Improving Earnings and Profits Should Push Stocks Higher

NUVEEN ASSET MANAGEMENT

WEEKLY INVESTMENT COMMENTARY

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The devastation caused by Hurricane Harvey dominated the news last week. From an economic perspective, damage to the region's energy infrastructure is likely to cause local disruptions and contribute to a temporary increase in gasoline prices. But we expect the broader economic and market effect to be limited. Equity prices rose for a second straight week, with the S&P 500 Index up 1.4%.[1] Health care, technology and industrials led the way, while financials and bond proxies such as telecommunications and utilities fared the worst.[1]

Weekly Top Themes

1. **Payroll growth is likely to slow as the expansion moves into its later stages.** New jobs in August came in less than expected at 156,000[2] and we expect the pace of jobs growth may continue to trail off. Wage growth also remains slow, with average hourly earnings climbing just 0.1% for a 2.5% year-over-year rate.[2] Should jobs and wage growth remain constrained, the Federal Reserve may elect to hold off on another rate hike in 2017.

2. **Increased competition and improved productivity from mass retailers are helping to hold down inflation.** Retail innovations from companies like Amazon are an important factor keeping inflation below the Fed's 2% target. This is another reason interest rate increases may be delayed.

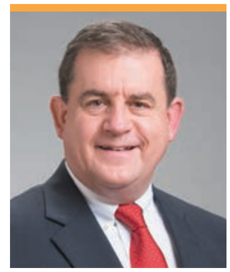
3. **Congress will likely pass a massive supplemental spending bill to help fund hurricane relief efforts.** Politically, the most interesting aspect may be whether the spending bill will also include language that increases the debt ceiling and a continuing resolution to fund the government. Should these elements be included, it would likely lessen the chances of a disruptive budget fight.

4. **Equity market risks appear skewed to the upside.** Persistently low volatility and the slow, if uneven, climb in prices suggest the stock market may be overdue for a correction. But we believe additional corporate earnings and profits growth should be boosted by improving manufacturing, solid jobs growth, increased capital spending and better and more synchronized global growth This should help equity prices.

5. **But several risks could derail markets.** Our list includes: 1) economic or earnings deterioration, 2) failure to pass tax reform, 3) a mistake in monetary policy, 4) a housing slowdown, 5) debt ceiling stress or a government shutdown,

Key Points

- Economic damage from Hurricane Harvey may cause near-term disruptions, but the broader effect should be limited.
- We see several risks investors should monitor, but expect rising corporate earnings should push stock prices higher.
- As such, we advocate sticking with a pro-growth investment stance.



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6) escalating tension in North Korea, and 7) technical deterioration in the markets.

Despite the Risks, We Advocate a Pro-Growth Stance

The summer has been quiet for financial markets, but we are starting to see rising tensions and mounting uncertainty. The global political environment in particular has become more troublesome as the situation in North Korea and the U.S. political environment both appear to be deteriorating.

At the same time, the Federal Reserve and European Central Bank have important meetings later this month. The Fed is widely expected to announce the start of balance sheet normalization while the ECB provides more clarity around tapering.

Against this backdrop of rising uncertainty, the value of the U.S. dollar has been falling sharply, oil prices have been churning, industrial metals prices have been rising and emerging markets equities have been outperforming. Together, these themes suggest that investors are growing less confident about the direction of the U.S. economy. Should confidence continue to deteriorate, it could begin to act as a headwind for U.S. equities.

We recognize the risks, but continue to believe that a pro-growth, risk-on investment stance is warranted, meaning we believe equities and other risk assets should continue to outperform. We expect the global economic expansion will continue, government bond yields will rise slowly, commodity prices will remain contained and corporate earnings will continue to rise.

Volatility will likely increase over the coming months, but the overall backdrop looks to us like a recipe for equities continuing to outperform bonds and cash. ■

2017 Performance Year to Date

	Returns	
	Weekly	YTD
S&P 500 Index	1.4%	12.2%
Dow Jones Industrial Average	0.9%	13.2%
NASDAQ Composite	2.7%	20.5%
Russell 2000 Index	2.7%	5.0%
Euro Stoxx 50	-0.1%	21.0%
FTSE 100 (U.K.)	1.1%	12.8%
DAX Index (Germany)	-0.5%	18.9%
Nikkei 225 (Japan)	0.3%	10.1%
Hang Seng (Hong Kong)	0.7%	30.1%
Shanghai Stock Exchange Composite (China)	2.4%	17.0%
MSCI EAFE (non-U.S. developed markets)	0.6%	18.0%
MSCI Emerging Markets	0.7%	29.1%
Bloomberg Barclays U.S. Aggregate Bond (bonds)	0.1%	3.5%
BofA Merrill Lynch 3-Month Treasury Bill (cash)	0.0%	0.5%

Source: Morningstar Direct and Bloomberg, as of 9/1/17. 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.

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1 Source: Morningstar Direct, as of 9/1/17 **2** Source: Bureau of Labor Statistics

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.

A WORD ON RISK

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