

WEEKLY INVESTMENT COMMENTARY

BLACKROCK®

What to Expect in 2014

2013: A Year of “Missed Risks”

This year began with many focusing on what could go wrong. We had just gone through the “fiscal cliff” debacle, investors were worried about the European debt crisis, and the outlook for U.S. and global economic growth looked uncertain.

Instead, however, 2013 proved to be a year when most major risks were avoided and the table was set for a strong investing year. The economic recovery continued (if unevenly), inflation remained low and, notwithstanding a mid-year jolt, interest rates rose (but not disruptively).

In this environment, equity markets enjoyed an impressive year, with U.S. stocks up more than 25% and the major indexes hitting new records along the way.

International markets also notched solid results, with the exception of emerging markets, which struggled with uneven growth and structural imbalances. Fixed income markets were choppy in 2013, with a long-awaited rise in interest rates finally occurring. As Treasury yields advanced nearly a full percentage point, bonds experienced a rare negative total return for the year (prices move in the opposite direction of yields).

Expect an Improving Economy and (Slightly) Higher Rates in 2014

So what should investors expect in the New Year? From a broad perspective, many may feel a sense of déjà vu, since we expect most of the macro factors that existed in 2013 to persist: improving (but still relatively slow) economic growth, very low inflation and slowly rising interest rates.

That said, we do expect growth to pick up modestly, both in the United States and globally. Although the Fed has begun its long awaited taper, policy remains accommodative and supportive of the economy. Lower energy prices and an improving housing market also represent tailwinds. In 2014, we expect the U.S. economy will edge past the 2% growth rate in which it has lived for the past couple of years and come in at around 2.5% to 2.75%. Global growth should accelerate from 3% in 2013 to around 3.5% next year.

Another important theme we expect to see in 2014: Slightly better growth should lead to an increase in real interest rates. We do not believe rates will rise rapidly or dramatically, partly because the Fed will likely keep the fed funds rate anchored at close to zero through 2014, but we do think yields will climb modestly. We would look for an increase of around 0.5% for the 10-year Treasury over the course of 2014.



Russ Koesterich, Managing Director, is BlackRock's Global Chief Investment Strategist, as well as Global Chief Investment Strategist for BlackRock's iShares business. Mr. Koesterich was previously Global Head of Investment Strategy for active equities and a senior portfolio manager in the U.S. Market Neutral Group. Prior to joining the firm in 2005, he was Chief North American Strategist for State Street Bank.

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Investment Themes for the New Year: Stick With Stocks; Focus on Credit in Fixed Income

Against this backdrop, we would advise investors to continue overweighting stocks in their portfolios. Equities may not be as inexpensive as they were a year ago, but they remain more attractive than bonds and cash. There are some important caveats to this view, however: We do expect more volatility in 2014 than we saw in 2013, and we think investors should be more selective. In particular, international stocks are worth investor attention, as they appear more reasonably priced than U.S. equities. We would also encourage investors with longer-term time horizons to consider emerging markets despite their recent underperformance, as they too offer compelling value.

There are few bargains in fixed income markets. With rates likely to rise and inflation still low, we would avoid both long-dated Treasuries and Treasury Inflation Protected Securities (TIPS). Instead, we advocate sticking with fixed income credit sectors, including high yield bonds. Additionally, we believe municipal market fundamentals are sound and that muni bonds look attractive—especially as investors complete their 2013 tax returns and feel the impact of higher taxes.

Stay Informed, Stay Connected

Of course, all of the above is merely a starting point for thinking about the year to come. For more information on our economic and investment views, as well as thoughts about additional areas of investment opportunity, we encourage you to visit blackrock.com, where you can find a wealth of related resources, including:

- ▶ [BlackRock's 2014 Outlook Webinar—What to Know and What to Do](#): A live, interactive webinar scheduled for January 7 at 4:15 (ET).
- ▶ [2014 Outlook—The List](#): What to Know, What to Do: Five “what to know” items and five “what to do” ideas for navigating the year ahead.
- ▶ [Investment Directions](#): Our monthly look at global markets, including our asset allocation views.
- ▶ [Squeezing Out More Juice](#): A detailed look at the year ahead from the BlackRock Investment Institute.

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