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Equity Strategy Insights

Sticking With Technology Despite Post-Election and NVDA Headwinds

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Executive Summary

- Expectations for AI investment beyond 2027 may be too high, but spending is still poised to exceed $1 trillion next year, supporting economic growth and technology sector profits.
- Technology earnings growth remains exceptionally strong, while the sector's recent correction has pushed valuations to unusually attractive levels relative to the broader market.
- Financing costs, regulatory pressures, weak hyperscaler free cash flow, and deteriorating technical trends create near-term risks, but we believe the sector's long-term fundamentals continue to support a positive outlook.
- In our latest Equity Strategy Insights, we share our latest thoughts on the technology sector following the midterm elections and Jensen Huang's unexpected departure from NVIDIA (NVDA).

AI Capital Investment Cycle May Peak Earlier Than Previously Expected, But It's Still Massive

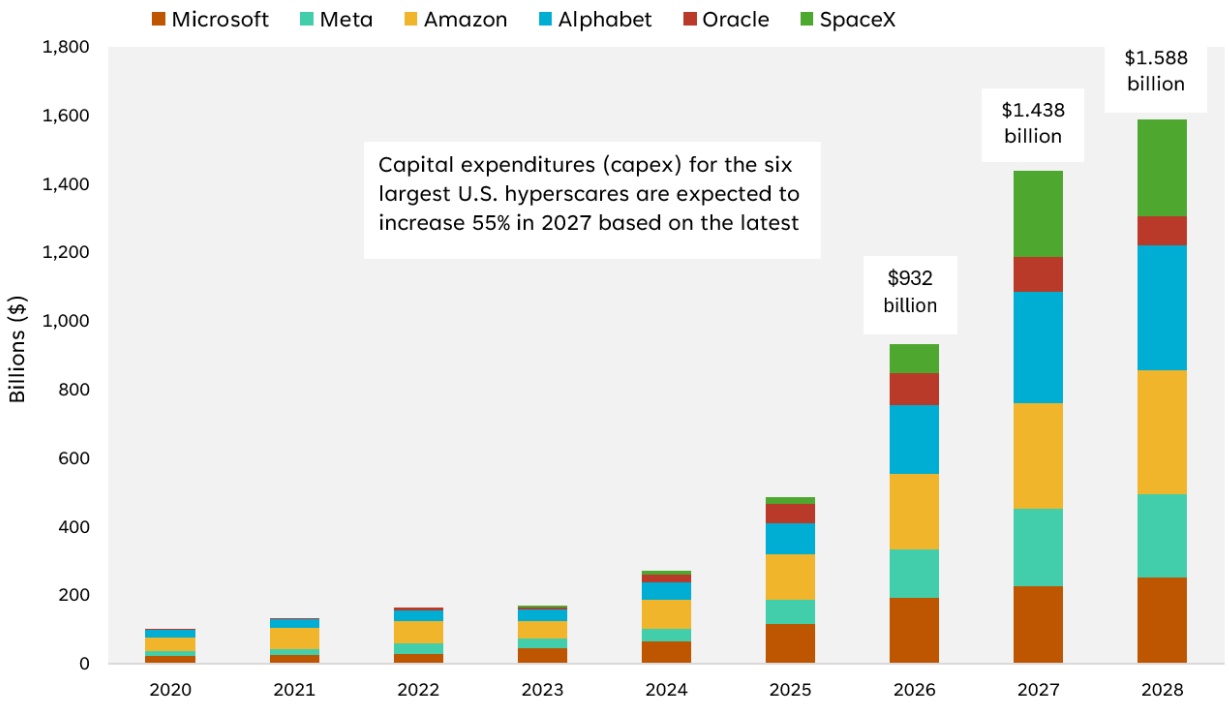
Jensen Huang's departure from NVIDIA (NVDA) this week has sparked a correction in the technology sector that has reached 17%, as measured by the S&P 500 Information Technology sector; as of November 17, 2026. Semiconductors have been the biggest losers, with the Philadelphia SOX Semiconductor Index down 34% from its peak set back in June (and down 27% from its more recent early-October peak).

The decline is not just because of the significant drag on the broad indexes from the 36% drop in NVDA shares. Jensen's departure has several potential implications for the AI infrastructure spending outlook. First, under his leadership, NVDA provided significant financing for the company's customers and data center construction. Interim CFO Colette Kress prefers a more conservative approach. We might have seen fewer deals without Jensen anyway given he has been the primary dealmaker. He has also been an effective cheerleader for AI, something that will be missing, or at least significantly diminished.

Political headwinds are also expected to strengthen in 2027. Democratic majorities in both chambers of Congress in 2027 will almost certainly slow the pace of data center construction, though probably not until 2028. Data center initiatives on local ballots were overwhelmingly rejected on Election Day. Getting necessary approvals will likely become more expensive as builders have to offer more incentives to local communities or choose less attractive sites. Rising financing costs hurt project feasibility. And more scrutiny on selling chips to Asian customers may constrain some of the growth longer term.

Bottom line, current consensus expectations for capital investment in 2028 — shown in the "Hyperscaler Capital Expenditures Expected to Surge Past $1 Trillion in 2027" chart — and beyond, may be pulled back some. Importantly, these numbers are still massive and can drive a lot of economic growth and technology sector profits.

Hyperscaler Capital Expenditures Expected to Surge Past $1 Trillion in 2027



Source: LPL Research, Bloomberg, 11/17/26
Disclosures: Past performance is no guarantee of future results. Estimates may not materialize as predicted and are subject to change.

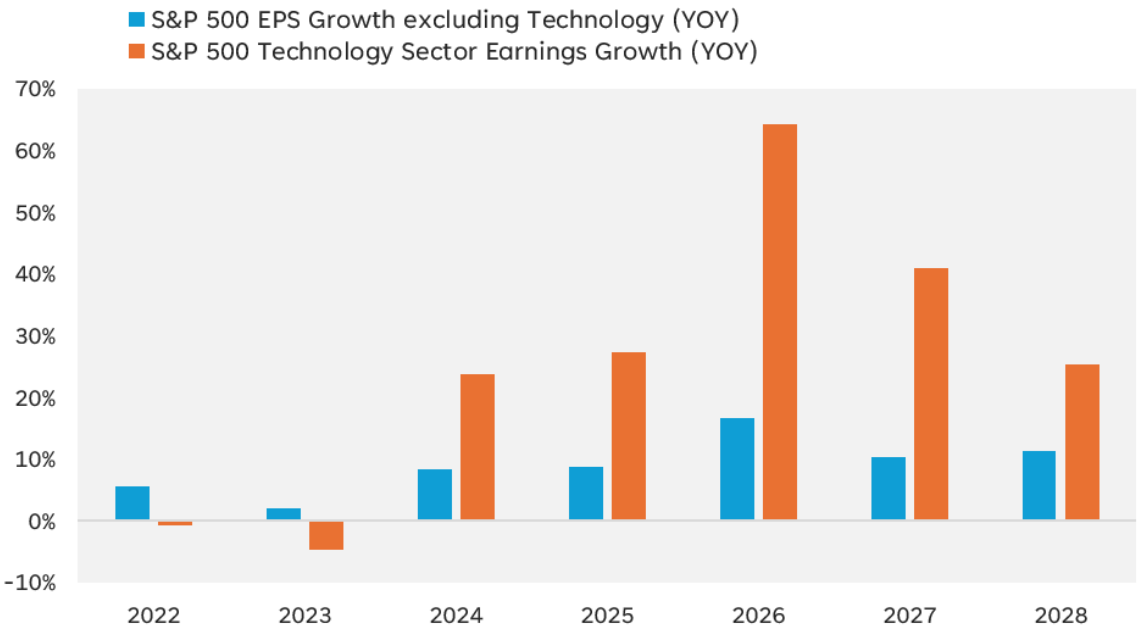
Earnings Growth Outlook Remains Extraordinary

This massive spending is good news for the stock market because it drives earnings for some of the biggest companies in the various indexes. The massive capital investment to build computing power is also good news because it's going to keep the U.S. economy out of recession in 2027 and probably 2028 as well.

The magnitude of the earnings effect, indicated by the "AI Boom Has Driven Strong Earnings Growth for the Technology Sector" chart, is striking. Sector earnings are expected to grow 64% in 2026, compared with 17% for the rest of the S&P 500. In 2027, growth in technology earnings is expected to quadruple that of the rest of the index, 41% to 10%. "Non-tech" earnings growth is respectable and above long-term averages, but it pales in comparison to the earnings from the technology sector.

The demand will have to be there to deliver against these expectations, of course. Beyond that, there are several potential stumbling blocks such as financing availability and costs, regulatory pressures, depressed hyperscaler free cash flow (more on that below), tight supplies of components, a possible slowdown in AI adoption by end users, and increased competition at lower prices from open-source Chinese models, among others. But based on strong demand for compute enjoyed by the hyperscalers selling cloud services, the chances seem good that the technology sector can meet current earnings expectations for 2027 (after blowing away 2026 estimates). Further out is a tougher call, but growing sector earnings by 25% in 2028 may be too high of a bar to clear.

AI Boom Has Driven Strong Earnings Growth for the Technology Sector



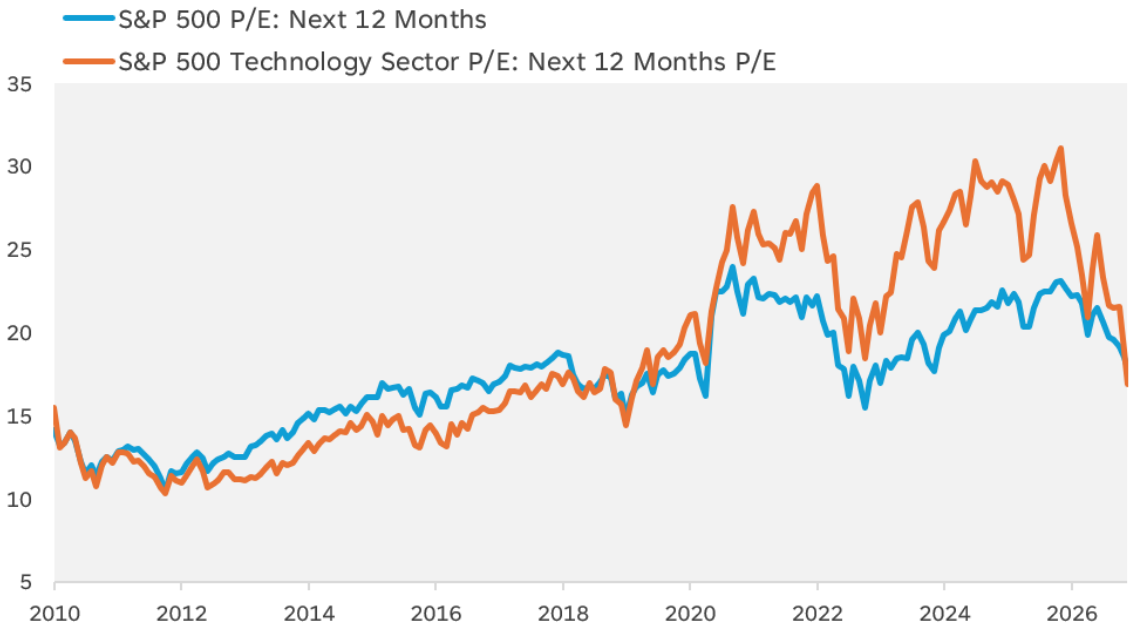
Source: LPL Research, Bloomberg 11/17/26
Disclosures: All indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results. Estimates may not materialize as predicted and are subject to change.

Strong Earnings Growth Outlook Comes at a Reasonable Price

Strong earnings growth is just one piece of the puzzle for investors. The price investors must pay for that attractive growth profile also matters. In this case we believe the market is currently offering a very attractive valuation for the sector, as indicated in the "Technology Valuations Are About As Low As They Get Relative To The Market" chart. In fact, the sector is trading at a price-to-earnings ratio (P/E) below that of the S&P 500 (16.9 vs. 17.8), which hasn't happened since 2019 — long before ChatGPT which came in 2022. If it wasn't for the strong growth, this wouldn't be so compelling. Not only is the technology sector delivering the strongest growth, but it has also posted more than double the operating margin of the rest of the S&P 500 every year since 2016. Those premium technology margins are expected to expand in 2027 before pulling back in 2028, while remaining more than double the rest of the S&P 500.

It's a rare opportunity to get such strong growth at a reasonable price, which underpins our positive view of the technology sector. However, because of the massive cost of the AI buildout, more technology companies have become capital intensive and have raised more debt. Markets assign lower valuations to debt-financed, capital-intensive businesses, particularly those with little or no free cash flow.

Technology Valuations Have Fallen Below The S&P 500



Source: LPL Research, FactSet, 11/17/26
NTM P/E is next 12 months price-to-earnings ratio.
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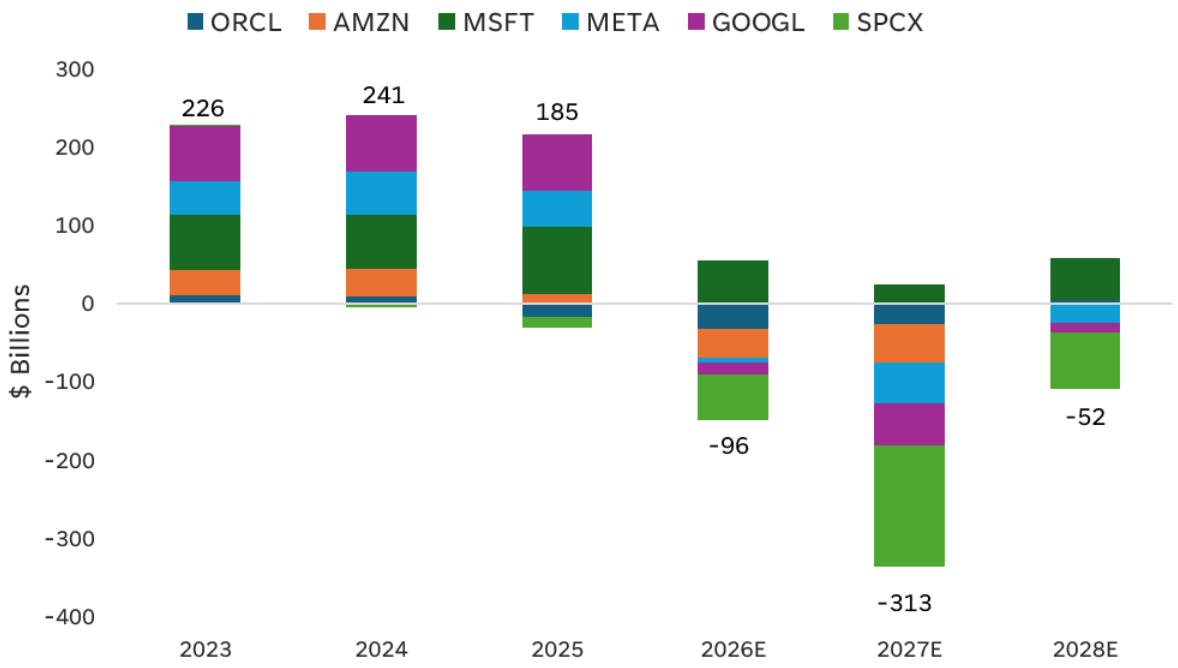
Skeptics Point to Cash Flow

The finance textbooks will tell you that the value of a stock is equal to the present value of its future cash flow, not its future earnings. Therein lies the challenge for the hyperscalers — though keep in mind Microsoft (MSFT) is the only hyperscaler classified as technology by S&P (the others are classified as communication services or consumer discretionary). The big AI companies look attractively valued on earnings but expensive on cash flow, as we wrote about in our Midyear Outlook 2026: Policy, Buildouts, and Bottlenecks on page 15.

As shown in the "Challenged Free Cash Flow Outlook for Hyperscalers in 2027" chart, the six companies listed are expected to generate negative free cash flow in 2026 and 2027 before returning to free cash flow positive in 2028. The best free cash flow generator of this group, MSFT, is the one that's classified as technology. NVDA is generating plenty of free cash flow based on the insatiable demand for AI chips right now (and is not a hyperscaler), while Apple (also not a hyperscaler) has chosen the capital-light approach to enabling AI on smartphones. This means the free cash flow outlook for the technology sector is better than consumer discretionary and communication services, where the other three hyperscalers (AMZN, GOOG/L, and META) are classified. In fact, in the second quarter of 2026, the most recent available data, the technology sector generated $166 billion in free cash flow. The next highest sector was healthcare at $79.8 billion.

Bottom line, cash flow matters. These companies must have the funds to deploy for building compute. Both debt and equity financing have become more expensive as interest rates have risen alongside concerns about the credit worthiness of the smaller cloud computing providers (called neoclouds). (We discussed AI debt in our latest Rate and Credit View from LPL Chief Fixed Income Strategist Lawrence Gillum.) If there is enough cash and working capital to fund the growth of the business, then the earnings should come through and be fully valued by the market. If not, the market will assign a lower valuation to account for the high cost of funding and elevated risk of earnings shortfalls.

Challenged Free Cash Flow Outlook for Hyperscalers in 2027



Source: LPL Research, Bloomberg, 11/17/26
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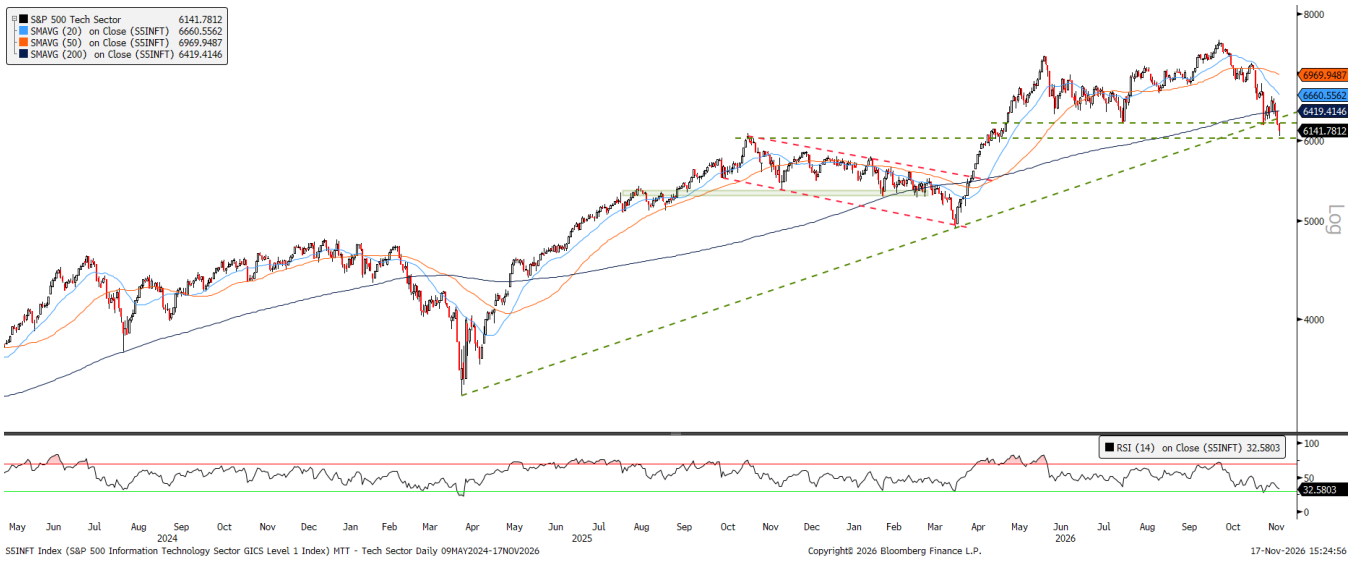
Some Worrisome Technical Analysis Developments

The technology sector has entered correction territory (10% or greater decline) over the past month as the AI trade faced increased scrutiny around data center construction and potential excessive spending. The NVIDIA scandal added to uncertainty around the AI spending cycle and dragged the broad market down due to its large weighting in the index.

From a technical analysis perspective, the sector has broken below several key support levels near the July lows, its prevailing uptrend, and its 200-day moving average. The breakdown raises the risk of further weakness, with the October 2025 highs representing the next key downside support level to watch. Momentum also remains bearish, with the 14-day Relative Strength Index (RSI) falling to roughly 33, near the 30 level that marks oversold conditions.

Bottom line, the technical backdrop has deteriorated following the breakdown of the sector's longer-term uptrend. While increasingly oversold conditions could set the stage for a short-term bounce, recovering the broken support zone and 200-day moving average will be important for rebuilding technical momentum. Getting through NVDA's earnings results and the Anthropic (ANT) IPO may help an oversold technology sector regain its footing.

Technology Sector Starting to Break Down Through Key Support Levels



Source: LPL Research, Bloomberg, 11/17/26
Disclosures: All indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results.

Conclusion

The AI capital investment cycle may peak sooner than previously expected, but that does not mean the AI boom is ending. We continue to expect AI spending to exceed $1 trillion in 2027, providing meaningful support for economic growth and corporate profits. Technology earnings growth remains exceptional, margins are strong, and valuations have become increasingly attractive following the sector's correction. AI still holds tremendous promise as a productivity enhancer.

At the same time, investors should recognize that the path forward has become more complicated. Higher financing costs, regulatory scrutiny, weaker hyperscaler free cash flow, a leadership vacuum at NVIDIA, and deteriorating technical trends may limit upside and increase volatility.

The key question is whether companies can generate enough cash flow from AI investments to justify continued spending and lofty earnings expectations. We believe the answer remains yes for 2027, although estimates for 2028 and beyond may prove too optimistic. Given the sector's favorable long-term fundamentals and reasonable valuation, we maintain our positive technology view, while acknowledging that near-term volatility may persist until technical conditions stabilize and visibility into the next phase of AI spending improves. Our Strategic and Tactical Asset Allocation Committee (STAAC) maintains its recommended modest overweight to the technology sector.

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Because of their narrow focus, sector investing will be subject to greater volatility than investing more broadly across many sectors and companies.

The Standard & Poor's 500 Index (S&P500) is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The PE ratio (price-to-earnings ratio) is a measure of the price paid for a share relative to the annual net income or profit earned by the firm per share. It is a financial ratio used for valuation: a higher PE ratio means that investors are paying more for each unit of net income, so the stock is more expensive compared to one with lower PE ratio.

Earnings per share (EPS) is the portion of a company's profit allocated to each outstanding share of common stock. EPS serves as an indicator of a company's profitability. Earnings per share is generally considered to be the single most important variable in determining a share's price. It is also a major component used to calculate the price-to-earnings valuation ratio.

All index data from FactSet.

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