

Weekly commentary

July 15, 2024

BlackRock

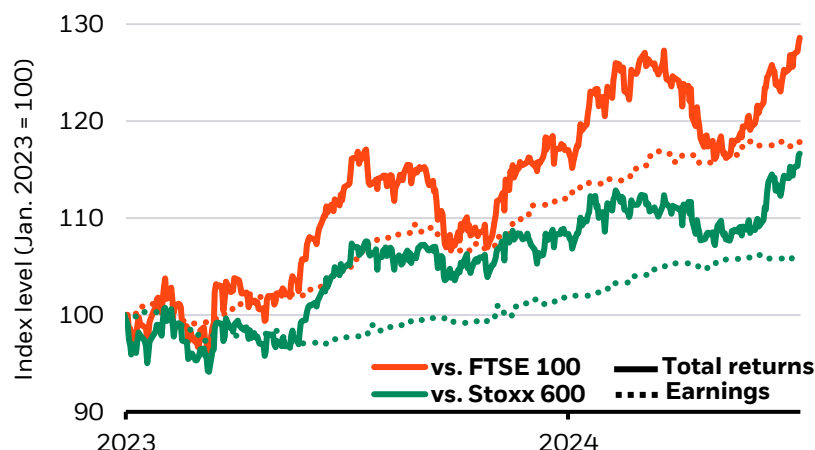
Why we keep leaning into risk

- We think a transformation akin to past technological revolutions is gearing up. We keep leaning into risk and the AI theme while upgrading UK stocks.
- U.S. stocks hit a new record high last week while 10-year Treasury yields fell. Volatility in small cap and tech shares shows markets can quickly get choppy.
- We expect the European Central Bank to hold policy rates steady this week. The ECB may cut rates in September, but we don't see a typical easing cycle ahead.

We see unprecedented waves of transformation creating an unusually wide range of outcomes. Our [2024 Midyear Global Outlook](#) shows how, rather than waiting for clarity, we're leaning into risk. We stay overweight U.S. equities and the artificial intelligence (AI) theme yet monitor valuations. We like private markets as a way to access early winners. Elsewhere, we go overweight UK equities and stay overweight Japan. We favor short-term bonds for income and prefer quality in credit.

All about earnings

S&P 500 relative performance, 2023-2024



Forward looking estimates may not come to pass. It is not possible to invest directly in an index. Index performance does not account for fees. Source: BlackRock Investment Institute, with data from LSEG Datastream, July 2024. Notes: The chart shows the S&P 500 relative performance of total returns and 12-month forward earnings vs. the UK's FTSE 100 and Europe's Stoxx 600 indexes.

A transformation of a historic scale could be unfolding. Investment opportunities transcend the unusual macro backdrop of sticky inflation, higher interest rates, slower growth and elevated debt. U.S. equities had a banner first half of 2024 versus other developed markets (DMs) even as markets priced out Federal Reserve rate cuts. The strength of U.S. stock gains has been matched by corporate earnings beating expectations, led by a handful of AI names. See the chart. As a result, we see concentration as a feature, not a flaw, of today's market environment. We expect some volatility ahead as markets grapple with a wide range of outcomes – as shown by last week's brief retreat in tech shares. Recent low market volatility doesn't reflect all risks ahead, in our view. We still think the next six to 12 months is a time to lean into risk but we prepare to reassess as new opportunities arise.



Jean Boivin

Head – BlackRock Investment Institute



Wei Li

Global Chief Investment Strategist – BlackRock Investment Institute



Vivek Paul

Global Head of Portfolio Research – BlackRock Investment Institute



Natalie Gill

Portfolio Strategist – BlackRock Investment Institute

Visit [BlackRock Investment Institute](#) for insights on the global economy, markets and geopolitics.

BlackRock Investment Institute

In the near term, we see a concentrated group of AI winners driving returns. We stay overweight U.S. stocks and the AI theme. AI-related data center investment could rise by 60-100% annually in coming years, according to a mix of forecasters including the International Energy Agency. We see the AI theme playing out in three phases. This first AI buildout phase is already producing early winners – including big tech firms, chip producers and companies supplying key inputs like energy, utilities, materials and real estate. Yet this phase faces challenges, such as whether the power grid can keep pace. We think markets and central banks underappreciate the inflationary impact of this early phase. The next phase could see investment broadening to companies looking to harness AI’s power. The final phase – potential economy-wide AI productivity gains – is highly uncertain. These gains can only come after AI capabilities are fully deployed, a process that could take many years.

We also lean into risk by going overweight UK equities. We see the Labour Party’s landslide UK election victory increasing the likelihood of a two-term government. The potential for long-term policy implementation should bring relative political stability, in our view. We think perceived stability can help improve sentiment – especially among foreign investors who own more than half of UK shares. We added to our overweight to Japan equities in March due to corporate reforms. Wage gains are filtering into mild inflation and corporate pricing power, reinforcing our optimism on a long-term strategic horizon.

We balance our risk-on view by staying selective in fixed income, focusing on quality. We prefer short-term government bonds and credit that are delivering much higher income than pre-pandemic. We are overweight short-term investment grade credit given signs that lower-quality pockets are starting to show cracks from higher-for-longer rates. Strategically, we like private credit over public. Private credit defaults remain relatively limited. Private markets are complex, with high risk and volatility, and not suitable for all investors. By region, we like long-dated UK gilts over long-dated U.S. Treasuries strategically.

Bottom line: We see unprecedented transformation unfolding in the real economy. We lean into risk as a result. In stocks, we like the U.S., UK and Japan. We prefer quality income in fixed income – especially in short-term credit – and like private credit.

Market backdrop

U.S. stocks hit a new record high last week while 10-year Treasury yields fell to around 4.21%, down nearly 50 basis points from their April highs. The U.S. CPI for June came in surprisingly soft, but we think this level of inflation is unsustainably low given ongoing wage pressures. The drop in yields sparked a surge in small cap shares and a brief retreat in tech shares. We think this reflects how markets can become choppy again, even if leaning into risk will be rewarded.

Assets in review

Selected asset performance, year-to-date return and range



Past performance is not a reliable indicator of current or future results. Indexes are unmanaged and do not account for fees. It is not possible to invest directly in an index.
Sources: BlackRock Investment Institute, with data from LSEG Datastream as of July 11, 2024. Notes: The two ends of the bars show the lowest and highest returns at any point year to date, and the dots represent current year-to-date returns. Emerging market (EM), high yield and global corporate investment grade (IG) returns are denominated in U.S. dollars, and the rest in local currencies. Indexes or prices used are: spot Brent crude, ICE U.S. Dollar Index (DXY), spot gold, MSCI Emerging Markets Index, MSCI Europe Index, LSEG Datastream 10-year benchmark government bond index (U.S., Germany and Italy), Bank of America Merrill Lynch Global High Yield Index, J.P. Morgan EMBI Index, Bank of America Merrill Lynch Global Broad Corporate Index and MSCI USA Index.

Week ahead

July 17	UK CPI data	July 19	Japan CPI
July 18	ECB policy decision; Philadelphia Fed business index		

We expect the ECB to hold rates steady this week after their policy meeting. We think the ECB will act on forthcoming data in September but see rates staying higher due to inflationary pressures in the longer term. Overall, this remains an atypical rate-cutting cycle.

Big calls

Our highest conviction views on tactical (6-12 month) and strategic (long-term) horizons, July 2024

Tactical	Reasons
AI and U.S. equities	<ul style="list-style-type: none">We have high conviction that AI can keep driving returns in most scenarios. We see its buildout and adoption creating opportunities across sectors. The AI theme has driven U.S. stock gains and solid corporate earnings, making us overweight U.S. stocks overall.
Japanese equities	<ul style="list-style-type: none">This is our highest conviction equity view thanks to support from the return of mild inflation, shareholder-friendly corporate reforms and a Bank of Japan that is cautiously normalizing policy – rather than tightening.
Income in fixed income	<ul style="list-style-type: none">The income cushion bonds provide has increased across the board in a higher rate environment. We like quality income in short-term bonds and credit. We’re neutral long-term U.S. Treasuries.
Strategic	Reasons
Private credit	<ul style="list-style-type: none">We think private credit is going to earn lending share as banks retreat – and at attractive returns relative to public credit risk.
Fixed income granularity	<ul style="list-style-type: none">We prefer inflation-linked bonds as we see inflation closer to 3% on a strategic horizon. We also like short-term government bonds, and the UK stands out for long-term bonds.
Equity granularity	<ul style="list-style-type: none">We favor emerging over developed markets yet get selective in both. EMs at the cross current of mega forces – like India and Saudi Arabia – offer opportunities. In DM, we like Japan as the return of inflation and corporate reforms brighten our outlook.

Note: Views are from a U.S. dollar perspective, July 2024. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This information should not be relied upon by the reader as research or investment advice regarding any particular funds, strategy or security.

Tracking five mega forces

Mega forces are big, structural changes that affect investing now – and far in the future. As key drivers of the new regime of greater macroeconomic and market volatility, they change the long-term growth and inflation outlook and are poised to create big shifts in profitability across economies and sectors. This creates major opportunities – and risks – for investors. See our [web hub](#) for our research and related content on each mega force.

- 1. Demographic divergence:** The world is split between aging advanced economies and younger emerging markets – with different implications.
- 2. Digital disruption and artificial intelligence (AI):** Technologies are transforming how we live and work.
- 3. Geopolitical fragmentation and economic competition:** Globalization is being rewired as the world splits into competing blocs.
- 4. Future of finance:** A fast-evolving financial architecture is changing how households and companies use cash, borrow, transact and seek returns.
- 5. Transition to a low-carbon economy:** The transition is set to spur a massive capital reallocation as energy systems are rewired.

Granular views

Six- to 12-month tactical views on selected assets vs. broad global asset classes by level of conviction, July 2024

Our approach is to first determine asset allocations based on our macro outlook – and what’s in the price. **The table below reflects this and, importantly, leaves aside the opportunity for alpha, or the potential to generate above-benchmark returns.** The new regime is not conducive to static exposures to broad asset classes, in our view, but is creating more space for alpha.

		Underweight	Neutral	Overweight	Previous view	
Asset					View	Commentary
Equities	Developed markets					
	United States				+1	We are overweight given our positive view on the AI theme. Valuations for AI beneficiaries are supported as tech companies keep beating high earnings expectations. We think upbeat sentiment can broaden out. Falling inflation is easing pressure on corporate profit margins.
	Europe				-1	We are underweight. Valuations are looking more attractive. A pickup in growth and European Central Bank rate cuts support an ongoing earnings recovery.
	UK				+1	We are overweight. Political stability and a growth pickup could improve investor sentiment, lifting the UK's low valuation relative to other DM stock markets.
	Japan				+2	We are overweight. Mild inflation and shareholder-friendly reforms are positives. We see the BOJ normalizing policy – not tightening aggressively. A weak yen is a drag on returns for international investors.
Fixed Income	Emerging markets				Neutral	We are neutral. The growth and earnings outlook is mixed. We see valuations for India and Taiwan looking high.
	China				Neutral	We are neutral. We see risks from weak consumer spending, even with measured policy support. An aging population and geopolitical risks are structural challenges.
	Short U.S. Treasuries				+1	We are overweight. We prefer short-term government bonds for income as interest rates stay higher for longer.
	Long U.S. Treasuries				Neutral	We are neutral. Markets have cut expectations of Fed rate cuts and term premium is close to zero. We think yields will keep swinging in both directions on new economic data.
	Global inflation-linked bonds				Neutral	We are neutral. We see higher medium-term inflation, but cooling inflation and growth may matter more near term.
	Euro area govt bonds				Neutral	We are neutral. Market pricing reflects policy rates in line with our expectations and 10-year yields are off their highs. Political developments remain a risk to fiscal sustainability.
	UK gilts				Neutral	We are neutral. Gilt yields have tightened to U.S. Treasuries and market pricing of future yields is in line with our view.
	Japanese govt bonds				-2	We are underweight. Stock returns look more attractive to us. We see some of the least attractive returns in JGBs.
	China govt bonds				Neutral	We are neutral. Bonds are supported by looser policy. Yet we find yields more attractive in short-term DM paper.
	U.S. agency MBS				Neutral	We are neutral. We see agency MBS as a high-quality exposure in a diversified bond allocation and prefer it to IG.
	Short-term IG credit				+1	We are overweight. Short-term bonds better compensate for interest rate risk. We prefer Europe over the U.S.
	Long-term IG credit				-1	We are underweight. Spreads are tight, so we prefer taking risk in equities from a whole portfolio perspective. We prefer Europe over the U.S.
	Global high yield				Neutral	We are neutral. Spreads are tight, but the total income makes it more attractive than IG. We prefer Europe.
	Asia credit				Neutral	We are neutral. We don't find valuations compelling enough to turn more positive.
	Emerging hard currency				Neutral	We are neutral. The asset class has performed well due to its quality, attractive yields and EM central bank rate cuts. We think those rate cuts may soon be paused.
	Emerging local currency				Neutral	We are neutral. Yields have fallen closer to U.S. Treasury yields, and EM central banks look to be turning more cautious after cutting policy rates sharply.

Past performance is not a reliable indicator of current or future results. It is not possible to invest directly in an index. Note: Views are from a U.S. dollar perspective. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast or guarantee of future results. This information should not be relied upon as investment advice regarding any particular fund, strategy or security.

BlackRock Investment Institute

The BlackRock Investment Institute (BII) leverages the firm's expertise and generates proprietary research to provide insights on macroeconomics, sustainable investing, geopolitics and portfolio construction to help BlackRock's portfolio managers and clients navigate financial markets. BII offers strategic and tactical market views, publications and digital tools that are underpinned by proprietary research.

General disclosure: This material is intended for information purposes only, and does not constitute investment advice, a recommendation or an offer or solicitation to purchase or sell any securities to any person in any jurisdiction in which an offer, solicitation, purchase or sale would be unlawful under the securities laws of such jurisdiction. The opinions expressed are as of July 15, 2024, and are subject to change without notice. Reliance upon information in this material is at the sole discretion of the reader. Investing involves risks. This information is not intended to be complete or exhaustive and no representations or warranties, either express or implied, are made regarding the accuracy or completeness of the information contained herein. This material may contain estimates and forward-looking statements, which may include forecasts and do not represent a guarantee of future performance.

In the **U.S. and Canada**, this material is intended for public distribution. In **EMEA**, in the UK and Non-European Economic Area (EEA) countries: this is Issued by BlackRock Investment Management (UK) Limited, authorised and regulated by the Financial Conduct Authority. Registered office: 12 Throgmorton Avenue, London, EC2N 2DL. Tel: + 44 (0)20 7743 3000. Registered in England and Wales No. 02020394. For your protection telephone calls are usually recorded. Please refer to the Financial Conduct Authority website for a list of authorised activities conducted by BlackRock. In the European Economic Area (EEA): this is Issued by BlackRock (Netherlands) B.V. is authorised and regulated by the Netherlands Authority for the Financial Markets. Registered office Amstelplein 1, 1096 HA, Amsterdam, Tel: 020 – 549 5200, Tel: 31-20-549-5200. Trade Register No. 17068311 For your protection telephone calls are usually recorded. In **Italy**, for information on investor rights and how to raise complaints please go to <https://www.blackrock.com/corporate/compliance/investor-right> available in Italian. In **Switzerland**, for qualified investors in Switzerland: This document is marketing material. Until 31 December 2021, this document shall be exclusively made available to, and directed at, qualified investors as defined in the Swiss Collective Investment Schemes Act of 23 June 2006 ("CISA"), as amended. From 1 January 2022, this document shall be exclusively made available to, and directed at, qualified investors as defined in Article 10 (3) of the CISA of 23 June 2006, as amended, at the exclusion of qualified investors with an opting-out pursuant to Art. 5 (1) of the Swiss Federal Act on Financial Services ("FinSA"). For information on art. 8 / 9 Financial Services Act (FinSA) and on your client segmentation under art. 4 FinSA, please see the following website: www.blackrock.com/finisa For investors in **Israel**: BlackRock Investment Management (UK) Limited is not licensed under Israel's Regulation of Investment Advice, Investment Marketing and Portfolio Management Law, 5755-1995 (the "Advice Law"), nor does it carry insurance thereunder. In **South Africa**, please be advised that BlackRock Investment Management (UK) Limited is an authorized financial services provider with the South African Financial Services Board, FSP No. 43288. In the **DIFC** this material can be distributed in and from the Dubai International Financial Centre (DIFC) by BlackRock Advisors (UK) Limited – Dubai Branch which is regulated by the Dubai Financial Services Authority (DFSA). This material is only directed at 'Professional Clients' and no other person should rely upon the information contained within it. BlackRock Advisors (UK) Limited - Dubai Branch is a DIFC Foreign Recognised Company registered with the DIFC Registrar of Companies (DIFC Registered Number 546), with its office at Unit 06/07, Level 1, Al Fattan Currency House, DIFC, PO Box 506661, Dubai, UAE, and is regulated by the DFSA to engage in the regulated activities of 'Advising on Financial Products' and 'Arranging Deals in Investments' in or from the DIFC, both of which are limited to units in a collective investment fund (DFSA Reference Number F000738). In the **Kingdom of Saudi Arabia**, issued in the Kingdom of Saudi Arabia (KSA) by BlackRock Saudi Arabia (BSA), authorised and regulated by the Capital Market Authority (CMA), License No. 18-192-30. Registered under the laws of KSA. Registered office: 7976 Salim Ibn Abi Bakr Shaikan St, 2223 West Umm Al Hamam District Riyadh, 12329 Riyadh, Kingdom of Saudi Arabia, Tel: +966 11 838 3600. CR No, 1010479419. The information contained within is intended strictly for Sophisticated Investors as defined in the CMA Implementing Regulations. Neither the CMA or any other authority or regulator located in KSA has approved this information. In the **United Arab Emirates** this material is only intended for -natural Qualified Investor as defined by the Securities and Commodities Authority (SCA) Chairman Decision No. 3/R.M. of 2017 concerning Promoting and Introducing Regulations. Neither the DFSA or any other authority or regulator located in the GCC or MENA region has approved this information. In the **State of Kuwait**, those who meet the description of a Professional Client as defined under the Kuwait Capital Markets Law and its Executive Bylaws. In the **Sultanate of Oman**, to sophisticated institutions who have experience in investing in local and international securities, are financially solvent and have knowledge of the risks associated with investing in securities. In **Qatar**, for distribution with pre-selected institutional investors or high net worth investors. In the **Kingdom of Bahrain**, to Central Bank of Bahrain (CBB) Category 1 or Category 2 licensed investment firms, CBB licensed banks or those who would meet the description of an Expert Investor or Accredited Investors as defined in the CBB Rulebook. The information contained in this document, does not constitute and should not be construed as an offer of, invitation, inducement or proposal to make an offer for, recommendation to apply for or an opinion or guidance on a financial product, service and/or strategy. In **Singapore**, this is issued by BlackRock (Singapore) Limited (Co. registration no. 200010143N). This advertisement or publication has not been reviewed by the Monetary Authority of Singapore. In **Hong Kong**, this material is issued by BlackRock Asset Management North Asia Limited and has not been reviewed by the Securities and Futures Commission of Hong Kong. In **South Korea**, this material is for distribution to the Qualified Professional Investors (as defined in the Financial Investment Services and Capital Market Act and its sub-regulations). In **Taiwan**, independently operated by BlackRock Investment Management (Taiwan) Limited. Address: 28F., No. 100, Songren Rd., Xinyi Dist., Taipei City 110, Taiwan. Tel: (02)23261600. In **Japan**, this is issued by BlackRock Japan. Co., Ltd. (Financial Instruments Business Operator: The Kanto Regional Financial Bureau. License No375, Association Memberships: Japan Investment Advisers Association, the Investment Trusts Association, Japan, Japan Securities Dealers Association, Type II Financial Instruments Firms Association.) For Professional Investors only (Professional Investor is defined in Financial Instruments and Exchange Act). In **Australia**, issued by BlackRock Investment Management (Australia) Limited ABN 13 006 165 975 AFSL 230 523 (BIMAL). The material provides general information only and does not take into account your individual objectives, financial situation, needs or circumstances. In **New Zealand**, issued by BlackRock Investment Management (Australia) Limited ABN 13 006 165 975, AFSL 230 523 (BIMAL) for the exclusive use of the recipient, who warrants by receipt of this material that they are a wholesale client as defined under the New Zealand Financial Advisers Act 2008. In **China**, this material may not be distributed to individuals resident in the People's Republic of China ("PRC", for such purposes, not applicable to Hong Kong, Macau and Taiwan) or entities registered in the PRC unless such parties have received all the required PRC government approvals to participate in any investment or receive any investment advisory or investment management services. For **Other APAC Countries**, this material is issued for Institutional Investors only (or professional/sophisticated /qualified investors, as such term may apply in local jurisdictions). In **Latin America**, no securities regulator within Latin America has confirmed the accuracy of any information contained herein. The provision of investment management and investment advisory services is a regulated activity in Mexico thus is subject to strict rules. For more information on the Investment Advisory Services offered by BlackRock Mexico please refer to the Investment Services Guide available at www.blackrock.com/mx.

©2024 BlackRock, Inc. All Rights Reserved. **BLACKROCK** is a trademark of BlackRock, Inc., or its subsidiaries in the United States and elsewhere. All other trademarks are those of their respective owners.

BlackRock

Not FDIC Insured • May Lose Value • No Bank Guarantee