

22 November 2021

COVID-19, growth fears make markets defensive

Last week's equity market activity reflected rapidly growing concern over possible economic restrictions associated with the latest wave of COVID-19, as growth and defensive stocks outperformed. Among broad-based indexes, the tech-heavy NASDAQ added 1.3% and the S&P 500 gained 0.4%, while the more cyclically oriented DJIA fell -0.4%. Outside the U.S., the MSCI EAFE, EM and ACWI ex-USA indexes lost between -0.8% and -1.3%, with developed markets faring better than EM.

KEY POINTS

- **Last week's strong retail sales and industrial production data underscored strength in the robust economy, reinforcing consumer strength and possible easing of supply chains.**
- **We continue to side with the Fed as employment and economic data continue to look promising; however, the impending chairman nomination may briefly inject volatility into equity markets.**
- **Concern for long-term economic growth was elevated last week, causing U.S. Treasury yields to fall and value stocks to underperform; we expect economic growth to reaccelerate into 2022.**



Saira Malik, CFA

CIO of Nuveen Equities

Saira Malik oversees the equities strategic direction for Nuveen as chair of the Equities Investment Council (EIC) and a member of Nuveen's Global Investment Committee (GIC). She has responsibility for equity portfolio management, equity research, equity trading, target date, quantitative and index strategies, as well as portfolio management responsibilities for global equity strategies.

Market drivers & risks

- **Supply chains and earnings continue to go hand-in-hand**, as we see our thesis for margin control play out in real time.
 - We have consistently maintained that firms with pricing power to defend/grow margins and overcome inflation, as well as business models capable of weathering the supply chain storm, will be rewarded by investors. Last week several big retailers released 3Q results that showed they had intentionally compressed margins, choosing not to pass higher input costs on to customers in an effort to build brand loyalty ahead of what is expected to be a very robust holiday shopping season. We believe this plan may pay off as long as inventory builds are strong and further COVID-19-related restrictions can be avoided.
- **Economic data remains solid**, with last week's releases of October industrial production and retail sales both beating expectations.
 - The duration of the current cycle will be predicated largely on how long economic growth can outpace inflation. At the same time, however, the longer the economic data stays strong, the more wary of inflation the equity markets will become. If the perception of an overheating economy begins to dominate, the Fed may be forced to change its messaging on the pace and/or timing of policy tightening. That said, we're still optimistic that supply chain pressures will subside and economic growth will continue in 2022.
- **The recent pullback in oil prices is being driven by factors that are unlikely to last.**
 - The West Texas Intermediate crude benchmark has tumbled roughly 10% from October's highs, to \$76 per barrel at the end of last week. Much of this decline has been driven by the Biden administration's deployment of strategic reserves to battle rising prices, a course of action the Chinese government is expected to



The next few months could remain challenging, with continued high volatility and possible near-term market selloffs.”

take as well. While this incremental boost in supply will provide some near-term relief, we expect burgeoning demand in 2022 to surpass 2019's pre-pandemic levels as producers exhibit greater discipline when it comes to adding capacity. Though we don't expect oil prices to rise sustainably higher from October's peak, we believe current levels are artificially low.

Highlights from last week

- Results were driven by growing fears over the possible reinstatement of economic restrictions as growth and defensive stocks were the relative outperformers. From a sector perspective, technology (+2.4%) and utilities (+1.0%) were among the best performing sectors. Financials (-3.6%) and energy (-4.2%) fell the most on a pullback in rates and oil prices, respectively. Consumer discretionary was the biggest winner last week, adding nearly 4% thanks in part to strong earnings results from home improvement retailers.
- Globally, COVID-19 trends have taken a turn for the worse, with headlines shifting focus away from policy and inflation and toward lockdowns and mandated vaccinations. In the U.S., 30 states are now showing worsening trends in cases and hospitalizations, prompting growing concerns about another round of possible economic restrictions. Last week's worrisome developments came as the FDA authorized booster shots (Pfizer/BioNTech & Moderna) for all adults, and as anticipation grows for approval of effective oral treatments by year-end.

Risks to our outlook

COVID-19 cases and hospitalizations are on the rise in many countries. Although a renewed wave of infections has been anticipated, the fear of economic restrictions (as enacted last week in Austria) will certainly weigh on equity markets.

The Fed will be under intense scrutiny as it tiptoes toward contractionary policy. With markets so accustomed to quantitative easing and low rates, volatility is likely to rise as investors grow leery of a misstep in timing or magnitude.

Volatility may begin to spike in the coming weeks as the December 15 deadline for raising the U.S. debt ceiling may now coincide with finalizing a potential “soft” infrastructure spending package.

Though it appears U.S. corporate tax rate hikes may ultimately be avoided, markets still must assess the expected impacts of potential increases in other U.S. tax rates, including a minimum tax on U.S. companies’ foreign income.

In focus

Tailwinds for BEVs.

While battery electric vehicles (BEVs) are by no means new to the automotive lexicon, they remain a small percentage of cars on the road. Still, BEVs are well on their way to becoming mainstream, as global economies from the U.S. to the EU to China are committing to sustainability across the auto industry. In fact, virtually all major traditional car manufacturers have begun to pledge a transition from fossil fuel-powered vehicles to BEVs over the next two decades for significant portions of their fleets.

From a user perspective, BEVs offer several advantages, from better performance and internet connectivity to obvious environmental benefits. As a result, large volume buyers such as car rental and shipping/logistic companies are already shifting orders away from standard internal combustion engines (ICEs) to their BEV counterparts. Looking further out, the impact of these purchases will be felt across used car markets, ultimately reducing the value of pre-owned ICEs.

The near-term outlook for BEV-related equities may be hampered by extended valuations, as well as the rising rate environment. Longer-term, the prospects for BEV makers are bright, as the number of entrants to the market increases and the costs to consumers become more competitive with existing ICE price tags — something we expect to see over the next 3 to 5 years. Additionally, investors may look to benefit from exposure to BEV component manufacturers given that BEVs require twice as many of their inputs as do their ICE counterparts.



Best ideas

In the U.S., reflation and expectations for higher yields could bolster returns for small caps and financials, as well as companies with pricing power and reopening tailwinds. Supportive monetary policy and the prospect of stronger relative earnings growth could boost certain stocks in cyclically oriented sectors in developed non-U.S. markets, particularly in Europe and select emerging markets, ex-China. Select growth companies well positioned for reopening, such as front-office software leaders, also look attractive. Our long-term approach tilts toward cyclicals and value stocks that exhibit strong earnings growth and pricing power.

About the Equities Investment Council:

The Nuveen Equities Investment Council (EIC) includes the firm's senior equity portfolio managers, averaging three decades of investing experience. The EIC brings global expertise across different styles of equity investing and provides value-added insights to Nuveen's investment process by refining and delivering the firm's collective equity market outlook, including key risks and drivers, to clients. Led by Saira Malik, CIO & Head of Equities, the team shares best global equities ideas, while focusing on individual areas of expertise to help generate alpha.

For more information or to subscribe, please visit nuveen.com.

Sources

All market data from Bloomberg, Morningstar and FactSet.

This material is not intended to be a recommendation or investment advice, does not constitute a solicitation to buy, sell or hold a security or an investment strategy, and is not provided in a fiduciary capacity. The information provided does not take into account the specific objectives or circumstances of any particular investor, or suggest any specific course of action. Investment decisions should be made based on an investor's objectives and circumstances and in consultation with his or her financial professionals.

The views and opinions expressed are for informational and educational purposes only as of the date of production/writing and may change without notice at any time based on numerous factors, such as market or other conditions, legal and regulatory developments, additional risks and uncertainties and may not come to pass. This material may contain "forward-looking" information that is not purely historical in nature.

Such information may include, among other things, projections, forecasts, estimates of market returns, and proposed or expected portfolio composition. Any changes to assumptions that may have been made in preparing this material could have a material impact on the information presented herein by way of example. **Past performance is no guarantee of future results.** Investing involves risk; principal loss is possible.

All information has been obtained from sources believed to be reliable, but its accuracy is not guaranteed. There is no representation or warranty as to the current accuracy, reliability or completeness of, nor liability for, decisions based on such information and it should not be relied on as such. For term definitions and index descriptions, please access the glossary on nuveen.com. **Please note, it is not possible to invest directly in an index.**

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.

CFA® and Chartered Financial Analyst® are registered trademarks owned by CFA Institute.

Nuveen provides investment advisory services through its investment specialists.

This information does not constitute investment research as defined under MiFID.

nuveen

A TIAA Company