Vital Briefing

Morningstar analysts expect U.S. slowdown despite AI boom

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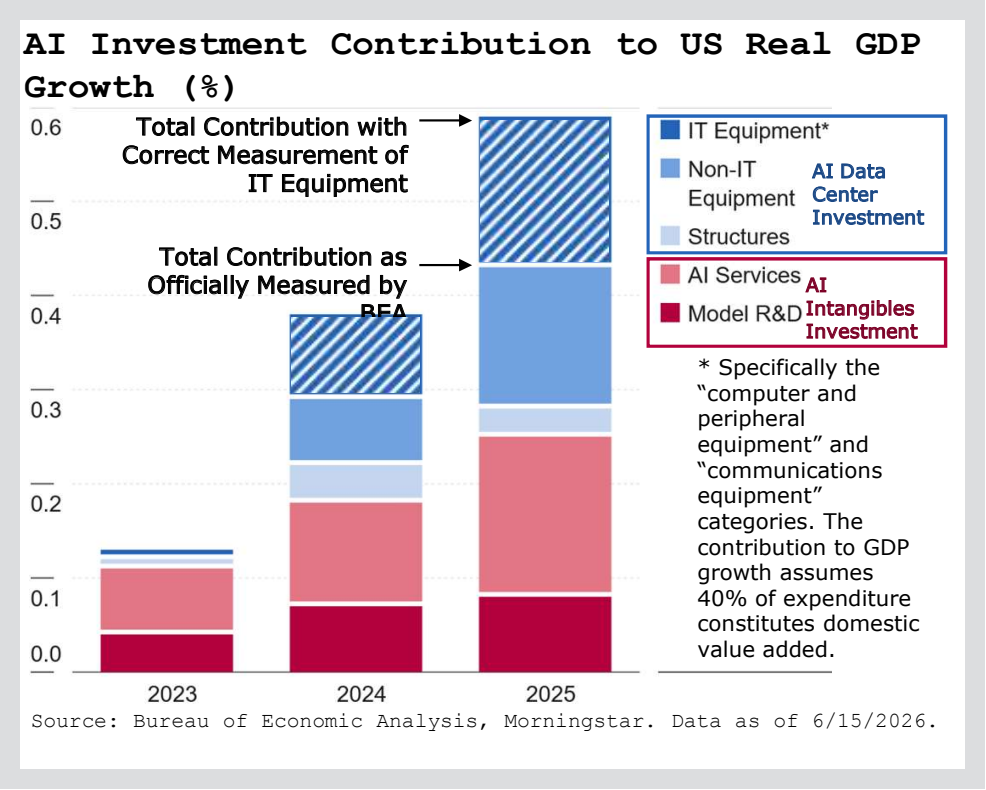
AI is boosting the U.S. economy but tailwinds may slow U.S. GDP somewhat over the next couple of years, analysts said at the 2026 Morningstar Investment Conference (MICUS). Longer term, growth depends on AI productivity increases materializing and on geopolitical conflicts deescalating.

Morningstar analysts in the "Taking the U.S. Economy's Pulse" panel discussion included Preston Caldwell, senior U.S. economist; Hong Cheng, head of fixed income and currency research, and Dominic Pappalardo, chief multi-asset strategist.

Overall economic outlook

Economic data shows that AI-related investment has been lifting the economy. Caldwell estimated that AI contributed 40 basis points to real GDP growth in 2025.

Fueled by AI, Caldwell expects real GDP growth to tick up slightly for the year, from 2.1 to 2.2 percent. But after that, he sees it slow to 1.7 percent in 2027 and 1.9 in 2028, before returning to 2.7 percent growth in 2029.



Fighting tailwinds, the U.S. economy needs AI to deliver real productivity increases for continued growth.

The expected GDP decline is due to several tailwinds, including:

- Stimulus payments drying up;
- Slower population growth, in part due to immigration outflows;
- High interest rates;
- Tariff-related price increases;
- An oil shock due to conflict in the Middle East.

Caldwell noted that households have been spending more income on basic necessities, which is weighing on consumer demand.

On the flip side, he estimated that inflation will fade from 3.4 percent in 2026 to 2.1 percent in 2028.

Ultimately the Fed will need to push interest rates lower, said Caldwell. He foresees flat rates through 2026, then a steady decline to 3 percent in 2028. On June 17, the Fed maintained the target range for the federal funds rate at 3-1/2 to 3-3/4 percent.

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AI investment boom

AI-related investment in the high-tech sector has seen significant growth over the past several years. Real private fixed investment in IT equipment, data centers, and software averaged about 3 percent to 4 percent growth last year.

Data centers are drawing major investments from AI services companies, which typically have high revenues and cash to spend.

"Data center owners are getting paid," said Caldwell.

AI buildout is also fueling record borrowing by hyperscalers. Bonds are selling well and companies have shown they are able to repay.

While AI companies are typically not yet profitable, "we can imagine a path to AI profitability," said Caldwell. This depends on consumers finding enduring value in AI technology and on tech borrowing not continuing to grow astronomically. If AI growth slows, it could cause problems for borrowing.

High tech has been the only source of investment growth this year, as investment has contracted in all other sectors. Starting in 2024, private fixed investment in non-high-tech sectors flattened or turned negative, including residential, commercial real estate, manufacturing and other businesses.

AI impact on economy and workers

What does the AI boom mean for the broader economy? That depends if AI delivers on productivity promises in the longer term, said Caldwell. He is watching for a "ChatGPT moment" for non-text inputs like visual data.

> *Even if AI replaces some human work, Caldwell doesn't see a "doomsday scenario" for workers.*

Regarding AI's impact on workers, Caldwell said he has not yet seen a huge effect on hiring. He is watching software engineering jobs as a leading indicator because software coding is a prime use case for LLMs. If those jobs decline, it could mean that AI is displacing workers.

But even if AI replaces some human work, Caldwell doesn't see a "doomsday scenario" for workers. This is because prices will decline as automation accelerates.

"Automation is a fact of labor history, but it hasn't been a disaster thus far," he said.

"We're all unemployed farmers," he added, pointing to a chart showing agricultural employment falling from 80 percent in 1800 to near zero today. Other employment sectors have taken agriculture's place, most notably services, which grew from less than 20 percent in 1800 to more than 80 percent today.

Geopolitical conflict

On another major economic story—fallout from the U.S.-Iran conflict—Cheng examined how the impact may wind down following the signing of a memorandum of understanding on June 17.

Overall, the energy price shock is expected to gently fade, with WTI oil declining from $80 a barrel in 2026 to a little over $60 in 2029. In turn, the personal consumption expenditures (PCE) index is expected to decrease by about half a percent. In May, the PCE index decreased 3.4 percent from one year ago.

However, economic impact depends heavily on continued de-escalation. Renewed conflict or the reclosure of the Strait of Hormuz would cause oil prices to spike again and may also have adverse implications for fixed-income returns.

Takeaways

AI and geopolitics are projected to have an outsized effect on the U.S. economy's trajectory.

Caldwell and Cheng are watching for these pivot points:

- Whether AI delivers actual productivity increases. If not, its GDP boost will fade;
- Whether workers are increasingly replaced by AI, resulting in lower labor demand;
- Whether conflict renews in the Middle East, especially if it involves the Strait of Hormuz.

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