
Fixed Income Outlook

Q2 2026

BlackRock

Contents

**Global fixed income:
Getting paid while the
picture develops**

04

**Systematic view:
You can run, but you still
can't hedge**

06

**European fixed income:
Short-term noise, long-
term drivers of return**

09

**Income and selectivity in
emerging markets debt**

12

**Divergence across
economies creates
opportunity in Asia**

15

**Repricing and selectivity
in municipal bonds**

17

Foreword



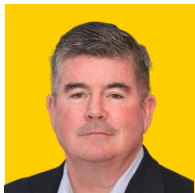
Rick Rieder

Chief Investment Officer
of Global Fixed Income



Tom Parker

Chief Investment Officer
of Systematic Fixed Income



Pat Haskell

Head of the Municipal
Bond Group

When the drivers change, positioning matters

A different kind of shock

Fixed income dynamics are shifting as the drivers shaping outcomes change. Geopolitical tensions in the Middle East have contributed to an energy-driven supply shock, lifting inflation in the near term while weighing on growth expectations.

An energy-driven supply shock changes how fixed income behaves. When inflation pressure comes from the supply side rather than demand, yields can remain elevated even as growth slows, correlations between rates and spreads can flip and dispersion across sectors and ratings becomes more pronounced. In this context, where capital is allocated matters as much as how much is allocated.

At the same time, artificial intelligence (AI) is accelerating a capital expenditure cycle that is reshaping corporate balance sheets, labor markets and the trajectory of productivity growth. The effects are already visible in credit markets, where AI-exposed sectors are dominating the narrative, generating different cash flow profiles and repricing more rapidly than the broader market, in both directions.

Wider dispersion, more deliberate positioning

Together, these forces are creating a fundamentally different opportunity set. Carry is playing a more central role, supported by higher starting yields that can absorb meaningful rate volatility. Outcomes across portfolios are diverging more noticeably, and this backdrop demands creativity, drawing on the full toolkit of global fixed income markets rather than relying solely on traditional core bonds.

This is an environment where active fixed income can play a more meaningful role in portfolios. In this quarter's Fixed Income Outlook, our teams across global markets explore these themes in greater detail, highlighting the opportunities and risks we see across regions and sectors.

“

Carry is playing a more central role, supported by higher starting yields that can absorb meaningful rate volatility.

Global fixed income: Getting paid while the picture develops



Rick Rieder

Chief Investment Officer
of Global Fixed Income

“

Navigating today's landscape requires what we call Dynamic Patience: deliberately building income, staying tactical on duration and deploying capital creatively.

The fixed income landscape entering the second quarter is defined by a tension that we think will persist for some time: a macro environment clouded by supply-side inflation and policy uncertainty, set against the most attractive yield opportunity in over a decade. Navigating that tension requires what we call Dynamic Patience: building income deliberately, staying tactical on duration and deploying capital creatively when the market misprices risk.

The first quarter sets the stage

The escalation of geopolitical tensions in the Middle East drove three to four standard deviation moves in front-end rates across developed and emerging markets. For instance, the German 2-year moved 72 basis points (bps) and Brazil's 2-year moved 158 bps.¹ Further, oil spiked in a way that immediately reshaped inflation expectations, pushing European markets to price policy rate hikes instead of cuts. Equities fell nearly 10%, and yet U.S. investment grade 10-year spreads widened just 15 bps and high yield BB widened 54 bps, underscoring the resilience of credit fundamentals.² Yet, this also highlights how narrow the compensation is for taking blunt spread risk at current levels.

The macro backdrop supports carry and precision, not broad beta

The U.S. economy remains structurally sound. Indeed, real household wealth is near all-time highs, debt-to-net-worth is at a seven-decade low, and capital spending is elevated with the AI buildout providing durable support. Even with crude oil prices at greater than \$100/barrel, we expect 2.1% real GDP growth this year, but the resilience is unevenly distributed. The fact is that the top 30% of consumers by income account for roughly half of all spending, and lower-income households spend 3.7% of income on gasoline versus 1.5% for the top decile.³ A major U.S. airline reported in the first quarter that premium and loyalty revenue grew in the mid-teens, even as economy-class volumes softened. This is the same economy, but increasingly we are witnessing very different experiences under the surface, as an energy shock doesn't soften demand uniformly; it concentrates stress in exactly the consumer-facing sectors where credit selection matters most.

The Fed's reaction function appears to have shifted at the April meeting

The Federal Open Market Committee's inflation assessment was upgraded to "elevated," and the range of plausible forward policy paths is wider than at any point since the cutting cycle began.

¹ Bloomberg, as of Mar. 31, 2026.

² Bloomberg, as of Mar.31, 2026.

³ Bureau of Economic Analysis and Bureau of Labor Statistics, as of Dec. 31, 2023.

Global fixed income: Getting paid while the picture develops

The urgency to ease has diminished, and absent a meaningful deterioration in labor markets, the timeline for any further cuts has likely extended. At the same time, U.S. front-end issuance now exceeds 100% of GDP, more than triple what it was just 10 years ago.⁴ The sensitivity of the debt trajectory to the path of rates and nominal growth means the fiscal position remains a critical variable in the policy calculus. For our portfolios, the implication is clear: the rate path is too uncertain for concentrated duration bets. We favor income-producing assets where carry adequately compensates us for holding through volatility, rather than making large bets on the direction of various points on the curve.

Yield, not spread, is where the opportunity lies

Credit spreads sit near the 5th percentile of the last eight years, and we do not see a compelling opportunity in spread compression from here.⁵ But all-in yields have risen alongside rates, and a diversified, income-oriented approach that uses the full fixed income universe, including securitized assets, European credit and emerging markets, can potentially generate north of 6% today, compared to roughly 4.6% for the U.S. Aggregate. In fact, high-quality, carry-focused, portfolios can deliver five times the real income of a cash allocation.⁶ We view this as a generationally attractive proposition for using fixed income as a source of meaningful, reliable income. Over any reasonable horizon, it is persistent carry, not attempting to time the bottom, that drives real returns.

Looking ahead, dispersion and flexibility will be key differentiators

In securitized assets, structure, yield and issuer-level variation make this a strong space for precision income, and patient investors can capitalize on

genuine dislocations as conditions evolve. In high yield, the widening gap between winners and losers means security selection matters far more than it did at earlier points in the cycle. Mortgages at nearly 1% spread with declining rate volatility offer an attractive diversifier to credit risk, with long/short opportunities across the coupon stack. And European peripheral rates, where the foreign exchange (FX) hedges work in your favor, look like a more attractive "spread product" than traditional corporate credit.

We also see meaningful opportunities in using the full toolkit that global macro and fixed income markets provide. Elevated implied volatility across rates, FX and credit has created attractive entry points for selling volatility where the market is overpricing tail risk. We can harvest premium from volatility that reflects fear rather than fundamentals, supplementing portfolio carry while maintaining a manageable convexity profile. Cross-market relative value, currency-hedged carry trades and structured credit all present return sources that a narrower approach would miss.

Our positioning reflects these convictions, and we are building income across the broadest opportunity set available, while staying tactical on duration, and using periods of elevated volatility to add exposures at better entry points. The macro picture will take time to resolve, but in the interim, we believe the most productive use of that time is to let carry compound, stay selective and maintain the flexibility to act decisively when conditions do shift. That is Dynamic Patience, and it is the framework we expect to guide our approach through the period ahead.

⁴ U.S. Treasury, as of Dec. 31, 2025.

⁵ Bloomberg, as of Apr. 16, 2026.

⁶ BlackRock and Bloomberg, as of Apr. 16, 2026.

Systematic view: You can run, but you still can't hedge



Tom Parker
Chief Investment
Officer, Systematic
Fixed Income



Jeffrey Rosenberg
Senior Portfolio
Manager, Systematic
Fixed Income

“

In a world of repeated supply shocks, and with inflation still persistently above target, bonds no longer hedge every form of risk.

The current macroeconomic backdrop is defined by more frequent and persistent supply shocks, a shift that is central to the fixed income outlook.

March added another example. The Iran oil shock did not produce a traditional growth scare, where weaker risk assets are offset by falling yields and reliable bond hedging. Instead, yields rose sharply, particularly in the front and intermediate segments of the curve, and bonds again failed to provide the diversification investors had come to expect in prior cycles.

That distinction matters because it reflects a broader shift in the macro environment. Before COVID, the dominant concern was persistent disinflation. Markets were shaped by a world of low neutral rates, repeated encounters with the lower bound and too low inflation that struggled to reach target even during long expansions.

Policy was geared toward that reality, with heavy use of forward guidance and asset purchases, and ultimately the adoption of flexible average inflation targeting after years of below-target inflation. At the time of the 2020 framework review, the “new normal” was widely understood to be one of low rates, low growth and low inflation, with ongoing concern that even a mild downturn would push policy back to the lower bound.

Post-pandemic, the nature of macro shocks has shifted. Inflation has been driven less by weak demand and more by disruptions to prices and supply, including commodity shocks and sector-

specific price spikes as demand collided with constrained supply. In each case, the negative macro surprise has arrived with an inflationary, rather than disinflationary, impulse.

The March episode fits squarely within that pattern. The war quickly moved the market away from a late-cycle expansion baseline, where modest Federal Reserve (Fed) easing later in the year still appeared plausible, toward a regime dominated by inflation repricing.

The initial outlook had favored front-end duration under a benign pre-war backdrop, but once the energy shock took hold, global rates markets traded primarily on inflation rather than growth concerns.

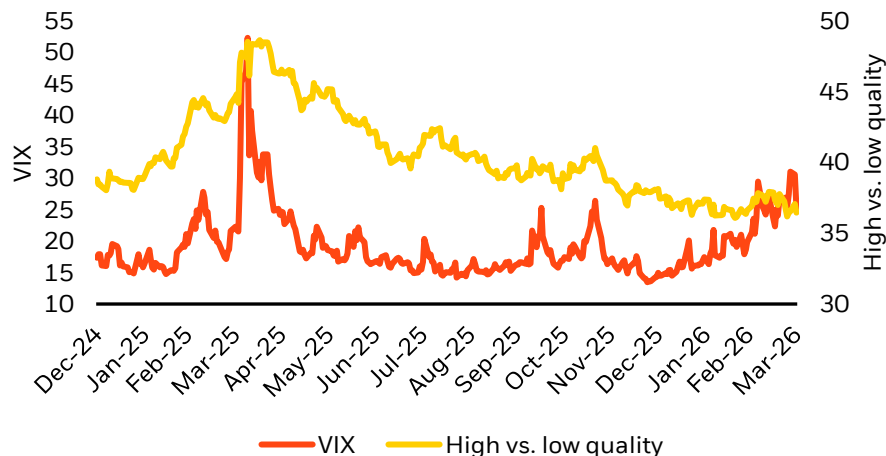
The first chart on the next slide shows how broader risk markets responded. Volatility rose sharply through March, but the relative performance of high- versus low-quality assets moved far less. This was not a classic recessionary rotation, where markets reward balance-sheet strength and penalize weaker quality.

Instead, the move was more consistent with broad de-risking. Volatility increased, correlations rose and investors appeared to be reducing overall exposure rather than reallocating toward a new set of fundamental winners. This reinforces that March was driven by a top-down inflation shock, rather than a fully formed growth slowdown that would more naturally support duration.

Systematic view: You can run, but you still can't hedge

Volatility spiked in March, without a typical risk-off rotation

VIX and high vs. low quality measure



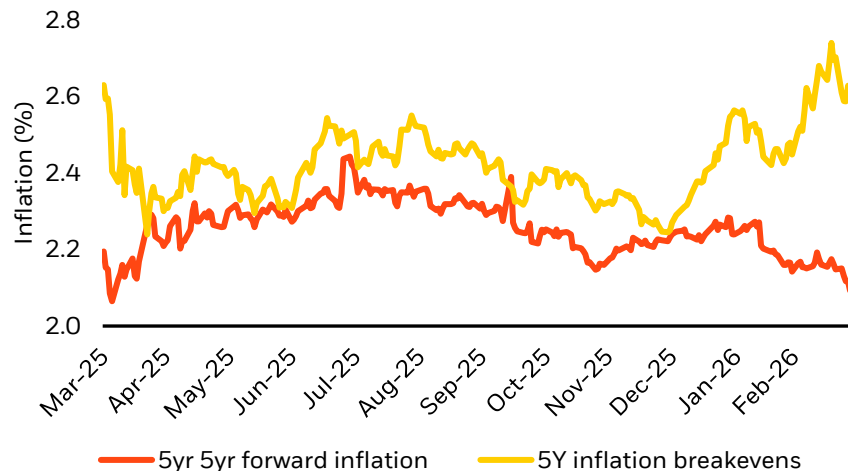
Bloomberg, as of Mar. 31, 2026. VIX Index and Bloomberg U.S. Low vs. High Leverage Index (LEVR).

The second chart shows the same dynamic in fixed income markets. Markets moved quickly to price the near-term inflationary effects of the war, reflected in the sharp rise in five-year breakeven inflation. At the same time, longer-run expectations moved lower, with 5y5y forward inflation drifting down over the month.

This combination points to a clear interpretation of the shock: Higher near-term inflation alongside weaker longer-term growth. It is also consistent with the flattening of the nominal Treasury curve from roughly the three-year sector out to the long end during March. Markets repriced the inflation impulse at the front end, while also recognizing that large or persistent energy shocks ultimately weigh on growth.

Short vs. long inflation expectations diverged in March

5-year breakeven inflation vs. 5y5y forward inflation



Bloomberg, as of Mar. 31, 2026.

That sequencing should remain central to the Q2 outlook. In the initial phase of a supply-driven inflation shock, duration can fail as a hedge, with yields rising alongside risk aversion. With inflation still above target, central banks have limited scope to lower rates, even as equity markets weaken. That constraint limits the reliability of bonds as a hedge. Only later, if the shock begins to weigh more meaningfully on demand and activity, shifting the balance of risks away from inflation and toward growth, does duration begin to recover its traditional defensive role.

Systematic view: You can run, but you still can't hedge

That is why the current fixed income stance argues for measured exposure rather than an aggressive duration call. Shorter maturities remain the cleaner place to own duration, with less exposure to the initial inflation repricing while preserving optionality if the growth consequences become more visible. At the same time, the relative case for lower-quality credit remains weak. Credit spreads still appear tight and offer limited compensation for the tail risks associated with a more disruptive energy scenario.

The broader lesson is that pre-COVID reflexes cannot be applied mechanically to the current environment. In a world of repeated supply shocks, and with inflation still persistently above target, bonds no longer hedge every form of risk in the same way or on the same timetable. The fixed income opportunity set remains attractive, but it depends on correctly diagnosing the nature of the shock. That, in turn, increases the need for a more systematic, data-driven approach to identifying these shifts and adjusting exposures as they unfold. March was a reminder that today's macro regime is not one of chronic disinflation and persistent lower-bound anxiety, but one in which supply-side disturbances more frequently drive both inflation and market outcomes.

European fixed income: Short-term noise, long-term drivers of return



James Turner
Head of Global
Fixed Income in
EMEA



Pradeep Swamy
Head of EMEA
Macro Investments
Office of the CIO,
Global Fixed Income

“

The environment is creating opportunities for patient capital, particularly where pricing has diverged from fundamentals.

Markets have been marked by heightened volatility, driven by geopolitical developments in the Middle East, energy-related supply shocks and shifting expectations for central bank policy.

Uncertainty has pushed many investors to the sidelines, leaving significant cash awaiting clarity. At the same time, equity technicals remain supportive, with buybacks continuing to outpace IPO activity, while in fixed income, new issues continue to see healthy demand at attractive yields, reinforcing the resilience of the asset class through recent volatility.⁷

Supply-driven shocks have important implications for monetary policy. While they tend to push inflation higher in the near term, they are also likely to weigh on demand, consumption and, in turn, growth. In this context, where investors take duration risk is important, as they assess the timing and impact of the Iran conflict.

In Europe, the conflict has increased uncertainty around the economic, monetary and fiscal outlook, raising downside risks to growth and upside risks to inflation. Our economists model euro area inflation rising from 1.9% YoY in February to around 3% under a de-escalation scenario by 2026 Q4.⁸ More adverse outcomes could push inflation higher, although these scenarios are not our central expectation.

Higher inflation, tighter financial conditions and uncertainty are likely to weigh on growth, although the risk of a deep recession remains limited given resilient household and private sector balance sheets.

Outside of a severe shock, fiscal policy is likely to be more restrained than in 2022 across both the euro area and the UK, with support remaining limited and more targeted. Monetary policy will remain highly contingent on the evolution of the conflict. Under a de-escalation scenario, the European Central Bank is likely to hold while the Bank of England could resume easing later this year or next. Further increases in energy prices could prompt renewed tightening, although outside of an extreme scenario, aggressive hiking cycles appear unlikely.

Staying anchored in a shifting macro backdrop

Despite recent market moves, the environment is creating opportunities for patient capital, particularly where pricing has diverged from fundamentals. Staying invested while selectively capturing shorter-term opportunities and maintaining focus on durable return drivers remains critical.

⁷ S&P Dow Jones Indices and Dealogic for equity supply dynamics; Bloomberg and ICE BofA indices for fixed income markets, as of April 2026.

⁸ BlackRock projection as of April 2026. Subject to change. The figures are for illustrative purposes only and there is no guarantee the projections will come to pass.

European fixed income: Short-term noise, long-term drivers of return

As the chart to the right illustrates, coupon income, rather than price movements, has driven the majority of total returns, with reinvestment and compounding playing a critical, though often underappreciated, role.

Flexibility and selectivity as dispersion rises

From a long-term perspective, we believe investors should focus on navigating current volatility through flexible solutions positioned to capture the best opportunities as they emerge.

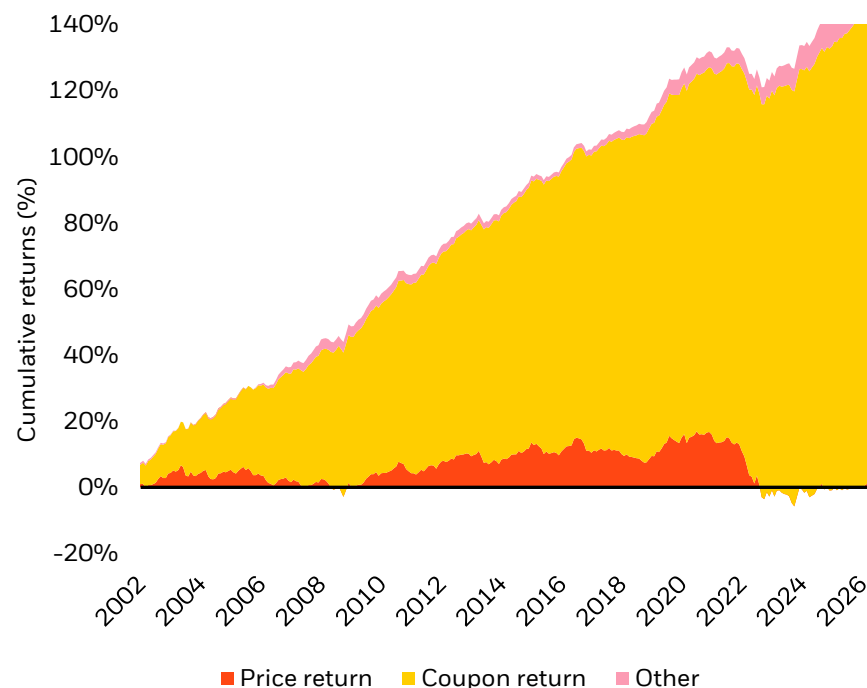
The repricing of European rates has been a key development. Given uncertainty around growth and the policy rate path, active duration management remains essential. In our view, the most attractive opportunities are in the front end of the curve, particularly in the two- to five-year segment. We remain more cautious on longer-duration exposures, where term premia remains subdued relative to elevated fiscal-driven upside risks.

European credit spreads have remained resilient, tightening back to, and in some cases beyond, pre-volatility levels. This suggests markets are largely looking through the noise, provided conditions remain on a de-escalation path.

Corporate fundamentals continue to provide support. Many issuers have taken a more cautious approach to balance sheet management, with leverage declining, proactive refinancing activity and margins remaining relatively healthy. As a result, the likelihood of a broad-based wave of downgrades or defaults remains low. Nonetheless, spreads remain tight and we need to respect that volatility is likely to persist.

Despite tight spreads in aggregate, dispersion remains elevated. The accelerating pace of AI adoption and advances in computational power are likely to drive greater divergence between winners and losers across sectors and the broader economy, reinforcing the importance of active credit selection as a key driver of alpha.

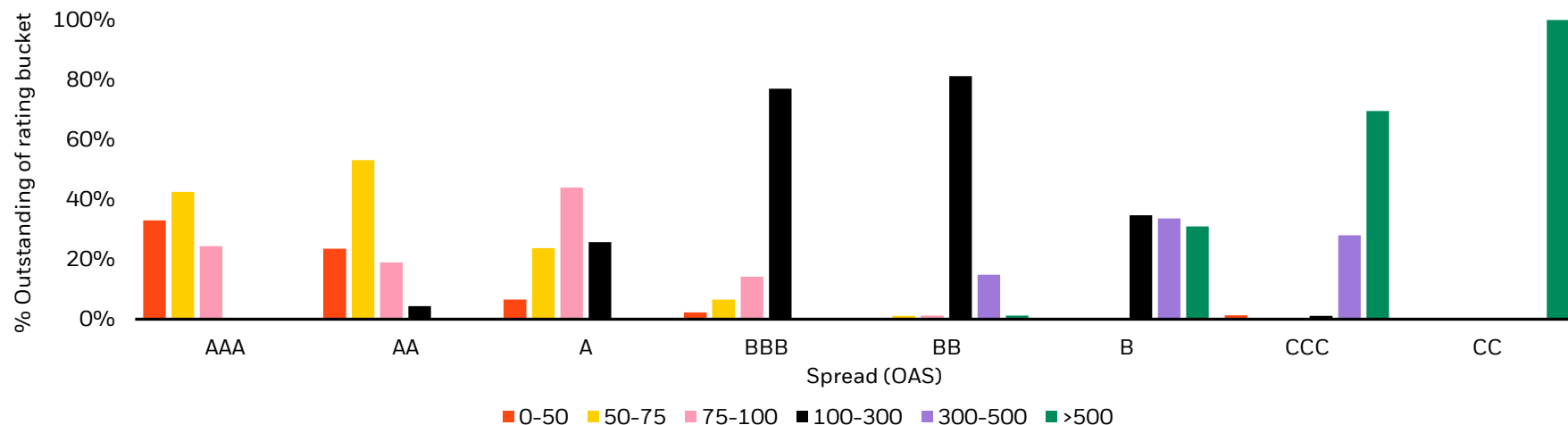
Income returns win in the long run



The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results. Index performance is shown for illustrative purposes only and does not predict or depict the performance of any BlackRock fund. Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged and one cannot invest directly in an index. The chart on the left takes the decomposed Total Return data and show the hypothetical cumulative returns of the income and price returns as if they were independent return streams; these return streams are not additive. Source: Barclays Live, as of Feb. 28, 2026. Indices used: Bloomberg Euro-Aggregate Index, Bloomberg Euro-Aggregate: Corporates, Bloomberg Pan-European High Yield Index, Italy Treasury Bond Index.

European fixed income: Short-term noise, long-term drivers of return

Credit markets show increasing dispersion across ratings



BlackRock, as of April 2026. The graph is based on the constituents of the Bloomberg Euro Corporate Bond Index and the BBG Pan European HY 3% Issuer Constrained 100% EUR Hedged Index. Fund ratings are determined according to Barclays methodology: When a security is rated by S&P, Moody's, and Fitch, the median rating is shown; if rated by two agencies, the lower rating is used; if rated by only one agency, that rating is applied. The percentage of outstanding is calculated as the total outstanding amount of the security divided by the total outstanding amount for each rating category.

Technology-driven productivity gains are already beginning to reshape labor markets. And while the full impact of AI-related substitution has yet to materialize, early signals are emerging, including a decline in job postings in AI-exposed sectors and a slowdown in youth employment growth since the release of GPT-4 in 2023.⁹ These developments raise important questions about the durability of established market relationships, the stability of correlations and the sustainability of cash flows.

We believe these dynamics support a framework of dynamic patience. While the recent conflict has increased uncertainty around trade, inflation and

consumer resilience, it has not fundamentally altered the underlying economic backdrop or the attractiveness of income and yield opportunities.

Maintaining exposure allows investors to capture income and compounding, while flexibility in portfolio construction helps navigate shifting correlations and take advantage of dislocations. Structural shifts, particularly the rapid evolution of AI, are likely to drive further divergence across sectors and issuers.

As markets become more driven by dispersion than direction, selectivity and active management are likely to be key drivers of outcomes.

⁹ Stanford University research on AI and labor market dynamics (2024-2025) https://digitaleconomy.stanford.edu/app/uploads/2025/11/CanariesintheCoalMine_Nov25.pdf.

Income and selectivity in emerging markets debt



Michel Aubenas

Head of Emerging
Market Debt

“

The depth and breadth of yield available in EMD remains one of the asset class's most compelling features.

Staying grounded in fundamentals

Recent market conditions have been marked by noise, volatility and fast-moving headlines. In this environment, short-term developments can dominate the narrative, obscuring the structural dynamics around the emerging markets (EM) that matter most.

EM economies are entering this period of volatility from a position of strength. Following years of global stress after the pandemic, policy frameworks have improved across the asset class, with stronger external buffers, more disciplined fiscal policy and greater central bank credibility across a broad set of issuers.

As a result, emerging markets debt (EMD) has become a more balanced and resilient asset class, supported by improving sovereign credit quality, reflected in a more constructive credit ratings backdrop. While recent developments in the Middle East have introduced near-term risks, they have not reversed the structural progress made in recent years. In our view, overall EMD fundamentals remain intact, and continue to support the asset class through the current period of uncertainty.

Compelling entry point amid elevated yields

EM valuations moved in line with broader global market volatility, with spreads widening during the peak of the value-at-risk shock and trading with betas to U.S. rates similar to other periods of sudden de-risking. Since then, spreads have tightened, reflecting the strength of underlying fundamentals and the credibility many issuers have established. The subsequent normalization has left the investor base less encumbered and better positioned, with pockets of opportunity beginning to emerge.

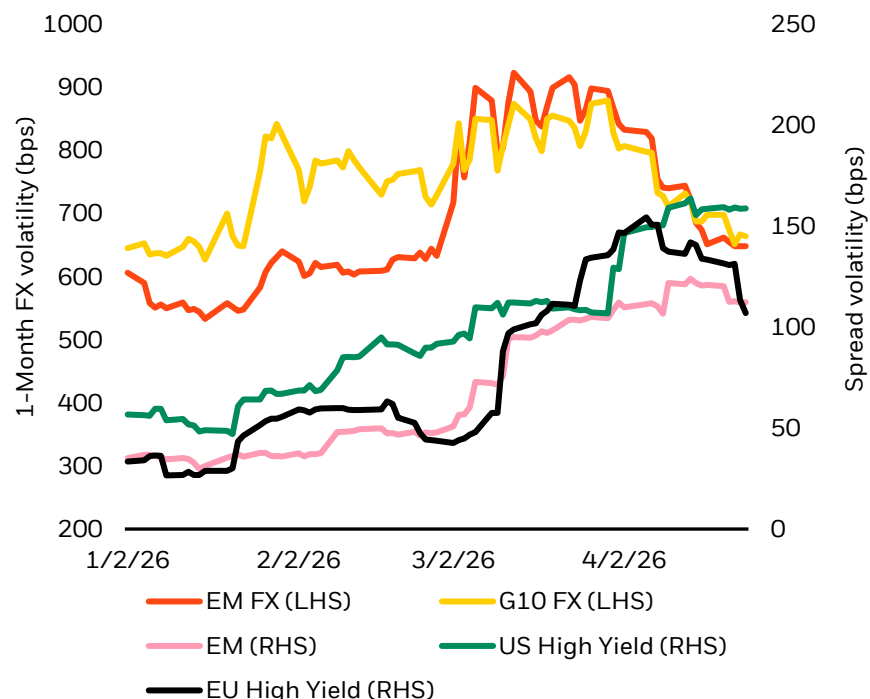
As markets reassess central bank responses to higher energy prices, we believe global duration can move from a recent headwind to a potential tailwind for EM performance as the focus turns to the potential impact on growth coming from energy supply constraints.

All-in yields are attractive across EMD segments, and contained spread and currency volatility underscores the strong income proposition. Investment grade, high yield and frontier markets all offer differentiated income opportunities across a broad and diverse opportunity set. In our view, the depth and breadth of yield available in EMD remains one of the asset class's most compelling features and a key driver of return in the current environment.

Income and selectivity in emerging markets debt

Volatility of foreign exchange and spread

2026 volatility of FX (LHS) and spread (RHS)



Currency dynamics remain a key driver

The trajectory of the U.S. dollar remains a key variable. Structural pressures, including the U.S. twin deficit and gradual diversification of global reserve allocations, suggest a longer-term bias toward dollar weakness. This would support EM hard currency debt by easing external financing conditions and improving debt sustainability.

A weaker dollar would also support local currency debt, where real yields remain elevated. The combination of attractive real yields and potential currency appreciation creates a dual return driver across the asset class.

Dispersion opens selection opportunities

Dispersion remains wide across emerging markets, reflecting differences in policy capacity, external balances and exposure to global developments. The recent environment has sharpened these distinctions, drawing a clear line between more resilient and more vulnerable economies.

Energy importing countries may face economic pressure if supply disruptions continue. Their ability to cushion the impact will depend on how much governments can support households and on the strength of currency reserves and external buffers, particularly if the energy shock lasts beyond the next few weeks. By contrast, commodity exporters and economies with stronger policy frameworks are better positioned to absorb volatility.

Political developments are also likely to be an important driver of performance. Elections in key markets, including Hungary, Colombia and Brazil, could lead to meaningful repricing as policy expectations evolve.

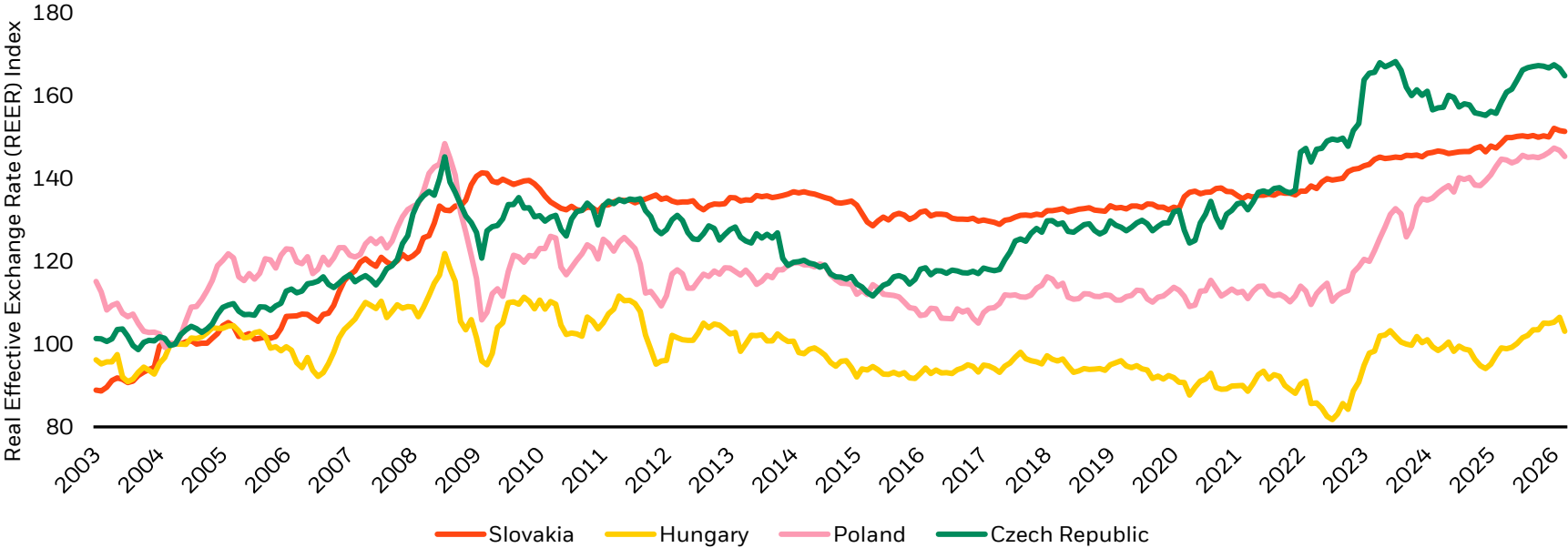
Bloomberg, as of Apr. 24, 2026, BlackRock calculations. EM FX = JPM EM FX Volatility 1M, G10 FX = JPM G10 FX Volatility 1M. EM Spread = JPM EMBI GD Sovereign Spread Index. U.S. High Yield Spread = Bloomberg U.S. Corporate High Yield Average OAS, EU High Yield Spread = EUR HY All Sectors OAS.

Income and selectivity in emerging markets debt

The opposition victory in Hungary and their intention to join the Eurozone opens the way for “convergence” trades. With the prospect of approval of financial support to Ukraine, the election outcome had broader positive ramifications.

With positioning cleaner, dispersion creating clearer entry points and fundamentals remaining broadly resilient, the case for selective engagement in EMD remains compelling. For investors with the clarity of view and conviction to act, the opportunity set remains meaningful.

Real effective exchange rate



BlackRock, as of Apr. 24, 2026.

Divergence across economies creates opportunity in Asia



Navin Saigal

Head of Global Fixed Income, Asia Pacific

“

Divergence across economies remains a defining feature of the region.

Geopolitical developments in the Middle East have driven a sharp increase in energy prices and heightened market volatility. In Asia, however, the impact of this shock has been uneven, reinforcing an important feature of the region: Divergence across economies, policy paths and market outcomes.

One shock, many outcomes

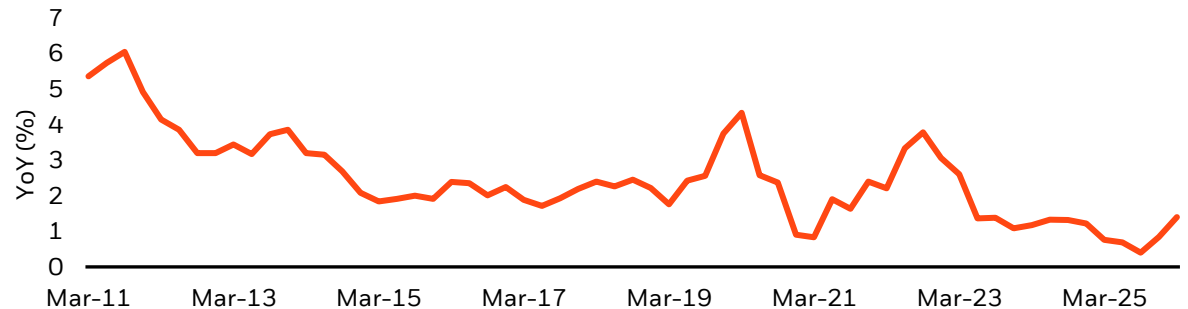
The impact of the recent shock on Asia has been far from uniform. In contrast to the U.S., inflation across many emerging Asian economies was already subdued prior to the conflict, struggling to reach central bank targets amid tariff pressures and slowing but resilient domestic demand. This lower starting point has provided central banks with greater flexibility to look through the oil price spike, particularly given uncertainty around its duration.

Divergence across economies remains a defining feature of the region. China has been relatively

insulated, with its bond market continuing to trade on domestic fundamentals. Australia stands apart: higher energy prices support national income through liquefied natural gas exports, but also reinforce already elevated inflation via commodity imports, placing it on a differentiated policy and yield path from the rest of the region. Japan faces a different dynamic, where imported energy inflation is interacting with domestic wage pressures, contributing to upward pressure on yields.

Across Southeast Asia, the combination of higher oil prices and a stronger dollar is having a tangible impact on net oil-importing economies. While markets have priced in policy tightening, the broader macro effect is more complex. Supply shocks of this nature are inflationary in the near term, but tend to weigh on demand over time, raising the risk that markets may be underestimating the growth impact.

Asia ex-Japan inflation entered the Middle East crisis from a very low base



Bloomberg, as of Mar. 31, 2026.

Divergence across economies creates opportunity in Asia

Policy trade-offs and market implications

Central banks across the region face a difficult balancing act. Tightening policy in response to inflation risks exacerbating the demand slowdown that often follows a supply shock. Policy responses have so far been measured and credible, but the gap between what markets are pricing and what economies can absorb remains an important source of potential dislocation.

This dynamic is particularly evident in economies such as the Philippines, where higher energy costs are already weighing on households and broader demand. These conditions highlight the importance of assessing not just the inflation impulse, but also the second-order effects on growth and policy.

Currency as a shock absorber

Currency flexibility plays a critical role in how Asian economies absorb external shocks. While depreciation can appear destabilizing, it often acts as an automatic stabilizer, tightening financial conditions and improving trade balances without requiring aggressive rate hikes. Over time, this supports macro stability and helps anchor local bond markets.

Where resilience meets diversification

Asian credit markets have remained resilient through recent volatility. Drawdowns have been broadly in line with historical experience, and spreads, particularly in investment grade, remain relatively contained, supported by stable fundamentals.

Looking ahead, the trajectory of U.S. monetary policy will be an important driver. If the Fed determines that the current energy shock is ultimately more damaging to growth than inflationary in a sustained way, rate cuts could materialize sooner than markets currently expect. This would be most supportive for front-end duration, where convexity remains attractive.

At the same time, the region's structural characteristics continue to stand out. Lower correlations, differentiated policy cycles and resilient fundamentals position Asian fixed income as a meaningful source of diversification and income within global portfolios.

From diversification to differentiation

Asian fixed income is increasingly transitioning from a diversifying complement to a differentiated source of return. Markets are shaped by distinct economic cycles, policy frameworks and reform trajectories, creating a broad and varied opportunity set.

However, this same dispersion raises the bar for investors. Capturing opportunity requires a clear framework, disciplined execution and the ability to adapt as conditions evolve. In our view, this environment reinforces the importance of selectivity and active management, as outcomes become more dependent on identifying relative value across markets, sectors and issuers.

Repricing and selectivity in municipal bonds



Pat Haskell
Head of the Municipal Bond Group



Lower reserves, moderating revenues and policy uncertainty point to a more issuer-specific and less forgiving credit environment.

Finding opportunity after the reset

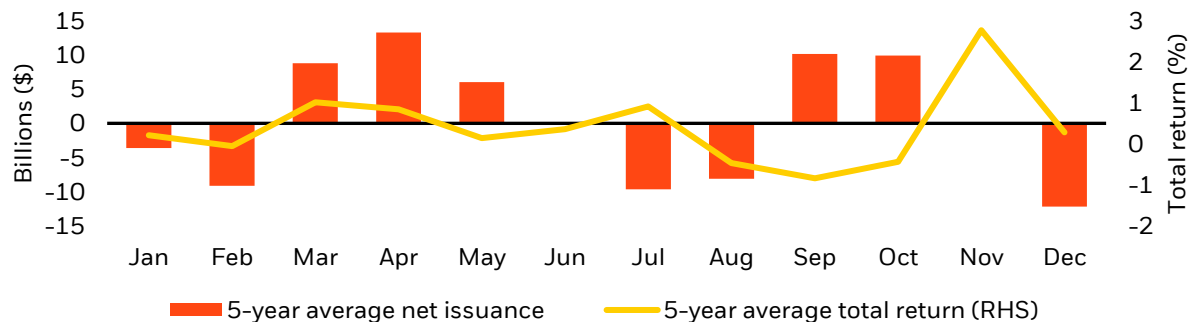
Municipal bonds began 2026 with their strongest returns since 2020, as exceptionally strong investor demand outpaced below-consensus issuance.

However, heightened geopolitical tensions disrupted momentum exiting the first quarter, and the market moved into the second quarter with a more constructive backdrop. The March sell-off materially improved both absolute and relative valuations, particularly in the intermediate segment, to levels last seen in late 2025, though subsequent strong performance in April has retraced a portion of that cheapening.¹⁰ Against a backdrop of elevated macro uncertainty, we believe the risk/reward profile is now more balanced and warrants a more measured stance.

While valuations have become less compelling, technical conditions are likely to provide a degree of support in the months ahead. As the market approaches the summer period, seasonal reinvestment demand from maturities, coupons and calls has historically met or exceeded new issuance, creating a reliable seasonal tailwind. Over the past five years, June and July have delivered the third- and second-highest average monthly returns, respectively.¹¹

These seasonal patterns are likely to hold this year. Although projected supply of approximately \$54 billion per month would represent a record pace for the summer period, demand conditions remain firmly supportive. Persistent inflows into open-end and ETF structures, combined with strong reinvestment needs, should be sufficient to absorb elevated issuance and provide a meaningful backstop, reinforcing the market's capacity to generate stable returns.

Municipal index performance can be impacted by issuance trends



Bloomberg Indices, Siebert, BlackRock, as of Apr. 15, 2026.

¹⁰ Refinitiv, Bloomberg, BlackRock, April 2026.

¹¹ Bloomberg Indices, BlackRock.

Repricing and selectivity in municipal bonds

Municipal credit fundamentals remain sound, but are normalizing from post-pandemic highs as supportive factors fade and dispersion increases. State tax collections were 2.3%, or \$9.3 billion, below their 15-year trend by mid-2025, with 40 states underperforming, while rainy day fund capacity declined for the first time since the Great Recession.¹²

Revenue growth persists but is moderating. Personal income and sales tax collections have slowed, and corporate tax gains remain volatile and concentrated. Local governments, especially school districts, are facing mounting pressure as federal aid expires. Rising labor, transportation and special education costs, combined with lagging state support, are driving reserve drawdowns and structural imbalances, contributing to increased downgrades and wider credit gaps.

Policy developments add another layer of uncertainty. Influential states including Texas and Florida are pursuing property tax reductions, often without full offsets. Given the importance of property taxes as a stable local revenue source, these changes could heighten fiscal strain. Taken together, lower reserves, moderating revenues and policy uncertainty point to a more issuer-specific and less forgiving credit environment.

In our view, these dynamics reinforce the importance of credit selection and a focus on resilient revenue streams, with outcomes increasingly dependent on issuer-level analysis and disciplined portfolio construction.

Positioning for resilience and selectivity

Against this backdrop, our positioning reflects a balance between caution and opportunism, requiring a more deliberate and selective approach.

Following the March repricing, we began selectively deploying capital, modestly reducing elevated cash balances to capitalize on concessions in the new issue market. Valuations in the 5–10-year segment reset to levels last observed in September 2025, providing an opportunity to incrementally extend duration on a selective basis, with a focus on issuers with strong underlying fundamentals.¹³

More recently, as valuations have retraced, we have shifted to a more patient stance. We are maintaining higher liquidity levels and are more opportunistic in deploying capital, waiting for aberrations in the market rather than systematically adding risk. In this environment, we are less inclined to extend duration and instead favor flexibility as conditions evolve. From a sector perspective, we maintain a preference for essential service revenue bonds over general obligation bonds.

Essential service sectors, including transportation, housing and utilities, benefit from more stable and predictable revenue sources. In our view, this stability is particularly valuable amid rising fiscal pressures and policy uncertainty. These issuers typically offer stronger revenue visibility and financial flexibility relative to general obligation credits, which may face greater exposure to budgetary and political constraints.

Credit selection remains central as dispersion increases. We are emphasizing issuers with strong governance, disciplined financial management and sustainable operating profiles, while avoiding sectors facing structural challenges or weaker sponsorship.

¹² A Pew analysis of data from the Urban Institute, U.S. Census Bureau, and U.S. Bureau of Economic Analysis.

¹³ Refinitiv, Bloomberg, BlackRock.

This material is prepared by BlackRock and is not intended to be relied upon as a forecast, research or investment advice, and is not a recommendation, offer or solicitation to buy or sell any securities or to adopt any investment strategy. The opinions expressed are as of May 2026 and may change as subsequent conditions vary. The information and opinions contained in this material are derived from proprietary and nonproprietary sources deemed by BlackRock to be reliable, are not necessarily all-inclusive and are not guaranteed as to accuracy. As such, no warranty of accuracy or reliability is given and no responsibility arising in any other way for errors and omissions (including responsibility to any person by reason of negligence) is accepted by BlackRock, its officers, employees or agents.

This material may contain “forward-looking” information that is not purely historical in nature. Such information may include, among other things, projections and forecasts. There is no guarantee that any of these views will come to pass. Reliance upon information in this material is at the sole discretion of the reader. This material is intended for information purposes only and does not constitute investment advice or an offer or solicitation to purchase or sell in any securities, BlackRock funds or any investment strategy nor shall any securities be offered or sold to any person in any jurisdiction in which an offer, solicitation, purchase or sale would be unlawful under the securities laws of such jurisdiction.

Stock and bond values fluctuate in price so the value of your investment can go down depending upon market conditions. The two main risks related to fixed income investing are interest rate risk and credit risk. Typically, when interest rates rise, there is a corresponding decline in the market value of bonds. Credit risk refers to the possibility that the issuer of the bond will not be able to make principal and interest payments. The principal on mortgage- or asset-backed securities may be prepaid at any time, which will reduce the yield and market value of these securities. Obligations of U.S. Government agencies and authorities are supported by varying degrees of credit but generally are not backed by the full faith and credit of the U.S. Government. Investments in non-investment-grade debt securities (“high-yield bonds” or “junk bonds”) may be subject to greater market fluctuations and risk of default or loss of income and principal than securities in higher rating categories. Income from municipal bonds may be subject to state and local taxes and at times the alternative minimum tax.

Emerging markets are generally more sensitive to economic and political conditions than developed markets. Other factors include greater ‘Liquidity Risk’, restrictions on investment or transfer of assets, failed/delayed delivery of securities or payments and sustainability-related risks.

Fixed income securities issued or guaranteed by government entities in emerging markets generally experience higher ‘Credit Risk’ than developed economies.

Index performance is shown for illustrative purposes only. Indexes are unmanaged and one cannot invest directly in an index.

Investing involves risk, including possible loss of principal.

© 2026 BlackRock, Inc. or its affiliates. All Rights Reserved. **BLACKROCK** is a trademark of BlackRock, Inc. or its affiliates. All other trademarks are the property of their respective owners.

260684T-0525