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CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Infrastructure investments could help bridge a recession gap

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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.

Bottom line up top:

What's going on with the economic data? The numbers are looking more than a little jumbled right now, but we think the latest U.S. releases are pointing to a combination of moderating inflation and an economy that remains hot in parts but is showing signs of strain. On the inflation front, October's Personal Consumption Expenditures Index — the Federal Reserve's preferred barometer of inflation — rose an annualized 6%. That's still pretty high, but it does show easing from prior months and lends credence to our view that inflationary pressures are receding. For the economy, the November ISM Service Sector Index climbed to a higher-than-expected 56.5, well above the 50 level separating expansion from contraction. And last month's employment report showed a much stronger increase in new jobs and a sharp rise in average hourly earnings. The consumer sector remains in decent shape thanks to the tightness of the labor market, but declining saving rates and rising debt burdens reveal some cracks.

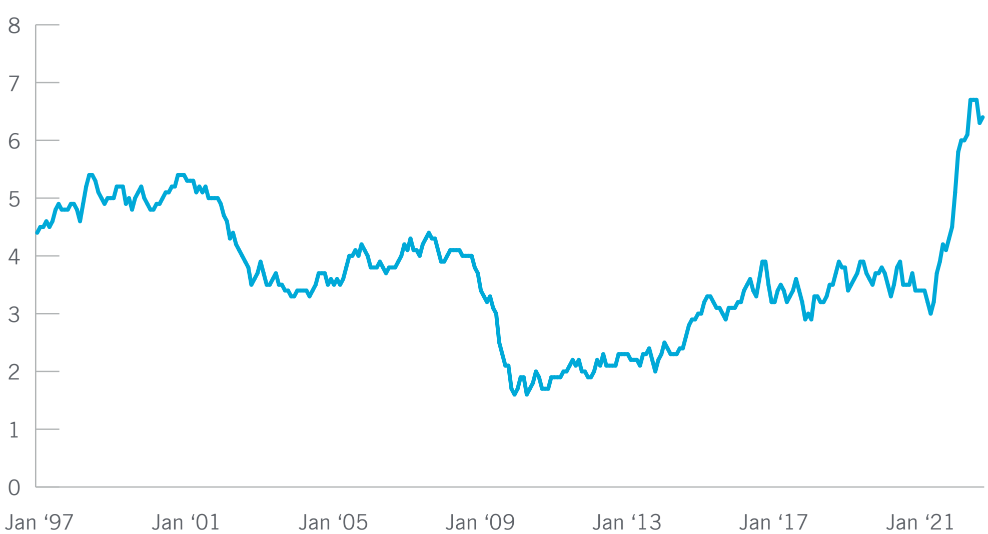
And what's the Fed going to do? The policy outlook remains a wildcard. Outsized rate hikes may finally be getting a hold on inflation. That could mean the Fed will be able to take its foot off the gas, but it's not coming to a full stop. Fed Chair Powell said as much in his recent speech at the Brookings Institution, where he pointed to the likelihood of smaller increases but emphasized that he and his fellow policymakers "have a long way to go in restoring price stability." We're banking on a 50 basis point hike at this week's Fed meeting. The pace and magnitude of rate increases appears to be plateauing, but until we see a more noticeable decline in inflation and clearer signs that economic growth is slowing, the Fed is likely to remain in hiking mode. In particular, we're keeping a close eye on wage growth, which is currently near all-time highs (Figure 1) and likely one of the last areas of the economy to feel the impact of tighter policy.

As we enter 2023, we see inflation risks coming down but recession risks moving up.

The bottom line of our bottom line: Inflation risks are receding, but recession risks are rising. While rate hikes have taken some of the bite out of inflation, we don't think they have yet worked their way through the economic data. In our view, the U.S. is inching closer toward a recession, but if and when one occurs, we believe it will be relatively mild.

FIGURE 1: WITH WAGE GROWTH NEAR ALL-TIME HIGHS, RATE HIKES AREN'T ENDING SOON

Atlanta Fed Wage Growth Tracker (%)



Data source: Bloomberg, L.P., January 1997 to November 2022.

Portfolio considerations:

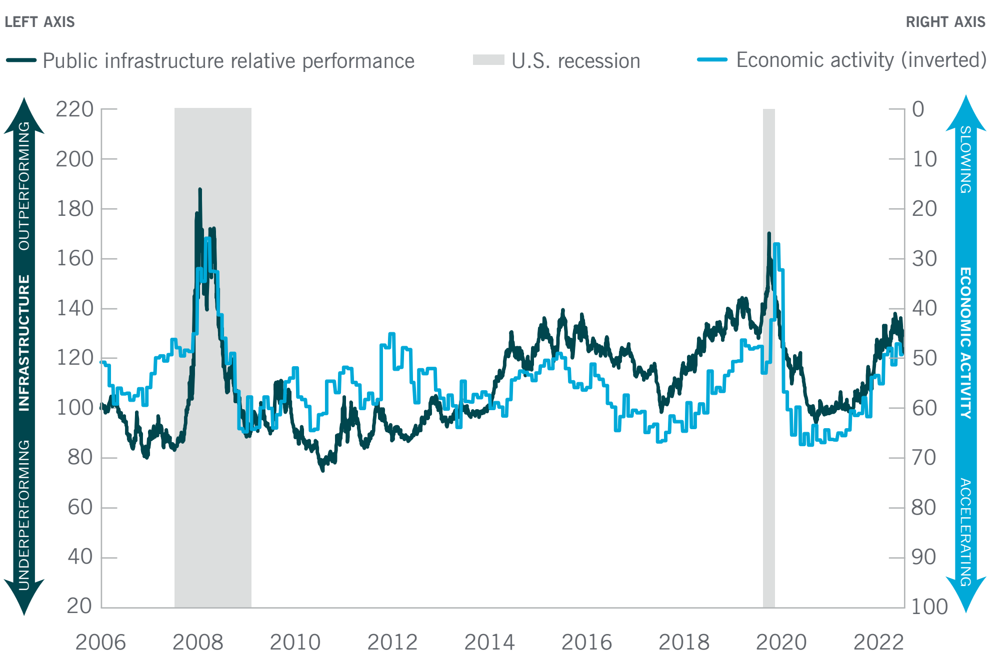
It may be time to reduce cyclicality. We anticipate weaker economic growth will translate into a rougher period for corporate earnings, which could put further pressure on equity markets. We think it makes sense for investors to be cautious toward cyclical equity sectors and to focus instead on quality, cash flow generation and dividend growth.

We see compelling opportunities in U.S. public infrastructure. This area of the market tends to be relatively well insulated from the higher costs of debt (i.e., rising interest rates) and elevated inflation. Additionally, inelastic demand for the necessary services that infrastructure provides could buffer the asset class from an economic slowdown. Figure 2 shows that infrastructure investment performance historically has been decoupled from economic growth.

Within public infrastructure, we prefer **renewable and midstream energy investments** that should benefit from pricing power associated with the growing challenges of global energy security as the U.S. becomes a larger, more reliable exporter of energy sources. We also favor **waste management** and **environmental services**, which tend to be high quality operations that can generate predictable cash flows during periods of economic contraction. Additionally, **electric utilities** look poised to be among the greatest beneficiaries of the recently passed Inflation Reduction Act that has drastically reduced the cost to deploy and finance renewable energy projects.

Infrastructure may be a rare area of the market that could perform well during a recession.

FIGURE 2: PUBLIC INFRASTRUCTURE HAS MORE THAN WEATHERED PREVIOUS GROWTH SLOWDOWNS



Data source: Bloomberg, L.P., November 2006 to November 2022. **Performance data shown represents past performance and does not predict or guarantee future results. Public infrastructure** is represented by the FTSE Developed Core Infrastructure Index. Performance depicted shows the ratio of the FTSE Developed Core Infrastructure Index performance relative to the FTSE Developed Market Index, indexed to 100. **Economic activity** depicts the ISM Manufacturing Index (a number over 50 indicates expansion; less than 50 indicates contraction).

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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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