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CIO Weekly Commentary
18 September 2023

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Expanding the horizons of your equity portfolio

Bottom line up top

We've yet to cross the border into rate-cut territory. Last week's release of August's Consumer Price Index data caused a bit of a stir among investors, as it provided further evidence that the recent disinflationary trend supporting market appreciation for much of 2023 has stalled. Familiar components of CPI (such as shelter) either remain too high or have reaccelerated after showing signs of easing, as was the case with energy prices, particularly gasoline (Figure 1). With this week's Federal Reserve meeting looming large, the recent inflation print may well support the case for an additional 25 basis points rate hike. In our view, with inflation still well above the Fed's 2% target, another rate increase is certainly more likely to occur before any rate cuts, despite the fondest wishes of the markets. That said, our base case calls for a pause in the current hiking cycle by the end of 2023, after which we expect rates to remain elevated but stable in 2024.

Think globally, not provincially, when it comes to rate expectations. Recent U.S. data highlights both stubborn inflation and some cracks beginning to form in the underlying economy. Yet the latest global fund manager survey conducted by Bank of America shows overweight allocations to U.S. equities for the first time in a year, as the vast majority of managers surveyed expect lower short-term rates. That's in contrast to our call for a "higher-for-longer" rate environment, which we think will persist until inflation gets much closer to the Fed's 2% target and will likely result in at least a modest contraction in U.S. GDP (as well as increased market volatility). While investors may find ways

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Chief Investment Officer

On behalf of Nuveen's Global Investment Committee

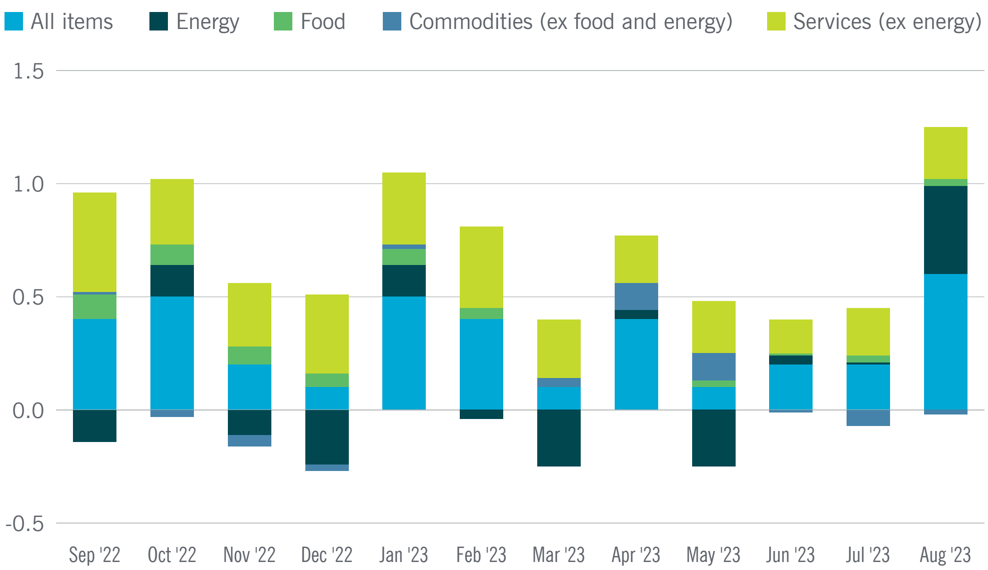
As Nuveen's CIO and leader of our Global Investment Committee, Saira drives market and investment insights, delivers client asset allocation views and brings together the firm's most senior investment leaders to deliver our best thinking and actionable investment ideas. In addition, she chairs Nuveen's Equities Investment Council and is a portfolio manager for several key investment strategies.

to play offense and defense in the U.S. equity market, the S&P 500 Index is currently trading at an approximately 6% premium to its 10-year average on a forward price-to-earnings basis. Rich valuations like these help inform our neutral stance on U.S. equities overall. But allocating more broadly via a globally diversified equity portfolio provides attractive opportunities in certain pockets of both developed and emerging markets.

Despite some expectations of a coming easing cycle, we think we'll remain in the 'higher for longer' environment for at least the next couple of quarters.

FIGURE 1: ENERGY PRICES ARE KEEPING INFLATION STICKY

Headline U.S. CPI month-over-month changes (%)



Data source: Bloomberg, L.P.

Portfolio considerations

Within **non-U.S. developed equities**, **Japan** and the **U.K.** are two markets where compelling valuations and, in our view, easy-to-beat growth expectations are setting up a strong backdrop. Japan is one of the few countries seeing accelerated economic expansion and upwardly revised GDP growth estimates (+1.6% forecast for fiscal year 2023, per Goldman Sachs). While growth forecasts for Japan's fiscal 2024 are lower (+1.0%), we take a different view, believing Japan could exceed the +1.1% growth outlook for developed markets overall (Figure 2). The Japanese consumer remains strong, evidenced by retail sales that are currently up 6.8% year-over-year — more than four times the long-term average. Corporate earnings have been robust too, with higher sales and profits driven in part by a weaker yen, which boosts results for exporters. Capital expenditures are on the rise as well, which should contribute to higher future earnings, while also benefiting investors in the form of higher dividends and share buybacks.

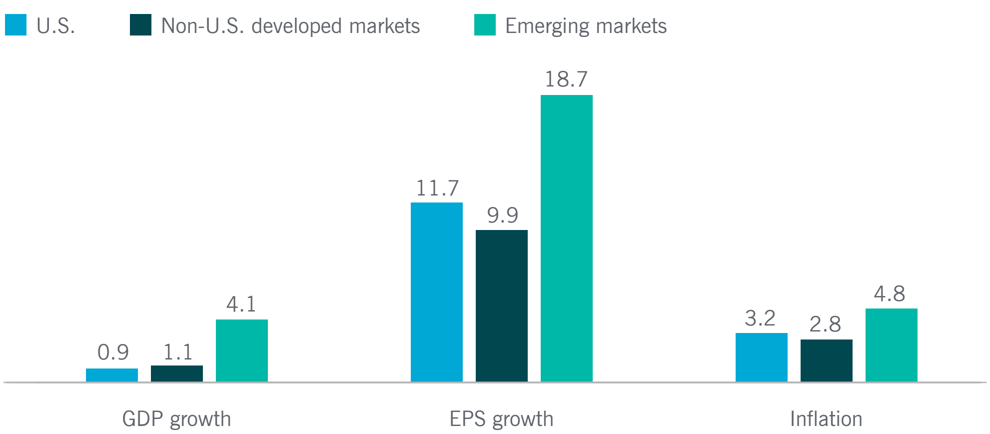
The **U.K.** has not fully participated in this year's strong global equity returns. Inflation has been a headwind, though headline price increases have slowed dramatically to 6.8% in July from last October's peak of 11.1%. A continued decline in inflation could be a positive for interest rate-sensitive stocks like homebuilders. The FTSE 100 Index is currently trading at a forward P/E ratio of 10.6x, more than 20% below its 10-year average. Lastly, we believe the Bank of England's aggressive tightening cycle is likely just one or two rate hikes away from ending, which could be another tailwind for U.K. equities.

We're seeing select opportunities within both developed and emerging market equities.

Within **emerging markets equities**, we consider **Brazil** and **Mexico** attractive. Both countries are experiencing high nominal and real interest rates, with decelerating inflation. After an early and aggressive hiking cycle that began in 2021, the Central Bank of Brazil cut rates for the first time early last month, and more cuts are expected. Mexico is benefiting from "nearshoring," whereby companies in neighboring countries relocate or expand their operations within Mexico to take advantage of supply chain efficiencies and lower costs. Mexican exports have hit record highs in recent months, as complicated U.S./China trade relations and Russia's invasion of Ukraine have led the U.S. to source more supplies from Mexico.

FIGURE 2: POCKETS OF OPPORTUNITY ACROSS MARKETS

2024 forecasts (%)



Data source: Bloomberg, L.P. and Goldman Sachs Research. Forecasts as of 12 Sep, 2023.

About Nuveen's Global Investment Committee

Nuveen's Global Investment Committee (GIC) brings together the most senior investors from across our platform of core and specialist capabilities, including all public and private markets.

Regular meetings of the GIC lead to published outlooks that offer:

- macro and asset class views that gain consensus among our investors
- insights from thematic "deep dive" discussions by the GIC and guest experts (markets, risk, geopolitics, demographics, etc.)
- guidance on how to turn our insights into action via regular commentary and communications

For more information, please visit nuveen.com.

Endnotes

Sources

All market and economic data from Bloomberg, FactSet and Morningstar.

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