LPL Financial

Economic Navigator

The Buildout Continues, But the Risks Are Rising

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Executive Summary

- After immense construction spending on data centers, business investment rose to 15% of the economy, although consumer spending is still over 67% of the economy and is the main bellwether. Nonresidential investment was at its peak in the early 1980s.
- While AI-related capital spending can move the margins of economic growth, the outlook still depends overwhelmingly on the health of the American consumer. Because the outlook for the labor market is stable, we expect consumer spending may drive the economy in 2027.
- Much of the AI buildout is from imported electronics, especially from Taiwan and upending historical trade dynamics. Because of the expanded trade deficit, net exports subtracted 3.3 percentage points from Q3 economic growth, and this may likely continue in the new year.
- The buildout comes with a cost. For example, Meta's recent record-high credit-default-swap spread signals that investors are demanding more compensation for the company's rapidly growing AI-related commitments and uncertainty over the eventual payoff.

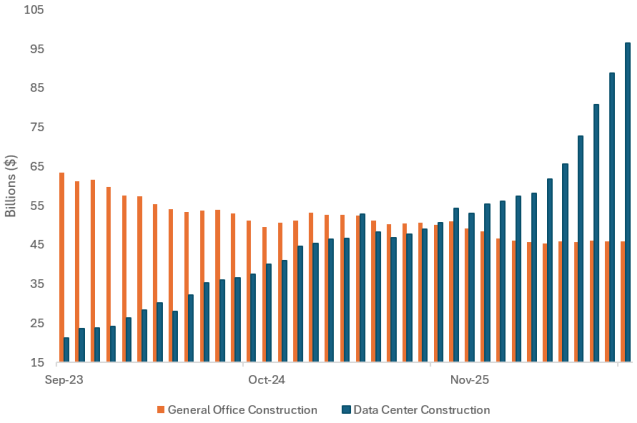
Why the Navigator?

The macroeconomic context is a key component of the investment process. Every asset class — whether credit, equities, currencies, commodities, real estate, or infrastructure — responds to the forces shaping the global economy. Inflation trends, interest rate cycles, fiscal and monetary policy shifts, and economic growth trajectories all influence market behavior and risk-adjusted returns. Ignoring these dynamics means missing the bigger picture.

So, what will the drivers of growth be for the coming year and what risks are associated with the outsized presence of the AI buildout and a Federal Reserve without a clear reaction function?

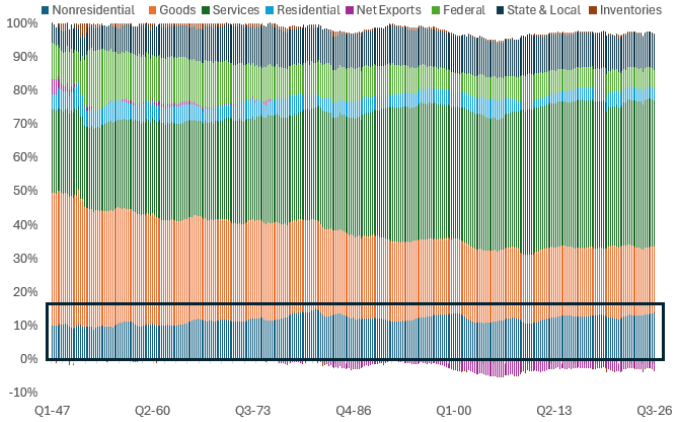
In this edition of the *Economic Navigator*, we explain how the AI buildout affects international trade and why investors are demanding more compensation for taking on risk.

Data Center Construction Goes Parabolic...



Source: LPL Research, Census Bureau, 11/04/26

Bringing Nonresident Investment up to 15% of GDP



Source: LPL Research, Bureau of Economic Analysis, 11/04/26

Past performance is no guarantee of future results. Economic forecasts may not develop as predicted.

For all the attention being paid to the AI investment boom, the U.S. economy still runs primarily on the consumer. As the accompanying chart shows, services dominate household spending, and once spending on goods is included, consumption accounts for more than 67% of the economy. Government represents a considerably smaller piece of the pie. State and local government accounts for just over 11% of gross domestic product (GDP), while the federal government represents 6.2%, hovering at an all-time low. Reviewing this economic composition is an important reminder that while AI-related capital spending can move the margins of economic growth, the outlook still depends overwhelmingly on the health of American households.

There is also good reason to think business investment can claim a larger share of the economy without becoming a source of concern. At roughly 15% of GDP today, business investment is elevated but not historically unusual, having accounted for a slightly larger share of the economy in the early 1980s. The current investment cycle also has plenty of runway as companies build data centers, expand power-generation capacity, and upgrade equipment and technology to support AI adoption. If that spending ultimately raises productivity, a larger investment share could be sustainable rather than excessive. In that sense, the shift toward more capital spending may represent less of an AI bubble and more of a gradual rebalancing of the economy toward investment that expands its productive capacity.

But a significant portion of the buildout is from imported products.

Real Q3 Growth Was 3.4% from Strong Business Investment Spending

Over half of the economic growth in the third quarter was from nonresidential business spending, which includes investment in information processing, industrial equipment, and intellectual property. But where does data center spending come into play?

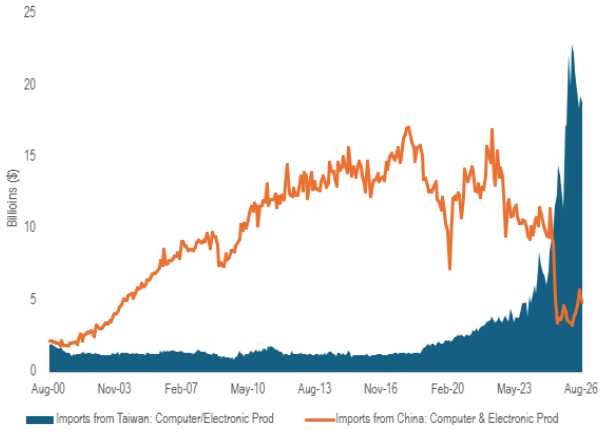
The AI buildout is becoming an increasingly important tailwind for the U.S. economy, particularly through the surge in data center investment. Federal Reserve[1] estimates suggest that data center spending on structures and equipment, after accounting for imported components, contributed roughly 0.2 percentage points to U.S. GDP

[1] The Fed - Estimating Aggregate Data Center Investment with Project-level Data (especially note p. 17)

growth in 2025 and could contribute around 0.4 percentage points in 2026. That is a meaningful boost from one segment of business investment.

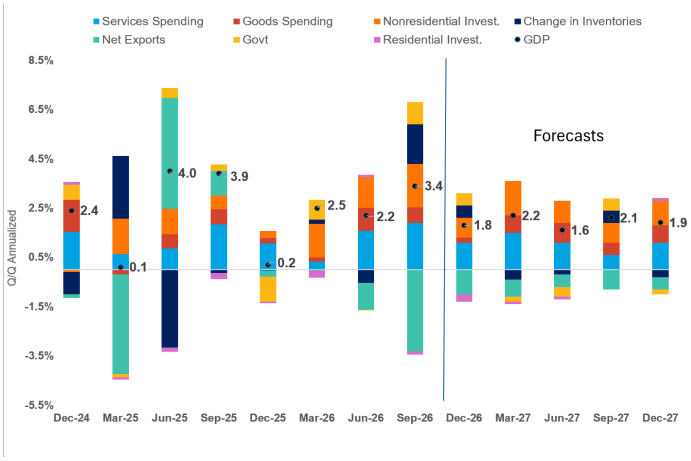
There are important spillovers as well, most notably the wealth effect from strong market performance providing wealth to investors. Rising equity prices among leading AI-related companies can support household wealth and spending, while construction activity and demand for electrical equipment are creating jobs in parts of manufacturing and construction.

AI Inputs Are Coming from Taiwan...



Source: LPL Research, Census Bureau, 11/04/26

And Subtracted 3.3 Percentage Points from Q3 GDP



Source: LPL Research, Bureau of Economic Analysis, 11/04/26

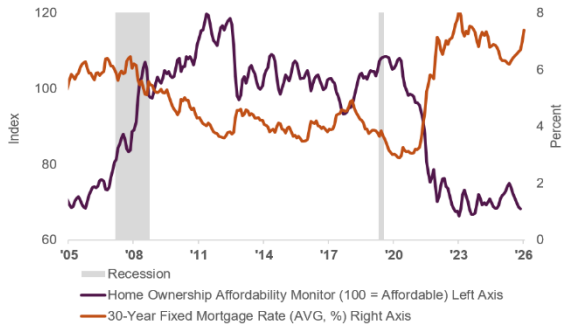
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At the same time, the benefits are not evenly distributed. Data centers require relatively few workers once they are operational, and heavy capital spending on AI infrastructure could compete with other investment for financing. Longer term, the bigger economic question is whether the AI buildout translates into a sustained improvement in productivity. History suggests that transformative technologies can take time to show up in the productivity data, much as they did during the IT revolution of the 1990s. For now, evidence of widespread AI-driven job displacement remains limited, though younger and entry-level workers could prove more exposed as adoption broadens. The bottom line is that AI is already supporting growth through capital spending, but the much larger prize would be a durable increase in productivity that allows the economy to grow faster without generating additional inflation.

The AI Buildout Is Widening the Trade Deficit, Subtracting 3.3 Percentage Points from Growth

The AI buildout is providing a meaningful boost to business investment, but not every dollar of that spending translates into domestic growth. A large share of data center capital spending, roughly two-thirds by some estimates, goes toward imported semiconductors, specialized servers, and other computer hardware rather than U.S.-produced construction materials and equipment. That helps explain why the AI boom is showing up on both sides of the GDP ledger: investment is rising rapidly, but so are imports. Since imports are subtracted when calculating GDP, the surge in purchases of foreign-made chips and computing equipment offsets part of the boost from domestic data center construction. So, the AI investment boom is clearly supporting economic activity, but the widening trade deficit means the headline increase in spending overstates how much of that demand ultimately flows through to U.S. GDP.

Home Affordability Is Near All-Time Lows...



Source: LPL Research, National Assoc of Realtors, 11/04/26

And Will Keep Rates Higher for Longer

Inflation Dashboard (Y/Y %)	Feb-26	Mar-26	Apr-26	May-26	Jun-26	Jul-26	Aug-26	Sep-26	Oct-26
Import Prices	0.99%	2.26%	4.52%	6.88%	6.75%	6.02%	6.74%	8.10%	
Producer Prices	3.35%	4.28%	5.69%	5.89%	5.59%	4.90%	5.58%	6.35%	
Services Prices Index	63.00	70.70	70.70	71.30	67.70	70.30	72.60	74.00	
Manufacturing Price Index	70.50	78.30	84.60	82.10	73.00	71.10	71.10	77.90	75.20
Global Supply Chain Pressure Index	0.49	0.63	1.78	1.81	1.21	0.93	1.20	1.28	
Gasoline Prices: U.S. Average	2.93	3.70	4.13	4.50	4.05	3.97	4.08	4.36	4.30
Consumer Prices (CPI)	2.41%	3.26%	3.81%	4.25%	3.53%	3.36%	3.40%	3.74%	
Consumer Prices (CPI) Ex Housing	2.15%	3.43%	4.05%	4.61%	3.58%	3.38%	3.53%	3.99%	
Rent Prices (CPI)	2.68%	2.56%	2.79%	2.92%	2.84%	2.86%	2.75%	2.78%	
PCE Deflator	2.80%	3.37%	3.57%	3.82%	3.45%	3.37%	3.44%	3.65%	
PCE Deflator: Core Services Ex Housing	3.31%	3.41%	3.33%	3.59%	3.55%	3.44%	3.49%	3.60%	

Source: LPL Research, AAA, Bureau of Economic Analysis, Bureau of Labor Statistics, NY Fed, 11/04/26

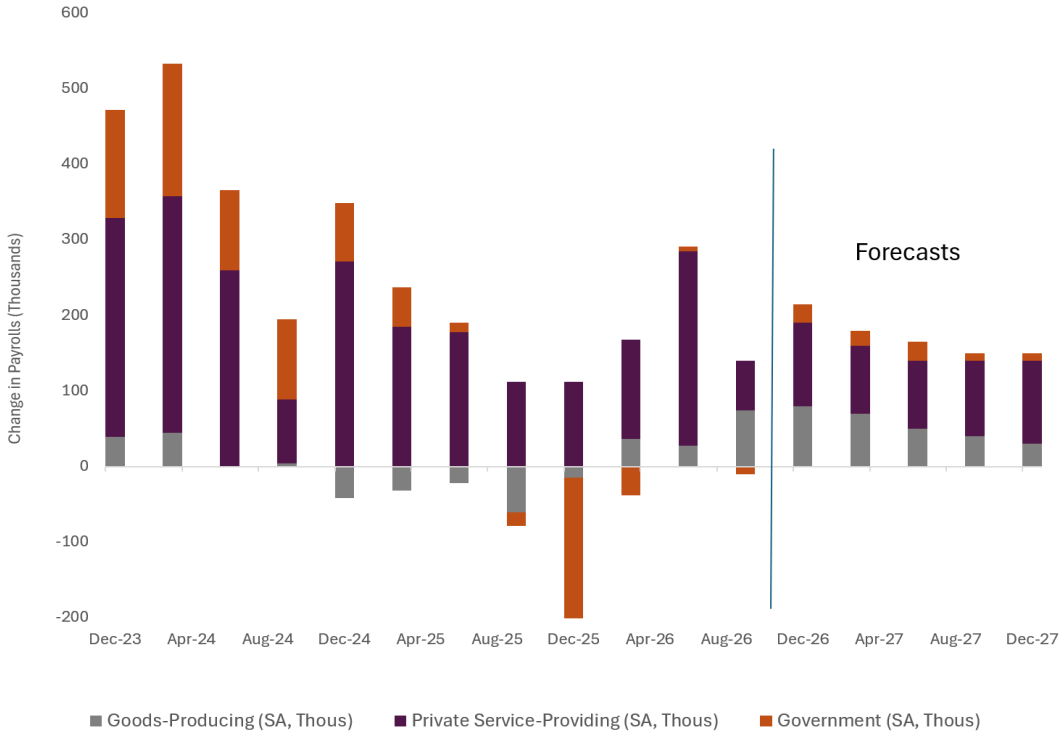
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Core PCE Inflation Will Not Fall Under 3% Until Next Year

Investors entered the fourth quarter with high hopes that inflation would finally resume its descent, but those expectations are running into a more stubborn reality. Global price pressures remain, the rapid buildout of AI infrastructure is competing for semiconductors, computers, and other electronics, and higher-income households continue to spend at a solid clip. Together, those forces could keep goods and services inflation firmer than anticipated. We now expect core inflation to remain above 3% through year-end, pushing our forecast for a move below that threshold into the first quarter of next year.

Housing is likely to remain another persistent source of pressure on household budgets. Builders simply aren't adding homes fast enough to meaningfully ease the supply shortage, while existing homeowners have little incentive to sell when many are carrying mortgage rates well below those available today. That lock-in effect constrains inventory, even as high borrowing costs reduce affordability for prospective buyers. The result is an unusual standoff: elevated mortgage rates are weighing on demand but doing relatively little to unlock supply, suggesting the affordability problem will take years, rather than months, to unwind. Despite the disappointment in the near term, core annual inflation will likely dip to 2.5% in April 2027 and should decelerate further to 2.3% by December 2027.

Payroll Growth Will Likely Keep Pace for Households



Sources: LPL Research, Bureau of Labor Statistics, 11/04/26
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The labor market is showing signs of stabilizing beneath the surface. The ISM manufacturing employment index has remained above 50 for four consecutive months, signaling that factories are expanding payrolls despite lingering trade tensions with Canada and other major U.S. trading partners. But conditions remain uneven across industries. Business leaders in entertainment are focused on controlling costs, while companies in other sectors appear more comfortable maintaining current staffing levels. Taken together, the signals point to a labor market that is converging to a slower run rate. We expect job growth to remain steady enough to keep the unemployment rate in a relatively narrow 4.2–4.4% range over the next few quarters, barring an unexpected economic shock.

Where Are the Risks?

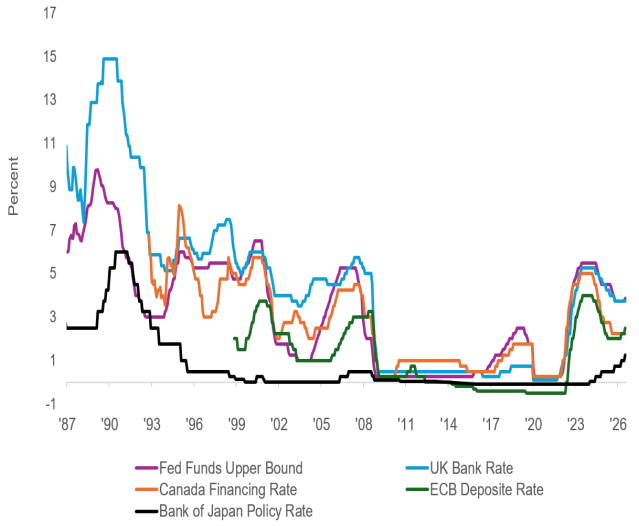
The AI spending boom is beginning to leave a more visible mark on credit markets. For example, Meta's five-year credit-default-swap spread climbed to a record as investors digested plans for higher capital spending, roughly $825 billion in future leases and contractual commitments, and a quarter of negative free cash flow. The move reflects growing concern about how much capital will be required to finance the AI buildout and how long it will take for those investments to generate sufficient returns.

More broadly, the AI arms race is increasingly becoming a financing race. As hyperscalers pour hundreds of billions of dollars into data centers, chips, and computing infrastructure, a growing pipeline of debt issuance could keep corporate credit spreads elevated even if Treasury yields decline. At the margin, higher financing costs could slow investment by cash-rich technology giants, but they also could become a bigger constraint further down the AI supply chain, where balance sheets are weaker and access to capital matters more. Over time, tighter financial

conditions could help separate projects capable of generating durable returns from those dependent on cheap financing and expectations of ever-rising AI demand.

Appendix: Supporting Macro Charts

U.S. Policy Rate Highest Among G7



Source: LPL Research, BOC, BOE, BOJ, ECB, Federal Reserve Board, 11/04/26

Global Purchasing Managers's Composite Index

	Oct-26	Sep-26	Aug-26	Jul-26	Jun-26	May-26	Apr-26	Mar-26
Global	54.3	53.5	52.7	52.0	51.9	51.8	51.0	53.3
Developed Mkts	55.4	54.1	53.3	51.2	50.6	51.1	50.5	52.2
Emerging Mkts	52.4	52.4	51.2	53.0	53.6	52.7	51.4	55.1
U.S.	57.6	58.4	56.0	54.5	51.9	51.5	51.7	50.3
Eurozone	51.7	53.1	52.0	52.0	50.0	48.5	48.8	50.7
Germany	53.4	53.8	51.8	51.3	49.5	48.8	48.4	51.9
France	46.6	51.1	48.5	49.4	47.2	44.9	47.6	48.8
Italy	50.8	51.0	53.6	52.5	50.8	50.4	50.5	49.2
Spain	56.2	56.8	55.8	56.5	53.3	50.2	48.7	52.4
U.K.	52.9	52.0	52.5	52.2	49.3	49.7	52.6	50.3
Russia	50.8	50.6	49.6	48.9	49.2	49.1	48.8	50.8
Japan	52.3	52.3	53.5	52.7	52.8	51.1	52.2	53.0
China	52.0	52.4	52.1	50.8	53.6	54.0	53.1	51.5
India	56.2	55.9	54.3	54.3	57.1	59.3	58.2	57.0
Brazil	47.4	49.1	48.8	50.7	49.5	52.4	49.9	51.3

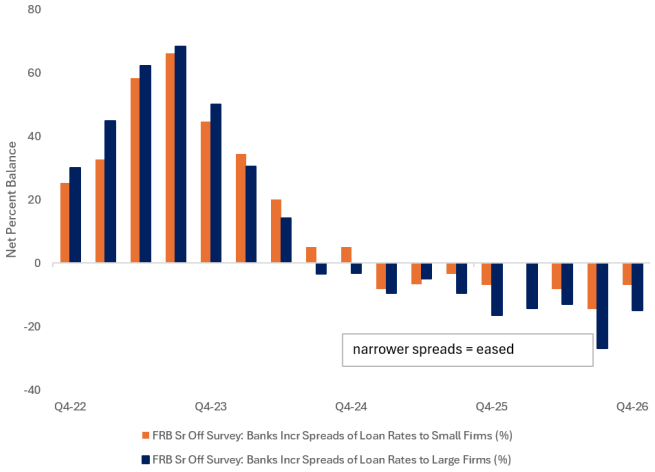
Source: LPL Research, S&P Global, 11/04/26

Firms Demand Less Loans, Banks Re-tighten...



Source: LPL Research, Federal Reserve Board, 11/04/26

While Banks Narrow Spreads Over Cost of Funds



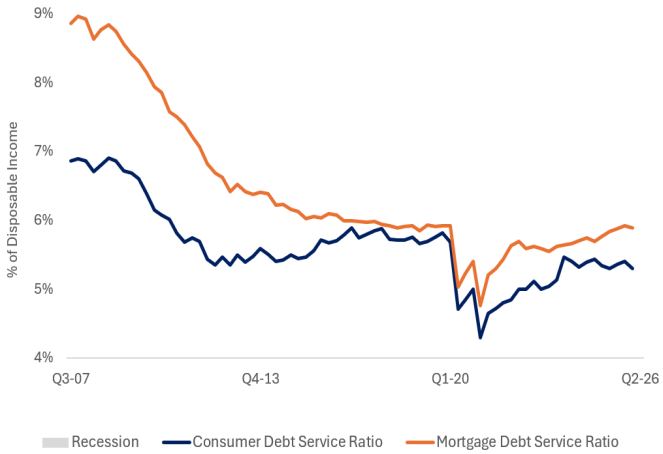
Source: LPL Research, Federal Reserve Board, 11/04/26

Housing is Stuck



Source: LPL Research, Bureau of Economic Analysis, 11/04/26

Debt Servicing Cost is Historically Low



Source: LPL Research, Federal Reserve 11/04/26

Forecasts Imply 2026 May Be a Pivotal Year

	2025				2026						
Growth	**Q1**	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**	**2024**	**2025**	**2026**
Nominal GDP (Y/Y %)	4.6	4.6	5.4	5.4	5.7	6.3	5.9	6.5	5.3	5.0	6.3
Real GDP (Yr/Yr %)	2.0	2.1	2.3	2.0	2.6	2.2	2.1	2.2	2.8	2.1	2.2
Real GDP (Q/Q Annualized)	-0.7	3.8	4.4	0.5	2.5	2.2	3.4	1.8			
Consumer Spending	0.6	2.5	3.5	1.9	0.71	3.77	3.77	1.7	2.9	2.6	1.9
Government Spending	−1.0	-0.1	2.2	-5.6	4.73	-0.09	5.28	2.5	3.8	1.1	1.3
Private Investment	23.3	-13.8	0	2.3	7.2	4.6	19.4	4.1	3.0	1.9	3.8
Exports	0.2	−1.8	9.6	-3.3	13.90	5.04	-5.74	2.1	3.6	1.6	4.3
Imports	38	−29.3	-4.4	-1.0	11.51	12.58	19.68	6.9	5.8	2.7	3.5
Real Final Sales to Domestic Purchasers (Q/Q Ann.)	1.4	2.4	2.8	0.6	2.3	3.8	5.0	2.1	3.1	2.4	2.5
Business Sector											
Nonfarm Productivity (Q/Q Annualized)	-0.9	4.2	5.2	1.6	0.82	1.42	1.8	1.6	2.9	2.2	2.4
Corporate Profits After Taxes (Yr/Yr %)	7.5	4.8	10.8	10.2	9.79	18.16	5.5	6.1	3.9	8.4	8.1
Industrial Production (Yr/Yr %)	0.7	0.5	1.7	1.5	0.79	1.55	1.74	2.5	-0.6	1.1	1.2
Consumer											
Real disposable income (Yr/Yr %)	2.0	1.8	1.8	1.0	1.71	0.98	1.26	1.7	2.9	1.7	1.5
Retail Sales (Yr/Yr %)	4.5	4.3	4.4	3.0	3.1	5.6	5.5	5.5	2.6	4.0	5.1
Retail Sales Ex-Autos (Yr/Yr %)	4.3	3.9	4.2	3.7	3.6	6.2	6.2	4.5	2.8	4.0	5.8
Consumer Confidence	99.8	93.1	97.4	94.2	90.7	92.2	87.7	93.0	104.5	96.1	90.9
Light Vehicle Sales (Mil. Units, SAAR)	16.4	16.2	16.5	15.7	15.5	16.5	16.2	16.1	15.9	16.2	16.1
Jobs & Housing											
Unemployment rate (%)	4.1	4.2	4.3	4.5	4.3	4.3	4.1	4.3	4.0	4.3	4.3
Nonfarm Payroll (Change in Thousands)	61	101	70	-116	218	242	152	210	1459	29	206
Housing Starts (Mil. Units)	1.40	1.35	1.35	1.32	1.42	1.35	1.29	1.31	1.37	1.36	1.3
Existing Home Sales (Annualized, Millions)	4.08	4.01	4.04	4.16	4.05	4.12	3.99	3.80	4.06	4.07	3.99
Inflation, Annual											
Consumer Price Index (CPI)	2.7	2.5	2.9	2.7	2.7	3.8	3.5	3.7	3.0	2.7	3.2
Core CPI	3.1	2.8	3.1	2.7	2.5	2.7	2.5	2.5	3.3	2.9	2.8
PCE Inflation	2.6	2.4	2.7	2.8	3.0	3.6	3.5	3.6	2.6	2.6	3.4
Core PCE Inflation	2.8	2.7	2.9	2.9	3.0	3.1	3.1	3.0	2.9	2.8	2.9
Brent Crude Spot Price (Average, $)	75.81	68.01	68.97	63.63	80.21	103.28	103.28	91.00	79.86	68.19	94.44
Rates											
Fed Funds (%, Upper Bound, Period End)	4.50	4.50	4.25	3.75	3.75	3.75	3.75	4.25	4.50	4.25	3.88
Mortgage Rates (30-year Fixed, Period End)	6.79	6.77	6.39	6.27	6.56	6.53	6.53	7.15	6.49	6.60	6.69

Source: LPL Research, Federal Reserve Bank of Philadelphia, Bloomberg 11/04/26
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All index data from FactSet.

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