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Viewpoints from the Global Investment Committee
2Q | 2021 OUTLOOK

Welcome to the upside scenario

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OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.
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Our initial 2021 outlook featured the theme “*Dark tunnel. Bright light.*” as a way to indicate that while we saw a strong possibility for economic and market upside, we also thought the path to get there would be difficult. And while the global pandemic remains a humanitarian crisis, that upside scenario is happening more quickly than we expected. That’s good news, in some ways, but also brings with it different risks and challenges. As we move closer to the end of the tunnel, Nuveen’s Global Investment Committee still sees opportunities across asset classes and remains committed to offering our clients ideas for how to navigate financial markets — for today and tomorrow.

Views from the TIAA General Account	1
Welcome to the upside scenario	2 – 7
Five portfolio construction themes	8 – 9

Views from the TIAA General Account



Nick Liolis
CIO, TIAA General Account

As part of his participation in Nuveen's Global Investment Committee, Nick Liolis offers his views from the perspective of one of the world's largest institutional investors. Neither Nick nor any other member of the TIAA General Account team are involved in portfolio management decisions for any third party Nuveen strategies.

Rising rates, rising risks

This has been a challenging year for bond investors. The 10-year U.S. Treasury yield has almost doubled as inflation fears tick up on the back of a tumultuous 2020, when the U.S. Treasury and the Federal Reserve supported the economy and markets by buying bonds, injecting liquidity and keeping rates low. As inflation uncertainty increases and with it interest volatility and term premiums, will the Fed need to step in to align the markets with its forward guidance? How can the Fed anchor investor expectations? These questions are causing many investors (us included) to grapple with the uncertainty of future fixed income returns.

Even though we've arguably just been through one of the biggest economic shocks of our lifetimes, credit markets still seem to be enjoying the bull run that began way back in 2009. In usual cycles, most of the credit excesses are cleaned out in a recession. But that didn't happen in 2020. The equity markets took a hit early in the year but quickly recovered, bolstered by the Fed's and the Treasury's actions. Corporate defaults did not reach the levels expected (and were primarily focused in hard-hit COVID-related sectors) and the bull market in credit effectively continued, while corporations and governments took advantage of the environment and issued record amounts of debt.

This raises several questions: How will long will this last? What will happen when the cycle ends? And most importantly, how to manage for all of this? Our answer at TIAA's General Account is broader and deeper diversification.

In our credit portfolios, we're investing across a range of issuers, sectors and geographies across both public and private markets, relying on the in-depth research from the experienced teams at our investment managers. Real estate and other real assets also have a role as they can provide solid income generation, and in many cases inflation protection should inflation risks continue to increase.

The unanswered, and maybe unanswerable, questions about the bond market reinforce the need for resiliency in portfolios — and allowing for the flexibility to achieve your return objectives within your risk appetite. The GA's resiliency is built through a flexible framework of multi-tiered asset allocation processes and plans that provide protection from the many known and unknown risks we face. We are in a unique position compared with many investors, as the GA has a very long investment horizon. Our approach is to employ a multi-decade strategic asset allocation plan, an annual dynamic plan and a near-term tactical plan simultaneously.

The GA's strategic asset allocation provides guardrails designed to help us deliver on our core promises to our participants. Our annual dynamic asset allocation highlights investment areas of relative value and risks given the state of the markets. And our shorter-term tactical asset allocation allows us to respond to quickly shifting market conditions as we move up or down the risk spectrum, investing in assets that offer appropriate compensation for taking on that risk.

Asset allocation plans that allow investors to achieve return objectives through different market conditions help create resilient portfolios. The challenge is sticking to them when conditions are difficult. However, following these plans should improve the chances of long-term success.

Welcome to the upside scenario



Brian Nick
Chief Investment Strategist

- Led by a well-stimulated United States, global growth should surge by the most in decades this year as large developed economies sprint into the post-pandemic world.
- As we revise up our outlook for global growth, we must also consider the related risks, with inflation chief among them.
- Effective vaccines and enormous budget deficits notwithstanding, not all financial assets will benefit equally from an economic boom.
- The rotation into economically sensitive assets seems likely to endure in the context of strong balance sheets, surging economic growth and a sharp bounce in corporate profits.
- We see the best opportunities in emerging markets assets, as well as U.S. small cap stocks, leveraged loans and other floating-rate areas and across most real assets, including real estate.

“

Inflation could create risks, but we expect it to remain contained. At least for now.”

Three months ago, the Nuveen Global Investment Committee offered an optimistic outlook for the global economy and financial markets in 2021. Evidence since then suggests we may not have been optimistic enough. Multiple COVID-19 vaccines are inoculating a rapidly growing share of the global population. New cases have fallen off a cliff in most of the worst-hit countries. And the world's largest economy has added nearly \$3 trillion of extra stimulus, creating an unprecedented amount of pent-up consumer demand ready to be unleashed when the coast is clear. Welcome to the upside scenario.

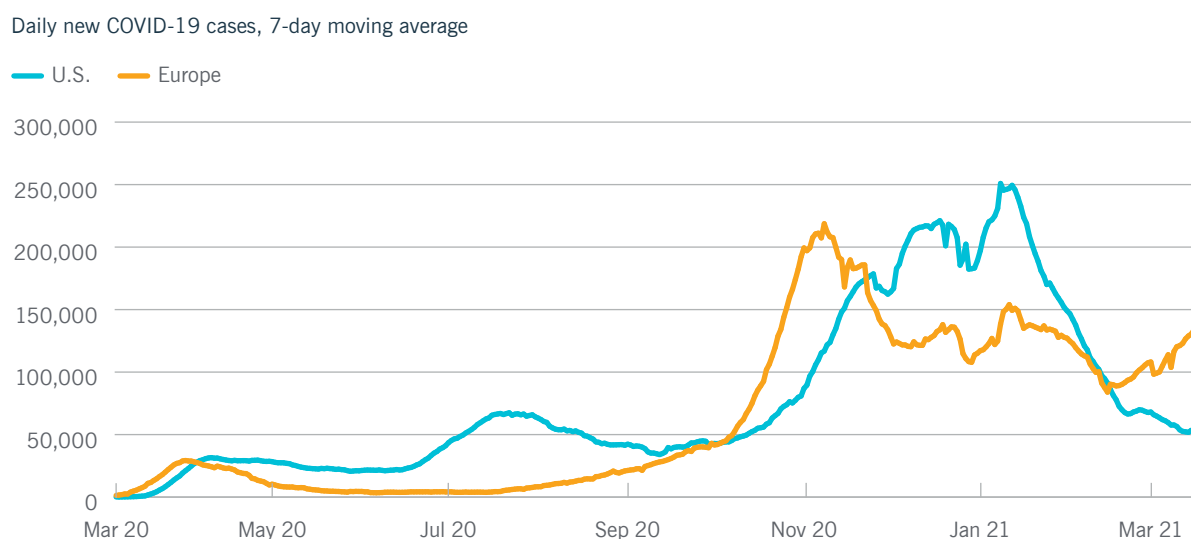
Brighter light, shorter tunnel

Economists and investors alike are busily revising up their already-high expectations for 2021. Fueled by a massive fiscal expansion and rapid vaccine deployment, the U.S. economy will set the pace this year, but the rest of the world won't be far behind. Economic data continues to consistently surpass expectations around the world, and in virtually every sector of the economy, from housing to manufacturing to labor.

So how did we arrive at this upside scenario? Fast and effective vaccinations and aggressive fiscal stimulus. Daily COVID-19 cases are well off their highs (Figure 1), and mitigation strategies are being rolled back in most places. The U.S. Senate flipping to the Democrats in January — again, unexpectedly — created a political alignment far more conducive to passing stimulus, which Congress promptly did with the American Rescue Plan Act signed in early March. Even before the various aid provisions in that bill took effect, personal income had spiked thanks to the previous fiscal relief bill (Figure 2), allowing both spending and savings rates to remain historically high.

Forecasts for economic growth have been pulled forward into the first half of this year, and financial markets have rotated — at times violently — out of last year's winners into more economically sensitive sectors, with energy the biggest winner so far. The highest global GDP growth in decades should translate into high corporate earnings growth, which will either ease equity market valuations, push stock prices higher or some combination of both (Figure 3). But we are also already seeing some of the downsides to the upside scenario. Improved growth expectations also mean rising interest rates and potentially higher inflation.

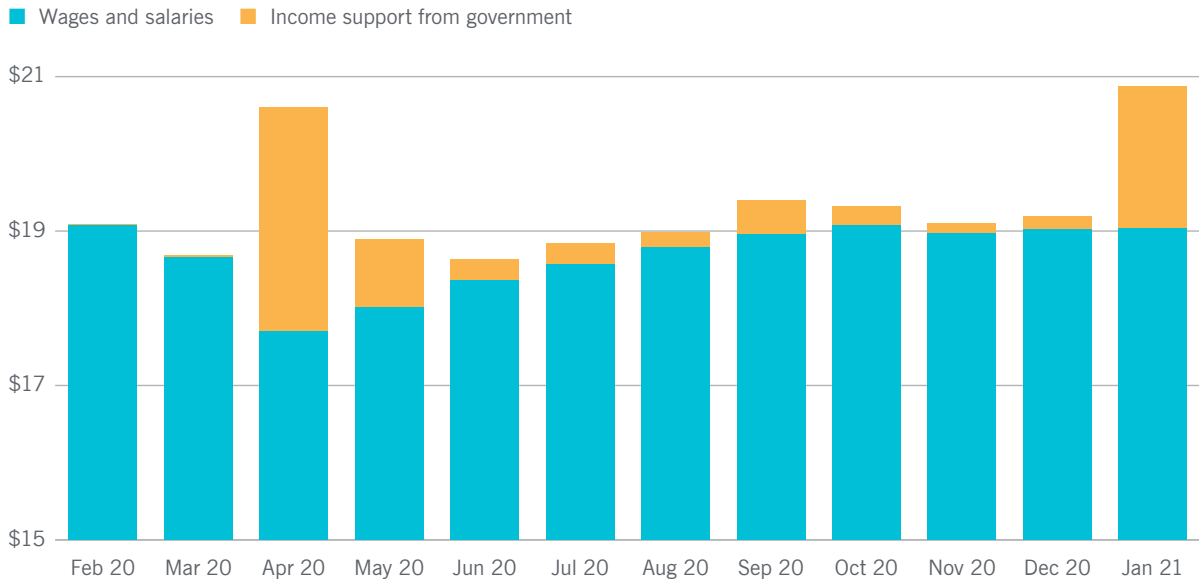
Figure 1 — COVID-19 cases are well off their highs in the U.S. and Europe



Source: Bloomberg, Johns Hopkins University, 01 Mar 2020 — 18 Mar 2021.

Figure 2 – U.S. personal income surged in January ... and is set to surge further

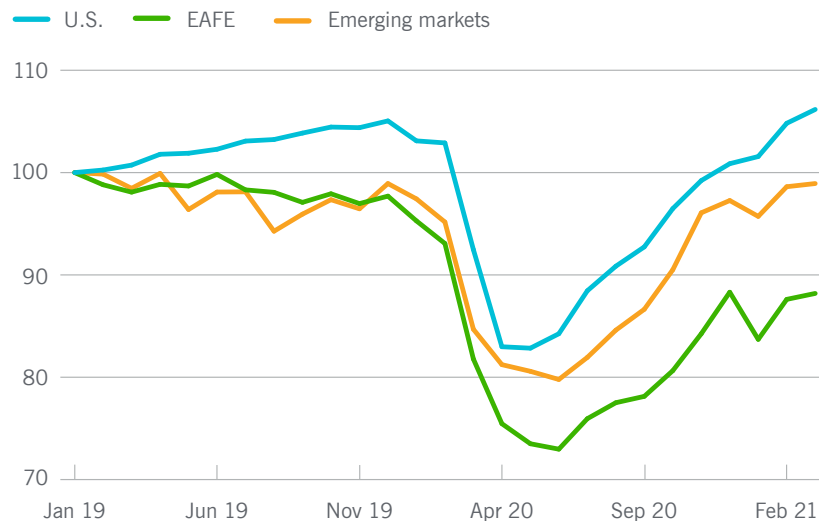
U.S. personal income, annualized (\$ trillions)



Source: Bloomberg, Bureau of Economic Analysis, January 2021.

Figure 3 – Corporate earnings expected to rebound strongly

MSCI Index 12-month forward earnings per share



Source: Bloomberg, MSCI, 01 Jan 2019 – 31 Mar 2021. Past performance is no guarantee of future results. Representative indexes: U.S., MSCI USA Index; EAFE, MSCI EAFE Index; Emerging markets, MSCI EM Index.

“Volatility may remain elevated, but we see opportunities across asset classes.”

“Upside risks” aren’t all good

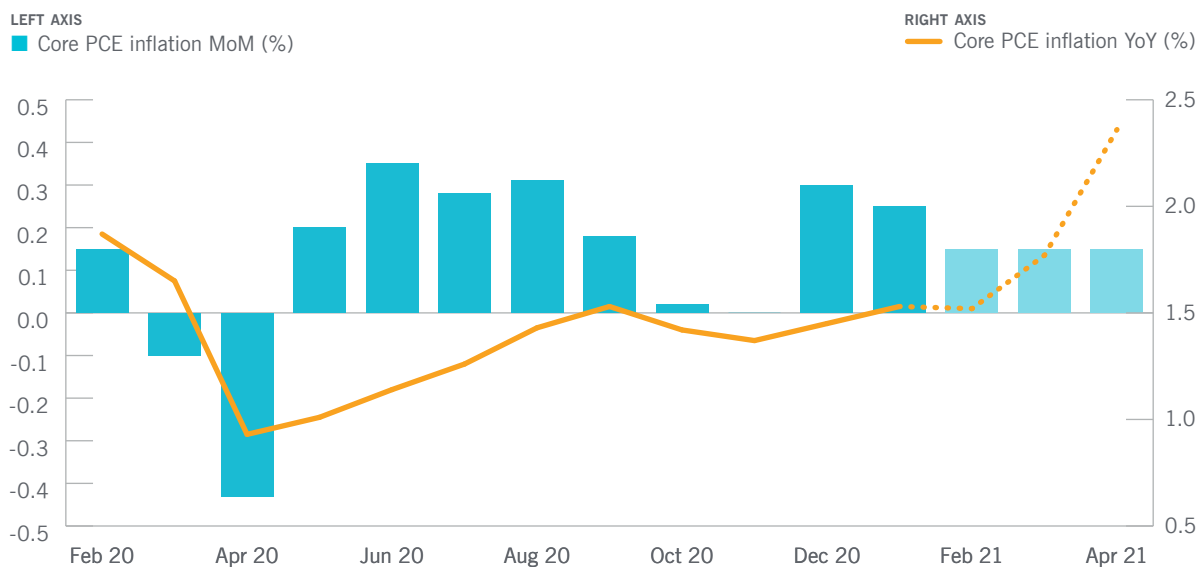
2021 is shaping up to be a fascinating case study in the relationship between economic growth and economic policy. Running fiscal and monetary policy ultra-loose in what was already expected to be the best year for growth in decades has never been tried before in a large, developed economy. Understandably, many investors are concerned that this formula could lead to inflation. In developed economies like the U.S., it’s an unfamiliar phenomenon to those who didn’t own financial assets before 1990. Rising prices can devastate consumer confidence and wreak havoc on investment portfolios, putting simultaneous downward pressure on both stock valuations and bond prices.

Inflation is almost certain to rise in 2021, but we expect it will do so only temporarily. Starting this spring, as last year’s extremely weak months roll out of the 12-month observation period, year-on-year inflation will almost certainly increase (Figure 4). Investors can safely ignore this data quirk, especially if monthly increases remain modest, as we expect they will.

Inflation may also rise this summer for more economically relevant reasons. As more consumers shift their spending from goods to services — eschewing home theater upgrades for meals out and vacations — we’re likely to see a relative shift in price pressures that could cause overall inflation to rise. This is especially true if businesses encounter difficulty quickly expanding their operating capacity in the face of a sudden increase in demand. Small business surveys already show this becoming an issue. Employers are having trouble finding new workers to fill open slots, and a large number expect to raise prices in the next few months. Job openings in the U.S. are more numerous than they were at the end of 2019. Central banks are unlikely to view such a phenomenon as a reason to urgently tighten policy, however. The overall increase in inflation is likely to be modest, and it should pass as supply rises to meet demand.

A broad-based and durable rise in inflation can only happen when an economy is running at full capacity or slightly beyond it. That is still a long way away for the world’s largest economies. In early 2020, as the U.S. economy was creating close to 200,000 jobs per

Figure 4 — Spring inflation “surge” will be a statistical quirk, not a worrisome trend



Source: Bloomberg, Bureau of Economic Analysis, Nuveen, January 2021. Dotted lines represent Nuveen forecasts.

month and the unemployment rate was dropping to 3.5%, inflation remained quite tame. Today, despite considerable progress since last April, the unemployment rate is 6.2% and over four million people have dropped out of the workforce altogether. This gives the Fed and other central banks facing similar conditions plenty of room to keep monetary policy easy for a good while longer. We do not expect the Fed or the ECB to reduce their asset purchases until the first quarter of 2022, at the earliest.

The reason the GIC spent so much time discussing inflation at our last meeting, however, is because we think risks are skewed toward overheating in 2021. Unprecedented fiscal expansion, along with a once-in-a-century positive demand shock to large segments of the economy, presents somewhat unknowable risks to financial assets. Some assets are well positioned for an economic boom and a moderately higher inflation environment. Others seem to have already incorporated this scenario into their prices. More important than successfully predicting inflation is knowing what types of investments are likely to perform well in a variety of inflation scenarios.

Where to focus if markets struggle to keep pace with the economy?

This year has already brought welcome news regarding the pandemic and the subsequent economic recovery. The trouble for investors is that much of this good news has already been priced into markets.

Figure 5 shows that the so-called “reflation trade” has gained momentum since last November, following the U.S. election results and the first news about the efficacy of several COVID-19 vaccines.

Markets are anticipating a strong global economic recovery, as well as higher inflation. Investments tied to those trends can continue to perform well, assuming the news continues to come in better than expected as it has in recent months. Better-than-expected economic data and faster-than-expected drops in new COVID-19 cases have boosted commodity prices, long-term interest rates and inflation expectations. They’ve also helped U.S. small cap stocks handily outperform large cap stocks, with the technology sector taking a



Broad diversification will be critical in this environment.”

back seat to energy and financials. Emerging markets assets have also received support, which is typical during periods of synchronous global economic growth, as long as sharply higher interest rates and a rising U.S. dollar don’t derail things.

We think the reflation trade — in its various forms — still has legs, but we advise investors to be more discerning in how they invest for the global reopening and recovery given the run many of these assets have already had.

Real assets like real estate, farmland and timberland are among our favored asset classes in a reflationary environment, especially given their inflation-resistant yield. We are investing in renewable energy infrastructure and U.S. housing in light of the sharp increase in demand for new construction and shifting demographics.

Within **equities**, we are emphasizing near-term opportunities in the financials and consumer-related sectors, while also keeping an eye on industrials that could benefit from publicly funded infrastructure investments. We remain bullish on U.S. small caps, emerging markets and cyclicals for the longer term as the economy reopens, but think those areas could be subject to volatility over the coming months. We see tactical opportunities in some growth stocks that have experienced recent underperformance.

In **fixed income**, while TIPS have outperformed nominal Treasuries as inflation expectations have increased, we prefer to take more risk in credit-sensitive parts of the market, including emerging markets. Improving fundamentals can help spreads compress even further, and higher-yielding parts of the market should prove less susceptible to a further increase in interest rates. Leveraged loans and other floating rate products are another preferred area for this reason.

One unmistakable feature of the first quarter was the increased interest in speculative investing among individual investors (as well as a handful of institutions). Intense interest in online trading

communities — in assets ranging from Bitcoin to Gamestop to silver — led to eye-popping rallies, some of which have proven to be more durable than others. With liquidity plentiful and average net worth at its highest level ever, many investors are willing to pay high prices — at times clearly divorced from fundamentals — for assets with no intrinsic value that generate no income as long as they believe they can sell them to the next buyer at a higher price.

Investments primarily, if not entirely, driven by speculation can be extremely volatile with inconsistent correlations to other asset classes. As such, they are difficult to incorporate into a diversified asset allocation and can be subject to sudden, severe losses. The bottom line: While we know it can be tempting to follow the latest trend or the hottest stock, we suggest remaining diversified and limiting exposure to any single asset or asset class.

Figure 5 — The so-called “reflation trade” cuts across virtually all markets



Source: Bloomberg, 01 Jan 2019 – 18 Mar 2021. Past performance is no guarantee of future results. Representative indexes: **Emerging markets currencies**: JPMorgan Emerging Markets Currency Spot Index; **Commodities**, Bloomberg Commodity Index; **Large caps**, Russell 1000 Index; **Small caps**, Russell 2000 Index, **TIPS**, 10-year U.S. TIPS breakevens.

A different type of uncertainty from here

If someone had told us six months ago that our primary focus in March 2021 would be on the risks surrounding inflation and rising interest rates, we would have been both surprised and delighted. But the truth is, as we exit a period of human and economic tragedy, we enter a new phase that will bring its own forms of uncertainty: rapid shifts in consumer behavior, unprecedented stimulus and a market less than a year removed from a recession already exhibiting some late-cycle tendencies.

We continue to see a range of opportunities for investors looking for yield and willing to diversify within their fixed income portfolios and into illiquid and alternative asset classes. Guarding that income stream against a rise in inflation — or inflation expectations — is moving up the list of necessities for all types of investors over the balance of 2021.

Five portfolio construction themes

The world has been moving through the “dark tunnel” more quickly than we expected a few months ago. While that is good news, it also brings risks and makes investment decisions challenging, as yields are rising and valuations look increasingly full across asset classes. So how to build portfolios? Nuveen’s Global Investment Committee offers portfolio construction themes for our clients to consider.

1 Expect reflation, not runaway inflation

A key question we’re hearing from clients is how to position portfolios in light of possible inflation risks. We are not seeing significant signs of higher inflation, but we think it makes sense to take advantage of the “reflation trade,” as global economic growth improves and yields are experiencing upward pressure.

In fixed income markets, valuations have returned to pre-pandemic levels in most sectors, and we think high yield, bank loans, preferred securities and emerging markets corporate bonds should perform well in a reflationary environment. We also see value in longer duration and high yield municipals. For public equity markets, we suggest focusing on areas such as U.S. small caps and emerging markets equities that appear attractive from a relative valuation perspective. Additionally, we see value in public and private industrial real estate and across real assets, areas that can act as a natural hedge should inflation start to rise.

2 It’s still all about income

Yields are creeping higher, but remain extremely low historically. The search for yield isn’t going away, and income generation will remain a challenge for institutional and individual investors around the

world. This means investors should consider different areas of the fixed income landscape, dividend-paying equities and alternatives such as real estate, real assets and private credit as tools to build a sustainable income portfolio.

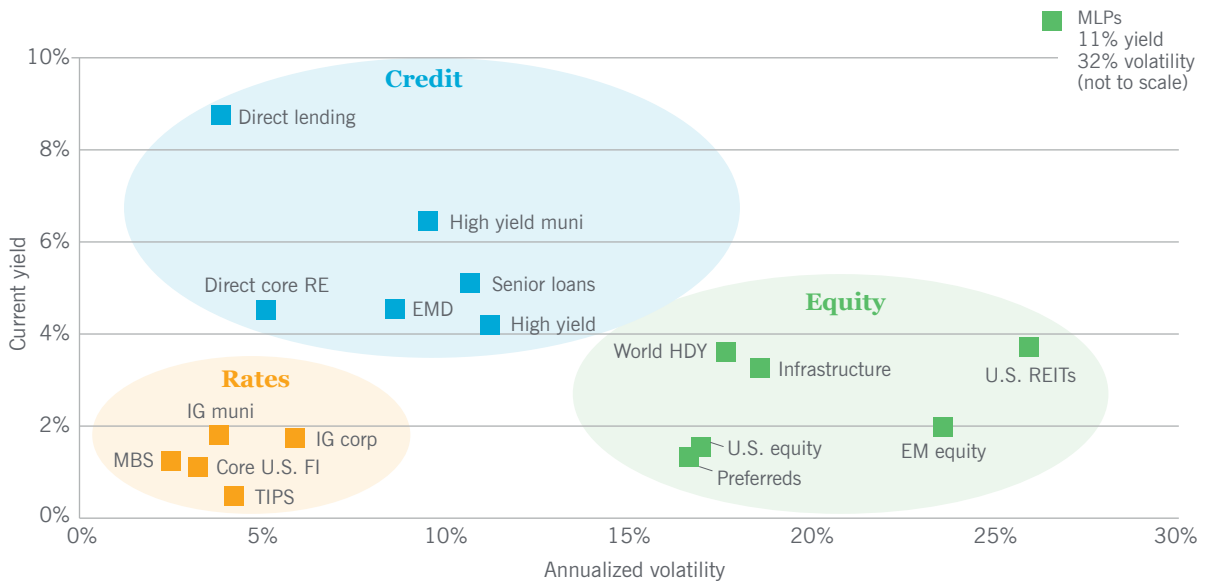
In casting this wider net, however, investors should understand which risks are entailed to generate more income and how these risks work together. Among a number of tools and options, we broadly categorize possible asset classes into buckets of interest rate risk, credit risk and equity risk. Each offers different yield and volatility profiles (Figure 6), and we suggest investors diversify across different income opportunities and risks.

3 Consider more illiquidity risk

In our observation, many (if not most) investors are under-allocated to alternatives in general and illiquid investments in particular. While many institutions have long leveraged the advantages of illiquid assets, we are also seeing a growing interest in private real estate and direct lending among individual investors.

We see compelling opportunities across the alternatives landscape, particularly middle market private debt, which looks attractive on both a valuation and fundamental basis. We also see value in alternative housing sectors, including single family rentals in the

Figure 6 — A broader reach can help achieve income goals



Source Bloomberg, L.P., 31 Dec 2020. **Past performance is no guarantee of future results.** Desmoothed volatility is 18% for direct core real estate and 5% for direct lending, which accounts for less frequent marked to market pricing. **Representative indexes: core U.S. fixed income:** Bloomberg Barclays U.S. Aggregate Bond Index; **U.S. TIPS:** Bloomberg Barclays U.S. TIP 1-10 year Index; **mortgage-backed securities:** Bloomberg Barclays U.S. Mortgage-Backed Securities Index; **investment grade municipals:** Bloomberg Barclays U.S. Municipal Bond Index; **U.S. equity:** S&P 500 Index; **world high dividend (HDY):** MSCI World High Dividend Yield Index; **U.S. REITs:** MSCI US REIT Index; **emerging markets equity:** MSCI Emerging Market Index; **direct core real estate:** NCREIF Property Index; **emerging markets debt:** JPMorgan Monthly EMBI Index; **high yield municipals:** Bloomberg Barclays High Yield Municipal Index; **preferred securities:** BofA Merrill Lynch Preferred Stock Fixed Rate Index; **senior loans:** Credit Suisse Leveraged Loan Index; **high yield corporates:** Bloomberg Barclays U.S. Corporate High Yield 2% Issuer Capped Index; **infrastructure:** S&P Global Infrastructure Index; **direct lending:** CDLI Total Return Index. MLPs: Alerian MLP Total Return Index. Municipal bond yields are taxable equivalent at 37% + 3.8% ACA tax rates.

United States and build-to-rent housing across Europe. Select farmland and timberland investments also look compelling, as investors increasingly look to benefit from low carbon investments.

Choosing illiquid investments can be especially tricky, as investors must consider such factors as frequency of pricing and how different investments work within an overall portfolio. It is important that investors understand their illiquidity tolerance, ensuring that investment time horizons match their need for capital. But taking on additional liquidity risk in exchange for diversification and return potential is a strategy we think investors should consider.

4 Lean into ESG themes for alpha and risk management

Investors have been increasingly focusing on environmental, social and governance factors in recent years. And for good reason: For us, ESG investing is not about excluding certain types of investments, but rather a tool to help generate returns and manage risks.

During the pandemic, we saw how strong corporate governance, business continuity, human capital and supply chain management were critical to drive performance across asset classes. And we don't see that changing. We are finding tremendous opportunity in areas such as renewable energy, clean technology, food sustainability and investments that focus on diversity, inclusion and employee well-being across public and private markets.

5 Harness the advantages of active management

This final theme may be the most important. Volatility will likely remain elevated, and in an environment of relatively full valuations and rising interest rates, long-term portfolio returns could be somewhat muted. Across asset classes, all members of our Global Investment Committee and portfolio management teams are finding investment ideas that are highly idiosyncratic and fast-moving.

Selectivity, research, nimbleness and confidence could all matter more in the coming years.

About Nuveen's Global Investment Committee

Nuveen's Global Investment Committee (GIC) brings together the most senior investors from across our platform of core and specialist capabilities, including all public and private markets. Quarterly meetings of the GIC lead to published outlooks that offer:

- macro and asset class views that gain consensus among our investors
- insights from thematic “deep dive” discussions by the GIC and guest experts (markets, risk, geopolitics, demographics, etc.)
- guidance on how to turn our insights into action via regular commentary and communications.

For more information, please visit nuveen.com.

Endnotes

Sources

All market and economic data from Bloomberg, FactSet and Morningstar.

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Such information may include, among other things, projections, forecasts, estimates of market returns, and proposed or expected portfolio composition. Any changes to assumptions that may have been made in preparing this material could have a material impact on the information presented herein by way of example. **Past performance is no guarantee of future results.** Investing involves risk; principal loss is possible.

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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. Investing in municipal bonds involves risks such as interest rate risk, credit risk and market risk, including the possible loss of principal. The value of the portfolio will fluctuate based on the value of the underlying securities. There are special risks associated with investments in high yield bonds, hedging activities and the potential use of leverage. Portfolios that include lower rated municipal bonds, commonly referred to as “high yield” or “junk” bonds, which are considered to be speculative, the credit and investment risk is heightened for the portfolio. Credit ratings are subject to change. AAA, AA, A, and BBB are investment grade ratings; BB, B, CCC/CC/C and D are below-investment grade ratings. As an asset class, real assets are less developed, more illiquid, and less transparent compared to traditional asset classes. Investments will be subject to risks generally associated with the ownership of real estate-related assets and foreign investing, including changes in economic conditions, currency values, environmental risks, the cost of and ability to obtain insurance, and risks related to leasing of properties. Socially Responsible Investments are subject to Social Criteria Risk, namely the risk that because social criteria exclude securities of certain issuers for non-financial reasons, investors may forgo some market opportunities available to those that don't use these criteria. Investors should be aware that alternative investments including private equity and private debt are speculative, subject to substantial risks including the risks associated with limited liquidity, the use of leverage, short sales and concentrated investments and may involve complex tax structures and investment strategies. Alternative investments may be illiquid, there may be no liquid secondary market or ready purchasers for such securities, they may not be required to provide periodic pricing or valuation information to investors, there may be delays in distributing tax information to investors, they are not subject to the same regulatory requirements as other types of pooled investment vehicles, and they may be subject to high fees and expenses, which will reduce profits. Alternative investments are not appropriate for all investors and should not constitute an entire investment program. Investors may lose all or substantially all of the capital invested. The historical returns achieved by alternative asset vehicles is not a prediction of future performance or a guarantee of future results, and there can be no assurance that comparable returns will be achieved by any strategy.

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