Weekly commentary

June 2, 2025

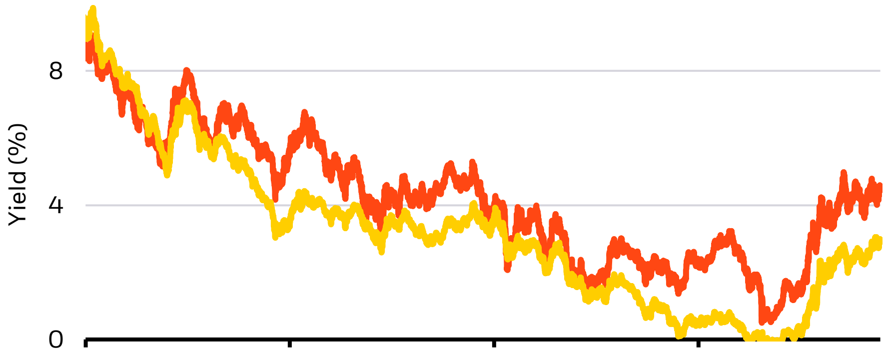
A bumpy ride upwards for global yields

- Investors now want more compensation for the risk of holding long-term bonds. We see this as a return to past norms and keep our long-held underweight.
- U.S. stocks rose nearly 2% last week, led by tech stocks. U.S. 10-year Treasury yields fell but are 50 basis points above their April lows.
- U.S. jobs data this week will show how the labor market is holding up. The European Central Bank is set to cut policy rates as it eyes the impact of tariffs.

Long-term U.S. bond yields jumped from April lows as policy developments, like the budget bill, draw focus to U.S. debt sustainability. This has revived questions about the diversification role of Treasuries. We have long pointed to the low, even negative, risk premium investors accepted for Treasuries – and expected it to change. That's now playing out, dragging up developed market government bond yields. We stay underweight long-term bonds but prefer the euro area to the U.S.

Following the U.S.

10-year U.S. yields vs. ex-U.S. developed market yields, 1990-2025



Past performance is not a reliable indicator of current or future results. Source: BlackRock Investment Institute, with data from LSEG Datastream, May 2025. Notes: The chart shows U.S. 10-year Treasury yields and an average of 10-year German, Japanese and UK government bond yields.

Ultra-low interest rates in the pandemic lulled investors into a sense of safety about ballooning government debt. They accepted lower term premium, or compensation for the risk of holding that debt over a long time. That pulled down global yields as well. See the chart. But long-term yields are up sharply since April as investors demand more term premium. We have long expected that. In 2021, we flagged that elevated government debt created a fragile equilibrium, with bonds vulnerable to changing investor perception of their risk. And we pointed to persistent inflation pressure from post-pandemic supply disruptions. Higher inflation, and thus higher policy rates along with any rise in term premium, boost debt servicing costs. We're still underweight long-term developed market (DM) government bonds, but have a relative preference for the euro area and Japan over the U.S.

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Our strongest conviction has been staying underweight long-term U.S. Treasuries. We maintain that view as concerns about the deficit mount. In March, we estimated the U.S. deficit-to-GDP ratio would land in the 5% to 7% range, based on external forecasts of the impact of proposed trade, fiscal and immigration policy. Since then, Moody's cut the U.S. top-notch credit rating and Congress is considering a budget bill that we think could push deficits to the upper end of that range – or beyond. We're watching to see if these changes impact foreign investors and drive term premium even higher.

In Japan, 30-year bond yields hit a record high in May, confirming our long-standing underweight. Japan's central bank – historically the largest government bond buyer as part of policy easing to lift the economy out of deflation – has trimmed purchases as part of its policy normalization. That has put pressure on long-term yields, and a recent long-term bond auction drew the weakest demand in a decade. This in turn prompted Japan's Ministry of Finance to consider trimming long-term bond sales. If yields rise more, the government's cost to service its debt – now twice the size of its economy – will also rise.

The UK is already rolling back long-term bond issuance amid lower demand and higher yields. Meanwhile, euro area yields have been rising as governments up defense and infrastructure investment. Yet we prefer euro area government bonds to the U.S. They're increasingly less correlated to fluctuations in U.S. Treasuries, and a sluggish economy gives the European Central Bank more room to cut rates in the near term. For income, we prefer shorter-term government bonds and European credit – both investment grade and high-yield – over the U.S. on cheaper valuations.

On equities, we flipped back to being pro-risk in April once it became clear that hard economic rules limit how far U.S. policy can move from the status quo, such as how foreign investors fund U.S. debt. Our U.S. equity overweight relies on that rule, just as another rule – supply chains can't rewire overnight without serious disruption – proved binding on trade policy. This overweight is grounded in the artificial intelligence mega force – reinforced by Nvidia's earnings beat last week.

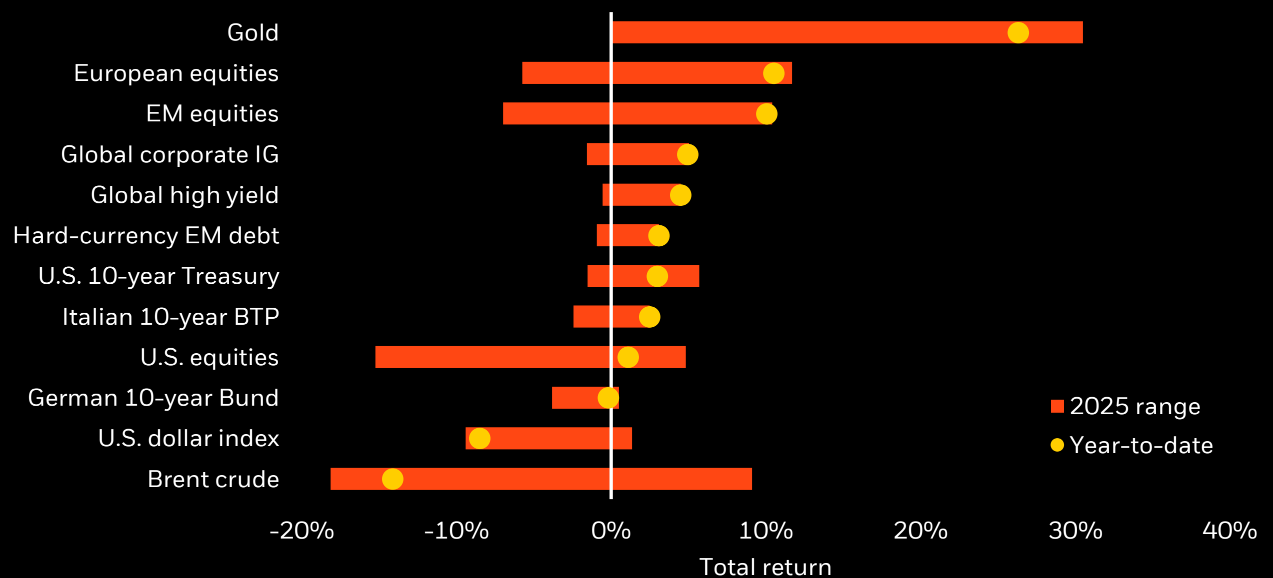
Bottom line: U.S. Treasury yields have jumped since April. That's a global story of normalizing term premium. We stay underweight long-term DM government bonds, preferring shorter-term bonds and euro area credit.

Market backdrop

U.S. stocks gained nearly 2% last week, led by tech stocks after Nvidia beat earnings expectations. The S&P 500 was up nearly 22% from its April lows. Stocks got a boost during the week after a U.S. trade court blocked most of the new U.S. tariffs. But a federal appeals court later granted a stay on the decision – allowing the tariffs to stay in place until a final decision is reached. U.S. 10-year Treasury yields edged down to 4.40% but are still 50 basis points above their April lows.

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 29, 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

June 3	Flash euro area inflation; euro area unemployment data
June 5	European Central Bank policy decision
June 6	U.S. payrolls

We're watching this week's U.S. payroll data for May after job gains topped expectations and wage growth cooled in April. We're tracking the impact of trade disruptions on hiring and how slowing labor force growth affects wage pressures. We see the European Central Bank cutting policy rates modestly but look for signs that it might cut more deeply if trade disruptions weigh on euro area growth.

Big calls

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