Insights
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Risk-on is back, higher volatility stocks rebound

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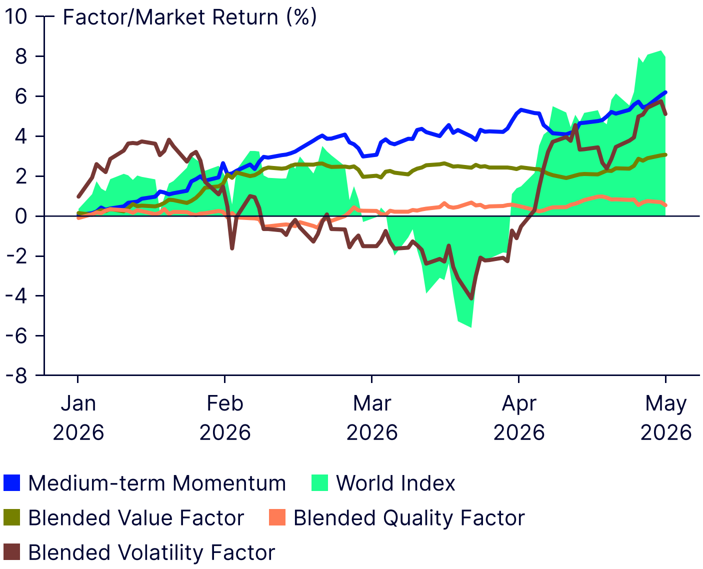
Figure 1: Market progress driven by high momentum and high risk stocks



Source: Factset, Axioma, MSCI, State Street Investment Management as at May 13, 2026. World Index is total returns for MSCI World Index. Momentum, Value Blend, Quality Blend, and Risk Blend represent cumulative daily returns for a subset of combined style factors from the Axioma WW4-MH risk model. The performance data quoted represents past performance. Past performance does not guarantee future results. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable.

Equity markets have continued to advance through 2026, but leadership has been highly selective. Since the late March lows, higher risk stocks have led performance, signaling a renewed risk on regime that has persisted despite ongoing geopolitical, economic, and inflation uncertainty.

Equity investors have had to navigate a challenging macro environment so far this year, characterized by elevated rates volatility, shifting growth expectations, and numerous policy driven headlines. Yet despite this backdrop, the equity Volatility factor has been strongly positive in the year to date, signaling outperformance of higher risk, higher beta stocks. This pattern is consistent with a risk-on regime, rather than a defensive one, and reflects a willingness by investors to re-engage with cyclical exposures despite persistent uncertainty.

Momentum and sector leadership

This risk seeking behavior has been reinforced by strong momentum dynamics; past winners have kept on winning, undeterred by conflicts, politics, or economic noise. Semiconductor-related and technology hardware stocks dominate momentum exposure, reflecting sustained capital investment in AI-related infrastructure.[1]

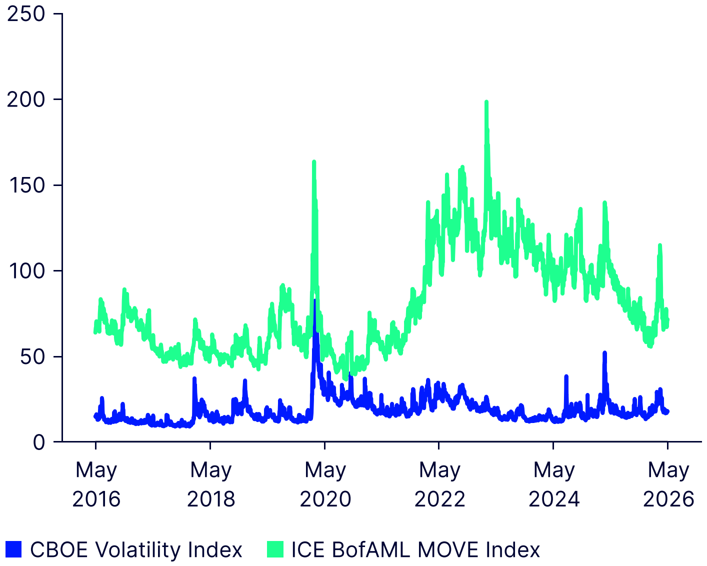
Importantly, there has been an evolution in the nature of investor risk-taking this year. While the start of 2026 was characterized by intermittent and fragile risk appetite, with episodes of defensiveness dominating headlines, behavior since early April has shifted decisively. Risk exposure has been rapidly rebuilding and this has persisted through mid May. The improvement in Volatility factor returns reflects this transition from tentative risk tolerance to active re risking.

At the sector level, software names currently have the largest average volatility exposure in developed markets, although returns have been directly hit by concerns around AI-related is intermediation. Energy has been the next best driver, with company share prices surging on the high oil and gas prices resulting from the Middle East conflict. AI-related hyperscaler stocks have been a major factor in cap-weighted market returns—Even excluding the disproportionate effect of the 10 largest stocks by market cap, semiconductors and energy have been among the largest contributors to high volatility exposure, while software has been a significant drag.

Equity volatility remains benign

Notwithstanding the evolution in risk appetite, equity implied volatility remains largely range bound—this reinforces the view that this has been a risk on environment rather than a stress regime. Fixed income markets, by contrast, have exhibited somewhat more persistent volatility, highlighting a divergence between equity risk appetite and the uncertainty prices into rates markets.

Figure 2: VIX stays calm, but fixed income markets are (slightly) stressed



Source: Factset, CBOE, ICE BofAML, State Street Investment Management as at May 13, 2026. Chicago Board Options Exchanges' CBOE Volatility Index (VIX). ICE BofAML MOVE (Merrill Lynch Option Volatility Estimate) Index. The performance data quoted represents past performance. Past performance does not guarantee future results.

This type of profile suggests that the risk-on attitude is not confined to a small subset of the universe, but is more pervasive. Higher-volatility names outperformed lower-risk names in 17 out of the 25 GICS[2] industry groups within developed markets so far this year.

Benign pricing of risk can persist for extended periods, but phases of high volatility outperformance rarely endure and can retrace rapidly. The current starting point is also challenging in the current market, given elevated valuations and signs that conflict in the Middle East war is starting to have a notable impact on the real economy, as is becoming evident within inflation numbers, for example.

While the current regime remains risk on, the acceleration in risk exposure suggests that forward returns are likely to be shaped more by rotation and dispersion than by broad beta. As ever, the transition from risk taking to risk pricing tends to be rapid. In such environments, diversification across styles, regions, and stocks continues to be important as both insurance and a source of opportunity.

To learn more about the views and investment capabilities of the Systematic Equity—Active team, please visit our website.

Endnotes

1 As discussed previously in What has happened to the great rotation? | State Street and What if investors get bored of AI? | State Street, for example.

2 The Global Industry Classification Standard (GICS) was developed by MSCI and S&P Dow Jones Indices. It categorizes global public companies based on their principal business activity to facilitate benchmarking, portfolio management, and financial research.

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* This figure is presented as of March 31, 2026 and includes ETF AUM of $1,940.32 billion USD of which approximately $184.18 billion USD in gold assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Investment Management are affiliated. Please note all AUM is unaudited.

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