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AlphaCurrents: The Economy Explained

The AI Build-Out: When the Cloud Comes to Town

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Artificial intelligence (AI) is often discussed as a future productivity revolution. But before AI changes how most people work, it is changing how companies spend and how local economies grow.

Hyperscalers are committing hundreds of billions of dollars to data centers, chips, servers, networking equipment, cooling systems, backup power and grid infrastructure. At the national level, the impact on the economy may look smaller than those headline capital spending numbers suggest, partly because much of the expensive hardware is imported. That national accounting lens also masks the micro effects on households and local governments.

Communities do not experience the AI build-out as a line item in GDP. They experience it as construction crews, utility upgrades, higher land demand, larger tax-base potential and, in some cases, higher utility and housing costs. With over 4,000 data centers spread across the US and 9% annual growth expected through 2030 by the Electric Power Research Institute, the effects of this build-out at the local level are set to grow rapidly.

The cloud, where AI computing and storage live, may feel weightless to users, but its economic footprint lands county by county.

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The Economic Multiplier

A new data center creates demand not only for servers. It also creates demand for electricians, concrete, steel, engineering firms, utility contractors, security services, dining services near the construction site and housing for workers moving into the area.

The economic multiplier is a way of measuring how each dollar of spending ripples through the economy in this way. One of the simplest ways to think about the multiplier is this: The more spending that stays local, the larger the local economic ripple effect.

Consider a hypothetical $10 billion AI project. If most of the money is spent importing chips and servers, the direct local benefit may be limited. But if the project also requires a data center shell, new substations, transmission upgrades, cooling systems, engineering services and local construction crews, the local effect can become much larger. Workers get paid, local suppliers receive contracts, local businesses see more customers and governments may collect more property and business tax revenue.

The academic evidence supports the idea that data centers can create measurable local activity. A 2026 National Bureau of Economic Research (NBER) paper examining US county-level data center expansion points to positive effects on employment, new business creation, tax returns, wages and adjusted gross income. It also finds that the most persistent labor market response occurs in data processing employment, while construction employment is strongest at shorter horizons, consistent with the build-out phase.

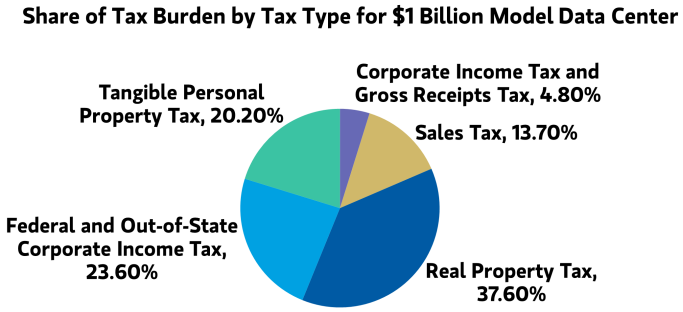
Data center multipliers are large but can be uneven over the build-out phase versus steady state operations, and they come with unintended costs, or negative externalities.

Why States Want Data Centers

Data centers are attractive to state and local governments because they can provide large capital investment without the long lead times of a traditional manufacturing cluster. They use land, require construction, expand the tax base and can signal that a region is plugged into the digital economy.

Tax revenue is the core attraction. Data centers are capital intensive and can generate significant property and sales tax revenues (see Exhibits 1 and 2).

Exhibit 1: Data Centers Pay Many Different Taxes

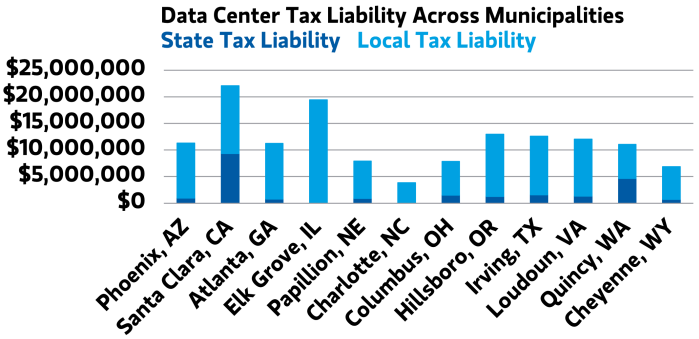


Notes: Calculations are for average tax liability over the first 10 years of operations to capture both new and depreciating property and taxable purchases; they represent an average across data centers in 12 modeled jurisdictions. The model firm has $220 million in gross revenue and 15 percent net income before tax, and calculations assume qualification for exemptions routinely available to data centers of this size.
Source: Tax Foundation, Morgan Stanley Wealth Management Global Investment Office as of Dec. 19, 2025

The National Conference of State Legislatures (NCSL) points to Loudoun County, Virginia, where data centers now pay enough in property taxes to fund the county's entire general operations budget. For smaller or fiscally constrained localities, that kind of tax base is hard to ignore.

As a result, the competition for data centers is intense. Currently, 38 states offer dedicated tax incentives for data centers, ranging from property tax abatements to sales and use tax exemptions on equipment and electricity.

Exhibit 2: Data Center Tax Liabilities Vary Significantly by Geography



Note: Chart shows annual and local tax liability for a $1 billion data center (mature operation) with $220 million of annual revenue and $33 million of net income before tax. Calculations are for data centers in a "steady state" where property is depreciating and being replaced on a regular schedule. Calculations assume qualification for exemptions routinely available to data centers of this size.
Source: Tax Foundation, Morgan Stanley Wealth Management Global Investment Office as of Dec. 19, 2025

The Incentive Tradeoff

The fiscal question is whether governments are paying too much to attract projects.

The Tax Foundation emphasizes that data center tax burdens depend heavily on state choices around sales and property taxation of equipment. Servers, cooling systems, backup generation and other equipment are costly, which makes exemptions valuable to companies and expensive for governments. NCSL similarly notes that every state with a dedicated data center incentive offers some form of sales tax exemption, and 14 states extend incentives to electricity used in regular operations.

This is where the policy tradeoff sharpens. Data centers may increase future tax revenue, but incentives can also remove a large share of the tax base that made the project attractive in the first place. Good Jobs First, an economic development advocacy organization, reports that 14 states and many localities fail to disclose how much revenue they lose to data-center tax abatements, while three states—Georgia, Virginia and Texas—already miss out on $1 billion or more per year.

States are starting to reassess. Some are adding sunset dates, clawbacks, energy requirements and payments in lieu of taxes, while lawmakers in multiple states have considered repealing or pausing incentives. That shift reflects a more complex policy debate: Data centers can expand the tax base, but poorly designed incentives can give away too much of it.

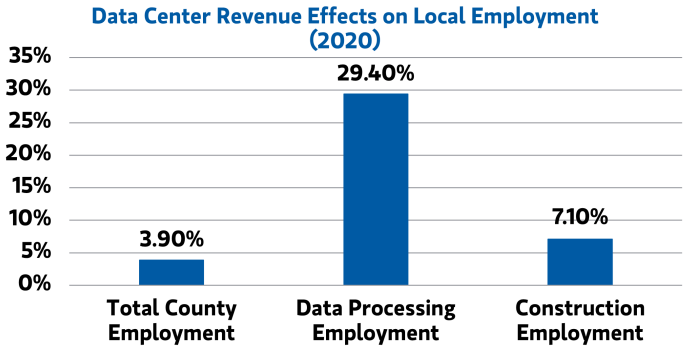
The Jobs Story Is Real, but Front-Loaded

The jobs story around AI data centers is nuanced.

Data centers can support significant employment during construction. The Joint Legislative Audit & Review Commission (JLARC) of Virginia finds that a 250,000-square-foot data center can support more than 1,500 workers during the construction phase.

But permanent employment is much lower. In Virginia, data centers employ only 50 full-time workers once operational. Illinois data shows that, among subsidized data centers subject to a 20-job requirement, 22 of 27 data centers created exactly 20 jobs, and only one reported more than 30 full-time positions. A national review prepared for Oklahoma suggested that data centers created an average of about 10 jobs per project in 2022.

Exhibit 3: Data Centers Boost Employment



Source: Alvarez, Fernando E., Argente, David, Chow, Joyce, and Van Patten, Diana (2026), "Data Centers and Local Economies in the Age of AI: A Shift-Share Approach" NBER Working Paper. Morgan Stanley Wealth Management Global Investment Office as of May 2026

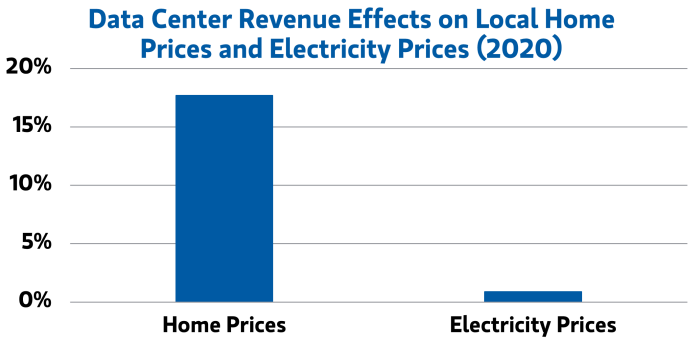
That does not mean the jobs impact is irrelevant. Construction jobs, skilled trades, engineering work and local supplier activity can still matter. But it does mean the multiplier is front-loaded. The strongest local labor market boost often comes while the facility is being built, not after it is operating. Exhibit 3 demonstrates that while there are significant effects on data processing jobs, the broader county employment impact is much smaller given that data processing employment accounts for less than 1% of total county employment.

Housing and Electricity Are the Pressure Points

While tax revenues and early labor market effects are significant, data center build-outs come with negative externalities: They are energy-, land- and water-intensive.

The NBER paper finds that counties more exposed to data center growth experience higher house prices and higher electricity prices. That is a critical point for households. Higher property values may benefit existing owners, but they can worsen affordability for renters and first-time buyers (see "The First-Time Homebuyer Squeeze," May 14, 2026). Higher electricity demand can require new generation, transmission, substations and grid upgrades, creating pressure on utility systems that were not built for AI-scale load growth (see Exhibit 4).

Exhibit 4: Data Centers Raise Home Prices and Utility Bills



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A typical AI data center may use as much electricity as 100,000 homes a year, while facilities under construction today could use up to 20 times that amount, according to the International Energy Agency. Those numbers help explain why residents may experience the AI build-out first through utility bills or local infrastructure debates rather than through productivity gains at work. Our public policy team has highlighted that the rising cost of electricity is becoming a key political issue ahead of the midterm elections this year (see "US Policy Pulse: Pricing the Politics of Power," Feb. 19, 2026).

The local policy question is therefore not whether data centers are good or bad. It is whether the community captures enough lasting benefit to justify the demands on land, power, water, housing and public finances.

Bottom Line

The AI build-out is not just a technology story. It is also a story about local economic development.

Data centers can bring capital investment, construction jobs, higher incomes, new establishments and meaningful tax-base potential. That is why states compete for them. But the benefits are uneven and often front-loaded, while the costs can show up in forgone tax revenue, higher electricity demand, housing pressure and greater strain on local infrastructure.

We are constructive on the economic and societal gains that will come from AI adoption, but the first major economic effect of AI is not broad productivity improvement. It is localized investment booms that reshape the communities where the infrastructure gets built. The cloud may live online, but its multiplier is being tested in concrete, copper, kilowatts and county budgets.

Disclosure Section

For index, indicator and survey definitions referenced in this report please visit the following: https://www.morganstanley.com/wealth-investmentsolutions/wmir-definitions

Glossary

Artificial Intelligence (AI) A field of study that seeks to train computers to process large amounts of unstructured information in a manner similar to human intelligence, capable of performing tasks such as learning and problem solving.

Risk premium is the return in excess of the risk-free rate of return an investment is expected to yield.

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