Cautious Optimism Toward Equities, but with Escalating Risks

NUVEEN ASSET MANAGEMENT

WEEKLY INVESTMENT COMMENTARY

FEBRUARY 27, 2017 | VOLUME 5.9

Investors generally focused on the positives last week. They digested continued solid earnings reports and remained optimistic about President Trump's economic agenda. The S&P 500 Index rose 0.7%, marking its fifth consecutive week of gains.[1] At the same time, the Dow Jones Industrial Average capped off the week with 11 straight days of gains.[1] Treasuries also rallied, as yields moved lower for the week.[1]

Political Expectations May Be Too High

Equity prices have been rallying on expectations that the president and Congress will enact tax reform, fiscal spending and regulatory changes that will boost growth. However, President Trump's legislative agenda appears to be stalled. Health care reform seems delayed over timing and specifics. And tax and spending legislation appears caught in a battle between those favoring growth and those concerned about the budget. President Trump will likely focus on prioritization in his speech Tuesday night. But if his focus appears hazy or if real progress is lacking, equity markets may react more negatively to the political backdrop.

Weekly Top Themes

1. **The global inflation backdrop is shifting from deflation to reflation.** This trend began emerging in 2016 and accelerated after the U.S. elections. In our view, consumer prices are set to rise in many markets, while pending fiscal stimulus around the world should contribute to broader inflationary pressures.

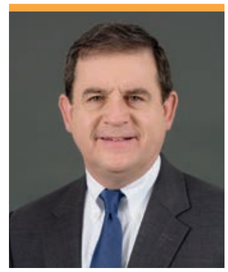
2. **Despite the recent decline, we expect Treasuries and other government bond yields to rise.** We think the 1.37% 10-year Treasury yield reached last summer marked a secular low, and we expect yields to move unevenly higher.

3. **Economic confidence may fade over the coming year.** Clarity around tax and regulatory policy would help, but we expect economic uncertainty to rise. Higher interest rates and a rising U.S. dollar could also be negative for the economy over time. Inflation is not yet problematic, but it may begin slowing global economic growth in the coming years

4. **The maturing economic cycle could benefit active equity management.** As tailwinds from monetary policy fade, equity markets should begin focusing more on company fundamentals such as earnings quality and specific valuation metrics. We believe this will increase dispersion between individual securities, which should benefit stock selection and active management.

KEY POINTS

- Stock prices continue to rally based on economic and political optimism.
- Over the coming year, we expect equities and bond yields to continue grinding unevenly higher.
- We remain constructive toward equities, but selectivity is growing more important.



Robert C. Doll, CFA

Senior Portfolio Manager,
Chief Equity Strategist

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

Where Can Investors Find Value in These Markets?

The recent behavior of equity and bond markets creates a conundrum for investors. Equity markets are rallying based largely on expectations for stronger economic growth, while bond yields have been falling and seem priced for economic stagnation. Which signal is correct? The economic environment may grow more complicated in time, but for now we expect acceleration to continue. The Federal Reserve is slowly tightening policy, but it would not move aggressively without a significant and unlikely inflation scare. Consumer spending and business investment are also rising, which should be positive for near-term economic growth.

The challenge for investors, however, is that few areas of the global financial market offer compelling value. Global equity markets are more expensive than several years ago and are probably fairly valued. Government bond yields are likely to rise, suggesting bond prices may be at risk. And very low short-term interest rates mean cash offers meager returns.

So what to do? We expect equity prices and bond yields to grind unevenly higher over the coming months. As such, we continue to expect equities to outperform bonds and cash. We believe a moderately pro-growth investment stance is warranted, given our expectation that economic growth and corporate earnings are both improving.

Within equity markets, we continue to believe U.S. stocks are better positioned than most non-U.S. markets. The eurozone, Japan and many emerging markets would appear to offer better long-term growth prospects, and international equities look generally more attractively valued. We expect equity market leadership to shift at some point, but for now U.S. stocks should benefit from stronger growth tailwinds. ■

2017 Performance Year to Date

	Returns	
	Weekly	YTD
S&P 500 Index	0.7%	6.1%
Dow Jones Industrial Average	1.0%	5.8%
NASDAQ Composite	0.1%	8.8%
Russell 2000 Index	-0.4%	2.9%
Euro Stoxx 50	-0.6%	0.9%
FTSE 100 (U.K.)	-0.2%	3.2%
DAX Index (Germany)	0.0%	3.0%
Nikkei 225 (Japan)	0.9%	4.9%
Hang Seng (Hong Kong)	0.0%	9.2%
Shanghai Stock Exchange Composite (China)	1.6%	6.0%
MSCI EAFE (non-U.S. developed markets)	-0.1%	4.2%
MSCI Emerging Markets	0.5%	9.5%
Bloomberg Barclays U.S. Aggregate Bond (bonds)	0.6%	1.1%
BofA Merrill Lynch 3-Month Treasury Bill (cash)	0.0%	0.1%

Source: Morningstar Direct and Bloomberg, as of 2/24/17. 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 indices are unmanaged and unavailable for direct investment.

"The challenge for investors is that few areas of the global financial market offer compelling value."

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

1 Source: Morningstar Direct, as of 2/24/17

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.

This material is not intended to be a recommendation or investment advice, does not constitute a solicitation to buy or sell securities, and is not provided in a fiduciary capacity. The information provided does not take into account the specific objectives or circumstances of any particular investor, or suggest any specific course of action. Investment decisions should be made based on an investor's objectives and circumstances and in consultation with his or her advisors.

A WORD ON RISK

This information represents the opinion of Nuveen Asset Management, LLC and is not intended to be a forecast of future events and this is no guarantee of any future result. Information was obtained from third party sources which we believe to be reliable but are not guaranteed as to their accuracy or completeness. 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 investments are subject to market risk or the risk that stocks will decline in response to such factors as adverse company news or industry developments or a general economic decline. Debt or fixed income securities are subject to market risk, credit risk, interest rate risk, call risk, tax risk, political and economic risk, and income risk. As interest rates rise, bond prices fall. Non-investment-grade bonds involve heightened credit risk, liquidity risk, and potential for default. Foreign investing involves additional risks, including currency fluctuation, political and economic instability, lack of liquidity and differing legal and accounting standards. These risks are magnified in emerging markets. Past performance is no guarantee of future results.

CFA® and Chartered Financial Analyst® are registered trademarks owned by CFA Institute.

Nuveen Asset Management, LLC is a registered investment adviser and an affiliate of Nuveen Investments, Inc.

GPE-BDCOMM4-0217P 23439-INV-W-02/18