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Weekly commentary

BlackRock

May 26, 2026

The need to diversify diversifiers

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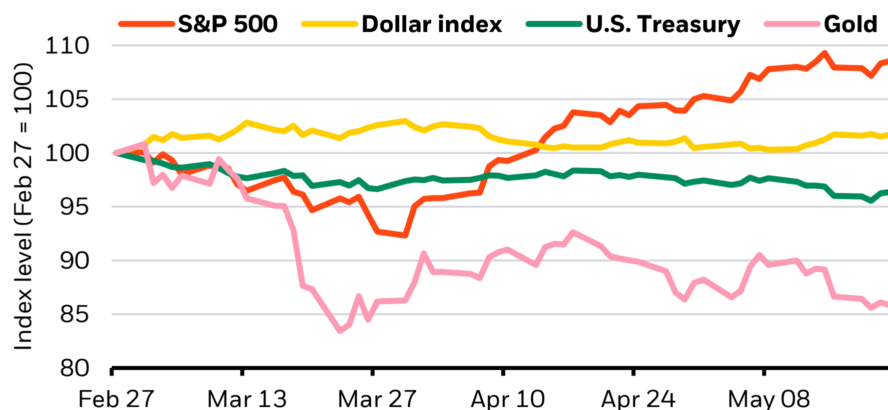
- Surging bond yields underscore our view that traditional portfolio diversifiers are challenged. We favor unique diversifiers: active returns and private markets.
- Since the Mideast conflict began, the S&P 500 is up 8%, while front month Brent crude prices are up 43% and U.S. 10-year yields nearly 60 basis points.
- U.S. PCE data will help confirm the CPI's upside surprise showing higher core inflation as markets price in a Federal Reserve interest rate hike later this year.

The supply chain disruptions from the Middle East conflict and the accelerating AI buildout have caused some of the sharpest moves in long-term bond yields across developed markets. U.S. 30-year bond yields hit two-decade highs above 5% last week, up 40 basis points since the start of the war. We see our diversification mirage theme playing out in real time as bonds don't cushion portfolios against risk asset selloffs. We favor diversifiers such as hedge funds and private markets.

Hard to find

Cross-asset performance, Feb. 27-May 22, 2026



Past performance is not a reliable indicator of current or future results. Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged and one cannot invest directly in an index. Source: BlackRock Investment Institute with data from LSEG Datastream, May 2026. Note: Lines show the returns of various assets since Feb. 27, 2026. Total returns are shown for the S&P 500 and U.S. Treasury, the latter proxied by 10-year U.S. Treasuries.

The selloff in long-term government bonds is a reminder that traditional portfolio hedges are proving less reliable today: Since the onset of the Middle East conflict, returns on U.S. 10-year Treasuries have been negative, driven by energy supply disruption concerns adding to already sticky inflation and persistent fiscal deficits. Stocks and long-term bonds have increasingly sold off together as these concerns dominate markets. But pressure on traditional diversifiers hasn't been confined to bonds: gold, touted as a portfolio diversifier that has sometimes worked in the past, has slid 15% since the conflict began, partly due to crowded positioning. See the chart. This underscores how long-held safe havens can become unreliable hedges. We think diversification is harder to achieve – thus the mirage – and that's why investors need to diversify their diversifiers, in our view.

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The Mideast conflict has triggered a broader reset in interest rate expectations amid fears that supply chain disruptions would add to already sticky inflation. The shift has been drastic: markets went from expecting rate cuts before the conflict to now pricing in Federal Reserve and Bank of England rate hikes. More recently, another factor has pushed yields higher: Investors are now demanding more term premium – or greater compensation to hold long-term government bonds – our long-held view. The term premium embedded in U.S. 10-year yields is rising back near its highest levels in 12 years, according to New York Fed estimates of the ACM model. The changing base of the U.S. Treasury market is also a factor. The make-up of investors is shifting toward short-term, leveraged players quick to sell – and push up long-term yields – in volatile markets. This validates our preference for short- and medium-term U.S. government bonds over long-term bonds.

These developments require finding ways to shield portfolios against higher inflation. The macro regime is shaped by mega forces as stubborn inflation and higher rates become structural features. Geopolitical fragmentation adds to the risk of ongoing supply disruptions, while persistent fiscal deficits in major economies pile pressure on long-term borrowing costs. At the same time, the AI buildout is driving sustained investment demand across the economy, further stoking inflation and demand for capital. That's one of the reasons we favor inflation-linked bonds on strategic horizons of five years or longer.

These developments also reinforce why new sources of portfolio diversification are needed. For strategic horizons, we like hedge funds and private markets as diversifiers less reliant on broader market moves and instead tied to manager skill. We favor macro and absolute return hedge fund strategies that can better diversify portfolios when macro shocks hit risk assets broadly. In private markets, we like infrastructure equity with cash flows often linked directly to inflation, as well as private credit tied to AI-driven investment demand. On a tactical horizon, the AI mega force underpins our pro-risk stance, supported by strong corporate earnings growth and balance sheets. Earnings growth has offset the drag from higher interest rates and helped stocks absorb the sharp rise in yields – though we're monitoring this key risk to our view.

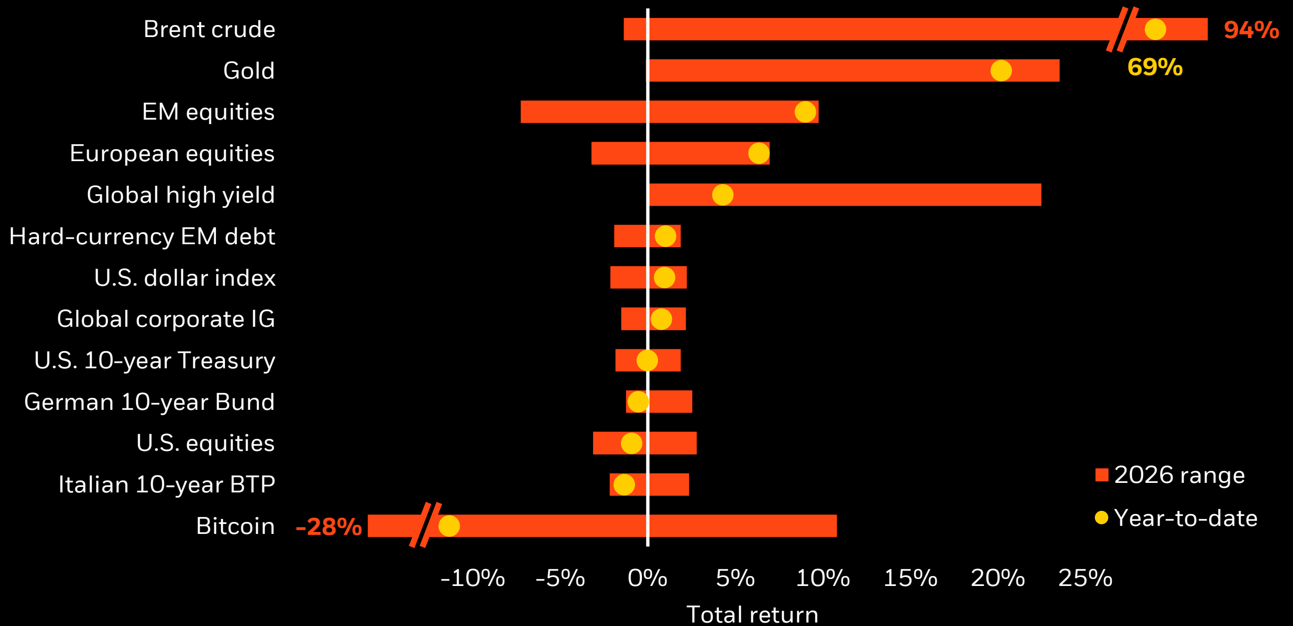
Bottom line: Traditional portfolio diversification is challenged today, underscoring the need for broader diversification sources. We stay pro-risk on solid corporate earnings and the AI theme.

Market backdrop

U.S. 30-year Treasury yields hit a 19-year high before easing as the global bond selloff paused. The S&P 500 was little changed near record highs as SpaceX set out its plan for what could be a record-sized stock listing. The S&P 500 has added 8% since the Mideast conflict began. European stocks outperformed with a 3% gain. Brent crude oil fell about 5% on hopes for a resolution to the conflict but is up about 70% this year. Energy flows through the Strait of Hormuz remain very limited.

Assets in review

Selected asset performance, year-to-date return and range



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Sources: BlackRock Investment Institute, with data from LSEG Datastream as of May 21, 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 26	U.S. consumer confidence	**May 29**	U.S. PMI; Japan CPI & unemployment
May 28	U.S. PCE inflation	**May 30**	China PMI

We eye U.S. core PCE for signs that higher energy costs are feeding through to underlying inflation. This comes as the Fed already faces a tougher trade-off between reining in inflation and supporting growth. We have been positioned for such an environment, underscored by our caution on long-term government bonds. We also eye Japan CPI data for evidence that inflation pressures remain persistent globally.

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 buildout 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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