RBC BlueBay Asset Management

AI Data Center Boom

How U.S. fixed income markets are powering the AI expansion

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Key points:

- 2026 could see nearly $500bn in AI-related debt financing across public and private markets. This unprecedented supply will pressure credit spreads, particularly in technology, creating near-term technical weakness rather than fundamental deterioration.
- Unlike the dot-com bubble, the companies driving AI investment have strong balance sheets, high cash flow generation, and low leverage. They're optimizing cost of capital, not re-leveraging, and can self-fund their AI buildout while maintaining shareholder returns.
- Institutional investors provide inelastic demand for high-quality credit that should cushion spread widening. Combined with early signs of AI revenue growth and 90% enterprise AI adoption, the risk of market collapse in the near term is low, though careful credit selection remains essential.

2026 is shaping up to be another historic year for fixed income markets as resiliency is yet again, put to the test. Supply/demand dynamics will be taking the front stage in the months to come as AI capex funding needs and growing merger & acquisitions (M&A) pipelines bring issuers to the market at a record pace. Compound this with a less restrictive interest rate environment – and the potential for further cuts – and we could be headed for the largest debt financing supercycle in recent history.

As the AI cycle moves from training to inference and ultimately agentic, the scale of capital needed to fund everything from data center construction, to compute capacity, to power generation and infrastructure is going to be extensive. And the capital needs are likely going to require participation from nearly every debt capital funding market, both public and private, to fulfill.

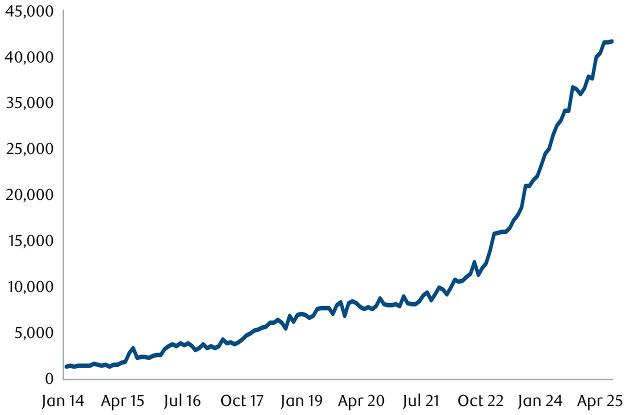
In this paper, we will discuss how the AI (artificial intelligence) supply boom is impacting fixed income markets. As we expect waves of debt issuance across investment grade and high yield markets to fund AI capex, it remains to be seen how much appetite investors may have for relatively unproven business models. Over the long term, we expect there to be winners and losers in the AI arms race and will be keeping a close eye on debt levels as it evolves. In the meantime, we plan to be tactical, treading carefully and being highly selective in individual credits across the heavy supply windows ahead.

AI driven data center boom to pressure credit markets

AI-driven compute demand is triggering the largest data-center buildout in U.S. history, and its capital intensity rivals energy and infrastructure megacycles. Until recently, the majority of this build out was financed with internally generated cash flows from large technology companies. But as shown in the charts below, the sheer size and amount of spend going into data centers continues to increase in proportion to revenues, resulting in the need for external sources of capital to continue to grow.

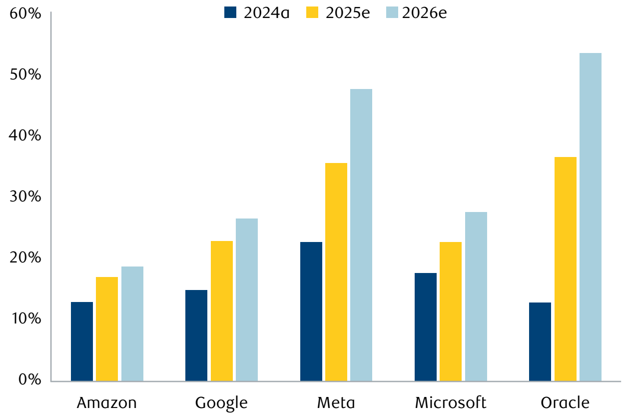
This is also what led to a significant acceleration of debt issuance in the 4th quarter of last year to fund AI-related capex and infrastructure investment. With close to $135bn borrowed by the hyperscalers alone, technology spreads felt the pressure over the period, unperforming broader market peers in both investment grade but more acutely in high yield.

Chart 1: Census Bureau Data Center "Put in Place" Spend



Source: Bloomberg, Census Bureau US Private Construction Spending Data Center, as of 3Q25.

Chart 2: Hyperscaler Capital Intensity (Capex/Revenue)

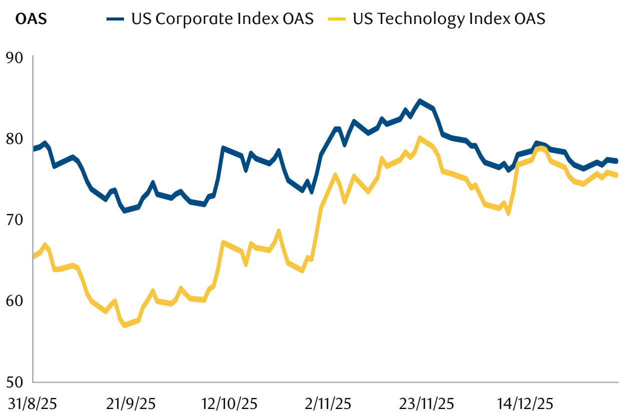


Source: Bloomberg, RBC GAM, BlueBay Fixed Income, as of 31 December 2025.

And we think this is just the beginning. With AI and data center capex set to increase by 30%+, we estimate related debt supply could be north of half a trillion dollars in 2026 across debt financing markets.

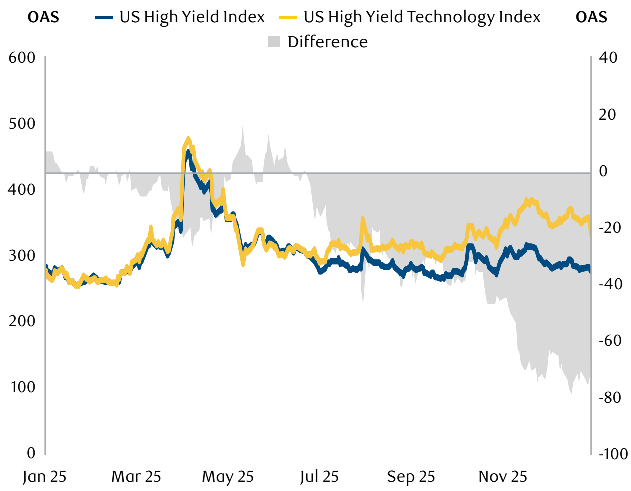
The lion's share of this supply will come into the public investment grade market, though high yield, securitized (ABS, CMBS), and private credit are likely to play an increasing role in financing the AI build out going forward.

Chart 3: Investment Grade Credit Spreads: Half a Trillion Dollar Build-Out Reshapes Credit Markets



Source: Bloomberg Indices, as of 31 December 2025.

Chart 4: High Yield Credit Spreads



Source: Bloomberg, ICE BofA, as of 31 December 2025.

In the near term, we anticipate credit markets will experience modestly wider spreads and heightened vulnerability, particularly within the technology sector, which is likely to face more sustained pressure. We also expect issuer dispersion to increase across the credit quality spectrum as the market digests unprecedented deal volumes at already stretched valuations.

While we do not, currently, see any major flashing red lights ahead, we are cognizant that the market could get spooked easily by any hint of deceleration in AI expectations and concerns of a bubble. This would likely impact equity more than credit, but we are mindful of the potential for spillover risk, which could be amplified by rising debt levels. With that said, we do not think 2026 is the year the AI bubble bursts, and near-term bouts of spread weakness are likely to present more of an opportunity than a risk.

Three pillars of support: why the AI debt boom differs from the Dot-Com bubble

As we recently witnessed in the technology sector, elevated levels of supply tend to put pressure on credit spreads, all else being equal. The reason for this is twofold:

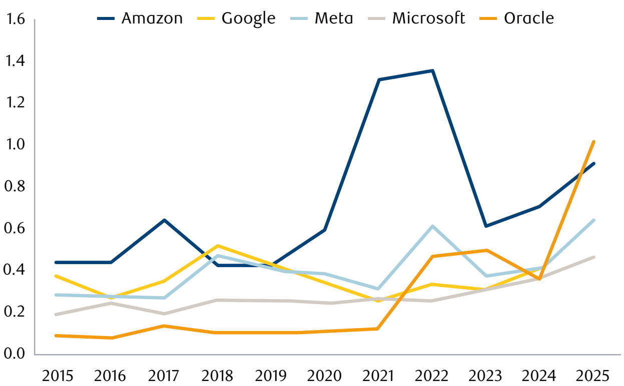
1. Technical factor: Increased supply can congest the market, creating a negative technical and driving spreads wider.
2. Fundamental factor: As debt increases, so does leverage and interest expense. If not managed prudently, this can result in deteriorating credit fundamentals and widening spreads as markets reprice this risk.

In the case of 2026, our view is that we will see more technical weakness than fundamental, and despite concerns that this is the dot com bubble all over again, we do believe there are a few key pillars of support that could help contain the impact should the AI exuberance stall:

Pillar 1: the issuers at the center of this build out – namely the recently dubbed "hyperscalers" – are, up to this point, generally high-quality corporations with large, liquid balance sheets. With the exception of Oracle and to a lesser extent, Meta, where some caution is likely warranted, these companies have high levels of cash on hand, strong cash flow generation, low leverage, and unencumbered access to capital markets.

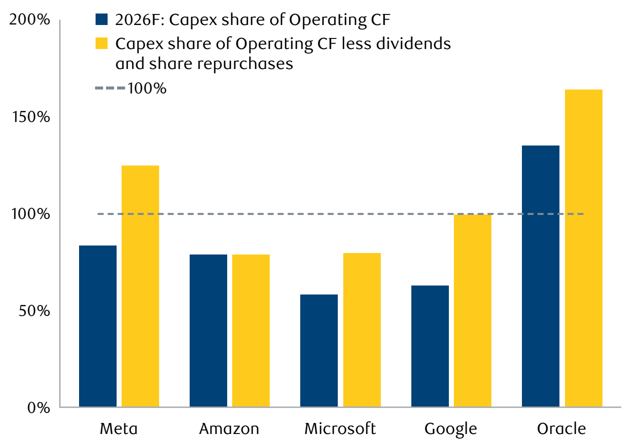
Even with a historic $4T of estimated AI-related capex spending by 2030, these companies have a lot of free cash flow runway, should they choose to use it, to fund their capital expenditure needs (Chart 5), while also supporting dividend and share repurchase policies (Chart 6).

Chart 5: Hyperscalers mostly have a capital expenditure/operating cashflow ratio of well under 1



Source: Deutsche Bank, as of 31 December 2025.

Chart 6: Capex vs. cash flow by issuer in 2026



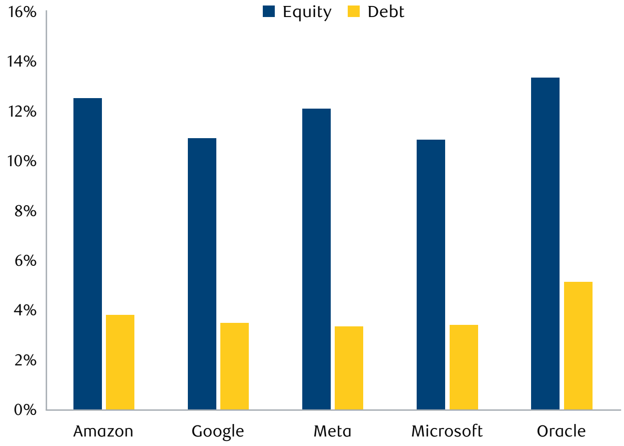
Source: BAML, as of 31 December 2025.

What this means is that this is not a re-leveraging event, it is an exercise in cost of capital optimization. These issuers do not **need** to raise debt, but given the financial flexibility enjoyed by a strong and stable balance sheet, they can choose and have chosen before to do so in lieu of sacrificing shareholder returns. Economically, this also makes sense for these corporations as the cost of equity capital is significantly higher than the cost of debt (Chart 7) and is expected to continue to be a preferred source of funding particularly given a tight spread and stable to decreasing interest rate environment.

Pillar 2: Though it is arguably still too soon to tell, we are seeing early signs of real revenue growth (Chart 8) and increasing AI entrenchment across business organizations. On the revenue side, AI companies like OpenAI and Anthropic are already seeing the revenue curve materialize. Whether this continues and broadens at a pace sufficient to justify the mass amounts of capital being invested is yet to be seen, and any breakthroughs or material and immediate efficiency gains (think Deepseek concerns in early 2024) remain a potential tail risk. Bottlenecks such as power supply could also amplify any growth concerns as we move later into 2026.

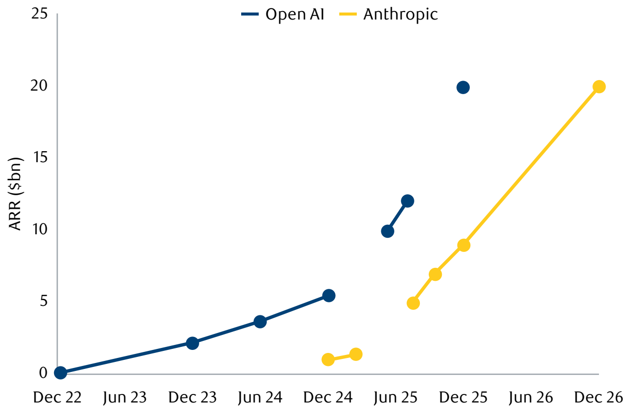
AI usage, meanwhile, is clearly expanding across the customer base. While many organizations are still in the pilot phase with AI, particularly at the enterprise level, AI usage is rapidly increasing with some surveys showing close to 90% of organizations – up from 55% 3 years ago – are now using AI in at least one business function and increasingly multiple business functions (McKinsey Global Survey Report.) We also have to remember that there are still sectors where AI is just starting to be explored and utilized, the largest being healthcare, which could unlock significant long-term benefits and new areas of application, data, and hence, increased compute demand.

Chart 7: Hyperscaler Cost of Capital



Source: Bloomberg WACC, company financial statements, as of 31 December 2025.

Chart 8: OpenAI and Anthropic Historic and Projected ARR ($bn)

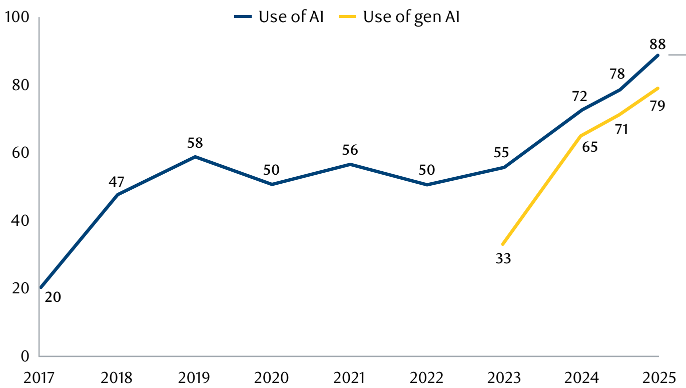


Source: proprietary estimates based on company filings, as of 31 December 2025.

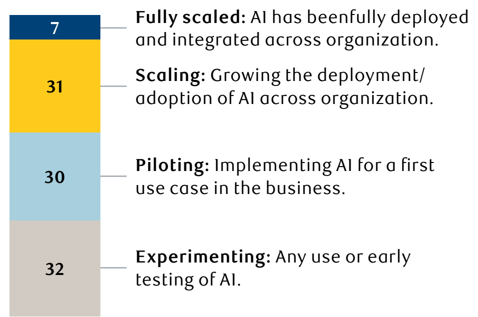
Chart 9: Reported use of AI in at least one business function continues to increase

Use of AI by respondents' organizations, % of respondents

Organizations that use AI in at least 1 business function[1]



Phase of AI use amoung organizations using AI in 2025



[1] In 2017, the definition for AI use was using AI in a core part of the organization's business or at scale. In 2018-19, the definition was embedding at least 1 AI capability in business processes or products. From 2020, the definition was that the organization has adopted AI in at least 1 function, and in 2025, the definition was regular use of AI in at least 1 function.

Source: McKinsey Global Surveys on the state of AI, 2017-2025, as of November 2025.

Pillar 3: Deep funding markets and inelasticity of demand for high quality credit should help mitigate downside risk on spreads. While investor appetite to finance unproven business models remains to be seen, there are natural buyers – namely pension funds with liabilities measured using a high-quality corporate discount rate, and insurance companies with regulated quality constraints – that provide a relatively inelastic source of demand for these bonds. In addition to traditional defined benefit pension plans, the $5T Target Date Fund 401(k) market should provide a stable source of demand for fixed income as glidepath allocations shift into more income generating assets over time.

Importantly, as these allocations are broadly agnostic to valuations they are unlikely to face selling pressure in shorter term market downturns. At the same time, the demand for yield and attractiveness of fixed income in today's rate environment in the US will also keep more valuation sensitive buyers, such as money managers, asset allocators, individual and foreign investors, in the mix. Should spreads widen in the event of either increased fundamental concerns or a market that becomes oversaturated with supply, these buyers are likely to step in at more attractive valuation levels, potentially providing a ceiling on the degree of spread widening that will occur.

Conclusion

Our main concerns stem from both the sheer exuberance and hype around the potential for AI and the inherent human need for immediate results. It is possible, if not likely, that reality will fall short of expectations, in large part due to insufficient power supply creating a bottle neck to compute capacity growth. How and how well markets adjust to AI realities will be a key area of focus for the months to come. In our view, markets are unlikely to collapse under the weight of AI capital spend, but they will continue to reprice risk as the story evolves.

In this environment, we continue to see a positive outlook in the year ahead for US Fixed Income and credit. Helped by high carry income and a better economic outlook, there is a good chance of high single digit returns for the asset class. Having said that, investors need to be careful as we navigate heavy issuance, developments in the AI space and various policy announcements. In portfolios, we are boosting dry powder and being highly selective in credit exposures, avoiding those issuers where such high levels of debt may start to erode cash flow generation and credit quality.

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