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# Equity volatility picks up amid higher inflation data

*Global equity markets declined last week, notching their worst weekly loss since the last week of February. Broad-based indexes tracking developed markets fared better, as the S&P 500, DJIA and MSCI EAFE fell between 1.0% and 1.4%, while the tech-heavy NASDAQ and the MSCI Emerging Markets indexes fell 2.3% and 3.0%, respectively.*

## HIGHLIGHTS

- **Headline CPI rose more than 4% year-over-year, and was up 0.8% month-over-month for April, while the core index rose 3.0% and 0.9%, respectively, over the same time periods.**
- **Following the prior week's disappointing employment data, initial jobless claims fell to a recovery-low of 473,000 while job openings increased.**
- **April retail sales were largely flat relative to March, although restaurants notably showed growth, while preliminary consumer sentiment fell in May on inflation fears.**



**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.

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## Weekly overview

- *The hotter-than-expected inflation data sparked an early-week selloff, although most indexes rebounded on Thursday and Friday. The S&P 500 gained over 1% on those days.*
- *Cyclicals outperformed, with financials (+0.3%), materials (+0.1%) and energy (-0.4%) topping the list. Conversely, growth and technology were the biggest losers: Consumer discretionary, information technology and communication services lost between 2% and 4%. Value and large caps outperformed growth and small caps.*
- *Both global and U.S. equities have experienced strong inflows so far this year. Investors appear to be looking past rising volatility and focusing on the positives of high liquidity, ongoing stimulus and growing confidence in the economic recovery.*

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## Market drivers & risks

- **Inflation concerns rise.** Equity market volatility rose significantly as inflation data ticked higher.
  - Although markets extended losses through Wednesday due to the larger-than-expected rise in consumer prices, equities recovered later in the week thanks to modest declines in commodity prices, including a commitment from the Chinese government to keep the cost of iron ore under control. Oversold conditions also likely helped the late-week rebound.
- **It's a supply issue.** In last week's commentary, we stated our belief that the April employment miss was likely due to a supply issue, not a lack of demand. As we continue to move away from



***While increasing inflation pressures are causing volatility, we expect the risks will be contained.***

the disappointing report, we grow more confident in this view.

- It appears likely to us that historic levels of stimulus and COVID-related fears remain major headwinds for understaffed businesses. Last week a number of notable headlines supported our theory: 1) the CDC's surprise announcement allowing vaccinated persons to no longer wear masks or practice social distancing; 2) the Jobs Opening and Labor Turnover Survey that showed over eight million unfilled job openings; 3) businesses beginning to offer wage increases, either through one-time bonuses or permanent wage hikes.
- **What's next?** It seems like a confluence of data shocks and lofty expectations have led to a "sell in May" environment. The S&P 500 has continued to hit record highs in 2021 thanks in large part to the ongoing recovery in the global economy. As a result, much of the anticipated recovery may have already been priced in, leaving equities vulnerable to higher volatility.
  - The global economic recovery is continuing, although at a rate less predictable than hoped. Earnings growth reached approximately 50% for the first quarter of 2021, and while we don't expect growth to continue at this level, valuations should compress considerably and ease concerns of an overvalued market. Our focus remains on identifying high quality companies with strong or improving fundamentals and earnings growth tied to the economic expansion.

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## Risks to our outlook

Though a disappointing employment report helped to support the Fed's "wait and see" approach to tapering, last week's surprisingly high CPI readings had the opposite effect. Chair Powell may be forced to make tapering comments if the transitory period of inflation persists.

The debate over tax reform is heating up as both political parties continue to express a willingness to negotiate. Any negativity surrounding these negotiations, as well as the legislative battle for an infrastructure package, will likely create pockets of volatility.

The CDC's announcement regarding easing safety measures for vaccinated people was welcomed by many. But there is a risk that if more relaxed measures lead to an increase in COVID-19 cases, markets would likely react poorly.

## In focus

# Commodity inflation gyrations

Commodity prices have increased sharply since the 2020 pandemic-driven lows. The supply of agriculture products, metals, lumber and basic chemical products had all been curtailed in anticipation of a large reduction in demand that never materialized. In fact, demand actually rose in some cases, such as lumber and paint for residential construction and DIY projects. We are now seeing spikes in inflation data that have led to increased market volatility.

Demand for certain commodities will likely remain high due to a variety of idiosyncratic circumstances, such as high growth levels of Chinese livestock that consume large amounts of agricultural goods or the growth of electric vehicles that require the use of specialty metals. Additionally, prices may remain elevated in some cases due to inherently slower "restocking" processes, such as in soybeans and corn. Overall, however, we expect the effects of commodity-driven inflation to be limited.

In this environment, we think it is critical to focus on underlying supply and demand trends for each commodity to judge the pace of 'normalization' as economies begin to reopen. Though the magnitude and duration of this inflation spike may be greater than originally anticipated, it should ultimately prove transitory. These pricing pressures should dissipate as supply chains recover and discretionary income shifts away from goods and commodities toward services and experiences, leading to a cooling of peak spot prices and a reduction in equity market volatility.



## Best ideas

*Improvements in vaccinations and economic reopenings, paired with recent underperformance, makes U.S. small caps particularly attractive. We also remain bullish on emerging markets, as higher inflation readings help the asset class and new COVID-19 cases are plateauing. We continue to favor consumer service sectors, and we are keeping an eye on industrials that could benefit from publicly funded infrastructure investments. Tactical opportunities remain in technology and growth stocks, however with a greater degree of selectivity as the "shelter-in-place" trade may no longer provide a sweeping benefit to all companies.*

## 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](https://nuveen.com).**

### Sources

All market data from Bloomberg, Morningstar and FactSet

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