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U.S. equities rebound as investors focus on fundamentals

In a reversal from last week, U.S. equities experienced their best week since November 2020. Losses due to the volatility surrounding GameStop headlines were completely erased, as the S&P 500, Nasdaq and Russell 2000 all reached record highs. All 11 sectors experienced gains, 10 advancing by greater than 2%, with six advancing almost 5% or more.

HIGHLIGHTS

- **Equities rebounded in part because the market realized the recent impact of individual investors is likely not systemic, and hedge fund de-risking may have been excessive.**
- **Earnings have continued to exceed expectations, led by record revenues for Amazon and Alphabet.**
- **Johnson & Johnson filed for emergency-use authorization for its vaccine. Approval would make it the third viable vaccine available for distribution in the U.S.**



Saira Malik, CFA
CIO of Nuveen Equities

Saira Malik oversees the equities strategic direction for Nuveen as chair of the Equities Investment Council (EIC) and a member of Nuveen's Global Investment Committee (GIC). She has responsibility for equity portfolio management, equity research, equity trading, target date, quantitative and index strategies, as well as portfolio management responsibilities for global equity strategies.

Weekly overview

- *Headline job gains of 49,000 disappointed, coming in at roughly half of consensus expectations. December's report was revised down, as the lower unemployment rate of 6.3% was due to reduced labor participation, rather than employment growth.*
- *January's ISM Services PMI reading came out stronger than expected at 58.7, but expectations for a \$1 trillion-plus stimulus package remain elevated. Senate Democrats took steps to ensure passage using budget reconciliation rather than a vote on the floor.*
- *The dovish Federal Reserve continued to underpin the equity bull market. The central bank remains patient as it seeks to avoid tapering its purchase program too soon, which could damage the ongoing recovery.*

Market drivers & risks

- **Have we turned a corner on the coronavirus?** The U.S. reached a grim milestone in daily death counts, surpassing 5,000 for the first time. However, 7-day rolling averages of new COVID-19 cases have fallen by 50% since January 12, while hospitalizations are below 90,000 for the first time since November. These remarkable improvements coincide with the potential of a third vaccine approved for distribution by mid-March and a broader-reaching federal plan to administer vaccines.
 - These improvements bolster our confidence in a return to “normal” sooner rather than later. As a result, we believe cyclicals and small caps should continue to outperform, driven by a recovery in pandemic-sensitive industries and substantial earnings growth.



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- **Economic data is hitting a sweet-spot.** Equities were broadly higher on Friday, capping a week of strong returns, despite January headline employment significantly missing expectations as labor force participation contracted. Service industry PMI remained firmly expansionary, however.
 - Markets seemingly shook off the abysmal jobs report as evidence of the need for a larger stimulus package. The lack of job growth and substantial unemployment has been largely contained to relatively few industries (leisure/hospitality, health care and retail). A more robust package will likely reach beyond those Americans hardest hit by the pandemic, which should boost economic growth further as consumer activity returns.
- **Earnings continue to grow.** With 59% of companies reporting actual results, the S&P 500 is now reporting earnings growth of 1.7%, up from a decline of 2.4% the prior week. Should this trend continue, it will be the first time earnings will experience year-over-year growth since fourth quarter 2019.
 - More companies than average are reporting earnings growth and by wider margins than average. Of the 59% of companies reporting, 81% have reported earnings surprises and by an average of 15% more than expected. These numbers exceed their 5-year averages of 74% and 6.3%, respectively. The financial sector, making up 10.5% of the index, has contributed the most with a blended earnings growth rate of 17.2%.

Risks to our outlook

An increasing number of new coronavirus variants have proven to be more infectious and possibly more deadly. An uncontrolled spike in coronavirus-related metrics would likely cause rapid and severe volatility.

Stimulus-driven volatility will likely persist in the near-term as Congress works to pass the proposed \$1.9 trillion package. Though indications are pointing toward its passage, President Biden has expressed a willingness to negotiate some provisions, such as backing off the immediate goal of a \$15-hour minimum wage.

Secretary of Treasury Janet Yellen expressed confidence in the resiliency in America's financial infrastructure following a review of the GameStop-driven frenzy. Nonetheless, we think individual investors have the ability to create sudden market corrections in certain cases.

In focus

Consumers at the gate

The U.S. consumer is poised to play a significant role in supporting our modest risk-on positioning in 2021.

While difficult to imagine, the personal savings rate has risen to its highest level since World War II. Low interest rates, suppressed commodity prices, historic fiscal stimulus and curbed spending due to lockdowns have led to approximately \$2 billion in "excess" savings. We expect consumer spending will normalize rapidly as the impacts of vaccinations become more prominent, based on observations from geographies that have previously experienced declining COVID-19 cases and rapidly eased government restrictions.

Consumer industries have been among the most severely impacted by the pandemic. While many small businesses may close permanently, this dynamic ultimately favors larger, well-capitalized companies that have adapted quickly to the pandemic environment and enhanced cost controls. In the full-service restaurant industry, for example, we suspect larger players could divide 5% to 15% of market share previously controlled by smaller chains. Those that have adapted will most likely ultimately be rewarded by investors.

Expect investors to refocus on fundamentals. Consumer stocks have been driven to a large extent by the coronavirus-related narrative, the macroeconomic environment and investor positioning. Leading-edge fundamentals have not mattered in the way that they did in 2019. Consistent with our outlook for the broader market, we expect this dynamic to normalize in 2021 and beyond.



Best ideas

We believe U.S. small caps offer value, and remain favorable toward emerging markets equities. Overall, our key investment theme centers on looking for quality across geographies, sectors and industries. Dividend-paying (and growing) companies should remain attractive in a low-rate environment. However, we have observed an uptick in rates in 2021 and will monitor the space.

About the Equities Investment Council:

The Nuveen Equities Investment Council (EIC) includes the firm's senior equity portfolio managers averaging three decades of investing experience. The group brings global expertise across different styles of equity investing and provides value-added insights to Nuveen's investment process by refining and delivering the firm's collective equity market outlook, including key risks and drivers, to clients. Led by Saira Malik, CIO & Head of Equities, the team shares best global equities ideas, while focusing on individual areas of expertise to help generate alpha.

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

Sources

All market data from Bloomberg, Morningstar and FactSet
Employment data from the Department of Labor
Manufacturing data from the Institute for Supply Management.

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A word on risk

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 investing involves risk. Investments are also subject to political, currency and regulatory risks. These risks may be magnified in emerging markets. Diversification is a technique to help reduce risk. There is no guarantee that diversification will protect against a loss of income.

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