

16 Aug 2021

Equities rally as economic and virus news shifts

Global equities were generally positive as inflation data cooled and markets eyed a potential peak in Delta variant cases. The S&P 500 ended the week at another all-time high, and on Friday the STOXX Europe 600 notched its tenth straight day of gains. Both the S&P 500 (+0.8%) and DJIA (+0.9%) rose, while the Nasdaq (-0.1%) edged lower. Non-U.S. developed markets (+1.6%) outperformed emerging markets (-0.9%), although Chinese equities (+1.7%) advanced despite regulatory concerns.

KEY POINTS

- **CPI inflation cooled in July, which we attribute to shifts in spending from goods to services, while PPI was hotter on continued supply chain issues.**
- **We think companies with pricing power will be able to preserve decade-high profit margins.**
- **Consumer sentiment posted its lowest reading since 2011, but equity markets were unfazed. Further strength in payrolls and manufacturing data should boost confidence and cyclical stocks.**
- **U.S. Delta variant cases may peak this month, prompting investors to refocus on Fed tapering.**



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.

Market drivers & risks

- **CPI inflation was lower than expected in July.** The slowdown in consumer prices was welcome news for markets, and supports the views of central bankers and others who have deemed this year's higher inflation numbers to be transitory.
 - Despite the deceleration in both headline and core CPI, bottlenecks remain in the economy. Base effects from relatively small CPI increases in the second half of 2020 could keep readings elevated for the balance of this year.
 - If the August jobs report comes in strong, we continue to believe the Fed will announce that it plans to begin tapering its asset purchases starting in the first quarter of 2022. We expect no rate hikes until 2023.
- **Demand for workers is at a record high.** There are currently more job openings in the U.S. than people unemployed.
 - The Job Openings and Labor Turnover Survey (JOLTS) hit another record in June 2021, with the number of open positions increasing by 590,000, to 10.1 million. This demand for labor is unprecedented, representing the highest level since the tracking of JOLTS data began in 2000.
 - The “quits” rate increased to 3.0%, just below its all-time high in April 2021, suggesting that workers are confident leaving their jobs. We expect this rate will decrease as enhanced unemployment benefits end.
 - Perhaps the most important signal from this data is that payroll growth should continue because of the tailwinds created by strong underlying business confidence. While the JOLTS report lags the payroll data by a month, it offers details about where the labor market's rebound is accelerating and where it faces challenges.
- **The U.S. Senate passes a \$1.1 trillion infrastructure package.** Passage of the



Market volatility will likely remain high in the near term as investors assess peak earnings growth, high valuations, yield curve movement and the spread of the Delta variant.”

bipartisan bill last Tuesday could be a catalyst for some companies to trade higher.

- While the bill still needs to be voted on in the House, it includes funding for existing projects as well as an additional \$550 billion over several years for new ones, largely focused on traditional infrastructure such as transportation. Searching for additional beneficiaries of this increased infrastructure spending is one way investors are diversifying their portfolios. Beyond the more obvious candidates (e.g., materials and industrials companies), there may be other sectors traditionally less associated with infrastructure that could also benefit such as utilities and REITs.

Highlights from last week

- Ten of the 11 GICS sectors gained last week. Materials performed best (+2.7%), followed by consumer staples (+2.1%) and financials (+1.9%). Energy (-0.4%) was the sole decliner. Large caps (+0.6%) outperformed small caps (-1.1%), while value (+1.1%) topped growth (+0.1%).
- Cyclical and value fared well despite continuing concerns about the Delta variant.
- Earnings season continued to wind down with elevated beat rates, a few cautious comments around the Delta variant and some debate among strategists about the sustainability of record margins amid persistent supply chain and input price pressures.

Risks to our outlook

The continuing spread of the COVID-19 Delta variant remains at the forefront. While elevated case counts, hospitalizations and deaths carry a heavy human cost and pose a potential threat to continued economic reopening, there are signs that Delta may be nearing its peak in the U.S. In China, another key port closure due to the virus has become a source of concern, although some data suggest the current outbreak there may be waning.

The University of Michigan's gauge of consumer sentiment unexpectedly tumbled to a preliminary August reading of 70.2 from a final July reading of 81.2. In our view, this drop — driven mainly by Delta variant worries — is temporary and likely to reverse on the strength of multiple economic growth indicators.

We maintain our view that equity markets are likely to remain highly susceptible to pullbacks and may react negatively to economic data that misses consensus expectations.

Despite these challenges, global equity markets proved again last week that they can be resilient when underlying fundamentals are strong.

In focus

Chinese equities: opportunities amid regulatory uncertainties

While the Chinese government has long intervened in its country's technology sector, the scope and frequency of recent regulatory tightening has surprised equity markets.

In July, policies targeting the IPO of ride-sharing service Didi and the education sector raised concerns that the government may impose its views regardless of the consequences on other areas of the market.

In China's technology sector, regulations put guardrails around companies, but are not intended to impair an industry that makes up 3% of GDP and is seen as the country's path to prosperity. Some foreign investors interpret the recent changes as a move to prioritize social policy goals rather than promote economic growth. It will take time to assess the government's attempts to enable profit-making by tech companies while limiting their degree of social influence. Earnings estimates for these companies should be adjusted accordingly.

We think investors should focus on companies with tangible valuation and strong cash flows that may provide a cushion to preserve capital and generate returns in an uncertain environment.

The bottom line: It's important not to overestimate the severity of China's regulations or their potential impact. And even if this environment persists for some time, we think it will moderate. Chinese equities have always come with more volatility than other markets, but select companies offer compelling opportunities.



Best ideas

Valuation differences are leading to opportunities in developed non-U.S. markets, particularly in Europe, which is experiencing higher COVID-19 vaccine uptake and should benefit from strong earnings growth and a more cyclically oriented economy. We also remain bullish on emerging markets, specifically Brazil, which offers opportunities tied to growth in the global digital economy, including innovative fintech and e-commerce names. In the U.S., passage of the infrastructure bill in the Senate and expectations for higher yields could lead to outperformance for cyclical sectors and small caps.

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 EIC 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.

This material is not intended to be a recommendation or investment advice, does not constitute a solicitation to buy, sell or hold a security or an investment strategy, and is not provided in a fiduciary capacity. The information provided does not take into account the specific objectives or circumstances of any particular investor, or suggest any specific course of action. Investment decisions should be made based on an investor's objectives and circumstances and in consultation with his or her financial professionals.

The views and opinions expressed are for informational and educational purposes only as of the date of production/writing and may change without notice at any time based on numerous factors, such as market or other conditions, legal and regulatory developments, additional risks and uncertainties and may not come to pass. This material may contain "forward-looking" information that is not purely historical in nature.

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.

All information has been obtained from sources believed to be reliable, but its accuracy is not guaranteed. There is no representation or warranty as to the current accuracy, reliability or completeness of, nor liability for, decisions based on such information and it should not be relied on as such. For term definitions and index descriptions, please access the glossary on nuveen.com. **Please note, it is not possible to invest directly in an index.**

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.

CFA® and Chartered Financial Analyst® are registered trademarks owned by CFA Institute.

Nuveen provides investment advisory services through its investment specialists.

This information does not constitute investment research as defined under MiFID.

nuveen

A TIAA Company