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CIO Weekly Commentary
23 May 2022

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

How much pain are asset classes pricing in?

Bottom line up top:

The economy is brewing a cuppa something, but whether it's iced or hot, diluted or full-strength remains to be seen. For much of this unusually volatile year, markets have sent a fairly consistent message with their negative performance: Wake up and smell the coffee! In other words, markets have signaled deep concerns about slowing growth, Fed tightening, geopolitical risks and other factors driving up the odds of a recession in 2022. Bearishness remains broadly elevated, although we've begun to see more variation among asset classes in terms of how much pain is being priced in (Figure 1).

Mixed economic signals make it difficult to declare the cup half empty or half full. Last week, continued consumer strength was on display with the release of April's robust retail sales numbers. However, a number of major retailers posted poor corporate earnings, sending stocks into a tailspin. On Tuesday industrial production surprised to the upside, but Thursday brought a significant miss in the Philadelphia Fed's manufacturing index. Both housing starts and building permits fell last month, as sharply higher mortgage rates tempered demand for new construction, while severely constrained supply dampened sales of existing homes. Also telling: The Conference Board's Index of leading economic indicators (LEI) moved lower on a year-over-year basis for the eleventh time in the past 12 months (Figure 2).

Our view: on balance, still a modestly constructive outlook. Figure 3 shows a range of possible economic scenarios, from best-case to worst, and is accompanied by portfolio construction ideas for the two outcomes — soft landing and mild recession — that we deem more likely to occur in 2022.

Saira Malik, CFA
Chief Investment Officer

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.

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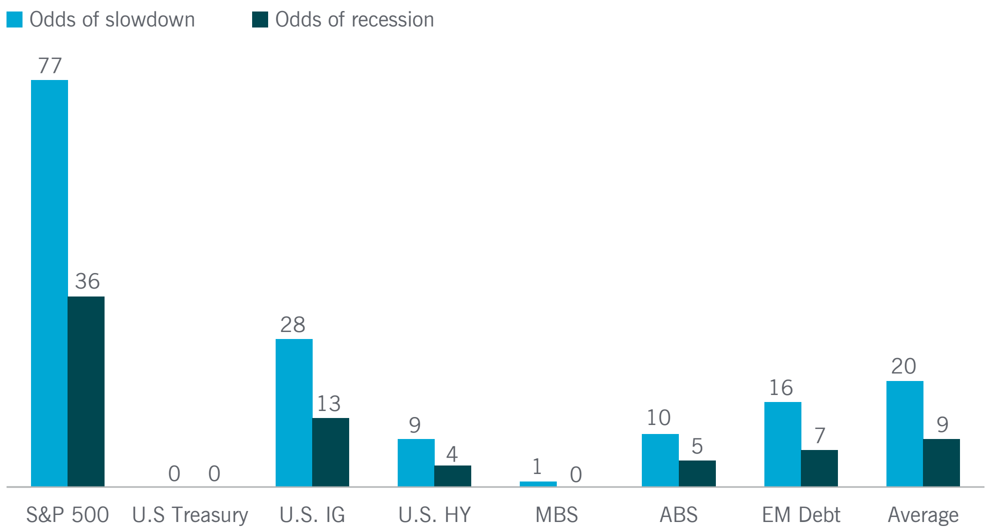
Equity markets are likely too bearish, and we're watching credit spreads for signs that bond investors are increasing their recession expectations as well.

FIGURE 1: EQUITIES ARE MORE PESSIMISTIC THAN CREDIT

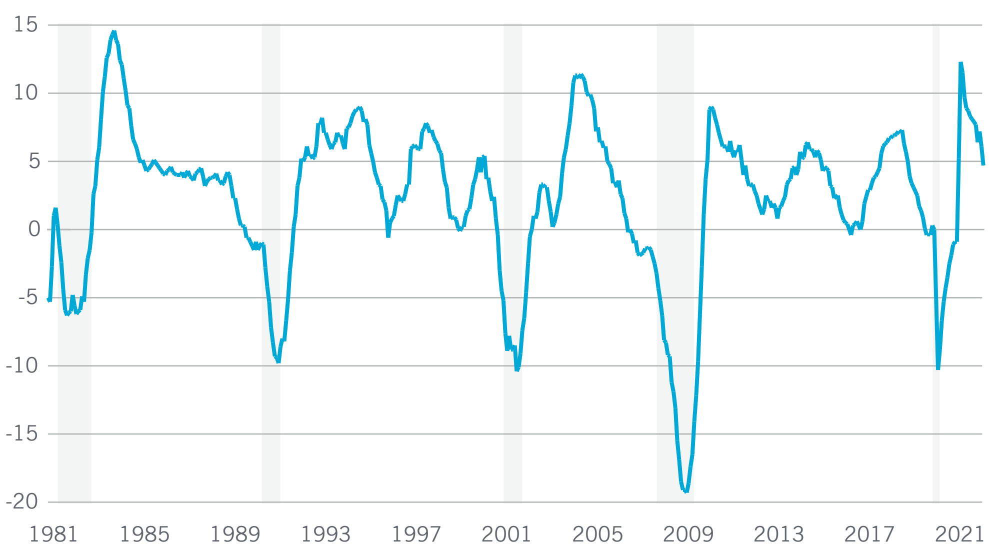
Market implied odds of recession (%)



Data source: Bloomberg, L.P. 19 May 2022. Representative indexes: U.S. Treasury: Bloomberg U.S. Treasury Index; U.S. IG: Bloomberg U.S. Corporate Investment Grade Index; U.S. HY: Bloomberg U.S. Corporate High Yield Index; MBS: Bloomberg U.S. Mortgage-Backed Securities Index; ABS: Bloomberg Asset Backed Securities Index; EM debt: Bloomberg Emerging Markets Hard Currency Aggregate Index **Past performance does not predict or guarantee future results.**

FIGURE 2: LEADING INDICATORS HIGH, BUT DECELERATING

Leading economic indicator index, YoY change (%)



Data source: Bloomberg, L.P., 31 Jan 1981 to 30 Apr 2022. **Past performance does not predict or guarantee future results.**

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FIGURE 3: LOOKING INTO OUR CRYSTAL BALL

Scenario	Best case (Goldilocks)	Soft landing	Mild recession	Worst case (Hard recession)
Fed hikes	Fewer than expected	To expectations	To expectations, or slightly past	Well past neutral
GDP	2.50%	1.50%	< 0%	< 0%
Core PCE	3.50%	4.00%	< 3%	> 5.50%
Inflation expectations	Falls	Falls	Falls	Rises, then falls

Data source: Nuveen views. **Past performance does not predict or guarantee future results.**

We believe a soft landing or a mild recession are more likely outcomes than either our best case or worst case scenarios.

Portfolio considerations

Our **best case (Goldilocks) scenario** entails inflation moderating, GDP growth proving resilient and the Fed pausing on raising rates when the coffee is neither too hot nor too cold. We think the odds of this optimistic view coming to fruition are small. At the other end of the spectrum, our **worst case scenario** is a **hard recession**, which we also think is unlikely. Instead of these extremes, our expectations hover between the **soft landing** and **mild recession** scenarios.

In a **soft landing**, inflation moderates, GDP growth is positive and the Fed hikes to expectations (i.e., tightening is priced into markets). The employment situation weakens slightly but remains strong. In this scenario, we would have a preference for growth stocks. Within fixed income, we would favor up-in-quality credit, including higher-quality high yield, where current yields of 6.3% cushion against both spread widening and rising rates. Taxable investors could take advantage of attractive entry points for municipals. We would not recommend adding interest rate sensitivity given lower-but-still-high inflation and a resolute Fed.

In a **mild recession**, the Fed may have been successful in combating inflation, but at the expense of economic expansion (i.e., GDP growth is negative). In this scenario, going into a recession cyclical stocks may lose their premium. Within equities, we would therefore prefer a blend of dividend growth stocks and value equities. The trickier call is finding the appropriate level of rates duration: holding duration while the Fed continues hiking could be problematic, but it may hedge growth risk if the economy is actually in a recession. Additionally, the attractive income offered by credit could help offset the effects of spread widening in a mild recession. Here, we would emphasize investment grade corporate and short- and intermediate-duration municipals.

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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

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. 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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