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CIO Weekly Commentary
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CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Why a too-strong dollar could cost a pretty penny

Bottom line up top:

Multiple drivers, one destination. The U.S. dollar has been on a tear in 2022, leaving most of its international currency peers in the dust (Figure 1). What's been driving the dollar's dominance?

- **Out of sync central banks.** Despite the European Central Bank's surprising 50 basis point hike last Thursday (vs. an expected 25 bps), the U.S. Federal Reserve's earlier start and more resolute hawkishness compared to other central banks have boosted interest rate differentials and real U.S. interest rates, contributing to the dollar's rise. A stronger greenback is an implicit goal of Fed tightening, as it helps reduce inflation.
- **Global "risk off" sentiment.** Amid decelerating growth and increased recession fears, the dollar has benefited from its traditional role as a safe-haven currency.
- **U.S. resilience to commodity price shocks.** Russia's invasion of Ukraine fueled a spike in energy and agricultural commodity prices, but the economic impact in the U.S. was less severe than in Europe, Asia and most emerging markets. More recently, commodity prices have moved lower — historically a favorable dynamic for the dollar.

A headwind for many risk assets. Broadly speaking, a firmer dollar tends to weigh on higher-beta asset classes. In **U.S. equities,** dollar strength will probably be cited frequently to justify lower corporate earnings this reporting season, particularly for multinationals that derive a large percentage of their revenue from overseas sales.

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.

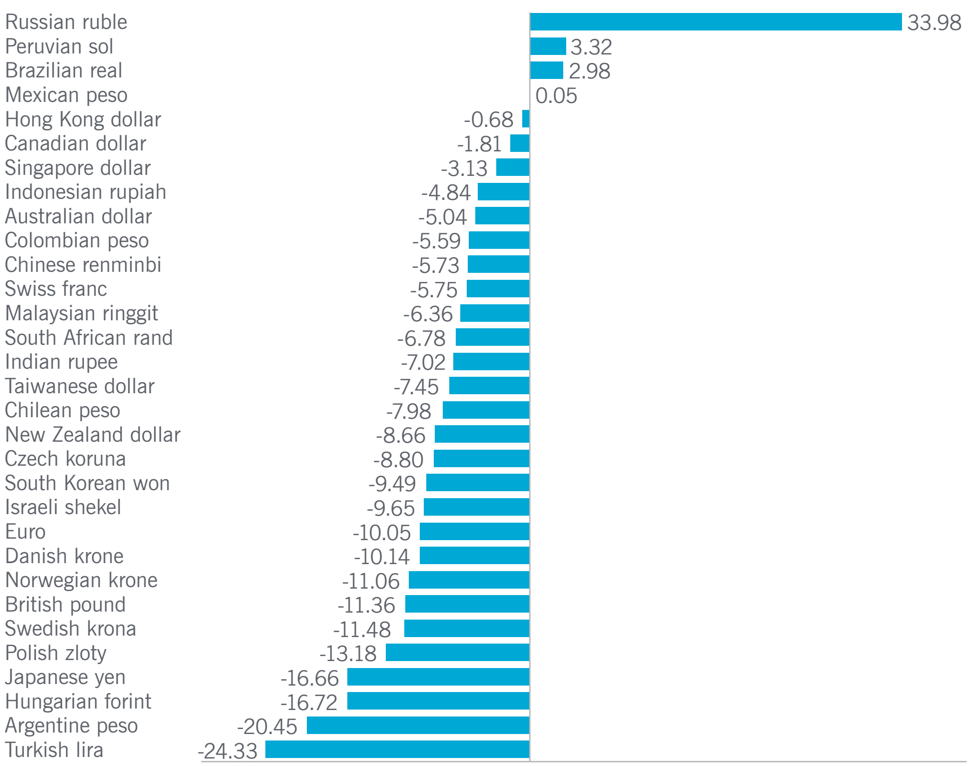
Historically, the U.S. dollar has been inversely related to inflation.

Non-U.S. equities generally don't benefit from of a robust dollar, although companies that export goods to the U.S. may welcome the currency exchange impact. **Emerging markets (EM)** equities, in aggregate, rarely produce positive returns when the dollar is appreciating materially. **EM debt**, specifically dollar-denominated issues, may also be pressured. Meanwhile, **commodities** typically have an inverse relationship to the dollar, so there's no advantage for the asset class itself when the dollar appreciates. But there is a broader silver lining: downward pressure on commodities prices should help temper overall inflation.

Odds favor stronger for longer. We expect the dollar to remain strong or climb even higher in the near to medium term, bolstered by still-elevated inflation and aggressively tighter monetary policy. From a portfolio perspective, this supports our general preference for U.S. over non-U.S. investments, credit sectors over equities and a diminishing reliance on commodities as an inflation hedge.

FIGURE 1: U.S. DOLLAR STRENGTH IS A SYMPTOM OF GLOBAL ECONOMIC UNEASE

Year-to-date returns by currency (%)



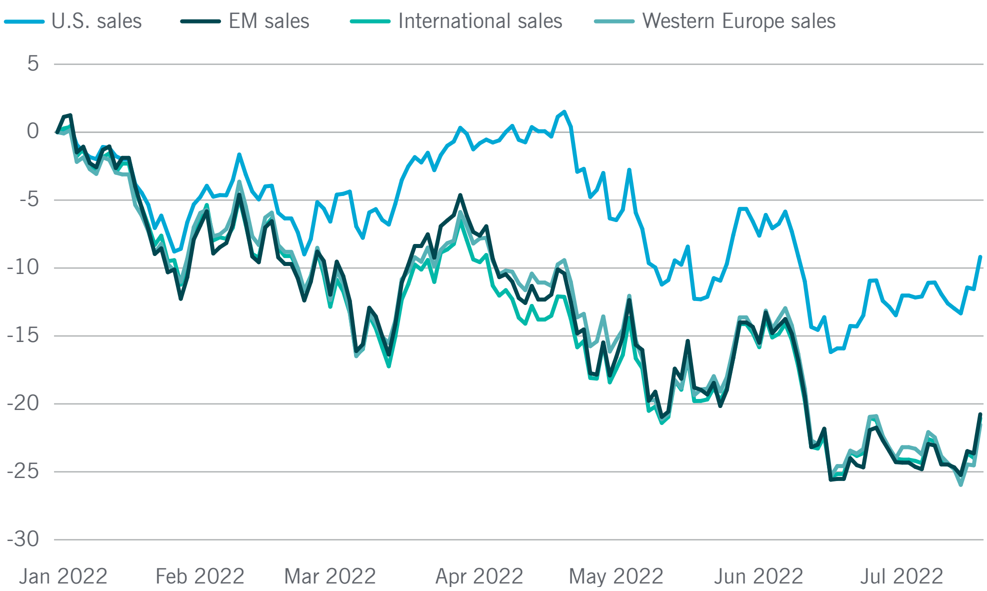
Data source: Bloomberg, L.P., 19 Jul 2022. Currency returns versus the U.S. dollar. **Past performance does not predict or guarantee future results.** Russian ruble is an outlier, primarily driven by capital controls imposed by the country's central bank, forcing its exporters to convert earnings into local currency.

Portfolio construction considerations

Given today's strong-dollar market, we generally favor U.S. companies sourcing most of their sales domestically.

FIGURE 2: DOMESTICALLY FOCUSED U.S. COMPANIES ARE MORE RESILIENT AMID DOLLAR'S RISE

U.S. company stock returns by geographic sales focus (%)



Data source: Goldman Sachs Research and Bloomberg, L.P., 31 Dec 2021 to 19 Jul 2022. **Past performance does not predict or guarantee future results.** Data is based on baskets of stocks identified by Goldman Sachs Research from 2021 company filings. **U.S. sales**: the 50 S&P 500 Index stocks with the highest U.S. revenue exposure; **EM sales:** the 50 companies in the Russell 1000 Index with the highest sales exposure to the EM countries and regions; **International sales:** the 50 S&P 500 Index companies with the highest international sales exposure; **Western European sales:** the 50 companies in the Russell 1000 Index with the highest sales exposure to Europe.

Within the S&P 500 Index, returns diverge between U.S. companies sourcing most of their sales domestically and those that rely more heavily on non-U.S. customers in various regions of the world (Figure 2). Given today's strong-dollar market, we generally favor the former group.

Narrowing our preference further, we continue to like dividend growth equities, which historically have outperformed during periods of higher interest rates and inflation. Dividend-growing companies are usually supported by healthy balance sheets that can help them better cope in a rising rate environment. Additionally, their dividends are a more reliable component of total return than price performance — a key consideration amid high levels of uncertainty.

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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