

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Munis get the job done while DC still dithers

Bottom line up top

There's a supply and demand problem — with data. Most of the available good news, like loosening monetary policy and solid earnings growth, is already baked into the current U.S. equity market rally. Yet investors are showing only a little caution in the face of several headwinds. Chief among these is the ongoing federal government shutdown, which continues to delay the release of critical economic data, including the monthly nonfarm payrolls report and key inflation metrics. The data deficit has left investors and the U.S. Federal Reserve in the dark at a time when illumination is needed most.

And though last week ended with at least a glimpse of government inflation data — thanks to Labor Department staff who returned to the office to produce the delayed (and ultimately benign) Consumer Price Index print for September — we're also relying on market-based indicators of inflation expectations, such as the 5- and 10-year breakeven inflation rates (Figure 1). Both currently stand at roughly 2.3%, signaling a relatively stable outlook.

Meanwhile, earnings numbers are showing, and going, up.

A solid third quarter earnings season for the S&P 500 Index continues apace, with year-over-year earnings growth at +9.2% as of 24 October. Technology and AI-driven firms are leading the pack, while health care and some consumer sectors lag. Although the beats rate remains high, the magnitude of upside is lower, suggesting that strong results are already reflected in the S&P 500's forward price-to-earnings (P/E) ratio of 22.6x - a significant premium over its 10-year average of 18.6x. Moreover, we're entering a seasonal November-January period 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.

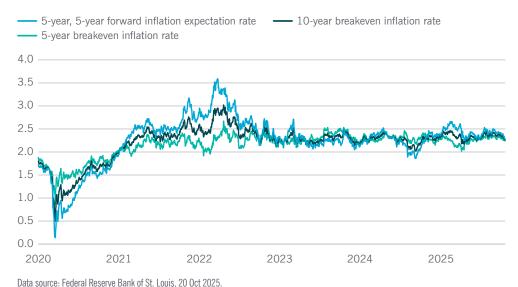
historical weakness for momentum stocks. This could pose downside risks for some of the high-flying Magnificent 7 names, especially given market whispers of a potential AI bubble.

With much of the equity upside likely already priced in, and the macro backdrop made more opaque by data delays, investors may want to consider diversifying their portfolios by initiating or increasing allocations to defensive, high-quality asset classes such as municipal bonds.

Investors may want to consider diversifying into defensive, high-quality assets like muni bonds.

FIGURE 1: INFLATION EXPECTATIONS ARE STABILIZING

Inflation expectations (%)



Portfolio considerations

Municipal bonds have rebounded impressively over the past two months, having underperformed taxable fixed income assets by a wide margin for most of the year. The dominant headwind has been historically high supply. Primary new issuance exceeded \$400 billion year-to-date through September, meaning supply in the first three quarters of 2025 had already surpassed the \$381 billion annual average seen over the previous decade.

But while supply has been hot, demand has not: Over 2022 and 2023, a massive \$175 billion exited the asset class, representing the largest calendar-year outflow on record. Investors began returning to munis in 2024, with \$41.5 billion in net positive flows. Year-to-date net inflows for 2025 stood at \$35.5 billion through 16 October. While the return to positive flows is encouraging, the amount that's returned to the asset class is less than half of what left during the record outflows.

That said, we expect investor demand to continue rising given the current backdrop of elevated yields, healthy fundamentals and the prospect of additional Fed rate cuts, which should push cash yields lower and help sway investors still on the sidelines to re-enter the market.

The municipal yield curve has nearly doubled in steepness since the start of 2025. The 1-to-30 year yield differential has expanded from 91 basis points (bps) to 170 bps as of 20 October. As a result, investors are being rewarded with higher yields as they move further out on the muni curve (Figure 2). For investors open to lengthening duration and taking on credit risk, high yield municipals offer a tax-equivalent yield of 9.53% for those in the top income tax bracket. That's one of the most compelling levels of income across the entire fixed income universe. High yield munis can be paired with investment grade municipal exposure (ICE BofA U.S. Municipal Securities Index), where the current spread and yield are in the 81st and 84th percentiles, respectively, relative to their trailing 10-year averages.

Lastly, fundamentals for issuing municipalities remain strong. Revenue collections and reserves are near the highest levels in more than 40 years. Meanwhile, credit rating upgrades continue to exceed downgrades, as they have over the past five years, and muni defaults are rare, isolated and idiosyncratic.

FIGURE 2: INVESTORS BEING REWARDED FOR EXTENDING MATURITIES

Taxable-equivalent yield curve (%)



Data sources: Bloomberg, L.P., Nuveen Portfolio Strategy Group, 20 Oct 2025, Taxable-equivalent yield (TEY) is the yield a taxable investment needs to possess (before taxes) for its yield to be equal to that of a tax-free municipal investment. The yields shown are based on the highest individual marginal federal tax rate of 37%, plus the 3.8% Medicare tax on investment income. Individual tax rates may vary. They do not take into account the effects of the federal alternative minimum tax (AMT) or capital gains taxes.

We expect investor demand for munis to continue rising, given the current yield backdrop and healthy fundamentals.

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- · 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

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Endnotes

Sources

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

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