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CIO Weekly Commentary
10 October 2022

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Real estate offers a shelter from inflation

Bottom line up top:

Inflation consternation drives market gyrations. It's indisputable that the direction of global investment markets continues to hinge on the expectations for (and reality of) inflation. For proof, look no further than the July jolt versus the September swoon. While we anticipate inflation data to remain a potential source of volatility, we remain confident that the 9.1% year-over-year increase observed in June's U.S. Consumer Price Index will ultimately prove to be peak inflation.

The bigger they are, the harder CPI falls (or rises). This summer's inflation cool down was largely predicated on rapidly falling gasoline prices (Figure 1), which represent one of the largest individual components of CPI at approximately 5%. Unfortunately, investors were ill-prepared for August's disappointingly-elevated CPI reading, driven by measures of the cost of shelter – up 0.7% from July and 6.3% year-over-year. Measured by owner's equivalent rent (22% of CPI – roughly reflective of the price of single family homes) and rent of residence (7% of CPI – the actual rents people pay), shelter inflation measures can take a year or more to reflect market conditions. Deceleration in both housing and rental markets suggest lower inflation readings in the future. But even as the rate of growth moderates, current pricing levels may prove sticky.

Opportunity knocks for commercial real estate. Adding exposure to direct real assets, particularly farmland, has been one of our highest-conviction investment views in 2022. Building on that theme, we believe investors can benefit from increasing their exposure to residential areas of the commercial real estate universe, especially rental markets. The relatively excessive cost of homeownership should

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On behalf of Nuveen's Global Investment Committee

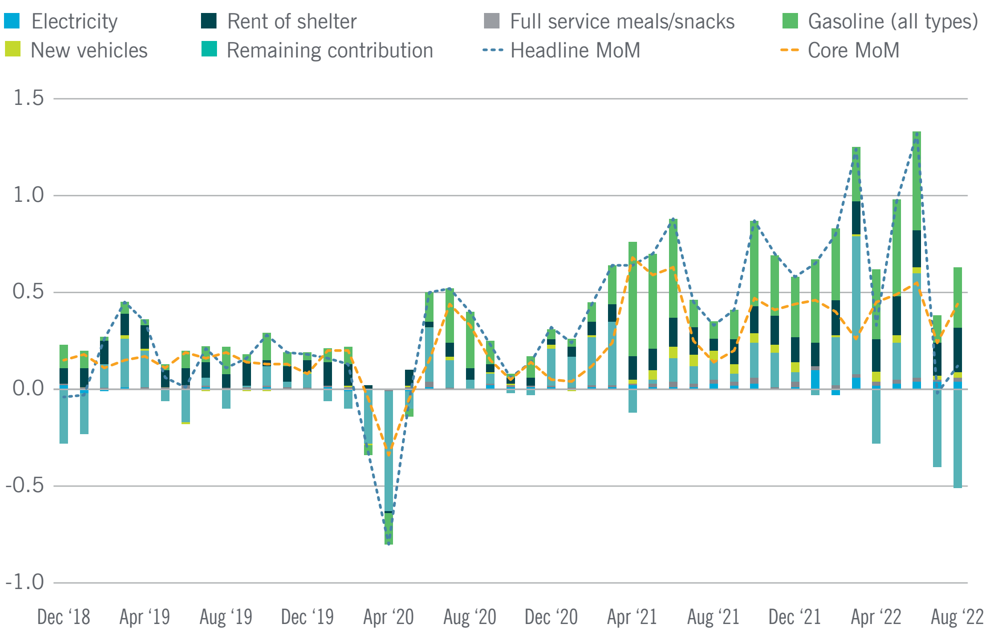
As Nuveen's CIO and leader of our Global Investment Committee, Saira drives market and investment insights, delivers client asset allocation views and brings together the firm's most senior investment leaders to deliver our best thinking and actionable investment ideas. In addition, she chairs Nuveen's Equities Investment Council and is a portfolio manager for several key investment strategies.

continue to translate into stronger demand for rentals (as well as resiliency in the level of cash rents) even as growth moderates. U.S. rental vacancy rates, for example, are historically low even as supply increases, which is another reason to believe upward price pressure will persist (Figure 2).

Investments in direct real estate offer a possible way to take advantage of persistently high inflation.

FIGURE 1: IT'S NOT JUST ENERGY: HIGH RENTS HAVE ALSO BEEN DRIVING INFLATION

Changes in month-over-month U.S. CPI and key subcomponent contributions



Data source: Bloomberg L.P., Dec 2018 to Aug 2022.

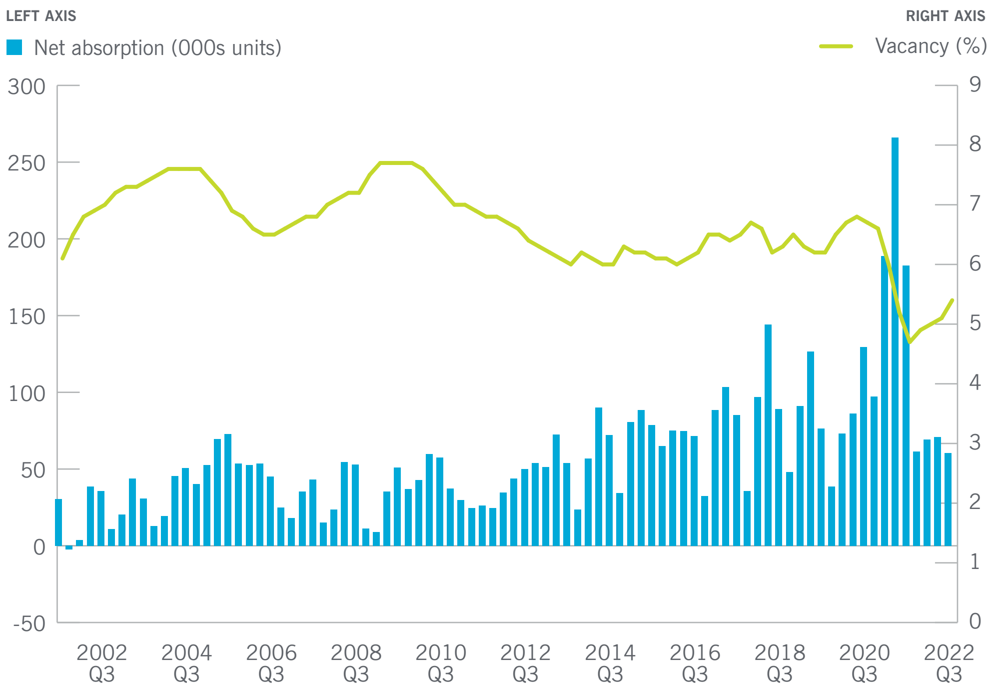
Portfolio considerations:

When the rate market sneezes (as it has this year), other asset classes are at risk of catching a cold; and commercial real estate is no exception. However **strong real estate fundamentals may help to provide some natural immunity to higher financing costs and any potential negative valuation adjustments**, particularly in the U.S. rental housing sector. Below-average vacancies in 43 of the top 50 U.S. cities continue to enable landlords to increase rents to offset higher operating costs. On the demand side, elevated home prices and the 30-year fixed rate mortgage's ascent to 7% means that the cost to rent has never been more attractive relative to the cost to own a home.

While macro headwinds will continue to impact markets into 2023, **U.S. apartments and single-family rentals may be a source of shelter from inflation-induced volatility** due to low vacancies and strong renter dynamics.

FIGURE 2: HOUSING LOOKS LIKE A SOLID INFLATION HEDGE

U.S. rental property unit growth and vacancy rates



Data source: CoStar, Sep 2001 to Sep 2022. **Net absorption** refers to the quarter-over-quarter change in occupied real estate space.

Strong fundamentals, low vacancy rates and high ownership costs should help the U.S. rental sector.

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.

Regular 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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