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A shopper looks over a 2026 Accord at a Honda dealership in Highlands Ranch, Colo. DAVID ZALUBOWSKI/ AP

U.S. Economy Grew 3.4% This Summer

Consumer spending, business investment powered the fastest expansion in a year

BY KONRAD PUTZIER

The U.S. economy grew at a 3.4% annual rate in the third quarter, marking the fastest pace in a year, as business investment surged and consumers continued to spend at a healthy clip.

The latest reading of gross domestic product—the value of all goods and services produced across the economy— beat analysts' expectations for a pace of 3.1%.

The report from the Commerce Department is the last major accounting of the U.S. economy before midterm elections on Tuesday. The numbers add to evidence that, despite tariffs, an immigration crackdown and high energy prices, the U.S. economy remains on solid footing.

Higher business investment was driven by the artificial-intelligence build-out, while strong consumer spending came despite high gas prices and other affordability concerns. The 3.4% annual economic growth rate is adjusted for inflation and seasonality.

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A separate report, also from the Commerce Department, found that the Federal Reserve's preferred measure of inflation accelerated in September.

Stocks fell slightly Thursday

amid a steep selloff in Google parent Alphabet's shares. Treasury yields were also down.

The reports on Thursday reinforce the widely held belief that the Fed will need to raise rates in December as it seeks to bring prices under control. The economy is powering ahead, consumers are spending more, and at the same time inflation is well above the Fed's target. That suggests current interest rates might not be high enough to cool prices.

"From an interest rates point-of-view, it's a bad news/ bad news story—rates need to be higher because of higher inflation and higher growth," said Chris Zaccarelli, chief investment officer at Northlight Asset Management.

Satyam Panday, chief U.S. economist at S&P Global Ratings, said: "You've got more reasons to raise rates than not."

The reports landed one day after a pivotal meeting where most Fed policymakers voted to hold rates steady.

Fed Chairman Kevin Warsh said Wednesday that he didn't view current financial conditions as restrictive, pointing to strengthening growth.

At the same time, Warsh said he didn't view demand from an overheating economy as the driver of inflation, arguing that rising productivity means the economy can now grow faster without causing runaway price growth.

"Is the economy running too hot? That isn't the judgment of most of my colleagues," he said Wednesday.

Consumer spending, the economy's main engine, grew at a 3.8% pace in the third quarter, unchanged from the second quarter's sturdy clip.

People increased their spending on goods including cars and parts, furniture and household equipment and apparel, as well as services like healthcare and food services and accommodation.

Strong consumer demand is also propping up corporate profits, especially from high-end spenders getting a boost from roaring stock markets. Cruise operator Royal Caribbean Group recently reported rising profit as households continue to shell out for vacations.

While spending growth was strong for the quarter, it lost some pace last month. Inflation- adjusted consumer spending was flat in September from August after rising by 0.5% the prior month.

And many consumers continue to increase their spending more than their incomes are rising, eating into their savings. A measure of personal savings as a share of after- tax income fell to the lowest level since 2022.

Spending on imported goods surged by more than a quarter on an annualized basis, driven in part by semiconductor purchases from abroad. Overall net imports subtracted 3.3 percentage points from GDP growth.

GDP reflects the total of all spending. But since some of that spending is on imported products, rather than things made in the U.S., imports are considered a drag on GDP.

Still, accelerated AI spending is driving economic growth. S&P Global Ratings estimated that high-tech business investment in things like IT equipment, software and research and design accounted for more than a third of GDP growth over the past year, even after accounting for the fact that chip imports are a drag on GDP. That's up from less than a quarter in the first half of the year.

Massive data-center spending has been fueling economic growth all year. Goldman Sachs recently projected that artificial-intelligence investment in the U.S. will hit a staggering 1.9% of GDP. While much of that money is spent on imported chips, the boom is also creating plenty of construction jobs in the U.S. as developers race to build server farms. The rise in construction spending has helped compensate for a decline in home-building.

A measure of underlying demand that carves out more volatile government, inventory and international trade numbers also strengthened. Called final sales to private domestic purchasers, this measure rose at a 4.9% rate in the third quarter. That was the

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fastest pace since the second quarter of 2021, when the economy was bouncing back from the pandemic.

Another driver of economic growth has been massive government borrowing. The federal debt hit 100% of GDP for the fiscal year ending in September. That's the highest level since 1946, when the U.S. was heavily indebted because of the cost of fighting in World War II.

The economic picture isn't all rosy. As prices have risen, wage growth has come down.

That combination means average real hourly earnings have fallen for six straight months. Lower-income people, who tend to spend a bigger share of their income on gasoline, have been particularly hurt by rising fuel prices.

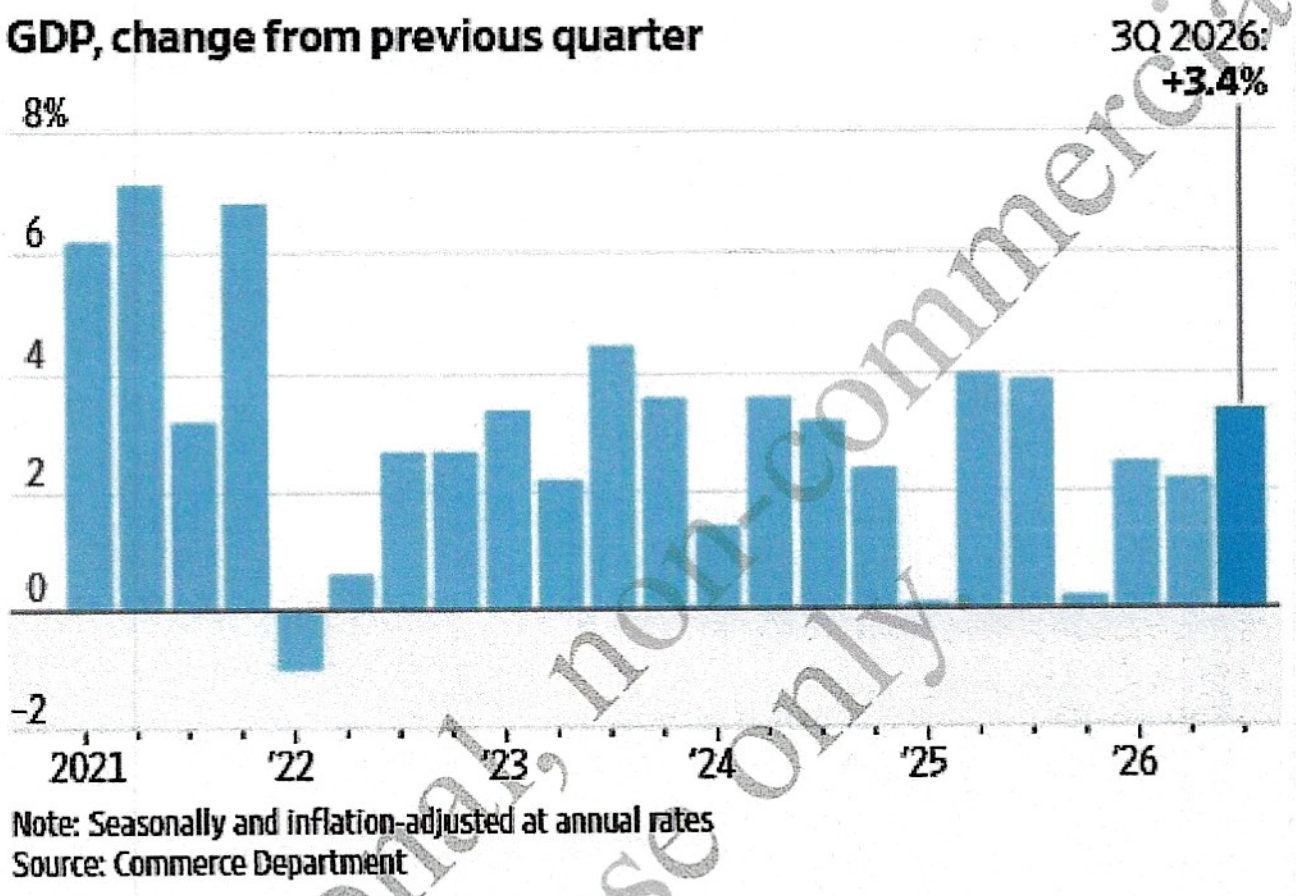
And while unemployment is low, growth in the labor market has been modest. Employ--ers added 29,000 jobs in September—far fewer than economists expected.

At the same time, high interest rates are hurting businesses tied to the housing market. Appliance maker Whirlpool said this week that it expected a loss for the year. The company said it has been dealing with higher raw-material and fuel costs.

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