

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Rate bells ring, are you listening?

Bottom line up top

Holiday cheer or new year drear: What will December bring?

For consumers, there are 16 shopping days until Christmas, and for investors, just 12 trading days. In either case, the holiday season is in full swing, and like countless children around the world wishing for something special from jolly old Saint Nick, equity markets are hoping the U.S. Federal Reserve will bring them a comfy-cozy interest rate cut (size 25 basis points, please) at next week's Fed policy meeting. Market odds currently favor just such a move.

But while equity markets are exuding holiday cheer as they trade at or near all-time highs, public fixed income investors appear more reserved, preparing for a higher-for-longer interest rate environment as the bond yield backup that followed the Fed's first rate reduction in September remains intact. Unexpected economic resilience in the wake of that cut makes it difficult to divine the direction and pace of monetary policy. Last week's release of consensus-topping U.S. nonfarm payrolls for November offered the latest evidence of labor strength, as job creation rebounded from a weak October marred by disruptive hurricanes and worker strikes. Meanwhile, wage growth remained steady at +4.0% year-over-year.

On balance, we think investors needn't be overly concerned that the Grinch or Scrooge will derail the Fed's sled this December. It's also worth noting that the current level of the real fed funds rate is not an outlier relative to history (Figure 1). So even if a beloved flying woodland creature with a storied illuminative nose were waylaid, this investment season still offers sound portfolio allocation ideas that can counter the potential chill of a higher-for-longer rate environment.



Saira Malik, CFA

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Chief Investment Officer*

On behalf of Nuveen's Global Investment Committee

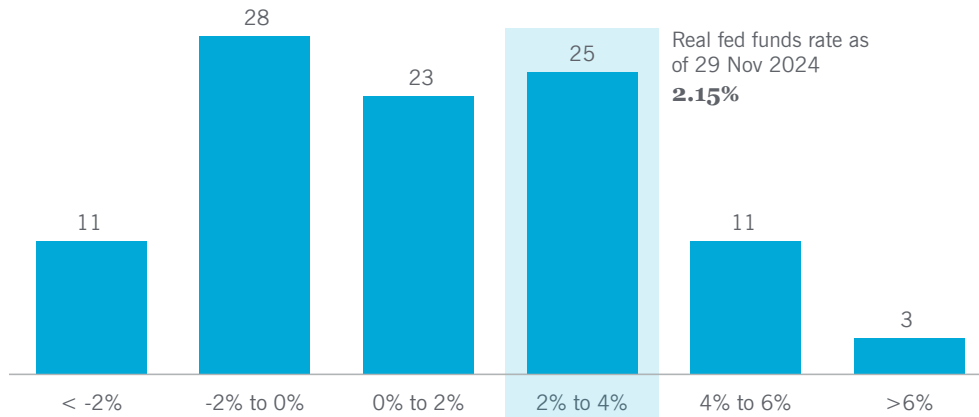
As Head of Equities and Fixed Income, Nuveen's CIO and leader of our Global Investment Committee, Saira drives market and investment insights, delivers client asset allocation views and brings together the firm's most senior investment leaders to deliver our best thinking and actionable investment ideas.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

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FIGURE 1: REAL FED FUNDS RATE NOT CURRENTLY AN OUTLIER

Real fed funds rate, percent of time spent in each range (%)



Data source: Bloomberg, L.P., 29 Nov 2024. Real fed funds rate is calculated by the fed funds target rate upper bound minus the U.S. CPI Urban Consumers YoY Index.

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Portfolio considerations

The U.S. economy is approaching 2025 on solid footing, with GDP growth above expectations and the employment market remaining resilient. We expect the Fed will continue its easing cycle, but at a slower pace than markets previously anticipated. A milder and more protracted decline in interest rates means fixed income investments may not benefit much from capital appreciation in the near term. Against that backdrop, our fixed income positioning for next year is focused on four themes:

- 1. Current yields are near their highest levels in more than 15 years.** Higher base rates have significantly enhanced income potential, with yields of about 6% or more for investment grade plus sectors such as preferred securities and securitized assets, including asset-backed securities (ABS) and commercial mortgage-backed securities (CMBS) (Figure 2).
- 2. Short- and long-term rates will be higher for longer.** That makes exposure to shorter-duration, floating-rate instruments such as senior loans — currently yielding 8.5% — a compelling choice, especially given their sound credit fundamentals. Like senior loans, ABS are also relatively low duration, in addition to providing attractive yields. Also worthy of consideration are esoteric securities backed by nontraditional assets, offering a spread between 75 and 125 basis points in yield compared to short-maturity corporate bonds.
- 3. Balance duration risk with credit risk.** Within investment grade categories, we are less positive on corporates, where duration is much longer than in other fixed income sectors. In contrast, preferred

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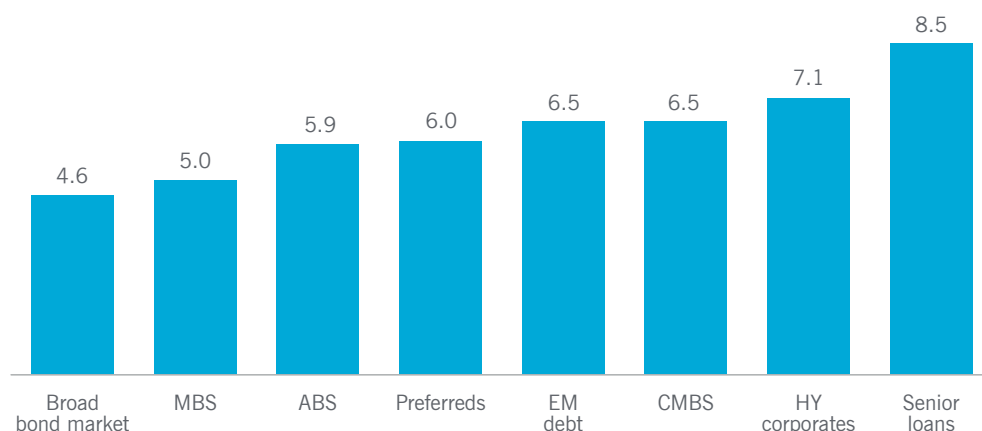
securities — in particular, the \$25 par segment — offer nearly 1.5% of yield per year of duration. Preferreds also look well-positioned for 2025, as potential deregulation and an expected pickup in M&A (mergers and acquisitions) activity could bode well for banks, the largest issuer of preferreds.

- 4. Position for volatility.** In the below-investment grade space, we favor an up-in-quality approach. Within senior loans, we find exposure to BB and B rated issues particularly attractive. BB rated loans, for example, have a healthy interest coverage ratio of 4.X, according to Bloomberg.¹

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FIGURE 2: FIXED INCOME OFFERS VARIOUS RISK AND DURATION PROFILES, WHILE CURRENT YIELDS ARE NEAR 15-YEAR HIGHS

Yield to worst (%)



Data sources: Bloomberg, L.P., 29 Nov 2024. Performance data shown represents past performance and does not predict or guarantee future results. Representative indexes: broad bond market: Bloomberg U.S. Aggregate Index; MBS: Bloomberg U.S. Mortgage-Backed Securities Index; ABS: ICE BofA Fixed Rate ABS AA-BBB Index; CMBS: ICE BofA Fixed Rate CMBS AA-BBB Index; preferreds: ICE BofA U.S. All Capital Securities Index; EM debt: Bloomberg Emerging Market USD Aggregate Index; HY corporates: Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index; senior loans: Credit Suisse Leveraged Loan Index. It is not possible to invest directly in an index.

¹ The interest coverage ratio measures a company’s ability to pay interest on its outstanding debt. It is calculated by dividing the company’s earnings before interest, taxes, depreciation and amortization (EBITDA) by the company’s interest expense.

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About Nuveen's Global Investment Committee

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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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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 investing involves risk. Investments are also subject to political, currency and regulatory risks. These risks may be magnified in emerging markets. A focus on dividend-paying securities presents the risks of greater exposure to certain economic sectors. Dividend yield is one component of performance and should not be the only consideration for investment.

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.

Debt or fixed income securities are subject to market risk, credit risk, interest rate risk, call risk, tax risk, political and economic risk, and income risk. As interest rates rise, bond prices fall. Credit risk refers to an issuer's ability to make interest payments when due. Below investment grade or high yield debt securities are subject to liquidity risk and heightened credit risk. Non-U.S. investments involve risks such as currency fluctuation, political and economic instability, lack of liquidity and differing legal and accounting standards. These risks are magnified in emerging markets. It is important to review your investment objectives, risk tolerance and liquidity needs before choosing an investment style or manager.

Investing in preferred securities entails certain risks, including preferred security risk, interest rate risk, income risk, credit risk, non-U.S. securities risk and concentration/nondiversification risk, among others. There are special risks associated with investing in preferred securities, including generally an absence of voting rights with respect to the issuing company unless certain events occur. Also in certain circumstances, an issuer of preferred securities may redeem the securities prior to a specified date. As with call provisions, a redemption by the issuer may negatively impact the return of the security held by an account. In addition, preferred securities are subordinated to bonds and other debt instruments in a company's capital structure and therefore will be subject to greater credit risk than those debt instruments. Credit risk is the risk that an issuer of a security will be unable to make dividend, interest and principal payments when due. Interest rate risk is the risk that interest rates will rise, causing fixed income securities prices to fall. Income risk is the risk that the income will decline because of falling market interest rates. This can result when an account invests the proceeds from new share sales, or from matured or called fixed income securities, at market interest rates that are below the account's current earnings rate. An investment in foreign securities entails risks such as adverse economic, political, currency, social or regulatory developments in a country including government seizure of assets, lack of liquidity and differing legal or accounting standards (non-U.S. securities risk). Preferred security investments are generally invested in a high percentage of the securities of companies principally engaged in the financial services sector, which makes these investments more susceptible to adverse economic or regulatory occurrences affecting that sector concentration/nondiversification risk). It is important to review your investment objectives, risk tolerance and liquidity needs before choosing an investment style or manager.

Nuveen, LLC provides investment services through its investment specialists.

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