NUVEEN ASSET MANAGEMENT

Sentiment is Slowly Improving, but Risks Remain High

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C20-16011 | 05/2020 | EXP 05/31/2021

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Weekly Investment Commentary

May 4 2020

Sentiment is slowly improving, but risks remain high

Stocks started the week in a positive direction before dropping sharply on Thursday and Friday. We think this sort of volatility is likely to persist for some time. The S&P 500 Index was down marginally for the week, but more cyclical and smaller cap stocks outperformed, indicating some optimism about the economic future.[1] Energy was the best-performing sector as oil prices enjoyed a 17% increase from depressed levels.[1]

HIGHLIGHTS

- **Investors are growing increasingly optimistic over prospects that the coronavirus pandemic is cresting and areas of the global and U.S. economies are starting to re-open.**
- **Cautious optimism is warranted, but we also expect economic activity to remain depressed and uneven for some time. The good news: Fiscal and monetary stimulus should help set a base for an economic recovery later this year.**
- **We continue to believe that stocks have already reached the cycle low, but also expect that near-term weakness is likely.**

Robert C. Doll, CFA
Senior Portfolio Manager and Chief Equity Strategist

Bob Doll serves as a leading member of the equities investing team for Nuveen, providing reasoned analysis through equity portfolio management and ongoing market commentary.

10 observations and themes

1) Equity valuations have climbed higher as volatility remains high. In 23 sessions between February 19 and March 23, U.S. stocks fell 35%.[1] In the 24 trading sessions that followed until April 29, stocks rose 35%.[1] Price improvements came from a sense that the coronavirus pandemic may be easing, stimulus measures were working and the recession could be short-lived. Corporate earnings expectations have been falling, however, pushing up valuation measures. On February 19, the 12-month forward P/E ratio for the S&P 500 was 19X.[1] At the market peak last week, it was up to 20X, its highest level since 2002.[1]

2) The rough first quarter GDP report will pale in comparison to what we expect to see in the second quarter. Growth fell 4.8% in the first quarter, the first contraction since 2014 and the worst number since 2008.[2] We expect second quarter growth will fall by 25% or more.

3) Unemployment continues to soar. On Friday, we'll see the April labor report, which is based on readings in the middle of the month. We think it will probably show an unemployment level of at least 15%, but factoring in the additional weeks of unemployment claims, we think the actual current rate is around 20% and rising.

4) Technology and less cyclical areas have been weathering the earnings storm relatively better. We're about two-thirds of the way through first quarter earnings season. Overall revenues are flat and earnings results are down around 15%.[3] The financial sector and cyclical areas of the market have been the worst performers.[3]

5) The coronavirus appears to be cresting in the United States. Investors are becoming increasingly optimistic about plans for re-opening areas of the economy around the country. These signs are encouraging, but we caution that confusion, uncertainty, backtracking and fresh rounds of infections all remain likely.

6) The relationship between the United States and China is worsening. Prospects for a phase-two trade deal seem to be completely off the table, as acrimony and distrust are mounting. Many in Washington are calling for an increased decoupling between the two countries, and we have a sense that China is moving from being a U.S. competitor to an adversary.

7) Recent volatility has accelerated the ongoing concentration in the U.S. stock market. Somewhat amazingly, the five largest U.S. companies (Microsoft, Apple, Amazon, Facebook and Alphabet) now comprise over 20% of the S&P 500 market capitalization.[1] In contrast, over 300 of the companies in the index have a weighting of less than 0.1%.[1]

8) Market sentiment is improving. Value styles, cyclical sectors and small cap stocks have outperformed recently, reflecting improved hopes for economic growth and increased confidence that the global economy will reopen as virus pressures slowly ease.

9) Volatility is likely to remain high in both positive and negative directions. Stocks remain caught between the massive $8 trillion in fiscal and monetary stimulus on the positive side and collapsing economic and earnings growth on the downside. We're optimistic over the longer term, but think markets could experience a period of weakness ahead.

10) The odds of a near-term market decline remain high. On February 19, the S&P 500 Index peaked at 3,386, before sinking to 2,192 on March 23.[1] Last week saw a high of 2,954 before the market sank 4.5% on Thursday and Friday to close at 2,832.[1] We would not be surprised to see stocks drop back to the 2,550/2,600 level over the coming weeks before attempting to rally again.

An uneven economic re-opening will likely prompt more volatility

Infection rates continue to rise in some areas of the world and, but there is a sense that the worst of the storm has passed. Hot spots such as Italy and New York are showing better data, and broad trends indicate that aggressive countermeasures have effectively limited coronavirus contagion.

Most of the world is now moving to a new and highly uncertain phase of economic reopening. The biggest risk, of course, is that without widespread and repeated testing, let alone effective treatments and vaccines, we could see renewed surges of infections as economic lockdowns start to ease. And even if we are largely able to avoid fresh coronavirus waves, re-opening economies will be uneven and uncertain, making it difficult to gauge the outlook for global economic growth into 2021 and beyond. But it is safe to say that the economy will be operating well below pre-crisis levels for some time, which will negatively affect earnings, profits and many financial asset values.

The good news is that the aggressive and unprecedented fiscal and monetary policy response has been a clear positive for equities and other risk assets. Although economic growth is in the midst of a widespread collapse, we think stimulus measures will help set the stage for the start of a recovery later this year.

Since the start of the current crisis, we have argued that containing the spread of the coronavirus will be the first and most critical condition necessary for improvement in the economic outlook and sustained upside in risk asset values. We may soon find out how well those steps have been working. Over the near term, market volatility is likely to remain high in both directions, making portfolio positioning a challenge. As we have been saying for some time, we think investors with long-term time horizons may want to consider using periods of near-term weakness as buying opportunities.

2020 PERFORMANCE YEAR TO DATE

	Returns	
	Weekly	**YTD**
S&P 500	-0.2%	-11.8%
Dow Jones Industrial Avg	-0.2%	-16.3%
NASDAQ Composite	-0.3%	-3.8%
Russell 2000 Index	2.2%	-24.1%
MSCI EAFE	3.1%	-18.7%
MSCI EM	4.3%	-17.3%
Bloomberg Barclays US Agg Bond Index	-0.1%	4.8%
BofA Merrill Lynch 3-mo T-bill	0.0%	0.6%

Source: Morningstar Direct, Bloomberg and FactSet as of 1 May 2020. All index returns are shown in U.S. dollars. Past performance is no guarantee of future results. Index performance is shown for illustrative purposes only. Index returns include reinvestment of income and do not reflect investment advisory and other fees that would reduce performance in an actual client account. All indexes are unmanaged and unavailable for direct investment.

"Although economic growth is in the midst of a widespread collapse, we think stimulus measures are setting the stage for a bumpy recovery for the balance of the year."

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

1 Source: Bloomberg, Morningstar and FactSet

2 Source: Bureau of Labor Statistics

3 Source: Credit Suisse Research

The **S&P 500 Index** is a capitalization-weighted index of 500 stocks designed to measure the performance of the broad domestic economy. The **Dow Jones Industrial Average** is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the *Nasdaq*. The **Nasdaq Composite** is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market. The **Russell 2000 Index** measures the performance approximately 2,000 small cap companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks. **Euro Stoxx 50** is an index of 50 of the largest and most liquid stocks of companies in the eurozone. **FTSE 100 Index** is a capitalization-weighted index of the 100 most highly capitalized companies traded on the London Stock Exchange. **Deutsche Borse AG German Stock Index** (DAX Index) is a total return index of 30 selected German blue chip stocks traded on the Frankfurt Stock Exchange. **Nikkei 225 Index** is a price-weighted average of 225 top-rated Japanese companies listed in the First Section of the Tokyo Stock Exchange. **Hong Kong Hang Seng Index** is a free-float capitalization-weighted index of selection of companies from the Stock Exchange of Hong Kong. **Shanghai Stock Exchange Composite** is a capitalization-weighted index that tracks the daily price performance of all A-shares and B-shares listed on the Shanghai Stock Exchange. **MSCI EAFE Index** is a free float-adjusted market capitalization weighted index designed to measure developed market equity performance, excluding the U.S. and Canada. The **MSCI Emerging Markets Index** is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. **Bloomberg Barclays U.S. Aggregate Bond Index** covers the U.S. investment grade fixed rate bond market. The **BofA Merrill Lynch 3-Month U.S. Treasury Bill Index** is an unmanaged market index of U.S. Treasury securities maturing in 90 days that assumes reinvestment of all income.

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GPE-BDCOMM1-0520P GWP-1174387PR-W0520P