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CIO Weekly Commentary
18 February 2025

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Familiarity breeds investment ideas

Bottom line up top

Inflation's devil is in the details. Financial markets found themselves on uneven footing last week as tariff rhetoric ramped up between the U.S., Canada, Mexico and other key trading partners. Meanwhile, inflation data shocked to the upside as measured by the Consumer Price Index (CPI) for January. Both headline and core CPI (which excludes the volatile food and energy components) came in hotter than expected on a monthly and year-over-year basis. Unfortunately, such readings have begun to look less like an aberration and more like a familiar, if unfriendly, face (Figure 1). Housing, in particular, remains a thorn in the side of monetary policymakers, with shelter costs (+0.4% for the month) staying stubbornly sticky and accounting for roughly one-third of the overall rise in January's CPI.

Investors got a bit of a reprieve 24 hours later with the release of January's Producer Price Index (PPI). This inflation gauge, which captures price changes at the wholesale level, included some encouraging fine print — notably, smaller-than-forecast increases in the costs of health insurance, financial investment advice and domestic airfares. These components feed into the U.S. Federal Reserve's preferred barometer of inflation, the core Personal Consumption Expenditures (PCE) Price Index, scheduled for release at the end of the month. Although markets settled, ending the week on a calmer note in light of the cooler PPI data, the outlook for Fed policy easing in 2025 now prices in just a single rate cut, most likely in December.

Seeing the forest for the trees. Some investors may feel like they've contended with a year's worth of headlines in only the first six weeks of

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On behalf of Nuveen's Global Investment Committee

As Head of Equities and Fixed Income, 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.

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2025. But taking a step back helps put current macroeconomic, policy and market factors in perspective. This reveals that the two major themes of the past three years — sticky inflation and higher-for-longer rates — are largely intact. Investors can therefore remain consistent in their search for portfolio opportunities that benefit from these conditions, while also considering asset allocation ideas that saw some success the last time trade wars and "pro-growth" policies, such as deregulation and corporate tax cuts, ruled the day.

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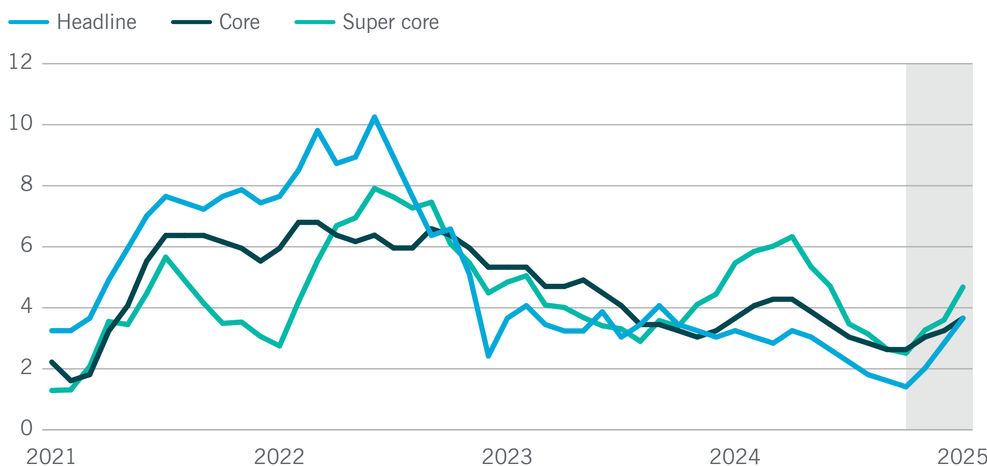
FIGURE 1: DISINFLATION TREND HITS A SPEED BUMP IN JANUARY

Six-month annualized inflation (%)



Data source: Bloomberg, L.P., 31 Jan 2020 – 31 Jan 2025. **Representative indexes: headline:** U.S. CPI Urban Consumers; **core:** U.S. CPI Urban Consumers Less Food & Energy; **super core (core excluding housing):** U.S. Bloomberg BLS CPI Core Services Less Housing. Data represent six-month annualized inflation rates.

Portfolio considerations

Amid the current flurry of tariff announcements and anticipated tax cuts under Trump 2.0, what lessons can investors glean by examining the results of such policies during Trump's first presidential tenure? In 2018, lowering the corporate tax rate from 35% to 21% drove profit growth of +21%, the strongest showing since 2010. On the other hand, consumer spending slowed in 2018, and the effects of a tit-for-tat trade war drove multinational companies' revenues lower. The net result: U.S. stocks outperformed their non-U.S. counterparts in both developed and emerging markets. In fact, robust earnings propelled the S&P 500 Index to 19 all-time highs in 2018.

The situation in early 2025 bears some similarities: Trade uncertainty has increased, although potential tax changes likely won't be passed until 2026. On balance, we think U.S. equities will continue to outperform in the medium term. That said, we've recently seen spikes of volatility in U.S. markets amid trade tensions, uncertainty around tech earnings, artificial intelligence (AI) and an extended pause in Fed rate cuts. In fact, European equity markets have fared better than the U.S. year to date, largely due to

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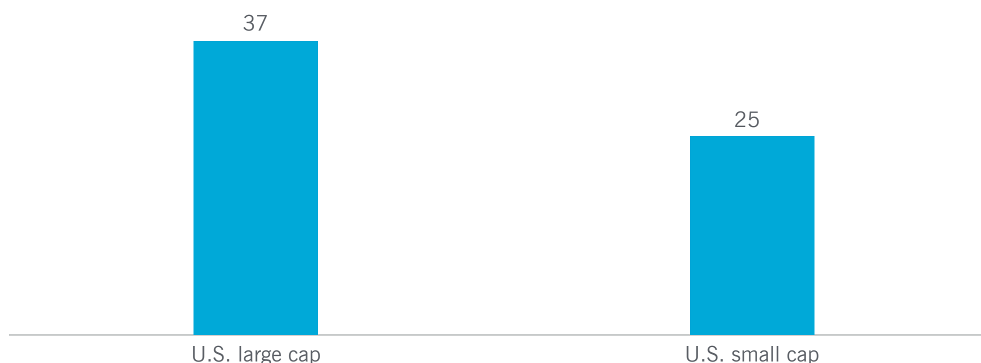
Dividend growth companies are supported by sound fundamentals, sustainable growth potential, healthy balance sheets and ample free cash flow. Their combination of capital flexibility, balance sheet strength and increasing dividend payments could help them mitigate potential inflationary pressures on input costs.

Infrastructure benefits from inelastic demand for the necessary services and operations these companies provide. This has historically been an effective hedge against inflation, thanks to inflation escalators built into underlying contracts. The emergence and evolution of generative AI and the associated need for data centers has created substantial energy infrastructure opportunities. Additionally, accelerated capital expenditures on power generation via renewable, gas and nuclear energy assets, along with power grid upgrades — all of which are necessary to meet unprecedented growth in demand — will be a hallmark of the future U.S. energy landscape.

Small caps over large caps. U.S. tariffs are likely to be more disruptive for U.S. companies that derive significant revenue from non-U.S. sources of demand, which tend to be larger cap. As an example, we looked at firms whose reported non-U.S. revenue accounted for more than half of their total revenue in the last fiscal year. Of those, 37% were large caps, compared to 25% for small caps (Figure 2). Lastly, a strong argument can be made for small caps on the basis of valuations. These remain less expensive relative to large caps and the broader market, while small cap earnings growth is expected to exceed that of large caps in 2025.

FIGURE 2: TARIFFS ARE MORE LIKELY TO IMPACT NON-U.S.-ORIENTED LARGE CAPS

Percent of U.S. companies whose reported non-U.S. revenue is more than 50%



Data source: Bloomberg, L.P., 11 Feb 2025. **Representative indexes: U.S. large cap**: S&P 500 Index; **U.S. small cap**: Russell 2000 Index. Reported revenue is based on the last fiscal year.

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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Important information on risk

All investments carry a certain degree of risk and there is no assurance that an investment will provide positive performance over any period of time.

Equity investments are subject to market risk, active management risk, and growth stock risk; dividends are not guaranteed. Non-U.S. investments involve additional risks, including currency fluctuation, political and economic instability, lack of liquidity and differing legal and accounting standards. These risks are magnified in emerging markets. The use of derivatives involves additional risk and transaction costs. It is important to review your investment objectives, risk tolerance and liquidity needs before choosing an investment style or manager.

Investments in smaller companies are subject to greater volatility than those of larger companies.

A focus on dividend-paying securities presents the risks of greater exposure to certain economic sectors rather than the broad equity market, sector or concentration risk.

Concentration in infrastructure-related securities involves sector risk and concentration risk, particularly greater exposure to adverse economic, regulatory, political, legal, liquidity, and tax risks associated with MLPs and REITs.

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