The Environment for Equities Is Becoming Less Perfect

NUVEEN ASSET MANAGEMENT

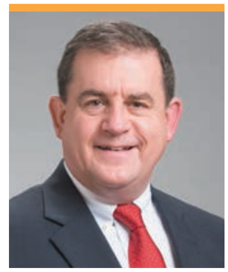
WEEKLY INVESTMENT COMMENTARY

NOVEMBER 13, 2017 | VOLUME 5.45

Market sentiment soured last week, snapping an eight-week equity winning streak, as the S&P 500 Index fell 0.1%.[1] Driving factors included scrutiny of the Time Warner/ATT merger, pressures in the high yield market, increased uncertainty over differences between the House and Senate tax reform plans and stronger focus on next year's midterm elections following strong Democratic gains in last week's contests. For the week, small caps and financials underperformed while defensive sectors and energy did well.[1]

Key Points

- Sentiment fell last week, causing stocks to end their eight-week winning streak.
- The current bull market is getting old, but we expect it should continue.
- Conditions are shifting, however, and we anticipate increased volatility and a more difficult environment for investors.



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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.

Weekly Top Themes

1. **Last week's elections signal possible trouble for Republicans in 2018.** We caution against reading too much into the results. But Democratic gains in Virginia and elsewhere confirm signals from national polling that suggest the GOP will struggle to hold the House next year.

2. **We expect a tax bill to be passed in 2018, which should help the economy and equity markets.** While there are significant differences between the two plans, the simple reality is that it would be political suicide for Republicans if they don't pass tax reform before next year's elections. Depending on the details of the final bill, we expect individual tax cuts to be a plus for consumption, while repatriation and corporate tax cuts should contribute to corporate revenues and earnings.

3. **Despite some views to the contrary, we believe the global economy should continue to improve.** Some argue the world is in a period of secular stagnation. After all, growth remains very slow despite years of low or even negative interest rates. In our view, the world economy is enjoying a period of reflation and should experience more synchronized growth in 2018.

4. **Stronger global growth is benefiting multinational companies.** These companies have reported stronger revenue and earnings results than domestically oriented companies this quarter.[1]

5. **The bull market in equities is aging but remains very much intact.** The current bull market is closing in on nine years, which makes it natural to ask how much longer it can continue. In our experience, there are several reasons for a bull market to end, including advanced Federal Reserve tightening, the flattening of the yield curve, slower levels of money growth, widening credit spreads and rising inflation. We are watching these factors closely, and don't see signals yet that would point to the end of the current run.

Equities May Struggle but Should Still Make Progress

For more than a year now, equity markets have enjoyed an unusual combination of low volatility and near-uninterrupted price gains due to a combination of accelerating economic growth, improving earnings, accommodative monetary policy and still-low inflation. This has been a near-perfect environment for stocks, but we think conditions could start to grow more difficult.

Economic growth should continue to improve, but expectations have risen, which means positive surprises will be harder to come by. At the same time, central bank policy is slowly tightening, which could contribute to market volatility. Additionally, accelerating growth and tighter policy may finally trigger an uptick in inflation, especially in wage inflation given the low level of unemployment. Should this occur, we expect bond yields will climb, which could jolt other financial assets including equity markets. We don't expect yields to rise unimpeded, but an ascending period of peaks and troughs looks likely.

Such a backdrop, combined with more lofty valuations for stock markets, could signal trouble for equities. Also, we think high yield bond spread movements tend to be a good forward indicator for stock markets. High yield spreads have widened slightly in recent weeks.[1] Should this continue, it could be bearish for stocks.

At this point, we think positive equity market momentum may be cresting, but we do not see the signals necessary that would presage the end to the bull market. As such, we think volatility is likely to rise and wouldn't be surprised to see a market correction or consolidation before prices can sustain another prolonged increase. To be clear, we aren't forecasting an end to the current economic cycle or to the equity bull market, but do think gains will be tougher to come by. As such, we would encourage investors to continue with a pro-growth investment stance and an overweight to equities, but we also to expect more bumps along the way. ■

2017 Performance Year to Date

Returns	Weekly	YTD
S&P 500 Index	-0.1%	17.3%
Dow Jones Industrial Average	-0.4%	21.0%
NASDAQ Composite	-0.1%	26.6%
Russell 2000 Index	-1.3%	9.9%
Euro Stoxx 50	-2.1%	24.4%
FTSE 100 (U.K.)	-0.6%	15.2%
DAX Index (Germany)	-2.1%	26.4%
Nikkei 225 (Japan)	1.2%	24.0%
Hang Seng (Hong Kong)	1.8%	36.5%
Shanghai Stock Exchange Composite (China)	1.6%	17.9%
MSCI EAFE (non-U.S. developed markets)	-0.4%	22.2%
MSCI Emerging Markets	0.2%	33.8%
Bloomberg Barclays U.S. Aggregate Bond (bonds)	-0.4%	3.0%
BofA Merrill Lynch 3-Month Treasury Bill (cash)	0.0%	0.7%

Source: Morningstar Direct and Bloomberg, as of 11/10/17. 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.

"Equity momentum may be cresting, but we don't see the signals necessary to presage the end of the bull market."

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1 Source: Morningstar Direct and FactSet, as of 11/10/17

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.

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