

US Economic Viewpoint

How to talk to your family about the economy over the holidays

Cold weather, heated debates

Whether you like to talk shop with your family or not, you'll probably get asked some difficult questions about the economy at a holiday gathering this year. Not to worry, we've got you covered. In this report, we list 10 questions you might get asked. For each question, we suggest both a short response – in case you were trying to avoid your interlocutor – and a more detailed one if you're actually enjoying the conversation.

1. So glad you could make it. I don't know I can afford to host everyone again next year. When will prices come back down? Is this because of the tariffs?

Short answer: Tariffs are one reason why your holiday budget won't go as far this year, but there are some deals to be had. Next year may not look much better.

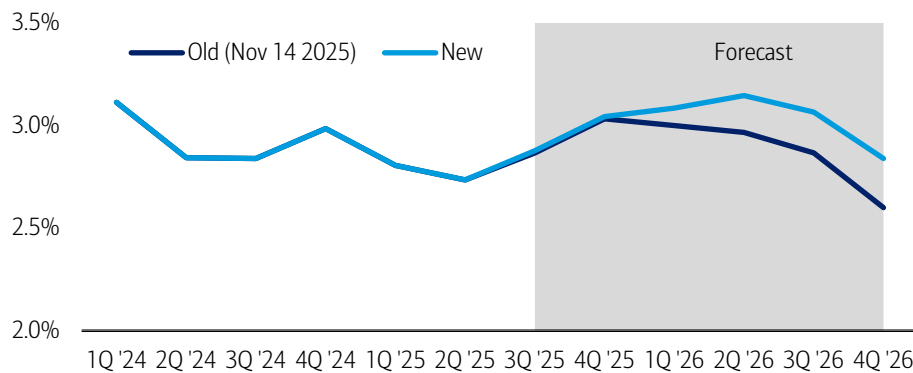
Long answer: Unfortunately, your holiday budget might not go as far as last year. Inflation is running at nearly 3%. Depending on which measure you use, that's similar to or a bit higher than where we were last year. Tariffs are one reason why inflation is still elevated. They likely explain about half a percentage point of inflation over the last year.

The good news is that inflation hasn't risen as much as many feared after the Liberation Day announcement in April. In fact, there are some deals to be had. Prices are down from last year for computers, sporting equipment, bicycles and clothing. Though we'll have to see if retailers offer similar-sized discounts to last year during the holidays. Guests from out-of-town may also save on a hotel, though not on the flight.

Those items may be where the good news ends. On balance, I'm not sure you'll be too happy when you go to pay your credit card bills at the end of the holiday season. And inflation may still give you heartburn next year (Exhibit 1). Tariffs, a strong economy and a Fed that isn't completely taking the eggnog away are a recipe for sticky-high inflation.

Exhibit 1: Our revised forecasts see stickier inflation next year

Core PCE inflation (quarterly, % y/y)



Source: Bureau of Economic Analysis, BofA Global Research

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NAR: National Association of Retailers

FOMC: Federal Open Market Committee

OBDDA: One Big Beautiful Bill Act

DOGE: Department of Government Efficiency

SNAP: Supplemental Nutrition Assistance Program

ACA: Affordable Care Act

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2. “Tell me about it. Alex has a good job but can’t afford to buy a house. Am I ever going to get my basement back?”

Short answer: Probably not any time soon. Housing affordability is likely to remain a major challenge.

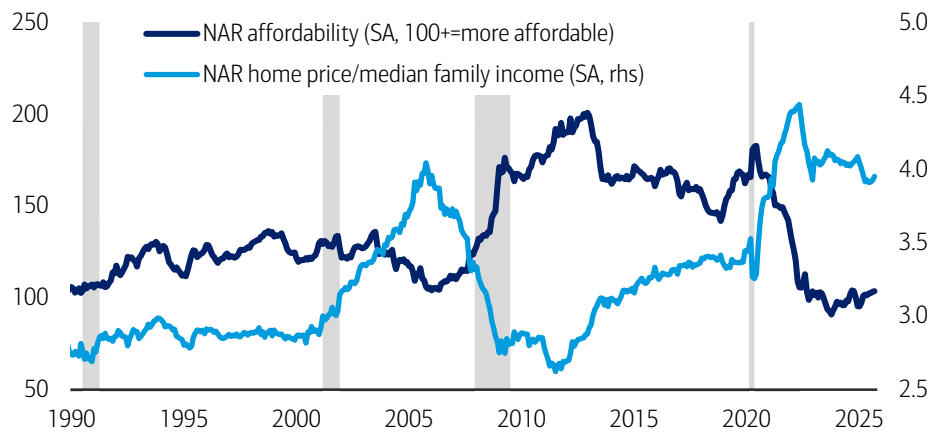
Long answer: Housing affordability remains a major problem because both mortgage rates and home prices are very elevated. 30-year fixed mortgage rates are currently around 6.4% on average. They might fall modestly next year on the back of Fed cuts. But with most homeowners locked into very low fixed-rate mortgages, it remains to be seen how responsive the housing market will be to lower rates (See report: [The housing market remains locked](#)).

The lock-in effect is also constraining the supply of existing homes. This, coupled with solid demand, has kept home prices elevated. Not to mention headwinds to construction supplies from tariffs. Despite some recent slowing, home prices remain around 16% above their pre-pandemic trend. And the ratio of home prices to median family income is higher than it was at the peak of the housing bubble in 2005. (Exhibit 2).

A recent NAR (National Association of Realtors) report notes that the median age of first-time homebuyers spiked to an all-time high of 40 years this year. It was 38 years in 2024 and 33 in 2020. Bottom line: you might not be an empty-nester any time soon!

Exhibit 2: Housing affordability has improved slightly, but remains at historically low levels

Home price to median family income ratio and affordability



Source: BofA Global Research, NAR

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3. "Okay but then why wouldn't the Fed just cut rates more? Your uncle Jay thinks that would be risky. The only risk I see is that I'll never have grandchildren."

Short answer: If the Fed cuts rates too much, the economy could over-heat. Mortgage rates depend on the 10-year Treasury yield, which might even increase in this scenario.

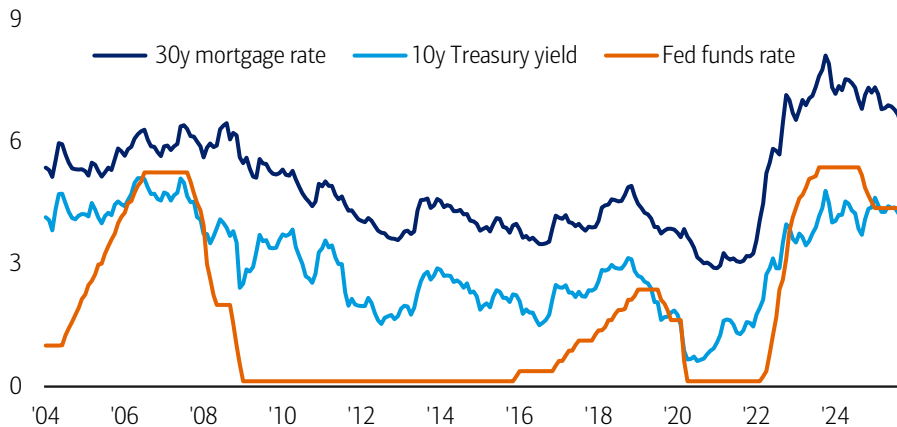
Longer answer: 30-year mortgage rates are generally viewed as the sum of the 10-year Treasury yield and the "mortgage spread", which is the difference between mortgage rates and the 10-year yield (Exhibit 3). Although the Fed has cut policy rates by 150bp since last September, the 10-year yield is actually up since the Fed started cutting. That's because the Fed only controls overnight interest rates. The 10-year yield is a function of not only near-term Fed policy rates but also considerations over the longer term (i.e., over a 10-year horizon), such as whether inflation will remain chronically elevated and the trajectory of government debt (which affects the supply of Treasuries).

If the Fed were to cut rates too fast, the 10-year Treasury yield might even increase. Markets could decide that policymakers aren't serious about getting inflation under control, and so the Fed might have to reverse course and hike down the line. Perceptions of an irresponsible Fed could even weaken the dollar because of a reduction in demand for dollar-denominated assets (which would also raise Treasury yields). So, believe it or not, Uncle Jay is making sense here!

I do have one piece of good news for you though. The mortgage spread is as low as it has been for nearly four years. As a result, the 30-year mortgage rate is down by around 50bp since the Fed started cutting rates and a whole percentage point since the start of this year.

Exhibit 3: Mortgage rates are more closely related to long-end Treasury yields than the Fed policy rate

30-year mortgage rates vs 10-year yield and Fed funds rate (%)



Source: Federal Reserve Board, Wall Street Journal, Haver Analytics

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4. “There’s going to be a new Fed Chair next year, right? Who do you think it will be? And what will they do?”

Short answer: Kevin Hassett is the front-runner for Fed Chair. He’ll probably push to cut rates a lot further, but he might not get his way.

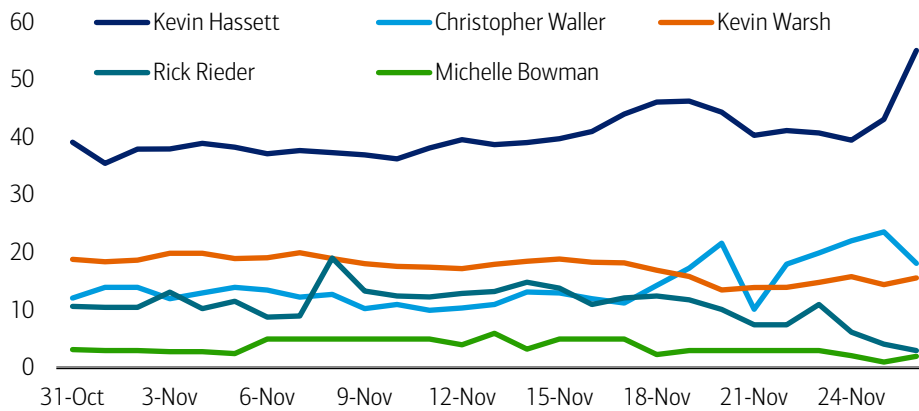
Longer answer: Fed Chair Powell’s term ends next May. Recent news reports suggest that National Economic Council Director Kevin Hassett is the front-runner to be the next Chair (Exhibit 4, see report: [Hassett has it in the bag?](#)). Hassett is a close ally of President Trump. He headed the Council of Economic Advisors in 2017-19, during which time he helped craft the 2017 tax cuts.

If Hassett becomes Fed Chair, he’s likely to push to cut rates well below 3%, as Trump has called for. The other candidates might do something similar. Whether they succeed will depend on both the state of the economy and the composition of the FOMC. If economy weakens significantly from here, then other Fed policymakers will be on board with deep rate cuts. In fact, some of those cuts would probably arrive under Powell.

But if the economy stays resilient, the next Fed Chair will struggle to make the case for deep cuts to the current members of the FOMC. The question would then become, how much turnover will there be on the committee? There are many permutations for how the composition of the FOMC could change next year, but it’s a bit of “inside baseball” so I won’t bore you with the details. The more important point is that if the Fed does cut rates more than the economy warrants, it runs the risk of causing longer-term Treasury yields to increase, as I mentioned earlier. And those yields have a bigger impact on the economy than Fed policy rates.

Exhibit 4: Hassett's odds have increased to around 55% in betting markets

Implied odds for the top Fed Chair candidates (%)



Source: Kalshi

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5. “Stop complaining Bob. At least Alex has a job. My twins graduated from college in June but they're still unemployed. What's going on?”

Short answer: We’ve been in a “low-hire, low-fire” job market for over a year. That has made life very difficult for young college grads.

Longer answer: There just aren’t as many jobs out there. In early 2022, there were two open jobs for every unemployed person. Now that number is a bit less than one. Hiring has slowed sharply this year as firms put a pause on hiring plans in the face of heightened tariff uncertainty. AI-related cost cutting and DOGE measures have also played a role. This has hit young graduates the hardest: the unemployment rate for 16-to-24 year olds is now more than 10%, which is nearly a ten-year high.

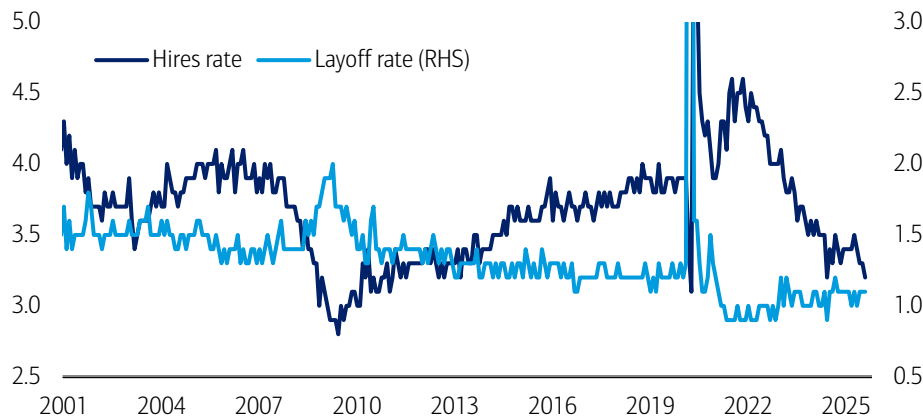
Sectors like professional and business services, which likely hire a lot of college graduates and where AI uptake has been faster, have seen many months of layoffs. But wages have been stable/rising, suggesting a shift toward higher-paying jobs, even as entry-level work gets replaced.

Hiring has weakened, but the silver lining is that layoffs have remained historically low (Exhibit 4). You’re probably thinking, what about recent layoff announcements by Amazon, UPS, Verizon, etc.? The fact is, they haven’t yet made a dent in the aggregate data (if that changes, I’ll get more worried!). In general, firms seem reluctant to do mass layoffs, likely because of i) worries about future labor shortages due to immigration restrictions (see: [Supply, supply, supply: Lower breakeven & full employment](#)), and ii) mental scars from trying to hire during the “Great Resignation” in 2022.

Going forward, business investment should benefit from favorable tax provisions in the OBBBA, the strength of the stock market and fading uncertainty about trade policy. This should help kickstart hiring and hopefully get your twins out of your hair before next Thanksgiving.

Exhibit 5: The layoff rate remains below pre-pandemic levels, but hiring has slowed much more dramatically

Hires and layoff rates (%)



Source: Bureau of Labor Statistics, Haver

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6. “But if the labor market is soft, why does my stock portfolio look so good?”

Short answer: Stocks have been boosted by AI optimism. This has led to “K-shaped” consumption, with strong higher-income spending but soft lower-income spending.

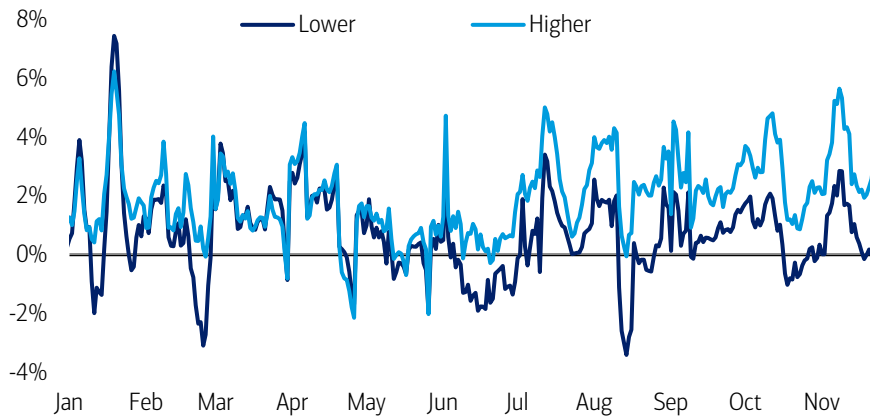
Longer answer: The stock market rally has been led by tech stocks because of optimism around AI. Other sectors such as financials have also performed well this year due to deregulation. Stocks have been able to brush off some of the weakness in the labor data for two reasons. First, the deterioration in the jobs data caused the Fed to start cutting rates again, which is viewed as good for the equity market. Second, markets might see some of the slowdown in hiring as driven by efficiency gains due to AI. That means lower costs for companies, which is again positive for stocks.

This is the third consecutive year that stocks have performed very well. The S&P 500 is up about 75% since the end of 2022. The NASDAQ is up around 120%. This has led to massive wealth gains for higher-income households. In turn, higher-income spending remained solid even as lower-income spending and the labor market started to wobble this spring. Some analysts have called this a “K-shaped” economy (Exhibit 6, see report: [A deepening conundrum](#)).

The risk in this situation is that if there is a big market shock, e.g. if the AI “bubble” bursts, consumer spending and the broader economy could take a big hit. The good news is that higher-income spending held up well after the post-Liberation Day stock market correction. So, it would probably take a larger and more sustained selloff to break the back of the extraordinarily resilient US consumer. Just like it’ll take a lot more turkey to break the back of my extraordinarily resilient appetite!

Exhibit 6: The “K-shaped” consumer

Total card spending per HH by income group, based on aggregated BAC card data (y/y % change of the 7-day moving average of spending levels)



Source: BAC internal data. See the report [BofA on USA: Weekly spending update through Nov 15](#) for methodology, limitations, and disclaimers related to BAC aggregated credit and debit card data.

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7. “Speaking of AI, what is a data center?”

Short answer: Data centers are the poster child of the AI boom, and investment in them as well as software and equipment has provided a major boost to the economy.

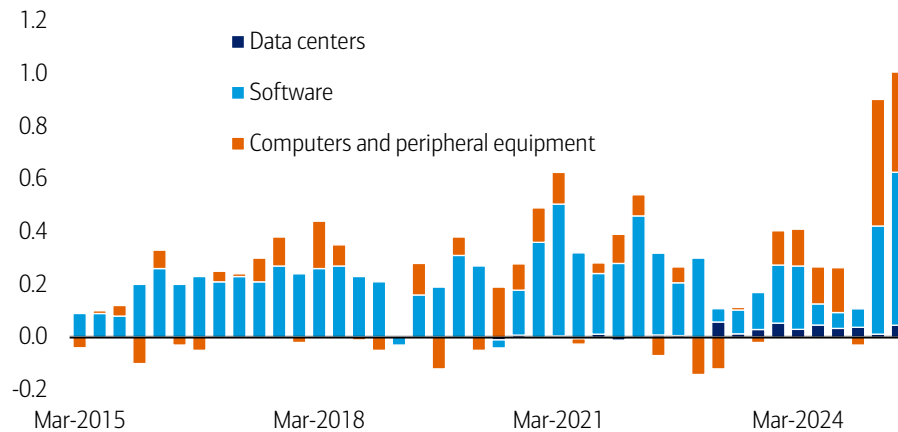
Long answer: Data centers are in many ways the heartbeat of the AI boom. They are the buildings that house all the computing infrastructure from networking equipment to super computers to the cooling systems that keep it all running 24/7. Billions of dollars have been invested in data centers because without them, supply of computing power couldn’t hold a candle to the rapidly growing demand from AI.

Data centers have been one of the lone bright spots in structures investment. Construction of other types of structures, such as office, retail and warehousing, remains depressed due to high borrowing rates and waning stimulus from the CHIPS and Inflation Reduction Acts.

Yet the bigger piece of the pie sits outside structures. Software and equipment investment have done the heavy lifting for capex growth. Hyper-scalers have ramped up spending on servers, GPUs, and other AI architecture at a pace far exceeding that of physical construction. So much so, that software and computers & peripheral equipment together contributed roughly 1pp to GDP growth in 1H 2025 (Exhibit 7).

Exhibit 7: AI and technology-related investment has been a big tailwind for growth this year

Contribution to % q/q GDP growth by category



Source: Bureau of Economic Analysis

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8. “I read that the government was shut down for six weeks. What does that even mean? Did the US default on its debt?”

Short answer: The shutdown will result in noisy economic growth over the next couple of quarters, but the overall effect is limited.

Long answer: That’s right. The shutdown was one for the record books (Exhibit 8). Shutdowns happen when Congress fails to fund government agencies in the annual budget process. This leads to a disruption in certain government functions. The shutdown left my economist friends a little unsure about what to do with themselves, since the collection and release of government data was paused. For non-economists, the shutdown may have meant a missed SNAP payment, flight cancellations, missed paychecks for government workers, and other inconveniences.

Thankfully, Congress reached a deal to reopen the government (see report: [Grand opening](#)). So, there’s a good chance we’ll be unwrapping more data than usual this holiday season. Moreover, government employees, will be back-paid for the duration of the shutdown and other government outlays (including SNAP) will be made up. As a result, though the GDP data in 4Q 25 and 1Q 26 will be noisy, the level of GDP will probably end up only a pinch lower than if there wasn’t a shutdown.

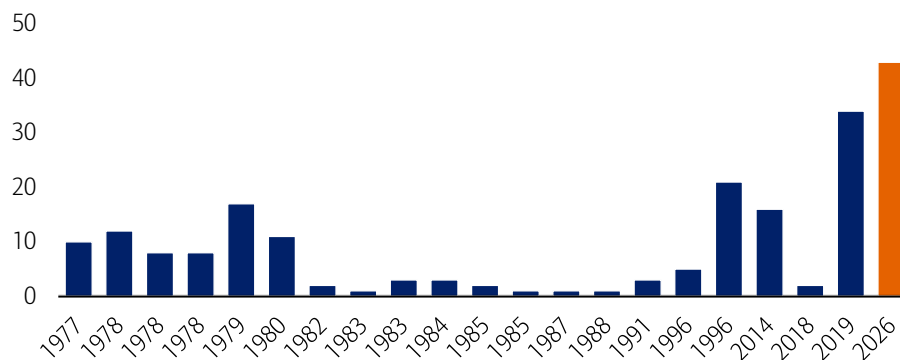
In the deal, Senate Republicans promised a vote to extend the expiring ACA subsidies. The agreement also funded a few government agencies for the full fiscal year (through September 30) and the rest through January 30. That means we might be talking about shutdowns again in January, though it’s hard to imagine there will be a shutdown during an election year.

Another reason to be thankful is that shutdowns are not the same as defaulting on our debt. Interest payments continue during shutdowns. Congress polices debt levels with the debt ceiling. They lifted that by \$5tn when they passed the OBBBA, which means we don’t have to worry about it until mid-2027. So, we can save this conversation for next year and get back to the food.

By the way, did you bring the stuffing? It’s really good!

Exhibit 8: The recent shutdown set a new record at 43 days

Government shutdowns length in days (Fiscal year)



Source: CRS

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9. “What a mess. My friend also told me that the Supreme Court might overturn the tariffs. Why would they do that? How would that affect the economy?”

Short answer: A reversal of IEEPA tariffs should be good for near-term growth. But inflation could be stickier, and debt might climb a little faster.

Long answer: 2025 may go down as the year of tariffs. The Trump Administration aggressively hiked tariffs mostly through a little-known law titled the International Emergency Economic Powers Act (IEEPA). IEEPA accounts for nearly two-thirds of today’s tariff rates (Exhibit 9). Since the law itself had never been used to enact tariffs, a few parties challenged the legality of the actions. After two lower courts ruled against the IEEPA tariffs, the Supreme Court is now determining their fate.

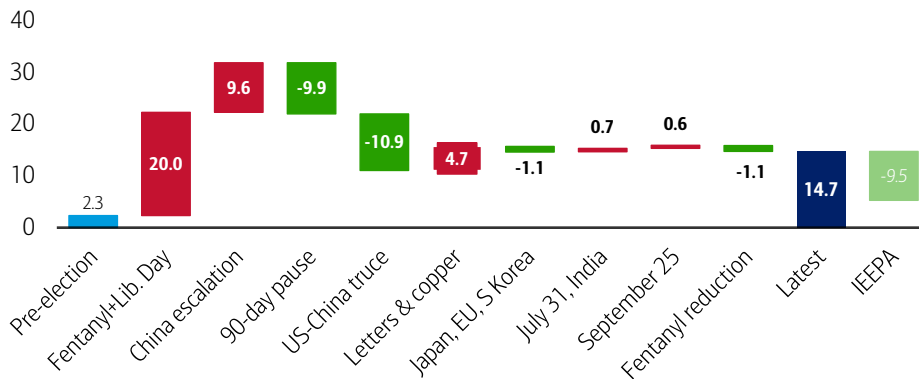
The Court might reverse these tariffs for various reasons, including: 1) the law does not explicitly allow for tariffs, 2) these tariffs are closer to taxation, which is really a power of Congress, and 3) if they allow these tariffs to persist, how could future congresses ever take blanket tariff authority away from the executive branch?

We are still awaiting a decision and will leave predictions to any lawyers in the room. That said, a reversal of the IEEPA tariffs would be a great holiday gift for many businesses, since the \$100bn+ of tariffs that have been collected to date would need to be refunded. A reversal also probably means a slight drop in overall tariff rates, even if the administration pivots to other, more tried and true tariff authorities.

Refunds and lower tariffs would be good for near-term growth as they would act as stimulus for the private sector (see report: [Remember, remember the 5th of November](#)). That said, it isn’t all rosy. Less tariff revenue could push borrowing costs up due to higher deficits, and uncertainty may spike again as the administration pivots to Plan B. Inflation might also be lower in the near term, but if growth gets another positive jolt, it might become even harder to get back to the Fed’s 2% target in the medium term.

Exhibit 9: After a period of volatility, we estimate the effective tariff rate stands at 14.7%, of which 9.5pp is due to IEEPA actions

Evolution of theoretical US effective tariff rate (%)



Source: BofA Global Research, Haver. Note: 90-day pause includes the electronics exemption. US-China truce includes UK deal. July 31, India includes Vietnam and Indonesia deals. IEEPA ruling assumes fentanyl/reciprocal tariffs are deemed invalid and trade deals are renegotiated upon.

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10. “I see you eyeing the dessert. Before I let you go, help me put this together. We have a soft labor market, a strong stock market, lots of AI capex and uncertainty about policy. How is that going to net out next year?”

Short answer: We are optimistic on US growth for next year with tailwinds from fiscal policy, easier financial conditions, steady AI investment and fading tariff uncertainty.

Longer answer: I know economists have a reputation for doom and gloom forecasts, but despite a soft labor market this year and heightened tariff uncertainty, we are optimistic on the bigger picture for next year. When the economy is growing - and is not in recession - it usually grows around 2% or more, and that’s roughly what we expect in 2026. Despite early-year worries, GDP growth in 2025 held up better than many thought. We are tracking y/y GDP growth close to 2%. That resilience is a good starting point for 2026. Looking ahead, we see five tailwinds for the economy next year that should help lift growth above 2% (see report: [US Economic Viewpoint: 2026 year-ahead outlook: Sunny side up](#)).

First, we expect OBBBA to add 0.3-0.4pp to GDP growth in FY26, owing in part to a ~\$100bn tax cut for consumers. Most of this will come as a tax-refund “windfall” due to favorable treatment of tip and overtime income and new deductions for seniors. That should boost spending in early 2026 and lead to at least a few spring shopping sprees.

Second, the lagged effect of ongoing Fed cuts will buoy activity through easier financial conditions. Third, trade policy should turn more supportive for growth regardless of whether the IEEPA tariffs are overturned, and if they are reversed, refunds would provide even more fiscal stimulus for the economy.

Fourth, we think AI-related investment will continue to be a positive driver of growth next year. I can’t make any sensational predictions on whether AI is a bubble not, but it’s at least not likely to burst anytime soon (famous last words). Last, base effects from the shutdown should mechanically boost 2026 GDP growth.

Taken together, these tailwinds should help stabilize the labor market and keep consumer spending firm. So, while growth may not boom, it should settle into a healthier, above-trend range, enough to keep the expansion going – and enough to let us wrap up our meal with some holiday cheer without any ghosts of recessions yet to come haunting dessert!

Exhibit 10: We expect 4Q/4Q growth of 2.4% in 2026 and 2.2% in 2027. Inflation should remain above 2% throughout our forecast horizon

Summary of our economic outlook

	3Q 25	4Q 25	1Q 26	2Q 26	3Q 26	4Q 26	1Q 27	2Q 27	3Q 27	4Q 27
Real GDP (% q/q saar)	2.7	1.4	2.5	2.8	2.3	2.0	2.0	2.0	2.3	2.3
Real GDP (% y/y)	1.9	1.8	2.6	2.4	2.3	2.4	2.3	2.1	2.1	2.2
Final domestic sales (% q/q saar)	2.0	1.0	2.5	2.6	2.2	1.8	1.8	1.8	2.1	2.1
Private consumption (% q/q saar)	3.2	1.8	2.1	3.0	2.5	2.0	2.0	2.0	2.5	2.4
Nonres investment (% q/q saar)	0.7	2.8	3.2	3.2	2.7	2.3	1.9	1.9	1.9	1.9
Residential investment (% q/q saar)	-6.0	-1.0	1.5	1.5	3.0	3.0	2.0	2.0	2.0	2.0
Unemployment rate (%)	4.3	4.5	4.5	4.5	4.4	4.3	4.3	4.2	4.2	4.2
Nonfarm Payrolls (avg m/m chg, 000s)	62	-5	33	42	60	65	65	65	65	65
PCE inflation (% y/y)	2.7	2.8	2.7	2.9	2.8	2.6	2.4	2.3	2.3	2.3
Core PCE inflation (% y/y)	2.9	3.0	3.1	3.1	3.1	2.8	2.6	2.5	2.5	2.4

Source: BofA Global Research

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