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Weekly commentary

BlackRock

May 18, 2026

Upping developed stocks strategically

- AI-driven earnings upgrades lead us to upgrade DM equities on a strategic basis. We downgrade high yield as we prefer taking growth risk through stocks.
- AI optimism and policy caution drove markets last week: the S&P 500 hit record highs on strong earnings, while bond yields rose as Fed cut expectations faded.
- European and Japanese data this week should show whether high energy costs and supply disruptions are feeding into inflation and production hiccups.

Stocks are rallying on strong AI earnings expectations, offsetting jitters over inflation pressures from geographical fragmentation such as the Middle East supply shock. That could change in the near term, but we look beyond this in our strategic views when we see these mega forces - big, structural trends - in action. We upgrade developed market stocks to overweight and downgrade high yield to neutral as we shift where we take growth risk on a horizon of five years or more.

Multiple outcomes

U.S. equity 12-month forward price-earnings ratio, 1991-2031

Forward-looking estimates may not come to pass. Past performance is not a reliable indicator of current or future results.
Source: BlackRock Investment Institute, with data from Robert Shiller, (Yale University), May 2026. Note: The line shows the forward price-earnings ratio of U.S. equities, the markers indicate future estimates of the ratio across various scenarios.

Markets are being pulled in different directions by competing mega forces. AI is driving stocks higher today, but we cannot say which force will dominate in the long run. That's why our capital market assumptions (for professional investors only) are built on multiple scenarios that imply fundamentally different macro paths. Our starting point (the green dot) reflects our latest thinking, and the gap between outcomes shows how mega forces could affect outcomes over a five-year period. In one, AI drives a productivity boom that could sustain stronger growth and earnings, justifying higher equity valuations over the strategic horizon, as the chart's pink dot shows. In another, geopolitical fragmentation fuels stagflationary pressures that push global risk premia higher as investors demand greater compensation for uncertainty. This would lower equity valuations, as the purple dot shows.

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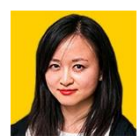

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For now, AI-driven earnings momentum looks strong: Upgrades to MSCI U.S. 2026 and 2027 earnings expectations in the past two quarters rank in the top five since 1988. And it's broadening: The gap between expected "magnificent seven" earnings growth and the rest of the S&P 500 in 2027 has narrowed to 3 percentage points, down from 31% in 2024. Leadership is also broadening across regions and sectors, as AI reshapes markets beyond asset classes. The technology sector is a larger share of the MSCI EM Index than it is of the S&P 500, reflecting Taiwan's and South Korea's key role in the AI supply chain. All this underpins our DM equities upgrade and existing EM equities overweight on a long-term horizon. We view these not as broad market exposures but through sectors and regions. In DM equities, we favor tech, AI-adopters such as health care and energy sectors tied to the AI buildout and rising power demand. We also favor EM tied to AI supply chains, including Taiwan and South Korea. We see India stocks benefiting from the demographic mega force: a growing workforce.

To fund the DM equities upgrade, we reduce our fixed income exposure in our strategic portfolios. Within this segment, we like high yield as it offers attractive income with less duration, or sensitivity to interest rate swings, than investment grade credit. But we don't build portfolios in asset class silos. Similar to a total portfolio approach, we prefer taking growth risk in equities, leading us to downgrade high yield to neutral. The reason: Investors can participate in equity upside rather than be capped by coupon income. We also downgrade DM government bonds to underweight, leaving our long-term portfolios with less duration risk than our benchmark. We overweight inflation-linked bonds as we expect inflation to be more persistent than markets currently price over a strategic horizon of five years or more.

The clash of mega forces across asset classes this year reinforces the need for a dynamic, scenario-based approach to navigate uncertain outcomes. We see the industry increasingly recognizing this shift through greater focus on total portfolio approaches that cut through asset class labels. A prime example is investing in infrastructure. We think infrastructure can do well under all our scenarios as it has historically been resilient in periods of market stress. Most investors can up their holdings materially, depending on their tolerance for illiquidity risk, or the risk of being unable to sell an investment quickly.

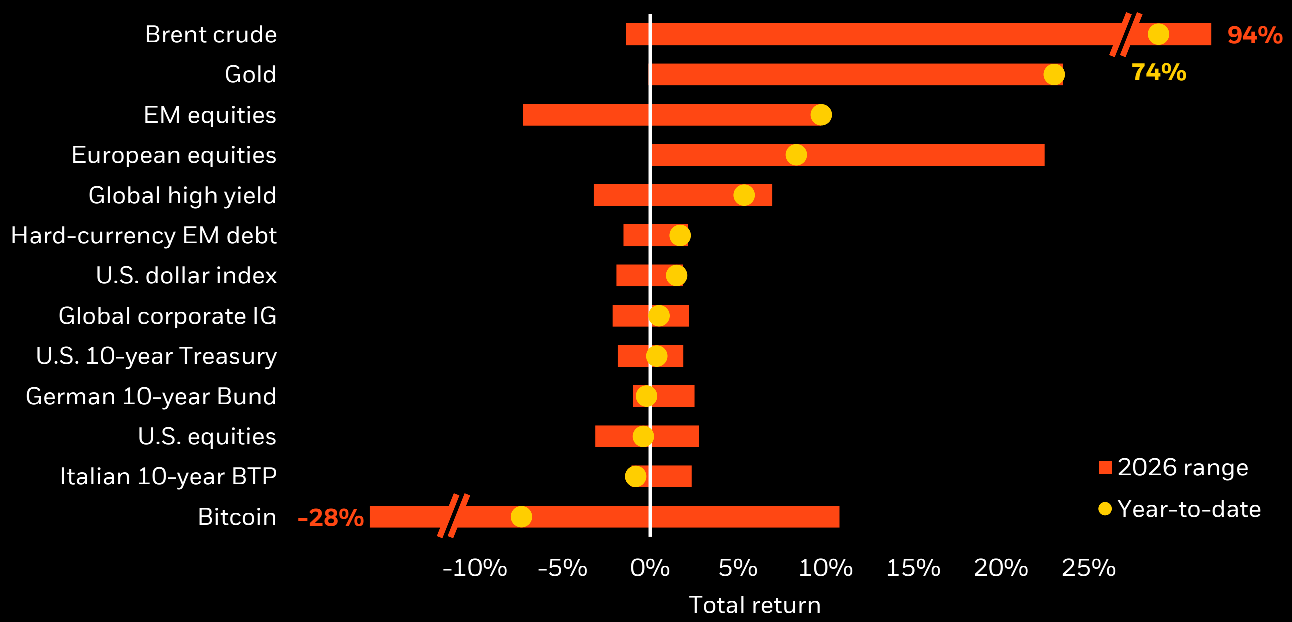
Bottom line: We upgrade DM equities on a strategic basis due to AI-driven earnings momentum strength. We downgrade high yield to neutral as we prefer to take growth risk in equities but still like it for income in a fixed income context.

Market backdrop

The S&P 500 last week notched another record high as investors kept their focus on strong AI-driven earnings before slipping on Friday. U.S. Treasury yields jumped to around 4.56% as investors scaled back expectations for Federal Reserve rate cuts while oil prices remained well above pre-conflict level amid ongoing supply disruptions caused by the Middle East conflict. Brent crude remained near $105, more than 40% above pre-conflict levels.

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 14, 2026. Notes: The two ends of the bars show the lowest and highest res at any point year to date, and the dots represent current year-to-date res. Emerging market (EM), high yield and global corporate investment grade (IG) res 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, spot bitcoin, MSCI Emerging Markets Index, MSCI Europe Index, LSEG Datastream 10-year benchmark government bond index (U.S., Germany and Italy), Bloomberg Global High Yield Index, J.P. Morgan EMBI Index, Bloomberg Global Corporate Index and MSCI USA Index.

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Week ahead

May 19	euro area trade balance; China Loan Prime Rate	**May 21**	Global Flash PMIs; euro area consumer confidence
May 20	UK CPI and PPI; Japan trade balance	**May 22**	Japan CPI

This week's focus is on inflation data from the UK and Japan, along with early signals on global production. Japan CPI will likely show how higher energy costs tied to the Middle East conflict are feeding into price pressures, while flash PMIs will indicate whether supply disruptions and rising costs are starting to weigh on activity.

Big calls

Our highest conviction views on six- to 12-month (tactical) and over five-year (strategic) horizons, May 2026

Tactical	Reasons
Favor AI beneficiaries	We favor infrastructure and equipment supporting the AI buildout such as semiconductors, power and data centers. We think they stand to benefit no matter AI's eventual winners or losers. We see the AI boom lifting U.S. corporate earnings. underpinning our U.S. equity overweight.
Selected international exposures	We like hard-currency EM debt on economic resilience, disciplined fiscal and monetary policy and a high ratio of commodities exporters. We're also overweight EM equities, preferring commodity exporters and AI beneficiaries. In Europe, we favor equity sectors like infrastructure.
Evolving diversifiers	We suggest looking for "plan B" portfolio hedges such as thematic opportunities related to the AI built-out and search for energy security. Long-term U.S. Treasuries no longer provide a buffer against equity market declines, and gold also has shown to be an ineffective diversifier.

Strategic	Reasons
Portfolio construction	We favor a scenario-based approach as AI winners and losers emerge. We lean on private markets and hedge funds for idiosyncratic returns and to anchor portfolios in mega forces.
Infrastructure equity and private credit	We find infrastructure equity valuations attractive as geopolitical fragmentation and the AI build-out underpin structural demand. We still like private credit but see an increase in dispersion of returns. This highlights the importance of manager selection.
Beyond market cap benchmarks	We get granular in public markets. We favor DM government bonds outside the U.S. Within equities, we favor EM over DM – and get selective in both. In EM, we like India because it sits at the intersection of mega forces. In DM, we like Japan amid inflation and corporate reforms.

Note: Views are from a U.S. dollar perspective, May 2026. 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 into the future. 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.

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.

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Granular views

Six- to 12-month tactical views on selected assets vs. broad global asset classes by level of conviction, May 2026

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

	Asset	View	Commentary
Equities	**Developed markets**		
	United States	+1	We are overweight. Contained damage to global growth from the Mideast conflict and strong earnings expectations – particularly in tech – keep us risk-on.
	Europe	Neutral	We are neutral. Europe's high exposure to the energy shock from the Mideast conflict makes it vulnerable to higher inflation and lower growth.
	UK	Neutral	We are neutral. Valuations remain attractive relative to the U.S., but we see few near-term catalysts to trigger a shift.
	Japan	Neutral	We are neutral. Japan's exposure to imported energy may erode strong equity gains powered by healthy corporate balance sheets and governance reforms.
	Emerging markets	+1	We are overweight yet stay selective. We favor Asian countries that manufacture critical AI components and Latin American energy and commodity exporters.
	China	Neutral	We are neutral. Trade relations with the U.S. have steadied, but property stress and an aging population still constrain the macro outlook. Relatively resilient activity limits near-term policy urgency. We like sectors like AI, automation and power generation.
Fixed Income	Short U.S. Treasuries	Neutral	We are neutral. Shorter-term bonds are relatively attractive as the market has woken up to persistent inflation and higher rates.
	Long U.S. Treasuries	-1	We are underweight. Yields already faced upward pressure from rising term premia, as investors demand more compensation for the risk of holding long-term debt. The recent energy price shock compounds this by aggravating pre-existing inflationary pressures.
	Global inflation-linked bonds	Neutral	We are neutral. We think inflation will settle above pre-pandemic levels, but markets may not price this in the near term as growth cools.
	Euro area govt bonds	Neutral	We are neutral short-term European government bonds. The market has repriced the ECB policy path more in line with our view. We think increased German bond issuance to finance its fiscal stimulus package is already largely reflected in the current level of 10-year yields.
	UK gilts	Neutral	We are neutral. We expect volatility in gilts over the near-term. Gas powers much of the UK's electricity, but storage is limited – making it especially vulnerable to a resurgence in inflation.
	Japanese govt bonds	-2	We are underweight. Rate hikes, higher global term premium and heavy bond issuance will likely drive yields up further.
	China govt bonds	Neutral	We are neutral. China bonds offer stability and diversification but developed market yields are higher and investor sentiment shifting towards equities limits upside.
	U.S. agency MBS	+1	We are overweight. Agency MBS offer higher income than Treasuries with similar risk and may offer more diversification amid fiscal and inflationary pressures.
	Short-term IG credit	Neutral	We are neutral. Corporate strength means spreads are low, but they could widen if issuance increases.
	Long-term IG credit	-1	We are underweight. We prefer short-term bonds less exposed to interest rate risk over long-term bonds.
	Global high yield	Neutral	We are neutral. High yield offers more attractive carry and shorter duration, but we think dispersion between higher and weaker issuers will increase.
	Asia credit	Neutral	We are neutral. Overall yields are attractive and fundamentals are solid, but spreads are tight.
	Emerging hard currency	+1	We are overweight. EM hard-currency indexes lean toward Latin American commodity exporters such as Brazil that stand to benefit as Mideast supply plummets.
	Emerging local currency	Neutral	We are neutral. The U.S. dollar has been strengthening as a safe-haven currency in the wake of the Middle East conflict. This could reverse year-to-date gains driven by a falling USD.

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