2021 global outlook
Q4 update
Looking beyond the restart
**2021 midyear investment themes**

**The new nominal** – The powerful restart of economic activity has broadened, with Europe and other major economies catching up with the U.S. We expect a higher inflation regime in the medium term. We see the Fed normalizing policy rates only in 2023 and the European Central Bank staying on hold for much longer.

**Tactical implication**: We are overweight European equities and inflation-linked bonds. We are neutral on U.S. equities. We upgrade EM local debt to overweight.

**Strategic implication**: We remain underweight DM government bonds and prefer equities over credit.

**China stands out** – China is on a path toward greater state control where social objectives at times taking primacy over the quantity of growth. Yet the growth slowdown has hit levels policymakers can no longer ignore and we expect to see incremental loosening across three pillars – monetary, fiscal and regulatory.

**Tactical implication**: We turn moderately positive on Chinese equities, and maintain an overweight on its debt.

**Strategic implication**: Our neutral allocation to Chinese assets is multiples larger than typical benchmark weights, with the case for government bonds particularly strong, in our view.

**Journey to 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 full consequences of the tectonic shift to sustainability are not yet in market prices, in our view.

**Tactical implication**: We are overweight the tech sector as we believe it is better positioned for the green transition.

**Strategic implication**: We like DM equities and the tech sector as a way to play the climate transition.

The opinions expressed are as of October 2021 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.
Reaffirming our directional views

Equities
- **Strategic horizon:** We keep our overweight on equities. We see a better outlook for earnings and moderate valuations. The relative appeal of developed market equities brightens on incorporating climate change in our expected returns.
- **Tactical horizon:** We stay overweight as we expect the restart to accelerate and interest rates to stay low.

Credit
- **Strategic horizon:** We maintain our underweight given rich valuations, with a preference for equities to take risk.
- **Tactical horizon:** We stay neutral credit following the tightening in spreads, particularly investment grade.

Govt bonds
- **Strategic horizon:** We keep our underweight given diminished ability to act as portfolio ballasts. We prefer inflation-linked bonds. Rising debt levels may eventually pose risks to the low-rate regime.
- **Tactical horizon:** We remain underweight duration on expectations of gradually climbing yields amid the restart.

Tactical granular view - highlights

Chinese equities  **Upgrade to overweight**
- We see incremental monetary, fiscal and regulatory loosening to counter slow growth. We see current valuations implying an overly pessimistic outlook.

EM debt - local currency  **Upgrade to overweight**
- We see attractive valuations and coupon income in a world starved for income. We prefer higher-yielding markets within EM.

U.S. Treasuries  **Stay underweight**
- We see yields moving higher with the Fed poised to announce tapering of its asset purchases before the end of 2021. Yet we believe any policy rate adjustment will be gradual, in line with our new nominal theme.

European equities  **Stay overweight**
- The European restart has broadened and we expect a return to pre-Covid levels by the end of the year. The European Central Bank’s new policy framework calls for additional policy support for several more years.
The restart has broadened out to the euro area and the UK

China activity levels surpassed pre-Covid trend estimates earlier this year. We see U.S. activity now back above pre-Covid levels. Restart momentum is now picking up in other developed economies.

Estimated GDP paths, 2020–2022

Forward looking estimates may not come to pass. Sources: BlackRock Investment Institute, U.S. Bureau of Economic Analysis, Eurostat, Cabinet Office of Japan, China National Bureau of Statistics, with data from Refinitiv Datastream and Reuters News, October 2021. The chart shows projections of the level of GDP in different economies, according to latest consensus estimates compiled by Reuters. Solid lines denote published GDP data, and dotted line denotes median consensus expectations.
Fed has largely achieved its inflation objective, ECB not quite

Higher inflation data in recent months have helped U.S. inflation make up for past undershoots. The ECB is some ways away from achieving its new symmetric 2% inflation objective.

Euro area and U.S. inflation and central bank forecasts, 2006-2024


Notes: The chart shows euro area headline inflation and U.S. personal consumption expenditure inflation. The dots show Federal Reserve and European Central Bank projections. The Federal Reserve projections show Q4 annual inflation published in the FOMC Summary of Economic Projections over 2021 Q4-2023Q4. The ECB projections show calendar-year average inflation rates over 2021-23. The triangle shows our estimate of average U.S. personal consumption expenditures (PCE) – the Fed’s preferred gauge of inflation - in five years’ time. We derive this from our estimate of consumer price index in five years’ time that currently stands at 3%. We assume a 0.3 percentage point wedge between PCE and CPI inflation based on the historical relationship and estimates of the factors that influence both.
The new nominal in action

Our *New nominal* theme calls for a slower pace of rate hikes, than in the past, at similar levels of growth and inflation. This supports equities and other risk assets, in our view.

**U.S. policy rate path vs past cycles**

Forward looking estimates may not come to pass. Source: BlackRock Investment Institute, Federal Reserve and Federal Reserve Bank of New York, with data from Refinitiv Datastream, October 2021. Notes: The left chart shows the median Fed dot plot – or the median expectations of the members of Federal Open Market Committee, a committee within the Federal Reserve that makes key decisions about interest rates, past rate hiking cycles since 1994 and our estimates for the path U.S. interest rates. The paths are shown on a time horizon of when the first hike took place. The Fed median dot plot comes from the October 2021 Summary of Economic Projections. We believe the Fed will start its next hiking cycle by early 2023. The right chart shows our expectations for the European Central Bank’s policy rate, market-implied pricing of the rate path as of end-July 2021 and the average projection from the ECB Survey of Professional Forecasters (SPF). Market pricing is based on futures on the Euro Overnight Index Swap Rate. The BlackRock estimate is part of the macro model in our capital market assumptions. The ECB Survey of Professional Forecasters: https://www.ecb.europa.eu/stats/ecb_surveys/survey_of_professional_forecasters/html/index.en.html. The euro area comprises countries within the European Union that have adopted the euro and for whom monetary policy is set by the ECB.

**Expectations of ECB policy interest rates**

<table>
<thead>
<tr>
<th>Change in rate</th>
<th>2021</th>
<th>2022</th>
<th>2023</th>
<th>2024</th>
<th>2025</th>
</tr>
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<tr>
<td>0%</td>
<td>0.0%</td>
<td>-0.1%</td>
<td>-0.2%</td>
<td>-0.3%</td>
<td>-0.4%</td>
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<tr>
<td>1%</td>
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<td>2%</td>
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<td></td>
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<tr>
<td>3%</td>
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<td>4%</td>
<td></td>
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</tbody>
</table>

*Notes: The left chart shows the median Fed dot plot – or the median expectations of the members of Federal Open Market Committee, a committee within the Federal Reserve that makes key decisions about interest rates, past rate hiking cycles since 1994 and our estimates for the path U.S. interest rates. The paths are shown on a time horizon of when the first hike took place. The Fed median dot plot comes from the October 2021 Summary of Economic Projections. We believe the Fed will start its next hiking cycle by early 2023. The right chart shows our expectations for the European Central Bank’s policy rate, market-implied pricing of the rate path as of end-July 2021 and the average projection from the ECB Survey of Professional Forecasters (SPF). Market pricing is based on futures on the Euro Overnight Index Swap Rate. The BlackRock estimate is part of the macro model in our capital market assumptions. The ECB Survey of Professional Forecasters: https://www.ecb.europa.eu/stats/ecb_surveys/survey_of_professional_forecasters/html/index.en.html. The euro area comprises countries within the European Union that have adopted the euro and for whom monetary policy is set by the ECB.*
Employment mandate key for Fed policy outlook

U.S. labor market dynamics will likely determine the pace of interest rate hikes, in our view. There is more progress needed on this front – both on total payrolls and the labor force participation rate.

U.S. non-farm employment and labor force participation rate, October 2021

Forward looking estimates may not come to pass. Sources: BlackRock Investment Institute and U.S. Bureau of Labor Statistics, with data from Refinitiv Datastream, October 2021. Notes: The chart shows total U.S. nonfarm payrolls (orange line) and the U.S. labor force participation rate (yellow line). The labor force participation rate is the percentage of the working-age population that is working or actively looking for work. Full details here: https://www.bls.gov/charts/employment-situation/civilian-labor-force-participation-rate.htm
New ECB strategy should spur additional asset purchases
The ECB’s new policy framework loosens previous constraints to deliver easier policy. We see the central bank stepping up asset purchases once pandemic-emergency purchases expire next March.

ECB asset purchase programs and monthly buying amounts, 2009–2021

Sources: BlackRock Investment Institute and ECB, with data from Haver Analytics, October 2021. Notes: The chart shows the evolution of the ECB’s different asset purchase programs since the GFC. The ECB’s purchases started with covered bonds (CBPP) and during the sovereign debt crisis briefly included government bond purchases under the Securities Markets Programme (SMP). In 2015, the ECB expanded purchases to government and supranational bonds (PSPP) and asset-backed securities (ABSPP), then in 2016 corporate bonds (CSPP). These all make up the overall Asset Purchase Programme (APP).
Authorities can no longer ignore extent of China’s slowdown

Policymakers have been willing to sacrifice short-term growth for longer-term social objectives. Yet they are not insensitive to a sharp slowdown in near-term growth.

Changes in broad credit growth, 2014-2021

China GDP, real vs estimates, Sept 2021

Forward looking estimates may not come to pass, Sources: BlackRock Investment Institute, China’s Ministry of Finance with data from Haver Analytics, October 2021. Notes: The left chart shows the 12-month change in monthly broad credit growth as a percentage of GDP. The right chart shows actual and projected GDP growth. Consensus forecasts are from Reuters polls as of 22 September, 2021. The “downside scenario” path is our estimate of how growth may evolve in the absence of any policy easing.
Wide range of potential outcomes

How does the current environment compare with the recovery after global financial crisis? We are on a very different trajectory now, in our view. Historic fiscal stimulus and innovative monetary policy – the policy revolution – make a repeat of the 10-year bull market in stocks and bonds unlikely. Our base case: the new nominal.

Policy revolution
Historic fiscal and monetary policy helps drive the restart.

Initial shock
Weak response: broad deleveraging, sluggish growth, low and falling inflation, over-reliance on monetary policy.

Back to trend growth
Historic fiscal and monetary policy helps drive the restart and a return to pre-Covid trend pace of growth.

Roaring ‘20s
Boost to productivity and potential growth, leading to a permanent shift higher in growth amid contained inflation.
Bullish stocks, neutral bonds

You are here

Policy tightened too late
Lose control of inflation expectations; interest rates surge.
Bearish stocks and bonds

New nominal
Fed adjusts policy in line with new framework, staying well behind the curve. Inflation rises in medium term.
Bullish equities, neutral bonds

1929 redux
The new framework allows asset bubbles to swell and burst. We don’t see major imbalances yet to make this a concern.
Bearish stocks, neutral bonds

Historical policy response
Policy tightened before inflation rises sustainably above target. We don’t see this as possible given the policy and political response.

COVID-19

Post–2008
Slowest recovery in post-World War II history
Bullish stocks and bonds for a decade

Sources: BlackRock Investment Institute, July 2021. Notes: The schematic shows hypothetical macro and policy outcomes now compared with the sluggish outcome following the GFC. These are our views on the implications for equities and government bonds as of July 2021. For illustrative purposes only. There is no guarantee that any forecasts made will come to pass.

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We maintain a pro-risk tactical stance
Low real yields alongside a strong growth backdrop and our belief that a Fed taper will not lead to a tantrum keeps us pro-risk. We acknowledge the path for risk assets to push higher has narrowed.

U.S. 10-year real yield, 2019–2021

[Graph showing U.S. 10-year real yield, 2019-2021]

Market pricing of Fed rate hikes, Sept 2021

[Graph showing market pricing of Fed rate hikes, Sept 2021]

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, October 2021. Notes: The left chart shows the pricing of Treasury inflation protected securities – the 10-year TIPS yield, or real yield. The real yield strips out the expected impact of inflation over the next decade. The right chart shows current market pricing of Fed funds futures.
Turning moderately positive on Chinese equities

Current valuations on Chinese equities imply too pessimistic an outlook. Coupled with the incremental policy easing we anticipate, we believe it’s time to dip our toes back in.

Equity risk premium, China vs U.S., Sept 2021

- **China**
- **U.S.**

YTD total returns, China vs U.S., Sept 2021

- **China**
- **U.S.**

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. Source: BlackRock Investment Institute, with data from Refinitiv Datastream, October 2021. Notes: The left chart shows the estimated equity risk premium for the MSCI USA index and MSCI China index. The equity risk premium is implied using a dividend discount model therefore incorporates forward looking views on the future dividend stream and risk-free rates. The right chart shows year-to-date performance for the two indices.
We prefer EM local debt over EM equities
We see attractive valuations and carry on offer for EM local debt, particularly in a world starved for income. EM equities remain expensive relative to recent history, in our view.

Total returns EM debt vs high yield, 2021

Equity risk premium for EM, 1995–2021

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 Bloomberg, October 2021. Notes: The left chart shows the year-to-date total returns for EM local and hard currency bonds and global yield. Index proxies are: JPM EMBI Global Diversified - Index, JPM GBI-EM Composite - Index and the Bloomberg Barclays Global High Yield USD. The right chart shows the performance of a basket of EM currencies against the U.S. dollar as measured by the JPMorgan GBI-EM Global Diversified FX Return Index.
Maintaining a large underweight on U.S. Treasuries

We see a disconnect between real growth and yields. The balance of risks is for gradually higher yields in our view, keeping us underweight U.S. Treasuries.

U.S. 10-year yield, breakeven inflation and real yield vs. our estimates, October 2021

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Source: BlackRock Investment Institute and Refinitiv Datastream, data as of 8 October 2021. Notes: The chart shows the U.S. 10-year Treasury yield (nominal yield) and the pricing of Treasury inflation protected securities – the 10-year TIPS yield, or real yield, and the breakeven inflation rate, or the future rate of inflation being priced by markets in TIPS. The short bars on the chart show our 5-year ahead expected values for U.S. 10-year nominal yields using the Bloomberg Barclays U.S. Government bond index as a proxy and our estimates for the average U.S. personal consumption expenditures inflation rate in five years’ time. We derive this from our estimate of consumer price index in five years’ time that currently stands at 3%. We assume a 0.3 percentage point wedge between PCE and CPI inflation based on the historical relationship and estimates of the factors that influence both. Forward looking estimates may not come to pass.
We are overweight European equities, and neutral Japan

The accelerated restart and vaccination rollout supports our positive view European equities. Sentiment around Japan is also brightening keeping us neutral on its equity market.

Earnings revisions, 2018-2021

Covid vaccine doses administered, Sept 2021

Sources: BlackRock Investment Institute, with data from Refinitiv Datastream and Bloomberg, October 2021. Notes: The chart shows the three-month change in aggregate analyst expectations for corporate earnings for each region shown. The markets are represented by the MSCI EMU Index, MSCI USA Index, MSCI Emerging Markets Index and the MSCI Japan Index.

Sources: BlackRock Investment Institute, Our World in Data, October 2021. Notes: The chart shows the doses per 100 of approved Covid 19 vaccines administered in the respective countries as detailed by Our World in Data.
We prefer equity to credit in strategic allocations

We find more appeal in equities where valuations appear more in line with history even after the rally. Credit spreads have tightened to historical lows following the sharp rebound from last March.

Equity risk premiums and credit spreads current vs. historical, October 2021

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Source: BlackRock Investment Institute and Refinitiv Datastream, data as of October 2021. The chart shows the equity risk premium and historical ranges since 1995 for major equity regions based on MSCI indices and the credit spreads for the U.S. Investment Grade and High Yield markets based on Bloomberg Barclays indices. We calculate the equity risk premium based on our expectations for nominal interest rates and the implied cost of capital for respective equity markets. Credit spreads are calculated by taking the difference between the credit market yields and the corresponding government bond yields.
We take deliberate views across the yield curve

The new nominal theme leads to a steeper yield curve expectation than market pricing. We see yields rising gradually, keeping us broadly underweight government bonds, particularly for longer maturities.

U.S. yield curve vs estimates, August 2021

Euro area yield curve vs estimates, August 2021

Forward looking estimates may not come to pass. Past performance is no guarantee of future results. Source: BlackRock Investment Institute, with data from Refinitiv Datastream, August 2021. Notes: The charts compare our estimate of the shape of the U.S. and European yield curves in five years’ time with market-pricing implied projection and the spot yield curve as of 30 June 2021.
## Directional views

### Strategic (long-term) and tactical (6-12 month) views on broad asset classes, October 2021

<table>
<thead>
<tr>
<th>Asset</th>
<th>Strategic view</th>
<th>Tactical view</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Equities</strong></td>
<td><img src="chart1" alt="Chart" /></td>
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<tr>
<td></td>
<td>+1</td>
<td>+1</td>
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<tr>
<td><strong>Credit</strong></td>
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<td><img src="chart4" alt="Chart" /></td>
</tr>
<tr>
<td></td>
<td>-1</td>
<td>Neutral</td>
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<td></td>
</tr>
<tr>
<td><strong>Govt bonds</strong></td>
<td><img src="chart5" alt="Chart" /></td>
<td><img src="chart6" alt="Chart" /></td>
</tr>
<tr>
<td></td>
<td>-1</td>
<td>-1</td>
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<td></td>
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<tr>
<td><strong>Cash</strong></td>
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<tr>
<td></td>
<td>Neutral</td>
<td></td>
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</tr>
<tr>
<td><strong>Private markets</strong></td>
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<td><img src="chart10" alt="Chart" /></td>
</tr>
<tr>
<td></td>
<td>Neutral</td>
<td></td>
</tr>
</tbody>
</table>

We keep our overweight equities on a strategic horizon. We see a better outlook for earnings amid moderate valuations. 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 stay overweight equities as we expect the restart to re-accelerate and interest rates to stay low. We tilt toward cyclical and maintain a quality bias.

We stay underweight credit on a strategic basis as valuations are rich and we prefer to take risk in equities. On a tactical horizon, we are neutral credit following the tightening in spreads in investment grade and high yield.

We are strategically underweight nominal government bonds given their diminished ability to act as portfolio ballasts with yields near lower bounds. Rising debt levels may eventually pose risks to the low rate regime. This is part of why we underweight government debt strategically. We prefer inflation-linked bonds – particularly in the U.S. relative to the euro area on valuations. We add to our underweight on U.S. Treasuries on expectations of gradually rising yields.

We are moderately pro-risk and keep some cash to potentially further add to risk assets on any market turbulence.

We believe non-traditional return streams, including private credit, have the potential to add value and diversification. Our neutral view is based on a starting allocation that is much larger than what most qualified investors hold. Many institutional investors remain underinvested in private markets as they overestimate liquidity risks, in our view. Private markets are a complex asset class and not suitable for all investors.

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

<table>
<thead>
<tr>
<th>Region</th>
<th>View</th>
<th>Commentary</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>Neutral</td>
<td>We are neutral U.S. equities. We see U.S. growth momentum peaking and expect other regions to be attractive ways to play the next leg of the restart as it broadens to other regions, notably Europe and Japan.</td>
</tr>
<tr>
<td>U.S. small caps</td>
<td>+1</td>
<td>We stay overweight U.S. small-caps. We see potential in this segment of the U.S. equity market to benefit from the cyclical rebound in domestic activity brought about an accelerated vaccination rollout.</td>
</tr>
<tr>
<td>Europe</td>
<td>+1</td>
<td>We stay overweight European equities on the back of a strong growth backdrop. We see a sizeable pickup in activity helped by accelerating vaccinations. Valuations remain attractive relative to history and investor inflows into the region are only just starting to pick up.</td>
</tr>
<tr>
<td>UK</td>
<td>Neutral</td>
<td>We are neutral UK equities following their strong performance. We see the market as fairly valued and prefer European equities.</td>
</tr>
<tr>
<td>Japan</td>
<td>Neutral</td>
<td>We are neutral Japanese equities. We see a global cyclical rebound helping boost earnings growth in the second-half of the year. The country’s virus dynamics are also improving.</td>
</tr>
<tr>
<td>China</td>
<td>+1</td>
<td>We turn moderately positive on Chinese equities as we see a gradual dovish shift in monetary and fiscal policy in response to the cyclical slowdown and anticipate that the regulatory clampdown will become less intense.</td>
</tr>
<tr>
<td>Emerging markets</td>
<td>Neutral</td>
<td>We are neutral EM equities. We see more uncertainty on the U.S. dollar outlook due to a risk premium from Fed communication. Many EMs have started tightening policy, showing less policy support and a greater risk of scarring.</td>
</tr>
<tr>
<td>Asia ex-Japan</td>
<td>Neutral</td>
<td>We are neutral Asia ex-Japan equities. Potential knock-on effects from slower growth in China and broader geopolitical risks dampen the outlook, in our view.</td>
</tr>
</tbody>
</table>

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## Tactical granular views: fixed income

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

<table>
<thead>
<tr>
<th>Asset</th>
<th>View</th>
<th>Commentary</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Treasuries</td>
<td>-2</td>
<td>We are underweight U.S. Treasuries primarily on valuations. We see the balance of risks is for gradually higher yields as markets continue to price in the economic restart, especially given the pullback in yields in recent months.</td>
</tr>
<tr>
<td>Treasury Inflation-Protected Securities</td>
<td>+1</td>
<td>We are overweight U.S. TIPS. We believe the recent pullback in the asset class presents an attractive opportunity, particularly on a relative basis against European inflation breakevens as the outlook for euro area inflation remains sluggish.</td>
</tr>
<tr>
<td>German bunds</td>
<td>Neutral</td>
<td>We are neutral on bunds. Although the ECB may begin tapering this year given inflation dynamics, we see little room for a substantive change in policy in the near term.</td>
</tr>
<tr>
<td>Euro area peripherals</td>
<td>Neutral</td>
<td>We are neutral euro area peripheral government bonds despite recent outperformance given stability in ECB policy, low volatility in peripherals and better value elsewhere.</td>
</tr>
<tr>
<td>China government bonds</td>
<td>+1</td>
<td>We are overweight Chinese government bonds. We see the relatively stability of interest rates and the carry on offer as brightening their appeal.</td>
</tr>
<tr>
<td>Global investment grade</td>
<td>-1</td>
<td>We remain underweight investment grade credit. We see little room for further yield spread compression and favor more cyclical exposures such as Asian fixed income.</td>
</tr>
<tr>
<td>Global high yield</td>
<td>Neutral</td>
<td>We are neutral high yield after the asset class’ strong performance. Spreads are now below where we see high yield as attractive valued. We prefer to take risk in equities.</td>
</tr>
<tr>
<td>Emerging market – hard currency</td>
<td>Neutral</td>
<td>We are neutral hard-currency EM debt. We expect it to gain support from the vaccine-led global restart and more predictable U.S. trade policies.</td>
</tr>
<tr>
<td>Emerging market – local currency</td>
<td>+1</td>
<td>We upgrade local-currency EM debt to overweight. We believe the asset class offers attractive valuations and carry in a world starved for income.</td>
</tr>
<tr>
<td>Asia fixed income</td>
<td>+1</td>
<td>We are overweight Asia fixed income. Outside of China, we like Asia sovereigns and credit for their yield and income given the region’s fundamental outlook.</td>
</tr>
</tbody>
</table>

*Underweight | Neutral | Overweight*  ● Previous view

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