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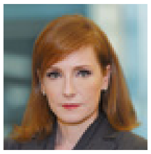

Kate Moore
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Key points

1 We see the momentum equity style factor outperforming, backed by a sustained economic expansion.

2 Oil prices entered a bear market on concerns about higher-than-anticipated global supply.

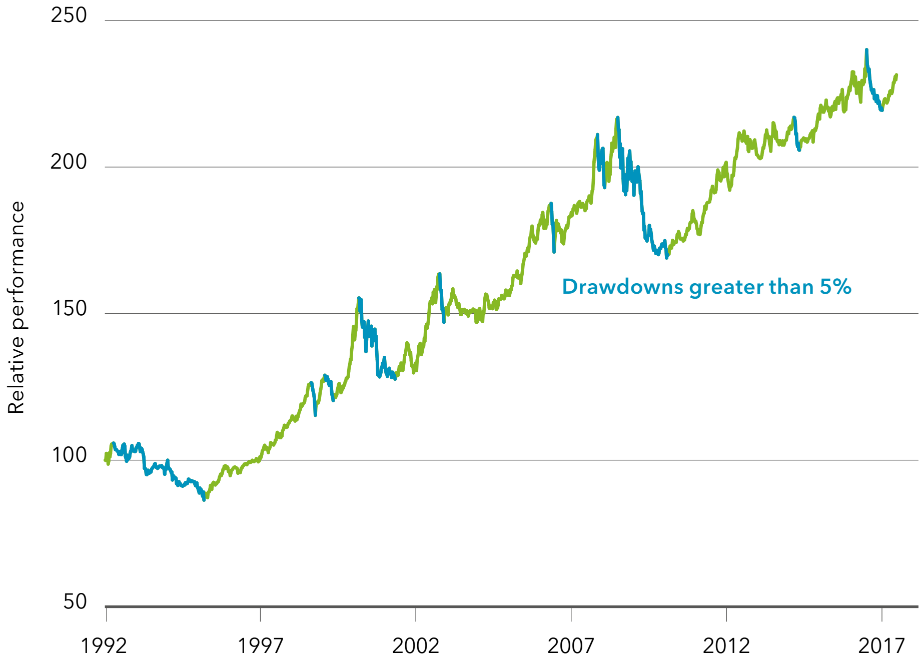
3 This week's U.S. and eurozone inflation data could shed some light on the direction of central bank policies.

1 Momentum's rally has legs

The momentum style factor – stocks that are trending higher in price – has been on a tear in 2017. Sustained above-trend economic growth and solid earnings prospects could help extend the gains, but it may be a bumpy ride.

Chart of the week

Relative performance of world momentum stocks, 1992-2017



Sources: BlackRock Investment Institute and MSCI, June 2017.
Notes: The line shows the performance of the MSCI ACWI Momentum Index relative to the MSCI ACWI Index, dividing the former by the latter and rebasing to 100 at the start of 1992. Areas in blue show periods of drawdowns, or peak-to-trough declines, of more than 5%, based on weekly data.

Momentum has historically outrun the broader market, but with periodic sharp drops. The biggest dips in its relative performance have coincided with recessions and financial crises. Our research shows momentum tends to perform best during steady economic expansions – and we see this cycle having ample room to run.

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Not just about tech

The technology sector has become the main driver behind momentum recently. The sector has the highest earnings growth forecast in 2017 outside of energy and materials, and technology is increasingly disrupting traditional business models.

A sharp drop in tech stocks caused a break in the momentum rally in mid-June. But we believe such episodes shouldn't spook investors. Momentum drawdowns typically last two months or less, barring major economic or financial shocks, our analysis of market data since 1991 suggests. The momentum factor today includes significant exposure to financials, which can help cushion the downside during any tech sell-off. In addition, analysis by BlackRock's Scientific Active Equity team points to an unusually broad set of macro and fundamental drivers behind the momentum factor. And we don't see the factor as particularly crowded or expensive. This points to resilience behind the trend.

We see the sustained economic expansion keeping us in a low-volatility regime longer than many expect. This bodes well for momentum trades. But a sudden shift in stock leadership as a result of a global growth slowdown, weaker-than-anticipated profits or a spike in bond yields could threaten the rally. Bottom line: We like momentum in today's economic environment, even if its performance could be prone to short-lived reversals.

2 Week in review

- Oil prices entered a bear market on concerns about higher-than-anticipated global supply. Energy-related stocks dropped, high yield energy debt sold off and emerging market currencies fell.
- MSCI announced it would include China A-shares in some of its indexes from mid-2018 — a key step toward opening China's stock market to foreign investment, though not an immediate game changer.
- Federal Reserve officials' speeches reinforced Chair Janet Yellen's message of ongoing policy normalization. The U.S. dollar rose and the Treasury yield curve reached its flattest level since 2007.

Global snapshot

Weekly and 12-month performance of selected assets

Equities	Week	YTD	12 Months	Div. Yield
U.S. Large Caps	0.2%	8.9%	15.4%	2.0%
U.S. Small Caps	0.6%	4.9%	22.4%	1.2%
Non-U.S. World	0.1%	14.2%	16.4%	3.1%
Non-U.S. Developed	-0.2%	14.1%	15.0%	3.2%
Japan	0.4%	10.9%	18.5%	2.1%
Emerging	1.0%	18.3%	23.8%	2.7%
Asia ex-Japan	1.3%	23.0%	27.5%	2.4%

Bonds	Week	YTD	12 Months	Yield
U.S. Treasuries	0.2%	2.6%	-0.2%	2.1%
U.S. TIPS	0.5%	1.6%	1.4%	2.1%
U.S. Investment Grade	0.3%	4.4%	4.2%	3.1%
U.S. High Yield	-0.4%	4.6%	12.0%	5.7%
U.S. Municipals	0.1%	4.1%	0.8%	2.2%
Non-U.S. Developed	-0.1%	6.2%	-3.5%	0.7%
EM $ Bonds	-0.3%	6.6%	7.7%	5.3%

Commodities	Week	YTD	12 Months	Level
Brent Crude Oil	-3.9%	-19.9%	-10.5%	$45.5
Gold	0.2%	9.5%	0.0%	$1,256.7
Copper	2.4%	4.8%	21.3%	$5,800.5

Currencies	Week	YTD	12 Months	Level
Euro/USD	0.0%	6.4%	-1.7%	1.12
USD/Yen	0.4%	-4.9%	4.8%	111.28
Pound/USD	-0.5%	3.1%	-14.5%	1.27

Source: Bloomberg. As of June 23, 2017. Notes: Weekly data through Friday. Equity and bond performance are measured in total index returns in U.S. dollars. U.S. large caps are represented by the S&P 500 Index; U.S. small caps are represented by the Russell 2000 Index; Non-U.S. world equity by the MSCI ACWI ex U.S.; non-U.S. developed equity by the MSCI EAFE Index; Japan, Emerging and Asia ex-Japan by their respective MSCI Indexes; U.S. Treasuries by the Bloomberg Barclays U.S. Treasury Index; U.S. TIPS by the U.S. Treasury Inflation Notes Total Return Index; U.S. investment grade by the Bloomberg Barclays U.S. Corporate Index; U.S. high yield by the Bloomberg Barclays U.S. Corporate High Yield 2% Issuer Capped Index; U.S. municipals by the Bloomberg Barclays Municipal Bond Index; non-U.S. developed bonds by the Bloomberg Barclays Global Aggregate ex USD; and emerging market $ bonds by the JP Morgan EMBI Global Diversified Index. Brent crude oil prices are in U.S. dollars per barrel, gold prices are in U.S. dollar per troy ounce and copper prices are in U.S. dollar per metric ton. The Euro/USD level is represented by U.S. dollar per euro, USD/JPY by yen per U.S. dollar and Pound/USD by U.S. dollar per pound. Index performance is shown for illustrative purposes only. It is not possible to invest directly in an index. Past performance is not indicative of future results.

3 Week ahead

June 28 Fed releases Comprehensive Capital Analysis and Review (CCAR) results for large banks

June 30 Eurozone inflation; U.S. Personal Consumption Expenditures (PCE); Japan Consumer Price Index (CPI), unemployment

June 26-30 U.S. Senate votes on health care bill

Markets expect the PCE reading – the Fed's preferred gauge for inflation – to fall further from its 2% target. Another weak reading on eurozone core inflation could provide more backing for a patient approach by the European Central Bank toward winding back stimulus.

Asset class views

Views from a U.S. dollar perspective over a three-month horizon

Asset class		View	Comments
Equities	U.S.	–	2017 earnings momentum is strong. Fading prospects for tax reform have been largely discounted, leaving room for positive surprises. We like value, momentum, financials, technology and dividend growers.
	Europe	▲	We see global reflation and an improving earnings outlook supporting cyclicals and exporters, particularly industrials and multinationals with EM exposures.
	Japan	▲	Positives are improving global growth, more shareholder-friendly corporate behavior and earnings upgrades amid a stable yen outlook. We see BoJ policy and domestic investor buying as supportive. Risks are yen strength and rising wages.
	EM	▲	Economic reforms, improving corporate fundamentals and reasonable valuations support EM stocks. Reflation and growth in the developed world are other positives. Risks include sharp changes in currency, trade or other policies.
	Asia ex-Japan	▲	The region's economic backdrop is encouraging. China's economic growth and corporate earnings outlook look solid in the near term. We like India, China and selected Southeast Asian markets.
Fixed income	U.S. government bonds	▼	Reflation challenges nominal bonds. We favor TIPS for the long run after valuations cheapened amid falling oil prices and weaker inflation readings. We are neutral on agency mortgages due to current valuations and potential future impacts of the Fed's balance sheet run off.
	U.S. municipals	–	Higher rates post election and muted issuance have restored value, and investor interest has perked up amid positive performance and market expectations that tax reform may be delayed or watered down. We are neutral on duration and favor 20+ year bonds.
	U.S. credit	▲	Stronger growth favors credit over Treasuries. We generally prefer up-in-quality exposures and investment grade bonds due to elevated credit market valuations. Floating-rate bank loans appear to offer insulation from rising rates, but we find them pricey.
	European sovereigns	▼	Markets' focus on improving economic data and high valuations make us cautious. Waning political risks should cause core eurozone yields to rise, and spreads of semi-core and selected peripheral government bonds to narrow.
	European credit	▼	Risks are tilted to the downside amid heady valuations and the possibility of shifting market expectations for central bank support. We are defensive and prefer selected subordinated financial debt.
	EM debt	–	We see broadening of growth beyond the U.S. benefiting EMs and limiting risks from dollar appreciation. This makes local currency debt more attractive to us. We see selected opportunities, but high valuations keep us neutral overall.
	Asia fixed income	–	We like markets with positive fundamentals and reform momentum, such as India. The upside is limited as spreads have compressed. A positive cyclical outlook for China is supportive, but U.S. trade protectionism is a risk.
Other	Commodities and currencies	–	We see further large declines in oil prices as unlikely – and believe fears of a supply glut are likely to moderate in coming months. We see gradual U.S. dollar strength in the medium term due to interest rate differentials with many other advanced economies.

▲ Overweight – Neutral ▼ Underweight

BlackRock Investment Institute

The ***BlackRock Investment Institute*** (BII) provides connectivity between BlackRock's portfolio managers, originates economic and markets research, develops investment views for clients, and publishes insights. Our goals are to help our portfolio managers become even better investors and to produce thought-provoking investment content for clients and policymakers.

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