



Marketing communication | As of 30 Jun 2025

- In the second quarter, the Flexible Income strategy outperformed its benchmark, the Bloomberg U.S. Aggregate Bond Index, on a gross- and net-of-fees basis.
- Contributors included an allocation in common stocks, in addition to investment grade corporates and preferreds.
- Detractors included an allocation in convertibles, with underperformance owed to a select holding in the capital goods industry.

Market review

Global economic data showed more signs of deceleration during the quarter, including a downward revision to first-quarter's U.S. gross domestic product (GDP) growth to -0.5% annualized. Although much of the weakness was due to a short-term surge in imports as businesses tried to front run tariffs, underlying U.S. consumer spending also slowed. June's U.S. employment report beat expectations, with higher job creation and a lower unemployment rate, but other labor market data continued to signal a further slowdown ahead. While inflation moderated to around 2.4% annually, according to the most recent Consumer Price Index print, the effects from tariffs may push core goods prices higher in the third quarter.

The Federal Reserve kept its target federal funds rate steady, in a range of 4.25%-4.50%, during the quarter. In June, Chair Jerome Powell stated that the current environment represents "a solid economy with decent growth," but that conditions were "highly uncertain" due to the Trump administration's trade and immigration policies. Given that uncertainty, Powell emphasized that "the appropriate thing to do is hold where we are."

Yields on U.S. Treasury bills were little changed for the quarter despite patches of volatility. For example, the yield on the 3-month security rose by 9 bps, to 4.41%, and that of the 1-year bill fell by 7 bps, to 3.96%. Meanwhile, the yield on the 2-year Treasury note, which is especially sensitive to near-term monetary policy, dipped 17 bps, to 3.72%, as the Fed penciled in two more rate cuts for the year. The 10-year Treasury ended close to flat for the period (4.24%) despite hovering around 4.00% in early April as uncertainty over the U.S. tariff policy outlook shifted toward outright pessimism and peaking at 4.58% in late May amid inflation fears and concerns over rising deficits.

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Investment grade

In the investment grade corporate sector, spreads widened more than 25 basis points after tariffs were announced, accompanied by a nearly equal rise in Treasury yields. This pushed yields on corporate bonds to a year-to-date high of 5.55% and spreads to 119 basis points. Despite the volatility to start the quarter, both investment grade spreads and yields consistently declined into quarter end, displaying remarkable resiliency in the face of a volatile geopolitical environment and highly uncertain trade policy. Technical factors remained the main driver of market support during the quarter as new issue volume continued to surpass 2024's pace. Issuance in the sector now stands at \$902 billion year to date, approximately 2% above the same point last year. Investment grade corporates ended the quarter with total return of 1.82%, outperforming Treasuries.

High yield

The high yield bond sector led the fixed income market with a 3.53% return during the quarter. Yield-to-worst ended the period lower at 7.36%, while the option-adjusted spread (OAS) tightened to 292 basis points over Treasuries. Within the asset class, CCC rated bonds outperformed their BB and B counterparts for the quarter, with spreads tightening the most in the B rated cohort. (Source: Bloomberg) While gross high yield issuance over the quarter totaled \$76.2 billion, the vast majority was driven by refinancing activity. Net supply was \$5.8 billion, with \$3.2 billion of that coming in the month of June. Mutual fund, actively managed and ETF flows collectively remained positive for the quarter at \$4.5 billion. The high yield default rate increased to 1.41% by quarter end, only 26 basis points higher than November's multiyear low, and significantly below their long-term average.

Preferred securities

Total returns across the preferred securities markets were positive during the second quarter, as \$1000 par securities (+2.7%) outperformed \$25 par securities (+0.2%). Excess returns were also positive, with +129 bps for \$1000 par preferreds and +13 bps for \$25 par preferreds. Despite underperforming, \$25 par issues remained relatively rich, with an OAS of 143 bps, versus 191 bps for \$1000 par. Average dollar prices for \$1000 par preferreds ended Q2 at a slight premium to par, while \$25 par preferred prices, on average, remained at a deep discount. We advise assessing \$25 par preferreds based on OAS and not price. While OAS for \$25 par preferreds increased during Q2 by +7 bps, OAS

decreased for \$1000 par preferreds (-18 bps). Generally, OAS for \$1000 par preferreds are trading below longer-term median levels, with \$25 par preferred OAS above the segment's longer-term average.

Equities

The S&P 500 kicked off a volatile period by plunging more than 11% during the first six trading days of the quarter, hit hard by the Trump administration's unveiling of broad increases to U.S. tariffs on its trading partners. But the S&P 500 roared back on 9 April, posting its highest one-day return (+9.5%) since 2008 following the president's abrupt decision to pause reciprocal tariffs on most countries for 90 days and exempt certain sectors (such as steel and aluminum) from the levies.

U.S. equities completed their V-shaped recovery in June, with the S&P 500 surpassing its February peak as the quarter wound down. Investors shrugged off escalating hostilities in the Middle East, focusing instead on resilient economic data, progress on trade deals and hopes for Fed interest-rate cuts later this year. For the second quarter as a whole, the S&P 500 returned +10.9%, a major turnaround from its -4.3% first-quarter loss.

Based on respective Russell indexes, the more economically sensitive small cap and mid cap categories fared well (both up +8.5%) but lagged large caps (+11.1%). Given the technology-led boom, large cap growth (+17.9%) significantly outpaced large cap value (+3.8%).

Portfolio review

The Nuveen Flexible Income strategy returned +3.89% (gross of fees) and +3.57 (net of fees) in the second quarter, outperforming the Bloomberg U.S. Aggregate Bond Index, which returned +1.21%. Uncertainty over U.S. trade tariffs was the dominant market theme during the period, with volatility spiking higher when President Trump announced new "Liberation Day" tariffs across the board. The most extreme measures were subsequently delayed with a 90-day pause, leading volatility to decline and risk assets to stage a strong and rapid recovery. At quarter-end, current yield and yield-to-worst for the institutional representative account were 6.18% and 5.44%, respectively.

Amid the risk-on rally, most major asset class exposures in the strategy delivered positive returns during the period. The strategy's allocation to common stocks was the largest contributor to performance, aided by strong stock selection in the media, banking and information technology sectors.

In addition, investment grade was a notable contributor, benefiting from tighter credit spreads and robust demand for high all-in yields. In terms of security selection, the strategy's overweight to BBB-rated bonds outperformed. Credit markets demonstrated steady resilience in the face of global trade and geopolitical tensions, supported by healthy fundamentals and positive technicals. Finally, an overweight in \$1000 par preferreds was advantageous as the segment meaningfully outperformed \$25 par preferreds, which were negatively impacted by retail outflows and thinner liquidity.

Portfolio positioning

The portfolio maintained a balanced and up-in-quality positioning across our major asset class exposures. We remained focused on companies with strong balance sheets, sound capital structures and durable free-cash-flow generation. Following the post- "Liberation Day" market selloff in early April, we utilized dry powder to take advantage of heightened market volatility and more attractive entry points.

In addition to moderating economic growth and trade tariff uncertainty, fuller valuations across risk assets have reinforced the importance of security selection. Overall, we are laser focused on understanding where companies source goods, what markets they sell into and the demand elasticity of pricing (i.e. essential vs. nonessential goods). We seek to strike a balanced approach, taking advantage of price dislocation, while being cognizant of potential downside risks. We are constantly evaluating the opportunity set across the capital structure from senior debt to equity, looking to find the optimal risk and reward at the security level.

We anticipated that interest rate volatility would pick up and believed that our portfolio would be well positioned to outperform the broad bond market, especially if rates were to move higher. This prediction came to light, as we've seen meaningful volatility through the first half of the year, as the 10-year U.S. Treasury yield hit peak levels at 4.8% in January before bottoming out at sub-4.0% in April. We maintained a relatively shorter duration profile overall through the period, seeing more attractive relative value in spreads vs. rates. We felt comfortable maintaining our spread overweights given healthy fundamentals and robust yields, while emphasizing a bias for quality and liquidity across asset classes.

Outlook

Despite the cooling economy, we believe that the probability of a U.S. recession this year remains low. Our revised U.S. GDP growth forecast stands at 1.0% for the year. This reflects a modest uptick from our previous estimate due to softening tariff rhetoric during the quarter. That said, these projections carry substantial uncertainty, as shifts in trade policy could materially impact growth trajectories in either direction, underscoring the fluid nature of the current economic environment. The Fed is likely to maintain its watchful stance until the full impact of policy and tariff changes materializes in economic data before initiating further easing measures. Our baseline forecast anticipates two cuts of 25 bps each in the latter half of the year, followed by 2-3 more cuts in 2026, depending on inflation and growth trajectories.

Our forward outlook anticipates a decline in shorter-term rates as the Fed resumes its easing cycle later this year. We project the 10-year U.S. Treasury yield to settle at 4.25% by year-end 2025, though heightened policy uncertainty has widened our forecast range. The anticipated economic deceleration typically exerts downward pressure on longer-term rates, which should benefit bond prices. This dynamic historically positions fixed income as a more resilient asset class during economic downturns compared to equities.

Corporate credit has displayed exceptional stability despite increased spread and rate volatility. Technical factors such as low net issuance and yields above 5% and 7% in investment grade and high yield, respectively, suggest demand will remain strong and spreads can stay firm even in broader macro uncertainty. Issuer fundamentals remain healthy and defaults, which have been concentrated in select lower-quality issuers, will likely remain below their long-term average. At current valuations, we believe spreads could be susceptible to widening if the growth outlook deteriorates more than the market anticipates.

The current environment of historically elevated yields offers compelling income opportunities, presenting investors with what we consider the most attractive fixed income entry point in decades. As the global economy moderates, these substantial starting yields should continue to drive steady returns. While cash yields will likely decline with anticipated Fed rate cuts, strategic positioning across fixed income sectors can help maintain attractive portfolio income levels. Rate cuts and a still growing economy provide a supportive backdrop for equities, but we emphasize that security selection continues to be paramount in generating alpha given fuller valuations.

For more information contact: 800.752.8700 or visit nuveen.com

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Glossary

The **Bloomberg U.S. Aggregate Bond Index** tracks the performance of U.S. investment-grade bonds. **It is not possible to invest directly in an index**. Clients should consult their financial professional regarding unknown financial terms and concepts.

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