

October 2019

BlackRock®

Global Investment Outlook: Q4 update


BlackRock
Investment
Institute

FOR PUBLIC DISTRIBUTION IN THE U.S., HONG KONG, SINGAPORE AND AUSTRALIA. FOR INSTITUTIONAL,
PROFESSIONAL, QUALIFIED INVESTORS AND QUALIFIED CLIENTS IN OTHER PERMITTED COUNTRIES


Summary

- Trade disputes and geopolitical frictions have become key drivers of the economy and markets. U.S. trade policy has become increasingly unpredictable. Recent geopolitical volatility – including attacks on Saudi oil infrastructure – underscores this message from our Midyear Outlook.
- Persistent uncertainty from protectionist policies is denting corporate confidence and slowing business spending. Yet we still believe the economic expansion is intact, supported by dovish central banks and a robust U.S. consumer. This suggests moderate risk-taking will likely be rewarded – even as recent events reinforce our call for a greater focus on portfolio resilience.
- We expect more Federal Reserve rate cuts, but believe markets are pricing in too much monetary easing. The ECB materially exceeded market expectations on stimulus, launching a broad package with a combined impact that should be greater than the sum of its parts.
- We do not believe monetary policy alone is a cure for the fallout from global trade tensions. Supply chain disruptions could deliver a hit to productive capacity that fosters mildly higher inflation even as growth slows. This complicates the case for further policy easing.
- Overall, we favor reducing risk amid the ongoing protectionist push. We prefer U.S. equities for their reasonable valuations and relatively high quality; and the min vol and quality factors for their defensive properties. We like EM debt for its coupon income. We are overweight euro area sovereigns: a relatively steeper yield curve brightens their appeal even at low yields. And we see government bonds as important portfolio stabilizers.


Our 2019 investment themes



Protectionist push – The substantial escalation in the U.S.-China conflict – and unpredictability of U.S. policy actions – have injected additional uncertainty into business planning, threatening to weaken economic activity. Market implication: We favour reducing risk, including raising some cash.



Stretching the cycle – Central banks have pivoted to easing. The record-long U.S. economic expansion is supported by healthy household spending and looks unlikely to morph into a deeper downturn any time soon. Market implication: We like U.S. equities and EM debt.

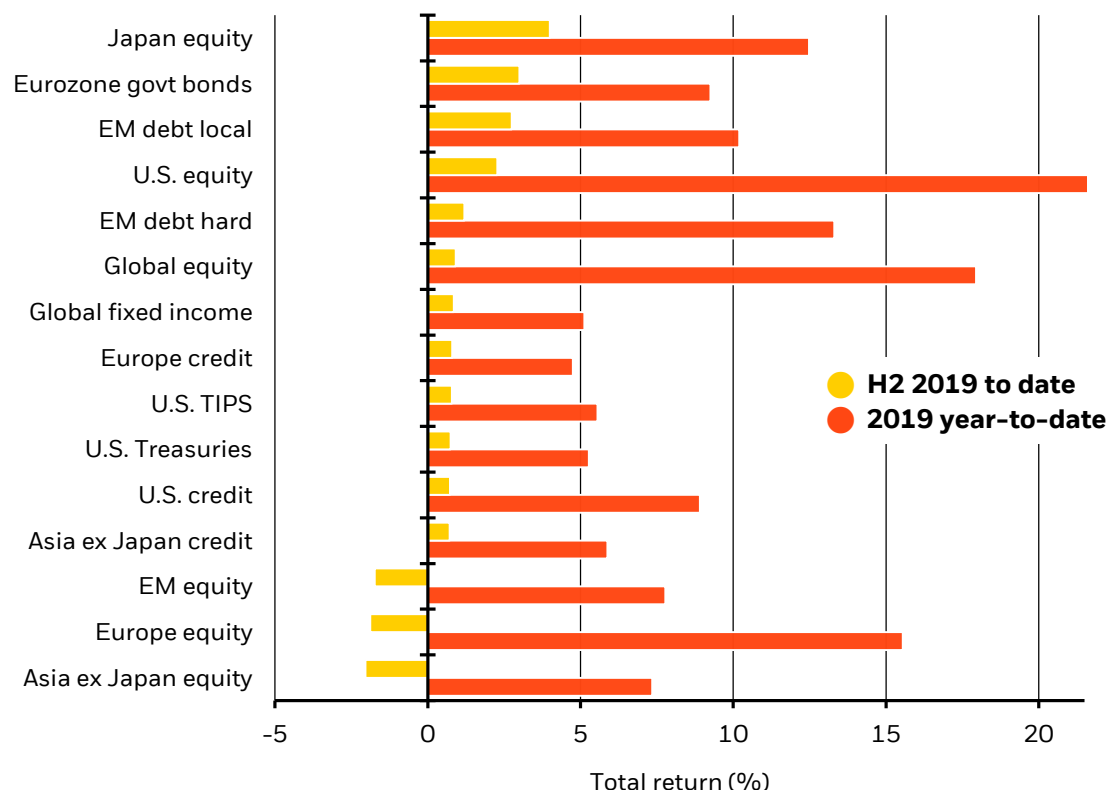


Raising resilience – Portfolio resilience is crucial at a time of elevated macro uncertainty. Market implication: Government bonds play an important role in building portfolio resilience – even at low yield levels.

Scoring our views

Risk assets have performed strongly this year to date, but geopolitical tensions loom as an ongoing risk. Government bonds have played an important diversification role.

Asset performance, 2019 second-half and year-to-date



- We have been surprised by the extent of the rally in government bonds, which have played a key role in cushioning against equity selloffs.
- Our overweight in U.S. equities has paid off. Yet rising geopolitical risks challenge our overall moderate pro-risk stance.
- EM and Asia-ex-Japan equities have underperformed since midyear, validating our shift to an underweight stance.
- Japanese equities have outperformed, contrary to our expectations, thanks to a lull in trade tensions that we see as temporary.

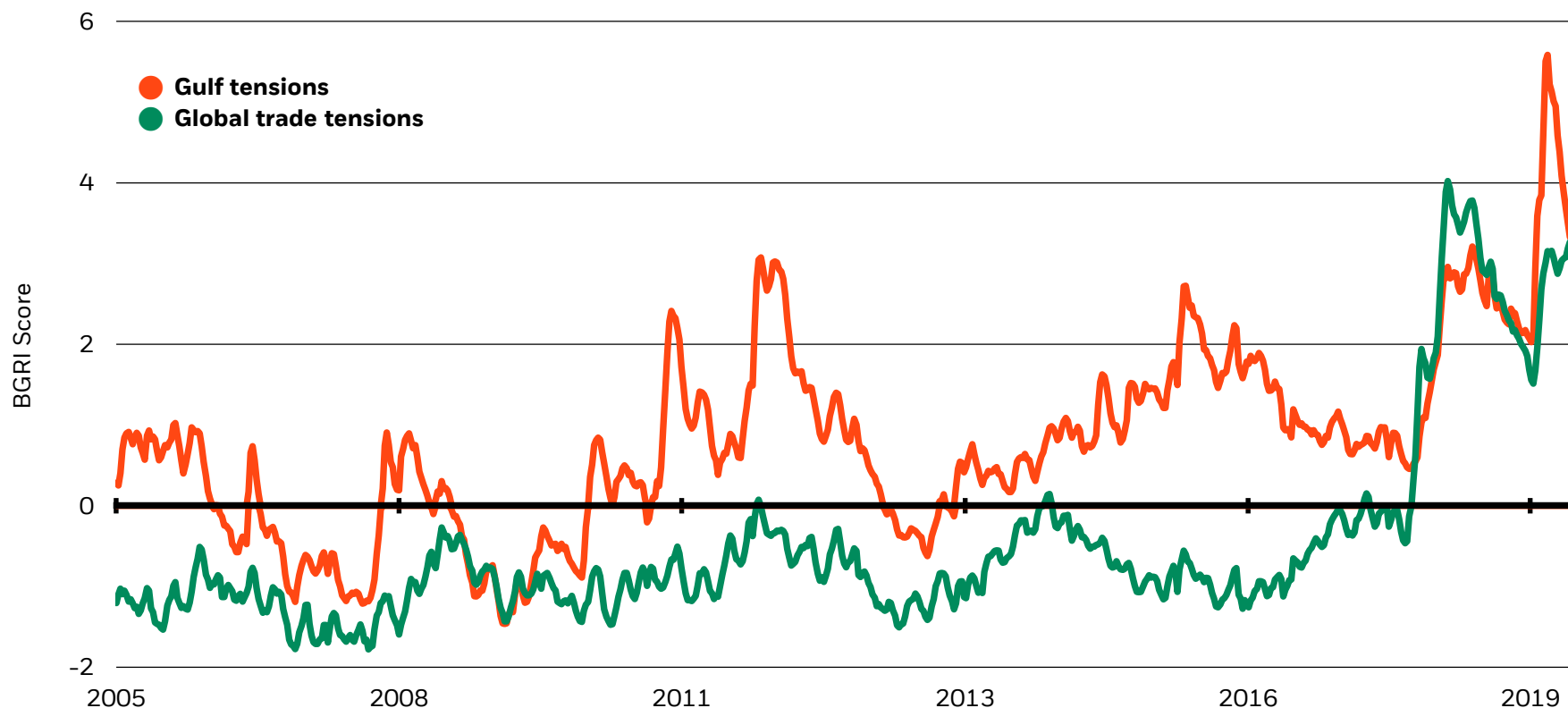
Past performance is not a reliable indicator of current or future results. It is not possible to invest directly in an index.

Source: BlackRock Investment Institute, with data from Thomson Reuters. September 2019 Notes: Data are through 16th September 2019. Indexes or prices used are: MSCI Japan Index, FTSE EMU Government Bond Index all maturities Index, JPM GBI-EM Global Diversified Composite Index, MSCI USA Index, JPM EMBI Global Diversified Index, MSCI AC World Index, Bloomberg Barclays Global Aggregate Index, Bloomberg Barclays Pan-European Aggregate: Corporate Index, U.S. TIPS USD Index, Bloomberg Barclays U.S. Treasury Index, Bloomberg Barclays U.S. Credit Index, Bloomberg Barclays Non-Japan Asia Credit Index, MSCI EM Index, MSCI Europe Index, MSCI AC ASIA ex. Japan Index,. Returns are shown in USD. Indexes are unmanaged and not subject to fees.

Persistent geopolitical uncertainty

The U.S. and China have both taken steps to cool tensions ahead of a new round of talks. Trade frictions and an escalation of Gulf tensions underscore the risk of supply shocks.

BlackRock Geopolitical Risk Indicators (BGRIs) for global trade and Gulf tensions, 2005–2019

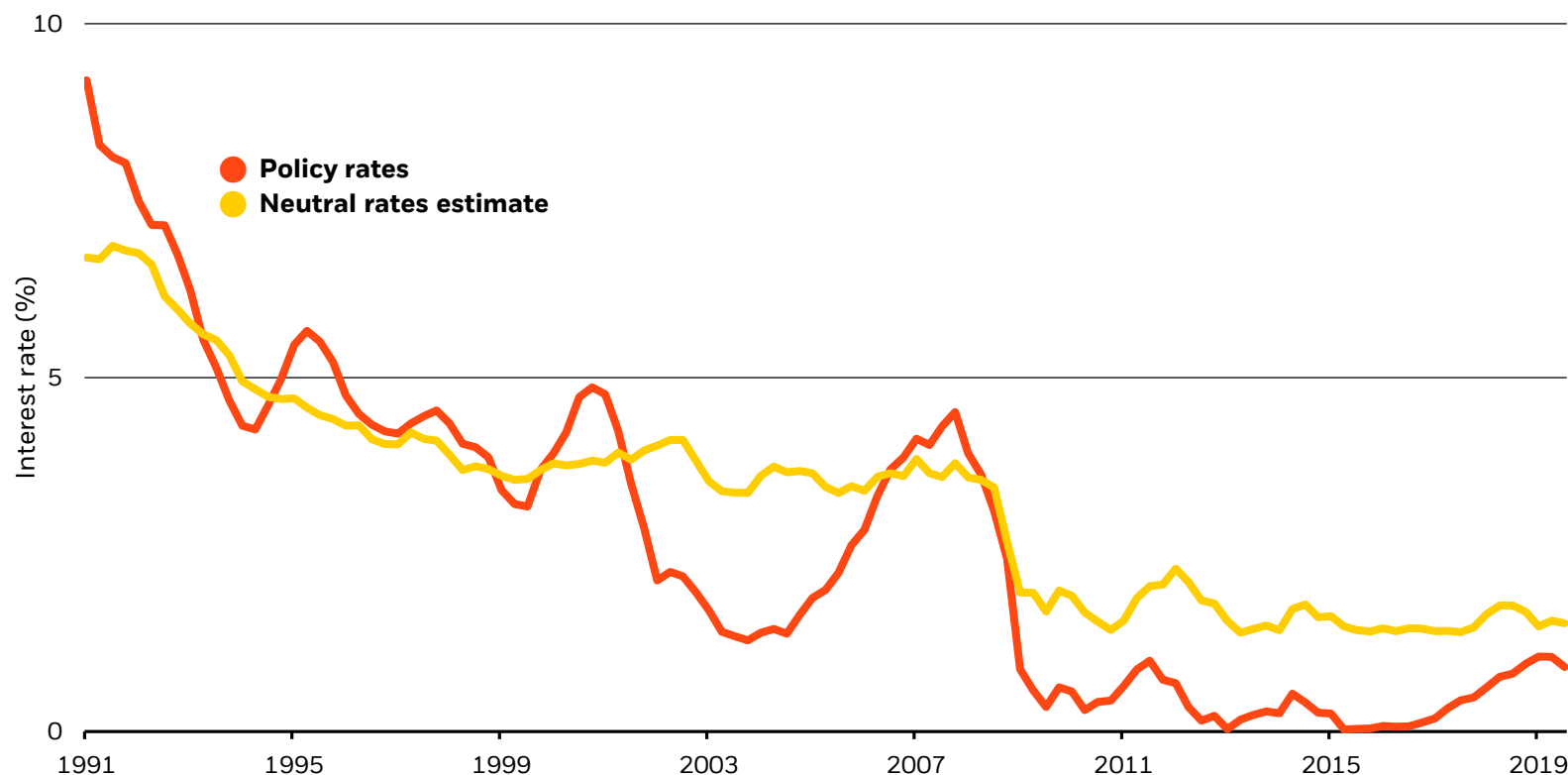


Source: BlackRock Investment Institute, with data from Refinitiv Datastream, September 2019. Notes: See BlackRock's [Geopolitical risk dashboard](#) for full details. We identify specific words related to geopolitical risk in general and to our top-10 risks. We use text analysis to calculate the frequency of their appearance in the Refinitiv Broker Report and Dow Jones Global Newswire databases as well as on Twitter. We then adjust for whether the language reflects positive or negative sentiment, and assign a score. A zero score represents the average BGRi level over its history from 2003 up to that point in time. A score of one means the BGRi level is one standard deviation above the average. We weigh recent readings more heavily in calculating the average. The BGRi's risk scenario is for illustrative purposes only and does not reflect all possible outcomes as geopolitical risks are ever-evolving.

Stimulus is here

Policy rates at major central banks are falling again, backing away from neutral rates. Central bank stimulus from an already loose policy stance should help sustain the expansion.

G3 policy interest rates and estimated neutral rates, 1991-2019



There is no guarantee that any forecast made will come to pass.

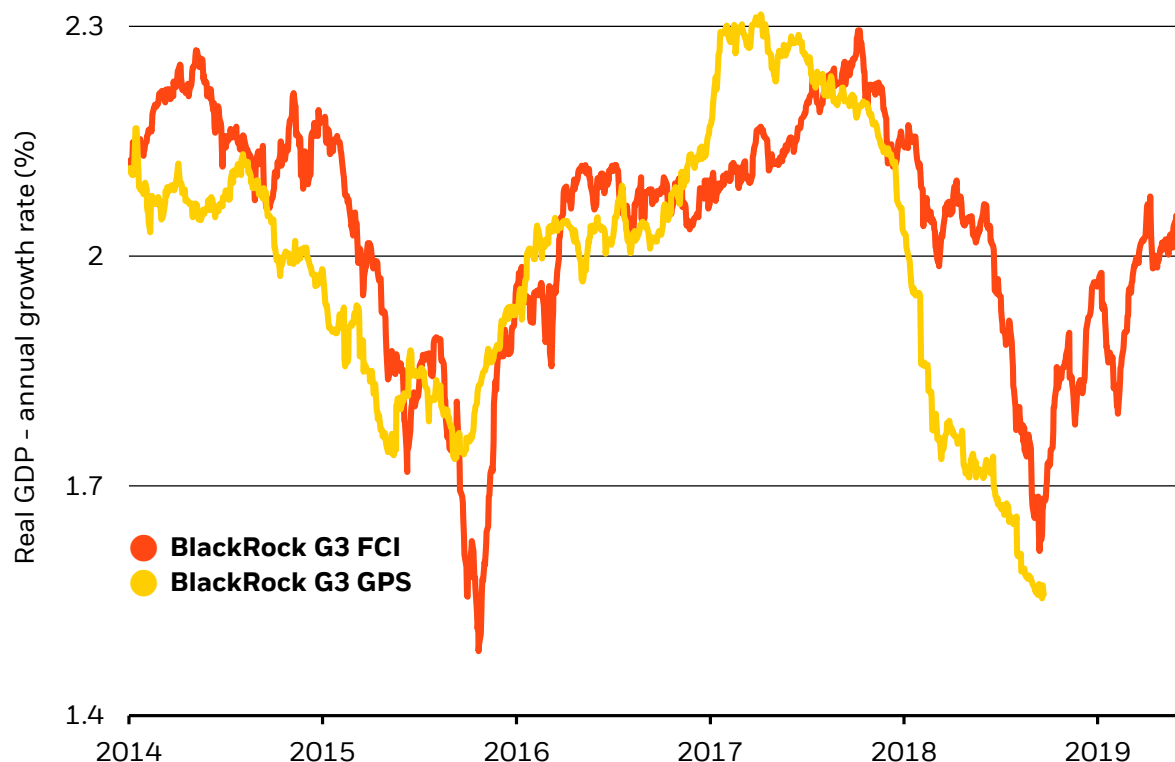
Source: BlackRock Investment Institute, Federal Reserve, National Bureau of Economic Research and European Central Bank, with data from Datastream Refinitiv, September 2019.

Notes: The chart shows our estimate of neutral rates (known as r-star) in nominal terms, adjusting for actual inflation, and the GDP-weighted nominal policy rates of the U.S., euro area and Japan. The neutral rate is an estimate of the short-term rate that neither fosters nor hinders GDP growth. The neutral rates are estimates based on an econometric model from a July 2018 [ECB working paper](#). We detailed our estimates of neutral rates in the November 2018 [Macro and market perspectives](#).

Easy does it

Accommodative financing conditions underpin our belief that weakness in the global industrial sector is unlikely to lead to a broader economic downturn in the near term.

BlackRock G3 Growth GPS and FCI, 2015-2019



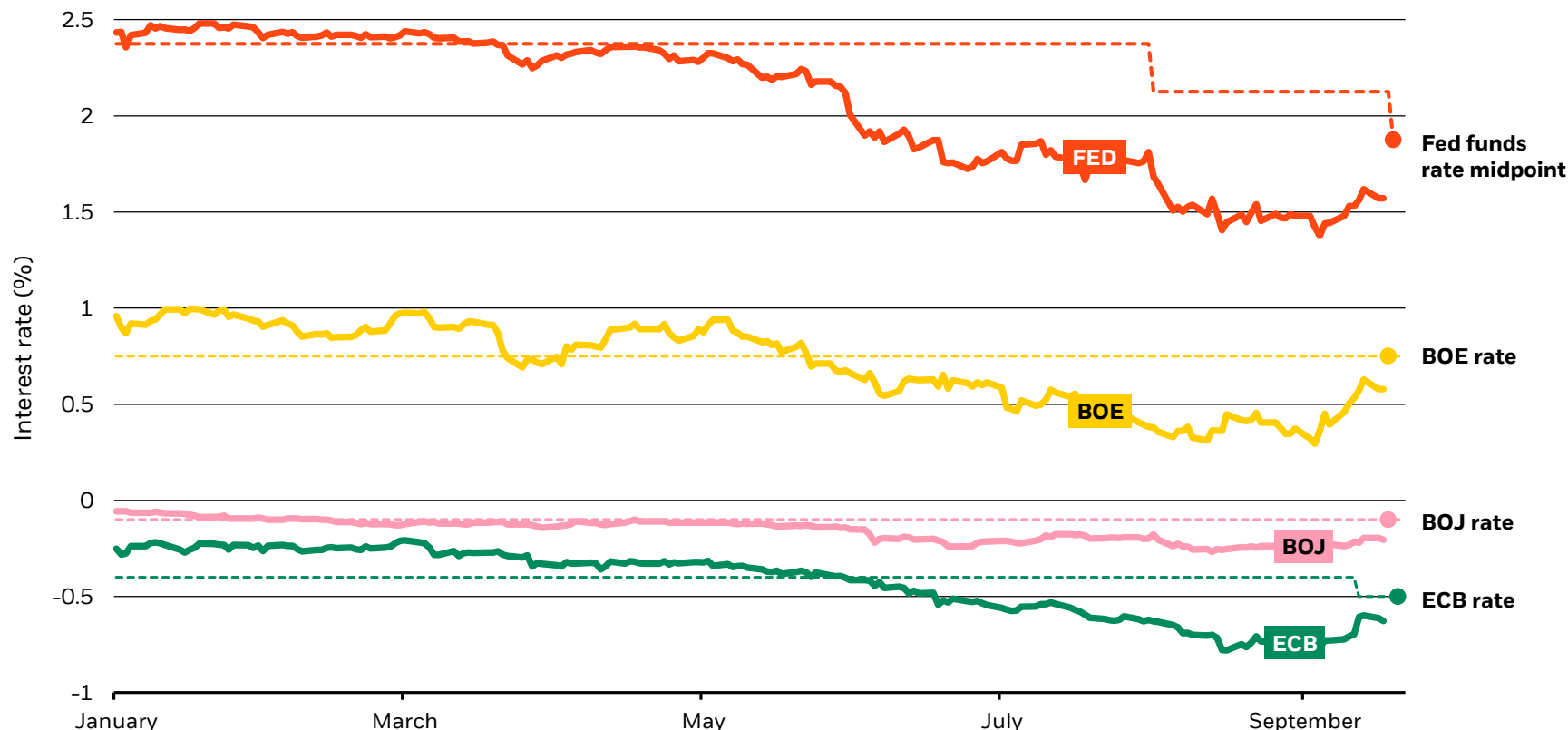
- Easier monetary policy has spurred a swift rebound in our financial conditions indicator (FCI).
- Growth expectations, highlighted by our G3 Growth GPS, are yet to reflect the significant easing of financial conditions. See more on our [Macro dashboard](#).
- Persistent and intensifying trade uncertainty is holding back business spending, in our view.

Source: BlackRock Investment Institute with data from Bloomberg and Consensus Economics, September 2019. Notes: The BlackRock Growth GPS shows where the 12-month forward consensus GDP forecast may stand in three months' time. The orange line shows the rate of GDP growth implied by our financial conditions indicator (FCI), based on its historical relationship with our Growth GPS, shifted forward six months. The FCI inputs include policy rates, bond yields, corporate bond spreads, equity market valuations and exchange rates. Forward-looking estimates may not come to pass.

Even lower for even longer

We see the Fed cutting rates further, but not by as much as what markets are pricing in. The ECB has launched open-ended asset purchases, cut rates and strengthened forward guidance.

One-year forward central bank policy rate pricing



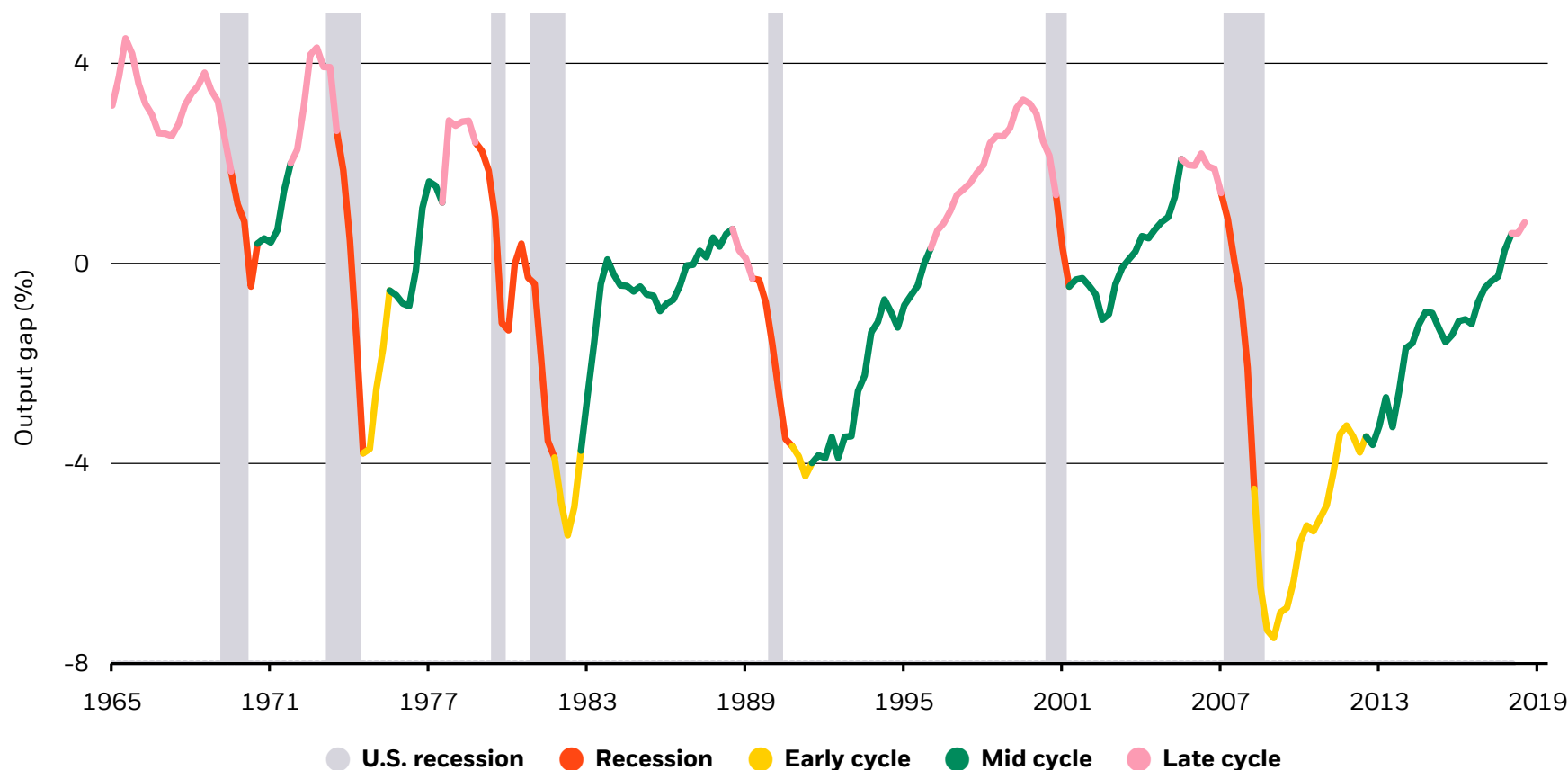
There is no guarantee that any forecasts made will come to pass. Past performance is no guarantee of future results.

Source: BlackRock Investment Institute with data from Bloomberg, as of 17th September 2019. Notes: The chart shows the market pricing of policy rates in overnight index swaps on a one-year horizon starting in one year's time.

Stretching the cycle

The U.S. economy entered the late stage of its expansion earlier this year. Below-trend growth suggests it could revert to mid-cycle conditions in coming months.

Output gap and stages of the U.S. business cycle, 1965-2019

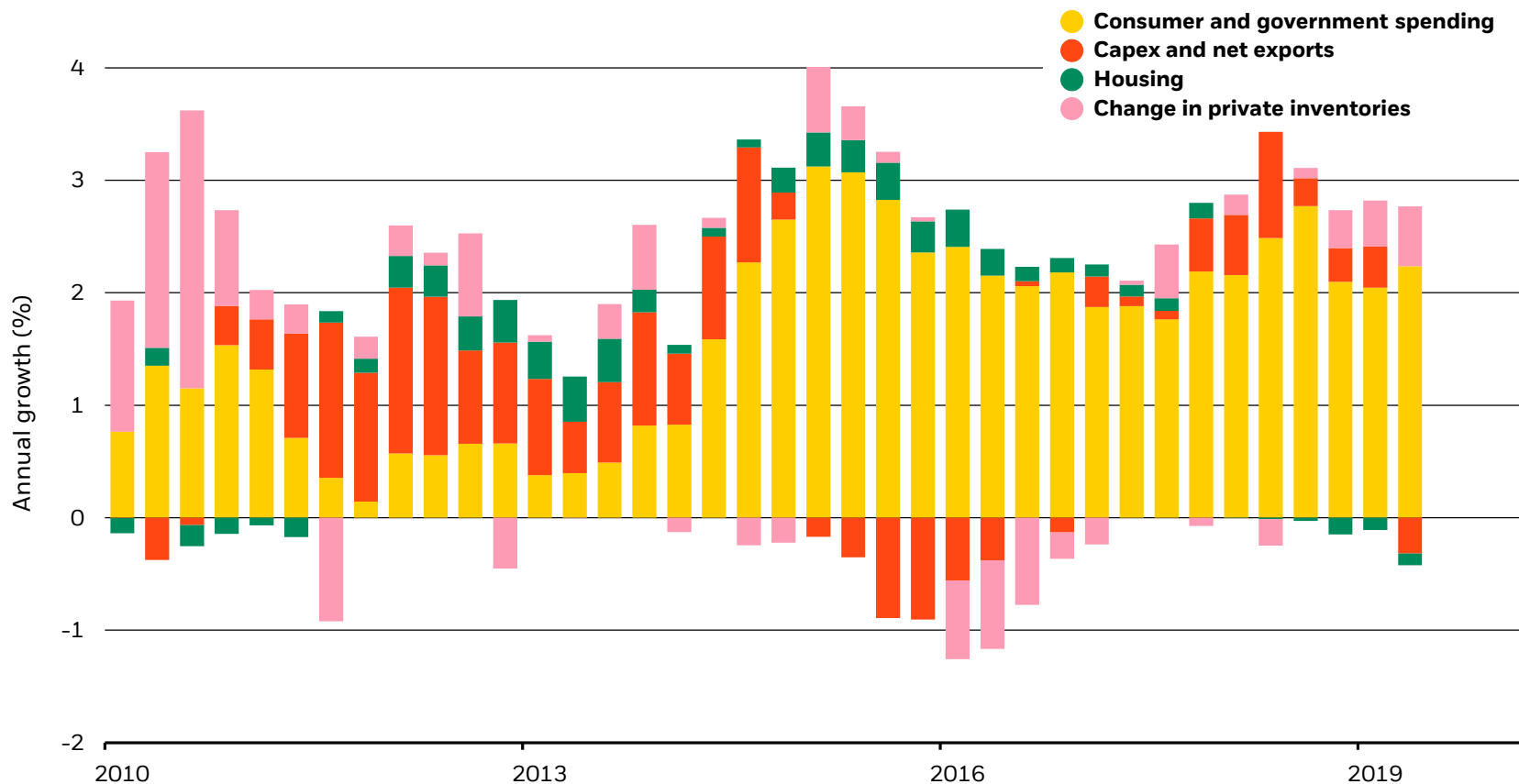


Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, as of July 2019. Notes: This chart shows an estimate of the U.S. output gap (that is, GDP as a percentage of potential GDP). We have classified different time periods as belonging to certain stages of the business cycle. The classification of the stage is done via a 'cluster analysis' that groups together time periods where economic series have behaved in similar ways.

Breaking down U.S. growth

Companies are building up inventories in expectations of tariffs and cutting investment spending. Resilient consumption is helping offset manufacturing weakness.

Composition of U.S. gross domestic product, 2010-2019

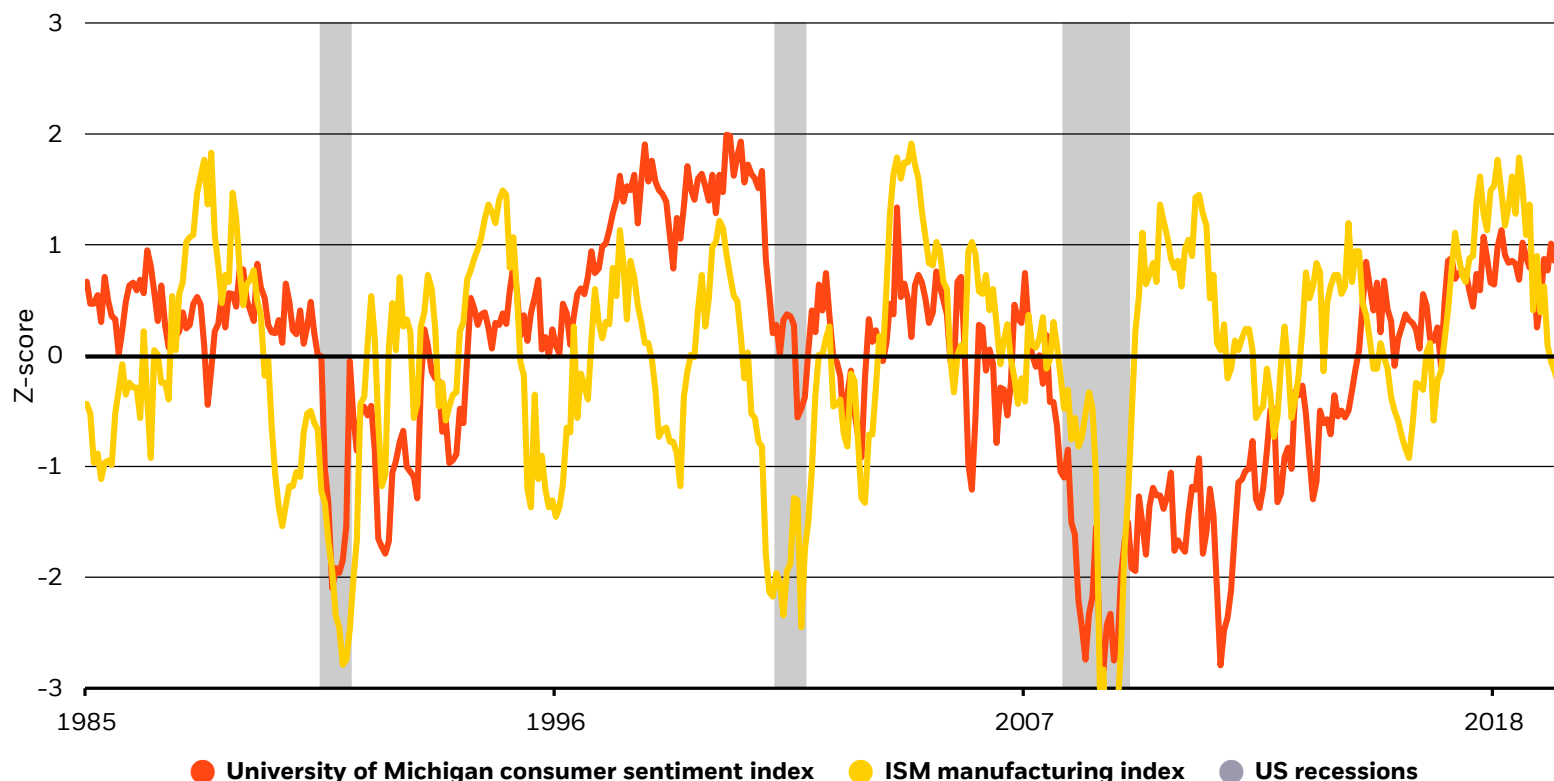


Source: BlackRock Investment Institute, with data from the U.S. Bureau of Economic Analysis, September 2019. Notes: The chart shows the annual rate of U.S. GDP growth broken down by components through the second quarter of 2019. Personal and government spending refers to a combination of personal consumption expenditures; government consumption expenditures and gross investment. Capex refers to non-residential domestic gross investment, and housing refers to residential investment.

A confident consumer

The record-long U.S. economic expansion is underpinned by healthy household spending and looks unlikely to morph into a deeper downturn in the near term.

U.S. consumer sentiment vs manufacturing sector, 1985-2019

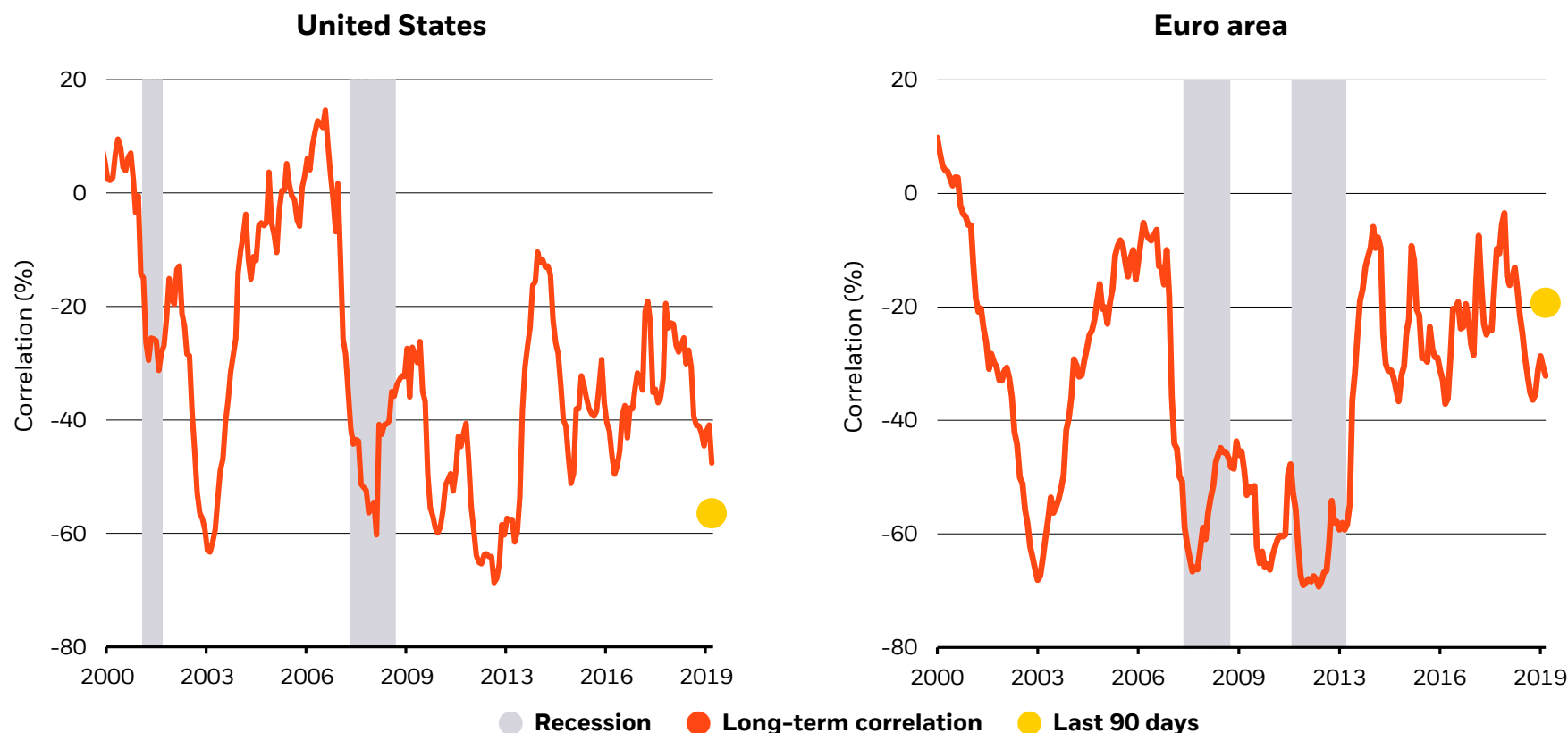


Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, University of Michigan, Institute of Supply Management, National Bureau of Economic Research, September 2019. Notes: The University of Michigan's survey of consumers captures consumer attitudes and expectations. It focuses on three areas: how consumers view prospects for their own financial situation, how they view prospects for the general economy over the near term, and their view of prospects for the economy over the long term. The index is rebased to 100 as of the first quarter of 1966. The ISM manufacturing survey is based on data compiled from purchasing and supply executives across the U.S. manufacturing sector. Z-scores measure how much current readings compare to historical averages over the 1985-2019 period, and are measured in standard deviations.

Raising resilience

Government bonds have played an important role in building portfolio resilience – even at ultra-low yields. In Europe, German bunds are less effective shock absorbers as yields approach their perceived floor.

Stock-bond correlations in the U.S. and Europe, 2000–2019



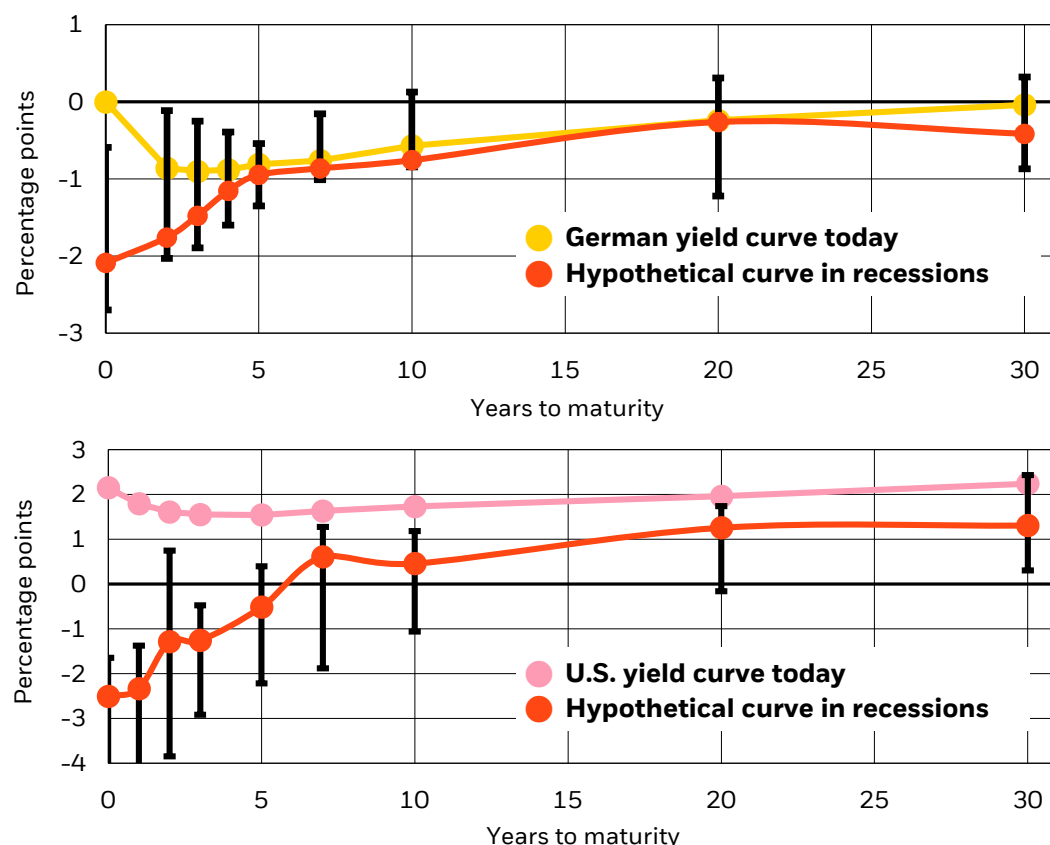
Past performance is not a reliable indicator of current or future results.

Source: BlackRock Investment Institute, with data from Refinitiv Datastream, September 2019. Notes: The charts show the correlations between daily percentage moves for stocks and bonds over a rolling one-year period. The dot shows the correlation over the most recent 90 day period. For the United States, we use the MSCI USA index for stocks and the 10-year Treasury for bonds. For the euro area, we use MSCI Europe ex-UK index and the German 10-year bund. Indexes are unmanaged and not subject to fees. It is not possible to invest directly in an index.

Hitting the limit

Monetary policy is almost exhausted as global interest rates plunge towards zero or below. We believe policymakers should lay the groundwork for a credible plan to navigate the next economic shock.

US and German yield curves, actual vs recession, 2019



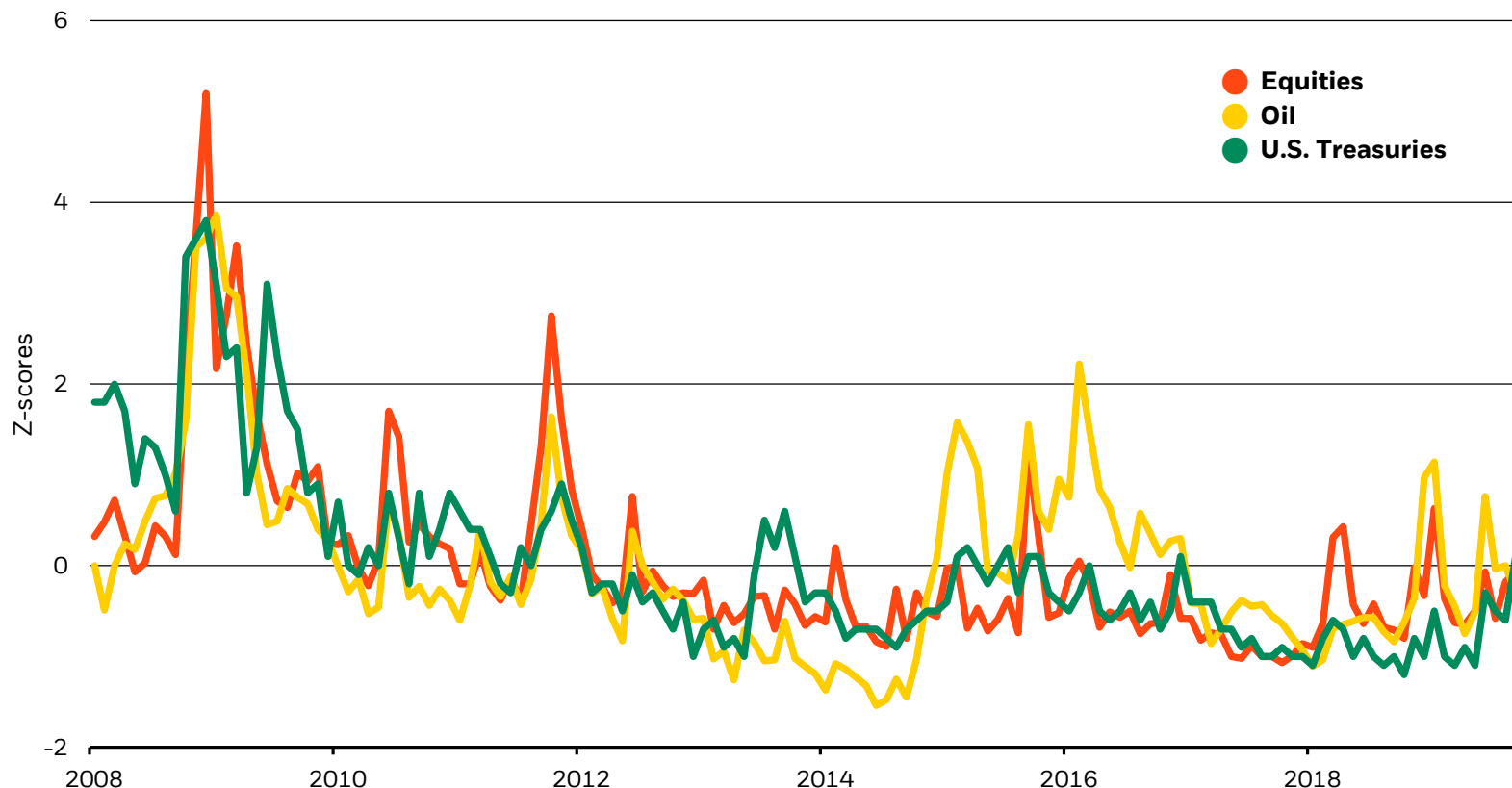
- We expect current central bank easing to be sufficient to sustain the expansion. Yet the plunge in bond yields shows there is not enough policy space to deal with the next downturn.
- The German yield curve is already near levels that would have prevailed based on past recessions. Further support cannot rely on interest rates falling.
- Fiscal policy should play a greater role – but it is unlikely to be effective on its own. An unprecedented response is needed when monetary policy is exhausted and fiscal policy alone is not enough.
- We believe there is a practical way for central banks to “go direct” in providing monetary financing for fiscal policy. Read more in our [August 2019 Macro and market perspectives](#).

Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, September 2019. Notes: The chart shows the current US Treasury and German bund yield curves and a hypothetical representation of the yield curve during recessions, based on the median yield moves during the past five recessions. The light grey bars show the range of the yield moves during those recessions. To account for the changing interest rate environment of the past few decades, the curve moves are adjusted based on the structural decline in neutral rates discussed on this page. Forward looking estimates may not come to pass.

Eyes on volatility

Relatively muted cross-asset volatility suggests markets are not fully pricing in heightened geopolitical risks. We believe central banks' dovish pivot is buying investors time to add resilience to portfolios.

Cross asset volatility, 2008–2019

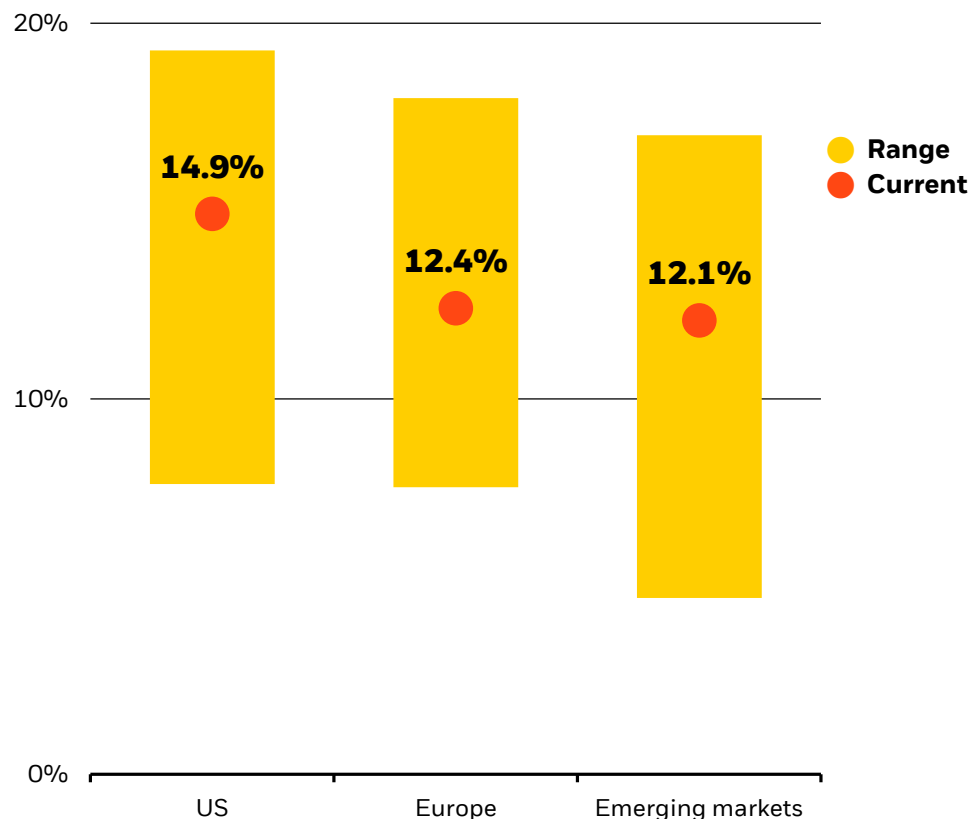


Source: BlackRock Investment Institute with data from Refinitive Datastream, CBOE and Bank of America-Merrill Lynch, September 2019. Notes: The chart shows cross-asset volatility measured as z-scores, or how current readings compare to historical risk-adjusted averages over the 2008-2019 period. Equities are represented by the VIX, Oil by CBOE's oil VIX, and US Treasuries by the BofA-ML's MOVE index.

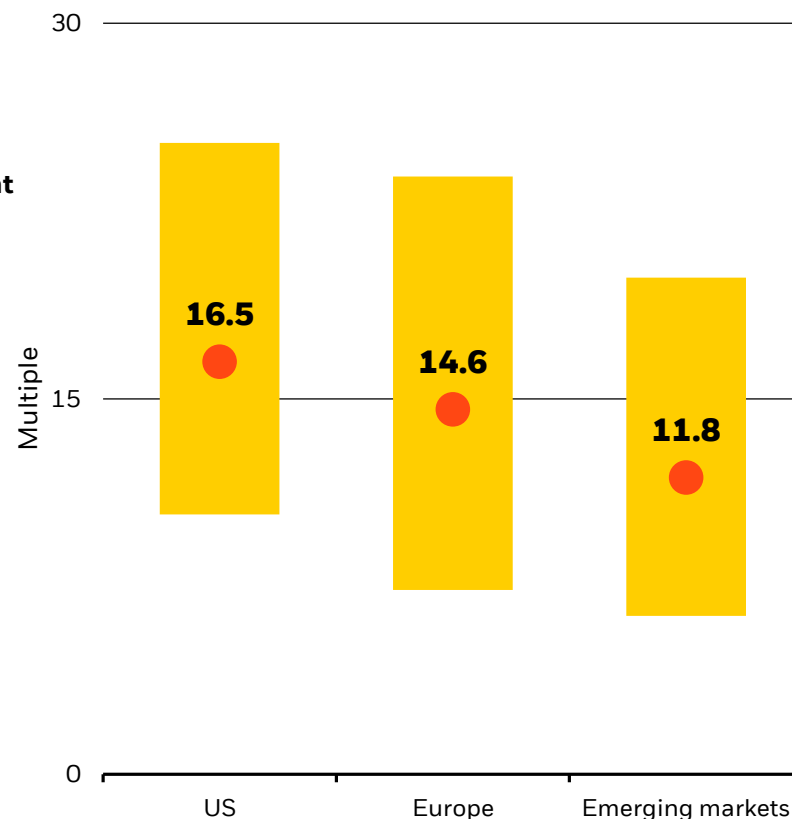
Market views: equities

We remain positive on U.S. equities on reasonable valuations and the concentration of high-quality companies, but rising geopolitical risks challenge our overall preference for equities over bonds.

Return on equity, 1995-2019



Price-to-earnings ratios, 1995-2019



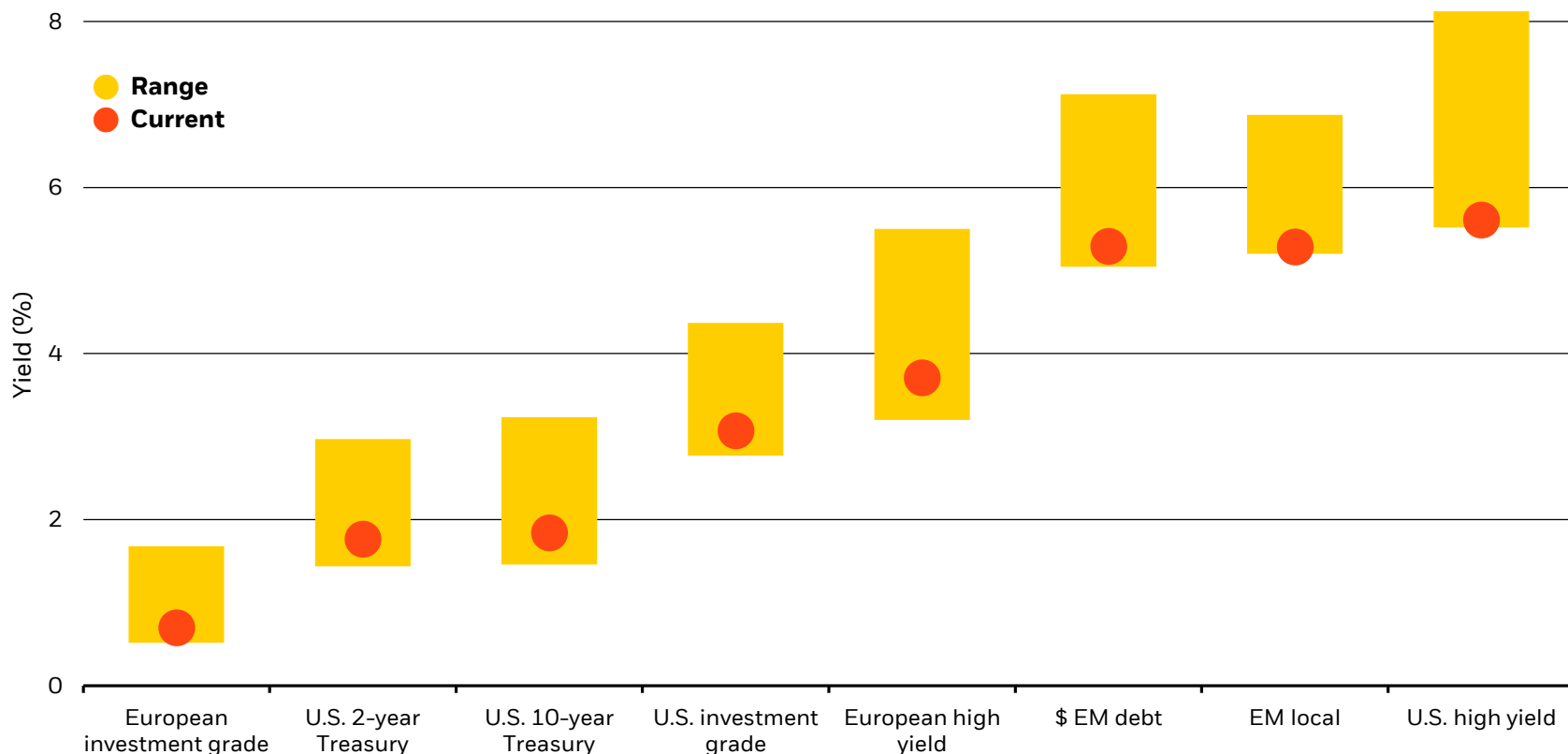
Past performance is not a reliable indicator of current or future results.

Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, September 2019. The bars show the historical ranges for the return on equity and price-to-earnings ratio for each market since 1995. Indices used: MSCI USA Index, MSCI Europe Index, and MSCI Emerging Markets Index. Returns are in local currency. Indexes are unmanaged and not subject to fees. It is not possible to invest directly in an index.

Market views: fixed income

We like sources of coupon income such as EM local debt, despite outsized returns this year. Valuations appear full in many sectors, with yields still near the bottom of historical ranges.

Selected fixed income yields, 2018-2019



Past performance is not a reliable indicator of current or future results.

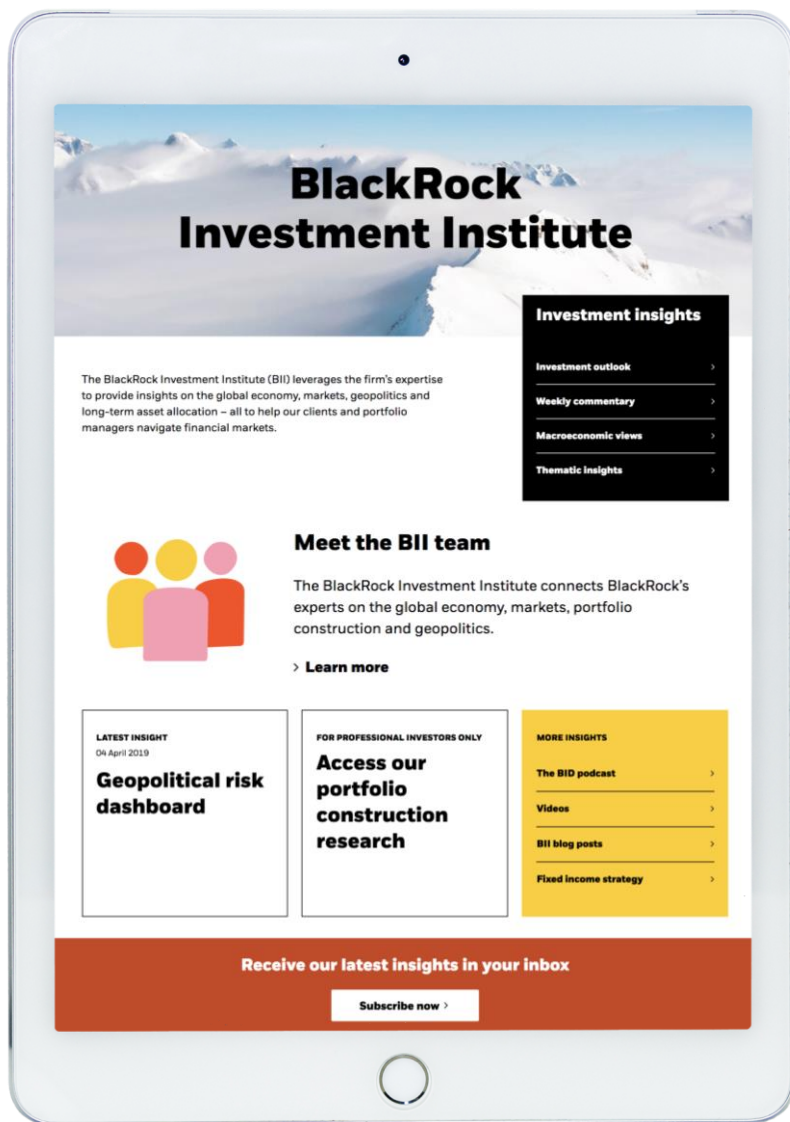
Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, Bloomberg Barclays and J.P. Morgan, September 2019. The bars show the range in yields for each index from the start of January 2018. Indices used: Bloomberg Barclays Pan-European Corporate, Refinitiv 2-year and 10-year benchmark U.S. Treasury, Bloomberg Barclays U.S. Corporate Investment Grade, Bloomberg Barclays Pan-European Corporate High Yield, J.P. Morgan Emerging Market Bond Index Global Diversified, JPM EMBI Global Diversified Index and Bloomberg Barclays U.S. Corporate High Yield Index. Indexes are unmanaged and not subject to fees. It is not possible to invest directly in an index.

Assets allocation views in brief

Six-to-12 month tactical views on selected assets, September 2019

Asset class	View	Comments	▲ Overweight	– Neutral	▼ Underweight
Equities	U.S.	▲ A supportive policy mix and the prospect of an extended cycle underpin our positive view. Valuations still appear reasonable against this backdrop. From a factor perspective we like min-vol, which has historically tended to perform well during economic slowdowns.			
	Europe	– We have upgraded European equities to neutral. We find European risk assets modestly overpriced versus the macro backdrop, yet the dovish shift by the European Central Bank (ECB) should provide an offset. Trade disputes, a slowing China and political risks are key challenges.			
	Japan	▼ We have downgraded Japanese equities to underweight. We believe they are particularly vulnerable to a Chinese slowdown with a Bank of Japan that is still accommodative but policy-constrained. Other challenges include slowing global growth and an upcoming consumption tax increase.			
	EM	– We have downgraded EM equities to neutral amid what we see as overly optimistic market expectations for Chinese stimulus. We see the greatest opportunities in Latin America, such as in Mexico and Brazil, where valuations are attractive and the macro backdrop is stable. An accommodative Fed offers support across the board, particularly for EM countries with large external debt loads.			
	Asia ex-Japan	▼ We have downgraded Asia ex-Japan equities to underweight due to the region's China exposure. A worse-than-expected Chinese slowdown or disruptions in global trade would pose downside risks. We prefer to take risk in the region's debt instruments instead.			
Fixed income	U.S. government bonds	▼ We remain underweight U.S. Treasuries. We do expect the Fed to cut rates by a further quarter percentage point this year. Yet market expectations of Fed easing look excessive to us. This, coupled with the flatness of the yield curve, leaves us cautious on Treasury valuations. We still see long-term government bonds as an effective ballast against risk asset selloffs.			
	U.S. municipal bonds	– Favorable supply-demand dynamics and improved fundamentals are supportive. The tax overhaul has made munis' tax-exempt status more attractive. Yet muni valuations are on the high side, and the asset class may be due for a breather after a 10-month stretch of positive performance.			
	U.S. credit	– We are neutral on U.S. credit after strong performance in the first half of 2019 sent yields to two-year lows. Easier monetary policy that may prolong this cycle, constrained new issuance and conservative corporate behavior support credit markets. High-yield and investment-grade credit remain key part of our income thesis.			
	European sovereigns	▲ The resumption of asset purchases by the ECB supports our overweight, particularly in non-core markets. A relatively steep yield curve – particularly in these countries – is a plus for euro area investors. Yields look attractive for hedged U.S. dollar-based investors thanks to the hefty U.S.-euro interest rate differential.			
	European credit	– Renewed ECB purchases of corporate debt and a “lower for even longer” rate shift are supportive. European banks are much better capitalized after years of balance sheet repair. Even with tighter spreads, credit should offer attractive income to both European investors and global investors on a currency-hedged basis.			
	EM debt	▲ We like EM bonds for their income potential. The Fed's dovish shift has spurred local rates to rally and helped local currencies recover versus the U.S. dollar. We see local-currency markets having room to run and prefer them over hard-currency markets. We see opportunities in Latin America (with little contagion from Argentina's woes) and in countries not directly exposed to U.S.-China tensions.			
	Asia fixed income	– The dovish pivot by the Fed and ECB gives Asian central banks room to ease. Currency stability is another positive. Valuations have become richer after a strong rally, however, and we see geopolitical risks increasing. We have reduced overall risk and moved up in quality across credit as a result.			

Note: Views are from a U.S. dollar perspective as of September 2019. 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.



Get BlackRock Investment Institute content:

blackrock.com/BII

Social content for a U.S. audience:



BLKInsights app



@blackrock



The Bid podcast



Alexa and
Google Assistant

Important information

General disclosure: This material is not intended to be relied upon as a forecast, research or investment advice, and is not a recommendation, offer or solicitation to buy or sell any securities or to adopt any investment strategy. The opinions expressed are as of September 2019 and may change. The information and opinions are derived from proprietary and non-proprietary sources deemed by BlackRock to be reliable, are not necessarily all-inclusive and are not guaranteed as to accuracy. As such, no warranty of accuracy or reliability is given and no responsibility arising in any other way for errors and omissions (including responsibility to any person by reason of negligence) is accepted by BlackRock, its officers, employees or agents. This material may contain 'forward looking' information that is not purely historical in nature. Such information may include, among other things, projections and forecasts. There is no guarantee that any forecasts made will come to pass. Reliance upon information in this material is at the sole discretion of the reader.

In the U.S., this material is intended for public distribution. **In Canada,** this material is intended for permitted clients only. **In the UK and outside the EEA:** This material is for distribution to professional clients (as defined by the Financial Conduct Authority or MiFID Rules) and qualified investors only and should not be relied upon by any other persons. Issued by BlackRock Investment Management (UK) Limited, authorised and regulated by the Financial Conduct Authority. Registered office: 12 Throgmorton Avenue, London, EC2N 2DL. Tel: 020 7743 3000. Registered in England No. 2020394. BlackRock is a trading name of BlackRock Investment Management (UK) Limited. In the EEA, it is issued by BlackRock (Netherlands) BV: Amstelplein 1, 1096 HA, Amsterdam, Tel: 020 – 549 5200, Trade Register No. 17068311. BlackRock is a trading name of BlackRock (Netherlands) B.V. **For qualified investors in Switzerland,** this material shall be exclusively made available to, and directed at, qualified investors as defined in the Swiss Collective Investment Schemes Act of 23 June 2006, as amended. **In South Africa,** please be advised that BlackRock Investment Management (UK) Limited is an authorised financial services provider with the South African Financial Services Board, FSP No. 43288. **In DIFC:** This information 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) and is only directed at 'Professional Clients' and no other person should rely upon the information contained within it. Neither the DFSA or any other authority or regulator located in the GCC or MENA region has approved this information. This information and associated materials have been provided for your exclusive use. This document is not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution would be unlawful under the securities laws of such. Any distribution, by whatever means, of this document and related material to persons other than those referred to above is strictly prohibited. **In Singapore,** this is issued by BlackRock (Singapore) Limited (Co. registration no. 200010143N). **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 China,** this material may not be distributed to individuals resident in the People's Republic of China ("PRC", for such purposes, excluding 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) and does not constitute investment advice or an offer or solicitation to purchase or sell in any securities, BlackRock funds or any investment strategy nor shall any securities be offered or sold to any person in any jurisdiction in which an offer, solicitation, purchase or sale would be unlawful under the securities laws of such jurisdiction. **In Latin America,** for institutional investors and financial intermediaries only (not for public distribution). This material is for educational purposes only and does not constitute investment advice or an offer or solicitation to sell or a solicitation of an offer to buy any shares of any fund or security. If any funds are mentioned or inferred in this material, such funds may not be registered with the securities regulators of any Latin American country and thus, may not be publicly offered in any such countries. The provision of investment management and investment advisory services is a regulated activity in Mexico thus is subject to strict rules. No securities regulator within Latin America has confirmed the accuracy of any information contained herein.

The information provided here is neither tax nor legal advice. Investors should speak to their tax professional for specific information regarding their tax situation. Investment involves risk including possible loss of principal. International investing involves risks, including risks related to foreign currency, limited liquidity, less government regulation, and the possibility of substantial volatility due to adverse political, economic or other developments. These risks are often heightened for investments in emerging/developing markets or smaller capital markets

© 2019 BlackRock, Inc. All Rights reserved. **BlackRock**, is a registered trademark of BlackRock, Inc., or its subsidiaries in the United States and elsewhere. All other trademarks are those of their respective owners.