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Viewpoints from the Global Investment Committee
MIDYEAR | 2022 OUTLOOK

From pain to gain

Portfolio perspectives for turbulent times

KEY TAKEAWAYS

1. **Our highest-conviction trade:** Municipal bonds have been unfairly beat up and offer compelling upside.

2. **Near-term risks favor battered public markets:** The dramatic corrections across public equities, credit and real estate relative to their private market equivalents could represent rebalancing and upside opportunities.

3. **Growth may slow, but credit sectors look solid:** We see compelling value in U.S. corporate high yield and loans, and expect a benign default environment.

Global Investment Committee members

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From pain to gain 1

Portfolio construction themes and our highest-conviction views 2

The economy and markets: key points to note 6

Our best investment ideas 8

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

From pain to gain

Portfolio perspectives for turbulent times

Saira Malik
Chief Investment Officer

As 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.

In our previous outlook, we encouraged investors to tune out "noise" and focus on "signal" — economic and asset class fundamentals evidenced in hard data. We continue to endorse this approach, but acknowledge that even the most diligent followers of such advice have ample reason to bid good riddance to the first half of 2022.

Crossing this midyear milestone may elicit a symbolic sigh of relief, but turning a calendar page doesn't alter market realities or address the matter of how best to position portfolios for the next six months and beyond. That's the critical task in an environment where the noise has only grown louder, certain signals look less favorable and financial markets have doubled down on volatility.

In fact, as we enter the second half of the year, most of the first half's significant headwinds are still in place: high levels of inflation, slowing growth, rising rates, Fed policy uncertainty and fallout from Russia's war on Ukraine.

Not all is bleak, however. As we explain in our review of the economy and markets, we see some potentially better news ahead, including more moderate inflation, the ongoing resilience of the consumer and a Fed that might lighten its tightening touch after completing its initial round of outsized rate hikes.

This mix of measured optimism and elevated risks was the backdrop when Nuveen's Global Investment Committee recently met to update our outlook and revisit best ideas for asset allocation and portfolio construction.

As a new step in this deliberative process, we asked our team of economic and investment specialists to think beyond the scope of their respective areas of expertise. The intentionality of this approach brought a truly cross-asset class perspective to the dialogue and debate, reflected in our asset class "heat map," highest-conviction views and areas of disagreement, detailed in the following section.

More broadly, GIC members agreed on several key portfolio construction themes over the next 6 to 12 months:

- **Fixed income credit sectors over equities.** This preference is based on their more favorable risk/reward profile.
- **Baby steps back to duration.** With recession odds on the rise and bond markets already pricing in most of the pain expected from Fed rate hikes, it's time to consider neutralizing duration underweights.
- **Real assets vis-à-vis inflation.** Infrastructure, farmland and commercial real estate may offer ways to combat high inflation — or benefit from it.
- **Publics poised to lead.** While there's no denying the importance and value of maintaining a strategic allocation to private assets, beaten-down public markets currently offer extremely compelling upside potential in the near term.

Lastly, though we are long-term investors, we recognize that transitioning "from pain to gain" requires more than simply being patient, as if time could heal all investment wounds. Patience may be a virtue, but it's not its own reward. That's why our portfolio construction themes center on the search for value in specific asset classes where we expect our clients to be adequately compensated for the risks taken. This is the essence of Nuveen's overall approach to pursuing successful outcomes in turbulent times — and all the time.

Portfolio construction themes

There were few places to hide during the first half of 2022. *But in the wake of the repricing of many public asset classes, we see opportunities to shift "from pain to gain" as we enter the second half. Our portfolio construction themes focus on ways to combat inflation and on areas of the market that have stabilized given the scope of central bank action that has already been priced in — with a particular emphasis on fixed income.*

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Fixed income looks more interesting than equities.

Asset class “heat map”

We’re pleased to offer our inaugural set of cross-asset class views indicating where we see the best relative opportunities within global financial markets. These are not intended to represent a specific portfolio, but rather to answer the question: “What are our highest-conviction views when it comes to putting new money to work?” These views represent a one-year time horizon and assume a U.S. dollar-based investor seeking long-term growth.

	Less Positive		Neutral		More Positive
Equities			●		
U.S. equities			●		
Non-U.S. equities	●				
Emerging markets equities		●			
Private equity			●		
Real assets				●	
Listed REITs			●		
Listed infrastructure				●	
Private real estate		●			
Private infrastructure				●	
Commodities			●		
Fixed income				●	
U.S. Treasuries (10 yr)	●				
Investment grade			●		
Municipals					●
High yield					●
Emerging markets debt	●				
Senior loans				●	
Real estate debt				●	
Private credit				●	

Downgrade from last quarter

Upgrade from last quarter

The views above are for informational purposes only and convey the relative merits of each asset class based on the collective assessment of Nuveen’s Global Investment Committee. They do not reflect the experience or performance of any Nuveen product, strategy or service. Upgrades and downgrades reflect quarterly shifts in these views.

Portfolio themes

- **Liquid credit over equities:** Entering bear market territory for stocks conjures the question of whether the drawdown has created true value, or simply a value trap. The S&P 500 Index currently trades at a forward P/E ratio of 15.7x, about 8% below the 10-year average of 17.1x. But this multiple doesn't reflect any negative earnings revisions that may come in the back half of the year. In light of this, we prefer to access risk-on exposure through public fixed income credit sectors, which we think offer more compelling near-term return prospects per unit of potential downside risk (see Figure 1).
- **Cautiously add back duration:** We firmly believe that investors who have shortened duration should consider inching their portfolios back to neutral over the next quarter, particularly as recession risk increases. Our assessment is that bond markets have largely priced in the expected trajectory of Fed interest rate increases. And while investors could still feel a sting — notably after factoring in inflation — much of the pain appears to be behind us.
- **Real assets remain compelling:** Many real assets can help mitigate inflation, and in some cases are still poised to produce positive real returns. From rent escalators found in commercial real estate to CPI-based infrastructure projects to farmland assets bolstered by rising crop and land values, we see a number of ways to participate in elevated inflation levels or provide a cushion against them.
- **Public assets paving the way:** Broadly speaking, private assets have yet to endure the sentiment-driven valuation adjustments that public markets have suffered this year, which leads to favorable near-term risk/reward profiles in these markets. For example, public REITs (the FTSE NAREIT Index) are in bear market territory. In contrast, directly owned core real estate (the NCREIF-ODCE Index) posted a 1% gain in the first quarter, the last reported. Private markets remain a key tool to deliver attractive risk-adjusted returns through an economic cycle. Moreover, their experience in 2022 highlights one of the many benefits of private market investing: a shield from day-to-day volatility. That said, it's difficult to ignore the upside opportunity presented by public markets after they experienced such a severe pullback.

Our highest-conviction views

- **Municipal bonds:** Across the GIC, we came to the consensus that municipal bonds offer value. Fundamentals remain solid, as tax revenues have continued to tick up and the ratio of rating upgrades to downgrades has increased. Our view is that the asset class has been unjustifiably punished this year by outflows, creating opportunities for long-term oriented, tax-exempt investors.
- **U.S. high yield:** GIC members agree that corporate high yield looks particularly attractive, with nominal yields north of 7% even on BB rated bonds. Importantly, if the U.S. were to enter a mild recession, we believe spread levels are compensating investors for the probability of higher defaults.
- **Infrastructure:** Inflation has not peaked, and it likely won't for another few months. And even after it peaks, it will remain elevated. It is not too late to add inflation hedges. But while equities are typically the best weapon to combat inflation over the longer run, for the near term we especially like infrastructure. It offers defensive equity properties that should benefit in a continued high-volatility environment. In addition, it has historically proven resilient during inflationary periods given its cash flow-heavy, regulated nature. Plus, CPI escalators are built into many contracts, and the replacement value of the operating assets will adjust due to higher costs of commodities and services.

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Municipal bonds and high yield look particularly attractive.

And where we have disagreement

- **Real estate:** Our most intense debate was over private real estate. The committee focused primarily on two things: strong fundamentals in the areas that our real estate team like — health care, industrials and multi-family housing — and the likelihood that the repricing in public real estate might be the canary in the coal mine for private real estate.
- **Commodities:** GIC members have disparate views toward commodities. Some of us see opportunities from an inflation protection perspective, while others are wary of lofty prices. We wound up offering a neutral positioning, but in all honesty this reflects a lack of consensus more than a conviction.
- **Emerging markets equities:** Yes, you'll see the heat map reflect a less positive view of EM stocks, but the committee distilled the view as a call on China, an unpredictable key driver of the overall asset class.

Figure 1: Compelling opportunities in fixed income credit sectors

As of 31 Dec 2021

	U.S. agg bond	IG corp	Preferreds	EMD ($)	BB HY	HY corp	Senior loans	Middle mkt loans	A muni	BBB muni	HY muni	Real estate
Yield to worst / cap rate	1.75	2.52	3.15	4.31	3.30	4.22	5.26	6.42	1.61	1.93	3.11	4.83
Spreads*	0.36	1.00	1.61	3.20	1.94	2.84	4.39	6.27	0.31	0.63	1.76	3.20
5-year Z-score	-0.70	-0.79	0.04	0.11	-0.77	-0.98	-0.36	-0.28	-1.39	-0.97	-1.08	-0.21

As of 21 Jun 2022

	U.S. agg bond	IG corp	Preferreds	EMD ($)	BB HY	HY corp	Senior loans	Middle mkt loans	A muni	BBB muni	HY muni	Real estate
Yield to worst / cap rate	3.98	5.00	5.68	7.10	7.00	8.51	8.54	8.17	3.24	3.58	4.88	5.03
Spreads*	0.54	1.56	2.43	3.73	3.45	4.96	5.63	6.77	0.56	0.90	2.14	3.55
5-year Z-score	0.81	1.05	0.91	0.65	1.00	0.95	0.76	0.05	2.01	0.19	-0.32	-0.27

Spreads tighter than historical average — Spreads wider than historical average

Data source: Bloomberg, L.P. and Thomson Reuters MMD as of 21 June 2022. Senior loans, middle market loans and municipals data as of 31 May 2022. **Yield to worst** is the lowest potential yield that can be received on a bond without the issuer actually defaulting. *Municipal spreads are versus equivalent AAA municipal yields, senior loans are versus the three-year life discount margin, all others are option-adjusted spreads versus Treasuries. **Z-score** is the number of standard deviations between the current spread level and the average spread. **Past performance does not predict or guarantee future results. Representative indexes and yield calculations: U.S. aggregate bonds:** Bloomberg U.S. Aggregate Bond Index; **investment grade corporate:** Bloomberg USD Liquid Investment Grade Corp Total Return Index; **preferreds:** ICE BofA Fixed Rate Preferred Securities Index; **emerging markets debt:** Bloomberg Emerging Markets Hard Currency Aggregate Index; **high yield:** Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index; **senior loans:** Credit Suisse Leveraged Loan Index; **middle market loans:** S&P/LSTA Middle Market Index; **municipal bonds:** Thomson Reuters MMD Scale (A and BBB Municipal); **high yield municipals:** Bloomberg Barclays High Yield Municipal Index; **real estate:** Green Street Advisors, Nominal Cap Rate of Major Sectors (Real estate).

> **Our biggest area of disagreement? Valuing private real estate.**

The economy and markets

Brian Nick
Chief Investment Strategist

Key points to note

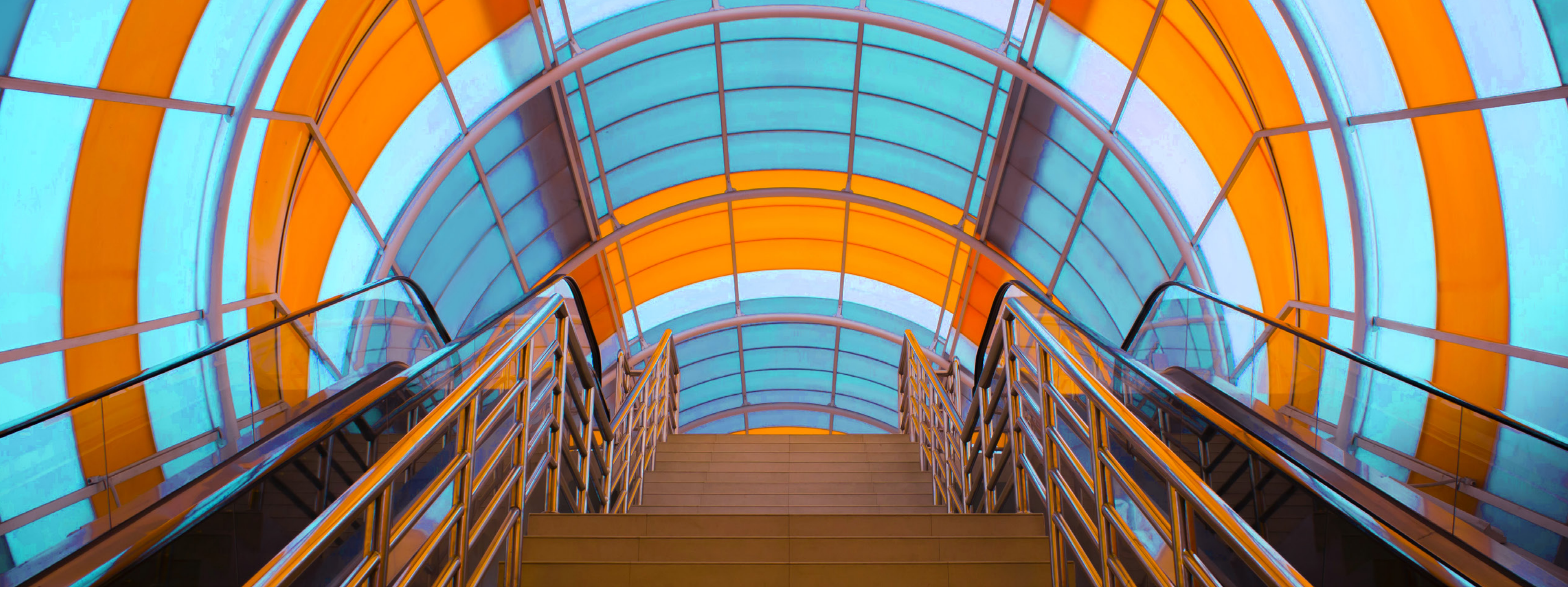
Expect normalization, not severe recession

Investors may be tempted to stock up on cushions as the debate heats up over whether the global economy will experience a hard or soft landing. But the data so far barely show a loss in altitude, let alone a sharp descent. Economic patterns have been abnormal for the past two years, but are slowly reverting to pre-pandemic form. Different countries and sectors are normalizing at different rates, creating market turbulence and exposing economic forecasts to ridicule. We expect a significant moderation in inflation over the next 18 months, as financial conditions tighten and economic growth slows in the world's largest economies. But a mild recession is certainly not out of the question.

Job security is the new consumer confidence

Consumer spending is keeping the developed world growing, with many countries still benefiting from pandemic-era pent-up demand and excess savings. Jobs have returned quickly and wages are rising about as fast as prices. Yet consumers have almost never reported feeling so down in the dumps. Sentiment surveys are registering lower readings today than even in the midst of the 2008 financial crisis. But while consumers aren't talking the talk, they are walking the walk: growing their spending well in excess of inflation (Figure 2). Rising net worth and job security are far more important predictors of consumer behavior than comments people are willing to share with survey takers.

> **Inflation is likely to moderate over the next 18 months.**



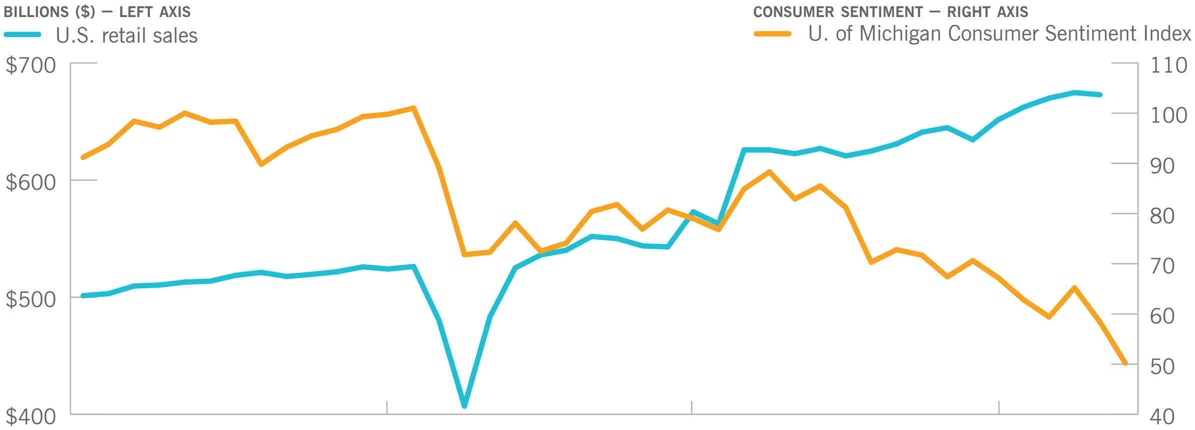
The food and energy "tax" is worse for lower-income consumers

Geopolitical strife has contributed to persistent increases in energy and food costs. This affects every consumer at some level, but higher-income households and wealthier countries are relatively insulated from the direst consequences. Some emerging markets may soon be susceptible to acute food shortages and even social unrest unless supplies replenish and price increases relent. But even countries like the U.S. will have a narrower base of consumption growth this year as fewer households meaningfully increase their real spending.

It's still all about central banks

Every economic data point is being refracted through the prism of how central banks will respond. This puts the labor market – a leading inflation indicator because wages play a big role in determining prices – at the center of our attention for the balance of 2022. News of job or pay freezes sounds bad, but they are necessary to slow the rapid pace of aggregate demand growth, rebalance the economy and allow policymakers to take their feet off the brakes. While a lot more central bank rate hikes lie ahead, a modest softening in employment data can help ensure they don't smother the young expansion.

Figure 2: Spending levels remain high despite sour sentiment



Source: Bloomberg, L.P., U.S. Commerce Department (retail sales) and University of Michigan Consumer Sentiment Index, 31 Jan 2019 to 31 May 2022.

GIC Asset class outlooks

EQUITIES

Saira Malik

Investment positioning

- We are neutral toward equities. Given the number of risks (rising interest rates, tightening monetary policy, slowing economic growth and ongoing geopolitical woes), we don't yet see an "all clear" sign.
- We're not neutral on everything, however. We prefer U.S. equities over non-U.S. developed and emerging markets, given the more defensive nature and better growth potential of U.S. stocks. For investors with greater near-term risk tolerance, we'd also put in a plug for Latin American equities, which offer solid relative value and good growth prospects.
- We're also focused on dividend growers. This area of the market should be relatively shielded from volatility and could see relative benefits from a rising-rates environment. From a style perspective, we see opportunities across both growth and value, depending on where we're finding the best risk/reward tradeoffs. And our favorite sector is energy, which should get a boost from rising demand and supply limitations.
- Private equity deal flow is slower than last year, but we continue to see pockets of opportunity, particularly in more defensive areas like health care.

BEST IDEAS: *1) U.S. large cap stocks, particularly growth companies that can expand operating profits and benefit from strong cash flows, and 2) energy companies able to capitalize on supply/demand dynamics.*

FIXED INCOME

Anders Persson

Investment positioning

- Taxable fixed income markets have been beaten up badly in the first half of the year. But we think most of the bad news has been priced in. Bond markets are forecasting an economic slowdown and possibly even a mild recession. If economic and inflation conditions don't materially worsen, that should be good enough for bonds. We don't need to see new catalysts; simply seeing some stability from here should be good enough for fixed income.
- We advocate a shorter duration stance, but are moderating that position as yields continue to climb. Overall, we think credit risk looks like a better bet. Credit fundamentals are solid (especially in high yield), and we don't expect to see a significant spike in defaults, even in a recession.
- This is particularly the case for high yield. With yields averaging more than 8%, the sector is actually offering a high yield. And spreads have widened to the point that high yield is providing a potential "cushion." Credit fundamentals look strong enough to survive an economic slowdown. Until/unless that happens, investors can benefit from clipping the current coupons.
- Private credit markets may come under pressure, as they haven't yet reacted to slower growth and higher inflation. But we see opportunities in areas with strong covenants and controls, such as middle market loans.

BEST IDEAS: *In the short term, we see value in leveraged loans, given solid fundamentals and aggressive rate hikes. Over the longer term, high yield offers impressive yield and strong credit fundamentals. We think both areas should withstand a growth slowdown and even a mild recession.*

MUNICIPALS

John Miller

Investment positioning

- Municipal bonds were unfairly punished in the first half of the year. The selloff resulted from broad macro issues (chiefly rising rates) rather than fundamental factors, which remain strong. State and local tax revenues look healthy, reserve funds and pension balances are solid and most sectors are seeing positive ratings upgrades.
- Both investment grade and high yield municipal bonds offer compelling value. If interest rates stabilize, we believe municipals could be poised for a jump in the second half of 2022.
- We think it makes sense to take on both duration and credit risk to seek out compelling yields and total return. The municipal yield curve is steeper than the Treasury

curve, and lower-rated credits present opportunities due to fundamentals and discounted prices.

- In general, we prefer bonds backed by property taxes and see value in the energy and electricity generation sectors.

BEST IDEAS: *From a national perspective, we see the best value in long duration, low coupon, high quality bonds in California and New York. We are also focused on project-specific high yield bonds in the transportation and retail sectors.*

REAL ESTATE

Carly Tripp

Investment positioning

- The case for private real estate hasn't changed, but we acknowledge near-term risks are growing. Real estate has had a phenomenal run the last few years, and has only priced in the effects of higher inflation and monetary policy tightening to a limited extent.
- Our key investment theme today is that we suggest overweighting new dollars to real estate debt over equity. With rates and spreads climbing, the return outlook remains strong, and we think debt markets may outperform real estate equity in the near term.
- From a sector perspective, we like for-rent housing, as the cost to own has increased drastically this year. We emphasize affordable housing throughout the U.S. Health care-related real estate also looks compelling, given its essential-service nature and because it represents a growing proportion of global economic output.
- Our theme of focusing on "global cities" remains intact, as we think select cities are demographically and structurally more attractive. For example, while the office space outlook is uncertain, office buildings in Miami's city center are attracting historically high rents despite market volatility.

BEST IDEAS: *We are focused on defensive areas of the market backed by strong structural trends, such as rental housing and senior living in the U.S., student housing in Europe and Australia and discount outlet malls in China.*

REAL ASSETS

Justin Ourso

Jay Rosenberg

Investment positioning

- We prefer more defensive positioning across real assets. Slowing global economic growth and worsening sentiment could represent headwinds for more cyclical areas. Additionally, we believe that the lagged effects of higher inflation and interest rate increases have not yet been fully priced into private markets.
- We are neutral toward public real estate, but price declines have created pockets of opportunity. Industrial real estate exhibits attractive fundamentals, and we think the downturn there has been overdone. We also like senior living, since this sector's recovery has lagged and it should benefit from long-term demographic trends.
- Public infrastructure offers broader opportunities. Regulated utilities in the U.S. should hold up well in an environment of slowing economic growth. And waste-related infrastructure has the pricing power to pass along increased inflation-related costs to customers.
- We have a more cautious view toward private real assets, in particular infrastructure, based on public markets repricing ahead of private revaluations. However, sound investment opportunities remain, especially those that can pass through price increases. Examples include farmland and agribusinesses benefiting from rising food prices, timber investments capitalizing on growing demand for housing, and infrastructure investments with pricing power.
- Renewable energy and energy transition investments within private real assets should continue to see short- and long-term tailwinds. In the short term, we prefer solar and offshore wind generation globally. We also see opportunity in low carbon transportation fuels, particularly renewable diesel in the form of oilseed markets.

BEST IDEAS: *In public real estate, we are positive on residential, senior housing and industrial real estate, while in public infrastructure we like waste and energy-related infrastructure. Across private real assets, we favor investments that align with climate transition, such as carbon sequestration, clean energy, renewable fuel sources and continued strong global demand for healthy foods.*

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. Quarterly 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.

Sources

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

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