Nationwide®
is on your side

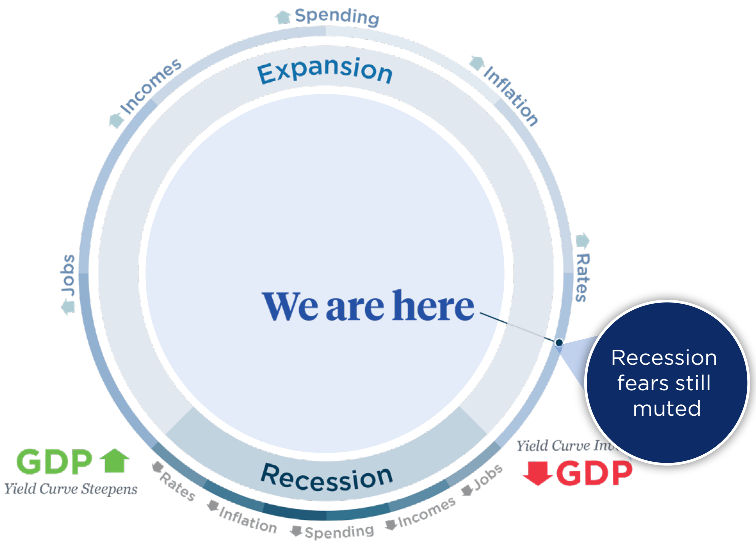
Economic & Financial Markets Monthly Review | August 2026

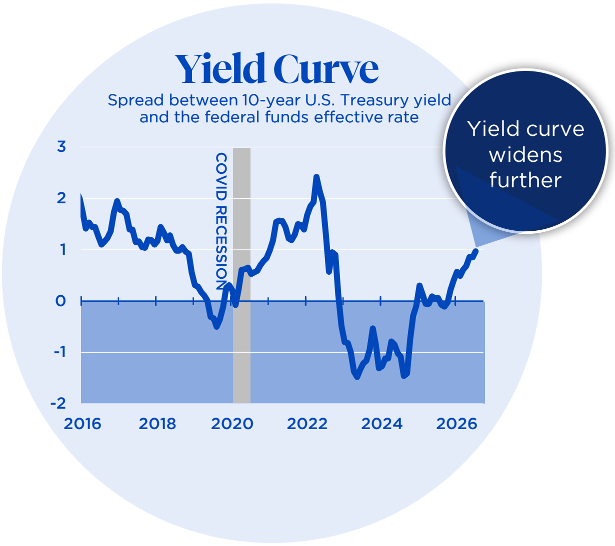
Softer shift in data reduces pressure to raise rates

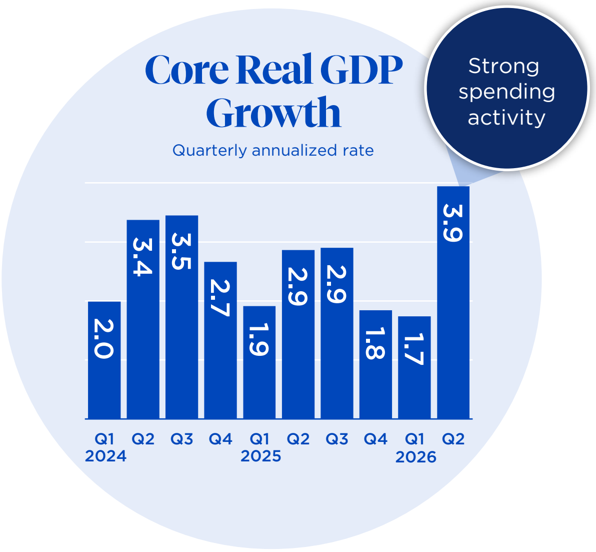
Economic Overview

Where is the economy now?

Geopolitical headwinds are lingering into the second half of 2026, but underlying economic activity has remained resilient with further upside potential for growth if energy prices ease in coming months. Fed officials appear split on whether to remain on hold or hike interest rates this year to combat inflationary pressures from the Iran conflict. While we expect energy prices and supply chains to slowly normalize later, the risk of extended inflation impacts is elevated.







Geopolitics only a minor drag on activity

Despite continued volatility and elevated energy prices from the Iran conflict, economic growth has maintained positive momentum into the third quarter. While growth would be stronger without the drag for consumers and businesses from higher energy costs, the base for the economy remains solid — fed by consumer activity and AI investment.

Treasury rates shift higher

Interest rates rose over the past month as financial markets priced in more uncertainty around Fed actions and an elevated bond term premium. The renewed spike in energy prices has added an additional risk factor for Treasury rates. The 2-10 Treasury spread, although widening this month, is tighter than earlier in 2026.

Strong underlying growth in Q2

Headline GDP growth was softer than expected in the second quarter at an annualized pace of 1.5 percent with a significant drag from net trade. But final sales to private domestic producers or core GDP growth (focused on consumer and business activity) increased by a strong 3.9 percent — indicating a robust underlying pace of activity across the economy.

What does this mean for the economic outlook?

Impacts for prices from the conflict in the Middle East could extend until year end, albeit likely fading over time. Unless hostilities escalate further, easing tensions should add to growth expectations over the second half of 2026 as supply chains normalize and prices decline.

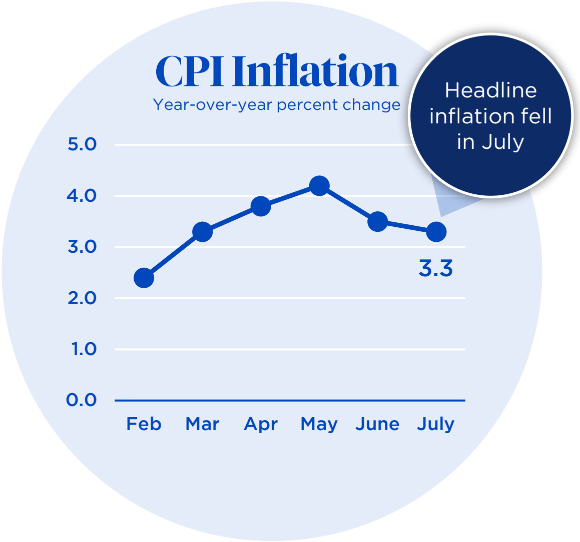
Inflation readings in coming months will determine if the Fed remains on pause or decides to raise rates at upcoming meetings. We still expect the Fed to hold the federal funds rate steady over 2026 despite financial markets pricing in a high chance of policy tightening.

The strong momentum for consumers and businesses should carry into the third quarter even with the renewed climb in energy prices. Substantial investment in AI technology and data centers should also add to growth over the second half of 2026 and into 2027.

Economic Review

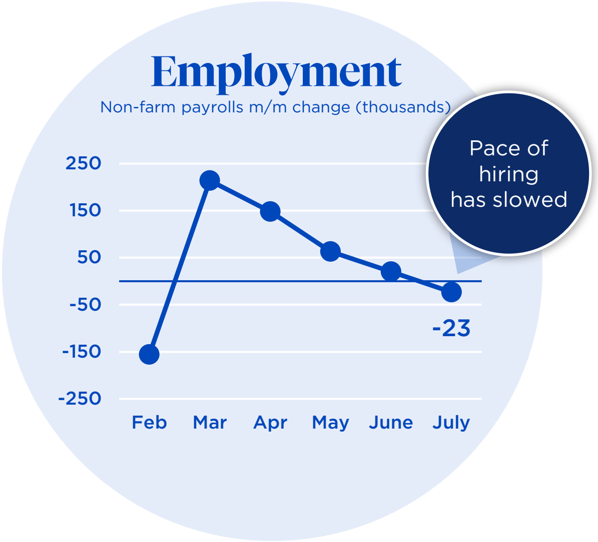
Labor market cools as inflation eases

Job losses in July and downward revisions to previous months indicate softer labor market trends than thought, while retail spending activity was weaker than expected as household savings dwindle. Consumer inflation was tame in July, giving the Fed room to hold rates steady in September, though the August inflation reports will be important. Meanwhile, a surge in small-business capex plans points to stronger investment ahead.



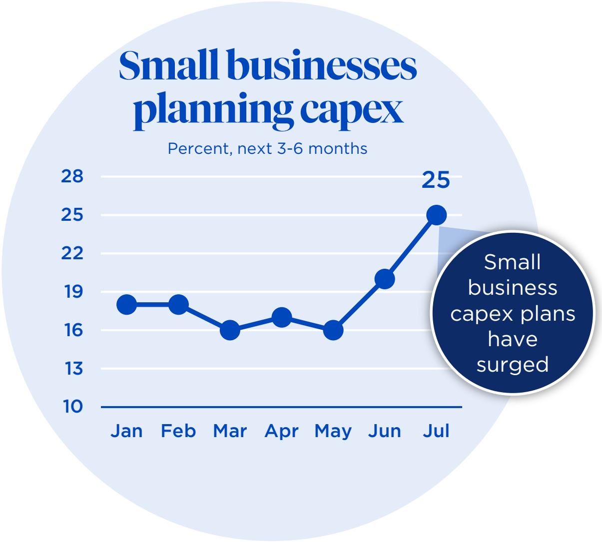
Mild inflation lowers odds of rate hike

The latest CPI report showed disinflation has resumed after a run-up in the prior months. Price pressures should continue to moderate as the energy shock and other temporary boosts fade, though progress toward the Fed's 2 percent target is likely to remain gradual.



Soft July employment report

Hiring in July was weak, with payrolls declining by 23,000 and large downward revisions to prior months. Wage growth slowed, while the unemployment rate fell to 4.1 percent due to a drop in labor force participation. Still, private sector hiring remained positive, with jobs in goods industries growing at a heathy pace.



Small business capex plans surge

The share of small business owners planning a capital expenditure in the next three to six months jumped to 25 percent in July, up from 20 percent in June and 16 percent in May. Investment plans have been weak for much of the year before rising sharply, reaching their highest level since December 2024.

What does this mean for the economic outlook?

The tame inflation report gives policymakers more breathing room to keep rates steady in September, contingent on the August inflation reports. Barring renewed upside risks, inflation should trend lower into 2027, but we do not expect the Fed to reach its inflation target until spring 2027 at the earliest.

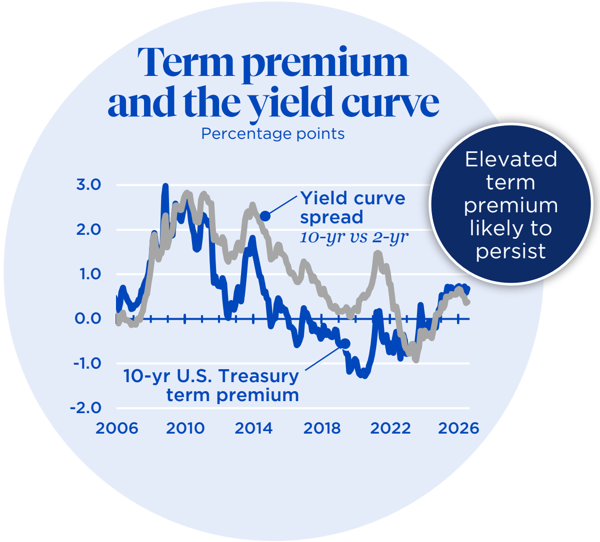
The private sector gains point to still-solid footing for the labor market and economy, but the recent downtrend in hiring in the service sector bears watching. If softer service sector hiring persists, income spending could lose support, even though the unemployment rate remains low.

The surge suggests a shift from deferred to catch-up investment, potentially due to larger tax incentives. Some spending may target automation amid labor shortages, though the survey does not establish an AI-specific motive. If realized, stronger capex would boost business investment and economic growth.

Financial Market Review

Equities rally as macro risks diminish

The stabilization in semiconductor chip stocks and still-strong earnings growth has returned some positivity to the equity market, pushing the S&P 500 index to new all-time highs. The Treasury yield curve has steepened as encouraging inflation data lead investors to price out Fed rate hike bets while long-end yields have increased. Solid economic growth and corporate earnings should keep interest rates elevated and stock prices buoyant.



Equity rally regains steam

The benchmark S&P 500 index is regaining upward momentum as the semiconductor chip stocks find their footing after falling sharply in July. Very positive second-quarter earnings reports are also bolstering equities, with many companies beating analysts' ebullient expectations.

Interest rates climb

The spread between the 2- and 10-year Treasury yields has increased. Short-end Treasury yields are trimming their gains as investors now see lower risks of Fed rate hikes. At the same time, buoyant economic growth, fiscal policy concerns ,and the deluge of corporate AI-related funding is raising long-term Treasury yields.

Term premium to remain elevated

The Fed left its policy unchanged at last month's policy meeting. The decision wasn't a surprise, but investors were unwelcoming of the Fed Chair's vague guidance at the post-meeting press conference. This will likely keep the term premium – the extra compensation investors demand for holding longer-term U.S. Treasury securities - elevated.

What does this mean for the economic outlook?

Positive economic and corporate fundamentals are overpowering downside risks from the Iran conflict, financing of the AI buildout, and elevated interest rates. These risks are unlikely to dissipate materially in the near term, yet we anticipate strong corporate earnings and a resilient economy will outshine them.

Investors are backing off on their Fed rate hike bets due to cooler inflation. We see the fundamental backdrop keeping interest rates elevated. Inflation remains high, energy prices are unlikely to fall sharply, and economic growth is expected to stay solid. If they continue rising, interest rates may pose a headwind for the equity rally.

Our baseline forecast continues to expect the federal funds rate to remain on hold for the remainder of 2026. Cooler inflation data for July support our call and investors are now moving toward our view. However, rate hikes are a risk so long as inflation stays elevated and the labor market trends in a positive direction.

Outlook

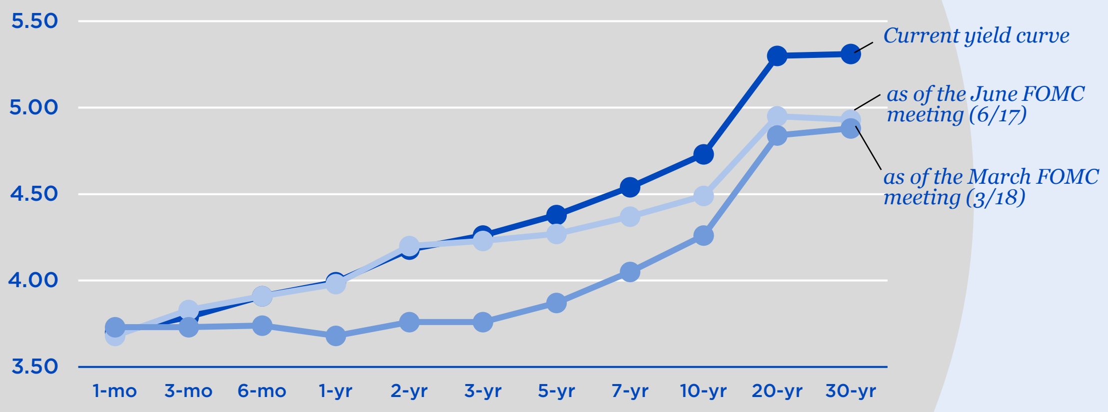
Minimal Fed guidance as Warsh drives new approach

The first two FOMC meetings under Fed Chair Kevin Warsh have been defined by reduced communication and a lack of forward guidance on future Fed actions, a stark difference in approach from past recent Fed chairs. With fewer guidance from the Fed, financial markets will need to read incoming economic data more closely to determine the forward path of monetary policy. This data-driven strategy allows Fed officials to use market pricing as an unfiltered source of information on economic conditions but also opens the possibility of a Fed surprise for markets and market volatility.

The FOMC has also taken a hawkish turn as the extended Iran conflict places upward pressure on inflation readings and ignite concerns about second round impacts. There were three hawkish dissents by Fed presidents at the July meeting, highlighting the “family fight” that Chair Warsh describes. Chair Warsh is unlikely to provide any clues on near-term policy decisions at the Jackson Hole Symposium in late August but may better describe the policy framework and broader operating philosophy under his leadership. Meanwhile the yield curve has steepened in part due to uncertainty about the path of monetary policy, and a crowding out effect from heavy AI-related debt issuance.

U.S. Treasury yield curve

Percent



Hear more in our podcasts PLAY

FIND **ECONOMIC INSIGHTS BY NATIONWIDE** WHEREVER YOU LISTEN TO PODCASTS

Forecast

Data as of August 2026

	2025 ACTUAL	2026 ESTIMATE	2027 FORECAST	2028 FORECAST	2029 FORECAST
REAL GDP [1]	2.0%	**2.1%**	**2.3%**	2.3%	2.3%
UNEMPLOYMENT RATE [3]	4.5%	4.2%	4.2%	4.2%	4.2%
INFLATION [1] (CPI)	2.8%	3.0%	2.1%	2.0%	2.0%
TOTAL HOME SALES	4.74	4.75	5.12	5.65	5.86
S&P/COTALITY HOME PRICE INDEX	1.3%	1.9%	2.7%	3.0%	3.0%
LIGHT VEHICLE SALES	16.2	16.0	16.4	16.5	16.5
FEDERAL FUNDS RATE [2]	3.50%	3.50%	3.00%	3.00%	3.00%
5-YEAR TREASURY NOTE [2]	3.73%	4.15%	3.70%	3.70%	3.70%
10-YEAR TREASURY NOTE [2]	4.18%	**4.45%**	**4.20%**	4.20%	4.20%
30-YEAR FIXED-RATE MORTGAGE [2]	6.18%	6.40%	5.90%	5.70%	5.70%
MONEY MARKET FUNDS	4.03%	3.53%	3.15%	3.03%	3.03%

Resilient economic growth to continue

After a solid first half of 2026, despite higher costs from the Iran conflict, economic activity is expected to pick up modestly through year-end. A swifter drop in energy prices would boost growth more, but even with elevated fuel costs spending by consumers and business should be resilient.

Higher long-term rates into 2027

Investors have pushed up the term premium for Treasuries given heavy AI-related debt issuance amid high government borrowing, and due to increased uncertainty about the forward path for the Fed.

[1] *Percent change Q4-to-Q4*
[2] *Year end*
[3] *Q4 average*

Contributors

Kathy Bostjancic
SVP & Chief Economist

Ben Ayers
AVP, Senior Economist

Oren Klachkin
AVP, Financial Market Economist

Vivian Chen
AVP, Financial Market Economist

Daniel Vielhaber
Economist

Brian Kirk
Communications Consultant

Sources

Page 1 |	**Where is the economy now?**	
	Business Cycle	*Nationwide Economics*
	Yield Curve	*Bloomberg; National Bureau of Economic Research*
	Core GDP growth	*Bureau of Economic Analysis*
2 |	**Economic Review**	
	Consumer Price Index	*Bureau of Labor Statistics*
	Nonfarm payroll gains	*Bureau of Labor Statistics*
	Small business capex plans	*National Federation for Independent Business*
3 |	**Financial Markets Review**	
	S&P 500	*Standard & Poor's*
	10-year Treasury yield	*Federal Reserve Board*
	Term premium and the yield curve	*FRB, FRBNY, Haver Analytics, Nationwide Economics*
4 |	**Outlook**	
	U.S. Treasury yield curve	*Bloomberg*
	Latest Forecast	*Nationwide Economics*

NFM-11356AO.3