NUVEEN ASSET MANAGEMENT

Middle Ground Between the Bear and Bull Case for Stocks

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Weekly Investment Commentary

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Middle ground between the bear and bull case for stocks

Stocks fell again last week, marking the first time in over a year that markets declined for four consecutive weeks.[1] The main culprit appears to be fading prospects for a new fiscal stimulus package in the U.S., even as Federal Reserve officials and others continue to call for new spending. Growing concern over U.S. election uncertainty also contributed to the decline, as did new surges in coronavirus cases, particularly in Europe.

HIGHLIGHTS

- **Stocks are down four weeks in a row, and weakness from the technology sector has spread to the broader market.**
- **We continue to think there is at best a small chance for an additional fiscal stimulus package before the November elections.**
- **Stocks appear balanced between positives and negatives. And growing uncertainty over the U.S. election is weighing on investors. As such, we think equity markets could be choppy and range-bound through the end of this year.**

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) Rising coronavirus cases around the world present a growing market risk, as they are raising the odds of additional economic containment.

2) The lack of a new fiscal stimulus package is hurting the U.S. economy. We continue to believe that a new stimulus package before the election has only a small chance of happening. Without one, consumer spending would likely take a hit and millions of individuals and thousands of businesses could face bankruptcy risks.

3) U.S. political uncertainty is rising. In addition to the usual election year uncertainty over potential shifts in leadership, confusion is running high over how voting will actually work, whether we will have a clear winner and whether either side will concede defeat. This uncertainty could persist for days or weeks after the election, and financial markets notoriously loathe political uncertainty.

4) Economic data is increasingly mixed as the recovery becomes choppier. On the negative side, initial weekly unemployment claims remain elevated. On the positive side, new home sales are climbing rapidly.

5) The surge in the housing market reflects pandemic-induced demographic trends. As virus cases continue to rise and millions are finding it difficult to leave their homes, many people are increasingly looking for new housing in suburbs and rural areas.

6) The corporate earnings outlook is mixed. Individual company-level forecasts imply that S&P 500 earnings could recover by the end of the year.[2] But that masks significant variation beneath the surface. Three-quarters of the year-over-year decline in second quarter earnings came from sectors directly hit by the pandemic, including travel, energy and loan-loss provisions in banks.[2] And forecasts are not suggesting recoveries in those areas. Rather, the good news is focused on technology and health care, which didn't take much of a hit to begin with.[2]

7) Prospects for (eventually) rising inflation are causing many to wonder if any areas of the market could benefit from such a trend. We would point to the traditional historical winners: small caps, bank, energy and industrial stocks, gold, short-duration corporate credit, TIPS, leveraged loans and convertibles.

8) The bear case for stocks: Markets may not be able to overcome significant headwinds, including a resurgence in infection rates, negative economic surprises and prospects for higher corporate tax rates next year.

9) The bull case for stocks: Despite these risks, massive monetary support will continue to support stock prices and we could still see some fiscal stimulus. These tailwinds should create buying opportunities during times of weakness until we see a vaccine, which should cause an economic resurgence.

10) Our view is somewhere in the middle: We think all of the bear and bull cases have some truth, which leads us to believe that stocks are likely to remain choppy and range-bound for the next several months.

The economy still relies on additional fiscal stimulus

Financial markets have been cooling off over the last month, with the correction in technology stocks spreading to the broader market. This shouldn't be much of a surprise after an incredibly strong run in equities over the summer, driven by optimism over economic growth. We had been expecting a gradual and choppy economic recovery, but stocks were pricing in a much rosier outlook as recently as a month ago. Now, it looks like the odds of a quick return to pre-pandemic economic conditions are a longshot. The services sectors in particular appear likely to remain stagnant until people around the world agree it is again "safe" to return to normal, and without a substantive and proven medical breakthrough, it is hard to see that happening.

At this point, the momentum behind U.S. economic growth is waning. In particular, two key tailwinds driving growth in late spring into summer are fading: the benefits from reopening segments of the economy and the benefits from increased unemployment, jobs protection and business assistance. The former appears unlikely to continue without a proven vaccine and the latter is being held back by rising political uncertainty. There looks to be only a small chance of a fiscal stimulus program being enacted before the November election, and it might take a more painful market decline and economic pain to compel politicians to act. The bottom line is that until a medical breakthrough makes it possible for the economy to enter a self-reinforcing expansion, ongoing fiscal stimulus is still needed.

For stocks, short-term risks remain high and we think volatility is likely to continue. We expect stocks to continue clawing their way higher and being beset by periodic setbacks. Some of the froth has been removed from markets over the last month, and pockets of value are being created, but this remains a time for caution and investment selectivity.

2020 PERFORMANCE YEAR TO DATE

	Returns	
	Weekly	**YTD**
S&P 500	-0.6%	3.5%
Dow Jones Industrial Avg	-1.8%	-3.1%
NASDAQ Composite	1.1%	22.5%
Russell 2000 Index	-4.0%	-10.7%
MSCI EAFE	-4.2%	-8.2%
MSCI EM	-4.4%	-3.0%
Bloomberg Barclays US Agg Bond Index	-0.1%	6.8%
BofA Merrill Lynch 3-mo T-bill	0.0%	0.6%

Source: Morningstar Direct, Bloomberg and FactSet as of 25 September 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.

"Until a medical breakthrough makes it possible for the economy to enter a self-reinforcing expansion, ongoing fiscal stimulus is still needed."

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1 Source: Bloomberg, Morningstar and FactSet

2 Source: Empirical Research Partners

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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