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CIO Weekly Commentary
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CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Is private real estate the next comeback kid?

Bottom line up top

The Hunt for Red or Blue November has all the makings of a thriller. That said, we may have to wait to learn how the story ends. Although voters in the U.S. cast their ballots tomorrow, opinion polls show a dead heat, and the outcome could be unknown for days or even weeks. U.S. history offers few examples on how investors might respond to a potential delay, but we know markets hate uncertainty.

The most famous deadlocked result in modern times occurred in 2000, when the presidential contest went all the way to the U.S. Supreme Court in Bush v. Gore. In the 24 trading days between Election Day and the Supreme Court's mid-December decision, the S&P 500 Index fell more than 4% and was down almost 8% by the end of 2000. Circumstances were quite different then, with the election taking place amid a bursting dot-com bubble, a rising rate environment and a weak earnings backdrop. However, U.S. equity market valuations today are uncannily similar to those in early November 2000 — and likely a warning to expect heightened volatility in the near term (Figure 1).

Investors' preference on the economy: "Land softly and stop carrying a big stick (of inflation)." Last week's wave of economic data couldn't be all things to all people, but on balance it offered financial markets some optimism that labor markets (despite impacts from weather and industrial action), GDP growth, inflation and consumer confidence were trending enough in the right direction to produce an eventual soft landing. For any undecided members on the U.S. Federal Reserve's policymaking committee, these latest numbers may help sway them toward the 25 basis points (bps) rate cut we expect at their post-Election Day meeting.

Saira Malik, CFA
Head of Nuveen Equities and Fixed Income, 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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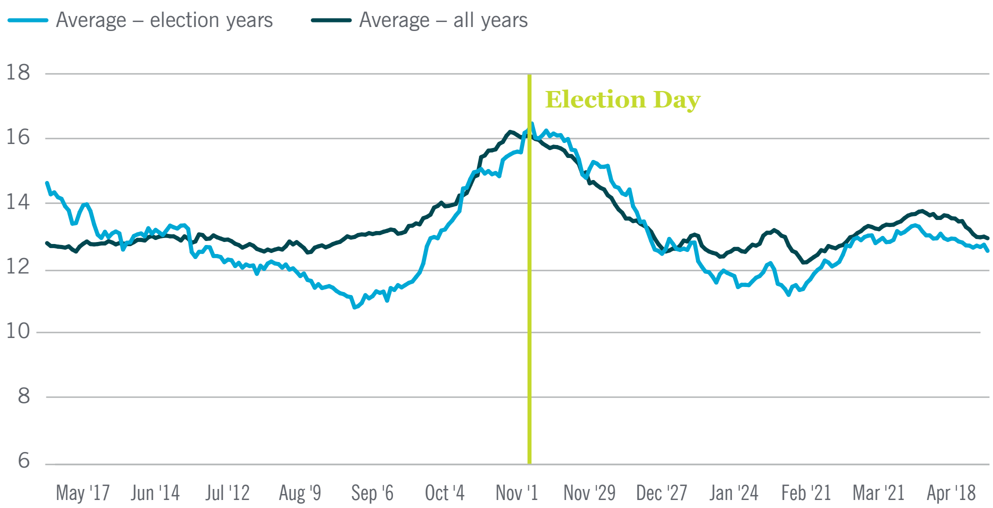
An improved earnings season may be shaping up. The S&P 500's blended earnings growth rate for the third quarter improved to +5.1% as of 1 November, up from +3.5% the week prior. While that's still lower than the +7.6% pace analysts estimated at the end of June, it keeps the index on track for a fifth consecutive quarter of positive earnings growth. Meanwhile, valuations continue to look frothy, with the S&P 500's forward price-to-earnings (P/E) ratio currently at 21.3x, well above its 5- and 10-year averages of 19.6x and 18.1x, respectively, according to FactSet.

FIGURE 1: VOLATILITY IS HIGHER IN THE FALL EVEN IN NON-ELECTION YEARS

Volatility before and after election day (%)



Data sources: Nuveen Portfolio Strategy Group, Bloomberg, L.P., S&P 500. 1948 – 2023. **Performance data shown represents past performance and does not predict or guarantee future results.** Data begins with the elected term of President Truman, who had assumed the presidency after President F.D. Roosevelt's death in 1945, as the start of the post WWII period. Average 30-day volatility across calendar years at the same calendar date in each year.

Portfolio considerations

Private real estate states its case

After seven consecutive quarters of negative total returns, the private real estate sector, as measured by the NCREIF ODCE Total Return Index, was up +0.25% in the third quarter of 2024. The extended downturn for real estate had been triggered by the Fed's aggressive 2022-2023 rate hiking cycle and post-pandemic stress in the office property sector. Now, however, with the Fed having initiated its easing cycle and projecting further rate cuts over the next two years, the interest rate environment should become a tailwind for the asset class. We believe both stabilizing fundamentals and transaction market pricing point to a broad recovery.

A pullback in new construction activity across property types bodes well in the medium term, helping to moderate supply, a positive for rent growth.

In the U.S. apartment and industrial markets, new construction starts are at less than one-third of their peak levels in 2021 (apartments) and 2022 (industrial). Meanwhile, the volume of square footage currently under construction has returned to pre-pandemic levels.

Markets experiencing increased demand due to population growth or other structural changes should see occupancies increase in the medium term. Historically, occupancy rates and rent growth are well correlated, offering investors the potential to realize gains from both, as well as from the associated increase in property values going forward.

Portfolio allocations to private real estate may be funded from either equity or fixed income, depending on the investor's objectives. Since 2000, private real estate has offered competitive returns versus equities, with less than half the volatility and half the number of negative quarters (Figure 2). During the same period, private real estate has outperformed bonds by nearly 3% annualized, with fewer negative quarters and compelling diversification benefits due to the negative correlation between the two asset classes.

With income a larger component of total return than capital appreciation in private real estate, sourcing a portfolio allocation from bonds can be a way to seek improved risk-adjusted returns, while also improving the tax efficiency of the income. Investors may receive up to the depreciated amount of the asset as return on capital, helping to minimize the impact of income taxes. In our view, the private real estate market correction is nearly complete — and now is a good time for investors to take a fresh look at the asset class.

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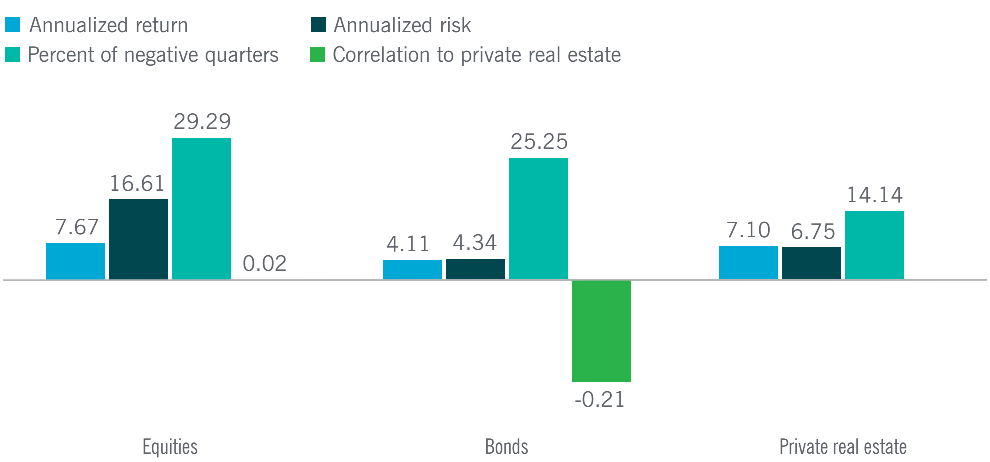
FIGURE 2: PRIVATE REAL ESTATE HAS OFFERED ATTRACTIVE RISK ADJUSTED RETURNS AND LOW CORRELATION

Relative characteristics (%)



Data source: Bloomberg, L.P., 31 Dec 1999 – 30 Sep 2024. **Performance data shown represents past performance and does not predict or guarantee future results.** Quarterly returns were used in the analysis. **Representative indexes: equities:** S&P 500 Total Return Index; **bonds**: Bloomberg U.S. Aggregate Total Return Index; **private real estate**: NCREIF Open End Diversified Core Total Return Index. Annualized risk is the standard deviation of quarterly returns.

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

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 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.

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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