Weekly commentary

BlackRock

May 27, 2025

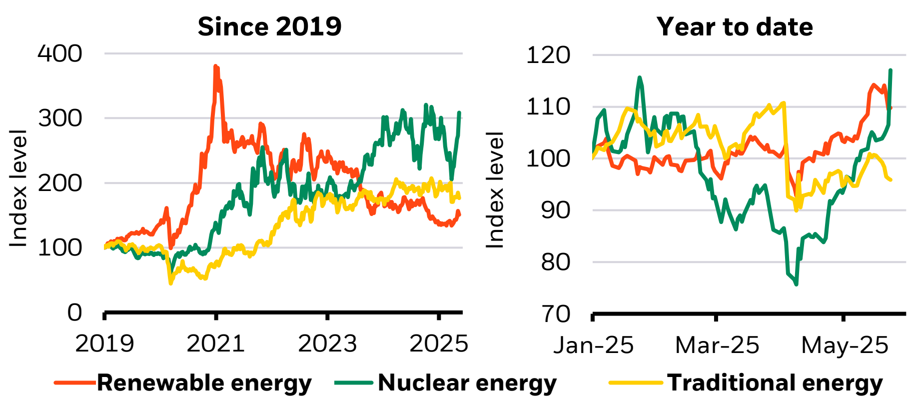
Staying nimble as energy policy pivots

- With global energy demand surging, many governments are recalibrating their energy policies and making waves in markets – but changes vary by region.
- U.S. stocks fell last week over higher bond yields and threats of new U.S. tariffs. We focus on actions over words as economic constraints spur policy rollbacks.
- U.S. PCE inflation this week is unlikely to reflect the full tariff impact, similar to the April CPI. But we see tariffs and a tight labor market keeping inflation sticky.

Proposed revisions to the U.S. Inflation Reduction Act are the latest in a wave of global policy changes as governments balance energy security, reliability and affordability with environmental objectives. That task is now trickier as mega forces – like power-hungry AI and geopolitical fragmentation – and electrification in some markets drive up energy demand. We see recent policy pivots causing volatility and unlocking regional opportunities, requiring investors to stay nimble.

Beaten up renewables

U.S. energy equity performance, 2019-2025



The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results. Index returns do not reflect fees, costs or expenses. Indices are unmanaged and one cannot invest directly in an index. Source: BlackRock Investment Institute, with data from Bloomberg, May 2025. Underlying indexes: S&P Global Clean Energy Transition Index for renewable energy, Solactive Global Uranium & Nuclear Components Total Return Index for nuclear and S&P Energy Select Sector Index for traditional.

In the U.S., policymakers want to amp up domestic energy production to power AI and promote national security, but are also looking for sources of tax revenue to fund tax extensions elsewhere. We see clean energy caught in the crosshairs of that balancing act. The latest revision of the House bill, now sent to the Senate, phases out clean energy tax credits in the Inflation Reduction Act sooner. Yet the U.S. likely needs more of all kinds of energy to meet AI's needs. Industry projections see U.S. data center electricity consumption rising between 50% and 200% by 2030 – a big jump after 15 years of flat national power demand. Where does this leave clean energy stocks? They had been slumping ever since a 2021 surge. See left chart. But since April, they have been eclipsing traditional energy on hopes of limited legislative changes. See right chart. Should investors dip their toe back in now?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In the near term, we think energy and trade policy volatility presents opportunities for stock pickers and we're watching for fresh policy revisions as the legislation heads to the Senate. Longer term, we see clean energy stocks positioned for strong growth. Renewables are quick to build and valuations are attractive: the factors that contributed to their slump – like high rates and tariffs – are now priced in, we think. AI and national security goals are likely to keep driving demand for all types of power, including nuclear. Last week, President Trump signed executive orders aimed at expediting nuclear power reactor deployment, and the most recent revisions to the House bill preserved the existing tax credits allotted to nuclear project developers. But given how long it takes to build nuclear power plants, we see natural gas and renewables benefiting sooner.

Nuclear was the topic of another recent about-face in public policy elsewhere. Last week, Germany ended its longstanding aversion to nuclear power, affirming it as a low-carbon source promoting EU energy independence and affordability. Most EU nations are now supportive – a potential boon for its competitiveness, long hampered by higher energy prices. We see opportunities in the electrical equipment chain, grid infrastructure and nuclear power generation. Yet we watch for hurdles. Europe lacks recent experience in nuclear projects – and the few that have happened overran budgets and deadlines.

Policy shifts are also afoot in traditional energy. OPEC+ – a group of petroleum-producing countries – has historically sought higher oil prices to fund government projects. Yet even as prices have fallen, hitting a four-year low in April, OPEC+ has kept boosting supply. Prices jumped last week on reports that Israel might strike Iran's nuclear facilities. But if prices stay low – and OPEC+ keeps upping production – this would mark yet another sea change. It may signal OPEC+'s efforts to reclaim market share from U.S. shale oil producers. It could slow adoption of electric vehicles, as lower oil prices make clean tech less attractive. It could also confront the U.S. with another balancing act: cheap oil means consumers pay less at the pump, but too-low prices jeopardize U.S. oil. We monitor the June 1 OPEC+ meeting for signs the change will persist.

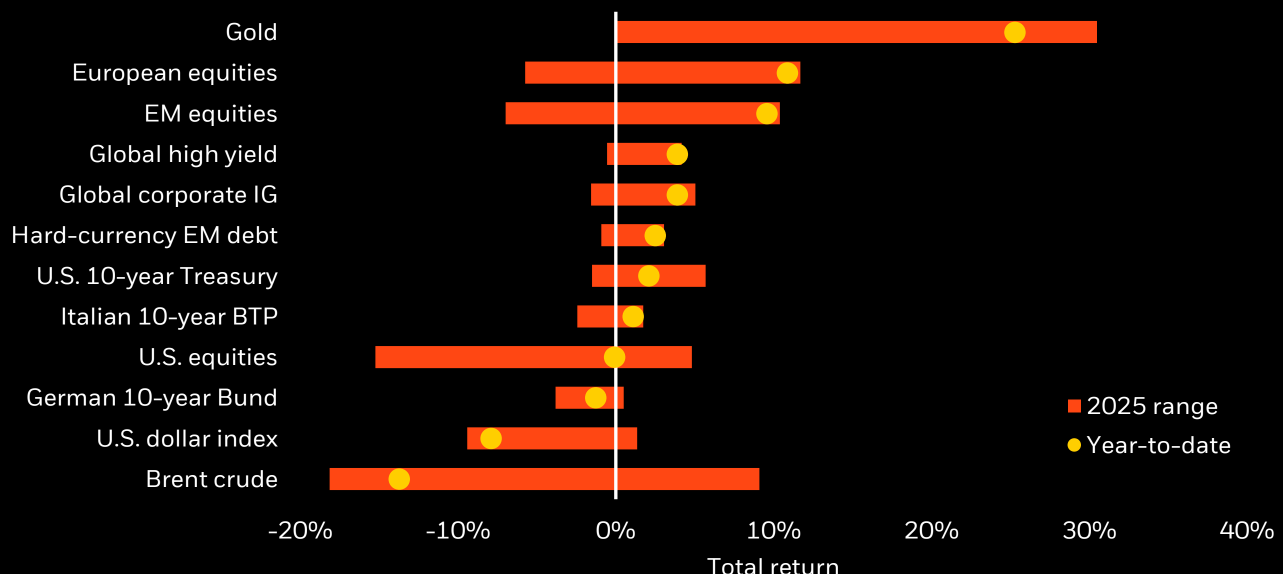
Bottom line: Growing power demand has policymakers rethinking the trade-offs between energy sustainability, affordability and security. We see opportunities in nuclear, U.S. natural gas and renewables (especially solar and batteries).

Market backdrop

The S&P 500 fell about 2% last week as worries about new fiscal pressures are pushing up U.S. Treasury yields. The slide was exacerbated after President Trump threatened to levy a 50% tariff on EU imports and a 25% tariff on Apple iPhones not made in the U.S. Yet we focus on actions over words as we've seen how economic constraints can spur policy rollbacks. U.S. 10-year Treasury yields ended the week at 4.51%, rising for a fourth week in a row. Japanese bond yields surged.

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 May 22, 2025. 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

May 27	U.S. consumer confidence	**May 31**	China manufacturing PMI
May 30	U.S. PCE		

This week, the focus shifts to U.S. April PCE, the Federal Reserve's preferred inflation gauge. Soft CPI and producer price data point to easing inflation pressures. But it's too soon to see the full effect of tariff hikes, and we see a tight labor market keeping wage pressures sticky – both leading to stubbornly high inflation. That likely limits how much the Fed can cut interest rates this year. Markets are pricing in two to three 25-basis point rate cuts by year end.

Big calls

Our highest conviction views on six- to 12-month (tactical) and over five-year (strategic) horizons, May 2025

Tactical	Reasons
U.S. equities	Policy uncertainty and supply disruptions are weighing on near-term growth, raising the risk of a contraction. Yet we think U.S. equities will regain global leadership as the AI theme keeps providing near-term earnings support and could drive productivity in the long term.
Japanese equities	We are overweight. Ongoing shareholder-friendly corporate reforms remain a positive. We prefer unhedged exposures given the yen's potential strength during bouts of market stress.
Selective in fixed income	Persistent deficits and sticky inflation in the U.S. make us underweight long-term U.S. Treasuries. We also prefer European credit – both investment grade and high yield – over the U.S. on more attractive spreads.

Strategic	Reasons
Infrastructure equity and private credit	We see opportunities in infrastructure equity due to attractive relative valuations and mega forces. We think private credit will earn lending share as banks retreat – and at attractive returns.
Fixed income granularity	We prefer short-term inflation-linked bonds over nominal developed market (DM) government bonds, as U.S. tariffs could push up inflation. Within DM government bonds, we favor UK gilts over other regions.
Equity granularity	We favor emerging over developed markets yet get selective in both. Emerging markets (EM) at the cross current of mega forces – like India – offer opportunities. In DM, we like Japan as the return of inflation and corporate reforms brighten the outlook.

Note: Views are from a U.S. dollar perspective, May 2025. 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, May 2025

We have lengthened our tactical investment horizon back to six to 12 months. The table below reflects this and, importantly, leaves aside the opportunity for alpha, or the potential to generate above-benchmark returns – especially at a time of heightened volatility.

Underweight | Neutral | Overweight | ● Previous view

	Asset	View	Commentary
Equities	**Developed markets**		
Equities	United States	+1	We are overweight. Policy-driven volatility and supply-side constraints are pressuring growth, but we see AI supporting corporate earnings in the near term and driving productivity over the long run.
Equities	Europe	Neutral	We are neutral, preferring the U.S. and Japan. We see structural growth concerns and uncertainty over the impacts of rising defense spending, fiscal loosening and de-escalation in Ukraine. Yet room for more European Central Bank rate cuts can support an earnings recovery.
Equities	UK	Neutral	We are neutral. Political stability could improve investor sentiment. Yet an increase in the corporate tax burden could hurt profit margins near term.
Equities	Japan	+1	We are overweight given the return of inflation and shareholder-friendly corporate reforms. We prefer unhedged exposure as the yen has tended to strengthen during bouts of market stress.
Equities	**Emerging markets**	Neutral	We are neutral. U.S. tariffs and trade tensions are likely to drag on growth in China and emerging markets more broadly, even with potential policy support.
Equities	China	Neutral	We are neutral. The uncertainty of trade barriers makes us more cautious, with potential policy stimulus only partly offsetting the drag. We still see structural challenges to China's growth.
Fixed Income	Short U.S. Treasuries	+1	We are overweight. We view short-term Treasuries as akin to cash in our tactical views – but we would still lean against the market pricing of multiple Fed rate cuts this year.
Fixed Income	Long U.S. Treasuries	-2	We are underweight. Persistent budget deficits and geopolitical fragmentation could drive term premium up over the near term. We prefer intermediate maturities less vulnerable to investors demanding more term premium.
Fixed Income	Global inflation-linked bonds	Neutral	We are neutral. We see higher medium-term inflation, but cooling inflation and growth may matter more near term.
Fixed Income	Euro area govt bonds	-1	We are underweight. Growth and inflation risks are balanced. Trade uncertainty may hurt growth more than it boosts inflation, allowing the ECB to cut rates more. Greater defense and infrastructure spending will support growth in the medium term but might boost term premia.
Fixed Income	UK gilts	Neutral	We are neutral. Gilt yields are off their highs, but the risk of higher U.S. yields having a knock-on impact and reducing the UK's fiscal space has risen. We are monitoring the UK fiscal situation.
Fixed Income	Japanese govt bonds	-1	We are underweight. Yields have surged, yet stock returns still look more attractive to us.
Fixed Income	China govt bonds	Neutral	We are neutral. Bonds are supported by looser policy. Yet we find yields more attractive in short-term DM paper.
Fixed Income	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.
Fixed Income	Short-term IG credit	+1	We are overweight. Short-term bonds better compensate for interest rate risk.
Fixed Income	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.
Fixed Income	Global high yield	Neutral	We are neutral. Spreads are tight, but the total income makes it more attractive than IG. We prefer Europe.
Fixed Income	Asia credit	Neutral	We are neutral. We don't find valuations compelling enough to turn more positive.
Fixed Income	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.
Fixed Income	Emerging local currency	-1	We are underweight. We see emerging market currencies as especially sensitive to trade uncertainty and global risk sentiment.

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