Business

Rob Kaplan on Recession Odds, the Fallout of Tariffs, and the Impact AI Is Having on Business

In an exclusive interview with *D CEO*, the former head of the Dallas Fed and current Goldman Sachs vice chair talks about the macroeconomic environment and trends to watch.

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Rob Kaplan, Goldman Sachs

D Magazine

Rob Kaplan: Tariffs Could Cause Many Small Businesses to Fold Before Year's End

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After six years as the top exec at the Federal Reserve Bank of Dallas, Robert Kaplan left his leadership post in 2021 amid scrutiny over some of his stock trades. In the years since, he taught courses at Harvard and Stanford while quietly advising companies and nonprofits on strategy. Last year, the central bank's Office of Inspector General cleared Kaplan, and a few months later, he rejoined Goldman Sachs, where he was a top investment banker from 1983 to 2005.

In late 2023, several investment firms courted Kaplan for CEO roles. But he turned down each opportunity. He says he asked himself, "Where will I have the greatest impact on the world?" And "although some of these other firms are great firms, there's nothing that came close to the impact I could make at Goldman Sachs," he said.

The banking world has drastically changed since Kaplan left Goldman in 2005. The financial giants itself has changed, too, with its employee base nearly tripling to 50,000.

In his new role as partner and vice chairman, Kaplan spends about 75 percent of his time advising CEOs on asset allocation, capital raising, capital structure, and the macroeconomic environment—across the U.S., Latin America, Asia, and Europe. The rest of the time he is focused on leadership and strategy and teaches a leadership class once a week to large groups.

Kaplan recently sat down with *D CEO* to talk about the U.S. macroeconomic environment. He shared his belief that many small businesses could dissolve before the end of the year. But he thinks corporate earnings will be resilient during that same time period. Here's why.

D CEO: How have you seen asset allocation change through the first half of this year?

ROB KAPLAN: "Companies I've talked to feel their assets might be overweighted in the United States. It's all a result of the enormous tailwind the tariffs have caused. Companies who might have stopped investing in Europe or Asia are now looking at investments in those continents. The global stock market index has historically been weighted 70 percent in the U.S. But many boards are shifting and feel more comfortable in the 60-percent range.

"Nobody knows how the net of all the changes—budget bills, tariffs, regulatory reform in energy, the restructuring of immigration policies—will play out. I think the stock market and corporate earnings are going to actually turn out to be resilient. Don't just assume underperformance is going to continue. A few months ago we might've thought earnings would drop 10 percent. I don't think so. I think corporate earnings in the U.S. will be up 6 to 7 percent. But you have to be worried about small and midsized businesses."

D CEO: You recently said you think a recession is less likely. Why?

KAPLAN: "We started the year seeing the deficit get cut. We saw the introduction of DOGE. They attempted to cut the $7 trillion budget by $1 trillion. All that was a headwind for growth. In my opinion, necessary, but contractionary. We were also concerned that there would be a dramatic drop off in labor force growth, and we've seen that. But what I didn't expect to see is the 10 million undocumented workers in the country not be allowed to stay.

"We're hearing all over the country how hard it is to find labor. Labor force growth drives GDP growth.

"Through March, the odds of a recession were inching up. Our odds were at 50 percent, but now it's closer to 30 percent. The budget bill isn't actually contractionary—the expected cuts haven't materialized, not even close. (DOGE only cut the budget by about $180 billion.) In fact, tax incentives have increased. We originally thought they'd just extend the Trump tax cuts, but with these additional measures, the overall budget impact could actually be neutral or even expansionary, which makes a recession less likely.

"The other thing that typically accompanies a severe downturn is a sharp rise in unemployment. When people are employed, they may be living paycheck to paycheck, spending every dollar. But if they think they're going to lose their job—or actually do—they stop spending. That's what leads to a severe downturn. However, we believe the labor market right now is much tighter than most people realize. Business might not be hiring, but they're also not as quick to fire.

"If you're a big business, you can manage through this. But if you're a small business—and I talk to many regularly—they often don't have the leverage to navigate all this uncertainty, especially around tariffs. I think we'll see more small businesses quietly decide to close down between now and the end of the year. We're already seeing signs of that; many are making plans right now.

"That's why we're having these conversations and seeing the trend in our surveys. Some owners are saying, 'Given my age, I can't afford to take the risk. I can't position this inventory or absorb the margin pressure if I can't sell it. It might be safer to just wind the business down.'

"These businesses are below $10 million in revenue, certainly below $5 million. Its restaurants, importers, local newspapers, even car dealerships."

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>
> *Rob Kaplan*

D CEO: So, small businesses could be having trouble securing—or expect difficulties if they attempt to secure it?

KAPLAN: "This is where small community banks play a critical role. Most small business lending in this country—whether we like it or not—comes from those banks. But credit risk for small businesses has increased. I talk to a lot of bankers and sit on several bank boards, and the message is clear:

lenders are being more cautious. So yes, depending on the nature of the business, access to credit is becoming a real concern—and that's a serious challenge."

D CEO: How did we get to this point? Many business owners were optimistic heading into this administration.

KAPLAN: "Let's walk through what's shifting—what's going away and what's coming in.

"From early 2022 through mid-2023, government-directed spending had a big effect on cities across the U.S. I saw it firsthand in every community I worked with. You had projects like lithium battery plants and stadium expansions, all fueled by funding from the Inflation Reduction Act and similar initiatives. That spending had a major impact on the labor market.

"But now, that spigot is shutting off. Much of that spending is either ending or being frozen. And because those projects often had strings attached—like mandatory union labor at $35 an hour—it created tension. For example, I've heard from restaurant owners who say they're losing workers to these higher-paying federally backed projects. They were paying $18 an hour, which already felt high, but they couldn't compete with $35. So while that funding helped the broader economy, it made things harder for small businesses trying to retain labor. Now, that pressure is starting to ease.

"That said, there are new things coming in—like accelerated depreciation. If you invest in the U.S., you may be able to write it off faster. Some companies were already investing and didn't do it for the tax benefit, but now it's a nice added incentive.

"Other potential changes could include tax relief on overtime or tips for low- and moderate-income workers. If I'm a restaurant owner, that's useful—I might not need to raise wages because workers would keep more of what they earn. We could even consider restructuring compensation or encouraging tipping in new ways, since the tax treatment could benefit employees.

"So, for some small businesses, these upcoming incentives could be helpful. But the wildcard is tariffs. A lot of small businesses—especially in Texas, which has massive import-export activity, particularly with Mexico—are waiting to see how the tariff situation plays out. Once that settles, I think many business owners will feel more optimistic. They're looking ahead and saying, 'If this stabilizes, maybe things will become more pro-business. Maybe access to credit will improve.'

"Right now, though, we're in the fog. This is the thick of it. I expect that by the end of summer, we'll have more clarity: tariff rates will be set, and the tax bill—whatever it ends up being—will likely be passed. We may not love it, but the business world will adjust. We always do.

"In the meantime, I'm constantly having conversations with business owners who ask, 'What should I do?' My advice is often: tell me about your financial situation. How leveraged are you? Can you wait this out? Can you kick the can down the road for three or four months?

"Big businesses can do that. They're already doing it. Small businesses are trying—but it's much harder for them. The recent de-escalation with China was actually enormously helpful for this group. Why? Because 40 percent of U.S. imports are intermediate goods from China. That shift made a big difference. We also have major agricultural communities in parts of the state,

people often overlook.

D CEO: So, of all these disruptions, which is most consequential?

KAPLAN: "Honestly, it's AI. I've never seen a period in my career like this. Right now, you're either small and distinctive enough to grow, or you're very large and can afford the significant investment in AI and other technologies. And those investments are expensive—they hit your margins. Everyone else is stuck in the middle.

"That 'middle' used to be a stable place to be in business. Not anymore. Even multibillion-dollar companies are saying, 'We're competing with Amazon, Costco, Walmart—and we're not sure which AI use cases will work and which won't.' Everyone is spending on AI, but there's still a lot of uncertainty about where the return will come.

"So what's happening? Companies are realizing they need to get bigger to survive. We're seeing a surge in merger discussions because the perceived risk of disruption is so high. Many companies that once thought of themselves as large now realize—they're not as big as they need to be.

"So yes, tariffs and other pressures matter, but AI remains the most disruptive force in the business landscape today."

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