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An AIRR Pocket for AI Data Centers: Revisiting the Opportunity

The buildout of Artificial Intelligence (AI) infrastructure is one of the largest industrial projects in history, with capital expenditures on data centers projected to exceed $1 trillion in 2027 alone.[1] We believe this creates a long-term secular opportunity that extends beyond semiconductors and other computer hardware to the physical infrastructure these facilities require, including power generation, electrical equipment, and construction.

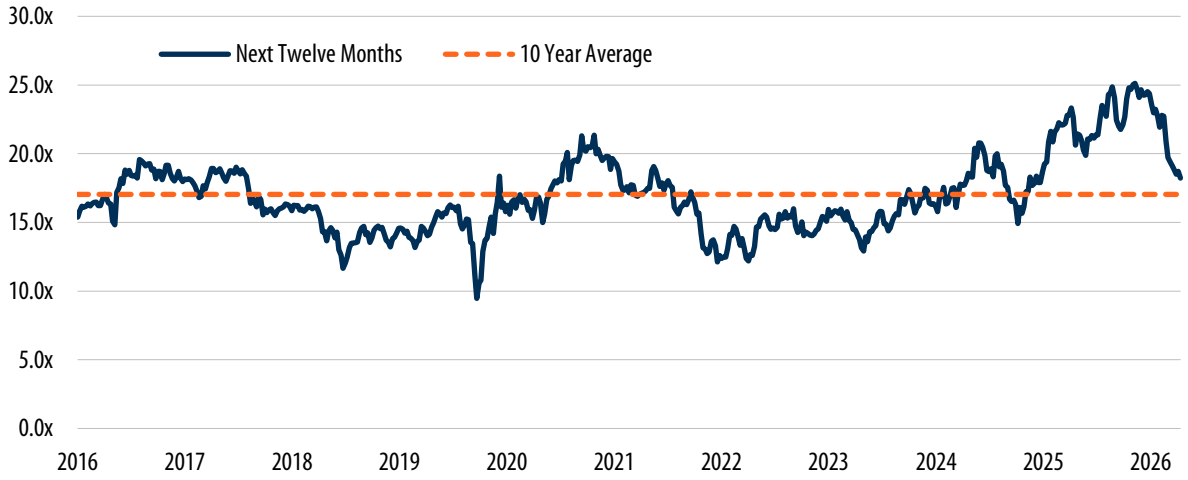
The First Trust RBA American Industrial Renaissance® ETF (AIRR) provides meaningful exposure to many of the small- and mid-cap US industrial stocks that are well-positioned to benefit from these trends, in our opinion. But while data center tailwinds have contributed to strong performance in recent years, the fund declined by 22.5% (30/6/26-30/9/26) amid a surge of volatility in the third quarter of 2026. Below, we assess some of the factors behind the pullback and why we believe the long-term case remains intact.

AIRR Under Pressure

In our view, three key factors contributed to AIRR's decline in the third quarter:

- ***Elevated Valuations*** – AIRR's forward P/E ratio was 24.9x on 30/6/26, roughly 45% higher than its historical 10-year average of 17.0x (30/6/16-30/9/26). In our view, higher valuations reflected expectations of stronger earnings growth for many AIRR holdings, largely driven by increased data center spending. However, higher valuations can also leave stocks more vulnerable to drawdowns from profit-taking, shifting sentiment, or any shortfall against growth expectations. By 30/9/26, the forward P/E ratio had declined to 18.1x, a 27% drop that was even larger than AIRR's price decline.

Chart 1: AIRR 10-Year Forward P/E



Source: Factset. Data from 30/6/2016-30/9/2026. Forward P/E is the price of a stock divided by estimated forward earnings. There is no assurance any forecasts will be achieved. Past performance is not a guarantee of future results.

- ***Midterm Politics*** – Criticisms of AI and data centers have intensified ahead of the November US midterm elections, and polling shows growing public opposition. An NBC News poll conducted in the second half of August found that 69% of respondents would oppose an AI data center in their local area.[2] Opponents often cite concerns that can be easily packaged into soundbites, ranging from increased power bills to water scarcity to noise pollution. In our view, the potential benefits of data centers for local communities, such as increased tax revenue and job creation may take longer to unpack. Hence, politicians from both sides of the aisle have recently taken steps to restrict or slow data center permitting, including the governors of New York, Pennsylvania, Texas, and Oregon, and more than 300 cities and counties across the US have adopted moratoriums or bans.[3] In our view, this has weighed on stocks involved with the data center buildout, as investors price in the potential for project delays and cancellations. So far, however, the practical impact appears to be limited, as just 2.3 GW of planned US capacity is currently delayed by moratoriums.[4]
- ***Interest Rates*** – Rising interest rates were also a headwind for stocks involved with the AI buildout in Q3, as the 10-year US Treasury yield climbed from 4.47% to 5.28% (30/6/26-30/9/26), its highest level since 2007. Higher yields can weigh heavily on stocks with elevated valuations, but rates also matter for the capital-intensive AI buildout itself, which is increasingly financed with debt. According to estimates, hyperscalers are expected to issue $420 billion of new debt in 2027, a 60% increase from 2026. By the third quarter of this year, bond investors were demanding wider spreads to absorb the supply.[5]

[1]Bloomberg, June 2026.
[2]NBC News
[3,4]SemiAnalysis
[5]Reuters citing Goldman Sachs estimates.

References to specific securities should not be construed as a recommendation to buy or sell and should not be assumed profitable.

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Why We Believe the Long-Term Thesis Remains Intact

Although the above factors weighed on AIRR in the third quarter, we believe there are several reasons to remain constructive on the AI Infrastructure buildout and AIRR's ability to benefit.

- ***More Attractive Valuations*** – AIRR's forward P/E ratio declined from 24.9x to 18.1x in Q3 (30/6/26-30/9/26) and now trades only modestly above the 10-year average of 17.0x. This represents a slight discount to the S&P 500's forward P/E of 19.0x, despite AIRR's stronger estimated growth. As of 30/9/26, AIRR's forward 12-month earnings growth was estimated at 24.3%, compared to 18.7% for the S&P 500 Index, and its revenue growth estimate was 13.0%, compared to 9.5% for the S&P 500. In our view, robust growth estimates help support AIRR's current valuation.
- ***Political Pragmatism May Follow the Midterms*** – One dynamic that may shift political narratives toward more pragmatic acceptance of data centers after the midterms is the prospect of significant tax revenue (or "payments in lieu of taxes") for local communities, combined with solutions to issues often raised by opponents. Loudoun County, Virginia, known as "data center alley," is one prominent example where data centers generated $1.2 billion in tax revenue, accounting for 39% of the county's overall budget in fiscal year 2026.[6] Meanwhile, several solutions may help address public concerns, such as outside air or closed-loop cooling (water usage),[7] company-funded power generation and grid updates (electricity costs),[8] enhanced sound barriers (noise), and ongoing engagement with community advisory boards.

  Some of these measures may increase costs or extend project timelines, but we believe they are manageable relative to the scale of the opportunity. Even if politics don't shift, the existing pipeline provides a cushion, in our view. According to Aterio.io, there are 79 gigawatts of compute capacity currently under construction in the US and an additional 433 gigawatts announced, compared with 54 gigawatts operating today.[9] While some announced projects may never break ground, we believe the committed pipeline alone should keep contractors busy for years, even if the pace of new announcements slows or cancellations rise.
- ***AI Spending Plans Continue to Rise*** – In our view, demand for compute remains robust, and the largest hyperscalers have continued to increase capital expenditure plans, despite market volatility, political pushbacks, and rising interest rates. Since 30 June capital expenditure growth expectations for 2027 were revised up 20% for the five largest hyperscalers.

  As funding shifts from free cash flow to debt (and equity) issuance, concerns about leverage are worth monitoring. However, we believe the four largest hyperscalers (Amazon, Microsoft, Alphabet and Meta) currently have strong balance sheets, with net debt to EBITDA ratios below 1x. While increased leverage and financing costs could create risks, we believe these balance sheets may provide flexibility for additional borrowing.
- ***Policy Tailwinds*** – The One Big Beautiful Bill Act (OBBBA), signed into law on 4 July 2025, includes tax incentives that lower the after-tax cost of capital investment. The law permanently restores 100% bonus depreciation for qualifying equipment, which can include servers, electrical systems, and other data center components, and creates a temporary 100% first-year deduction for new manufacturing facilities that begin construction before 2029.[10] It also raised the advanced manufacturing tax credit for semiconductor fabs to 35% for projects that begin construction by 2026.[11] In our view, these provisions are a supportive policy tailwind for the capital-intensive AI buildout, including domestic semiconductor and hardware manufacturing.
- ***AIRR is more than just AI*** – While data centers have been a key driver for many of AIRR's holdings, they're not the only one. AIRR also has exposure to long-term reshoring trends, such as building semiconductor plants in the US or supplying machinery and equipment for manufacturing. Although US factory construction spending has declined from its recent peak, it remains well above pre-pandemic levels, and incentives such as the OBBBA's expensing provisions may support future activity.[12] In addition, AIRR has a meaningful allocation to aerospace and defense stocks (14.6% as of 30/9/26), which may benefit from higher defense spending.

Looking Forward

Over the past several years, a willingness to weather periods of volatility has been necessary for investors to participate in AIRR's historical outperformance. AIRR's decline in Q3 was the sixth >20% drawdown since inception in 2014. Nevertheless, AIRR has outperformed several broad market indices during that same period, including the S&P 500, the S&P MidCap 400, and the S&P SmallCap 600 (see the table and chart on the following page). We believe AIRR's future performance will depend on the ability of its mid- and small-cap industrial holdings to navigate the risks discussed above and capitalize on one of the most powerful capital spending booms in history. With AIRR's forward P/E ratio down from 24.9x to 18.1x in the third quarter, we believe the long-term case remains intact and may warrant a fresh look from long-term investors.

Performance data quoted represents past performance. Past performance is not a guarantee of future results and current performance may be higher or lower than performance quoted. Investment returns and principal value will fluctuate and shares when sold or redeemed, may be worth more or less than their original cost. You can obtain performance information which is current through the most recent month-end by visiting www.ftportfolios.jp.

[6]Loudoun County

[7]Amazon

[8]Such as Florida and Texas

[9]Aterio.io

[10,11]BDO

[12]US Census Bureau, as of 31/8/26 (most recent).

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Overall Morningstar Rating™

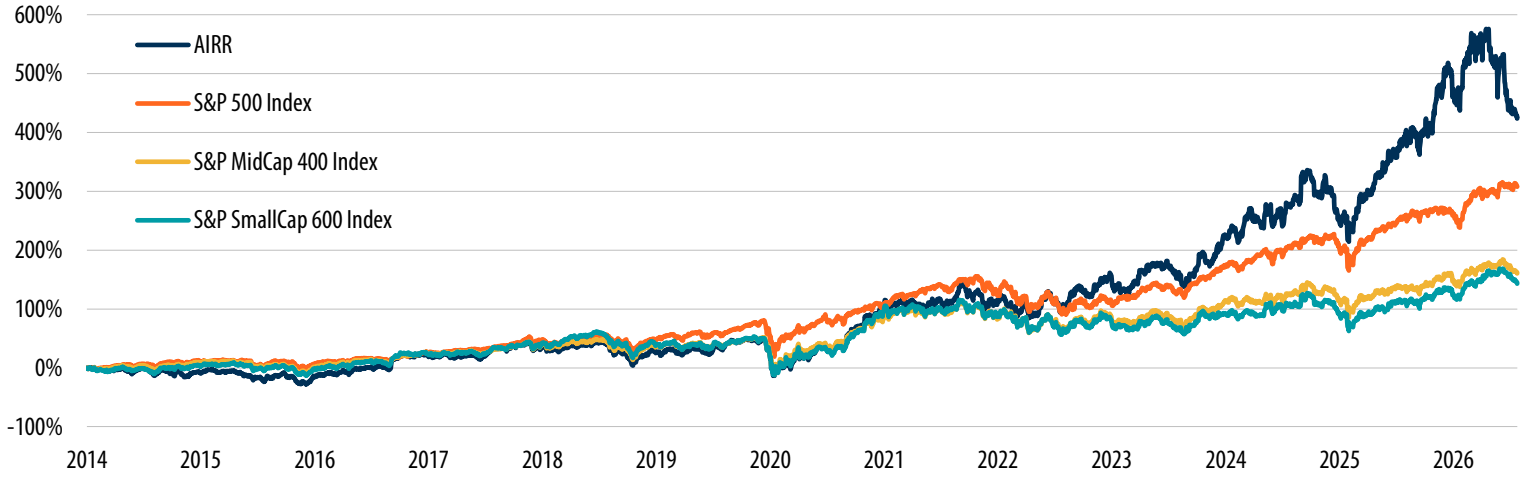
★★★★★

As of 30/9/2026. Among 46 funds in the US Fund Industrials category. This fund was rated 4 stars/46 funds (3 years), 4 stars/40 funds (5 years), 5 stars/32 funds (10 years) based on risk adjusted returns.^

AIRR Performance Summary (%) as of 30/9/2026

Fund Performance*	3 Month	1 Year	3 Year	5 Year	10 Year	Since Fund Inception
Net Asset Value (NAV)	-22.53	6.83	26.25	20.59	17.78	14.23
Market Price	-22.50	6.82	26.22	20.57	17.78	14.23
Index Performance**						
Richard Bernstein Advisors American Industrial Renaissance® Index	-22.41	7.58	27.18	21.48	18.64	15.09
S&P 500® Industrials Index	-9.66	9.50	19.85	13.06	12.78	11.51
Russell 2500™ Index	-6.37	17.45	17.74	7.46	10.81	9.44
S&P 500® Index	2.30	15.74	22.89	13.79	15.33	13.81

Chart 2: Cumulative NAV Total Return of AIRR vs. Benchmarks Since Inception



Data from 10/3/2014-30/9/2026.

Performance data quoted represents past performance. Past performance is not a guarantee of future results and current performance may be higher or lower than performance quoted. Investment returns and principal value will fluctuate and shares when sold or redeemed, may be worth more or less than their original cost. You can obtain performance information which is current through the most recent month-end by visiting www.ftportfolios.jp.

Fund Inception: 10/3/2014. Total Expense Ratio: 0.69%. The Investment Advisor has implemented fee breakpoints, which reduce the fund's investment management fee at certain asset levels. Please see the fund's Statement of Additional Information for full details.

***NAV** returns are based on the fund's net asset value which represents the fund's net assets (assets less liabilities) divided by the fund's outstanding shares. **Market Price** returns are determined by using the midpoint of the national best bid offer price ("NBBO") as of the time that the fund's NAV is calculated. Returns are average annualized total returns, except those for periods of less than one year, which are cumulative.

**Performance information for each listed index is for illustrative purposes only and does not represent actual fund performance. Indexes do not charge management fees or brokerage expenses, and no such fees or expenses were deducted from the performance shown. Indexes are unmanaged and an investor cannot invest directly in an index.

^The Morningstar Rating™ for funds, or "star rating", is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The Morningstar Rating does not include any adjustment for sales loads. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods. ©2026 Morningstar, Inc. All Rights Reserved. The Morningstar Rating™ information contained herein: (1) is proprietary to Morningstar;(2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use

You should consider the fund's investment objectives, risks, and charges and expenses carefully before investing. Contact First Trust Japan Co., Ltd. at www.ftportfolios.jp to obtain a prospectus which contains this and other information about the fund. The prospectus should be read carefully before investing.

Risk Considerations

You could lose money by investing in a fund. An investment in a fund is not a deposit of a bank and is not insured or guaranteed. There can be no assurance that a fund's objective(s) will be achieved. Investors buying or selling shares on the secondary market may incur customary brokerage commissions. Please refer to each fund's prospectus and Statement of Additional Information for additional details on a fund's risks. The order of the below risk factors does not indicate the significance of any particular risk factor.

Unlike mutual funds, shares of the fund may only be redeemed directly from a fund by authorized participants in very large creation/redemption units. If a fund's authorized participants are unable to proceed with creation/redemption orders and no other authorized participant is able to step forward to create or redeem, fund shares may trade at a premium or discount to a fund's net asset value and possibly face delisting and the bid/ask spread may widen.

Community banks were significantly impacted by the decline in the subprime mortgage lending market in the U.S. which brought about legislative and regulatory changes, changes in short-term and long-term interest rates, inflation and changes in government monetary and fiscal policies. Unlike larger national or other regional banks that are more geographically diversified, a community bank's financial performance may be highly dependent upon the business environment in certain geographic regions of the U.S. and may be adversely impacted by any downturn or unfavorable economic or employment developments in its local market and the U.S. as a whole.

Current market conditions risk is the risk that a particular investment, or shares of the fund in general, may fall in value due to current market conditions. For example, changes in governmental fiscal and regulatory policies, disruptions to banking and real estate markets, actual and threatened international armed conflicts and hostilities, and public health crises, among other significant events, could have a material impact on the value of the fund's investments.

A fund is susceptible to operational risks through breaches in cyber security. Such events could cause a fund to incur regulatory penalties, reputational damage, additional compliance costs associated with corrective measures and/or financial loss.

Depositary receipts may be less liquid than the underlying shares in their primary trading market and distributions may be subject to a fee. Holders may have limited voting rights, and investment restrictions in certain countries may adversely impact their value.

Equity securities may decline significantly in price over short or extended periods of time, and such declines may occur in the equity market as a whole, or they may occur in only a particular country, company, industry or sector of the market.

An index fund will be concentrated in an industry or a group of industries to the extent that the index is so concentrated. A fund with significant exposure to a single asset class, or the securities of issuers within the same country, state, region, industry, or sector may have its value more affected by an adverse economic, business or political development than a broadly diversified fund.

A fund may be a constituent of one or more indices or models which could greatly affect a fund's trading activity, size and volatility.

There is no assurance that the index provider or its agents will compile or maintain the index accurately. Losses or costs associated with any index provider errors generally will be borne by a fund and its shareholders.

Industrials and producer durables companies are subject to certain risks, including the general state of the economy, intense competition, consolidation, domestic and international politics, excess capacity and consumer demand and spending trends. They may also be significantly affected by overall capital spending levels, economic cycles, technical obsolescence, delays in modernization, labor relations, and government regulations.

Market risk is the risk that a particular security, or shares of a fund in general may fall in value. Securities are subject to market fluctuations caused by such factors as general economic conditions, political events, regulatory or market developments, changes in interest rates and perceived trends in securities prices. Shares of a fund could decline in value or underperform other investments as a result. In addition, local, regional or global events such as war, acts of terrorism, spread of infectious disease or other public health issues, recessions, natural disasters or other events could have significant negative impact on a fund.

A fund faces numerous market trading risks, including the potential lack of an active market for fund shares due to a limited number of market makers. Decisions by market makers or authorized participants to reduce their role or step away in times of market stress could inhibit the effectiveness of the arbitrage process in maintaining the relationship between the underlying values of a fund's portfolio securities and a fund's market price.

An index fund's return may not match the return of the index for a number of reasons including operating expenses, costs of buying and selling securities to reflect changes in the index, and the fact that a fund's portfolio holdings may not exactly replicate the index.

Securities of non-U.S. issuers are subject to additional risks, including currency fluctuations, political risks, withholding, lack of liquidity, lack of adequate financial information, and exchange control restrictions impacting non-U.S. issuers.

A fund and a fund's advisor may seek to reduce various operational risks through controls and procedures, but it is not possible to completely protect against such risks. The fund also relies on third parties for a range of services, including custody, and any delay or failure related to those services may affect the fund's ability to meet its objective.

A fund that invests in securities included in or representative of an index will hold those securities regardless of investment merit and the fund generally will not take defensive positions in declining markets.

High portfolio turnover may result in higher levels of transaction costs and may generate greater tax liabilities for shareholders.

The market price of a fund's shares will generally fluctuate in accordance with changes in the fund's net asset value ("NAV") as well as the relative supply of and demand for shares on the exchange, and a fund's investment advisor cannot predict whether shares will trade below, at or above their NAV.

Securities of small- and mid-capitalization companies may experience greater price volatility and be less liquid than larger, more established companies.

Trading on an exchange may be halted due to market conditions or other reasons. There can be no assurance that a fund's requirements to maintain the exchange listing will continue to be met or be unchanged.

First Trust Advisors L.P. is the adviser to the fund. First Trust Advisors L.P. is an affiliate of First Trust Portfolios L.P., the fund's distributor. First Trust Japan Co., Ltd. is the fund's sub-distributor.

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Definitions

Richard Bernstein Advisors American Industrial Renaissance® Index is an optimized, risk-weighted index of companies in the U.S. small and mid-cap industrial and community banking sectors.

Russell 2500™ Index is an unmanaged market-cap weighted index that includes the smallest 2,500 companies from the Russell 3000 Index.

S&P MidCap 400® Index is an unmanaged index of 400 stocks used to measure mid cap U.S. stock market performance.

S&P 500® Index is an unmanaged index of 500 companies used to measure large-cap U.S. stock market performance.

S&P 500® Industrials Index is an unmanaged index which includes the stocks in the industrials sector of the S&P 500 Index.

S&P SmallCap 600® Index is an unmanaged index of 600 stocks used to measure small cap U.S. stock market performance.

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