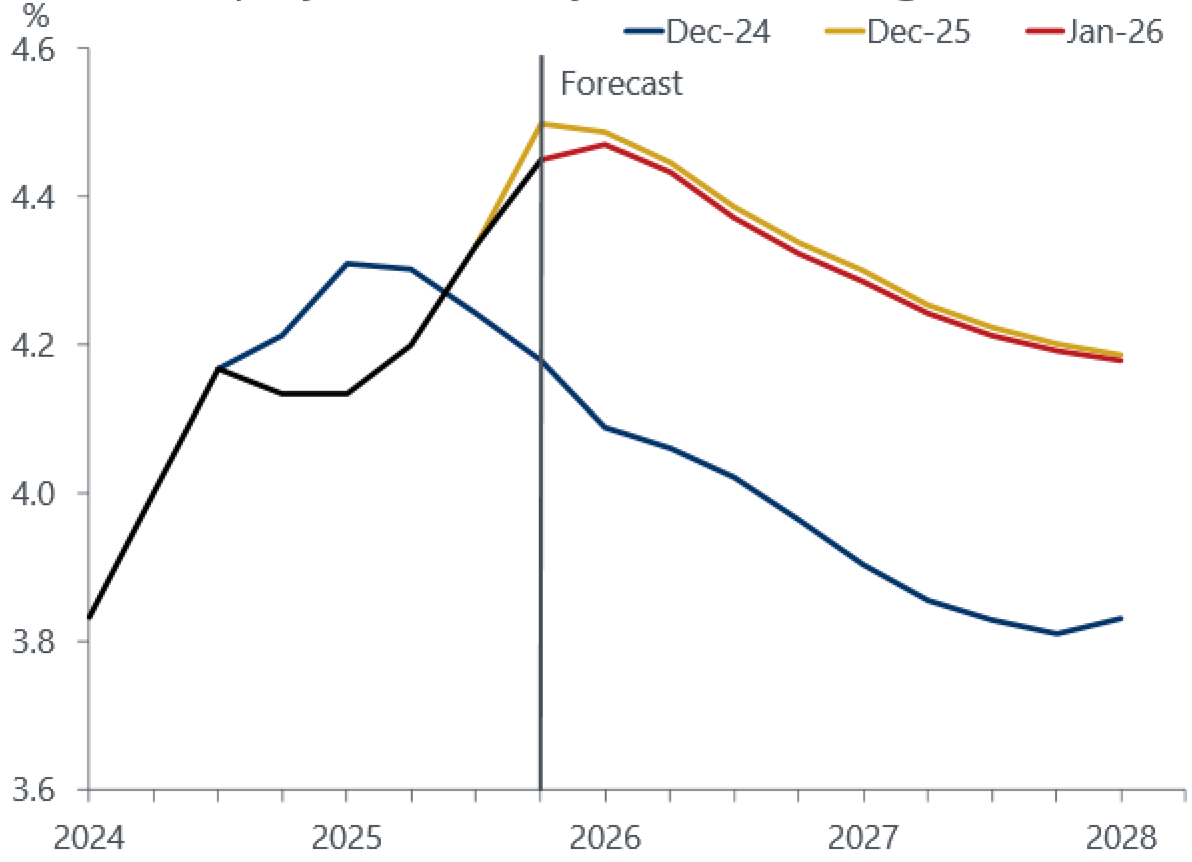
No high frequency indicators are raising alarm bells



Sources: Oxford Economics, Haver Analytics

Labor market is broadly steady

Labor market set to stabilize in 2026

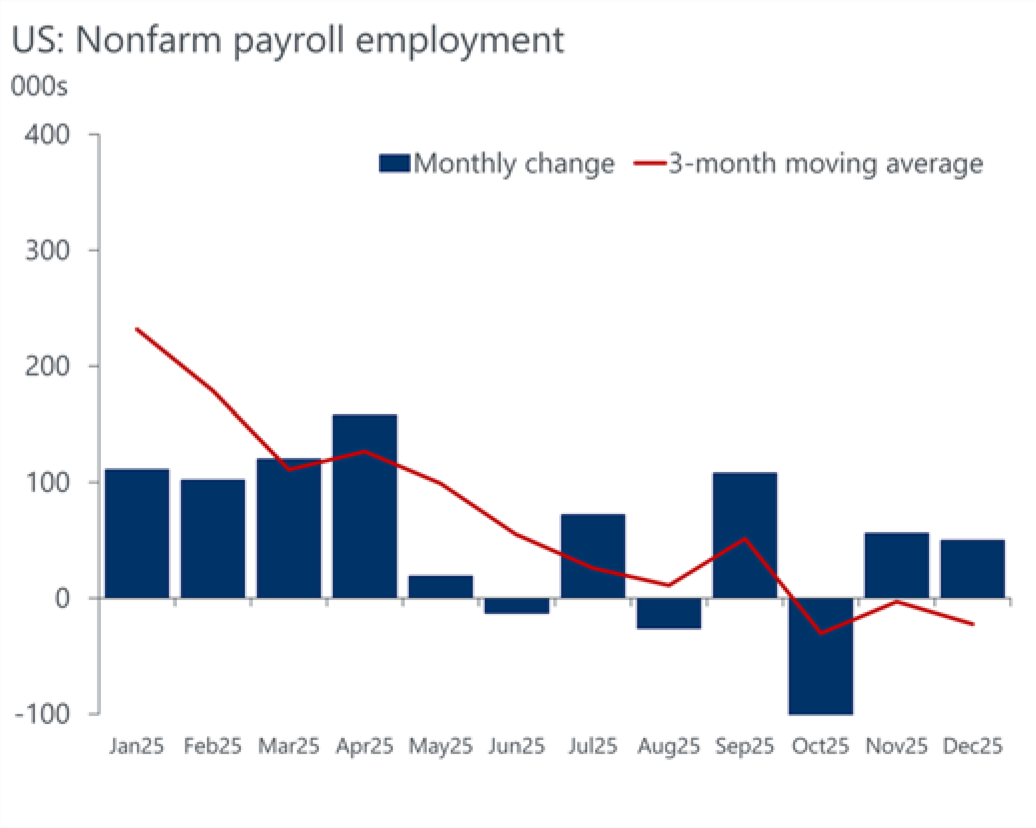


Sources: Oxford Economics, Haver Analytics

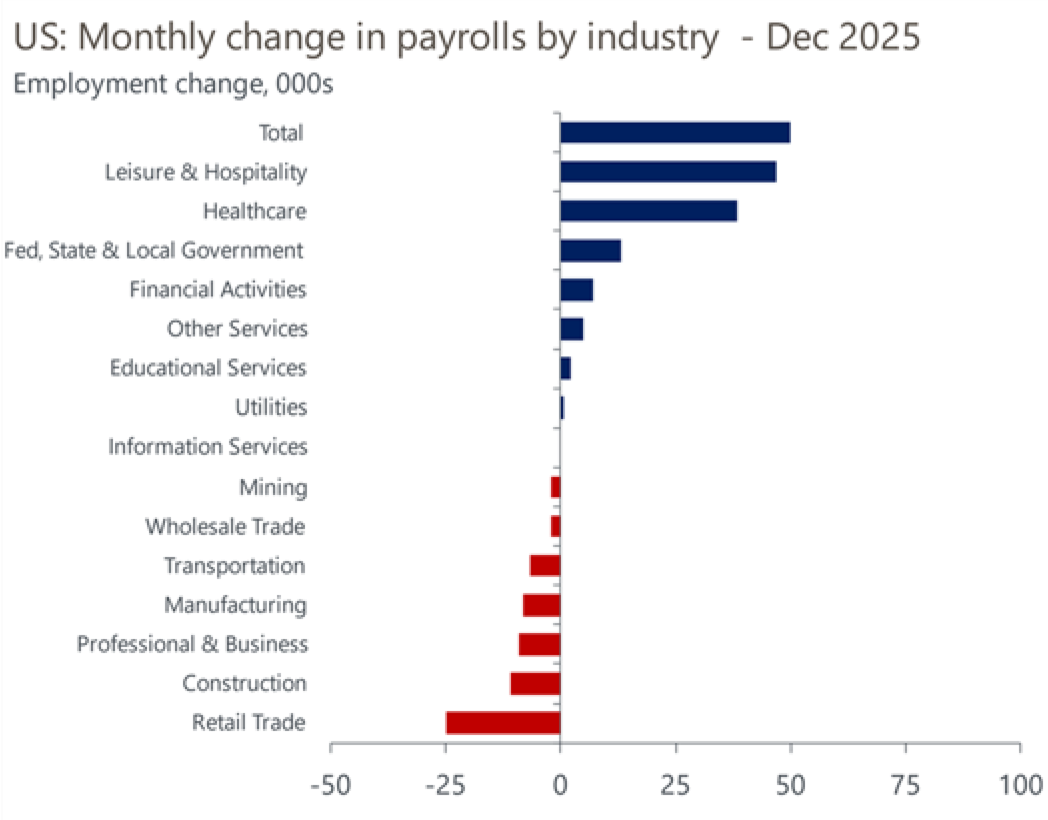
Key takeaways

- Although December nonfarm payrolls were softer than expected, trend job growth in the private sector remains positive at 29k, hovering close our estimate of the breakeven rate of 30k.
- Declines in federal employment accounted for roughly one-fifth of the increase in the national unemployment rate last year, despite representing only about 3% of total employment.
- Small firms, which account for more than 40% of payrolls, added jobs in December, registering positive gains for the first time in four months.
- Through hiring remains sluggish, employers continue to avoid layoffs.

December was another soft month for job gains

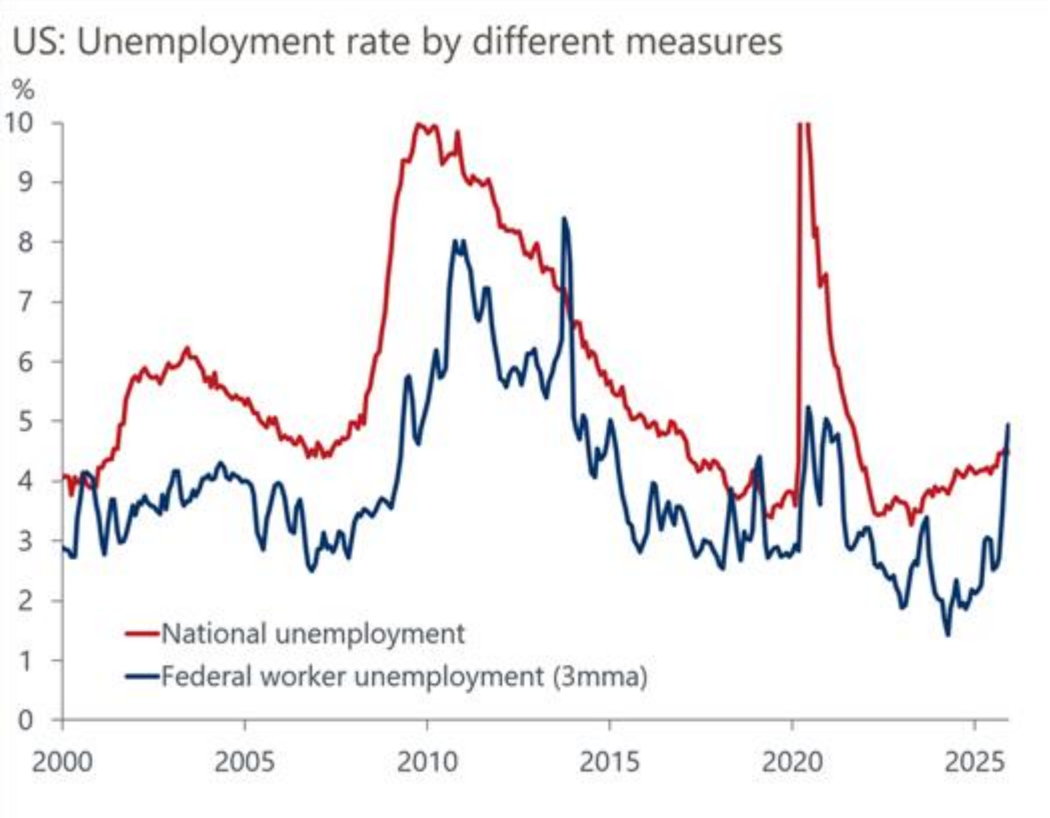


Sources: Oxford Economics, Haver Analytics

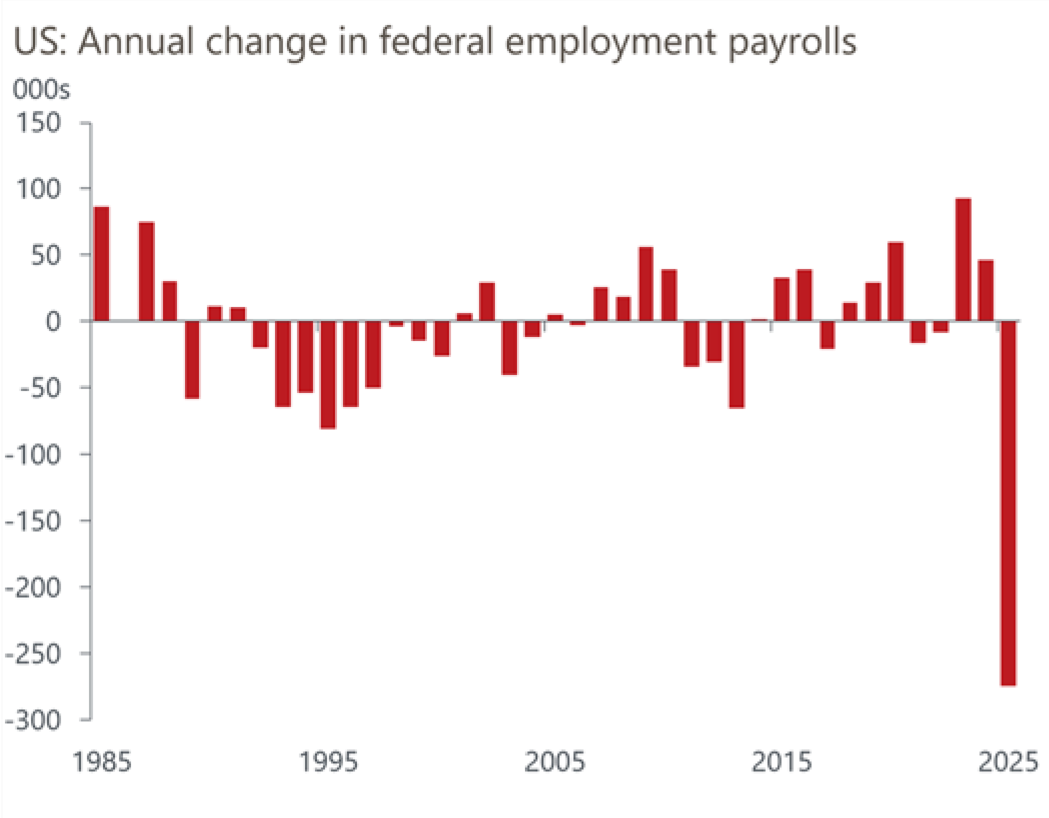


Sources: Oxford Economics, Haver Analytics

Federal declines were a key driver of rising unemployment

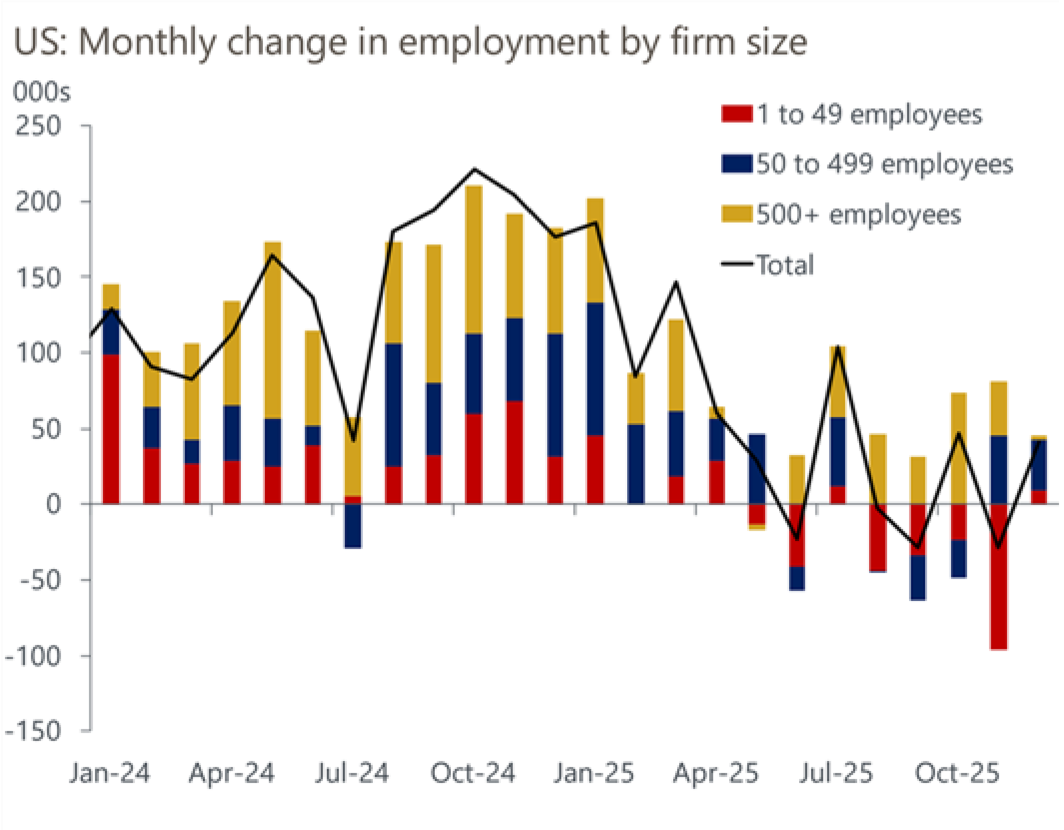


Sources: Oxford Economics, Haver Analytics

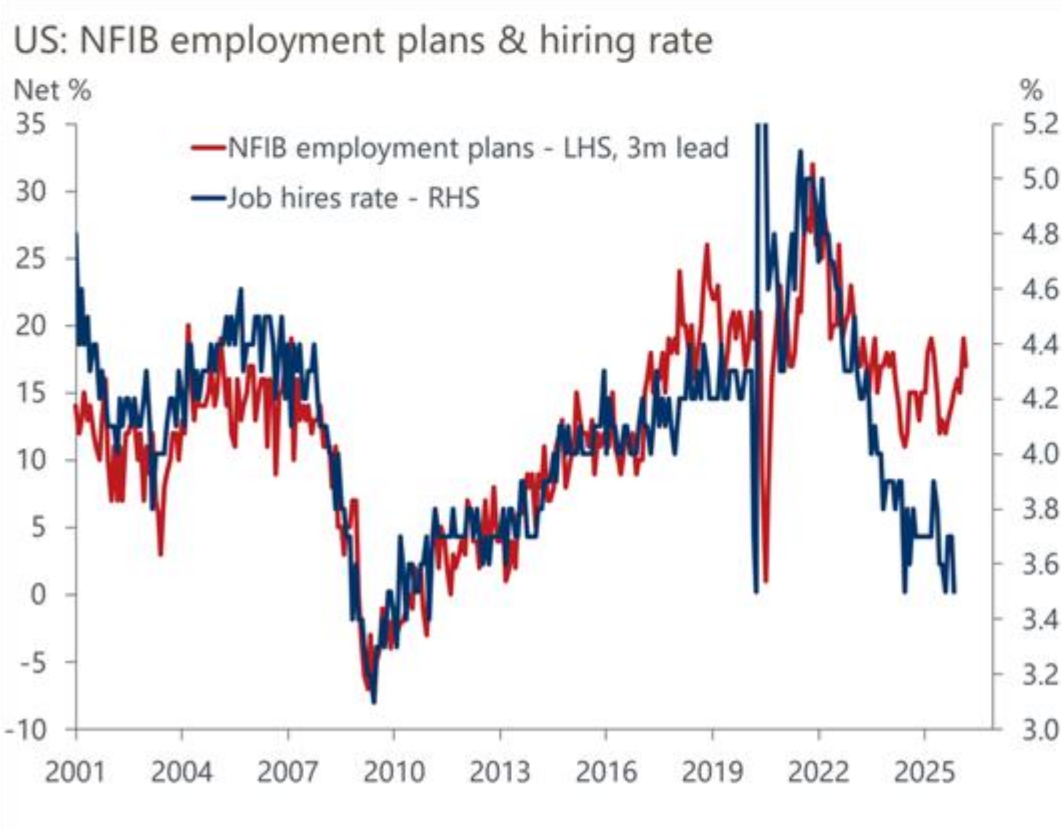


Sources: Oxford Economics, Haver Analytics

Small firms registered employment gains in December



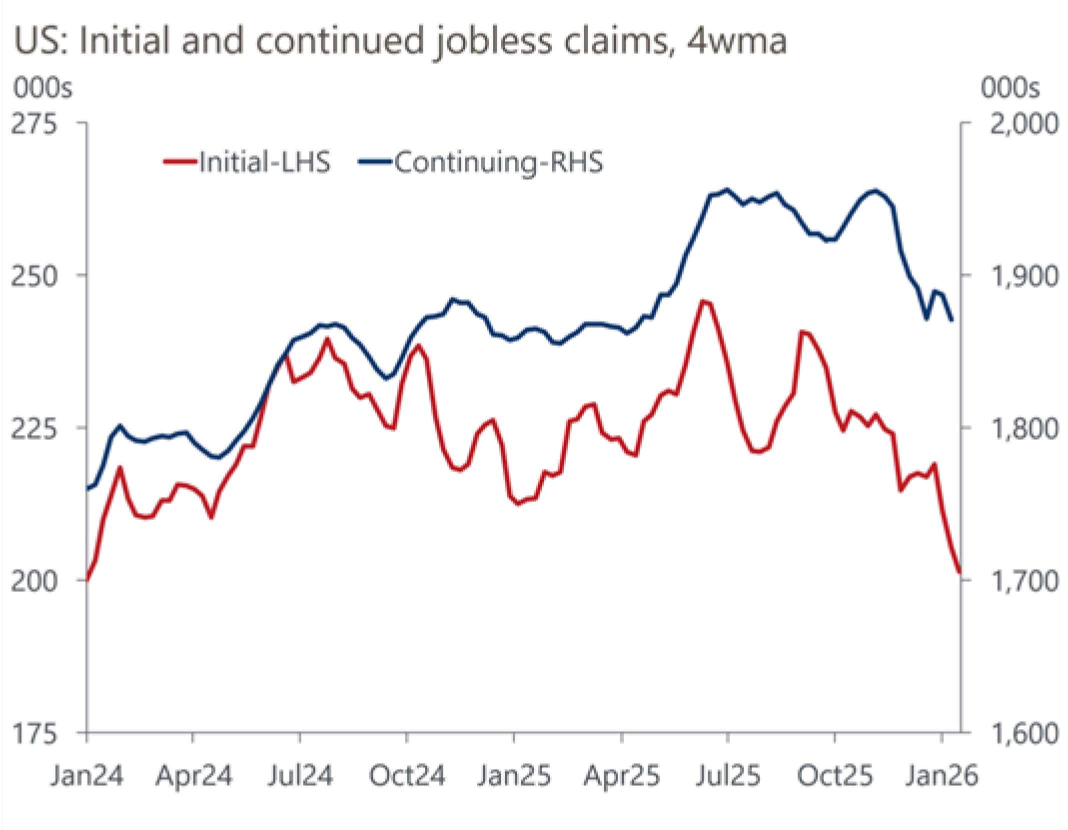
Sources: Oxford Economics, Haver Analytics



Sources: Oxford Economics, Haver Analytics

Low layoffs and claims point to a stabilizing labor market

Sources: Oxford Economics, Haver Analytics

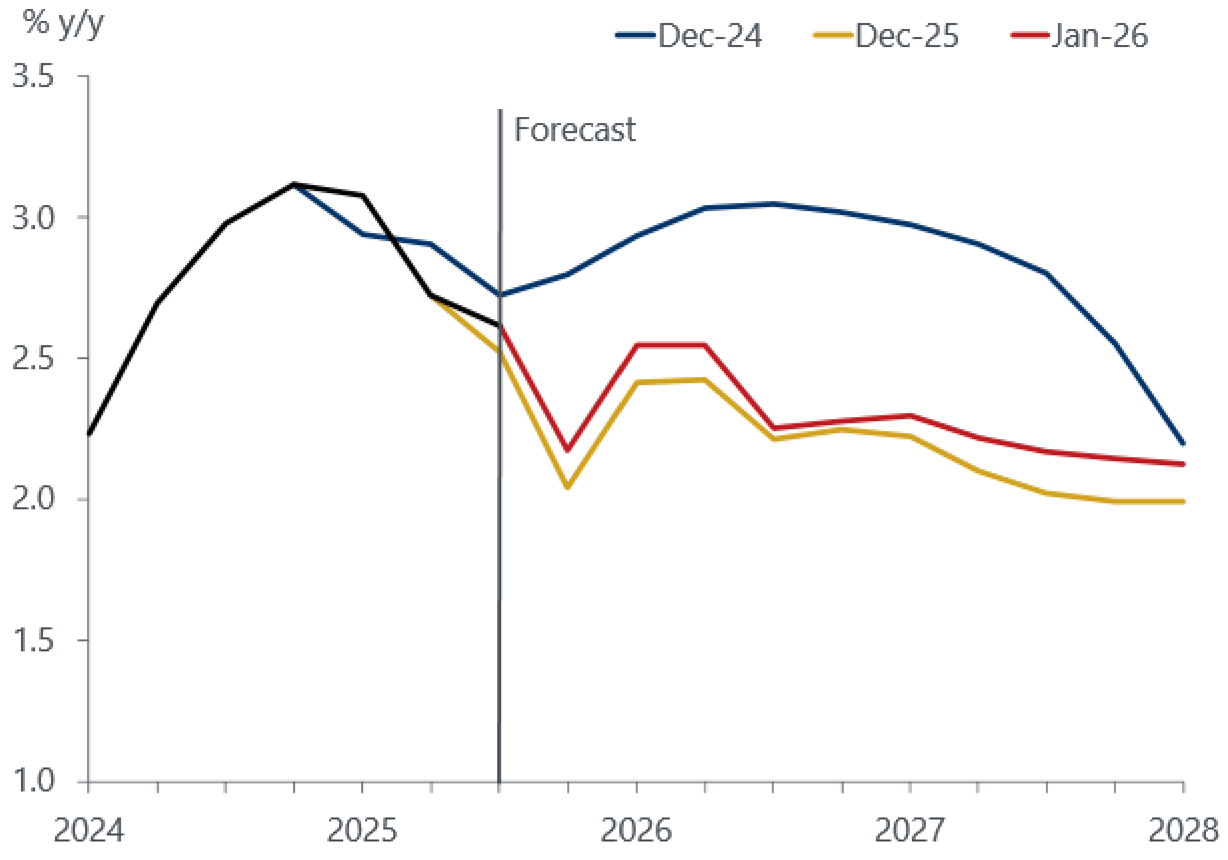


Sources: Oxford Economics, Haver Analytics

Consumer spending in solid shape

Resilient outlook for consumer spending

US: Consumer spending by forecast vintage

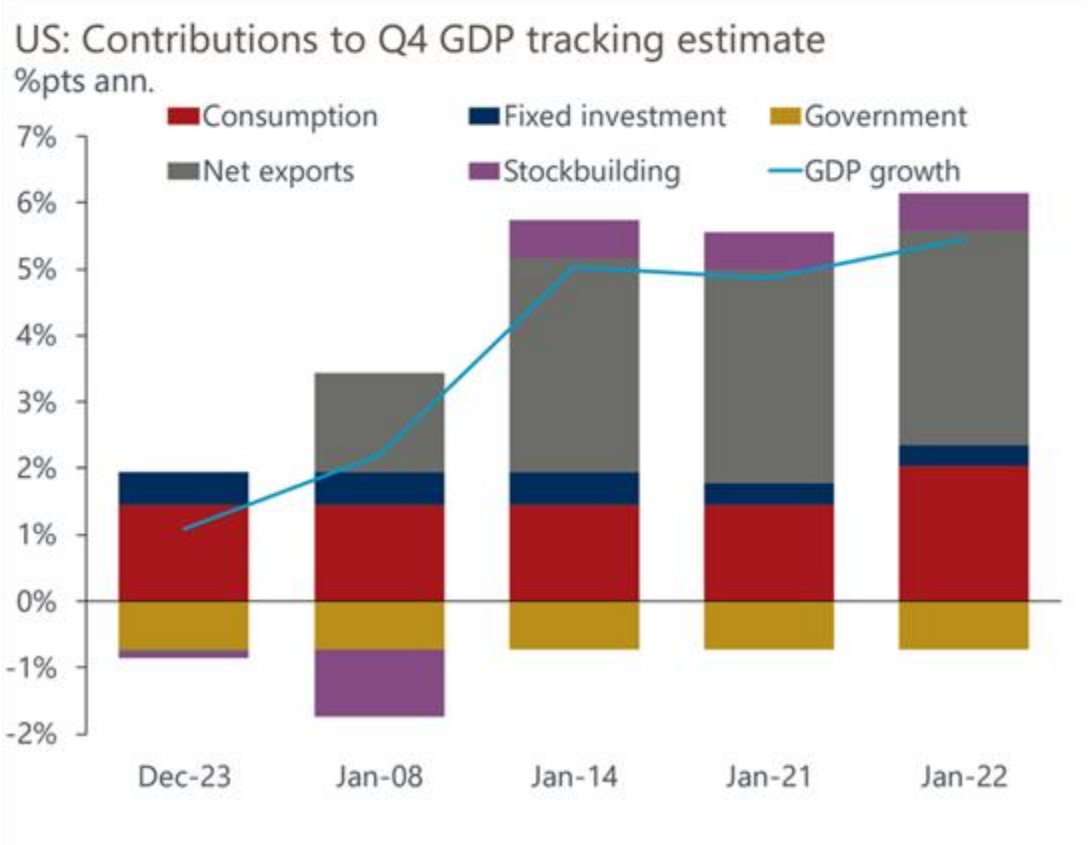


Sources: Oxford Economics, Haver Analytics

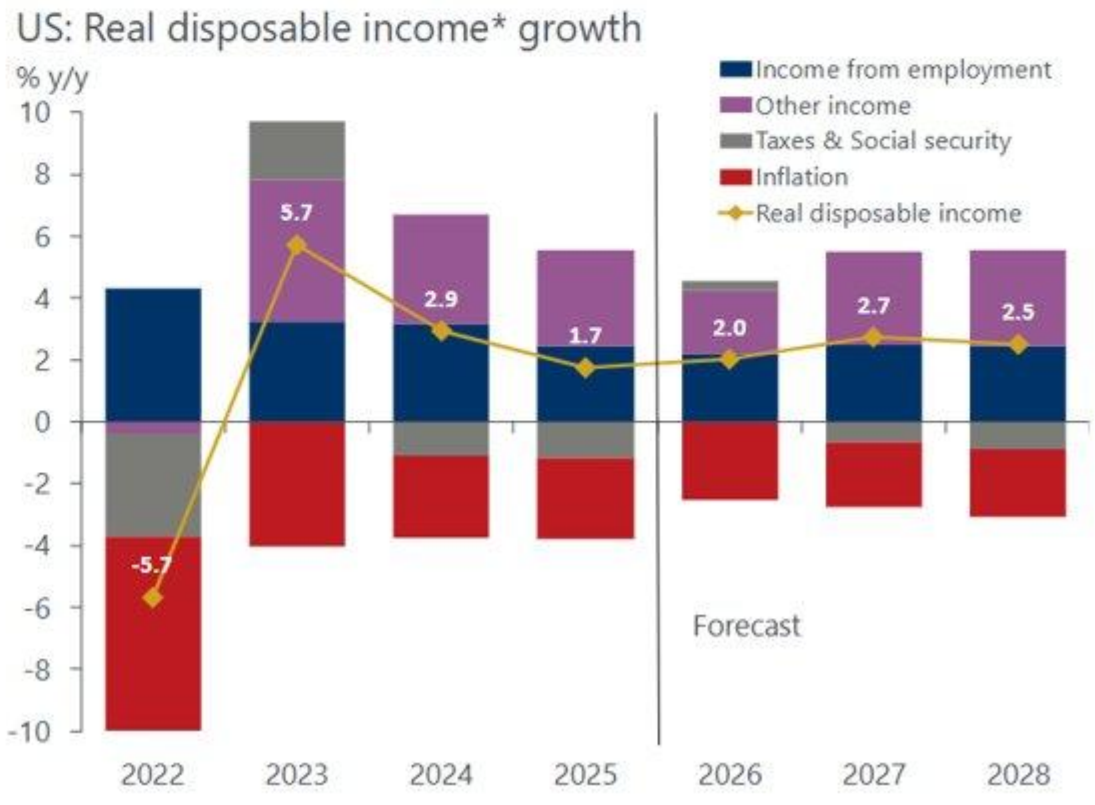
Key takeaways

- Solid consumer spending will be supported by growth in real disposable incomes this year. We expect consumer spending growth to remain solidly above 2% in 2026.
- Consumer bifurcation will intensify in 2026, with the OBBBA tax cuts set to benefit high income consumers most, whereas tariffs and cuts to social benefits disproportionately burden low- income consumers.
- Sticker shock, survey changes, and increased media bias partially explain the post-pandemic disconnect between consumer sentiment and economic fundamentals.

Strong spending will remain supported by income growth



Sources: Oxford Economics, Haver Analytics



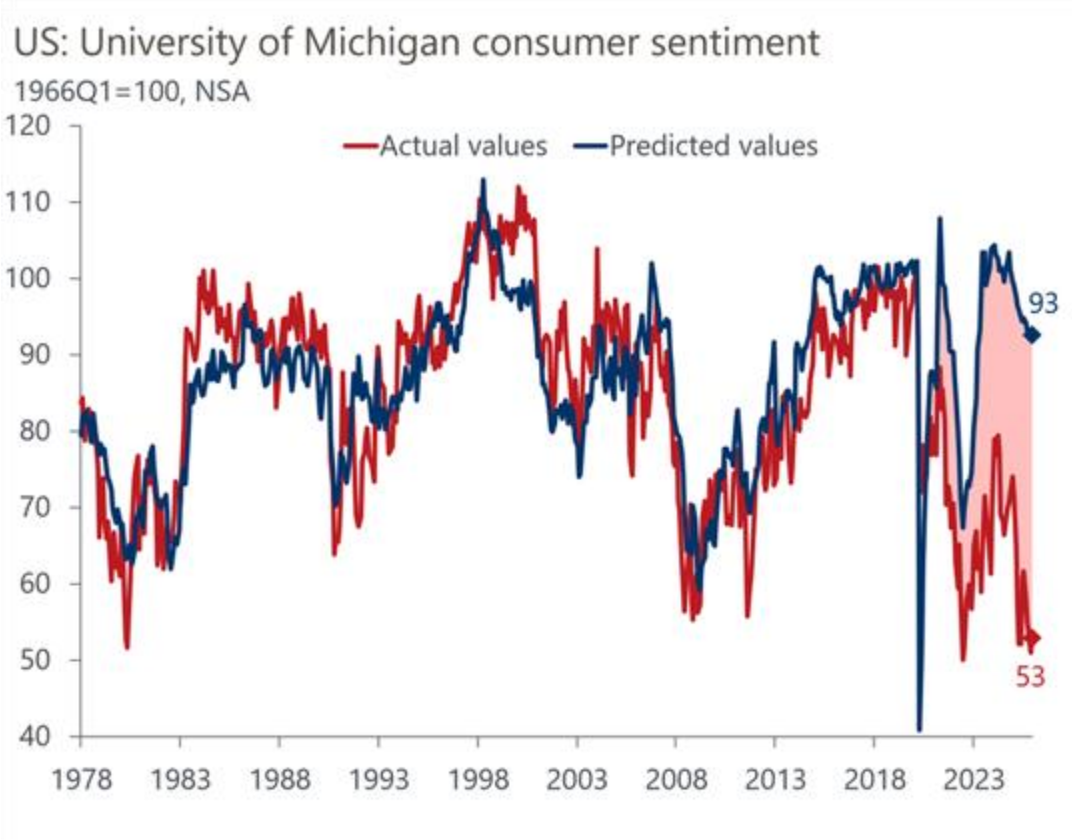
Sources: Oxford Economics, Haver Analytics

Wealth effects continue to support high income spending

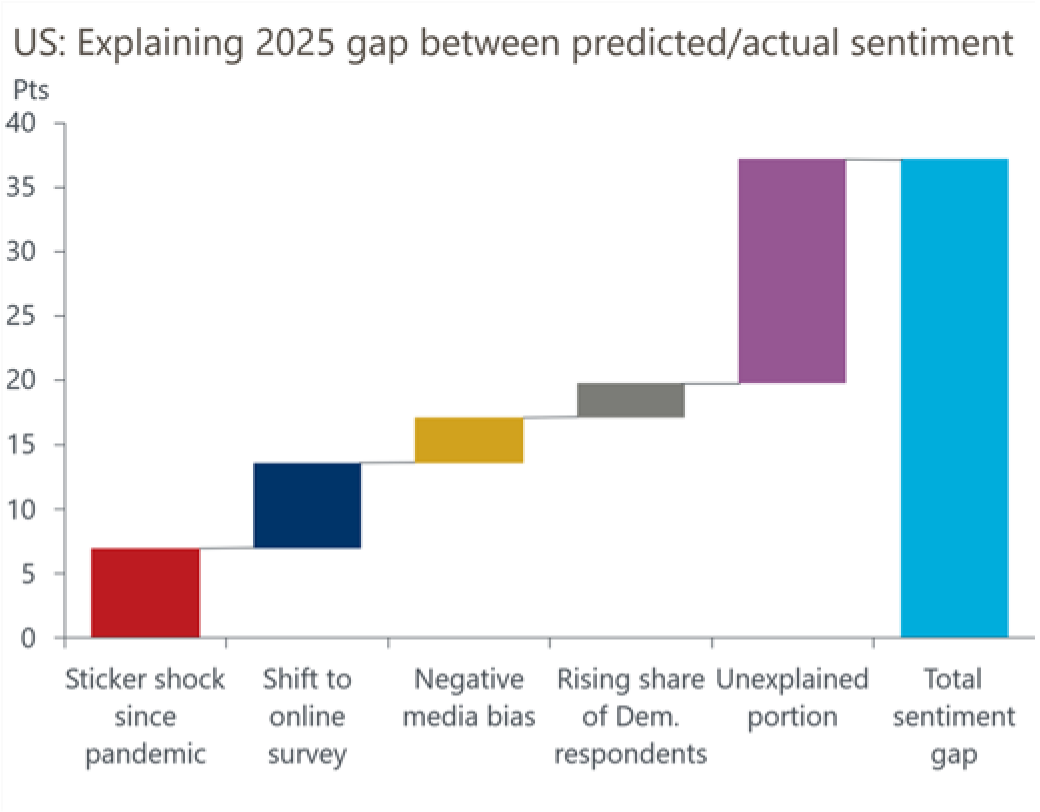
Sources: Oxford Economics, Haver Analytics

Sources: Oxford Economics, Haver Analytics

Consumer sentiment is disconnected from the hard data



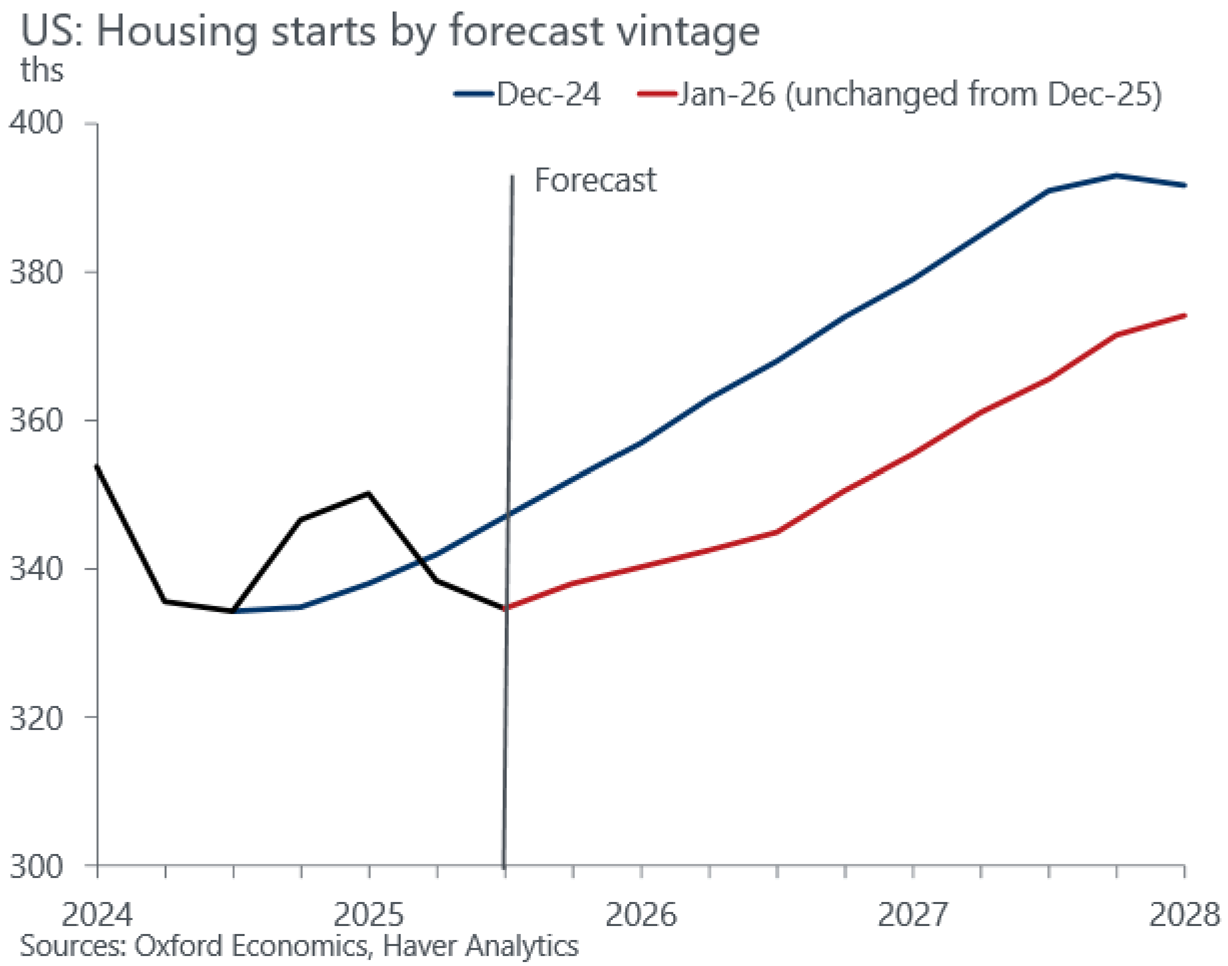
Sources: Oxford Economics, Haver Analytics



Sources: Oxford Economics, Haver Analytics

Housing market to slowly recover

Gradual recovery ahead for housing

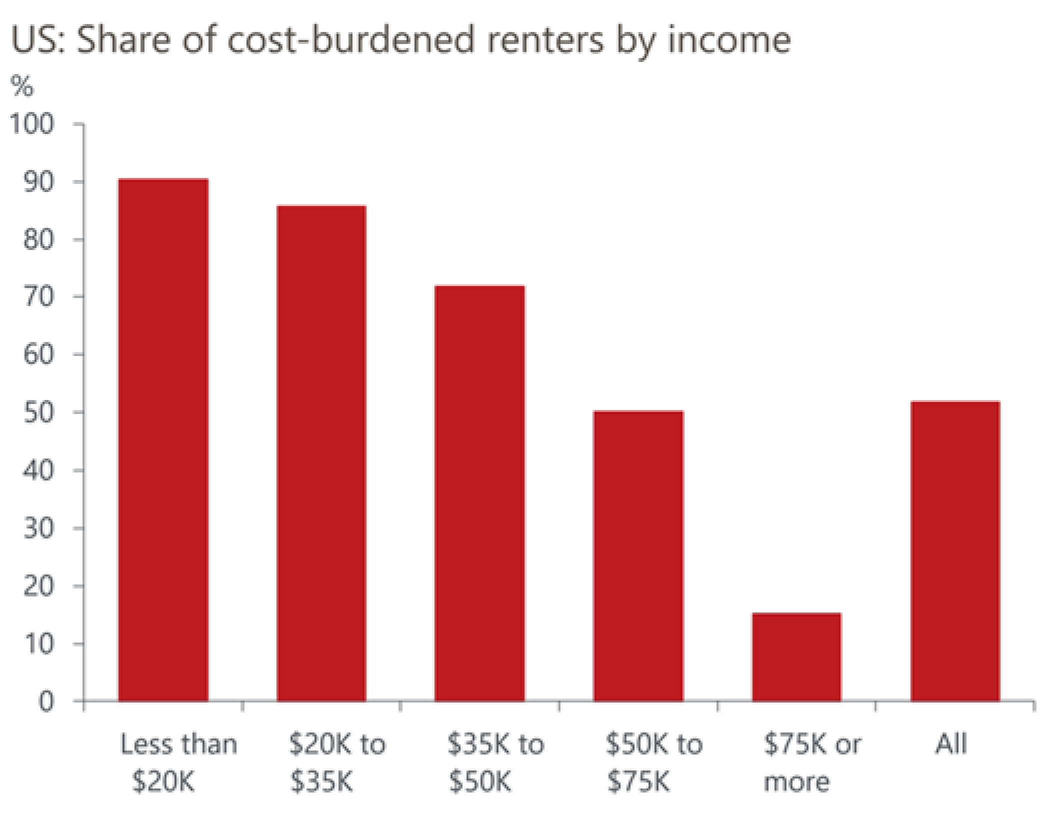


Key takeaways

- While new construction will aid in a gradual housing market recovery, the build up of existing inventories is a barrier. We forecast this year's housing starts will still fall short of the 3mn units needed to eliminate supply shortages.
- Supply shortages are a major obstacle to housing affordability, leaving home ownership out of reach for many low- and middle-income households.
- Although builders were more pessimistic in January, we expect sentiment to improve as declining mortgage rates, and an improving labor market will support the sector in 2026.

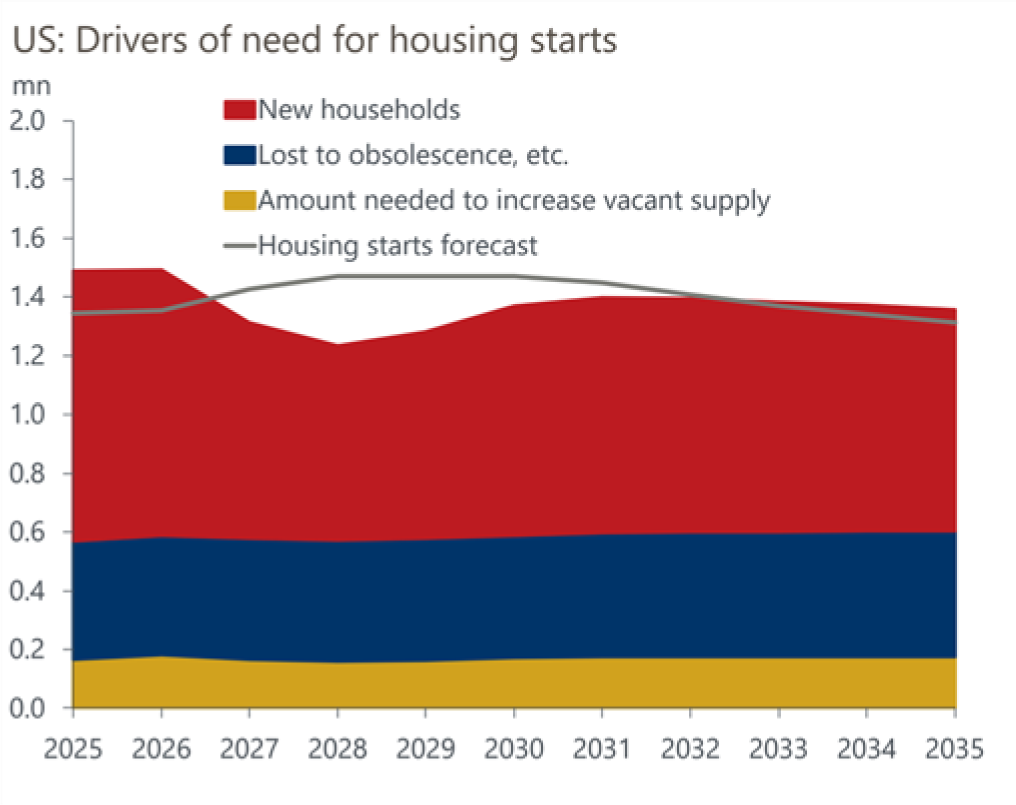
Supply shortages are a key driver of elevated housing costs

Sources: Oxford Economics, Haver Analytics

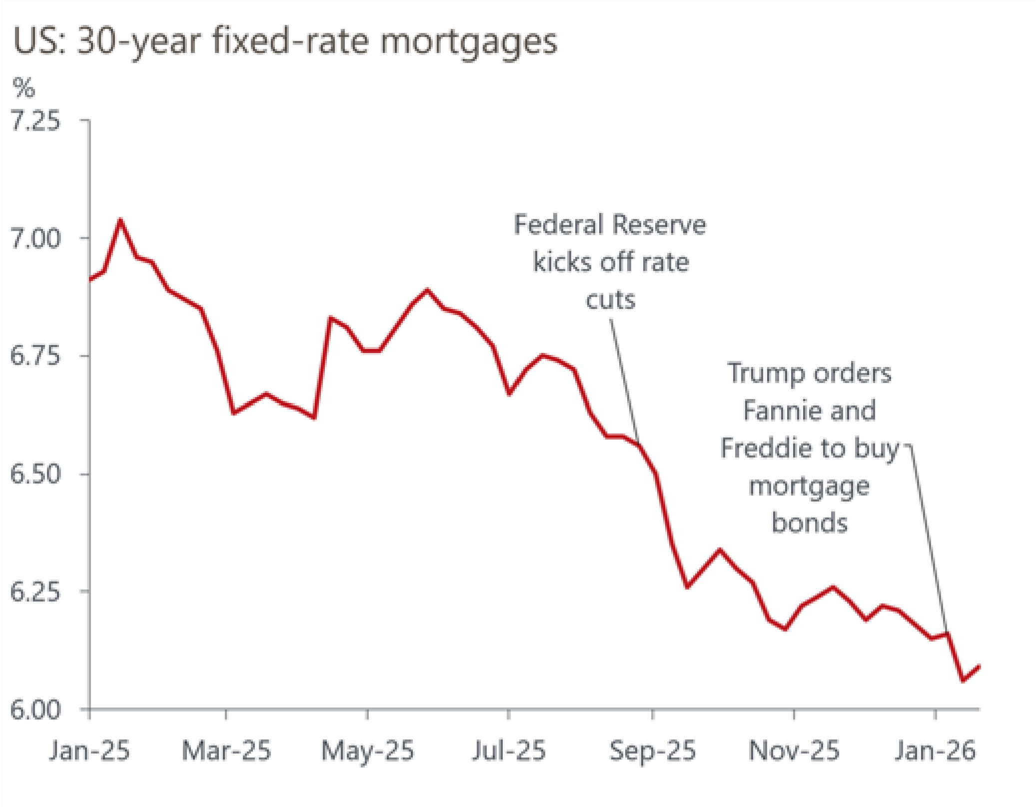


Sources: Oxford Economics, Haver Analytics

Starts and falling rates will gradually support recovery

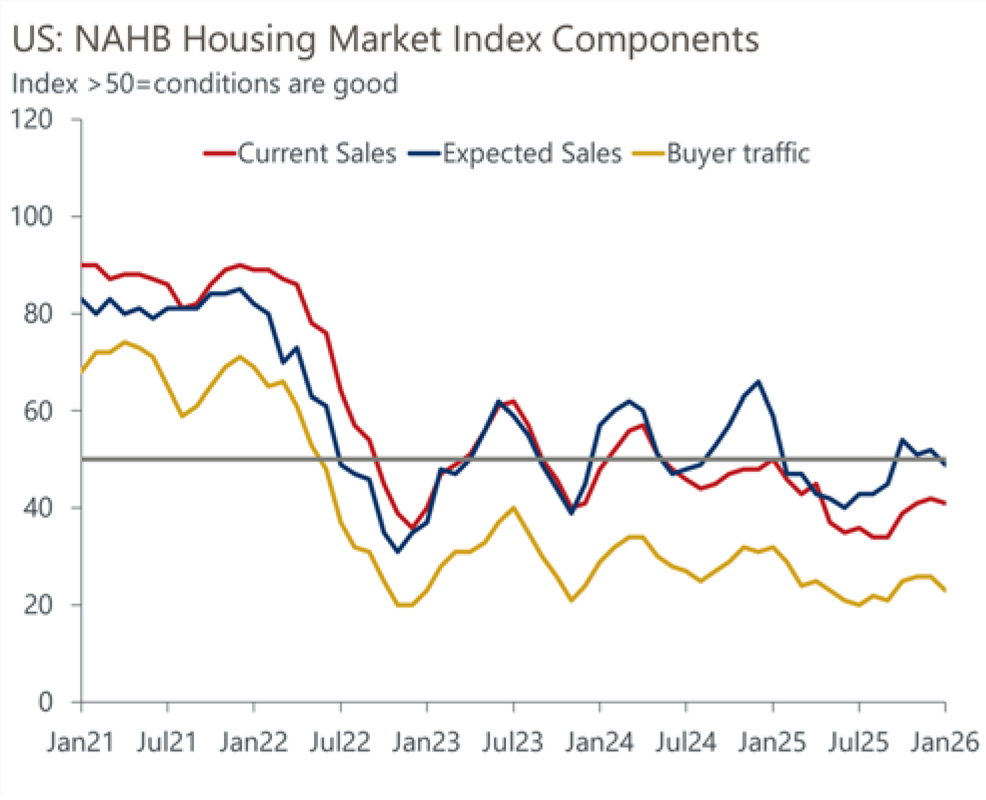


Sources: Oxford Economics, Haver Analytics

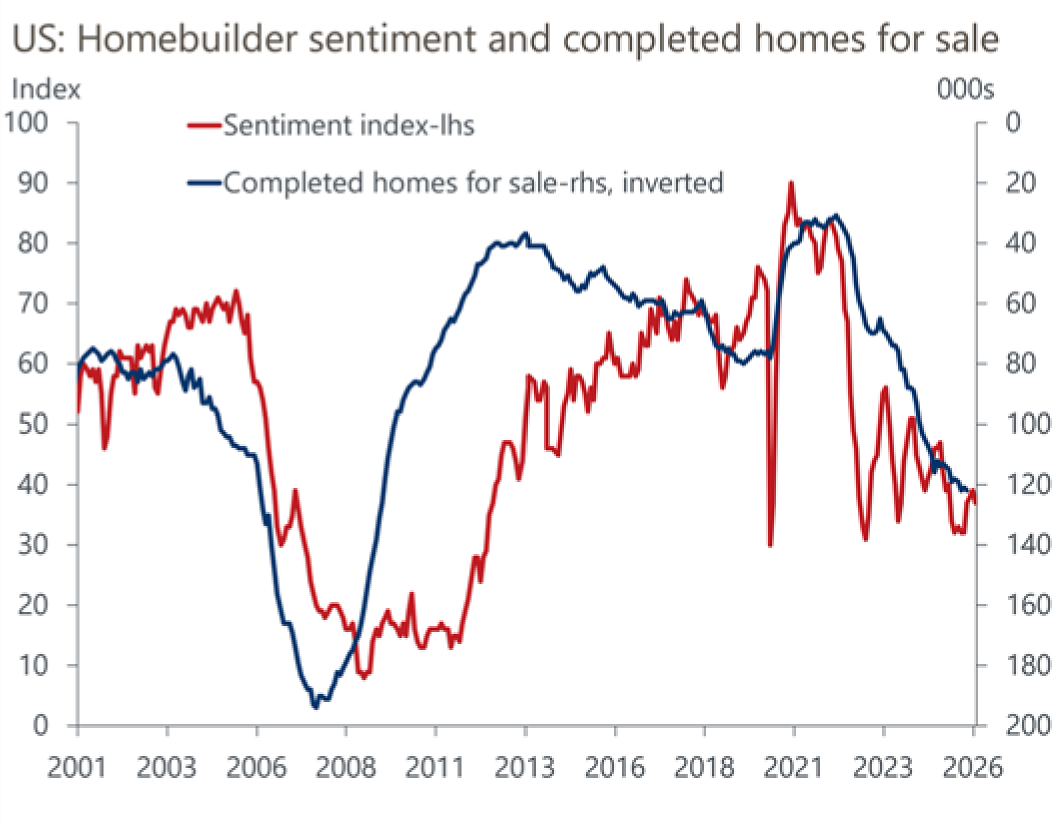


Sources: Oxford Economics, Haver Analytics

Builders continue to offer incentives to support sales



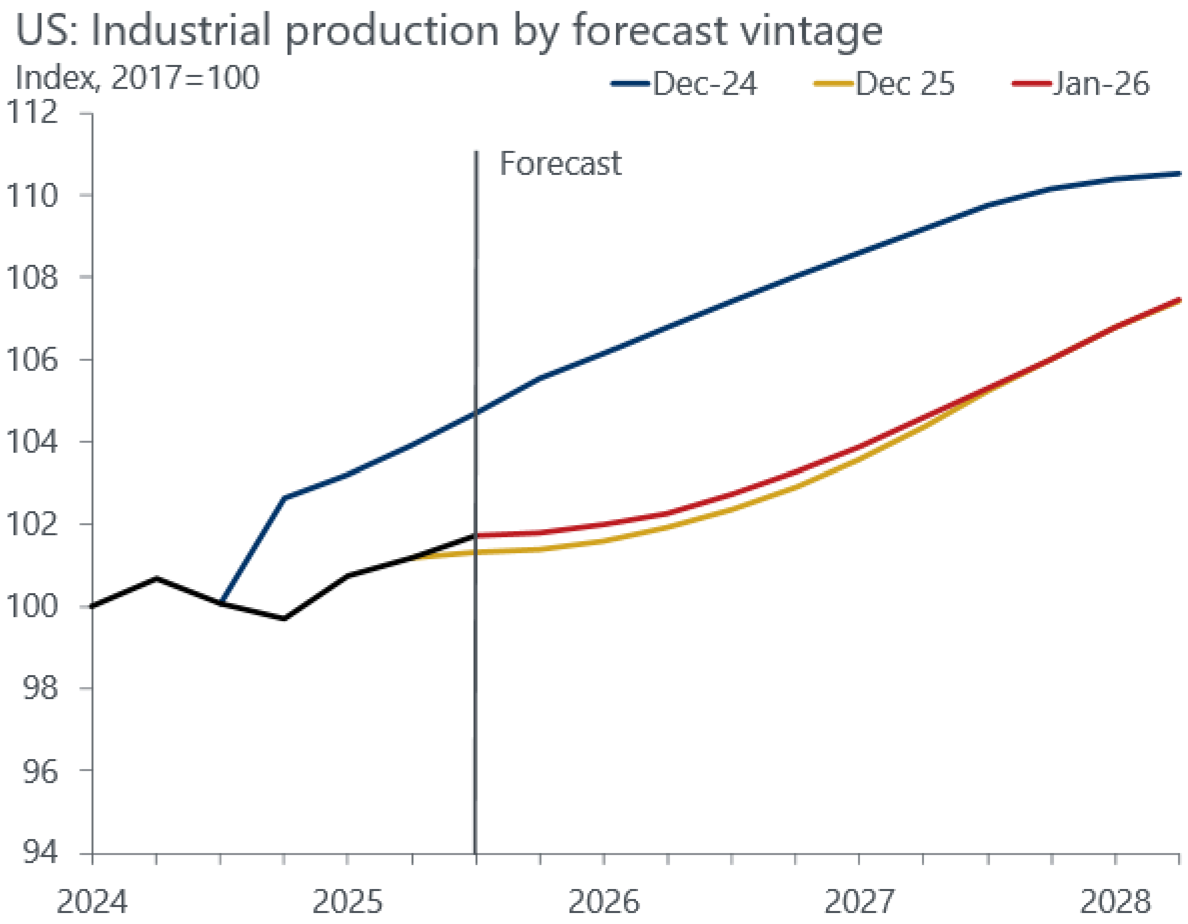
Sources: Oxford Economics, Haver Analytics



Sources: Oxford Economics, Haver Analytics

Manufacturing sector faces a slow recovery

Manufacturing faces a slow recovery

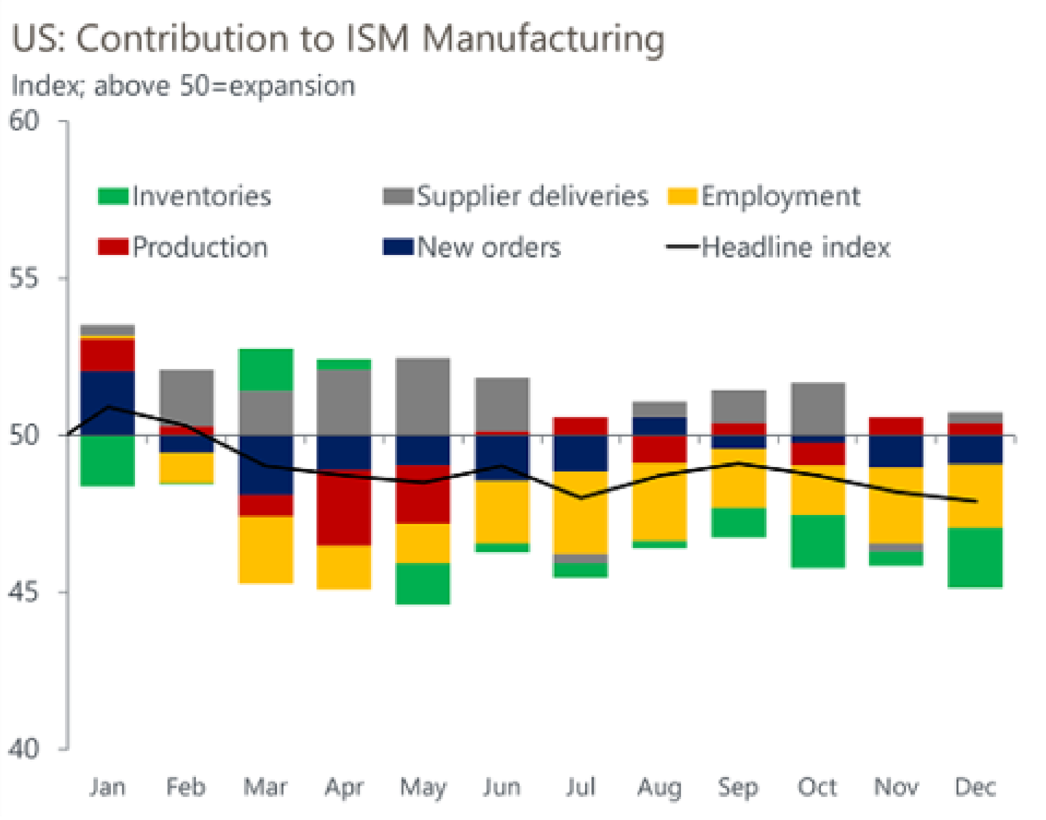


Sources: Oxford Economics, Haver Analytics

Key takeaways

- Higher prices and economic uncertainty continued to drag on the manufacturing sector in the final months of 2025.
- Geopolitical and tariff risks aside, tax incentives for business investment under the Republican spending bill, more interest-rate relief, and ongoing strength in AI and aerospace spending will support growth in factory production in 2026.
- Integrated North American supply chains make the US manufacturing industry vulnerable to changes in USMCA. The potential elimination of exemptions for USMCA compliant good is one of the largest downside risks.

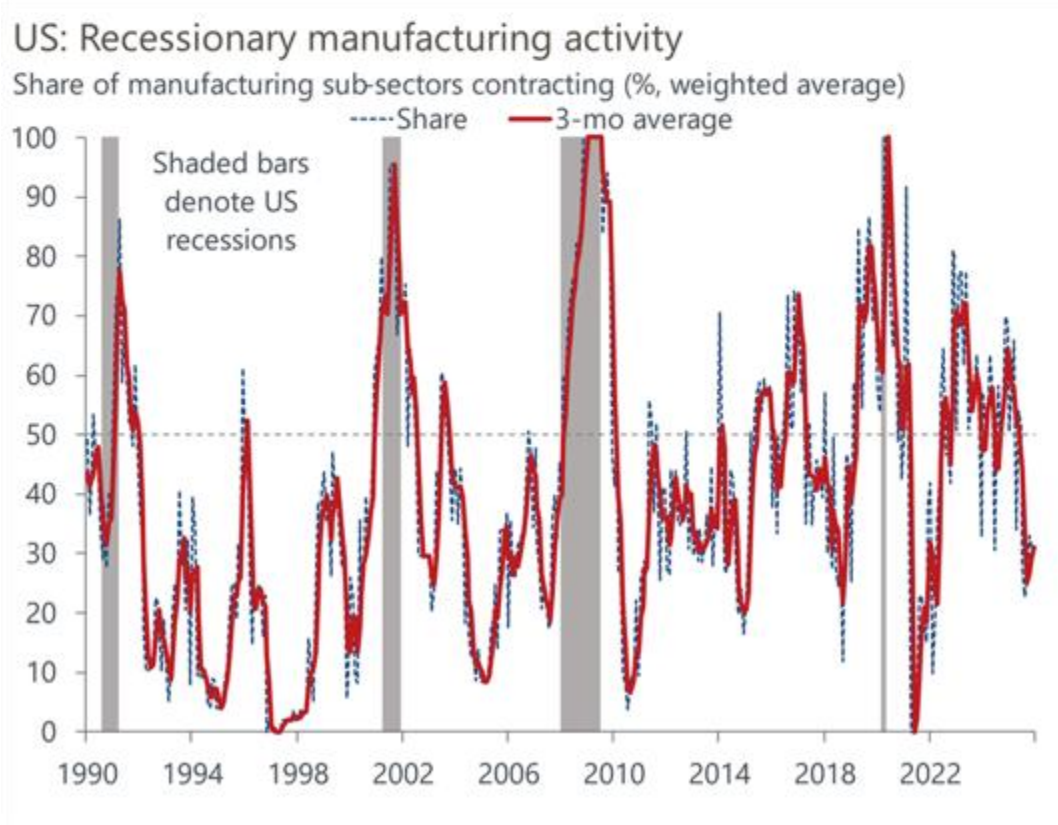
ISM index ended the year with a third consecutive decline



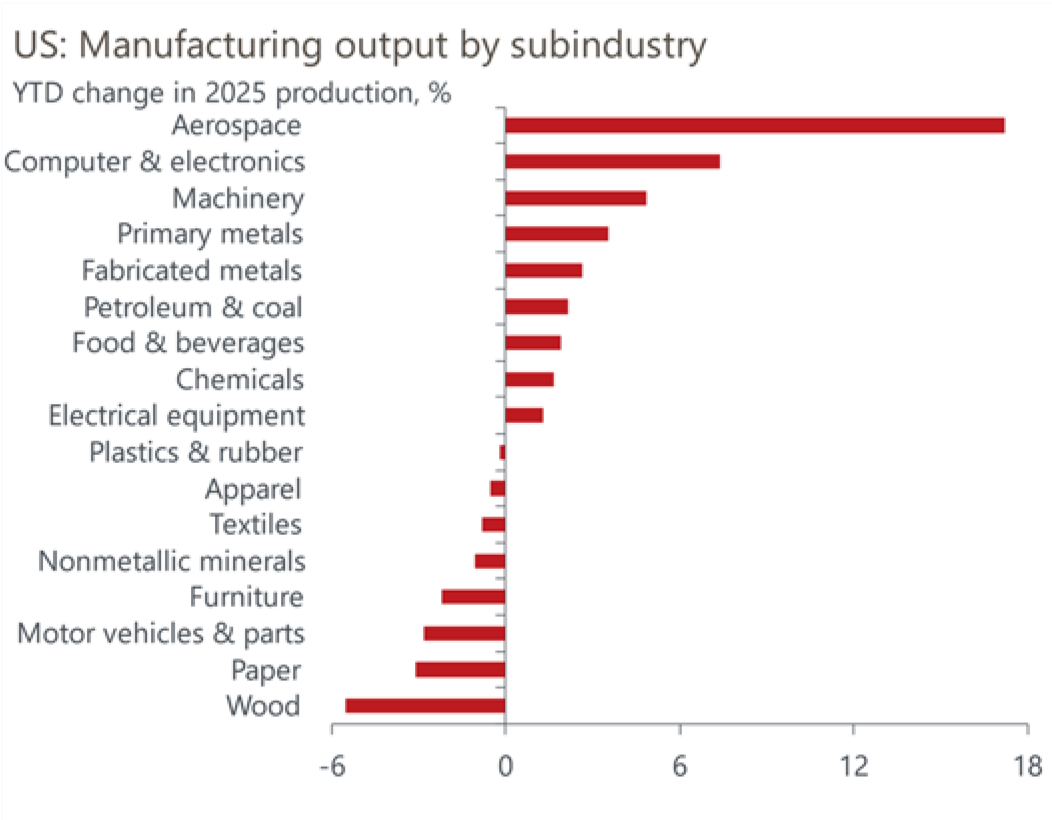
Sources: Oxford Economics, Haver Analytics

Sources: Oxford Economics, Haver Analytics

Factory output was surprisingly robust at the end of 2025

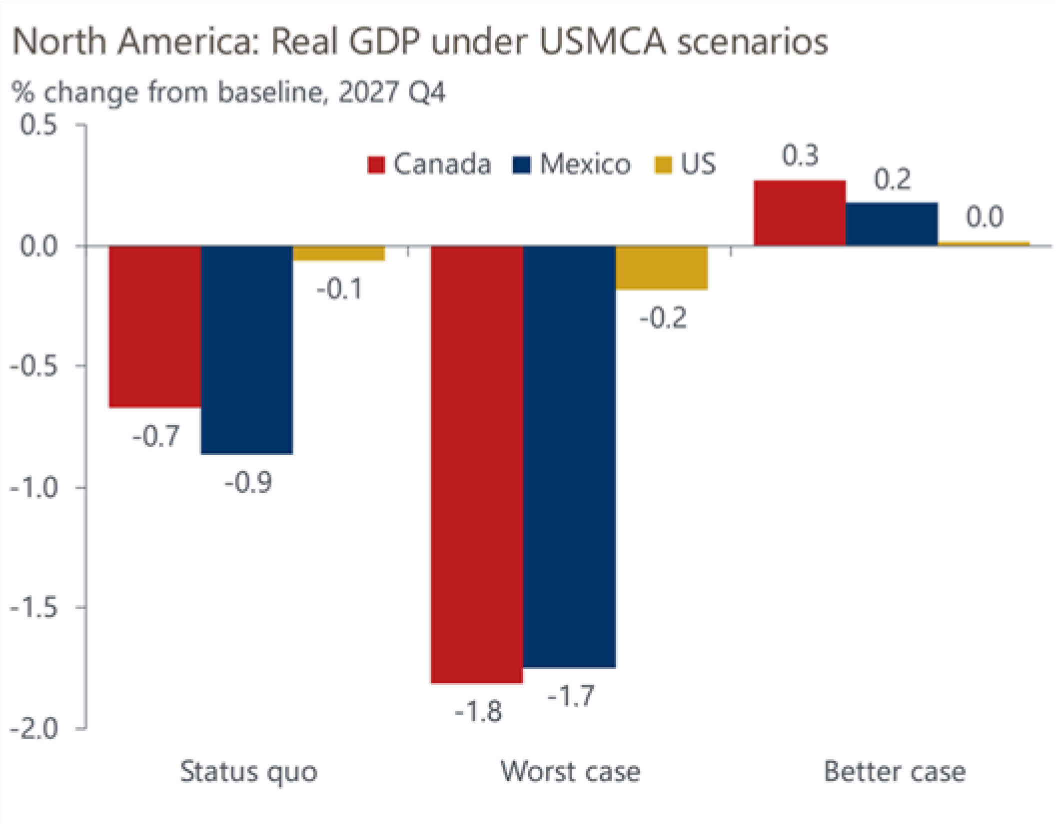


Sources: Oxford Economics, Haver Analytics

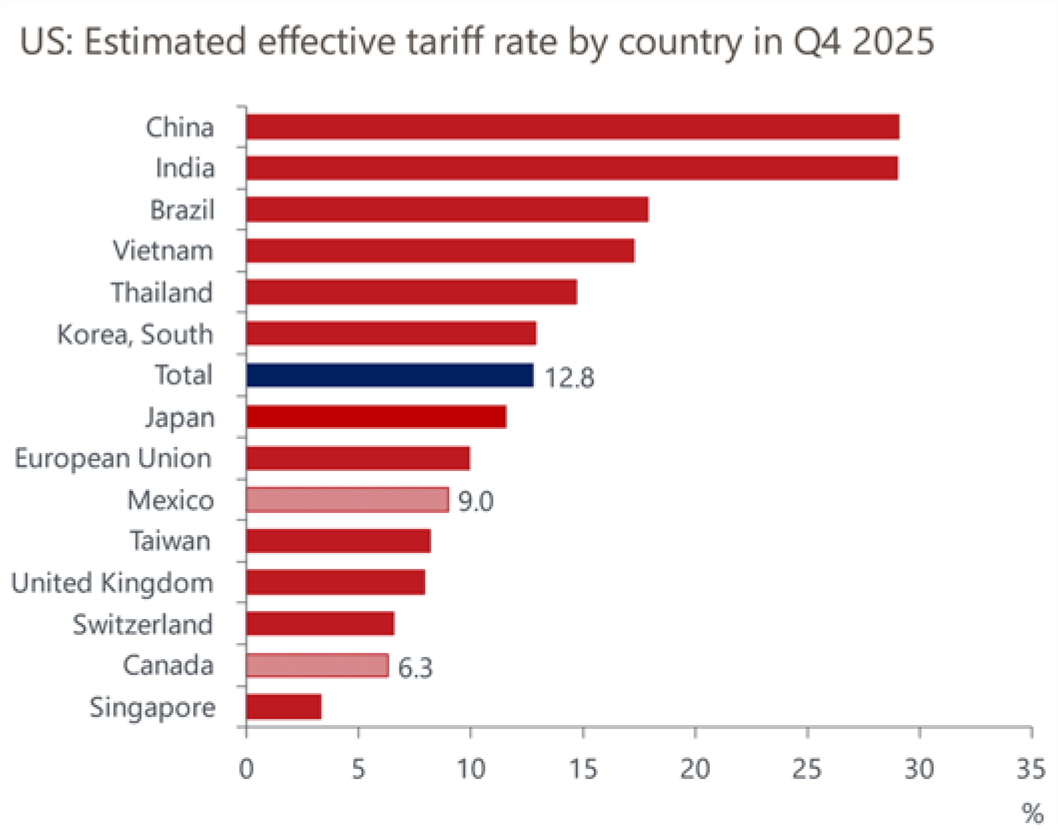


Sources: Oxford Economics, Haver Analytics

The manufacturing industry is vulnerable to USMCA changes



Sources: Oxford Economics, Haver Analytics

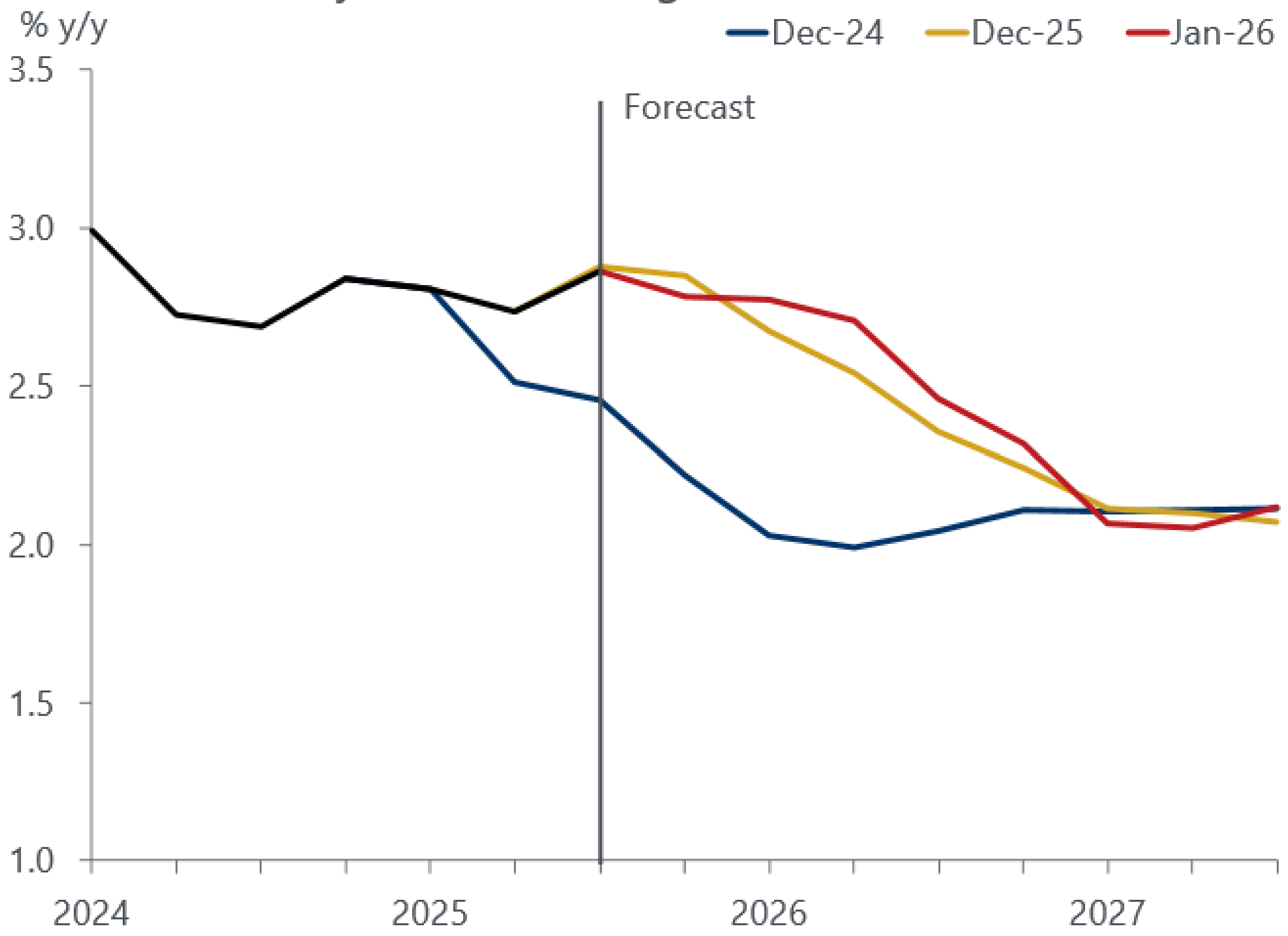


Sources: Oxford Economics, Haver Analytics

Core inflation to moderate in 2026

Inflation will fall closer to target in 2026

US: Core PCE by forecast vintage

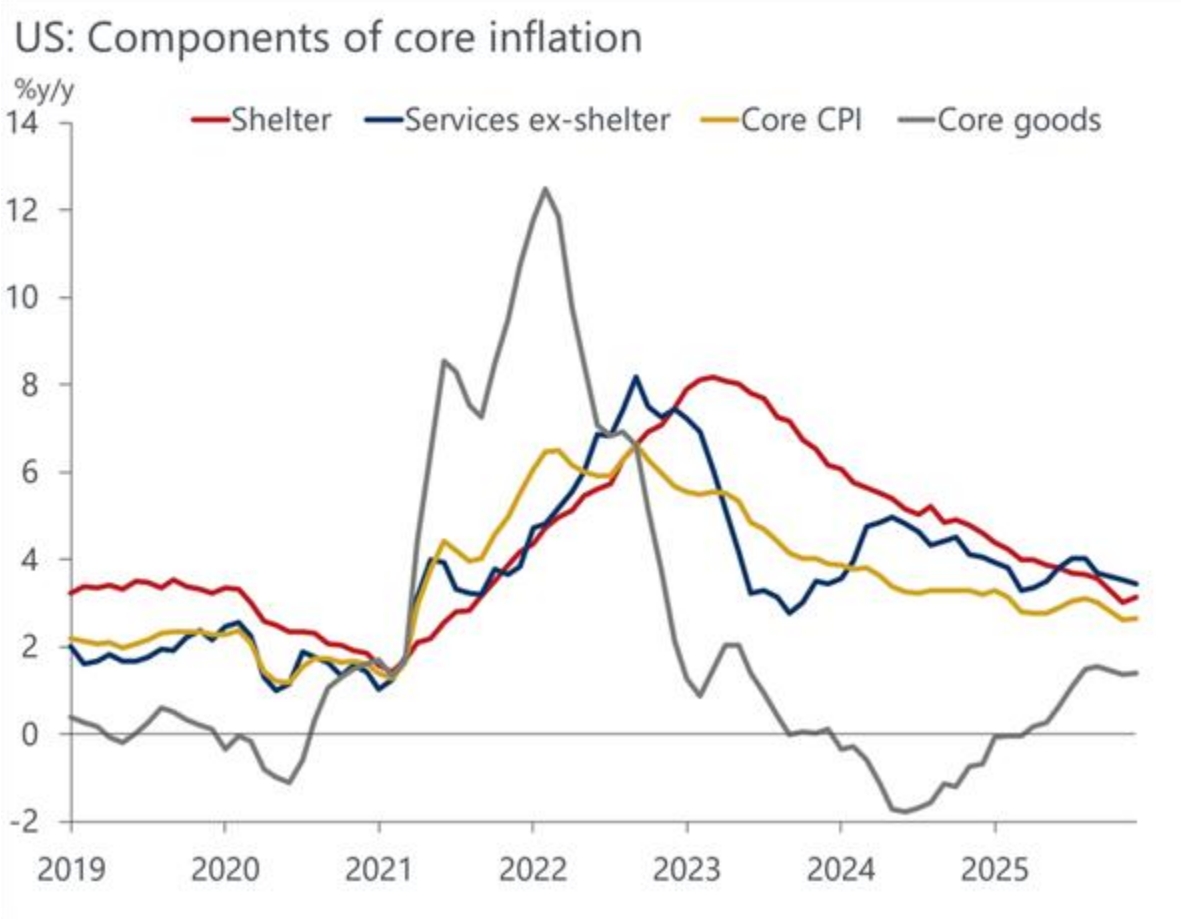


Sources: Oxford Economics, Haver Analytics

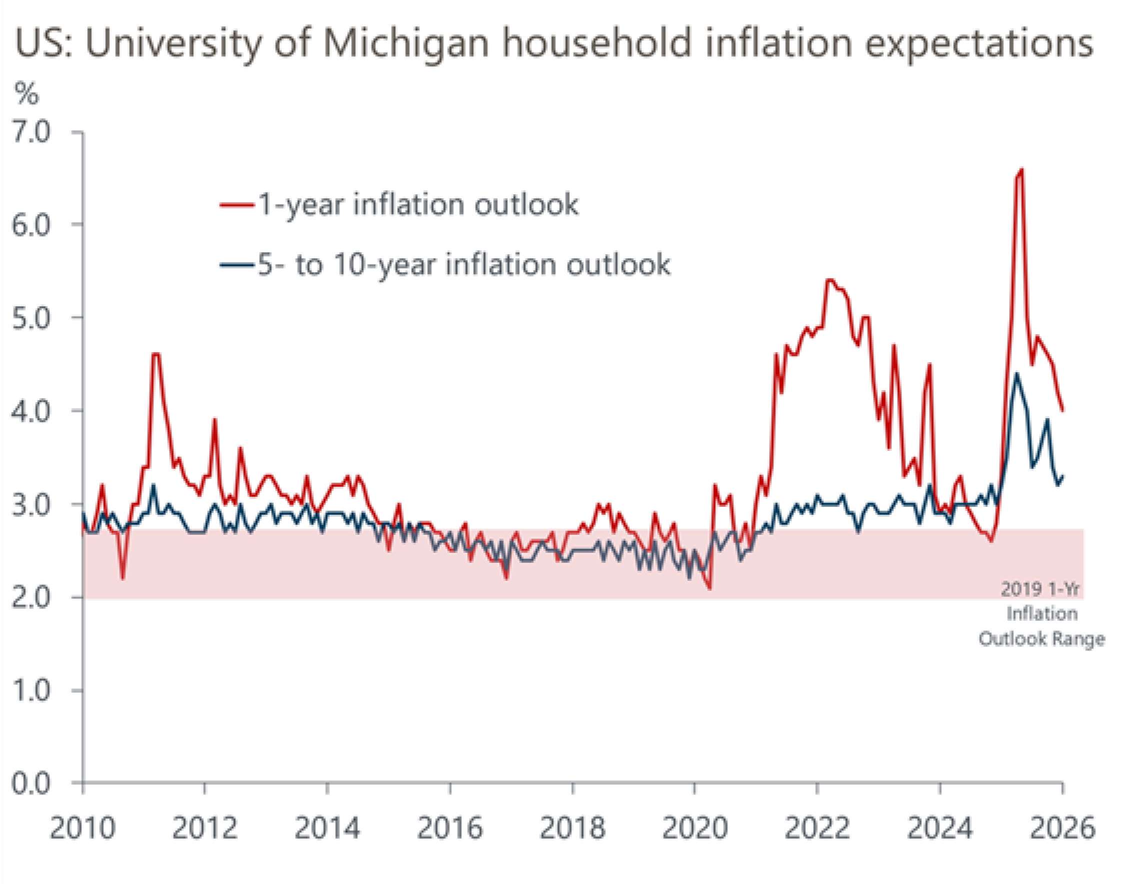
Key takeaways

- Recent inflation figures suggest that inflation has peaked. Goods inflation will find relief now that most of the tariff passthrough is behind us. On the services side, housing disinflation will also help guide inflation closer to its 2% goal by the end of 2026.
- Surging productivity growth will prevent wage growth from being a source of inflation. However, it also increases the risk of a jobless expansion, leaving the economy more vulnerable to adverse shocks.
- Low freight rates, stabilizing trade volumes, and healthy inventories will prevent inflationary supply supply-chain stress in 2026.

Core inflation moderates, expectations fall

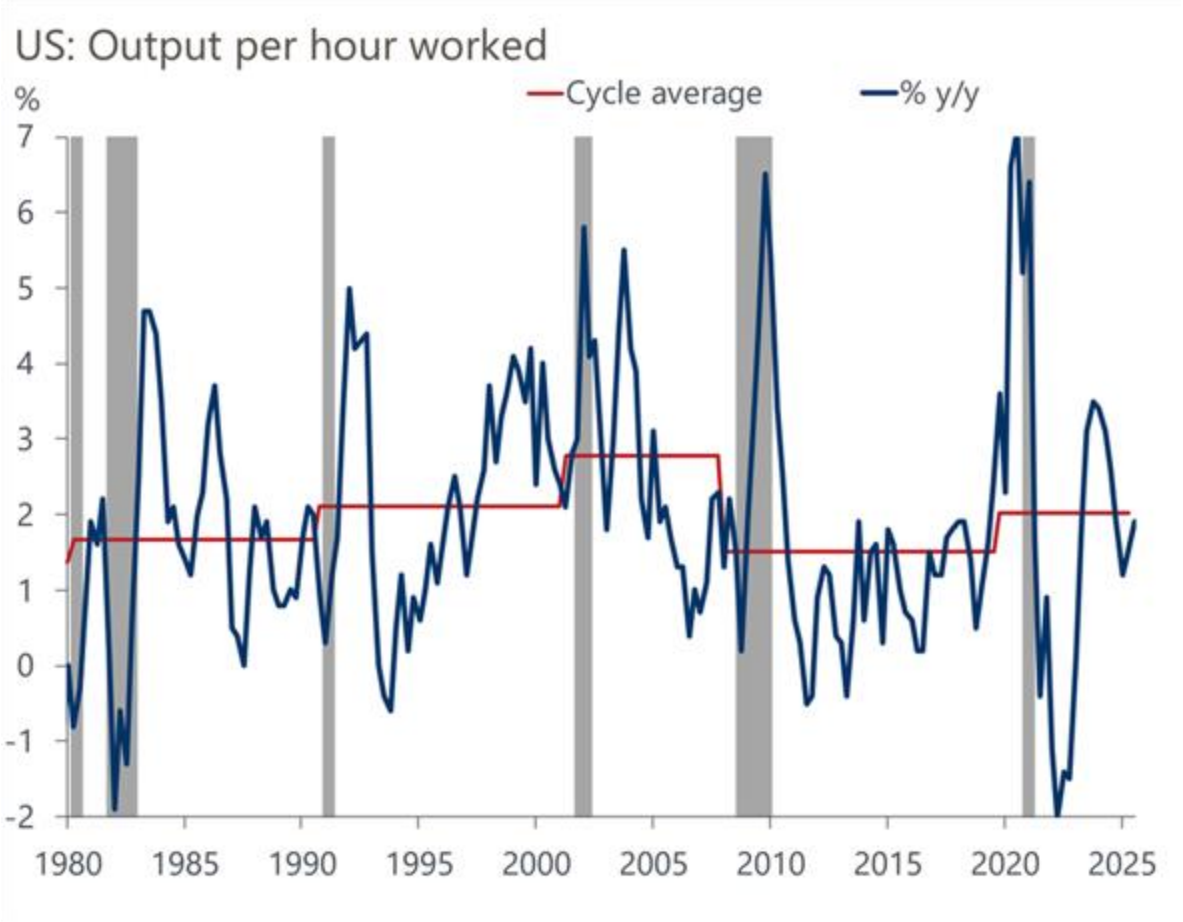


Sources: Oxford Economics, Census Bureau

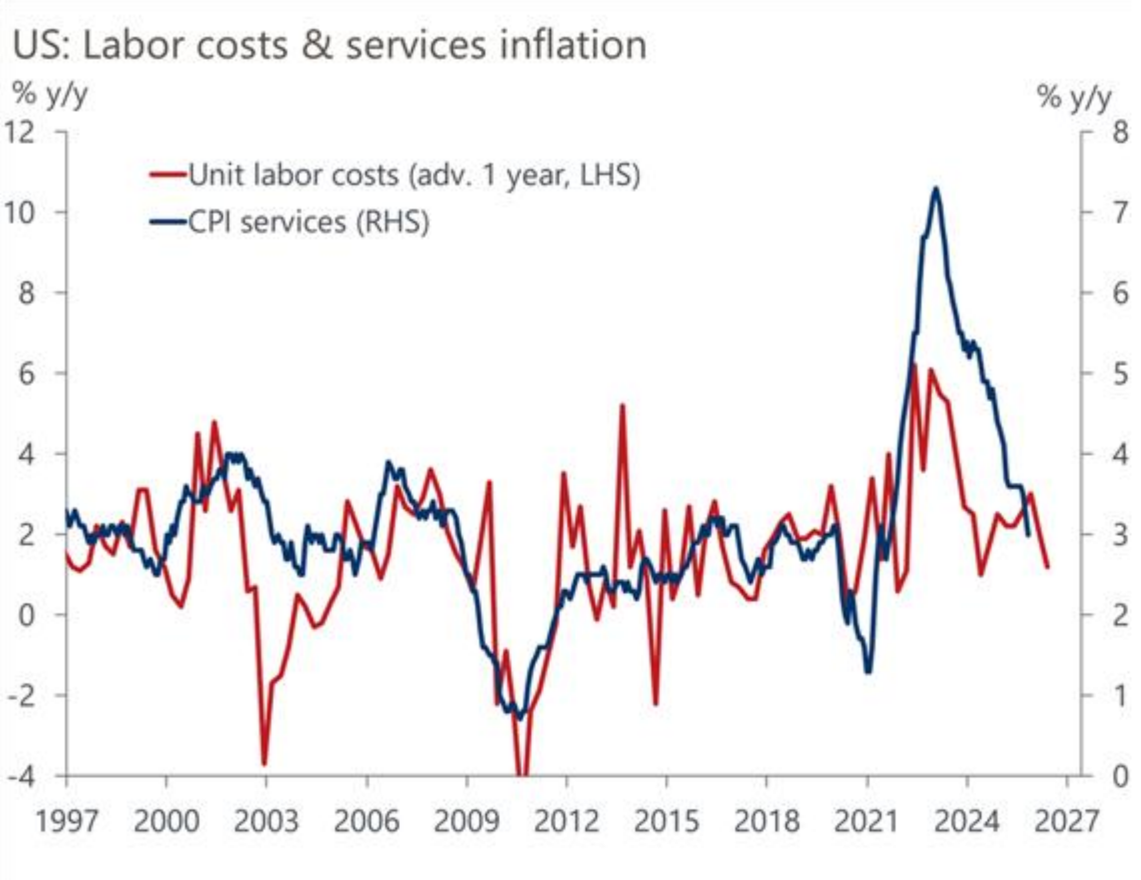


Sources: Oxford Economics, Haver Analytics

Productivity gains could support growth with limited inflation

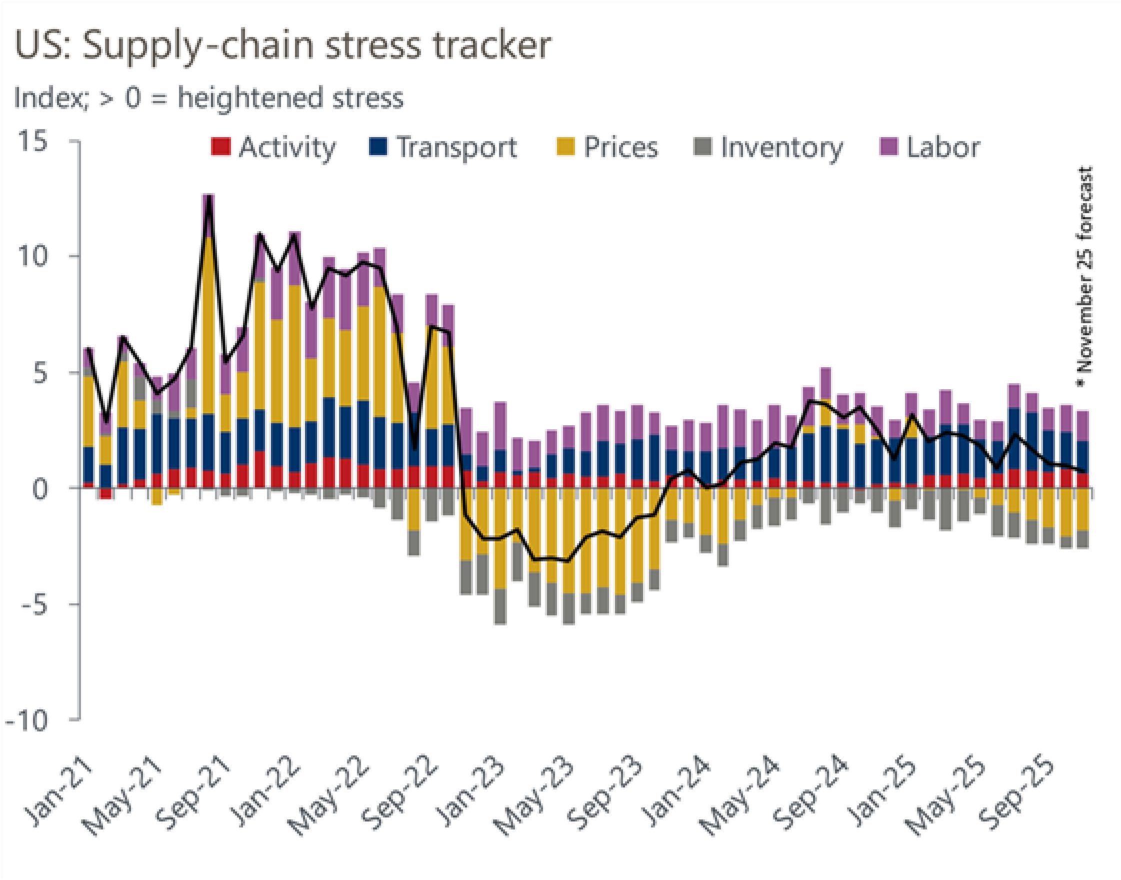


Sources: Oxford Economics, Haver Analytics

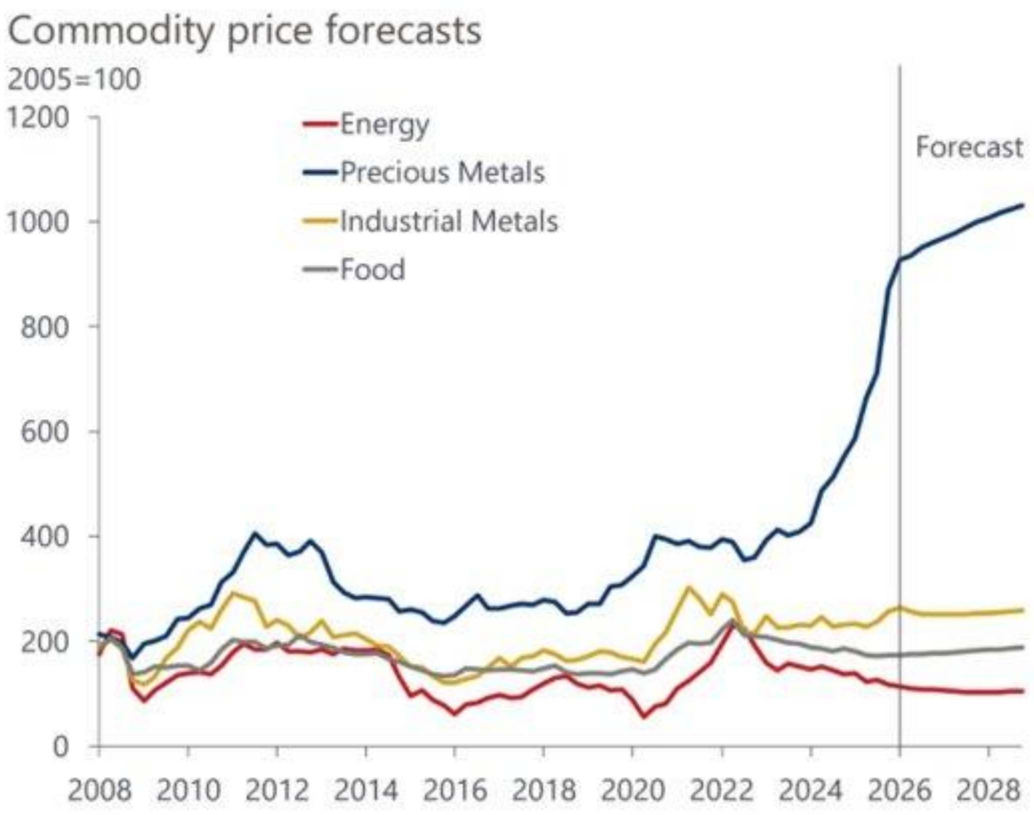


Sources: Oxford Economics, Haver Analytics

Depressed oil prices to prevent inflationary supply chain stress



Sources: Oxford Economics, Haver Analytics

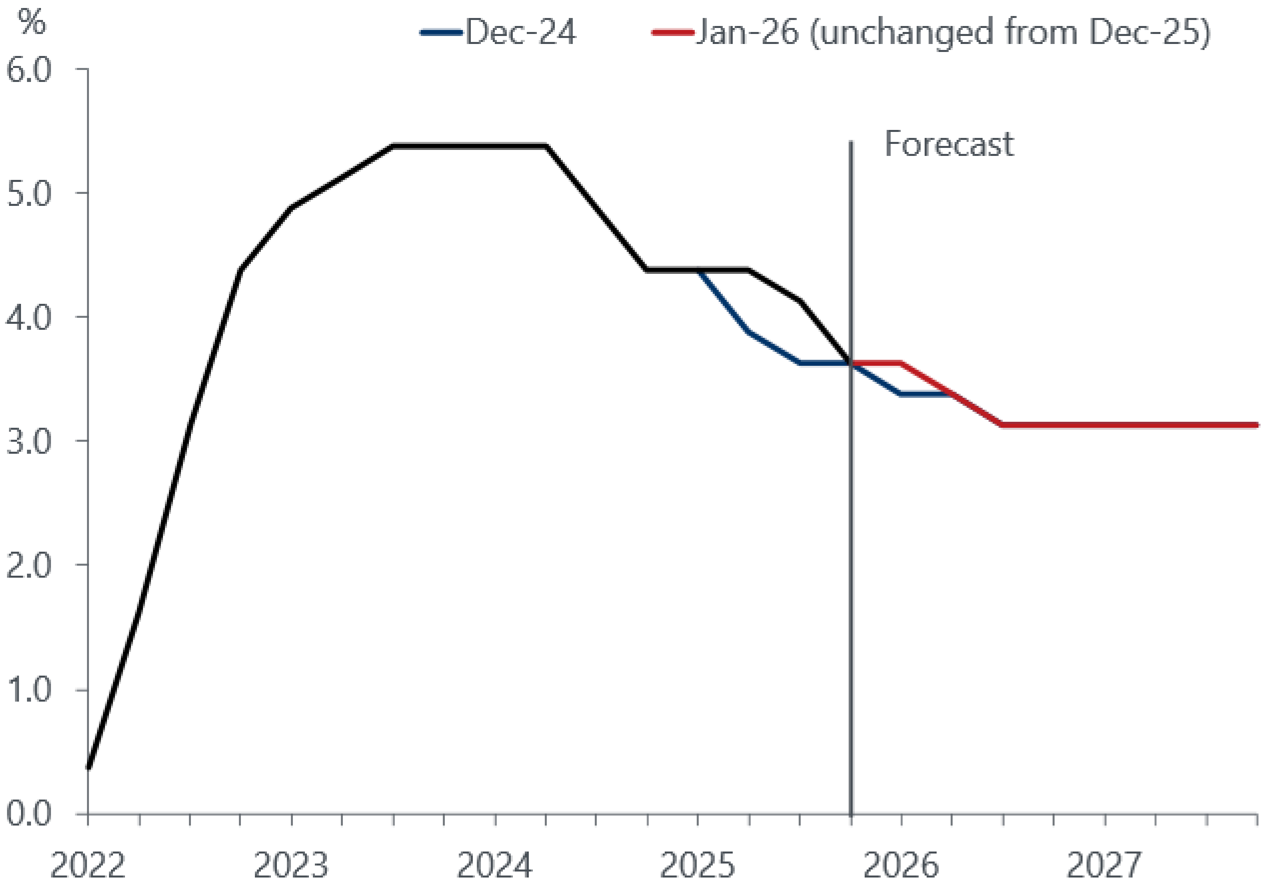


Sources: Oxford Economics, Haver Analytics

Financial market conditions and the Fed

Fed to proceed with caution in 2026

US: Fed funds rate by forecast vintage

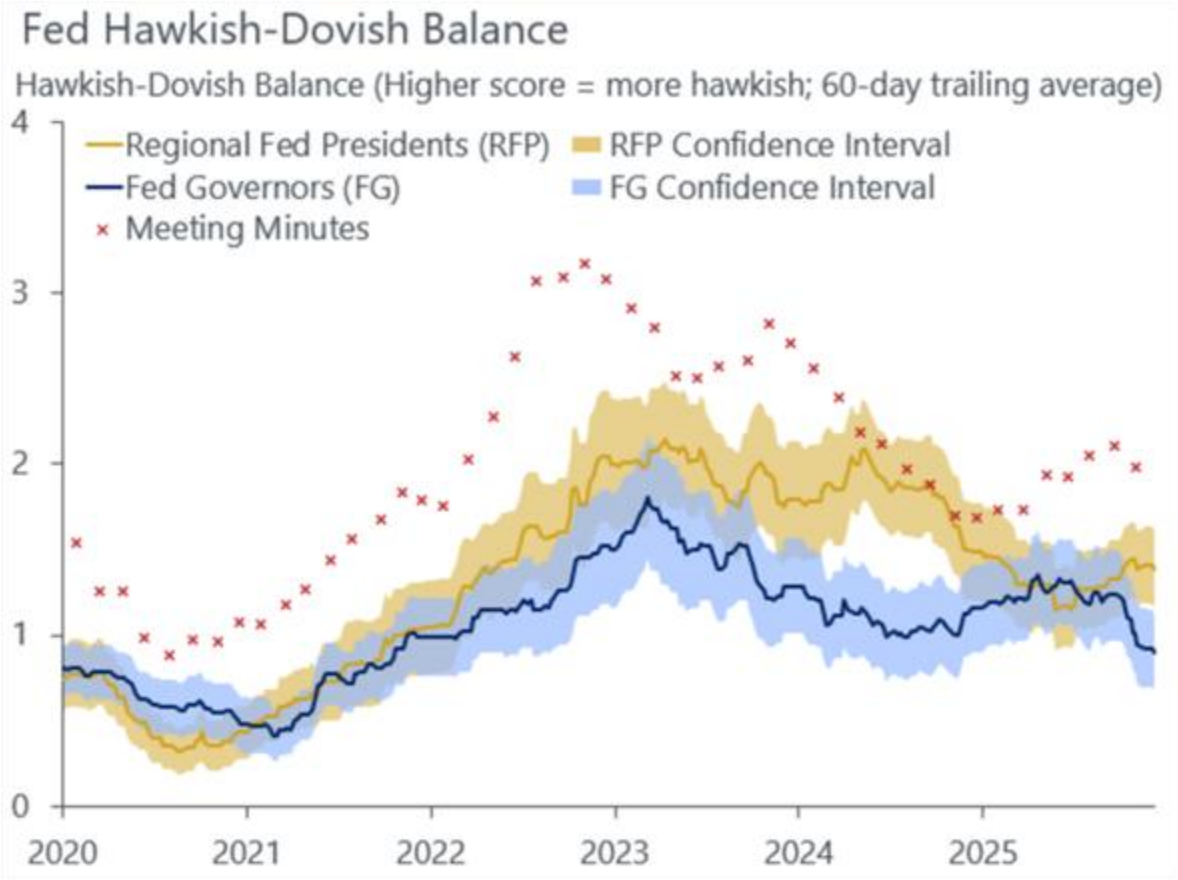


Sources: Oxford Economics, Haver Analytics

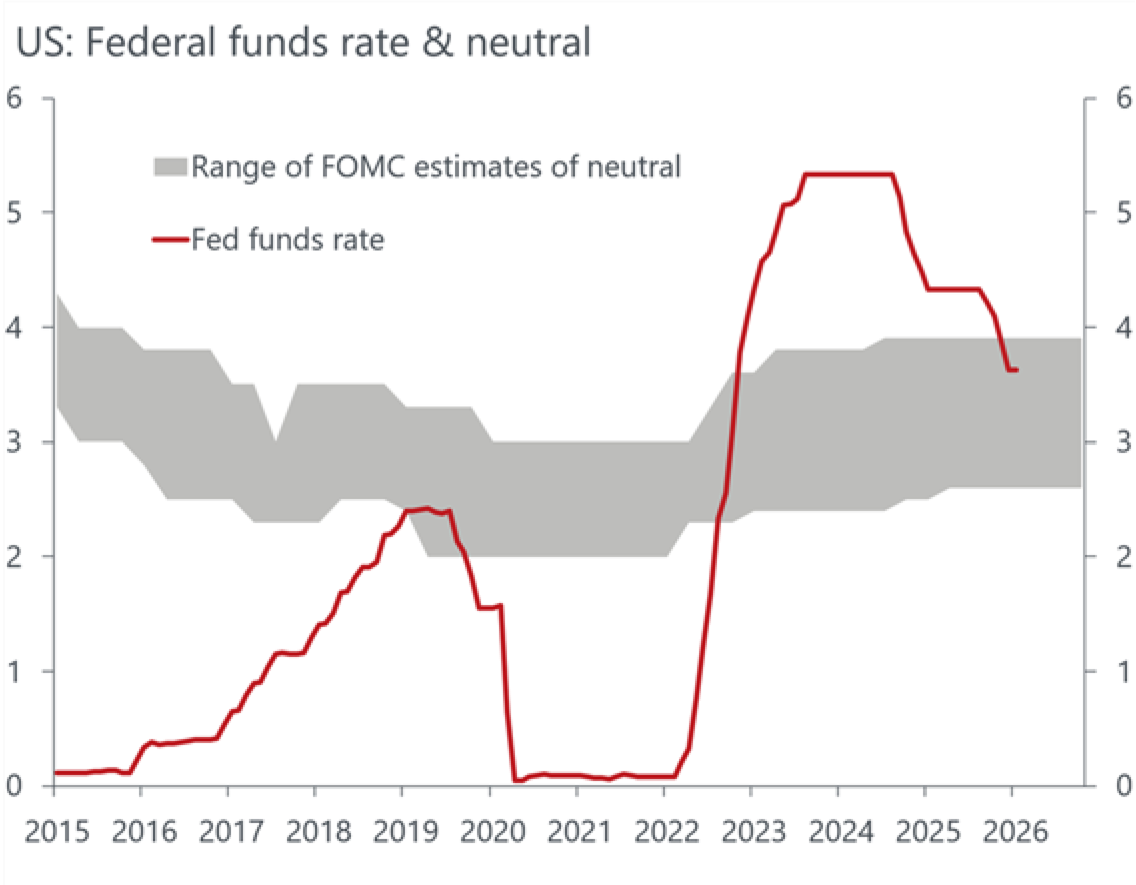
Key takeaways

- The FOMC left rates unchanged in January. We think the Fed is likely to opt for an extended pause as rates are close to neutral and the downside risks to the labor market have begun to ease. We forecast cooling inflation to motivate cuts in June and September.
- Despite trade tensions, strong corporate profits and investment incentives continue to drive earnings momentum in both tech and non-tech cyclical sectors.
- Although the EU holds significant dollar-denominated assets, a large-scale selling in reaction to Greenland threats is unlikely due to losses.

Fed to stay on pause, although the Committee is still divided



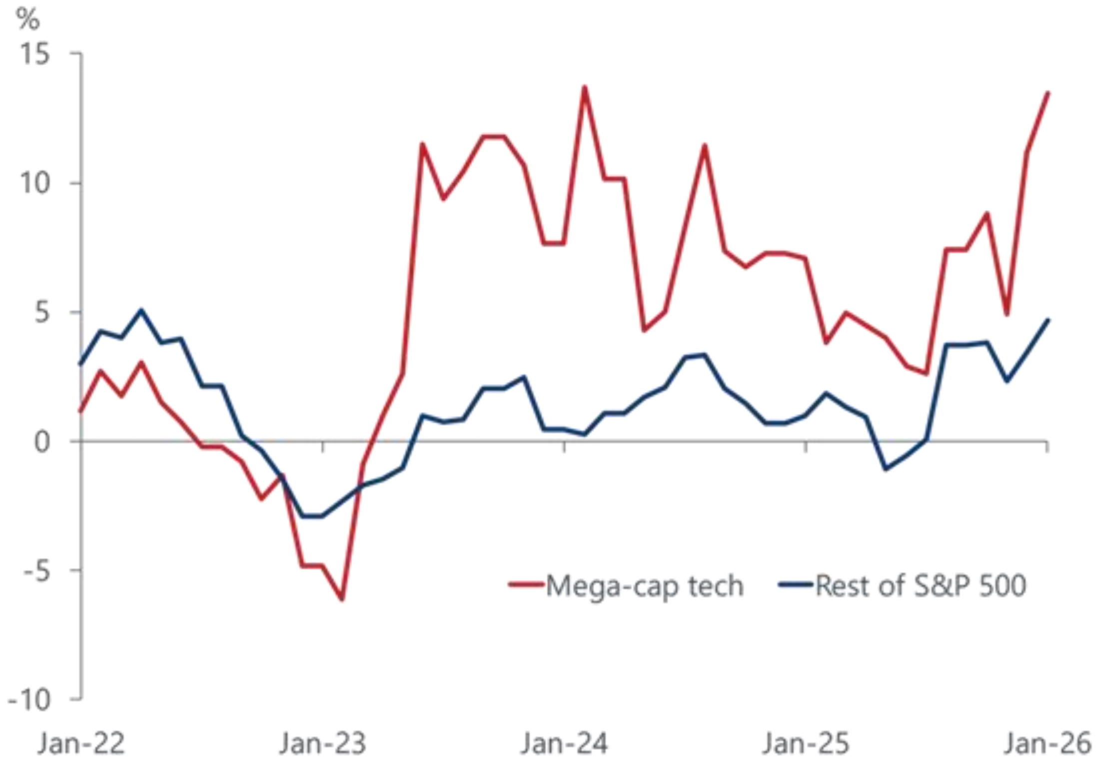
Source: Oxford Economics



Sources: Oxford Economics, Haver Analytics

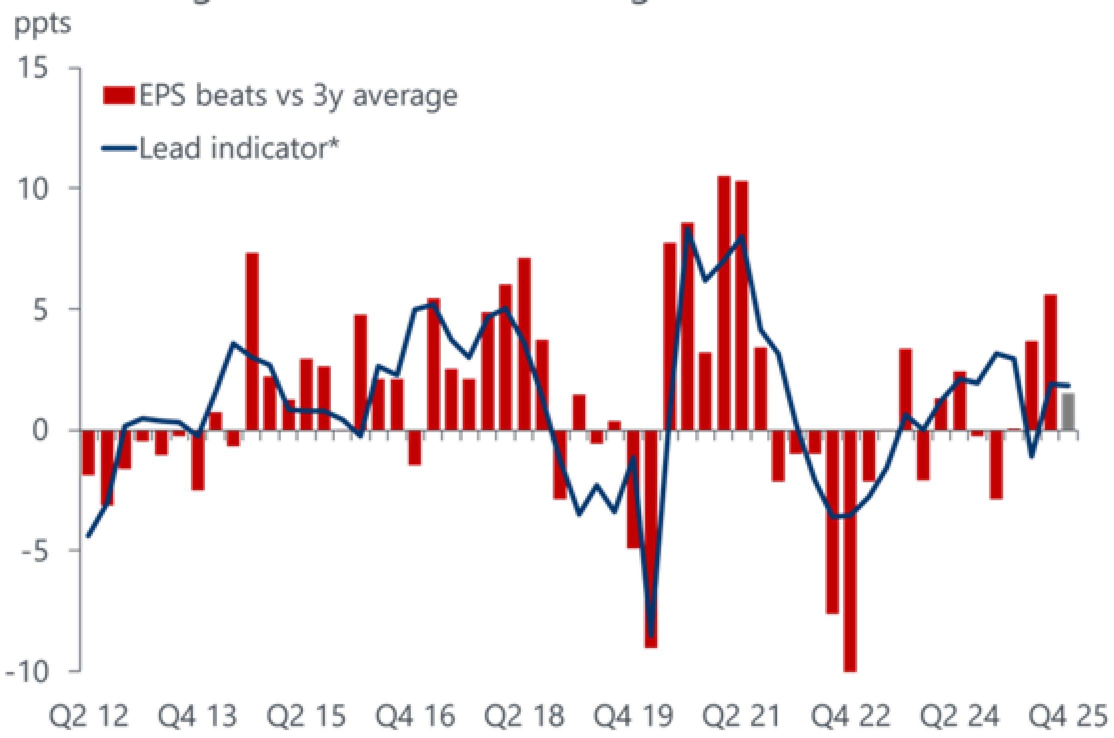
Earnings momentum drives broadening strength in equities

EPS momentum: 3 month change in 12m fwd EPS



Sources: Oxford Economics, LSEG DataStream

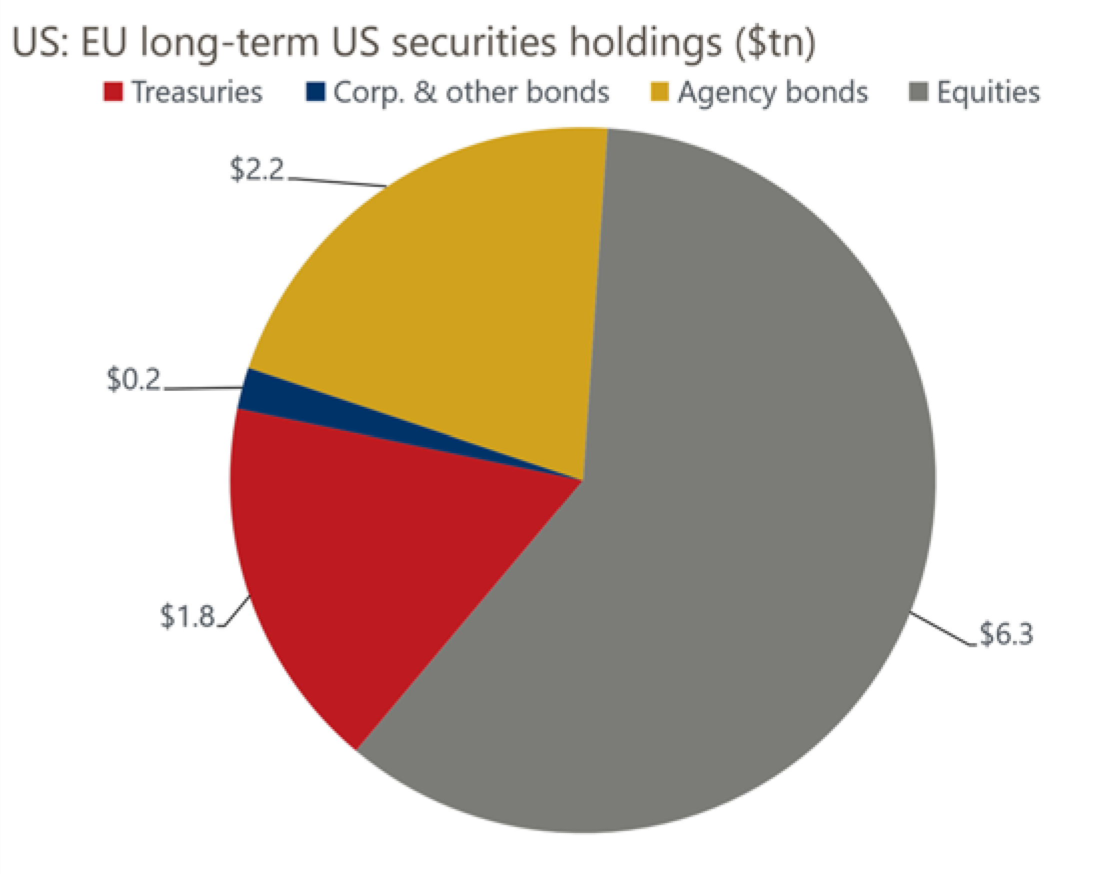
US earnings season beats vs average



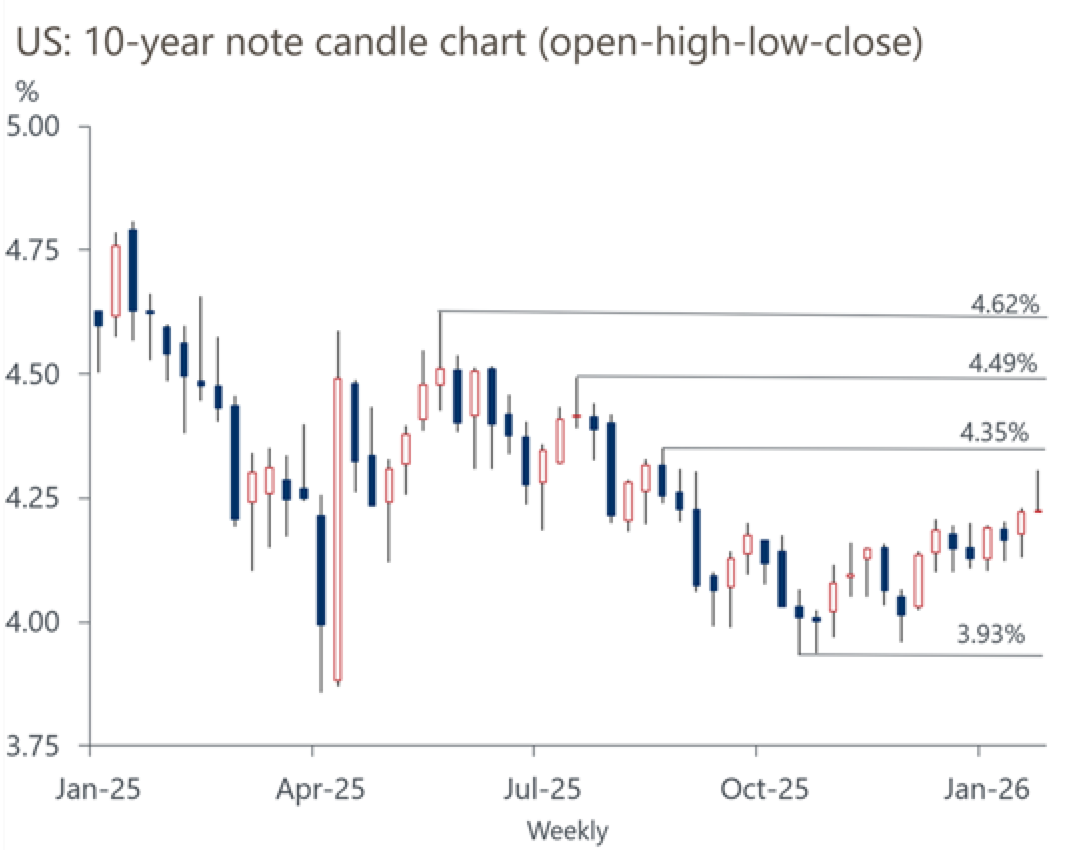
*based on CEO confidence, earnings preannouncements and US activity surprises

Sources: Oxford Economics, LSEG DataStream

The threat of a foreign sell-off is unlikely to materialize



Sources: Oxford Economics, Bloomberg LP, US Treasury TIC



Sources: Oxford Economics, Bloomberg

Forecast summary

US yearly outlook table

Forecast for United States (Annual percentage changes unless specified)	2023	2024	2025	2026	2027	2028
GDP	2.9	2.8	2.2	2.8	2.3	2.2
Private consumption	2.6	2.9	2.6	2.4	2.2	2.1
Fixed investment	3.8	3.5	3.0	3.9	3.8	3.3
Government consumption	3.0	3.3	0.8	2.0	1.0	1.0
Exports of goods and services	2.8	3.6	1.8	2.2	2.2	2.0
Imports of goods and services	-0.9	5.8	2.4	-2.0	3.7	3.1
Industrial production	-0.2	-0.6	1.3	1.2	2.3	2.7
Consumer price index	4.1	3.0	2.7	2.4	2.2	2.3
Unemployment rate (%)	3.6	4.0	4.3	4.4	4.2	4.2
Current a/c balance (% of GDP)	-3.3	-4.0	-3.6	-2.9	-3.0	-3.0
Government balance (% of GDP)	-6.1	-6.2	-5.8	-7.1	-6.8	-6.5
Central bank policy rate (%, EOP)	5.38	4.38	3.63	3.13	3.13	3.13
10yr government. bond yield (%, EOP)	3.88	4.58	4.18	4.21	4.20	4.20
Exchange rate (Yen per US$, EOP)	141.91	156.65	156.43	148.24	142.27	137.31
Exchange rate (US$ per euro, EOP)	1.11	1.04	1.18	1.16	1.16	1.16

Source: Oxford Economics

US quarterly outlook table

Quarterly forecasts for US	2025 Q3	2025 Q4	2026 Q1	2026 Q2	2026 Q3	2026 Q4	2027 Q1	2027 Q2
GDP (% chg, saar)	4.3	2.3	2.7	2.5	2.2	2.3	2.4	2.3
CPI inflation (% year)	2.9	2.8	2.5	2.7	2.4	2.2	2.2	2.1
Core CPI inflation (% year)	3.1	2.7	2.6	2.8	2.5	2.6	2.6	2.5
PCE inflation (% year)	2.7	2.7	2.6	2.7	2.4	2.2	2.0	2.0
Core PCE inflation (% year)	2.9	2.8	2.8	2.7	2.5	2.3	2.1	2.1
10-year Treasury yield (%, EOP)	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
Federal funds rate (%, EOP)	4.125	3.625	3.625	3.375	3.125	3.125	3.125	3.125

Source: Oxford Economics

Fiscal Policy Assumptions

Permanent Version in the One Big Beautiful Bill Act as Assumed in the Baseline Forecast												
Estimated Budgetary Effects Relative Current Policy												
	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2025-2029	2025-2034
Net Deficit Impact	**-46,962**	**270,653**	**153,507**	**134,089**	**73,542**	**14,477**	**-29,525**	**-55,489**	**-29,925**	**-19,544**	**584,828**	**464,819**
TCJA Expansions	21,878	89,657	82,395	87,036	82,709	87,131	91,987	95,447	100,226	103,535	363,677	842,003
Campaign Tax Proposals	2,663	54,773	44,970	44,603	48,447	51,633	53,645	55,045	56,624	58,380	195,456	470,783
Investment Incentives	100,034	128,307	100,156	83,070	61,882	40,132	22,144	15,018	13,118	12,703	473,449	576,564
Defense	2,020	41,864	44,677	45,741	47,868	48,932	51,059	52,123	54,251	55,314	182,170	443,850
Border Security/Immigration	0	13,683	25,455	35,890	37,966	38,533	41,349	41,490	42,902	44,281	112,994	321,549
IRA Recissions (Outlays)	-857	-1,027	-1,316	-937	-607	-360	-112	0	0	0	-4,744	-5,216
IRA Recissions (Tax Credits)	138	-11,276	-36,791	-53,755	-67,749	-79,073	-86,370	-94,397	-60,658	-52,728	-169,433	-542,659
Social Benefits Cuts (Medicaid)	-835	-21,813	-54,248	-73,117	-106,367	-127,074	-146,220	-156,518	-170,171	-186,243	-256,380	-1,042,606
Social Benefits Cuts (SNAP)	0	-7,961	-16,116	-21,645	-21,744	-21,748	-21,565	-24,743	-25,150	-25,268	-67,466	-185,940
Social Benefits Cuts (Other health	4	-4,047	-11,992	-16,518	-12,543	-9,233	-10,715	-12,274	-14,706	-16,533	-45,096	-108,555
Other (Spending)	-171,940	-9,411	1,144	-7,304	-11,174	-23,155	-31,933	-33,690	-28,685	-19,642	-198,685	-335,790
Other (Revenue)	-68	-2,097	-24,828	11,024	14,853	8,759	7,206	7,009	2,324	6,656	-1,114	30,836

Source: Oxford Economics

Major tariff assumptions

Tariff assumptions in our baseline (based on information available as of December 5)		
Tariffed countries	**US tariffs**	**Retaliation measures**
US / Canada	Tariffs of 50% on steel, aluminium, and copper, 10% on lumber, 25% on furniture, 25% on the non-US content of USMCA-compliant autos and trucks, 10% on non-USMCA-compliant energy and potash, and 35% on all other non-USMCA-compliant products. USMCA compliance rose sharply after tariffs were implemented. Consequently, the effective tariff rate on Canada is estimated to peak not much higher than 6% this year. Most tariffs are still assumed to be removed by Q3 2026 as the USMCA is renegotiated, but smaller 10% targeted tariffs remain in place permanently for metals and select agricultural products.	As of March 4, 25% tariffs on C$30bn of US goods imports. As of March 13, 25% tariffs on an additional C$29.8bn of US goods imports (i.e., steel, aluminium, and other products). As of April 9, 25% tariffs on C$35.6bn of non-USMCA-compliant autos and the US content of USMCA-compliant autos. As of October 23, GM and Stellantis reductions in remissions leaves C$31.6bn of US auto imports eligible for tariff relief until mid-2026. As of September 1, Canada removed counter tariffs on all non-auto products except for C$15bn worth of steel and aluminium products, of which we estimate about half are eligible for remission until mid-December. Most tariffs are assumed to be removed by Q3 2026 as the USMCA is renegotiated, but smaller 10% targeted tariffs remain in place permanently for steel and aluminium products.
US / Mexico	Tariffs of 50% on steel, aluminium, and copper, 10% on lumber, 25% on furniture, 10% on non-USMCA-compliant potash, and 25% on non-USMCA goods and the non-US content of autos and trucks. As with Canada, USMCA compliance has risen sharply. As a result, the average tariff rate on Mexico is estimated to peak at 9% this year. However, these tariff hikes are assumed to be largely reversed in mid-2026 when a new USMCA trade deal is agreed.	Mexico does not retaliate and instead concedes to US demands on border security, hoping to secure a reduction in the current 25% tariff on non-USMCA-compliant exports.
US / EU	The 50% tariff on steel, aluminium, and copper apply to the EU. However, the EU-US trade deal imposes a 15% tariff ceiling for EU goods subject to reciprocal tariffs. The 15% flat rate also applies to autos, auto parts, and furniture, not to mention additional product categories such as pharmaceuticals and semiconductors that are subject to Section 232 trade investigations. For now, the baseline is holding off from assuming a 15% tariff on pharma and chips until more details are known. The US cut tariffs on aircraft and parts to zero as part of the deal.	We now assume no retaliation from EU countries following the agreement with the US announced on 27 July.
US / China	The US has recently cut the earlier 20% 'fentanyl' tariffs on China to 10%, while the baseline 10% rate remains. We assume the latest de-escalation in US-China trade tensions is permanent. Accounting for exemptions and other sectoral tariffs, including the new 10% lumber and 25% furniture tariffs, we estimate the effective tariff rate on Chinese exports to the US is now lower at 29%.	Revised bilateral trade terms in October brought China tariffs on US goods down to around 18%, from around 30% previously. Under those terms China would also suspend retaliatory non-tariff countermeasures taken against the US since March - including restrictions on export licenses valid for critical minerals and the listing of certain American companies on China's unreliable entity lists. We expect the effective tariff rate to stay at the new current level, despite still-meaningful risks that a re-escalation of bilateral tensions could drive tariffs back up again.

Source: Oxford Economics

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