

## Dividend Growth

Marketing communication | As of 31 Dec 2024

- **The U.S. equity markets moved higher during the fourth quarter driven by the stronger performance of growth-oriented companies and expectations for the pro-growth initiatives of the incoming administration.**
- **The Dividend Growth strategy underperformed its benchmark, the S&P 500, due to stock selection and allocation effects.**
- **With lingering inflation concerns and higher valuations, we remain steadfast that investors should remain diversified and focus on companies with attractive fundamentals, healthy balance sheets, ample free cash flow generation, and management teams with a strong commitment to return capital to shareholders.**

### Market review

The U.S. economy continued to expand during the fourth quarter fueled by robust consumer spending. Although inflation worldwide remained above desired levels, monetary policy varied among key central banks. The Federal Reserve (Fed) made its second and third consecutive rate cuts of the year, trimming by 25 basis points in November and December. After the December meeting, however, Fed policymakers projected a slower pace of cuts in 2025 given still-sticky inflation and the potential for inflationary policy moves under the incoming Trump administration. The Bank of England made its second rate cut of the year in November and then paused, while the European Central Bank made its fourth rate cut of this cycle in December amid signs of weakening European Union growth, political chaos in France and tariff concerns. The People's Bank of China remained on hold but continued to affirm its supportive policy stance as it faced pressure to reflate the country's economy. The Bank of Japan also stood pat at its October and December meetings, awaiting more information on the policies of the new U.S. administration while debating timing of a pending rate hike.

The U.S. equity market experienced significant volatility during the quarter, losing ground in October as strong economic data propelled U.S. Treasury yields higher. Stocks rebounded in November following Donald Trump's election victory and optimism over his pro-growth agenda featuring lower taxes and fewer regulations. However, the rally stalled in December as hawkish comments by the Fed quickly dampened the enthusiasm. The bond market struggled throughout the quarter with yields steadily rising as progress on inflation slowed and the election results increased the potential for more persistent price pressures down the road.

Despite fourth quarter's volatility, 2024 ended as a banner year for equity investors. The technology-heavy Nasdaq Composite continued to notch new record highs, particularly in the aftermath of the U.S. presidential election, crossing the 20,000 milestone during the period. The Nasdaq ended the quarter and year returning 6.35% and 29.57%, respectively, fueled by ongoing enthusiasm for technology stocks,



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artificial intelligence (AI) and crypto in the wake of lower rates and the Trump victory. Meanwhile, the Dow Jones Industrial Average faced more downward pressure in December, posting its worst monthly performance in more than two years. However, the index still eked out a positive return of 0.93% for the quarter and was up 14.99% over the full year.

The S&P 500 Index ended the quarter up 2.41% despite some year-end weakness caused by the Fed comments. However, only four of 11 sectors posted positive returns for the quarter including consumer discretionary, communication services, financials, and information technology. The materials and health care sectors lagged the most, both declining by double digits over the three-month period. Meanwhile, value stocks across the market cap spectrum posted negative returns for the quarter as measured by Russell indexes. For the full year, the S&P 500 produced a stellar return of 25.02%, only the fourth time in history that the index has notched two consecutive years of returns over 20%.

## Portfolio review

During the fourth quarter of 2024, the Dividend Growth portfolio underperformed its benchmark, the S&P 500 Index on a gross and net of fee basis. Both security selection and sector allocation effects had a negative impact on relative performance during the quarter. The information technology sector had the largest contribution to relative performance driven by positive stock selection effects. The consumer discretionary sector was the largest detractor to relative performance due to stock selection effects and the portfolio's lack of exposure to non-dividend payers such as Tesla and Amazon.com which performed strongly. The Dividend Growth strategy's mandate to maintain representation to all 11 GICS sectors was not beneficial as sector performance dispersion was high during the quarter.

## Contributors

Global semiconductor and software infrastructure solutions company **Broadcom Inc.** was the top contributor to performance. The company reported quarterly earnings results slightly above estimates and provided guidance for the upcoming quarter in-line with expectations. The stock was up significantly as management highlighted the company's continued AI momentum and the massive growth opportunity for the AI semiconductor market. The company now estimates the AI market opportunity for accelerators and networking will range between \$60-90 billion in fiscal year 2027. Management noted continued strong prospects for maintaining AI custom ASIC (Application-Specific

Integrated Circuits) leadership and market share gains. Broadcom already has working custom ASIC 3nm silicon that will ship this spring, well ahead of anybody in the market (merchant or custom). Non-AI semiconductor dynamics continue to demonstrate a modest cyclical recovery. Furthermore, the company increased its dividend by 11% in December and management expects significant free cash flow growth in fiscal year 2025.

Another top contributor was semiconductor maker **Taiwan Semiconductor Manufacturing Co.** The company reported impressive quarterly earnings per share results highlighted by strong revenue growth and better than expected margins driven by increased utilization. The company continues to see strong demand for artificial intelligence chips, which is expected to nearly double in 2025. Utilization, yields, and margins should ramp up on their leading edge N3 node with demand from smartphone and CPU customers. Fears of increased competition from Intel's efforts to rebuild their foundry business have faded as that company faces internal struggles.

Major U.S. bank **JPMorgan Chase & Co.** further contributed to relative performance during the quarter. The company reported strong quarterly results driven by better-than-expected results for net interest income, trading, and investment banking. Investors showed confidence in the company's near-term outlook which remains stable with continued (albeit fewer) rate cuts likely to stimulate capital markets activity, the job market remains healthy, consumer spending has been resilient, and capital ratios have been better than expected. Following the U.S. election results, investors embraced the financials sector given expectations that the incoming administration will focus on de-regulation that will increase capital deployment.

## Detractors

Managed care organization **Elevance Health Inc.** was the largest detractor from performance during the quarter as the company faced headwinds from higher medical costs and a decline in Medicaid enrollment. Elevance reported quarterly earnings per share in mid-November that missed expectations as benefit expenses were above expectations. While the company reaffirmed long-term guidance, management reduced guidance for fiscal year 2024 due to Medicaid cost trend weakness and investors remain concerned that margins could be pressured further. The managed care industry was also negatively impacted by the tragic murder of UnitedHealth Group executive Brian Thompson with wide speculation that the shooter was upset by how a relative was treated by medical insurance.

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Cell tower real estate investment trust **American Tower Inc.** was another top detractor from performance. The company's quarterly results included several one-off items including FX headwinds and bad debt expenses related to a tenant in South America, which added confusion when assessing the results and comparing updated guidance. Importantly, the rise in bond yields negatively impacted the real estate sector and the cell towers specifically which tend to be a more interest rate sensitive industry. Additionally, the potential for lower corporate tax rates would make REITs less attractive relative to non-REIT securities.

Integrated utility company **NextEra Energy Inc.** further detracted from performance during the quarter despite reporting quarterly earnings per share above consensus estimates. The strong outperformance of growth stocks and rising interest rates were meaningful headwinds to the utilities sector during the fourth quarter. In particular, investors feared higher interest rates would hinder the profitability of NextEra's renewable energy business. Following the U.S. election outcome, concerns regarding the potential for the incoming administration to remove renewable energy initiatives weighed further on the stock. On a positive note, the company's renewable business has a strong backlog through 2027 and management recently reiterated its guidance for approximately 10% annual dividend growth through at least 2026.

### Portfolio positioning

At Nuveen, we believe dividend growth-oriented companies offers desirable long-term attributes and are well positioned for compelling relative performance in the coming year. Over the long-term, companies that continued to grow or initiate dividends have generated higher annualized returns with a lower annualized standard deviation, than all other segments of the equity market. While dividend growth companies do not outperform in all market environments, their strong risk-adjusted returns over long periods of time make them an ideal core building block for any equity allocation.

We believe an allocation to dividend growth-oriented companies offer advantages to investors seeking to maintain equity exposure that balances quality, stable growth, and defensive characteristics. In our view, dividend-paying equities supported by attractive fundamentals, sustainable growth potential, healthy balance sheets, ample free cash flow, stable profit margins, and management teams committed to returning capital to shareholders should be well-positioned to benefit from continued economic growth. The ability of these companies to maintain and expand

margins amid input cost inflation and higher interest rates — while also providing investors with a cushion against market volatility — is likely to be rewarded in the new year. We believe an actively managed approach focused on companies with the financial ability to maintain and increase their dividends regardless of the economic environment is appropriate today given the various crosscurrents impacting capital markets.

We continue to focus on companies supported by attractive fundamentals and sustainable dividend growth potential while maintaining adequate diversification. As of quarter-end, the Dividend Growth portfolio's largest absolute sector allocations were in the information technology, financials, health care, and industrials sectors. During the fourth quarter, we added Danish biopharmaceutical company Novo Nordisk A/S and packaging company Smurfit Westrock Plc to the portfolio and fully eliminated Charles Schwab Corporation and Packaging Corporation of America.

Danish health care company Novo Nordisk A/S was added to the Dividend Growth portfolio given our belief that the company will remain a leader in treatments for metabolic diseases despite the risk of competitive entrants. We expect the company's obesity drugs, Wegovy and Ozempic, to drive years of strong earnings growth at a reasonable valuation. We are attracted to the company's focused strategy and capital allocation policies focused on returning capital to shareholders.

Packaging Corporation of America was eliminated from the Dividend Growth portfolio given uncertainty regarding the company's dividend growth prospects. Despite strong fundamental results, the company appears focused on organic capex funding and uncertainty remains regarding when the company's next dividend increase will materialize. Furthermore, the stock performed strongly over the past two years and experienced considerable multiple expansion. Given the uncertainty regarding dividend growth in the coming year, we felt it was an opportune time to replace the stock with industry peer Smurfit Westrock PLC. Earlier in the year, Smurfit Kappa and WestRock merged to create Smurfit Westrock, a new global leader in corrugated packaging, with revenues of more than \$30B and the only company with leadership positions in both North America and Europe. We believe merger synergies, the restructuring of WestRock's underperforming U.S. business, and volume recovery following unprecedented 2022-23 industry destocking will underpin a multi-year growth inflection with simultaneous debt reduction. We expect normalized free

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cash flow generation at more than \$2.5B per annum starting in 2025 to support progressive dividend growth at a double-digit compound annual growth rate and a sizeable buyback program as debt is reduced.

Diversified financial services company Charles Schwab Corporation was eliminated from the portfolio in November. Cash sorting headwinds continue to weigh on Schwab's financial results and balance sheet as management focuses on paying down high-cost, short-term borrowings. We believe the uncertain interest rate outlook and the recent CEO and CFO changes will result in investor uncertainty and weigh on the stock in the coming quarters. Given our belief that these headwinds may hinder the company's near-term dividend growth potential, we decided to eliminate the position in favor of other investment opportunities with more attractive risk/reward potential.

### Outlook

Heading into 2025, U.S. GDP growth is set to slow but still hover above pre-Covid levels, driven by rising income and strong consumer spending. However, the U.S. economy could face potential headwinds from President-elect Trump's sweeping tariff proposals on exports from U.S. trading partners, most notably China, Canada, Mexico, and the European Union. Also, an extension of the tax cuts from 2017, which expire at the end of 2025, could add significantly to the rising federal budget deficit. In addition, while the U.S. and global economies and markets remained resilient last year in the face of mounting geopolitical concerns and wars in Ukraine and the Middle East, these issues remain on our radar. That said, our current base case calls for modest U.S. economic growth with improved business confidence and deregulation.

Although we believe U.S. inflation could fall thanks to declining housing and core services costs, it's likely to remain above the Fed's 2% target this year. We expect the Fed to reduce rates twice more during this cycle, taking its policy rate range to 3.75%-4.00% by year-end 2025. The exact timing of these cuts will depend on incoming data and developments on the new administration's policies.

Following two straight years of +20% gains for the S&P 500, we are expecting more moderate returns in 2025, likely in the mid-to-high single digit range. This outlook is based on three factors: a 10-year Treasury yield that remains

rangebound, making equities relatively more attractive versus the risk-free return on government securities; solid earnings per share growth that is well above the long-term average of 7.2%; and continued easing by the Fed.

Although the CBOE Volatility Index (VIX), a measure of the implied volatility of the S&P 500, dipped in the weeks following the U.S. presidential election, it quickly reversed course after the Fed's December meeting. In our view, market volatility will remain high in 2025, with U.S. and global economies still in the process of recovering from high levels of inflation and historic rate hikes, and central banks engaged in a delicate balancing act of taming inflation and nurturing growth.

Given the uncertainty facing the economy and 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.

We find the strong dividend activity this past year to be an important positive signal from management teams regarding confidence in their business prospects despite persistent cost pressures and higher interest rates. According to S&P Dow Jones, over 320 companies in the S&P 500 increased or initiated a dividend during calendar year 2024. Of particular importance, several mega cap technology-oriented companies announced dividend payments for the first time which may pressure other current non-dividend paying companies to follow suit. The S&P 500's dividend payout ratio remains below its long-term average and consensus estimates point to 15% earnings per share growth in 2025, both of which should support attractive returns of capital to shareholders. According to FactSet estimates, the S&P 500 dividends per share grew by 7.6% in 2024 and are expected to advance by 4.2% in 2025.



**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

**Beta** is a measure of the volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole. **Earnings per share (EPS)** is the portion of a company's profit allocated to each share of common stock. Earnings per share serve as an indicator of a company's profitability. **Federal funds rate** is the interest rate which is charged by banks to lend to other banks needing overnight loans. The Federal Reserve Board sets the target for this rate which is the most sensitive indicator of the direction of short-term interest rates. **Free cash flow** is a measure of financial performance calculated as operating cash flow minus capital expenditures. It represents the cash that a company is able to generate after laying out the money required to maintain or expand its asset base. **Inflation** is a rise in the prices of goods and services, often equated with loss of purchasing power. **Payout ratio** is a financial metric showing the proportion of earnings a company pays shareholders in the form of dividends, expressed as a percentage of the company's total earnings. **Valuation** is the process of determining the current worth of an asset or a company; there are many techniques used to determine value. An analyst placing a value on a company looks at the company's management, the composition of its capital structure, the prospect of future earnings and market value of assets. **Volatility** is the fluctuations in market value of a portfolio or other securities. The greater a portfolio's volatility, the wider the fluctuations between its high and low prices. The **S&P 500®** measures the performance of large capitalization U.S. stocks. **It is not possible to invest directly in an index.** Clients should consult their financial professional regarding unknown financial terms and concepts.

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