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iShares by BlackRock

Precision insights: Credit

May 2026

Highlights

- **Credit markets entered Q2 in a holding pattern, with spreads no longer at their tights but stabilising at wider levels than the start of the year.** Geopolitical tensions, higher energy prices and shifting central bank expectations are keeping risk appetite in check. While macro fundamentals and investor demand continue to provide a cushion, differentiation across regions and sectors is becoming more pronounced, with Europe relatively more vulnerable, in our view.
- **In Europe, credit dynamics are increasingly driven by issuer- and sector-specific factors rather than broad market trends,** with uneven rating movements in investment grade (IG) and significant repricing in leveraged loans creating selective opportunities. Stressed loan valuations and evolving CLO demand are reshaping relative value versus high yield (HY), reinforcing a preference for higher-quality exposures and careful sector selection.

We outline our current views on broad developed market (DM) credit exposures, updated to reflect the latest macro and microeconomic developments.

Click through to explore our precision credit views in detail.

Exposure	View	Outlook
€IG		**€IG spreads remain resilient in absolute terms, but the balance of risk is less supportive than earlier in the year,** as Europe faces a weaker growth and policy backdrop than the US. We prefer selectivity over a broad up-in-quality shift: we think spread widening is likely to stay modest but rating and sector dispersion should continue to build, with caution warranted in more rate- and energy-sensitive BBB segments.
€HY		**€HY remains the more vulnerable part of the regional credit complex,** with wider risk premia, softer technicals, and greater sensitivity to slower growth, higher input costs, and refinancing pressure. Leveraged loan and CLO signals point to a more defensive backdrop, and while defaults are still expected to stay below the 2024 highs, we think stress will remain concentrated in lower-quality, floating-rate, and more cyclical issuers.
$IG		**$IG looks relatively better positioned for Q2,** in our view, supported by firmer underlying fundamentals, resilient earnings, strong yield-based demand and better relative value versus Europe. Within the market, we continue to prefer higher-quality exposure, especially longer-dated single-A credit, where curve steepening and attractive all-in yields offer a stronger entry point than lower-rated, long-end paper, we think.
$HY		**$HY should remain supported by a still-constructive macro base case and healthy demand for carry,** but spreads are likely to stay somewhat wider than earlier in the year as investors price a more uncertain rate, inflation and geopolitical backdrop. We expect only a moderate rise in defaults from here, with risks centred less on a broad systemic shock and more on issuer-specific pressure points such as private credit-linked stress, software exposure and highly levered refinancing stories.
CLOs		**European AAA-rated CLOs offer high-quality, floating-rate income with minimal duration risk, we believe,** supported by strong structural protections, resilient demand, and yields that remain attractive relative to similarly rated credit.

Note: $ denotes US dollar, unless stated otherwise.

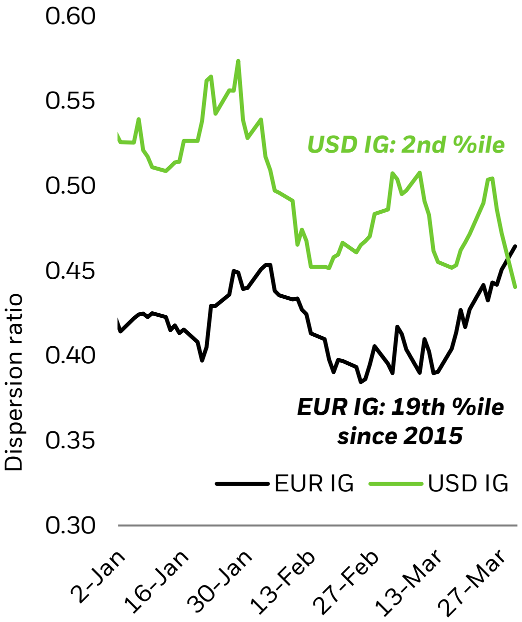
€IG

Our view on €IG sits between a more constructive stance on $IG and a more cautious view on €HY. From a valuation perspective, €IG spreads have only modestly widened, despite increased macro risks. All-in yields provide some cushion following the rise in Bund yields, we think, but valuations still appear tight relative to downside risks from weaker growth and sustained energy price pressures, particularly given Europe's significant dependence on energy imports.

Turning to technicals, demand from yield-oriented investors continues to anchor the market, supported by a relatively manageable supply backdrop, with below-average issuance recently.[1] This stands in contrast to the US, where heavy tech-led issuance has weighed more meaningfully on technicals. That said, dispersion has begun to rebuild in €IG, rising from the 3rd to the 19th percentile,[2] as investors increasingly differentiate between sectors exposed to energy costs and cyclical pressures.

Fundamentally, credit quality remains broadly stable but increasingly uneven. Financials – particularly banks and insurers – remain resilient, in our view, while energy-linked sectors benefit from pricing power, despite gradually rising leverage. In contrast, consumer and other energy-intensive sectors are facing margin compression and higher leverage. The primary risks remain a prolonged energy shock, weaker European growth, European Central Bank (ECB) policy constraints and further spread decompression – particularly in lower-quality and cyclical segments. However, more limited exposure to private credit spillovers and large-scale tech issuance than €IG reduces idiosyncratic pressures, we think, leaving €IG supported but without a strong catalyst for outperformance.

Chart 1: €IG dispersion has been falling since the start of the year
Sector level dispersion for €IG and $IG, January-March 2026



Source: Goldman Sachs, as of 2 April 2026.

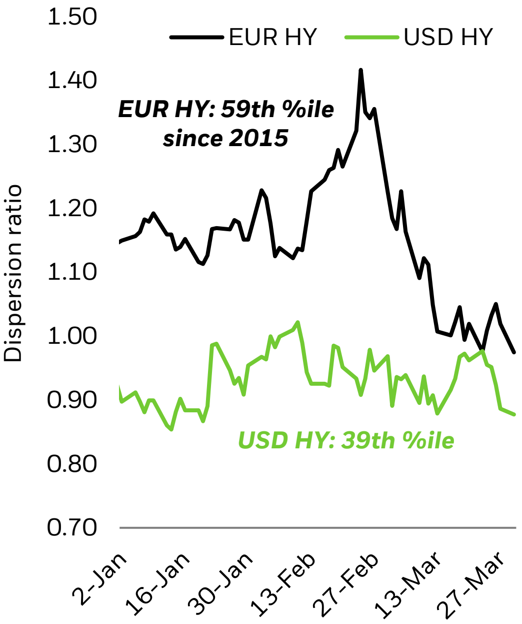
€HY

€HY warrants a mildly negative stance, in our view, reflecting an increasingly fragile balance between improved headline valuations and a deteriorating macro/technical backdrop. Spreads have widened but remain anchored by a still-benign default regime and therefore don't fully compensate for Europe's weaker growth trajectory (~1.0% versus 2.5% in the US)[3] and heightened sensitivity to a prolonged energy shock. Weaker investor appetite versus $HY and persistently elevated dispersion (c.59th percentile)[4] suggest that the market is transitioning from idiosyncratic to more systemic repricing, with scope for further decompression, particularly in lower-quality cohorts. 2026 YTD default rates of 4.5% in Europe versus a still modest 3.1% in the US further underscores our regional preference.

Technicals are becoming more complex and less uniformly supportive. While yield-based demand and manageable near-term maturity walls provide a buffer, underlying loan market dynamics point to weakening risk appetite. The European Leveraged Loan Index has repriced materially, with over 90% of loans now trading below par (versus 36% in December) and the share of distressed assets rising to 7.8% (the highest since April 2020).[5] Meanwhile, relative value versus loans remains stretched (c.158bp pickup, ~92nd percentile).[6]

Fundamentally, the outlook is deteriorating at the margin. Higher energy costs are compressing margins in input-sensitive sectors (autos, transport, consumer), while tighter financial conditions and potential for ECB hikes raise refinancing risk for floating-rate borrowers. Although default expectations remain below prior peaks (~4%),[7] downgrade trends and 'repeat defaulter' dynamics are building, particularly in sponsor-backed and software-exposed segments. Combined with higher equity beta and macro sensitivity, this leaves €HY exposed to further spread widening and performance dispersion, in our view.

Chart 2: High yield dispersion has fallen across geographies, particularly Europe
Sector level dispersion for €HY and $HY, January-March 2026



Source: Goldman Sachs, as of 2 April 2026.

$IG

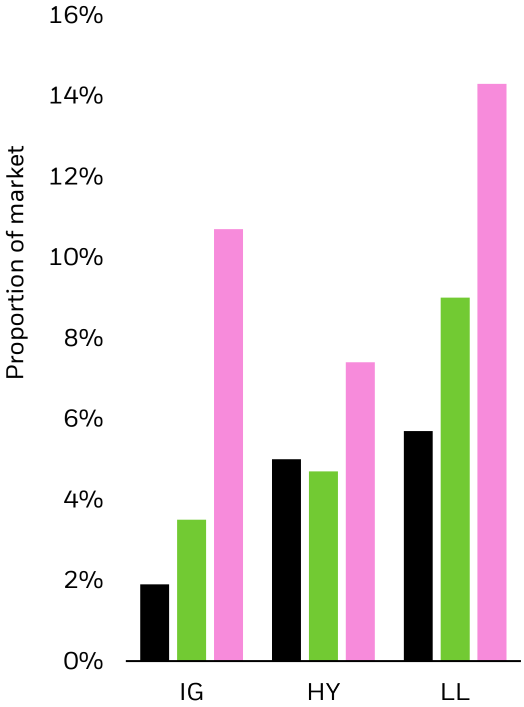
$IG has become our preferred overweight after recent geopolitical events, given the relative resilience of technicals and fundamentals, rather than outright valuations. Whilst $IG screens as expensive versus €IG (~10bps),[8] under the hood this premium reflects structural advantages exposed by the recent energy shock. Notably, spreads have held within a relatively tight range despite oil volatility and geopolitical escalation, demonstrating lower beta to broader risk than both €IG and HY. Our systematic fixed income team's signals support this view and they see increased security selection opportunity in energy and basic materials, including chemicals and metals.

The supply/demand backdrop for $IG has turned more complex but remains supportive, on net. Year-to-date US corporate issuance has reached ~$775B (+15-16% year-on-year),[9] with a pronounced skew towards long-end maturities and A-rated issuers, particularly large-cap technology and hyperscalers funding AI-related capex. This has driven curve steepening (notably in 10s30s) and created episodic indigestion in the long end. In parallel, the US market also carries greater exposure to private credit (~$1.3T ecosystem)[10] and recent BDC-related stress (including rising redemptions and gating) has introduced a new technical overhang, particularly via financials and structured credit linkages.

However, demand remains structurally deep and diversified, which is the key offset. Foreign inflows – especially from Asia – have accelerated, with buying skewed towards higher-quality and intermediate tenors, while elevated all-in yields (~5%)[11] continue to anchor demand from liability-driven and yield-sensitive investors. Issuance has begun to slow into blackout periods, dealer inventories have improved and hedging markets (such as CDX and futures) are providing additional liquidity buffers. **Fundamentals reinforce this technical resilience,** through stronger margins, better earnings momentum than other regions and >2% trend growth.

Chart 3: Tech has become a significant component of US credit markets

Tech sector outstanding debt as a proportion of US index market value, 2006-2026



Source: J.P. Morgan, as of 16 April 2026. LL=leveraged loans.

$HY

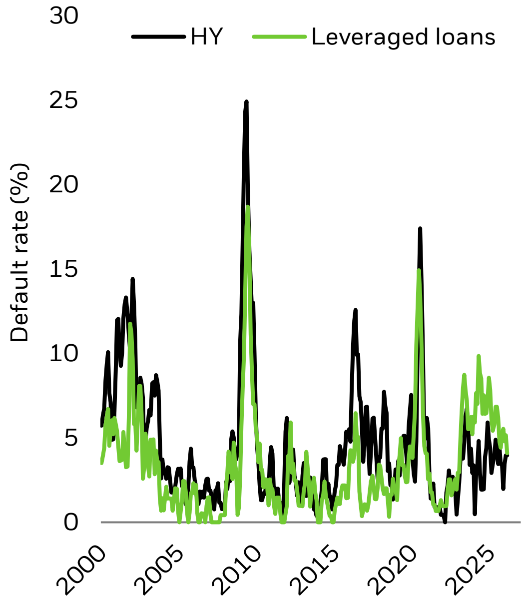
We turn more mixed on $HY, which has repriced modestly wider. Index spreads have moved through 300bps for the first time since June 2025,[12] but the more relevant signal is the internal dispersion and quality segmentation. While median spreads have widened c.45bp from year-to-date tights (to ~214bps),[13] this remains near the 11th percentile historically,[14] indicating that the selloff has been orderly. The widening has been driven disproportionately by lower-quality cohorts: single-B spreads are >30bps wider versus June 2025,[15] with unsecured Bs lagging most (~37bps),[16] underscoring increasing differentiation by capital structure and refinancing risk, rather than broad macro repricing.

Technicals and market structure distinguish HY from IG. Exposure to private credit is more direct, with BDC-related stress feeding through to $HY via finance companies. Technology-related risk is more acute in HY through lower-rated, capex-intensive or disruption-exposed issuers, whereas in IG issuance is concentrated in higher-quality balance sheets. The HY bond market composition provides a partial offset, however: it's more heavily weighted towards asset-intensive sectors (e.g. energy ~11%, basic industry ~9%)[17] and less exposed to software than leveraged loans (c.4-5% versus ~14-15%),[18] supporting relative fundamental resilience, in our view.

Primary activity has become increasingly episodic and event-driven (~$26B in March, >50% of which was M&A-related),[19] with forward supply likely constrained amid elevated yields (~7%+).[20] Overall, while carry remains supportive, rising dispersion, private credit spillovers and weak sentiment towards unsecured exposures reinforce our selective bias, favouring secured structures and asset-backed sectors over lower-quality, growth-sensitive segments.

Chart 4: High frequency default rates for $HY and leveraged loan issuers have been falling

Three-month trailing issuer-weighted default rate in $HY and leveraged loan markets



Source: Goldman Sachs, as of 2 April 2026.

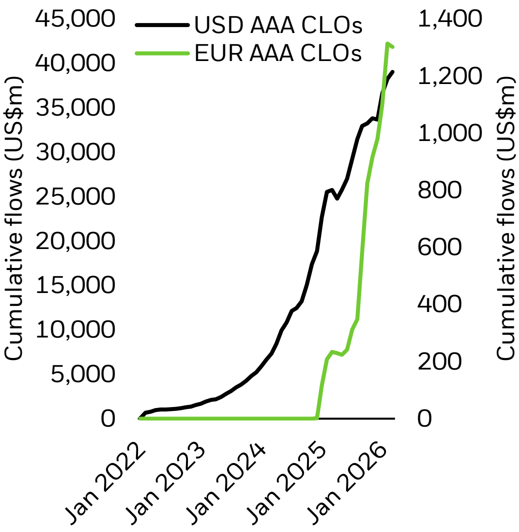
CLOs

AAA-rated collateralised loan obligations (CLOs) remain one of the more interesting areas of public credit for investors seeking high-quality income without taking on meaningful duration risk, in our view. Structurally, they sit at the top of the CLO capital stack, benefiting from substantial credit enhancement and historically very low impairment experience, while their floating-rate coupons reset regularly with policy rates. That combination has helped support relatively stable pricing versus many traditional fixed income segments and makes the asset class relevant in portfolios where investors want to preserve income while limiting sensitivity to rate volatility, we believe. Due to these features, demand for AAA-rated CLO ETFs has remained resilient globally, despite markets experiencing broader volatility and risk-off sentiment.

The case today is about recognising resilient fundamentals and demand in senior CLOs, we think, despite a more uncertain macro backdrop. The AAA CLO market still benefits from benign portfolio fundamentals, resilient demand and spreads that remain wider than similarly rated corporate credit, although the tone has become more selective as investors monitor deterioration in lower-quality loan tails more closely. AAA-rated CLOs still offer higher yields than other short duration € & $ IG strategies.

Chart 5: Demand in AAA-Rated CLO ETFs has remained resilient

Global flows into AAA-rated CLOs, January 2022-January 2026



Source: BlackRock, as of 31 March 2026.

Currency hedging

Hedging currency risk can significantly impact both total returns and yield of credit allocations. The cost or benefit of hedging is largely driven by interest rate differentials, with higher-yielding currencies incurring a hedging cost when converting to lower-yielding currencies, due to the negative carry from FX forwards. Conversely, hedging from a low-rate currency into a higher-rate currency can enable investors to enhance returns by capturing the forward premium. Over time, this dynamic has shifted: while EUR-USD hedging was once seen as uneconomical for a $-based investor and generally worthwhile for a €-based investor, due to the stark rate differentials, higher yields in € credit and higher policy rates in the US relative to Europe, the risks have equalised, making hedging decisions more balanced in terms of return impact.

Notes

1, 9 Source: Goldman Sachs, as of 2 April 2026.

2, 4, 6, 14 Source: Goldman Sachs, as of 2 April 2026, covering the period January to March 2026.

3, 5, 8, 11, 12, 13, 15, 16, 17, 18 Source: Bloomberg, as of 8 April 2026.

7, 10, 19, 20 Source: Barclays, as of 27 March 2026.

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