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CIO Weekly Commentary
15 May 2023

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

You can't be too prepared as the debt deadline nears

Bottom line up top

Fed's inflation fight finally gets real. Last week's release of Consumer Price Index (CPI) data for April confirmed that U.S. inflation remains elevated and "sticky," even as disinflationary pressures continue to have a noticeable, if uneven, impact. While headline CPI ticked up to 0.4% for April, the year-over-year number edged down to 4.9%, versus 5.0% in March. That's the lowest reading since April 2021 and marks the 10th consecutive month in which the annual inflation rate has decreased. The current level of CPI, combined with the U.S. Federal Reserve's 25 basis points (bps) rate hike earlier in May, has pushed real rates — i.e., the Fed's policy rate minus the inflation rate — into positive territory for the first time since May 2020 (Figure 1). Over the near term, positive real rates should allow policymakers to pause this historic rate-hike cycle as inflation continues to moderate. And while sticky inflation in areas like shelter costs and rising wages won't let the Fed pivot to rate cuts anytime soon, rate stability could be a modest tailwind for most risk assets. That doesn't alter our view that a mild recession still looms in what we expect will be a higher-for-longer interest rate environment.

The "X" date marks the spot. There's a big "X" on the map to an agreement between the White House and Congress regarding the U.S. government's legal borrowing capacity (i.e., the "debt ceiling"). Whether that X will yield treasure or trauma depends on the ability of the negotiating parties to resolve their differences by June 1. That's the estimated date after which the U.S. Treasury Department would be forced to delay or even miss bond payments — an unprecedented event. Leading

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On behalf of Nuveen's Global Investment Committee

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.

up to that point, we expect risk assets to undergo a period of heightened volatility amid a flurry of headlines on progress (or lack thereof) toward a compromise that would avert a U.S. default. We think a deal will ultimately be hammered out by the deadline, even if it's a short-term fix that kicks a more "permanent" solution down the road. In the meantime, it would be prudent for investors to prepare for a less favorable outcome by positioning their portfolios to better weather the potential storm.

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FIGURE 1: REAL RATES IN THE U.S. RETURN TO POSITIVE TERRITORY

U.S. real rates (%)

Data source: Bloomberg, L.P., 31 March 2023. **Performance data shown represents past performance and does not predict or guarantee future results.** Real rates are calculated by subtracting the policy rate by the inflation rate of each country.

Portfolio considerations

As the June 1 "X date" approaches, one thing investors can be certain of is that more uncertainty lies ahead. We can expect further volatility across equity and fixed income markets until we have greater clarity on the outcome — and probable impacts — of the U.S. debt ceiling negotiations. In our view, the most likely scenario is a resolution, perhaps at the eleventh hour, enabling the federal government to meet its obligations. That said, adjustments to portfolio positioning may need to be considered if an agreement is not reached in time.

Within fixed income, intermediate and longer-duration securities would be expected to outperform their shorter-duration counterparts. Additionally, we favor core bonds over short-term Treasuries, as they tend to outperform immediately after a pause in a Fed's tightening cycle, such as the one we likely entered following the May 3.

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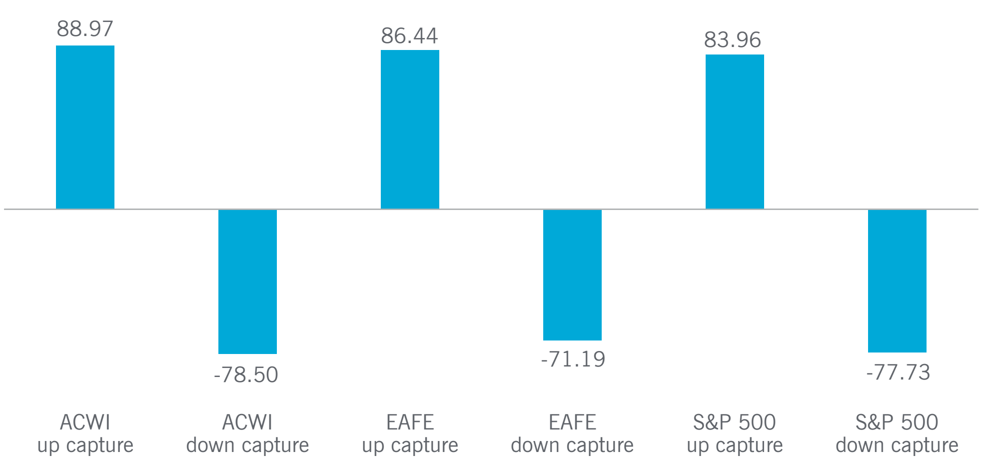
As for equities, we remain defensive ahead of a potential recession later this year — a stance that is reinforced by the prospect of a failed debt ceiling resolution. One area we prefer is global infrastructure, which is less cyclical and generally benefits from durable cash flows, even during volatile periods. Since 2001, global infrastructure has participated in just 70%-80% of equity market downside across different geographical regions (Figure 2). Diversification via global infrastructure has proven especially compelling when unsettled conditions are country- or region-specific, as with the U.S. debt ceiling showdown. In this environment, we expect non-U.S. equities, particularly those more defensive in nature. Within U.S. infrastructure, we currently favor less cyclical sectors such as regulated utilities and communications infrastructure.

While higher interest rates are not an ideal backdrop for infrastructure assets given the increased cost of capital, infrastructure companies are often able to pass through such costs to the end user. This should help the asset class outperform if our base case of a successful debt ceiling resolution does not materialize. Lastly, our higher-for-longer rate outlook, which contrasts with the market's expectation of three rate cuts by year-end, would bode well for global infrastructure.

FIGURE 2: GLOBAL INFRASTRUCTURE CAN HELP SMOOTH RETURNS, EVEN IN VOLATILE PERIODS

S&P global infrastructure up/down capture, 01 Dec 2001[1] – 31 Mar 2023



Data source: Morningstar Direct, 31 March 2023. **Performance data shown represents past performance and does not predict or guarantee future results.**

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.

Regular 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

1 01 Dec 2001 is the inception date of the S&P Global Infrastructure Index. All information presented prior to the index inception date is back-tested. The back-test calculations are based on the same methodology that was in effect when the index was officially launched. The returns and risk in the chart represent past performance of the indexes and should not be viewed as a guarantee of future index or investment performance. Market indexes do not include fees.

Sources

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

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Important information 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. Debt or fixed income securities are subject to market risk, credit risk, interest rate risk, call risk, derivatives risk, dollar roll transaction risk, and income risk. As interest rates rise, bond prices fall. Foreign investments involve additional risks, including currency fluctuation, political and economic instability, lack of liquidity, and differing legal and accounting standards. 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. Concentration in infrastructure-related securities involves sector risk, particularly greater exposure to adverse economic, regulatory, political, legal, liquidity, and tax risks associated with MLPs and REITs.

Nuveen provides investment advisory services through its investment specialists.

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

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