

Weekly commentary

December 4, 2023

BlackRock®

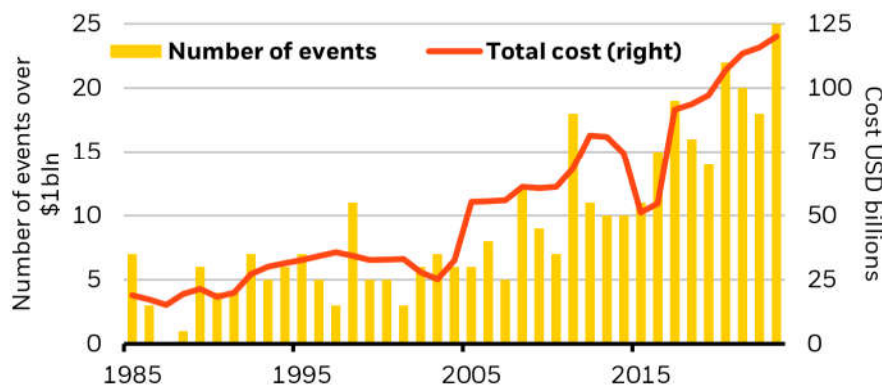
Three investment themes at COP28

- We track the low-carbon transition to identify investment opportunities and risks. We're eyeing three related themes at the annual UN climate conference.
- U.S. stocks last week hit their highest level of the year, and U.S. 10-year Treasury yields fell lower. We expect near-term volatility and rising yields in the long term.
- U.S. payrolls data this week will show if jobs growth is still slowing. We think the U.S. can only sustain a fraction of recent job growth without inflation resurging.

The low-carbon transition is one of five mega forces, or structural shifts, we track for investment risks and opportunities. We're following three investment themes at the UN climate conference (COP28) in Dubai. First, climate resilience – society's ability to prepare for and withstand climate risks – is an underappreciated theme, we think. Second, we eye progress on unlocking climate finance in emerging markets. Third, we watch for new policy plans that could shape the transition path.

Physical damages mount

U.S. events with inflation-adjusted losses over \$1 billion, 1985-2023



Source: BlackRock Investment Institute, NOAA National Centers for Environmental Information (NCEI) U.S. Billion-Dollar Weather and Climate Disasters (2023), data as of November 2023. Notes: The yellow bars show the number of climate events with losses greater than US\$1 billion. The data include droughts, flooding, severe storms, hurricanes, wildfires, winter storms and freezes. The orange line shows the total cost as a 10-year moving average. The data are adjusted for inflation using 2022 dollars. All currency figures are in USD.

We highlight climate resilience first because it is an emerging theme not yet fully appreciated by investors. We think companies that create and adopt products and services that boost climate resilience will become a more widely recognized opportunity. Why? The number of U.S. climate events with damages above \$1 billion has steadily climbed over the past roughly four decades. See the yellow bars in the chart. As such risks increase, we are seeing early signs of growing demand for climate resilience solutions. Case in point: Demand for home air-filtration appliances in the northeastern U.S. spiked during the Canadian wildfires in early 2023. Emerging markets (EMs) are set to bear some of these risks more acutely given greater exposure to physical climate damage. Yet they face difficulties in raising financing needed for the transition. We think this also offers an investment opportunity and is key to tracking the transition's overall speed and shape.



Wei Li

Global Chief Investment Strategist – BlackRock Investment Institute



Christopher Kaminker

Head of Sustainable Research and Analytics – BlackRock Investment Institute



Chris Weber

Head of Climate Research – BlackRock Investment Institute



Jessica Thyne

Sustainable Research and Analytics – BlackRock Investment Institute

Visit [BlackRock Investment Institute](#) for insights on the global economy, markets and geopolitics.

BlackRock
Investment
Institute

The IPCC has reported persistent increases in average annual temperatures, precipitation and sea levels. The frequency and intensity of acute weather events, such as extreme heat and widespread floods, has also increased. We see policy and regulation driving the growth of the market for resilience products. Any COP28 agreement on a global plan for climate adaption could spur new policy. Some incentives to invest in resilience are already in place, including \$50 billion from the Infrastructure Investment and Jobs Act and over \$20 billion from the Inflation Reduction Act. Other support comes from building code updates in the U.S. and Europe explicitly focusing on improving climate resilience. Read more in our [new paper](#).

We are closely watching policy developments that could unlock investment opportunities in EMs. They play a pivotal role in the global reduction in carbon emissions, in our view. Why? We estimate EM will account for over half of energy demand and carbon emissions by 2050. Yet transition-related investment in EMs will likely be lower than in DMs due to a higher cost of capital from greater perceived investment risk, and greater exposure to physical climate damage. We think closing the financing gap would require significant public sector reforms and private sector innovation, resulting in greater "blending" of public and private capital. We think successful reforms could see low-carbon investment in EMs rise on average by a further \$200 billion a year – or \$4 trillion overall – above our base view of a major increase in investment between 2030–2050.

We think COP28 will also provide further details about policies that are likely to influence how the mix of energy use evolves – and the investment opportunities. We see policy, technology and consumer preferences driving an accelerating shift to renewable energy in DMs. 2023 has seen record growth of about 50–70% for renewable energy, according to the International Energy Agency. Countries at COP28 look poised to agree to a goal to triple capacity by 2030. We think further policy support may make the goal achievable – and yet the S&P global clean energy index is down about 28% year to date, LSEG data show. Even with this growth in renewables, meeting global energy demand will rely on traditional energy for some time – and we think it can outperform at times, especially when there are supply-demand mismatches.

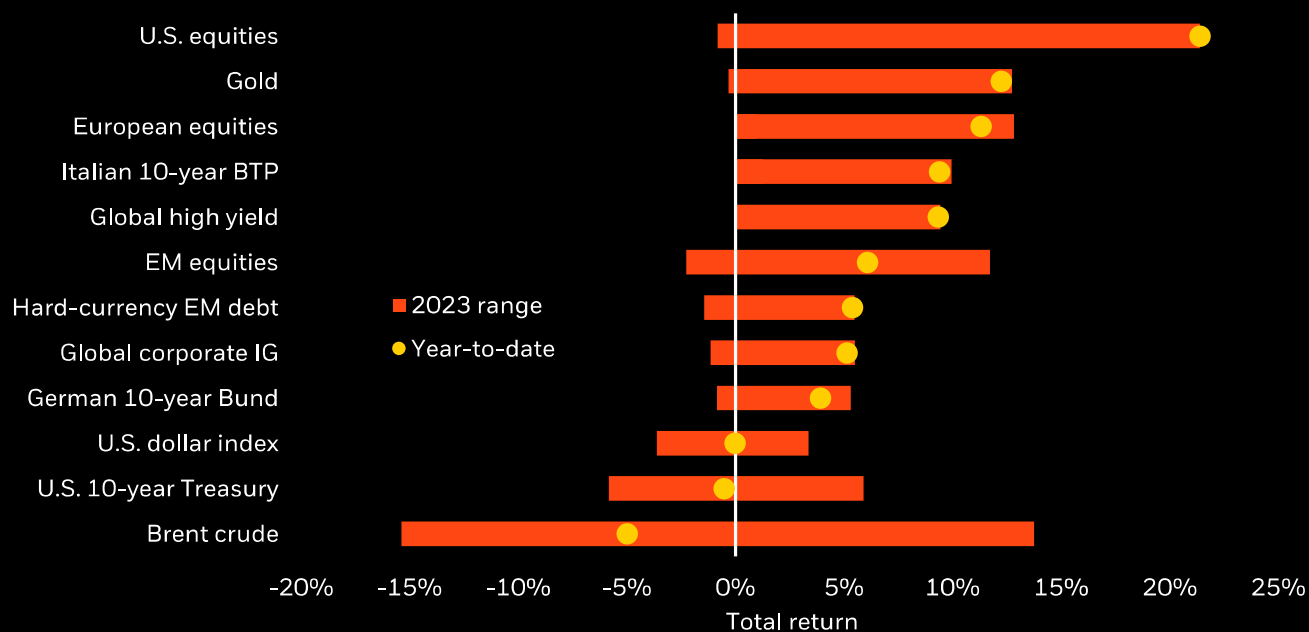
Bottom line: We monitor COP28 for signs of growth in transition-related investment themes. We see granular opportunities in public companies that produce climate resilience solutions across sectors. Solutions like early monitoring systems to predict floods or retrofitting buildings to better withstand extreme weather make the technology and industrial sectors stand out to us. And we think reforms could make it easier for private market players to fill the EM financing gap.

Market backdrop

Last week, the S&P 500 closed at its highest level this year after rising roughly 9% in November – the largest monthly gain in 16 months. The U.S. 10-year Treasury yield slid lower to near 4.30%, with its November drop of more than 50 basis points marking the largest monthly fall in 12 years. We expect further volatility for bonds in the near term as policy rates peak. We think long-term yields will rise again as investors demand more compensation for the risk of holding long-term bonds.

Assets in review

Selected asset performance, 2023 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 Nov. 30, 2023. Notes: The two ends of the bars show the lowest and highest returns at any point in the last 12-months, and the dots represent current year-to-date returns. Emerging market (EM), high yield and global corporate investment grade (IG) returns 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, MSCI Emerging Markets Index, MSCI Europe Index, LSEG Datastream 10-year benchmark government bond index (U.S., Germany and Italy), Bank of America Merrill Lynch Global High Yield Index, J.P. Morgan EMBI Index, Bank of America Merrill Lynch Global Broad Corporate Index and MSCI USA Index.

Macro take

U.S. activity data released last week revealed weaker economic growth in Q3 than earlier data suggested. The average of income- and spending-based measures of activity shows Q3 growth was 3.3% lower than the 5.1% reported by spending-based data alone. That's still above the recent trend, but we think it's an outlier. Zooming out shows growth over the past seven quarters hasn't been this weak outside a recession since 1945. See the chart.

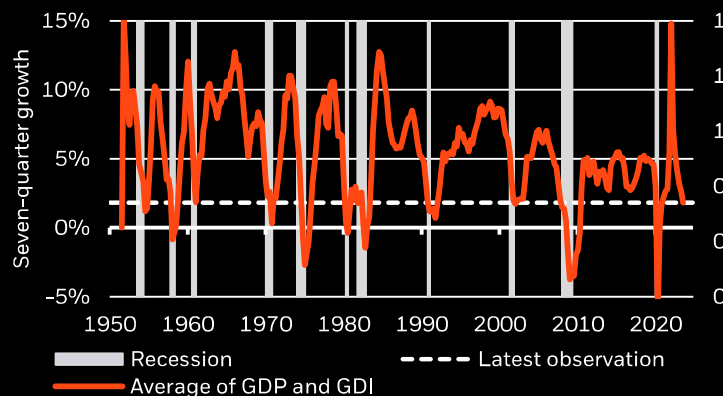
Strong spending fueled Q3 growth as consumers drew from pandemic savings. We don't think that's sustainable: Spending data for October shows consumers are saving much less today than they were pre-pandemic. So we don't expect strong growth next year as spending slows.

Even with weaker growth ahead, we don't see the Federal Reserve cutting rates as quickly as markets expect. We think rates cuts will come in the second half of 2024 but see inflationary pressures keeping rates higher than before.

Read our latest Macro take post [here](#).

Stealth stagnation

Seven-quarter growth in U.S. activity, 1950-2023



Source: BlackRock Investment Institute, U.S. Bureau of Economic Analysis, with data from Haver Analytics, December 2023. Notes: The chart shows U.S. activity growth over a rolling seven-quarter period (orange line). The white dotted line shows the most recent observation (for 2023Q3), and gray shaded bands show U.S. recessions as defined in the National Bureau of Economic Research classification of business cycles.

Investment themes

1 Holding tight

- The U.S. is navigating two large and unprecedented shocks. The first: A massive, pandemic-induced shift in consumer spending — most visible from services to goods — created a mismatch in what the economy was set up to produce and what people wanted to buy. The second: a worker shortage as baby boomers age into retirement.
- Our assessment is that we are set for “full-employment stagnation.” Most of the inflation and wage growth we’ve seen to date reflects the mismatch associated with the pandemic. That is now reversing, and inflation is set to fall further. But as the process of resolving the mismatch ends and labor shortages start to bind, we expect inflation to go on a rollercoaster ride, rising again in 2024. A smaller workforce means the rate of growth the economy will be able to sustain without resurgent inflation will be lower than in the past.
- We see central banks being forced to keep policy tight to lean against inflationary pressures. This is not a friendly backdrop for broad asset class returns, marking a break from the four decades of steady growth and inflation known as the Great Moderation.
- **Investment implication:** Income is back. That motivates our overweight to short-dated U.S. Treasuries.

2 Pivoting to new opportunities

- Greater volatility has brought more divergent security performance relative to the broader market. Benefiting from this requires getting more granular and eyeing opportunities on horizons shorter than our tactical one. We go granular by tilting portfolios to areas where we think our macro view is priced in.
- We think dispersion within and across asset classes — or the extent to which prices deviate from an index — will be higher in the new regime amid the various crosscurrents at play, allowing for granularity. That offers more ways to build portfolio “breadth” via uncorrelated exposures, in our view.
- We think it also means security selection, expertise and skill are even more important to achieving above benchmark returns. Relative value opportunities from potential market mispricings are also likely to be more abundant.
- **Investment implication:** We like quality in both equities and fixed income.

3 Harnessing mega forces

- Mega forces are structural changes we think are poised to create big shifts in profitability across economies and sectors. These mega forces are digital disruption like artificial intelligence (AI), the rewiring of globalization driven by geopolitics, the transition to a low-carbon economy, demographic divergence and a fast-evolving financial system.
- The mega forces are not in the far future — but are playing out today. The key is to identify the catalysts that can supercharge them and the likely beneficiaries — and whether all of this is priced in today. We think granularity is key to find the sectors and companies set to benefit from mega forces.
- We think markets are still assessing the potential effects as AI applications could disrupt entire industries.
- Geopolitical fragmentation, like the strategic competition between the U.S. and China, is set to rewire global supply chains, we think.
- The low-carbon transition causing economies to decarbonize at varying speeds due to policy, tech innovation and shifting consumer and investor preferences. Markets have historically been slow to fully price in such shifts.
- We see profound changes in the financial system. Higher rates are accelerating changes in the role of banks and credit providers, shaping the future of finance.
- **Investment implication:** We are overweight AI as a multi-country, multi-sector investment cycle unfolds.

Week ahead

Dec. 5

Japan CPI; China PMI

Dec. 8

U.S. payrolls; University of Michigan consumer sentiment survey

Dec. 7

China trade data

Dec. 9

China CPI and PPI

The U.S. payrolls report for November is in focus this week. We are looking for signs that job growth is slowing further as the post-pandemic normalization runs its course. Structural labor shortages as the U.S. population ages means the economy will only be able to sustain a fraction of recent job growth without stoking inflation again, in our view.

Directional views

Strategic (long-term) and tactical (6-12 month) views on broad asset classes, December 2023

		Underweight	Neutral	Overweight	● Previous view	
		Asset	Strategic	Tactical	Commentary	
Equities	Developed					

Note: Views are from a U.S. dollar perspective. 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.

Granular views

Six- to 12-month tactical views on selected assets vs. broad global asset classes by level of conviction, December 2023

		Underweight	Neutral	Overweight	Previous view
Asset	View	Commentary			
Equities	Developed markets				
	United States			We are underweight the broad market – still our largest portfolio allocation. We don't think earnings expectations reflect the macro damage we expect. We recognize momentum is strong near term.	
	Europe			We are underweight. We see the European Central Bank holding policy tight in a slowdown, and the support to growth from lower energy prices is fading.	
	UK			We are neutral. We find that attractive valuations better reflect the weak growth outlook and the Bank of England's sharp rate hikes to deal with sticky inflation.	
	Japan			We are overweight. We think stronger growth can help earnings top expectations. Stock buybacks and other shareholder-friendly actions may keep attracting foreign investors.	
	Pacific ex-Japan			We are neutral. China's restart is losing steam and we don't see valuations compelling enough to turn overweight.	
	DM AI mega force			We are overweight. We see a multi-country and multi-sector AI-centered investment cycle unfolding set to support revenues and margins.	
	Emerging markets			We are neutral. We see growth on a weaker trajectory and see only limited policy stimulus from China. We prefer EM debt over equity.	
Fixed Income	China			We are neutral. Growth has slowed. Policy stimulus is not as large as in the past. Yet it should stabilize activity, and valuations have come down. Structural challenges imply deteriorating long-term growth. Geopolitical risks persist.	
	Short U.S. Treasuries			We are overweight. We prefer short-term government bonds for income as interest rates stay higher for longer.	
	Long U.S. Treasuries			We are neutral. The yield surge driven by expected policy rates is approaching a peak. We now see about equal odds that long-term yields swing in either direction.	
	U.S. inflation-linked bonds			We are overweight and prefer the U.S. over the euro area. We see market pricing underestimating sticky inflation.	
	Euro area inflation-linked bonds			We are underweight. We prefer the U.S. over the euro area. We see markets overestimating how persistent inflation in the euro area will be relative to the U.S.	
	Euro area govt bonds			We are overweight. Market pricing reflects policy rates staying higher for longer even as growth deteriorates. Widening peripheral bond spreads remain a risk.	
	UK gilts			We are overweight. Gilt yields are holding near their highest in 15 years. Markets are pricing in restrictive Bank of England policy rates for longer than we expect.	
	Japanese govt bonds			We are underweight. We see upside risks to yields from the Bank of Japan winding down its ultra-loose policy.	
	China govt bonds			We are neutral. Bonds are supported by looser policy. Yet we find yields more attractive in short-term DM paper.	
	Global IG credit			We are underweight. We take advantage of tight credit spreads to fund increased risk-taking elsewhere in the portfolio. We look to up the allocation if growth deteriorates.	
	U.S. agency MBS			We're overweight. We see agency MBS as a high-quality exposure within diversified bond allocations.	
	Global high yield			We are underweight. Spreads do not fully compensate for slower growth and tighter credit conditions we anticipate.	
	Asia credit			We are neutral. We don't find valuations compelling enough to turn more positive.	
	Emerging hard currency			We are overweight. We prefer emerging hard currency debt due to higher yields. It is also cushioned from weakening local currencies as EM central banks start to cut policy rates.	
	Emerging local currency			We are neutral. Yields have fallen closer to U.S. Treasury yields. Plus, central bank rate cuts could put downward pressure on EM currencies, dragging on potential returns.	

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. 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.

BlackRock Investment Institute

The BlackRock Investment Institute (BII) leverages the firm's expertise and generates proprietary research to provide insights on macroeconomics, sustainable investing, geopolitics and portfolio construction to help BlackRock's portfolio managers and clients navigate financial markets. BII offers strategic and tactical market views, publications and digital tools that are underpinned by proprietary research.

General disclosure: This material is intended for information purposes only, and does not constitute investment advice, a recommendation or an offer or solicitation to purchase or sell any securities to any person in any jurisdiction in which an offer, solicitation, purchase or sale would be unlawful under the securities laws of such jurisdiction. The opinions expressed are as of Dec. 4, 2023, and are subject to change without notice. Reliance upon information in this material is at the sole discretion of the reader. Investing involves risks. This information is not intended to be complete or exhaustive and no representations or warranties, either express or implied, are made regarding the accuracy or completeness of the information contained herein. This material may contain estimates and forward-looking statements, which may include forecasts and do not represent a guarantee of future performance.

In the **U.S. and Canada**, this material is intended for public distribution. In **EMEA**, in the UK and Non-European Economic Area (EEA) countries: this is Issued by BlackRock Investment Management (UK) Limited, authorised and regulated by the Financial Conduct Authority. Registered office: 12 Throgmorton Avenue, London, EC2N 2DL. Tel: + 44 (0)20 7743 3000. Registered in England and Wales No. 02020394. For your protection telephone calls are usually recorded. Please refer to the Financial Conduct Authority website for a list of authorised activities conducted by BlackRock. In the European Economic Area (EEA): this is Issued by BlackRock (Netherlands) B.V. is authorised and regulated by the Netherlands Authority for the Financial Markets. Registered office Amstelplein 1, 1096 HA, Amsterdam, Tel: 020 – 549 5200, Tel: 31-20-549-5200. Trade Register No. 17068311 For your protection telephone calls are usually recorded. In **Italy**, for information on investor rights and how to raise complaints please go to <https://www.blackrock.com/corporate/compliance/investor-right> available in Italian. In **Switzerland**, for qualified investors in Switzerland: This document is marketing material. Until 31 December 2021, this document shall be exclusively made available to, and directed at, qualified investors as defined in the Swiss Collective Investment Schemes Act of 23 June 2006 ("CISA"), as amended. From 1 January 2022, this document shall be exclusively made available to, and directed at, qualified investors as defined in Article 10 (3) of the CISA of 23 June 2006, as amended, at the exclusion of qualified investors with an opting-out pursuant to Art. 5 (1) of the Swiss Federal Act on Financial Services ("FinSA"). For information on art. 8 / 9 Financial Services Act (FinSA) and on your client segmentation under art. 4 FinSA, please see the following website: www.blackrock.com/finisa For investors in **Israel**: BlackRock Investment Management (UK) Limited is not licensed under Israel's Regulation of Investment Advice, Investment Marketing and Portfolio Management Law, 5755-1995 (the "Advice Law"), nor does it carry insurance thereunder. In **South Africa**, please be advised that BlackRock Investment Management (UK) Limited is an authorized financial services provider with the South African Financial Services Board, FSP No. 43288. In the **DIFC** this material can be distributed in and from the Dubai International Financial Centre (DIFC) by BlackRock Advisors (UK) Limited – Dubai Branch which is regulated by the Dubai Financial Services Authority (DFSA). This material is only directed at 'Professional Clients' and no other person should rely upon the information contained within it. BlackRock Advisors (UK) Limited - Dubai Branch is a DIFC Foreign Recognised Company registered with the DIFC Registrar of Companies (DIFC Registered Number 546), with its office at Unit 06/07, Level 1, Al Fattan Currency House, DIFC, PO Box 506661, Dubai, UAE, and is regulated by the DFSA to engage in the regulated activities of 'Advising on Financial Products' and 'Arranging Deals in Investments' in or from the DIFC, both of which are limited to units in a collective investment fund (DFSA Reference Number F000738). In the **Kingdom of Saudi Arabia**, issued in the Kingdom of Saudi Arabia (KSA) by BlackRock Saudi Arabia (BSA), authorised and regulated by the Capital Market Authority (CMA), License No. 18-192-30. Registered under the laws of KSA. Registered office: 29th floor, Olaya Towers – Tower B, 3074 Prince Mohammed bin Abdulaziz St., Olaya District, Riyadh 12213 – 8022, KSA, Tel: +966 11 838 3600. The information contained within is intended strictly for Sophisticated Investors as defined in the CMA Implementing Regulations. Neither the CMA or any other authority or regulator located in KSA has approved this information. In the **United Arab Emirates** this material is only intended for -natural Qualified Investor as defined by the Securities and Commodities Authority (SCA) Chairman Decision No. 3/R.M. of 2017 concerning Promoting and Introducing Regulations. Neither the DFSA or any other authority or regulator located in the GCC or MENA region has approved this information. In the **State of Kuwait**, those who meet the description of a Professional Client as defined under the Kuwait Capital Markets Law and its Executive Bylaws. In the **Sultanate of Oman**, to sophisticated institutions who have experience in investing in local and international securities, are financially solvent and have knowledge of the risks associated with investing in securities. In **Qatar**, for distribution with pre-selected institutional investors or high net worth investors. In the **Kingdom of Bahrain**, to Central Bank of Bahrain (CBB) Category 1 or Category 2 licensed investment firms, CBB licensed banks or those who would meet the description of an Expert Investor or Accredited Investors as defined in the CBB Rulebook. The information contained in this document, does not constitute and should not be construed as an offer of, invitation, inducement or proposal to make an offer for, recommendation to apply for or an opinion or guidance on a financial product, service and/or strategy. In **Singapore**, this is issued by BlackRock (Singapore) Limited (Co. registration no. 200010143N). This advertisement or publication has not been reviewed by the Monetary Authority of Singapore. In **Hong Kong**, this material is issued by BlackRock Asset Management North Asia Limited and has not been reviewed by the Securities and Futures Commission of Hong Kong. In **South Korea**, this material is for distribution to the Qualified Professional Investors (as defined in the Financial Investment Services and Capital Market Act and its sub-regulations). In **Taiwan**, independently operated by BlackRock Investment Management (Taiwan) Limited. Address: 28F., No. 100, Songren Rd., Xinyi Dist., Taipei City 110, Taiwan. Tel: (02)23261600. In **Japan**, this is issued by BlackRock Japan. Co., Ltd. (Financial Instruments Business Operator: The Kanto Regional Financial Bureau. License No375, Association Memberships: Japan Investment Advisers Association, the Investment Trusts Association, Japan, Japan Securities Dealers Association, Type II Financial Instruments Firms Association.) For Professional Investors only (Professional Investor is defined in Financial Instruments and Exchange Act). In **Australia**, issued by BlackRock Investment Management (Australia) Limited ABN 13 006 165 975 AFSL 230 523 (BIMAL). The material provides general information only and does not take into account your individual objectives, financial situation, needs or circumstances. In **New Zealand**, issued by BlackRock Investment Management (Australia) Limited ABN 13 006 165 975, AFSL 230 523 (BIMAL) for the exclusive use of the recipient, who warrants by receipt of this material that they are a wholesale client as defined under the New Zealand Financial Advisers Act 2008. In **China**, this material may not be distributed to individuals resident in the People's Republic of China ("PRC", for such purposes, excluding Hong Kong, Macau and Taiwan) or entities registered in the PRC unless such parties have received all the required PRC government approvals to participate in any investment or receive any investment advisory or investment management services. For **Other APAC Countries**, this material is issued for Institutional Investors only (or professional/sophisticated /qualified investors, as such term may apply in local jurisdictions). In **Latin America**, no securities regulator within Latin America has confirmed the accuracy of any information contained herein. The provision of investment management and investment advisory services is a regulated activity in Mexico thus is subject to strict rules. For more information on the Investment Advisory Services offered by BlackRock Mexico please refer to the Investment Services Guide available at www.blackrock.com/mx

©2023 BlackRock, Inc. All Rights Reserved. BLACKROCK is a trademark of BlackRock, Inc., or its subsidiaries in the United States and elsewhere. All other trademarks are those of their respective owners.

BlackRock

Not FDIC Insured • May Lose Value • No Bank Guarantee