May 2022

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# Global outlook – Q2 2022 update

BlackRock Investment Institute

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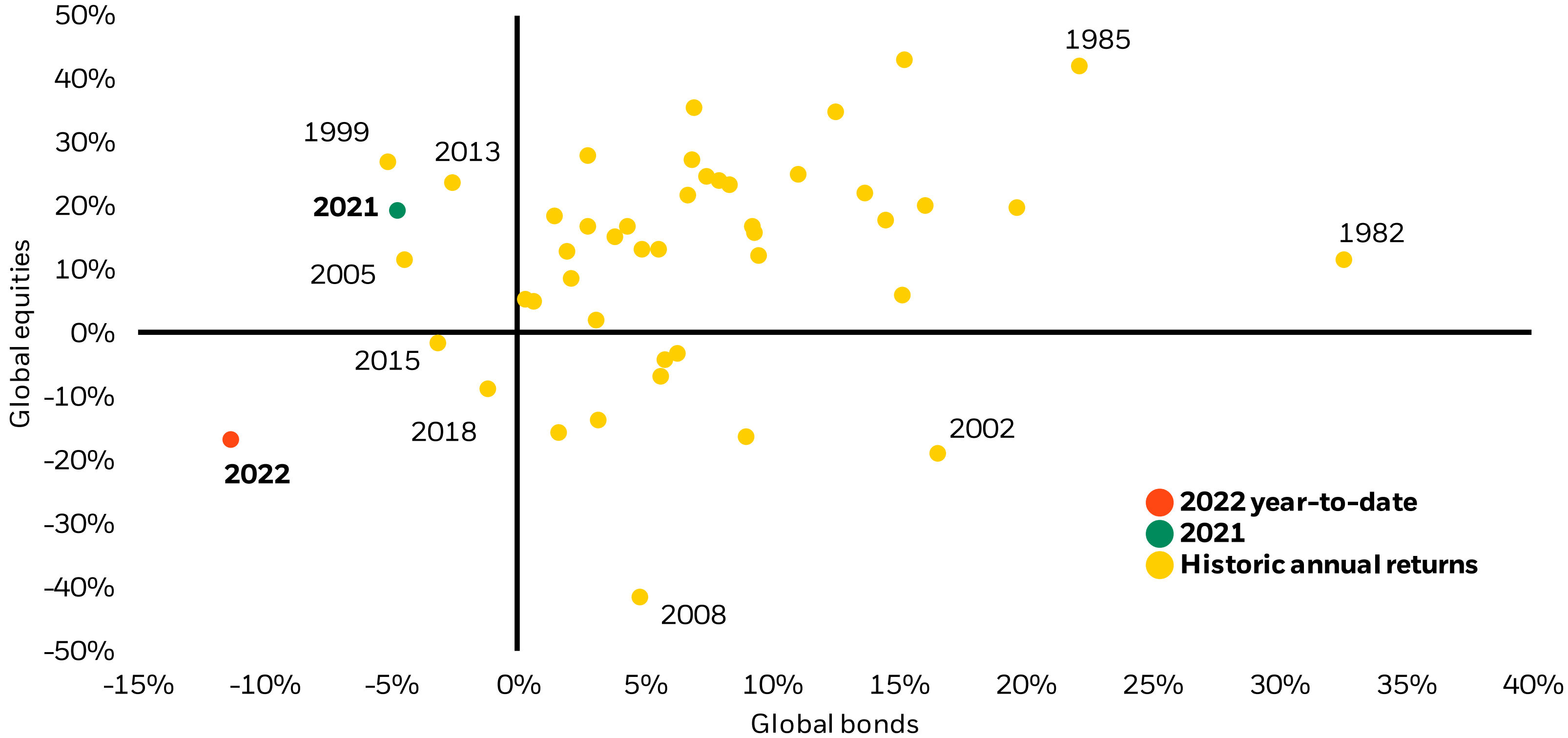
# A historically challenging market regime

Both stocks and bonds are down year-to-date as policy confusion and Russia's invasion roil markets. We still see stocks up and bonds down for a second straight year – a first since data started in 1977.

**Global equities vs. global bonds, annual returns, 1977-2022**



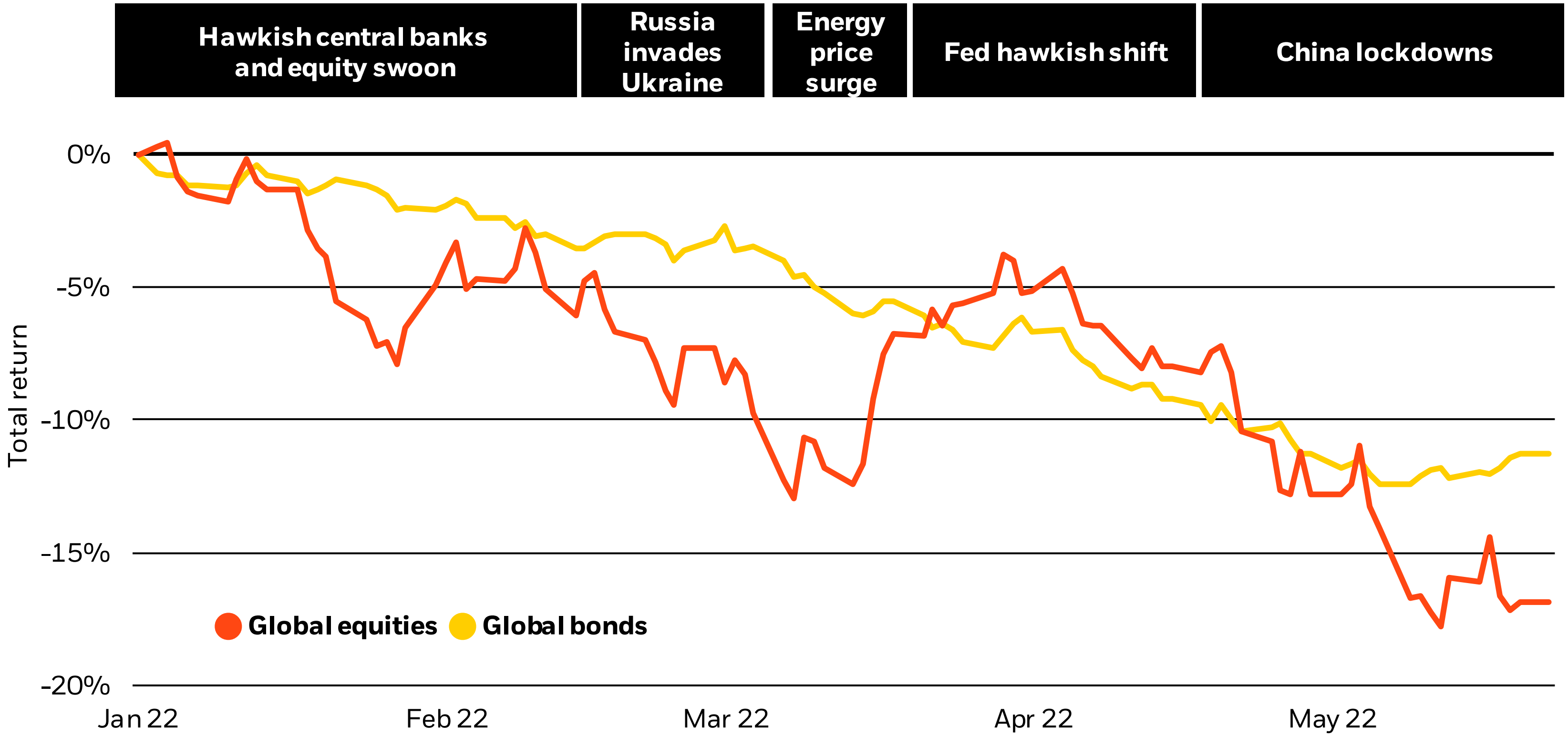

**Past performance is not a reliable indicator of current or future results. Indexes are unmanaged and not subject to fees. It is not possible to invest directly in an index.**

Sources: BlackRock Investment Institute with data from Refinitiv Datastream and Bloomberg, May 2022. Notes: The chart shows annual returns for global equities and bonds in U.S. dollar terms from 1977-2021. Index proxies are the MSCI All-Country World index for equities (MSCI World before 1988) and Bloomberg Global Aggregate index for bonds (U.S. Aggregate before 1991).

# War, energy shock and the Fed's pivot – in a single quarter

The tragic war in Ukraine, a global energy shock and the Fed's surprisingly hawkish pivot – all in the space of a few months – have sparked reassessments of macro scenarios among market participants.

**Global equities and bond total returns, 2022**

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Sources: BlackRock Investment Institute with data from Refinitiv Datastream and Bloomberg, May 2022. Notes: The chart shows year-to-date to returns for the MSCI ACWI index and Bloomberg Global Aggregate index for bonds since the start of the year.

## Macro landscape

● Our base case ● Market worry ● Key risk

### Living with inflation
Higher inflation meets with a muted central bank response, keeping real rates historically low. Stocks can thrive, but bonds still suffer as the yield curve modestly steepens.

### Safety premium questioned
The perceived safety of government bonds is questioned amid rising debt levels. Investors demand larger compensation for the risk of holding long-term bonds. The yield curve steepens sharply. Yet this is a relative asset shift: equities can still do well.

### Productivity boom
Sustained capital investment boosts potential growth, keeping the macro environment disinflationary. The Fed is patient and keeps policy loose, with rates below neutral. The yield curve steepens, real yields stay low, and risk assets do well.

### Slamming the brakes
Higher energy and commodity prices slow growth, particularly in Europe. Central banks revert to old policy responses to higher, supply-driven inflation. This hits activity, slows growth further and sparks a surge in long-term yields. Result: recession with high inflation. The yield move hits stocks hard.

### Runaway inflation
Inflation expectations become unanchored amid the energy shock and geopolitical tensions. A messy transition to net zero could exacerbate this. 1970s-style stagflation is back. Yields surge across the curve and risk assets sell off.

### Stagnation
Growth slumps. Inflation pressures abate as central banks cannot revive growth and inflation. The yield curve flattens, and equities fall.

### Classic risk-off
Asset bubbles form and burst. Long-term yields fall sharply amid a flight to perceived safety and the term premium turns negative again. Risk assets suffer.

Global equities: + / −

Global bonds: − / +

Sources: BlackRock Investment Institute, March 2022. Notes: The schematic shows hypothetical macro and policy outcomes. These are our views on the implications for equities and government bonds as of May 2022. For illustrative purposes only. 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 funds, strategy or security in particular.

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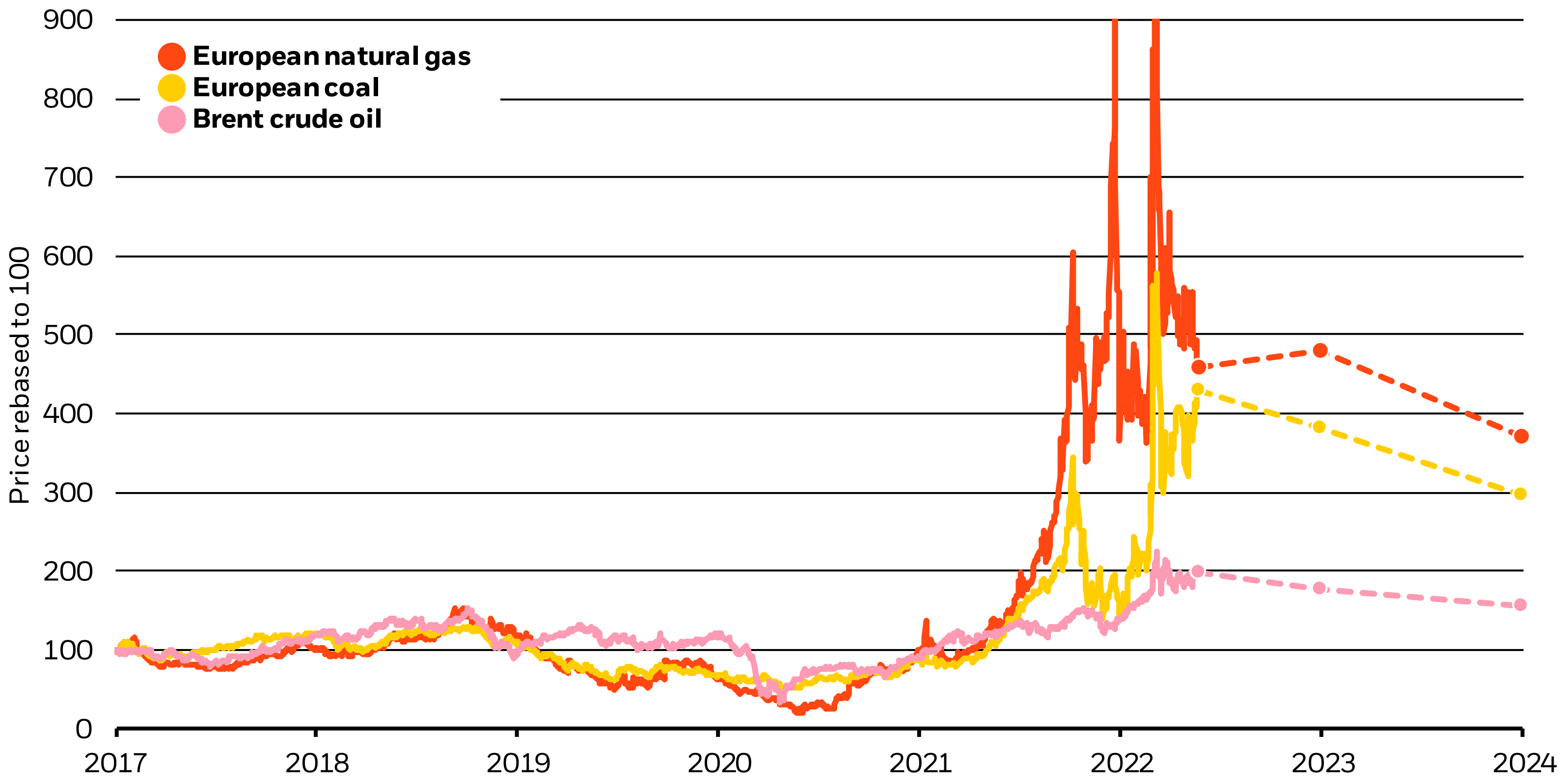
# Western nations have quickly prioritized energy security

Russia's invasion of Ukraine has stoked a drive for energy security among Western nations and a further surge in energy prices, particularly in Europe where prices had already soared on tight supply.

## Futures prices of European coal and natural gas, and Brent crude oil, 2017–2024

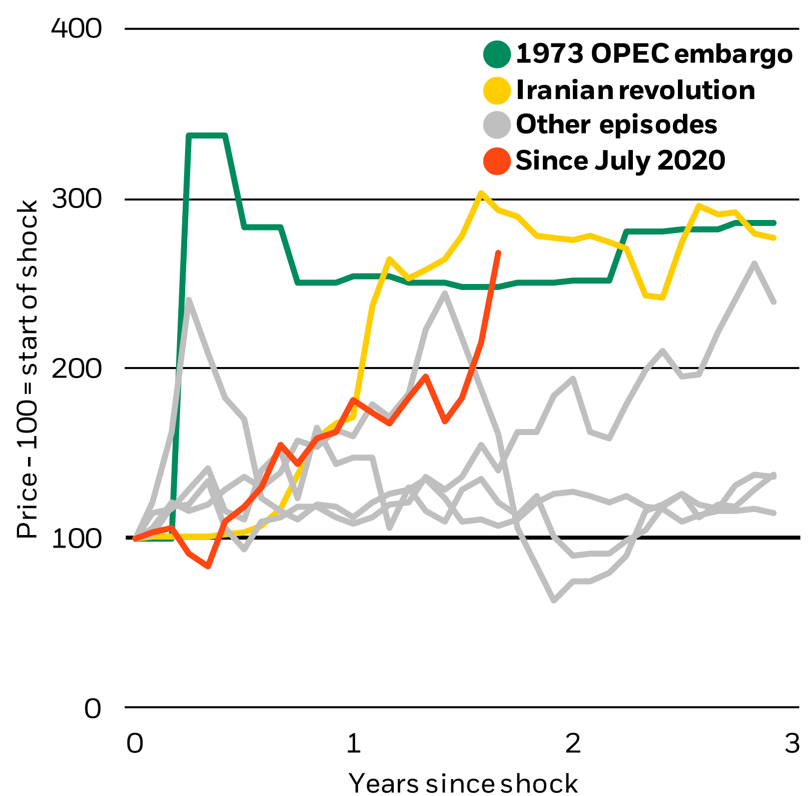



**Past performance is not a reliable indicator of current or future results.** Sources: BlackRock Investment Institute, with data from Refinitiv, May 2022. Notes: The chart shows natural gas, coal and crude oil prices rebased to 100 at the start of 2017. We use the European Energy Derivatives Exchange natural gas futures, ICE Rotterdam coal futures and Brent crude oil futures to represent natural gas, coal and oil respectively. The dots show futures prices for contracts that expire in December 2023 and December 2024.

# Energy supply shock on top of restart-driven inflation

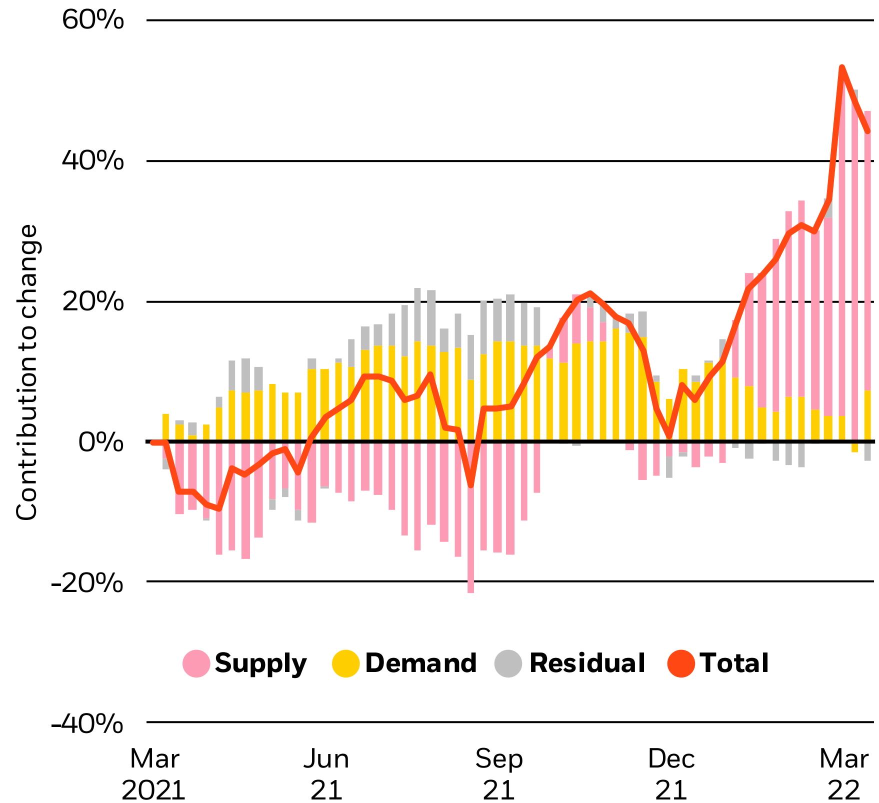
This year's energy supply shock builds on the restart driven jump in energy prices in 2021. Higher energy costs – the main macro transmission channel from the Ukraine conflict – are stagflationary.

### Brent crude oil prices vs. past shocks




Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, March 2022. Note: The chart shows the evolution of Brent oil prices over historical episodes of shocks to energy, as defined by Hamilton (2011), 'Historical oil shocks', NBER. Data are monthly and assume that the latest daily price is projected forward for the remainder of the month to calculate the current monthly average.

### U.S. crude oil price driver breakdown, 2021-22

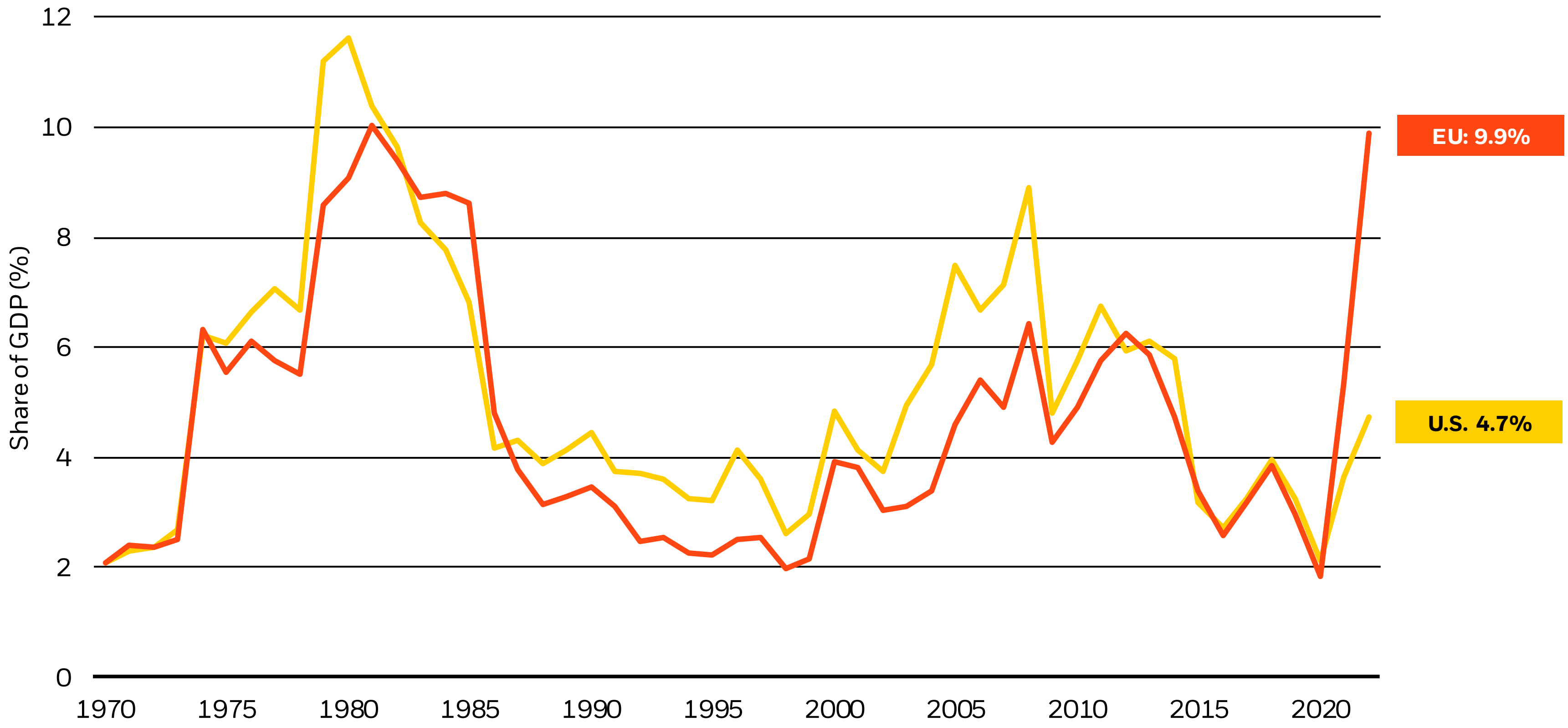



Sources: BlackRock Investment Institute and Federal Reserve Bank of New York, with data from Haver Analytics, March 2022. Note: the chart shows the breakdown of changes in oil prices since March 2021 into different drivers – demand, supply, and other factors – resulting from a model of oil prices developed by the NY Federal Reserve.

# Energy shock a much bigger deal for Europe

The hit to euro area growth, with its heavy reliance on Russian gas, could be large on top of higher inflation. The current energy burden in Europe is more than twice that of the U.S., risking stagflation.

## Energy burden as share of GDP, 1970–2022

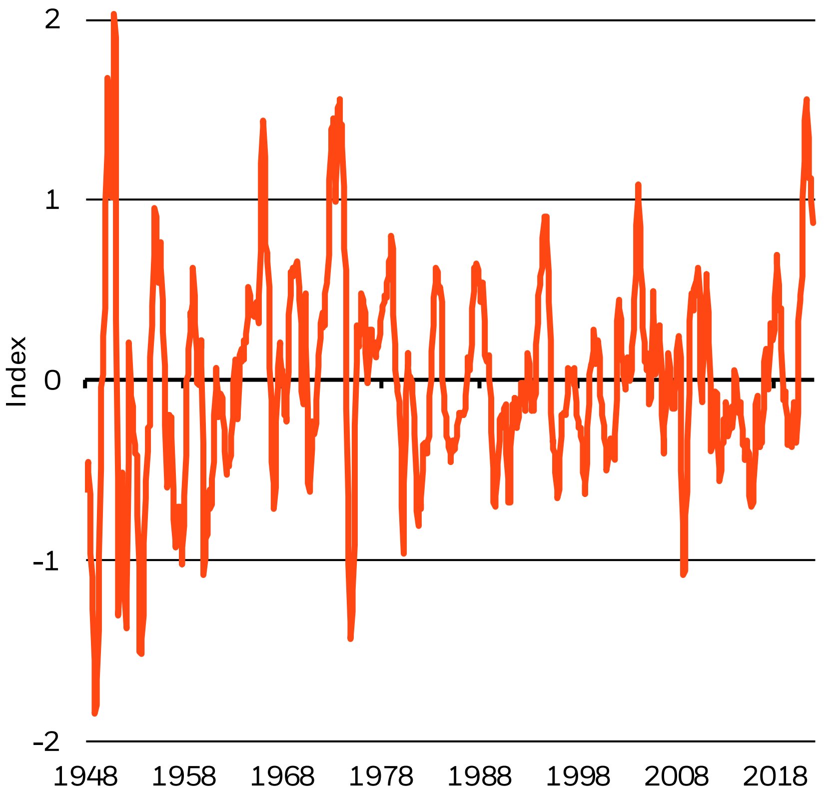



Sources: BlackRock Investment Institute and BP Statistical Review of World Energy 2021, with data from Haver Analytics, May 2022. Notes: The chart shows the cost of oil, gas and coal consumption in the European Union and U.S. as a share of GDP. We use regional energy prices and divide by GDP in U.S. dollars. Data for 2022 are based on IMF's latest GDP forecasts and the year-to-date average of daily commodities prices

# Supply disruptions already elevated before war

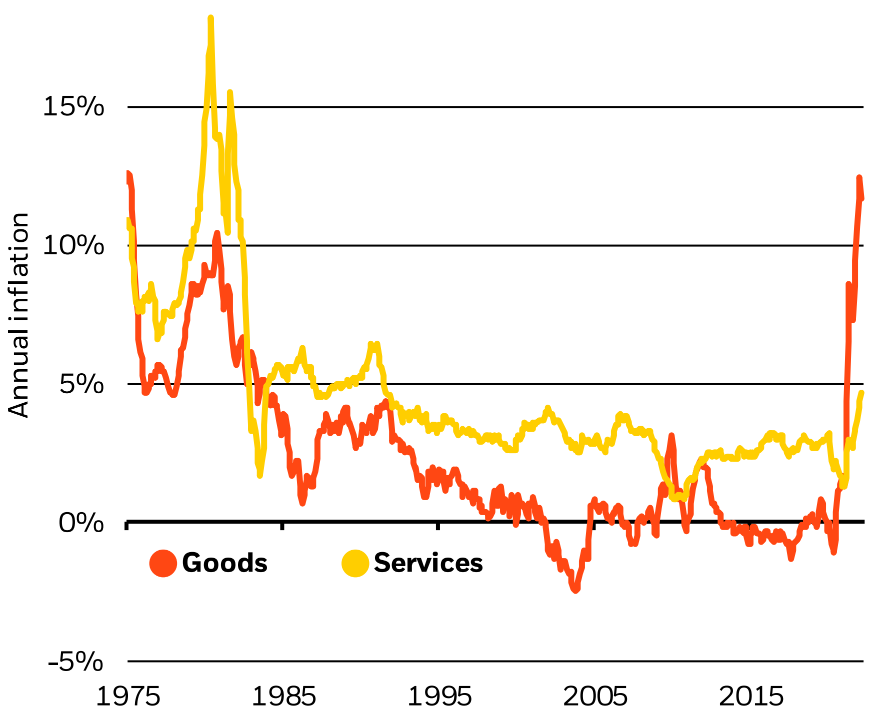
Highly unusual supply shocks drove inflation higher due to the changing mix of consumer spending between goods and services, creating historically high bottlenecks and constraints.

## U.S. supply chain constraints, 1948–2022




Sources: BlackRock Investment Institute, and Institute for Supply Management, with data from Haver Analytics, May 2022. Note: The index of manufacturing supply chain constraints is based on ISM survey indicators: supplier delivery times, backlog of orders, prices paid and inventories.

## U.S. CPI inflation breakdown, 1975–2022

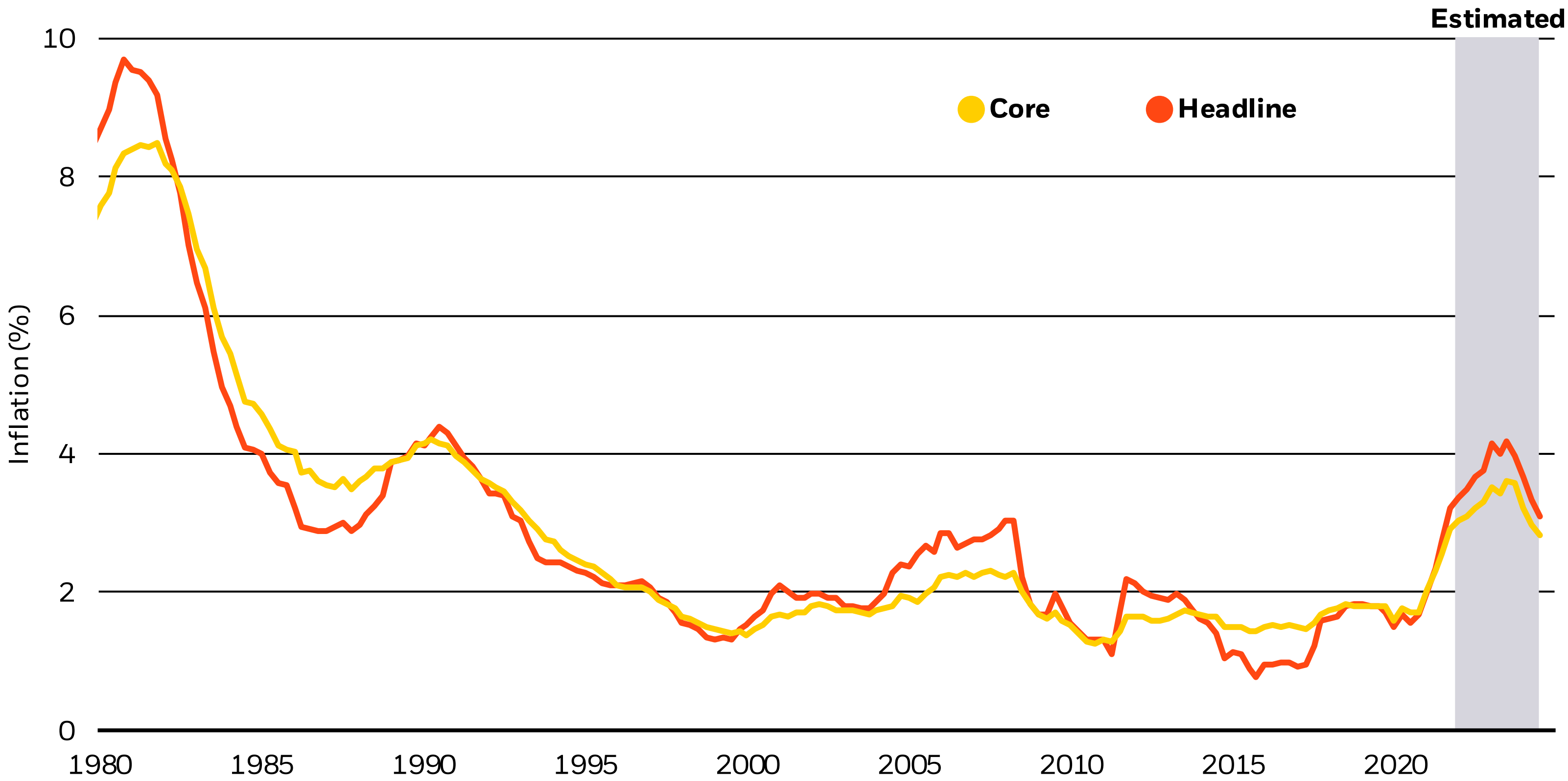



Sources: BlackRock Investment Institute, and U.S. Bureau of Labor Statistics, with data from Haver Analytics, May 2022. Note: The orange and yellow lines show core goods and core services CPI inflation respectively, measured by the year-on-year percent change in prices.

# A key risk: inflation expectations become de-anchored

The big risk we see: higher near-term inflation becomes embedded in expectations, forcing central banks to slam the policy brakes with sharply higher rates, crushing demand to reset expectations.

**Average U.S. PCE inflation, 1980–2022**

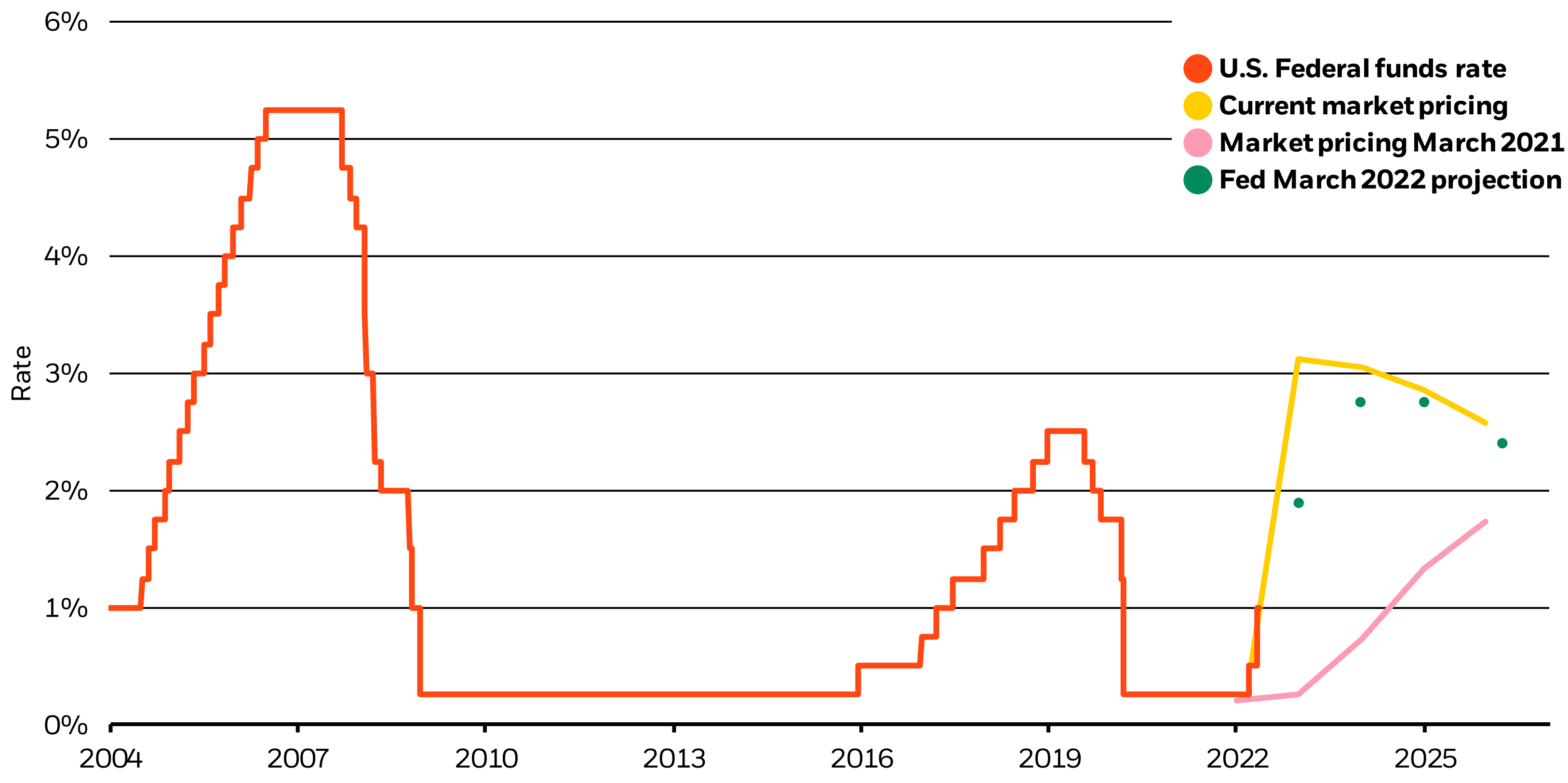



Sources: BlackRock Investment Institute, U.S. Bureau of Economic Analysis, Bloomberg, Federal Reserve Board, with data from Haver Analytics, March 2022. Notes: The chart shows the 3-year average annualized inflation rates for headline U.S. PCE inflation (orange) and core PCE inflation (yellow). Future values are derived from Bloomberg consensus forecasts up to 2022Q3, and thereafter from Federal Reserve projections published in the March 2022 FOMC Summary of Economic Projections. Forward-looking estimates may not come to pass.

# Markets starting to price in a more aggressive Fed

The Fed struck a surprisingly hawkish tone in kicking off its hiking cycle. We see a higher risk of the Fed slamming the brakes on the economy as it may have talked itself into a corner.

### U.S. policy rate pricing current vs. year ago, 2004-2025



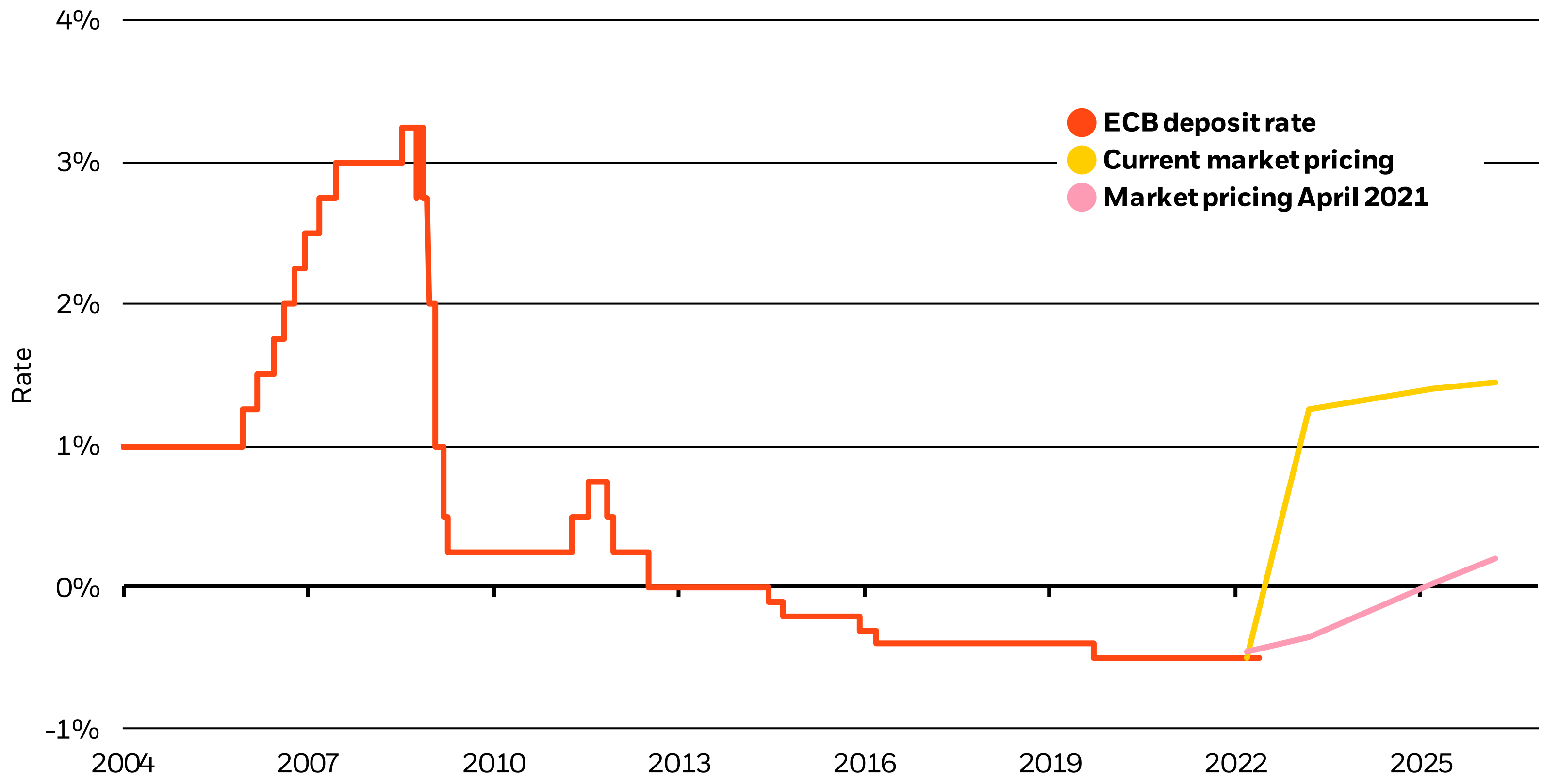

**Past performance is not a reliable indicator of current or future results. Indexes are unmanaged and not subject to fees. It is not possible to invest directly in an index.**

Sources: BlackRock Investment Institute, with data from Haver Analytics and Refinitiv Datastream, May 2022. Notes: The left chart shows historical fed funds rate, current and year-ago market pricing in forward overnight index swaps and the Fed's March 2022 projection based on the median dot of policymaker projections for the end of each year. The final green dot represents the Fed's long-term policy rate expectation.

# Growth shock to shape ECB policy normalization

Growth shock to the euro area implies the ECB has less to do to get to neutral policy. The ECB has emphasized flexibility on kicking off hikes, and we think market pricing this year is too aggressive.

**Euro area policy rate pricing current vs. year ago, 2004-2025**



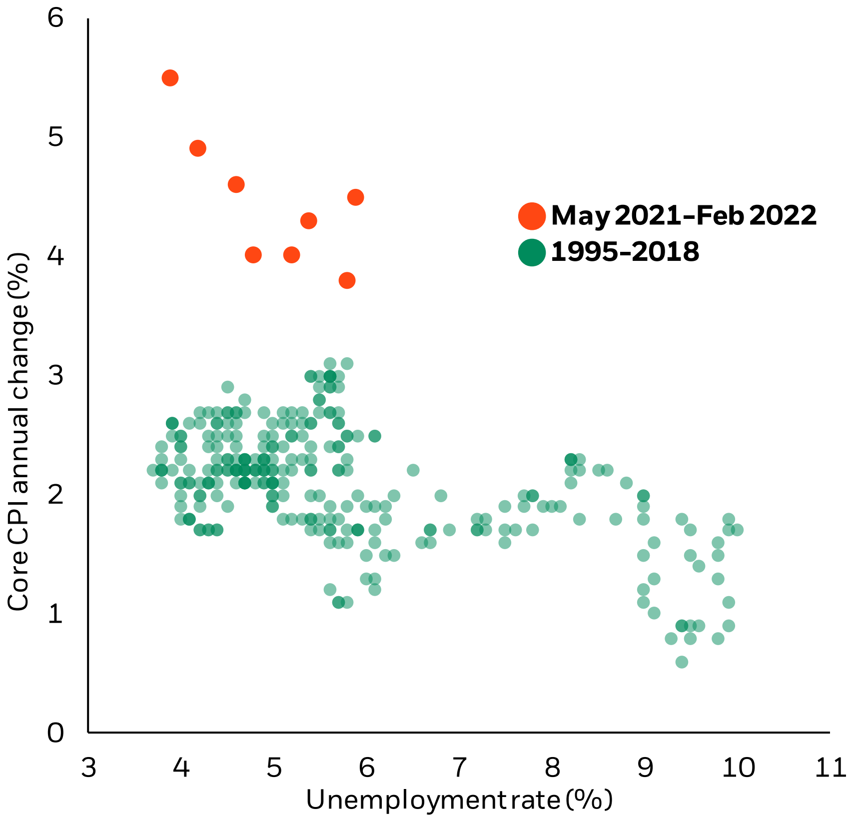

Past performance is not a reliable indicator of current or future results. Indexes are unmanaged and not subject to fees. It is not possible to invest directly in an index.

Sources: BlackRock Investment Institute, with data from Haver Analytics and RefinitivDatastream, May 2022. Notes: The chart shows the European Central Bank's current deposit rate against the latest market pricing vs. a year ago.

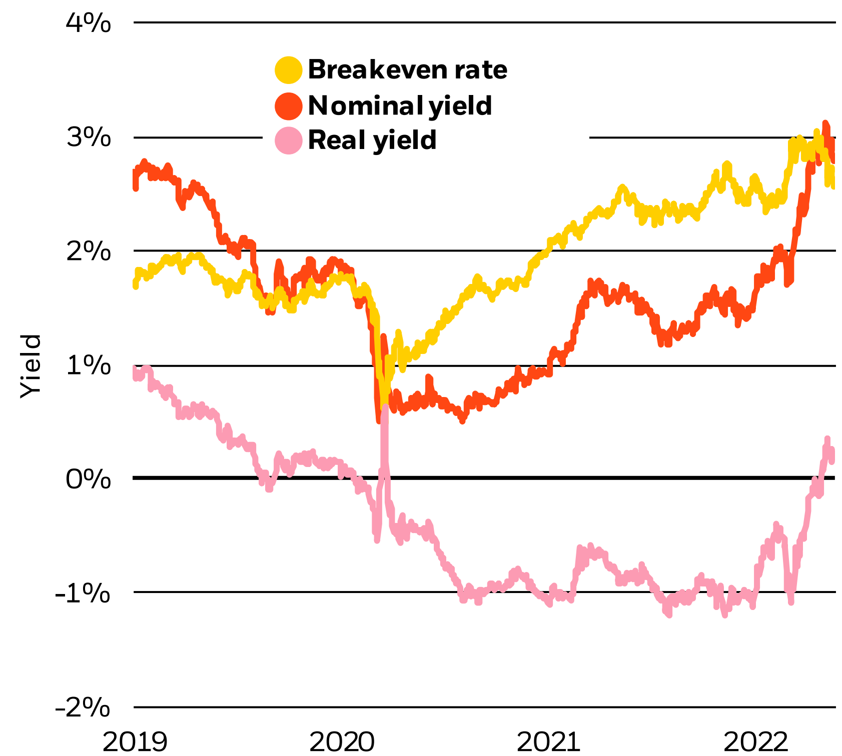
# We see central banks living with inflation

Raising policy rates to restrictive levels to curb inflation would destroy demand and boost unemployment. We believe central banks will ultimately live with inflation, keeping real yields low.

## U.S. unemployment and inflation, 1995-2021




## U.S. Treasury 10-year yield breakdown, 2019-22

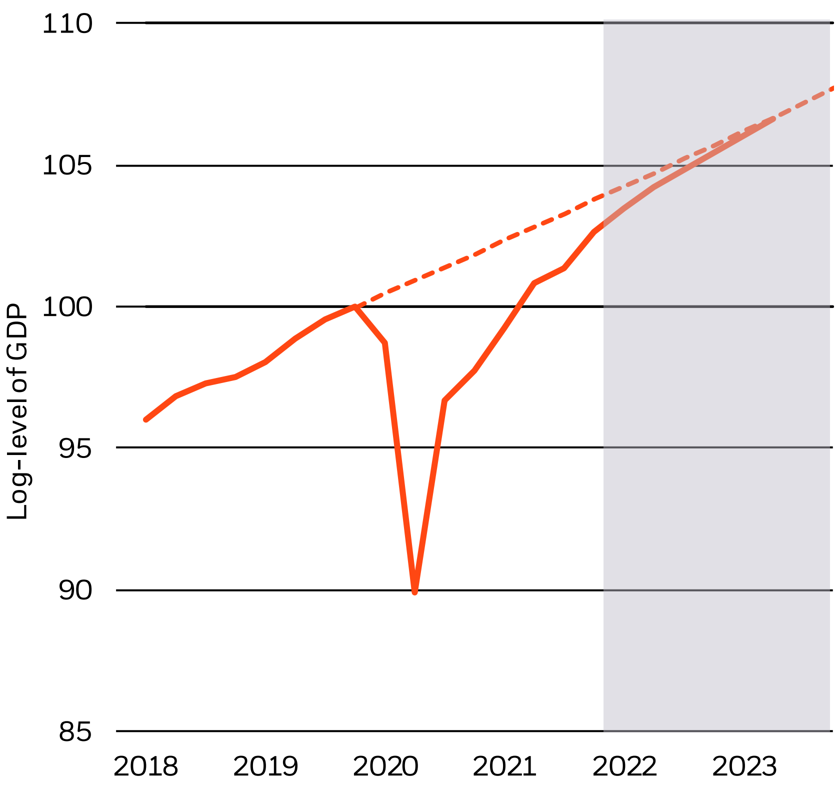



**Forward looking estimates may not come to pass.** Sources: BlackRock Investment Institute, U.S. Bureau of Economic Analysis, Eurostat, Reuters News with data from Haver Analytics, May 2022. Notes: The left chart shows the U.S. unemployment rate (horizontal axis) compared with the U.S. annual core inflation rate (measured by the year on year percentage change) for different periods (vertical axis). The green dots show the period January 1995 - December 2018, and the orange dots show May 2021 to present. All data are at monthly frequency. The right chart shows the U.S. 10-year Treasury yield broken down as nominal yield, inflation breakeven and real yield.

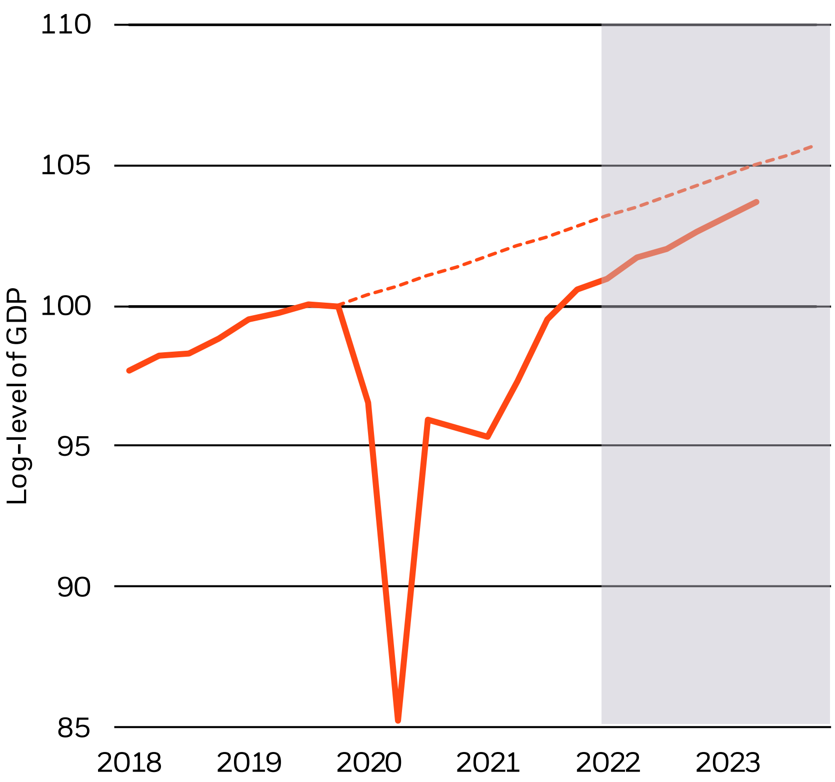
# Restart dynamics still fundamental driver of growth

The strong restart momentum going into the Ukraine crisis should help cushion the stagflationary impact of supply shocks – particularly in energy prices.

## U.S. GDP and projection, 2018–2023




## Euro area GDP and projection, 2018–2023




**Forward looking estimates may not come to pass.** Sources: BlackRock Investment Institute, U.S. Bureau of Economic Analysis, Eurostat, Bloomberg with data from Haver Analytics, March 2022. Notes: The charts show actual GDP and consensus projections (as of 23 March 2022) for the U.S. and Euro area in orange. The gray shaded area denotes the consensus forecast period. The dashed lines show projections of trend growth starting in Q4 2019 to illustrate what GDP might have been had it grown at pre-Covid trend from 2020 onwards. The trend growth assumptions reflect the likely growth of potential output in the run-up to the Covid-19 shock. The scale is expressed as the log-level of GDP.

# Snapshot of our views – May 2022

## Latest directional views

| | Strategic view | Tactical view |
|---|---|---|
| Equities | +2 | Neutral |
| Credit | -1 | Neutral |
| Govt bonds | -1 | -1 |

We stay overweight equities in our strategic views, yet are trimming our overall tilt as the relative appeal versus bonds has diminished. Incorporating climate change in our expected returns brightens the appeal of developed market equities given the large weights of sectors such as tech and healthcare in benchmark indices. Tactically, we downgrade DM equities to neutral due to a higher risk of central banks overtightening policy and a deteriorating global growth backdrop.

We are underweight credit on a strategic basis against a backdrop of rising interest rates. We prefer to take risk in equities instead. Tactically, we had upgraded credit to neutral as the dramatic selloff this year restored value in areas such as investment grade. We overweight local-currency EM debt on attractive valuations and potential income. A large risk premium compensates investors for inflation risk, in our view.

We are strategically underweight nominal government bonds, with a preference for shorter-dated maturities over long-dated bonds. We see yields broadly climbing higher. We stay firmly underweight the long-end as we see investors demanding higher compensation for holding government bonds amid rising inflation and debt levels. We prefer inflation-linked bonds instead. Tactically, we also underweight government bonds as we see the direction of travel for long-term yields as higher – even as yields have surged in 2022 – as term premium rises. We prefer inflation-linked bonds as portfolio diversifiers in the higher inflation regime.

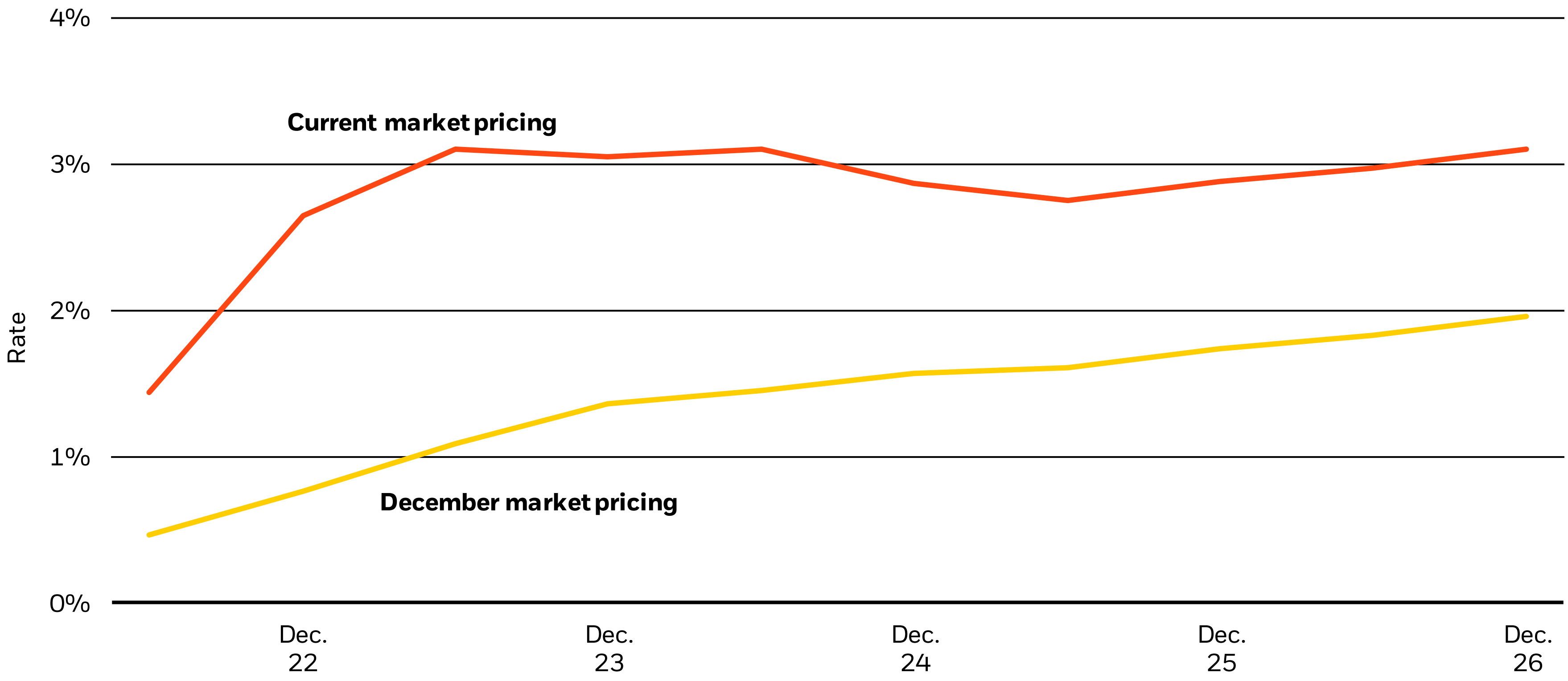
## Tactical granular views – highlights

| | | |
|---|---|---|
| DM equities | **Neutral** | We cut DM equities to neutral on a risk of the Fed talking itself into overtightening policy and China adding to a weaker global outlook. |
| U.S. Treasuries | **Underweight** | We stay underweight U.S. Treasuries even after the historically weak start to the year for the asset class as we see yields climbing further from here. |

# A steeper rate path ahead

The Fed appears to be constraining itself to the hawkish side of policy options. As long as markets believe the Fed's hawkish rhetoric on fighting inflation, we don't think it's time to buy the dip.

**Market pricing of the fed funds rate, Dec. 2021 vs. current**

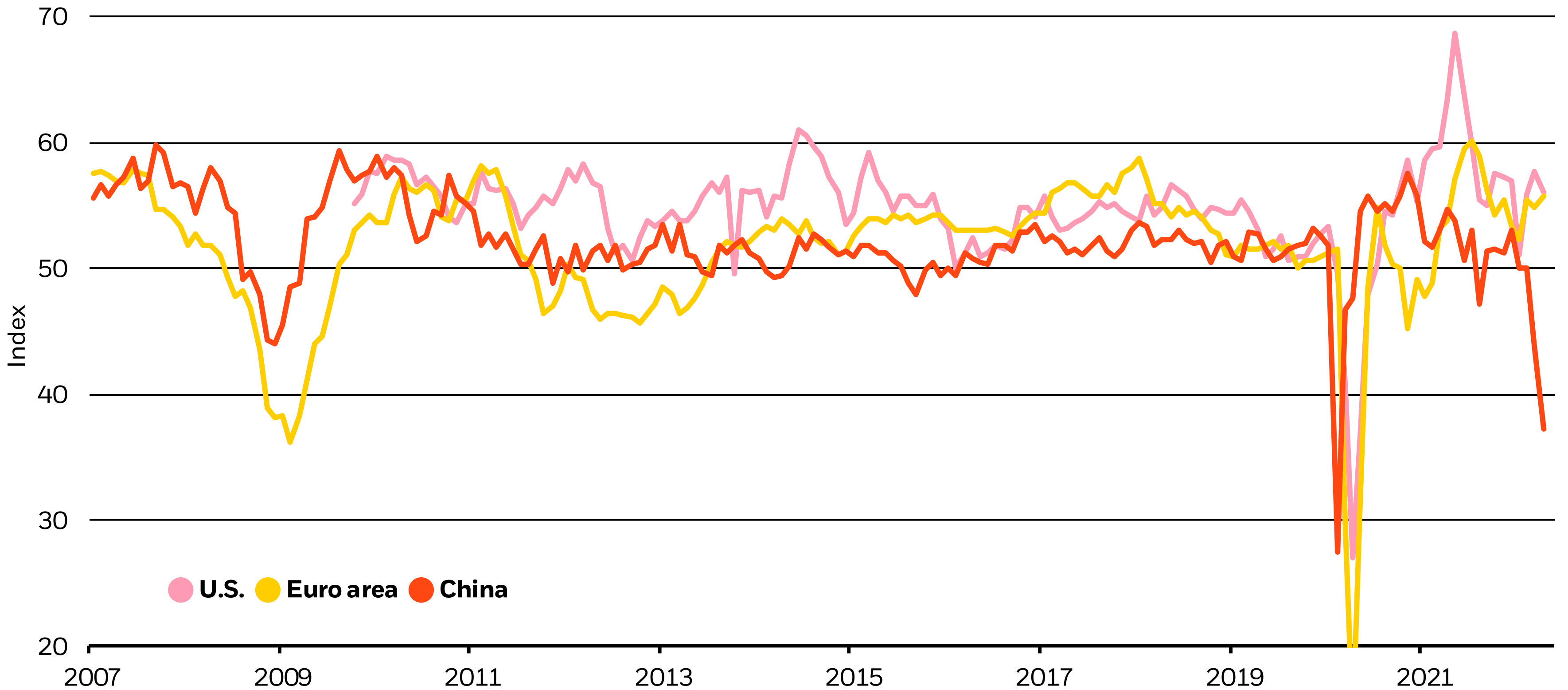



Sources: BlackRock Investment Institute, with data from Bloomberg, May 2022. Notes: The chart shows expectations for the path of U.S. short-term interest rates based on futures market prices compared to the market's December expectations of the rate path.

# China slowdown to ripple across globe

China's slowdown is starting to rival its 2020 shock and already surpasses the one from the global financial crisis. This will reduce growth in major economies and nudge up DM inflation, in our view.

## Composite PMIs, 2008–2022

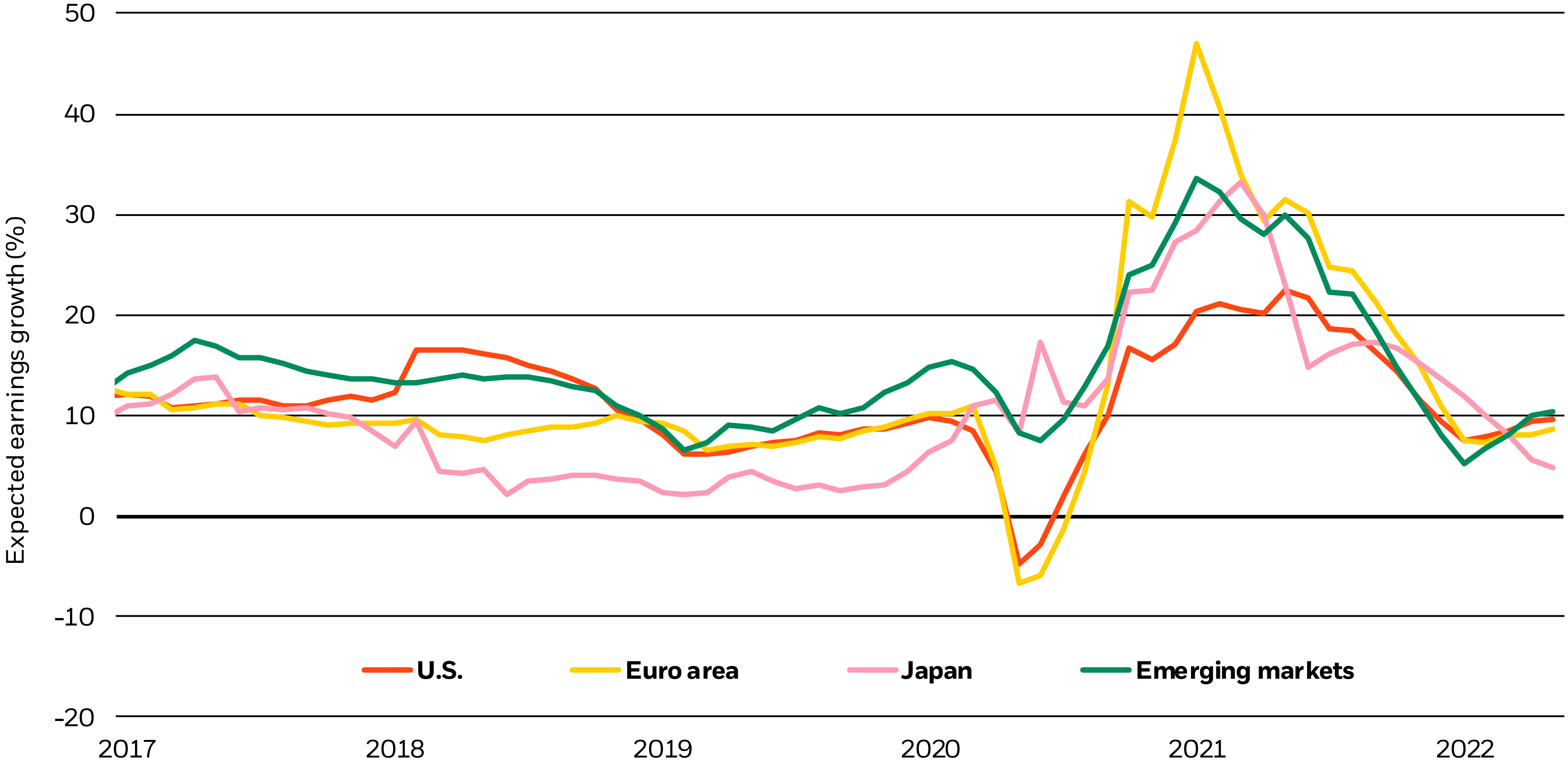



Sources: BlackRock Investment Institute, S&P Global and Caixin, with data from Refinitiv Datastream, May 2022. Notes: The chart shows composite (manufacturing and services) Purchasing Managers' indexes (PMI). An index level above 50 indicates an improvement in economic activity, while an index level below 50 indicates a decline. S&P PMIs are used for U.S. and Euro area, Caixin for China.

# We see the outlook for corporate earnings worsening

We believe current consensus earnings across major equity markets may be too optimistic given our view of a deteriorating global growth backdrop in light of the energy shock and China's lockdowns.

## Consensus expectations for 12-month forward regional corporate earnings, 2017-2022

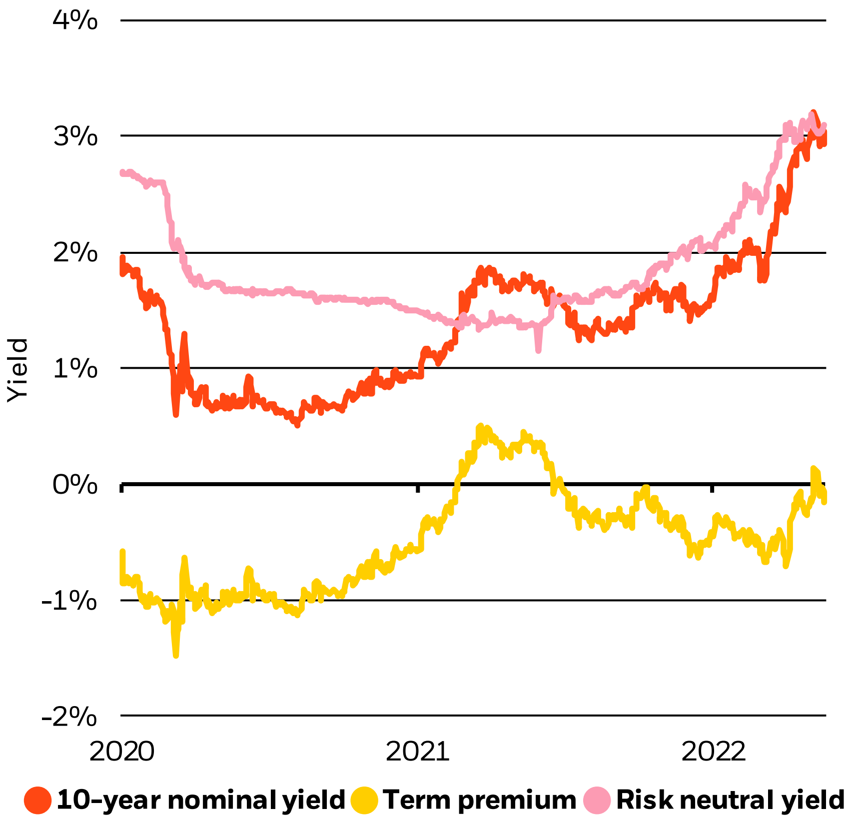



Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, May 2022. Notes: The chart shows forward 12-month earnings growth estimates for the MSCI USA, MSCI EMU, MSCI Japan and MSCI Emerging Markets indices based on Refinitiv I/B/E/S data.

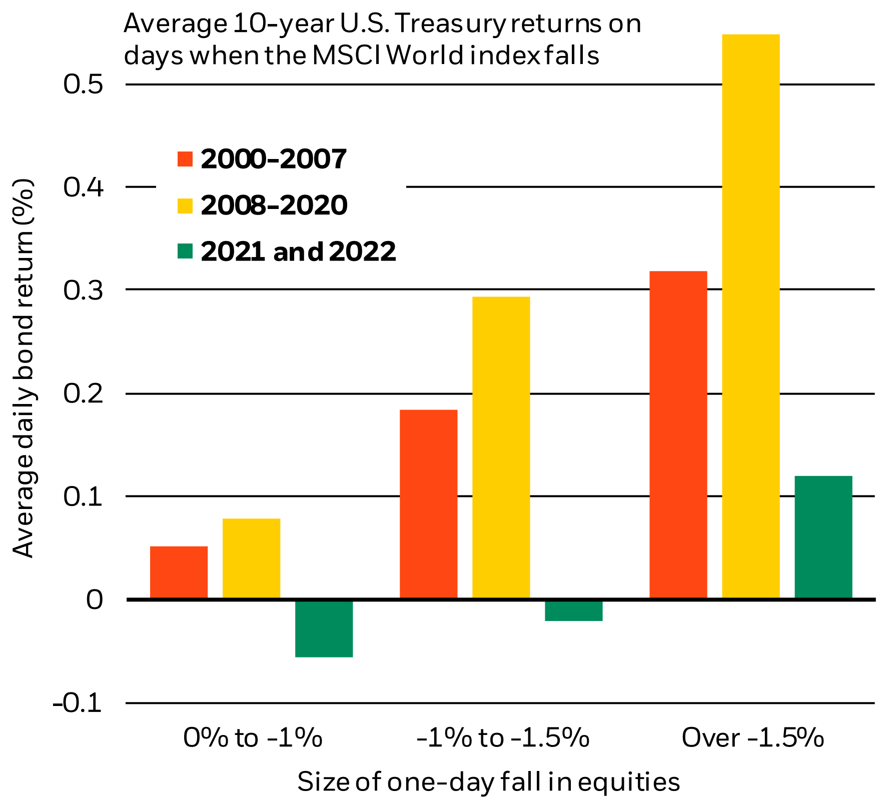
# Underweight DM government bonds even after steep selloff

We see yields rising further as investors question long-term government bonds' perceived safety – driving up the term premium. The asset class has also proven to be an ineffective portfolio diversifier.

## U.S. term premium breakdown, 2020-2022




## U.S. Treasury returns on equity dips, 2000-2022

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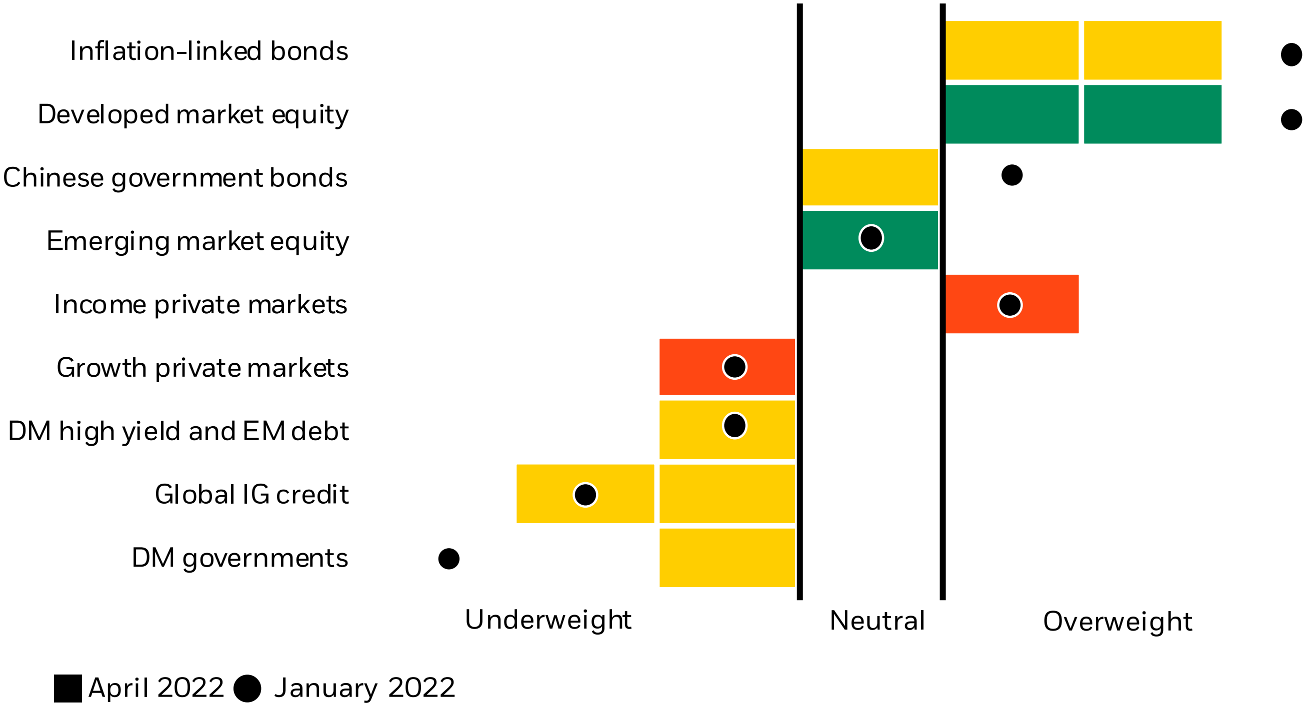
Sources: BlackRock Investment Institute, with data from Refinitiv Datastream and Bloomberg, May 2022. Notes: The left chart shows the U.S. 10-year government bond yield along with New York Federal Reserve estimates of two components of that yield: the average expected interest rate (risk neutral yield) and the term premium – the compensation investors typically demand to hold riskier long-term government bond. The chart on the right shows average daily return on the benchmark 10-year U.S. Treasury on days when the MSCI World equity index fell between 2000-2007 (orange bars), 2008-2020 (yellow bars) and in 2021-2022 (green bars).

# We prefer equities over credit, government bonds

The sharp repricing of interest rate expectations has hit risk assets. We still prefer equities over bonds but see the relative gap between them narrowing.

## Hypothetical U.S. dollar 10-year strategic views vs equilibrium, May 2022

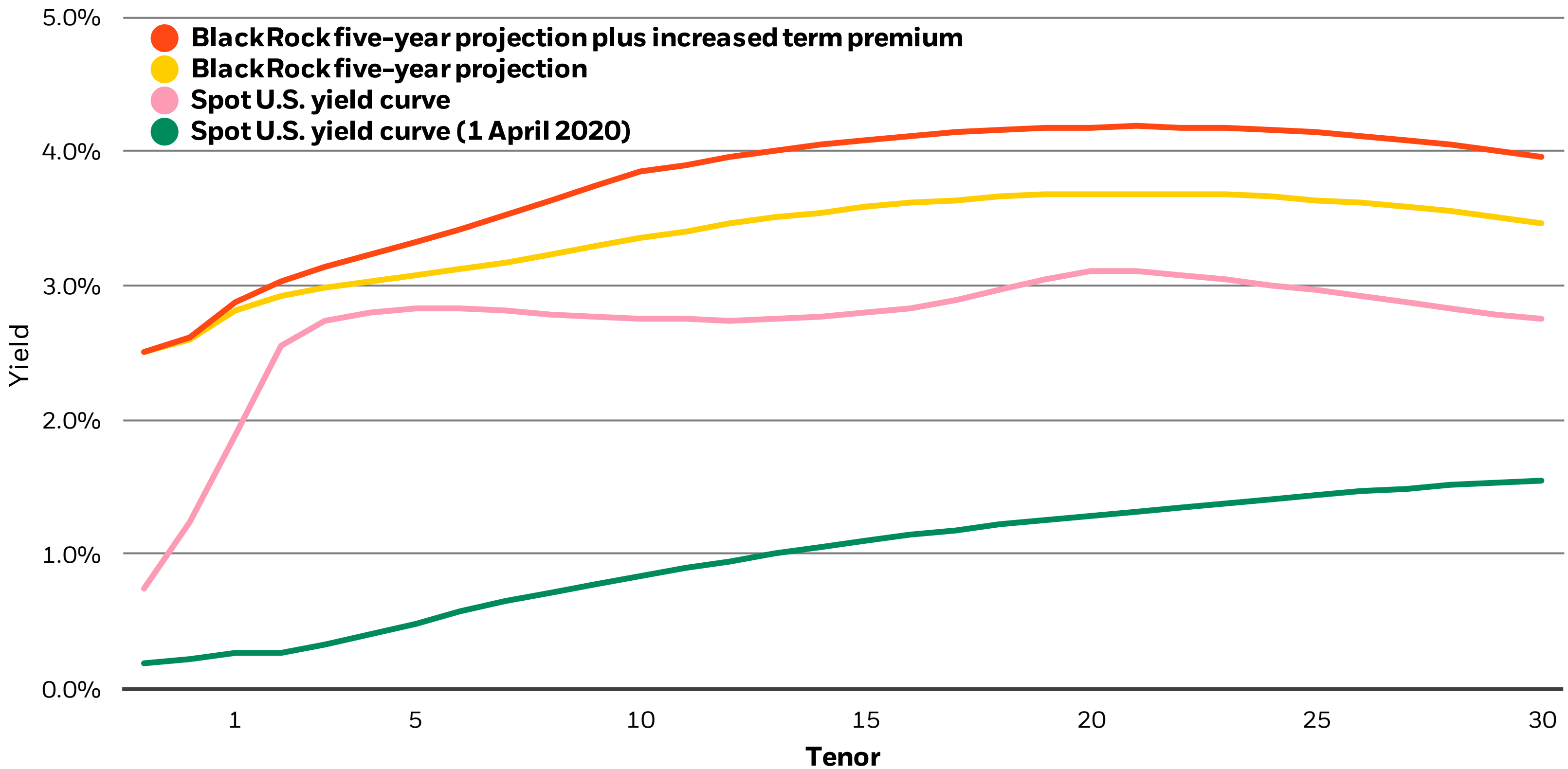



**This information is not intended as a recommendation to invest in any particular asset class or strategy or as a promise - or even estimate - of future performance.** Source: BlackRock Investment Institute, May 2022. Data as of 11 April 2022. Note: The chart shows our asset views on a 10-year view from an unconstrained U.S. dollar perspective against a long-term equilibrium allocation. Global government bonds and EM equity allocations comprise respective China assets. Income private markets comprise infrastructure debt, direct lending, real estate mezzanine debt and US core real estate. Growth private markets comprise global private equity buyouts and infrastructure equity. The allocation shown is hypothetical and does not represent a real portfolio. It is intended for information purposes only and does not constitute investment advice. Index proxies: Bloomberg Barclays US Government Inflation-Linked Bond Index, MSCI World US$, Bloomberg Barclays China Treasury + Policy Bank Total Return Index, MSCI EM, Bloomberg Barclays U.S. Credit index, JP Morgan EMBI Global Diversified Index, Bloomberg Barclays Global Credit Index, Bloomberg Barclays Global Aggregate Treasury index. We use BlackRock proxies for private market assets. The hypothetical portfolio may differ from those in other jurisdictions, is intended for information purposes only and does not constitute investment advice.

# We still expect steeper yield curves driven by term premium

Markets have swiftly repriced a steeper near-term path of front-end interest rates in the U.S. Yet we see markets underappreciating higher term premium in bond markets in the long-run.

## U.S yield curves, spot vs. estimates, May 2022

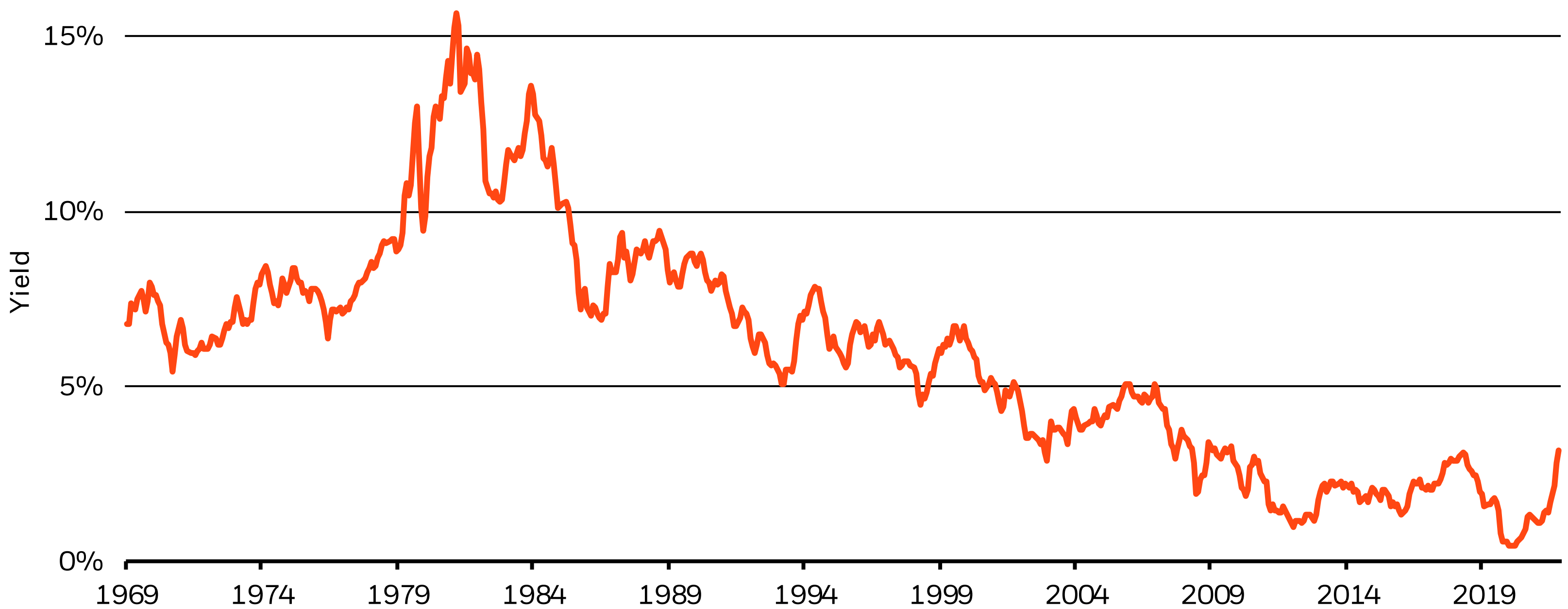



**Past performance is no guarantee of future results. Forward looking estimates may not come to pass.** Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, May 2022. Notes: The chart shows the current spot U.S. yield curve (pink), a market-implied projection of the yield curve five years from now based on overnight index swap pricing (yellow line) and our estimate (orange line) of where U.S. yields will be in five years' time.

# Proximity to effective lower bounds still in play for bonds

Bond yields have risen from the lows of last year yet remain close enough to their effective lower bounds that nominal government bonds' role as portfolio ballast remains challenged.

## U.S. seven-year Treasury yield, 1969-2022

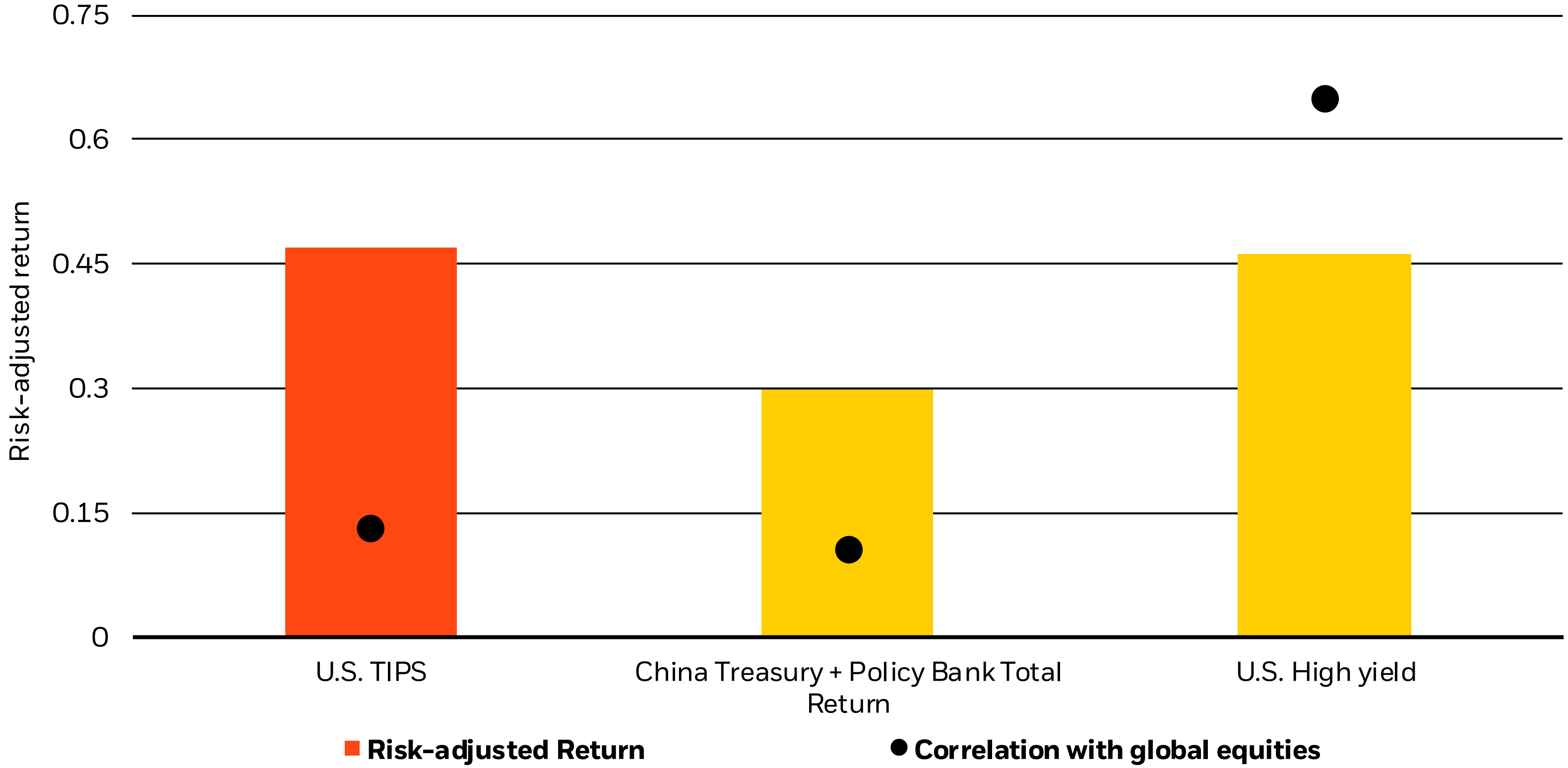



**This information is not intended as a recommendation to invest in any particular asset class or strategy or as a promise - or even estimate - of future performance. Indexes are unmanaged and do not account for fees. It is not possible to invest directly in an index . Past performance is not a reliable indicator of future results.** Source: BlackRock Investment Institute and Federal Reserve of St. Louis, with data from Refinitiv Datastream. May 2022.Notes: The chart shows the daily market yield data for seven-year constant maturity U.S. Treasury Securities from the FRED database. We use the seven-year constant maturity to reflect the current average duration of the Bloomberg all-maturity U.S. Government index but choose the FRED data to get a longer history of the data. Index data is only available from the mid-1980s. **Forward looking estimate may not come to pass.**

# We stay overweight inflation-linked bonds

Our view of a shift to higher inflation than market pricing drives higher expected risk-adjusted returns for TIPS vs. other medium-risk assets, while having a lower correlation to equities.

## Risk-adjusted returns vs. correlation with global ex-U.S. equities, February 2022




**Forward looking estimates may not come to pass. Indexes are unmanaged and do not account for fees. It is not possible to invest directly in an index.** Source: BlackRock Investment Institute, with data from Refinitiv Datastream, January 2022. Notes: The orange column on the chart shows our estimates of the risk-adjusted total returns – or expected returns after accounting for the asset class' historical volatility – for the Bloomberg U.S. Treasury Inflation Protected Securities (TIPS), the Bloomberg China Treasury and Policy Bank total return index and the Bloomberg U.S. High yield index. The black dots indicate the correlation of each respective asset class' monthly returns over a 20-year period with the MSCI World ex-U.S. index.

# Net-zero transition set to accelerate globally

We see the West's drive for energy security giving further impetus to the transition. Yet some regions will produce more fossil fuels in the near-term as global energy systems are rewired.

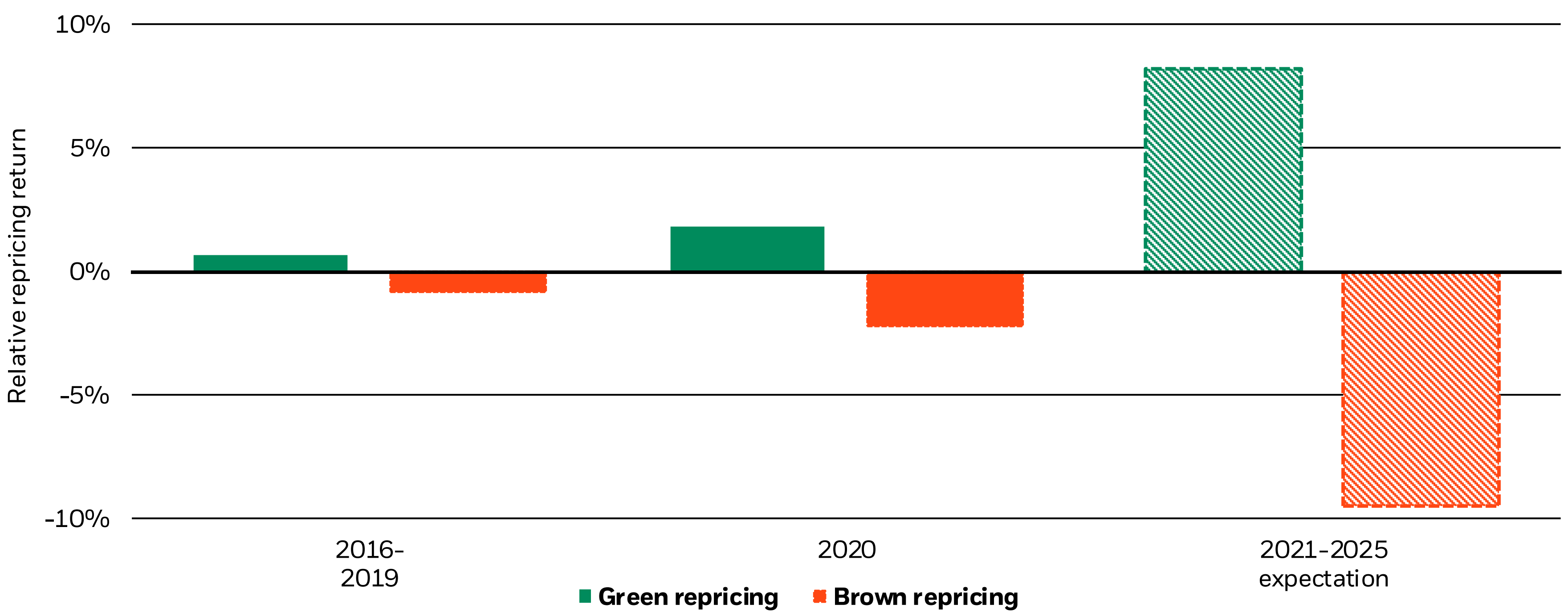
### Total returns of global clean energy and traditional energy vs global equities, 2022


**Past performance is no guarantee of future results.** Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, May 2022. Notes: The chart shows the total return index for the MSCI World Energy Index, MSCI World Equity Index and S&P Global Clean Energy Index rebased to 100 at the start of January 2022.

# Climate repricing is happening but has a long way to go

The net-zero transition is now driving relative repricing. We see a return advantage over coming years for "greener" sectors such as tech and healthcare over "browner" sectors such as energy and utilities.

## Relative returns of green vs. brown sectors, 2016-2025

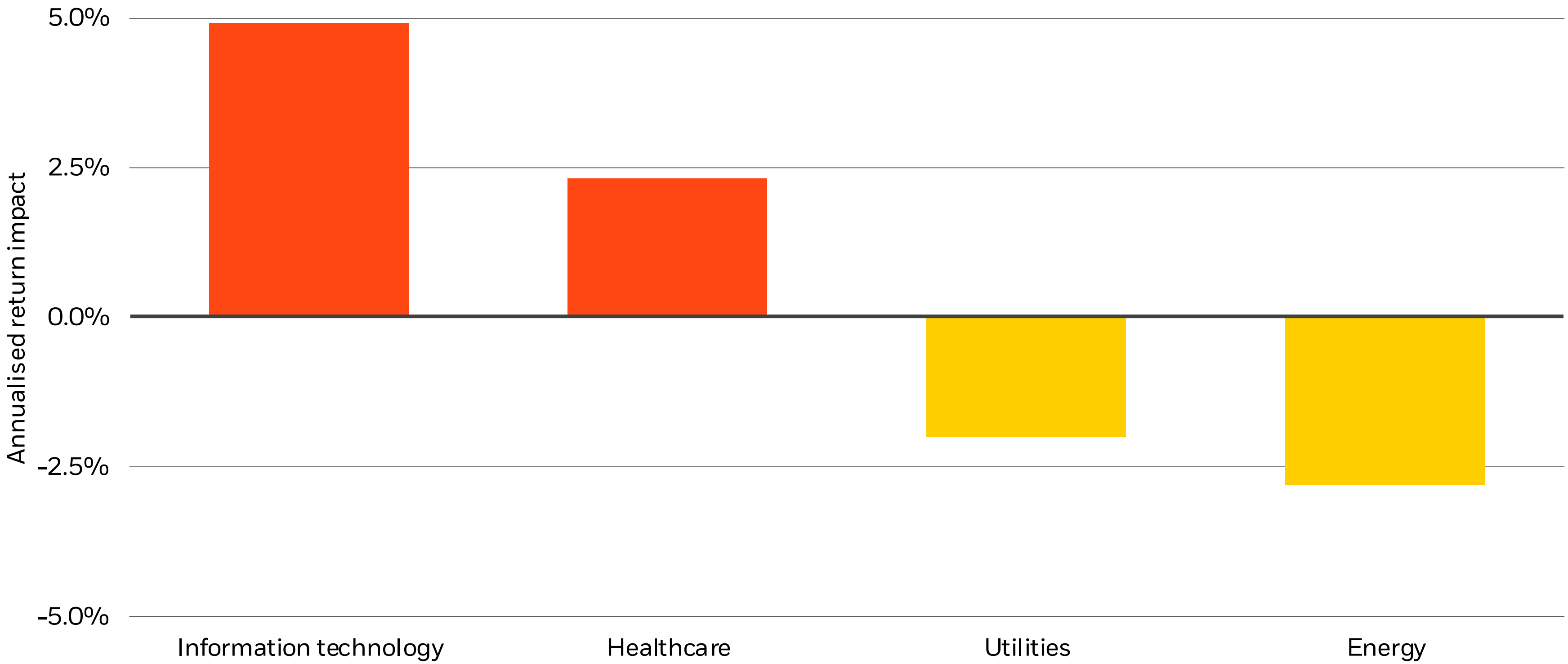



**Past performance is no guarantee of current or future results. Forward looking estimates may not come to pass.** Sources: BlackRock Investment Institute, with data from the Center for Research on Security Prices, Feb. 1, 2022. Notes: To estimate climate-driven repricing, we attribute historic returns to two drivers: cashflow news and discount rate (DR) news. We then identify the DR news associated with climate change using carbon emission intensity (CEI) as a proxy. To isolate the DR component of returns, we apply the standard decomposition formula of Campbell (1991) using a standard factor model of expected returns (which embed well-known predictors such as value, momentum, and quality). Attribution to climate scores is then given by forecasting regressions of DR news on a measure of CEI. Sector returns are MSCI US Sector index-weighted averages of stock level returns. Green represents the technology sector, the most "green" in our work, whereas the utilities sector is the most "brown" in the repricing. The 2016-2019 bars represent the total repricing over this period; and the 2021-2025 expectation is the cumulative repricing we expect over that period. The estimate is highly uncertain and is based on factors including risk premia effects in other long-run transitions such as demographic trends, market pricing of green bonds, and investor survey data on how much return they would be willing to give up to for more sustainable assets. See Sustainability: the tectonic shift transforming investing of February 2020 for details.

# The transition will have a big relative impact across sectors

We believe avoiding climate-related damages will help drive growth and improve returns for risk assets broadly. We see climate-resilient sectors such as tech and healthcare as potential beneficiaries.

## Return assumption differentials in green transition vs. no-climate-action




**For illustrative purposes only. This information is not intended as a recommendation to invest in any particular asset class or strategy or as a promise - or even estimate - of future performance.**
Sources: BlackRock Investment Institute, with data from Refinitiv Datastream and Bloomberg, February 2021. Notes: The chart shows the difference in U.S. dollar expected returns over the next five years from February 2021 for four sectors of the MSCI USA Index in our base case of a "green" transition (policies and actions taken to mitigate climate change and damages, and to limit temperature rises to no more than 2 degrees Celsius by 2100) vs. a no-climate-action scenario. The estimated sectoral impact is based on expected differences in economic growth, corporates earnings and asset valuations across the two scenarios. Professional investors can access full details in our *Portfolio perspectives* and CMAs website.

# Updated 2022 investment themes

**Living with inflation –** Central banks are facing a growth-inflation trade-off. Hiking interest rates too much risks triggering a recession, while not tightening enough risks causing runaway inflation. It's tough to see a perfect outcome.

**Implication**: We are neutral DM equities after having further trimmed risk.

**Cutting through confusion –** The Russia-Ukraine conflict has aggravated inflation pressures and has put central banks in a bind. Trying to contain inflation will be more costly to growth and jobs, and they can't cushion the growth shock. We see a worsening macro outlook due to the Fed's hawkish pivot, the commodities price shock and China's growth slowdown.

**Implication**: We remain underweight U.S. Treasuries and overweight inflation-linked bonds.

**Navigating net zero –** Climate risk is investment risk, and the narrowing window for governments to reach net-zero goals means that investors need to start adapting their portfolios today. The net-zero journey is not just a 2050 story; it's a now story.

**Implication**: We favor equity sectors better positioned for the green transition.

The opinions expressed are as of May 2022 and are subject to change at any time due to changes in market or economic conditions. Strategic implications refer to long-term views, tactical implications refer to asset views on a 6-12 month horizon.

# Snapshot of our views – May 2022

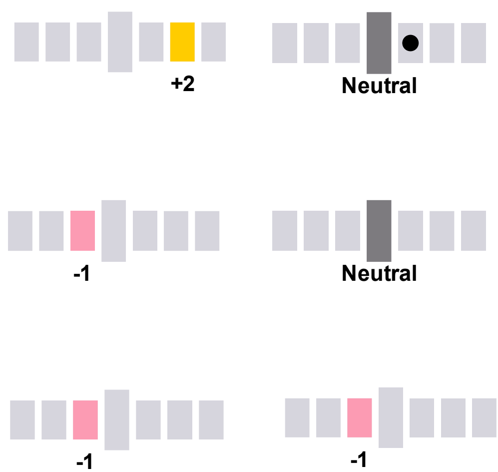
## Latest directional views

Strategic view | Tactical view

Equities

Credit

Govt bonds




We stay overweight equities in our strategic views, yet are trimming our overall tilt as the relative appeal versus bonds has diminished. Incorporating climate change in our expected returns brightens the appeal of developed market equities given the large weights of sectors such as tech and healthcare in benchmark indices. Tactically, we downgrade DM equities to neutral due to a higher risk of central banks overtightening policy and a deteriorating growth backdrop in China and Europe.

We are underweight credit on a strategic basis against a backdrop of rising interest rates. We prefer to take risk in equities instead. Tactically, we had upgraded credit to neutral as the dramatic selloff this year restored value in areas such as investment grade. We overweight local-currency EM debt on attractive valuations and potential income. A large risk premium compensates investors for inflation risk, in our view.

We are strategically underweight nominal government bonds, with a preference for shorter-dated maturities over long-dated bonds. We see yields broadly climbing higher. We stay firmly underweight the long-end as we see investors demanding higher compensation for holding government bonds amid rising inflation and debt levels. We prefer inflation-linked bonds instead. Tactically, we also underweight government bonds as we see the direction of travel for long-term yields as higher – even as yields have surged in 2022. We prefer inflation-linked bonds as portfolio diversifiers in the higher inflation regime.

## Tactical granular views – highlights

| | | |
|---|---|---|
| DM equities | **Neutral** | • We cut DM equities to neutral on a risk of the Fed talking itself into overtightening policy and China adding to a weaker global outlook. |
| U.S. Treasuries | **Underweight** | • We stay underweight U.S. Treasuries even after the historically weak start to the year for the asset class as we see yields climbing further from here. |

# Tactical granular views: equities

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

| Region | View | Commentary |
|---|---|---|
| Developed markets | Neutral | We downgrade DM stocks to neutral due to uncertainty over policy amid a worsening macro picture. Their appeal relative to bonds has also diminished. The risk has risen that central banks slam the policy brakes as they focus solely on inflation without fully acknowledging the high costs to growth and jobs. |
| United States | Neutral | We cut U.S. equities to neutral. The Fed's hawkish pivot has raised the risk that markets see rates staying in restrictive territory. The year-to-date selloff partly reflects this, yet we see no clear catalyst for a rebound. |
| Europe | Neutral | We cut European equities to neutral as the fresh energy price shock in the aftermath of the tragic war in Ukraine puts the region at risk of stagflation. |
| UK | Neutral | We are neutral UK equities. We see the market as fairly valued. |
| Japan | Neutral | We cut Japan stocks to neutral as part of a broader push to take more caution across DM equities. |
| China | Neutral | We recently downgraded Chinese equities to neutral on a worsening macro outlook. China's ties to Russia also have created a new geopolitical concern that requires more compensation for holding Chinese assets, we think. |
| Emerging markets | Neutral | We are neutral EM equities given challenged restart dynamics, high inflation pressures and tight policies. |
| Asia ex-Japan | Neutral | We are neutral Asia ex-Japan equities. China's deteriorating macro outlook is a worry, and policymakers have yet to fully deliver on promises of easing. |

**Underweight** **Neutral** **Overweight** ● Previous view

**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, May 2022. 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.

# Tactical granular views: fixed income

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

| Asset | View | Commentary |
|---|---|---|
| U.S. Treasuries | -1 | We underweight U.S. Treasuries even as yields have surged this year. We see long-term yields move up further as investors demand a higher premium for holding governments bonds. We prefer short-maturity bonds instead. |
| Treasury Inflation-Protected Securities | +1 | We overweight U.S. TIPS as we see inflation as persistent and settling above pre-Covid levels. We prefer TIPS as diversifiers in the inflationary backdrop. |
| European government bonds | Neutral | We are neutral European government bonds. Market pricing of euro area rate hikes is too hawkish, we think, given the energy shock's hit to growth. |
| UK Gilts | Neutral | We are neutral UK Gilts. We see market expectations of rate hikes as overdone amid constrained supply and weakening growth. |
| China government bonds | Neutral | We are neutral Chinese government bonds. Policymakers have been slow to loosen policy to offset the slowdown, and yields fell below U.S. Treasuries. |
| Global investment grade | Neutral | We are neutral investment grade credit to neutral as this year's sell-off has made valuations more attractive. Coupon income is the highest in about a decade. |
| Global high yield | Neutral | We are neutral high yield. We do not expect credit spreads to tighten but find the income potential attractive. |
| Emerging market – hard currency | Neutral | We are neutral hard-currency EM debt. We expect it to gain support from higher commodities prices but remain vulnerable to rising U.S. yields. |
| Emerging market – local currency | +1 | We are modestly overweight local-currency EM debt on attractive valuations and potential income. Higher yields already reflect EM monetary policy tightening, in our view, and offer compensation for interest rate risk. |
| Asia fixed income | Neutral | We are neutral Asia fixed income. A worsening macro outlook and geopolitical concern about China's Russia ties make Chinese assets riskier, in our view. Outside China, we like Asian sovereigns and credit for income. |

**Underweight** **Neutral** **Overweight** ● Previous view

**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, May 2022. 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.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