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Viewpoints from the Global Investment Committee
2Q | 2022 OUTLOOK

Cut through the static

Separating noise from signal for better investment outcomes

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It feels like the number of "unknowns" is rising for investors, which is creating a lot of noise in the markets. But there are things we know, and focusing on these certainties should help investors create better outcomes.

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OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

Cut through the static

Separating noise from signal for better investment outcomes

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.

Our initial 2022 outlook themes generally played out as expected in the first quarter: strong but slower economic growth, persistently hotter inflation, the onset of interest rate hikes and further bouts of elevated market volatility.

But two developments were unexpected: The geopolitical and humanitarian crisis unleashed by Russia's invasion of Ukraine and a worsening disconnect between hard economic data and investor sentiment. Despite positive signals — powerful job creation, a steady drop in the unemployment rate and consumer resilience, to name a few — markets often behaved as if the only messages getting through were fragmentary sound bites on a doom and gloom wavelength.

To be sure, an inverted yield curve and an oil price spike can create meaningful implications for the economy, but neither means a recession *must* follow. Likewise, the combination of higher inflation and modestly decelerating growth that has characterized the past several months does not herald a return to 1970s stagflation. Lack of nuance in coverage of hot topics like these creates static that can interfere with calm, fact-based decision-making. Cutting through the noise is essential, especially during times of heightened turmoil.

That's not to say genuine risks should be ignored. In fact, discussing and debating the toughest challenges — and the investment opportunities they create — is exactly what Nuveen's Global Investment Committee has done in developing our outlook.

Our dialogue was spirited and far-reaching, as one would expect for a diverse group of economic and asset class specialists with strong convictions. Ultimately we coalesced around three portfolio construction themes built on familiar but evolving market drivers:

- **The Fed:** Certainty replaced "will they or won't they?" speculation in March as the Fed initiated its long-awaited rate liftoff. While a headwind for duration-sensitive assets, rate hikes make credit more attractive on a relative basis. Some equity categories may benefit as well.
- **Market volatility:** Risk-on investors with the fortitude to weather wide price swings might find compelling entry points in beaten-up asset classes like emerging markets debt. For those with a lower risk tolerance, less-volatile private assets may provide refuge.
- **Inflation:** While we expect inflation to remain somewhat elevated, we don't predict an out-of-control inflationary spiral. Allocations to select real assets and other traditional inflation hedges will likely serve portfolios well.

We explore our asset allocation ideas in greater detail in the outlook that follows. On balance, we're confident investors can achieve positive results by isolating the clearest, strongest signals and tuning out the noise. We invite you to read on to learn more.

Portfolio construction themes

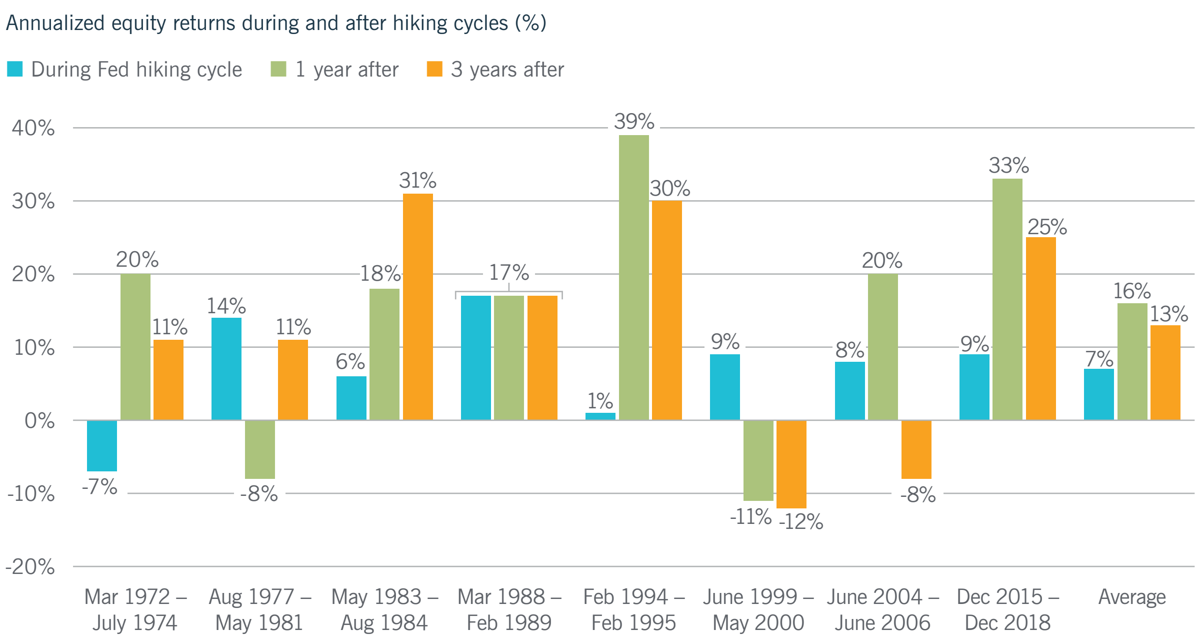
Three things we know

A volatile start to the year underscored the adage that "markets do not like uncertainty." We are not going to pretend that making portfolio construction decisions is easy right now. Because of this, we anchor our views on the premise that taking a longer-term view has proven to provide the right perspective. And we suggest investors focus on the knowns, rather than the many unknowns.

1 The Fed has embarked on a tightening cycle

- **Rate-sensitive asset classes remain vulnerable:** Our Global Investment Committee members agreed that asset classes with duration risk should continue feeling pressure. As such, we advocate an underweight duration posture to mitigate negative capital appreciation as yields rise. Instead, we continue to favor credit risk, specifically broadly syndicated loans and high yield, where yields are attractive, fundamentals are sound and we expect default rates to remain very low. This view will evolve as rates increase, but for now we don't think it makes sense to add duration risk.
- **Equities have historically performed well through tightening cycles** (even when the yield curve inverts), albeit not without volatility (Figure 1). At our recent GIC discussion, we spent quite a bit of time debating the question, "If an investor has cash available to put to work, where do we see the best opportunities?" We were unanimous that **U.S. large cap equities look attractive,** especially after their recent selloff. As a group, we were divided on the growth vs. value debate, which leads us to suggest a balanced approach (select growth names are looking inexpensive compared to our long-term profit forecasts; sectors more heavily weighted in the value complex may do well in an environment of higher inflation). The U.S. is still trading at a premium compared to international equities, offering investors a relative safe haven from geopolitical and economic disruption.

Figure 1: Equities have actually done quite well when policy tightens



Data source: Bloomberg, L.P. **Past performance is no guarantee of future results.** Equity returns reflect the S&P 500 Index during the most recent Fed rate-hiking cycles.

> **There are many unknowns. Let's focus on the knowns.**

2 Market volatility will continue to be friend and foe

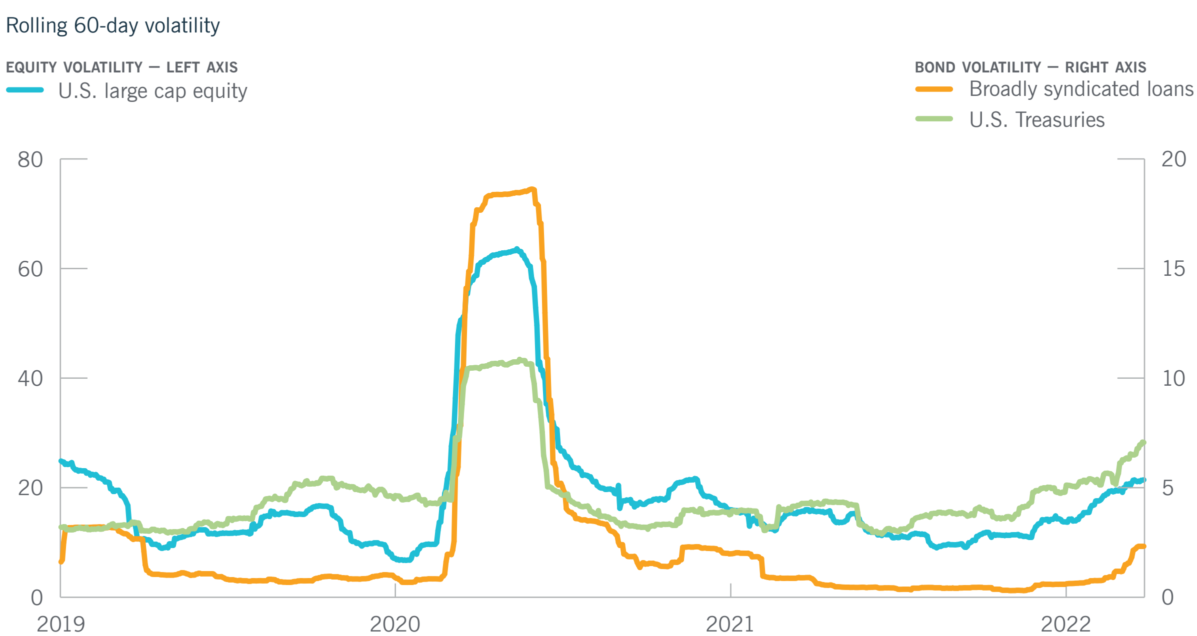
- **Markets are typically skittish later in an economic cycle, but geopolitical risk magnifies this.** All of our GIC members expect volatility to remain elevated — especially in public markets. Volatility reflects concerns of a precarious backdrop of low starting yields and high inflation — questioning whether the economy can handle the Fed's next move. And it's not surprising that market volatility has been particularly acute in Treasuries — even more so than in stocks and broadly syndicated loans (Figure 2).

We see two ways to approach this volatility:

- **Participate in it:** Hold tight to strategic asset allocations (rebalancing prudently), while using extra or new cash to take advantage of the incredible pullbacks we've witnessed year-to-date. For example, we see **contrarian opportunities in distressed and undervalued areas such as emerging markets debt,** but would stop short of adding to areas that still present too much risk due to ongoing turmoil caused by the Russian invasion. These latter areas include European equities, European infrastructure and emerging markets equities.

- **Shield portfolios:** Investors seeking safe harbor from market volatility should consider incorporating (or increasing) less liquid investments into their portfolios. In our experience, investors tend to overestimate the amount of portfolio liquidity they need, potentially sacrificing better risk-adjusted returns by underinvesting in private assets. **Private assets** may add to diversification through illiquidity premiums and idiosyncratic risks. For those investors looking to increase portfolio yield, **private credit (specifically, middle market direct lending)** offers healthy levels of income with low volatility as the demand for **private equity** deal financing shows no signs of slowing. In fact, committed-but-unallocated global private equity capital stood near all-time highs at $1.78 trillion in February as institutional investors continue to embrace the asset class as a potential antidote for lower long-term return expectations.

Figure 2: Rising volatility creates risks — and opportunities



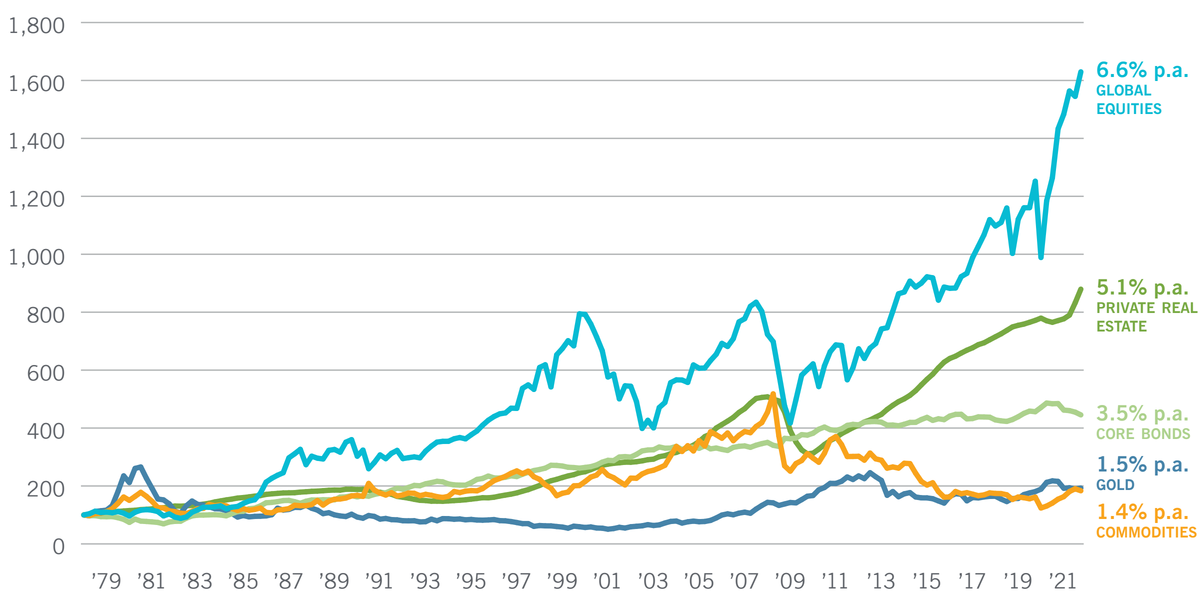
Data source: Bloomberg, L.P., 02 Jan 2018 – 28 Mar 2022. Volatility is measured by the standard deviation of rolling 60-day periods on an annualized basis. **Past performance is no guarantee of future results. Representative indexes: U.S. large cap equities:** S&P 500 Index; **U.S. Treasuries:** Bloomberg U.S. Treasury Total Return Unhedged Index; **broadly syndicated loans:** Credit Suisse Leveraged Loan Total Return Index.

3 Inflation has taken hold

- We believe the economic expansion will continue contributing to **above average inflation,** but demand will soften, supply shocks will dissipate and inflation will eventually moderate. This stands in contrast to a worst-case scenario of persistently higher inflation and a Fed unable to tame it, sending the economy into a tailspin.
- We favor **long-term inflation protection in the form of productive, cash-flow-generating assets, such as equities, real estate and real assets** (Figure 3). While broad global equities have an outstanding track record of growing real, after-inflation wealth, the profit outlook for certain sectors and regions has improved dramatically against the backdrop of elevated commodity prices and more persistent inflation. In addition, real estate can offer capital appreciation and income despite higher inflation; many leases have built-in rent escalators that protect real income generation. Higher nominal wages can lead to bigger budgets for housing, which has been in short supply since the Global Financial Crisis, a trend exacerbated by COVID-induced migration and higher costs of materials slowing the pace of new inventory.

Figure 3: Focus on long-term inflation hedges

Inflation-adjusted returns ($100 initial investment) and per-annum return rates



Data source: Bloomberg, L.P., 01 Jan 1978 – 31 Dec 2021. Inflation reflects quarterly readings of U.S. CPI. **Past performance is no guarantee of future results. Representative indexes: Global equities:** MSCI World Index; **Commodities:** Bloomberg Commodities Total Return Index; **Core bonds:** Bloomberg U.S. Aggregate Total Return Index; **Gold:** Bloomberg Gold Subindex; **Private real estate:** NCREIF Fund Index Open End Diversified Core Index.

> **We don't expect a worst-case scenario for inflation.**

The economy and markets

Brian Nick
Chief Investment Strategist

Key points to note

Monetary policy: carefully calibrated, data dependent

We think trying to forecast what central banks will do is the wrong approach. They are data dependent, and will use their policy tools — and their rhetorical powers — to calibrate an appropriate path for rates as the data come in. Investors should be prepared for a variety of outcomes. Hopefully central bankers are ready, as well.

Recession: not this year, but market risks remain elevated

Risks of a premature end to this young cycle have admittedly increased, given the steep path of interest rate increases we're already seeing. But absent a major policy error or additional exogenous shock, we do not see growth turning negative in 2022. This leads us to see potential for the S&P 500 to hit a new all-time high before the year is out thanks to solid earnings growth. Note, however, that while most asset classes are currently trading at their most attractive valuations in several years, low interest rates and high price-to-earnings ratios still do not compare favorably to the prior decade (Figure 4). This means return expectations should be somewhat subdued when compared to the 2010s.

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Absent a major policy error or additional exogenous shock, we do not see growth turning negative in 2022.

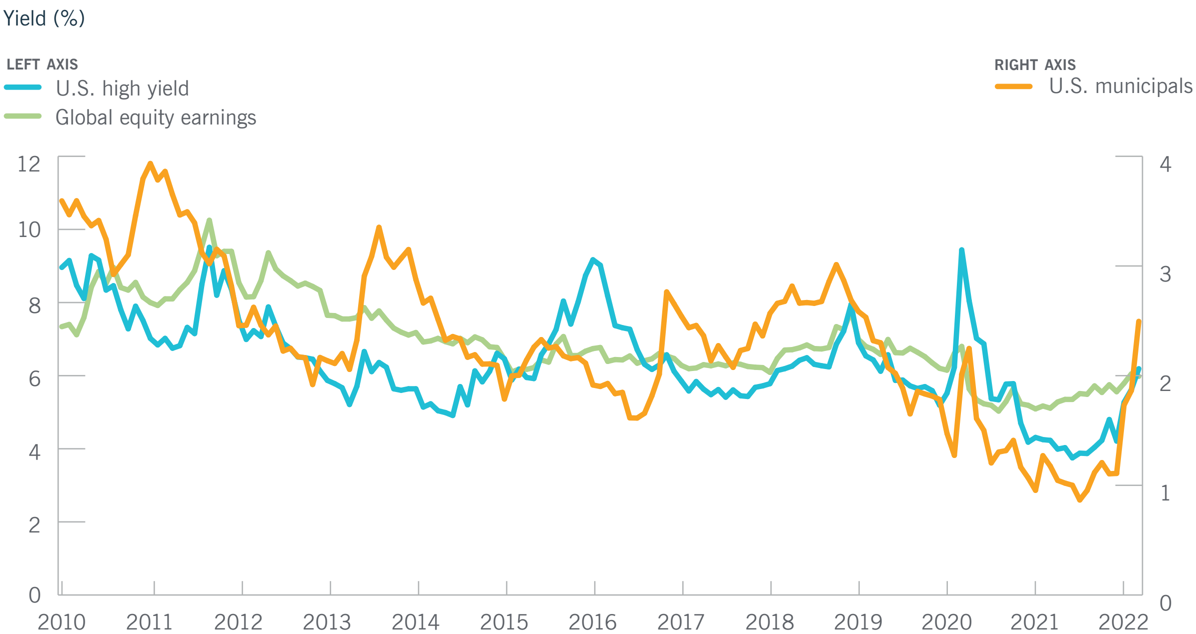
Inflation: high but peaking

Just what the global economy didn't need: An energy price shock to give another boost to already white-hot inflation across developed and emerging markets. But March likely marked the peak for both headline and core inflation in most major economies, with many goods prices likely to fall outright and wage pressures showing signs of easing. Disinflation would be welcomed by policymakers and investors alike.

Long-term interest rates: a slower climb from here

Falling inflation would seem to go hand in hand with falling interest rates, but we expect 10-year government bond yields to rise further from here. While rates are already up considerably — and by much more than we expected — this is mainly due to higher inflation expectations. We expect real rates to rise as policy turns more hawkish and inflation moderates, producing slightly higher nominal yields by the end of the year.

Figure 4: Rates and risk premiums have risen together, presenting a rare opportunity



Source: Bloomberg, L.P., 01 Jan 2010 – 31 Mar 2022. **Past performance is no guarantee of future results. Representative indexes: U.S. high yield:** Bloomberg U.S. Corporate Total High Yield Index; **global equities:** MSCI All-Country World Index; **U.S. municipals:** Bloomberg Total Return Municipal Bond Index.

GIC

Asset class outlooks

EQUITIES

Saira Malik

Investment positioning

- Our outlook for global equities remains moderately bullish. With economic data painting a generally favorable backdrop, valuations have improved since the beginning of the year, and corporate earnings, while decelerating, are still strong. We expect equity returns to be positive for all of 2022, but volatility will likely stay elevated, making stock selection increasingly important.
- Regarding the style debate, we see opportunities in both value and growth. Growth stocks are looking more attractive and are well positioned as economies slow. And value could benefit from still-high inflation. Geographically, emerging markets offer a better opportunity than non-U.S. developed markets thanks to better valuations and the balance of geopolitical risks. We think China, Brazil and, to a lesser extent, Indonesia are worth exploring.
- From a sector perspective, energy continues to top our list (despite already outsized gains this year and ongoing turbulence in the oil and gas markets), as demand remains healthy and supply is still constrained. We also favor the technology sector, especially in the U.S., which has become more attractively valued and offers some defensive characteristics.

BEST IDEAS: *In addition to positive supply/demand dynamics, energy companies should benefit from capital spending discipline and a focus on returning cash to shareholders. Select emerging markets stocks, especially in regions with a strong or improving consumer base, also warrant a closer look.*

FIXED INCOME

Anders Persson

Investment positioning

- We strongly favor taking credit risk and minimizing duration risk given our forecast for peaking, but higher-than-average inflation over the near-to-intermediate term, continued strong credit fundamentals and attractive valuations as a result of recent volatility.
- We see the best relative value opportunities in higher-quality below-investment-grade areas of the global fixed income markets. Yields have improved significantly and fundamentals remain sound. Specifically, we like broadly syndicated loans, BB-rated U.S. high yield corporates and preferred securities.
- Emerging markets debt has experienced significant volatility and has come under extreme pressure due to the invasion of Ukraine, subsequent sanctions of Russia and contagion effect across markets. However, there are compelling opportunities in areas such as sovereign bonds in the Middle East and Latin America, and also certain corporate industries such as pulp and paper and metals and mining.

BEST IDEAS: *We favor broadly syndicated loans, shorter-duration high yield bonds in the BB credit range and preferred securities.*

MUNICIPALS

John Miller

Investment positioning

- This has been the most challenging first quarter of the year for municipal markets since 1994. The asset class has been experiencing outflows and has cheapened significantly relative to Treasuries as rising rates (more specifically, expectations for rising fed funds rates) have hurt the market. Critically, though, the municipal selloff is not related to credit issues. Supply and demand factors remain a tailwind, defaults continue to be rare and we've seen numerous high-profile upgrades in credit quality.

- This is presenting opportunities. In particular, we think it makes sense to become more aggressive by taking on credit risk in select lower-quality areas. Distressed sectors of the market and turnaround credit stories, such as bonds from Chicago, Detroit and Puerto Rico, look compelling and offer attractive yields.
- More broadly, we have a favorable view of bonds backed by property taxes, and we see value in the energy and electric generation sectors.

BEST IDEAS: *We particularly favor shorter duration high yield municipals, which are experiencing improving credit quality and have been relatively insulated from interest rate volatility. We also like bonds tied to taxes on residential real estate and those focused on electricity generation.*

REAL ESTATE

Carly Tripp

Investment positioning

- Private real estate investments have been relatively insulated from recent market volatility, and we believe continuing global economic reopening and strong capital flows should provide ongoing tailwinds.
- From a contrarian perspective, we see idiosyncratic opportunities in distressed retail real estate, especially in the U.S. but also in Europe. New store openings, increased foot traffic, good leasing activity and compelling prices are all causing us to take a close look.
- We continue to see value in alternative real estate sectors, including senior living housing, medical offices and industrial properties.
- We're also continuing to work with the properties we own to drive renewable energy and sustainability to help enhance value.

BEST IDEAS: *From a geographic perspective, we favor single-family rentals and highly specialized medical offices in the U.S., suburban housing and data centers in Europe and senior living and industrial properties in Asia.*

REAL ASSETS

Justin Ourso **Jay Rosenberg**

Investment positioning

- We continue to see good opportunities in publicly traded real estate, especially in U.S. retail REITs that are benefiting from good leasing activity and appear attractively valued. Across real estate, we prefer companies with shorter lease durations and those with improving cash flow prospects, as these areas should be better insulated from rising rates.
- In public infrastructure, we favor regulated utilities and energy infrastructure, including pipelines and renewable energy experiencing a tailwind from higher energy prices. In addition, U.S. waste-related infrastructure is appealing. This sector has the pricing power to pass along increased costs to customers and can do well when inflation is rising.
- Private real assets including infrastructure, agriculture and timber should continue to benefit from high investor demand and relative insulation from inflation and economic cycles. We are focusing on assets and investments that have the ability to pass through price increases to mitigate inflation risks.
- For investment themes, we're focused on a renewable-energy and transportation-related infrastructure, agriculture investments benefiting from rising demand for timber and carbon sequestration, and sector-specific opportunities across infrastructure, agribusiness and farmland with the ability to mitigate and/or benefit from supply chain disruptions.

BEST IDEAS: *In public markets, we are focused on investments that should withstand or even benefit from higher inflation, such as shopping centers where landlords can withstand and pass along rent increases, waste companies and midstream energy. In addition, we see opportunities in transmission and renewable energy investments. Across private real assets, we favor investments that align with climate transition themes such as carbon sequestration in natural resources, 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.

Endnotes

Sources

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

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A word 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. Diversification is a technique to help reduce risk. There is no guarantee that diversification will protect against a loss of income. Investing in municipal bonds involves risks such as interest rate risk, credit risk and market risk, including the possible loss of principal. The value of the portfolio will fluctuate based on the value of the underlying securities. There are special risks associated with investments in high yield bonds, hedging activities and the potential use of leverage. Portfolios that include lower rated municipal bonds, commonly referred to as "high yield" or "junk" bonds, which are considered to be speculative, the credit and investment risk is heightened for the portfolio. Credit ratings are subject to change. AAA, AA, A, and BBB are investment grade ratings; BB, B, CCC/CC/C and D are below-investment grade ratings. As an asset class, real assets are less developed, more illiquid, and less transparent compared to traditional asset classes. Investments will be subject to risks generally associated with the ownership of real estate-related assets and foreign investing, including changes in economic conditions, currency values, environmental risks, the cost of and ability to obtain insurance, and risks related to leasing of properties. Socially Responsible Investments are subject to Social Criteria Risk, namely the risk that because social criteria exclude securities of certain issuers for non-financial reasons, investors may forgo some market opportunities available to those that don't use these criteria. Investors should be aware that alternative investments including private equity and private debt are speculative, subject to substantial risks including the risks associated with limited liquidity, the use of leverage, short sales and concentrated investments and may involve complex tax structures and investment strategies. Alternative investments may be illiquid, there may be no liquid secondary market or ready purchasers for such securities, they may not be required to provide periodic pricing or valuation information to investors, there may be delays in distributing tax information to investors, they are not subject to the same regulatory requirements as other types of pooled investment vehicles, and they may be subject to high fees and expenses, which will reduce profits. Alternative investments are not appropriate for all investors and should not constitute an entire investment program. Investors may lose all or substantially all of the capital invested. The historical returns achieved by alternative asset vehicles is not a prediction of future performance or a guarantee of future results, and there can be no assurance that comparable returns will be achieved by any strategy.

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