NUVEEN ASSET MANAGEMENT

Stocks Climb as Economic Data Worsens

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Weekly Investment Commentary

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Stocks climb even as economic data worsens

After falling the previous two weeks, stock prices rebounded last week due to increasing optimism over prospects for re-opening the economy. Many investors sense that global economic activity may be bottoming and the world could start to see a recovery. In the U.S., the S&P 500 Index climbed 3.6%, led by energy thanks to another sharp increase in oil prices.[1] *Technology also outperformed, while more defensive areas such as utilities and consumer staples lagged.*

HIGHLIGHTS

- **Equity prices remain volatile on a day-to-day basis, but haven't moved much over the last several weeks. It seems that investors are waiting to see how smoothly economic re-opening plans progress.**
- **We continue to believe the U.S. and global economies will start to recover in the second half of 2020, but investors may be overly complacent about near-term risks.**
- **We remain cautiously optimistic about long-term prospects for stocks, but markets could be due for an additional period of consolidation in the coming weeks.**

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) The employment landscape looks dire. The April unemployment rate spiked to 14.7%, the highest level since October 1940.[2] Job losses from March and April have totaled 21.4 million, wiping out all of the gains since the Great Recession.[2] We expect to see at least one more month of sharply rising unemployment before a slow recovery could start.

2) The economy could recover in the second half of 2020. The data are already worse than the 2008/2009 recession in manufacturing, employment and auto sales. And we expect the same across retail sales, housing starts and industrial production. GDP declined 5% in the first quarter, and we expect it will fall by 25% or more in the second.[3] The third quarter could see a sharp rebound to around 10% growth with perhaps 5% growth in the fourth.

3) We think April will mark the low for this recession. A combination of declining coronavirus cases in some areas, more hospital capacity, falling tax revenues and restlessness among consumers and businesses are pushing governors and other policymakers to start reopening some states and regions. One positive signal: One month ago, states with decelerating daily new COVID-19 cases made up 20% of the country's GDP. That number has risen to 72%.[4]

4) We expect another massive fiscal stimulus package of $1 trillion or more. We expect state and local government assistance, additional checks for individuals, targeted help for certain industries, tax breaks and more funding for unemployment insurance. We do not expect infrastructure spending to be included.

5) Corporate earnings remain under intense pressure. With about 90% of S&P 500 companies reporting, revenues are flat and earnings are down close to 15%.[5] Cyclical areas have been particularly hard hit, while health care has been a bright spot.

6) Extreme monetary accommodation is keeping stock prices afloat. We have not seen a meaningful pullback in stock prices since the March 23. Equity valuations have been climbing since late March, as earnings have been falling.

7) Equity valuation increases have been uneven. The 12-month forward price-to-earnings ratio for the S&P 500 rose from 14X on March 23 to 19.4X at the end of last week.[1] Some sectors have seen modest valuation increases, such as health care (12.9X to 15.9X), technology (16.7X to 20.8X) and financials (8.3X to 13.1X).[1] Others have seen more extreme climbs, including consumer discretionary (16.8X to 28.8X) and energy (10.9X to an incredible 157X).[1]

8) Stocks appear stuck at their current range. The bull case rests on central bank easing, more fiscal stimulus and hopes over economic re-opening. The bear case is based on rising valuations and high uncertainty over the path of the coronavirus and economic reopening.

9) Growth styles are looking expensive, but timing a rotation back to value is not clear. Weak corporate profits and low bond yields have been favoring growth over value. Relative price momentum and valuations suggest that growth is approaching extremes. But a sustained rotation into value would require a noticeable improvement in the economic backdrop, which could take time to develop.

10) The U.S. political backdrop looks highly uncertain. With President Trump's poll numbers continuing to slip, a Democratic sweep of the White House and Congress is possible—or at least more of a possibility than markets are forecasting. Should that occur, we could expect tax increases and a more stringent regulatory environment, which could create headwinds for stock prices.

Investors may be overly complacent about near-term risks

Markets have stalled in recent weeks, after a sharp setback for stocks and other risk assets in March and a subsequent sharp recovery through much of April. Although volatility remains elevated, stock prices have struggled to move significantly higher or lower. At this point, investors can either bet on a positive outcome marked by a steady return to economic activity or a negative one in which economic re-opening struggles due to further rounds of infections and lockdowns.

We expect the economy will rebound modestly in the second half of 2020, but we also think investors may be pricing in a too-optimistic short-term view. Current stock valuations reflect a more even and clear re-opening scenario than we think is likely. We expect confusion and uncertainty as some regions start to re-open, and we are concerned that some areas of the world and within the U.S. are unlocking their economies prematurely. We also think it is too early to be optimistic over prospects for treatments and vaccines. If those take longer than expected to materialize, it could shatter investor sentiment. Looking down the road, we are also concerned about political uncertainty surrounding the U.S. elections and a possible increase in protectionism as the relationship between the U.S. and China continues to deteriorate.

Looking further ahead, we think the biggest positive so far is probably the massive and unprecedented monetary and fiscal stimulus and the prospects for additional support. The economic recovery will be uneven and will take some time, but we think the underlying economic structure of the world and U.S. remains sound. Corporate earnings are likely to remain under pressure for some time and corporate fundamentals will likely continue to deteriorate. But we are counting on better prospects for the economy and corporate earnings in the second half of this year and into 2021.

2020 PERFORMANCE YEAR TO DATE

	Returns	
	Weekly	**YTD**
S&P 500	3.6%	-8.7%
Dow Jones Industrial Avg	2.7%	-14.0%
NASDAQ Composite	6.1%	2.0%
Russell 2000 Index	5.5%	-19.9%
MSCI EAFE	0.9%	-18.0%
MSCI EM	-0.5%	-17.7%
Bloomberg Barclays US Agg Bond Index	-0.3%	4.5%
BofA Merrill Lynch 3-mo T-bill	0.0%	0.6%

Source: Morningstar Direct, Bloomberg and FactSet as of 8 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.

"Economic data are likely to continue plummeting before recovering in the second half of 2020."

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1 Source: Bloomberg, Morningstar and FactSet
2 Source: Bureau of Labor Statistics
3 Source: Bureau of Economic Analysis
4 Source: Strategas Research
5 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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