Large Cap Core

Marketing communication | As of 30 Sep 2024

- **During the third quarter, the Large Cap Core SMA performed in line with the benchmark Russell 1000® Index.**
- **Security selection was favorable overall, particularly in the consumer staples sector, while allocation effect modestly detracted.**
- **Market leadership shifted during the quarter away from larger-cap, growth-oriented names and toward value-oriented and smaller-cap stocks, as well as more interest rate sensitive sectors, as the Federal Reserve (Fed) made its first rate cut of the current cycle.**

Market review

Economic growth continued to expand during the third quarter, although more signs of a slowdown emerged. Second quarter's U.S. gross domestic product (GDP) growth came in stronger than expected at an annualized pace of 3.0%, while full-year growth is tracking just slightly below that rate, underpinning investors' hopes for an economic soft landing. Encouraging headline inflation prints during the quarter led key central banks to lower interest rates, even as core inflation remained sticky. The Fed garnered the biggest headline by kicking off its long-awaited policy easing cycle with a 50-basis-point cut in September, larger than many investors had expected. The Bank of England also began lowering rates while the European Central Bank made its second rate cut of this cycle. The People's Bank of China launched a battery of stimulus measures including rate cuts to help kickstart the country's deteriorating economy and ward off deflation. Meanwhile, the Bank of Japan (BoJ) was the outlier with a surprise increase to the country's key interest rate to help curb the yen's fall versus the U.S. dollar.

The stock market started the quarter on a positive note in July, aided by falling Treasury yields and optimism over approaching Fed rate cuts. By month end, the bullish start had given way to concerns about slowing earnings growth for technology companies, which have powered the market for much of the year. In early August, global equity markets sold off sharply after a disappointing U.S. jobs report fanned recession fears, China's economy showed greater signs of deterioration, and the BoJ's surprise rate hike sparked an unwinding of the yen carry trade. As the month progressed, however, the tide quickly turned as inflation reports showed pricing pressures continuing to ease, corporate earnings remained strong, and Fed Chair Powell indicated the time had come for U.S. rate cuts. Throughout September, various market indexes such as the Dow Jones Industrial Average, S&P 500 Index and Nasdaq Composite notched new record highs as investors anticipated the Fed's cut.

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While all major U.S. equity indexes performed well, the market rally broadened out during the quarter with small- and mid-cap stocks and more value-oriented stocks leading the way. Smaller companies, which tend to carry more floating-rate debt on their balance sheets, rallied as the Fed lowered borrowing costs. The small-cap focused Russell 2000® Index returned 9.27% for the quarter but still lags large caps with its 11.17% year-to-date return.

The benchmark large-cap Russell 1000® Index returned 6.08% for the quarter, led by double-digit gains in five sectors. The defensive utilities sector led the pack as earnings expectations continued to be very high for these companies. Real estate and industrials followed close behind as the market rotated into interest-rate sensitive sectors in anticipation of the beginning of the Fed's easing cycle. Energy was the worst performer in the Russell 1000® and the only sector in the red for the quarter as oil prices fell amid cooling demand from China. The year's previous high-flying sectors, information technology and communication services, posted only modest gains for the quarter. Year to date, the Russell 1000® has advanced 21.18%.

Overseas, both emerging market (EM) stocks and non-U.S. developed markets outpaced the U.S. market, with the dollar's decline boosting returns for U.S. dollar-based investors. The aggressive stimulus package by the Chinese government sent equities in that country soaring, with the Shanghai SE Composite Index returning 18.32% for the quarter. China's strong advance helped fuel an 8.88% gain for the MSCI Emerging Markets Index as results among other EM countries were mixed. Developed markets, as measured by the MSCI EAFE Index, returned 7.33% as European markets rallied in the face of mixed economic data. Meanwhile, Japan's stock market quickly recovered from its 15% plunge in early August triggered by the BoJ's surprise rate increase and the resulting strengthening of the yen. The Nikkei 225 Index ended the quarter with an 8.38% return.

Portfolio review

The Large Cap Core SMA performed in line with the Russell 1000® Index on a gross and net of fees basis for the quarter. Security selection was favorable overall, particularly in the consumer staples sector, while allocation effect modestly detracted.

Contributors

Within the industrials sector, shares of Parker-Hannifin, a global manufacturer of motion and control technologies, aided results. The company's quarterly revenue was around 2% ahead of expectations, driven by outperformance within its Aerospace Systems segment, with the Diversified Industrial North American and International segments reporting in-line results. Overall, orders remain higher within Aerospace, while the Industrial businesses have turned neutral. Earnings margin performance was slightly better across all three business segments. Parker-Hannifin's free cash flow was up around 15% year-over-year to $3.0 billion, supporting the company's quicker pace of debt reduction.

Another top contributor was integrated utility company NextEra Energy. The company reported quarterly earnings above consensus estimates due to continued new investment growth in its Florida Power & Light and NextEra Energy Resources businesses. Management reaffirmed its earnings per share guidance range of 6-8% annual growth through 2027 and annual dividends per share growth of around 10% through at least 2026. Furthermore, the company benefited from the rotation to defensive and value-oriented sectors and the decline in interest rates during the quarter.

Financial services and technology firm Fiserv reported solid quarterly results while also raising guidance. Despite slower spending in the Merchant solutions segment, demand for the company's software-integrated point-of-sale solution called Clover remained strong, growing faster than its peers and gaining market share. While Merchant remains the primary growth driver for the company, Financial Solutions growth also improved. Margin expansion continued and free cash flow conversion inflected better, which indicates that Fiserv's execution remains solid ahead of a strong pipeline of global product launches.

Detractors

Semiconductor equipment supplier Applied Materials gave back last quarter's gains despite posting a solid quarterly earnings report and modest increase in guidance, driven by increased demand for artificial intelligence (AI) related products and services. Investors remained cautious toward the stock as one of the company's major clients, Intel, continued to reduce its capital expenditures. Several other issues weighed on Applied Materials' shares including subdued memory spending and U.S. election uncertainty as the country considers tighter restrictions on exports of semiconductor equipment to China. In addition, the U.S. Commerce Department denied the company's Chips Act funding request for its new research and development facility in California. We sold Applied Materials shortly after quarter-end.

In the health care sector, a position in biotechnology company BioMarin Pharmaceutical detracted during the quarter. The stock declined in September after competitor Ascendis Pharma released promising test data from its trial of a new drug to treat the genetic growth disorder achondroplasia. If approved, the drug would compete with BioMarin's Voxzogo, which is currently the only FDA-approved treatment for children with achondroplasia and open growth plates. Investors were concerned the increased competition will diminish the company's growth prospects and result in increased legal expenses in order to defend patents.

Also in information technology, a position in memory chipmaker Micron Technology gave back gains from the prior quarter because of a slowdown in demand and pricing for personal computers and smartphones, which were expected to weigh on the company's results. However, the fears were overblown, and Micron Technology's report at the end of the quarter reflected a strong earnings beat and raised guidance. The company continues to experience growing data center demand for its dynamic random-access memory (DRAM) and high bandwidth memory (HBM) products driven by the substantial storage and faster memory speeds needed to run AI. This demand more than offset the inventory build in the weaker PC and smartphone markets, areas where management expects to see better growth starting in the second half of 2025 as AI-enabled products begin to gain more meaningful traction.

Portfolio positioning

The Large Cap Core portfolio management team remains intently focused on identifying companies supported by dependable fundamentals, attractive earnings growth potential, and upcoming catalysts. The team continues to favor companies supported by strong free cash flow generation, balance sheet strength, and the ability to maintain and improve profit margins. Given market hypersensitivity to disappointing economic data, rising geopolitical risk, and heightened political uncertainty ahead of the U.S. elections in November, we anticipate persistent volatility during the fourth quarter. We believe it is particularly important to maintain a balance between companies with compelling earnings growth potential and defendable competitive advantages, while being mindful of current valuations and maintaining broad diversification.

During the third quarter, we established new positions in Stryker, Permian Resources, M&T Bank, Alliant Energy, BioMarin Pharmaceutical, and Bristol-Myers Squibb. We fully eliminated the portfolio's positions in Danaher, Accenture, United Therapeutics, Huntington Ingalls Industries, and Charles Schwab. While the portfolio's overall composition did not meaningfully change during the quarter, the team felt the eliminated securities were facing company-specific risks that would result in diminished growth potential and weaker sentiment in the coming quarters. We believe the new purchases provide more compelling business fundamentals with attractive risk/reward profiles.

Overall, our bottom-up security selection process has resulted in modest tilts toward stocks with higher profit margins and profitability metrics. From a risk mitigation standpoint, we've focused on maintaining lower exposure to more volatile companies compared to the index by slightly reducing the portfolio's beta during the quarter. As of quarter-end, the portfolio's largest relative sector overweights were in the communication services and financials sectors. The portfolio's largest relative sector underweights were in the consumer discretionary and information technology sectors.

Outlook

We anticipate U.S. economic growth will continue to decelerate over the balance of the year. Consumer spending, which makes up about 70% of GDP, is facing headwinds from depleted household savings and increased use of credit. Manufacturing activity is also contracting, while the housing market continues to face challenges from steep home prices and still-high mortgage rates. Markets may also be too optimistic about future rate cuts as Fed officials have indicated a preference to move steadily, which means they will likely cut 25 basis points per meeting. We expect the Fed to eventually get back to a neutral policy stance of around 3.25% to 3.50% by the middle of 2025.

Several factors have the potential to increase market volatility going forward including recession fears, an unusually busy global election season, and the escalation of military conflicts in the Middle East. We anticipate market volatility will likely continue to remain elevated until the November 5th U.S. elections, and potentially beyond, fueled by the market's hypersensitivity to disappointing economic data and multiple global military conflicts. Equity valuations have become less favorable amid the 2024 rally with the S&P 500's forward P/E ratio currently trading above its five- and 10-year averages, according to FactSet, and not reflecting even a modest economic contraction.

Given the uncertainty facing capital markets, we believe investors should maintain adequate portfolio diversification and focus on identifying companies supported by attractive fundamentals, sustainable growth, ample free cash flow, and healthy balance sheets. Although volatility and uncertainty present challenges for investors, we continue to believe equity investors are best served by staying in the market, and may benefit from a flexible investment approach supported by rigorous, bottom-up research, careful stock selection, and thoughtful portfolio construction.

For more information contact: 800.752.8700 or visit nuveen.com

Minimum investment is $100,000.

Important information on risk

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Glossary

The **S&P 500® Index** measures the performance of large capitalization U.S. stocks. The S&P 500® is a market weighted index of 500 stocks traded on the NYSE, AMEX and NASDAQ. The **Russell 1000® Index**, a subset of the Russell 3000® Index, represents the 1000 top companies by market capitalization in the United States. Index returns assume reinvestment of dividends, but do not reflect any applicable sales charges or management fees. **Volatility** is the fluctuations in market value of a portfolio or other security. The greater a portfolio's volatility, the wider the fluctuations between its high and low prices. I**t is not possible to invest directly in an index.** Clients should consult their financial professionals regarding unknown financial terms and concepts

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