

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

A blast from the past

Bottom line up top

Banking pressures could persist. The failure of Silicon Valley Bank has sparked broader market volatility, especially across regional banks, even though this is a niche bank focused on venture capital, and is not representative of the broader banking sector. While bank depositors should be protected given policymaker actions, bank equity and bond holders could see additional downward pressure, especially as higher interest rates act as a headwind for the banking system.

Higher for longer... or is lower simply over? The ultra-low-rates environment investors have grown accustomed to seems to be ending. But a look back at the fed funds effective rate suggests we are not at risk of leaving a period of normalcy, but rather a period of irregularity (Figure 1). Since the Fed began lowering rates during the Global Financial Crisis in July 2008 until the current rate hiking cycle started in March 2022, the average yield on an overnight deposit between lending institutions was just 0.7%. In the half-century leading up to the Global Financial Crisis, the average rate was 5.7%.

Recency bias is the term describing the assumption that the current state of being will continue indefinitely. As we face the potential end of an era of easy money, prudent investors should be prepared to adjust their portfolio construction from what has worked over the last decade. Even the traditionally idealized 60/40 split between equity and fixed income allocation is under scrutiny, as correlations between the two asset classes have risen significantly. Rather than fearing change, average investors should consider how they may benefit as asset classes that were once off-limits to some are now more accessible.



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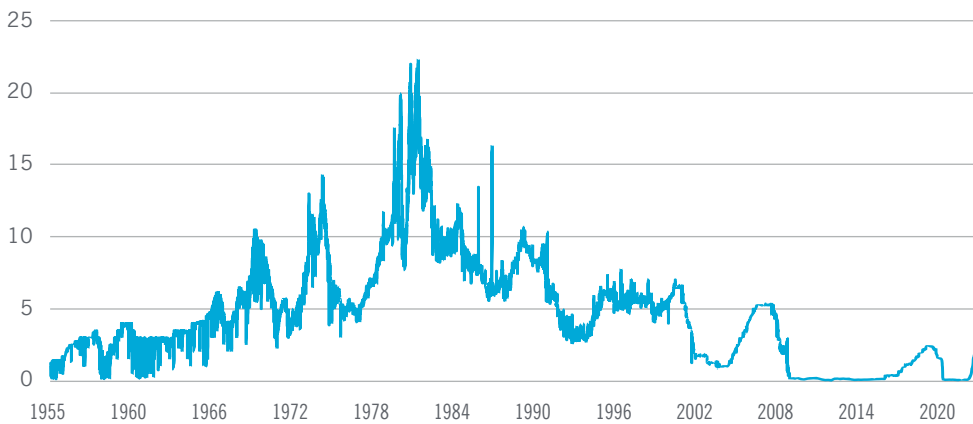
On behalf of Nuveen's Global Investment Committee

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.

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FIGURE 1: RATES MAY BE LEAVING A PERIOD OF IRREGULARITY

Fed funds effective rate, not seasonally adjusted (%) July 1954 – March 2023



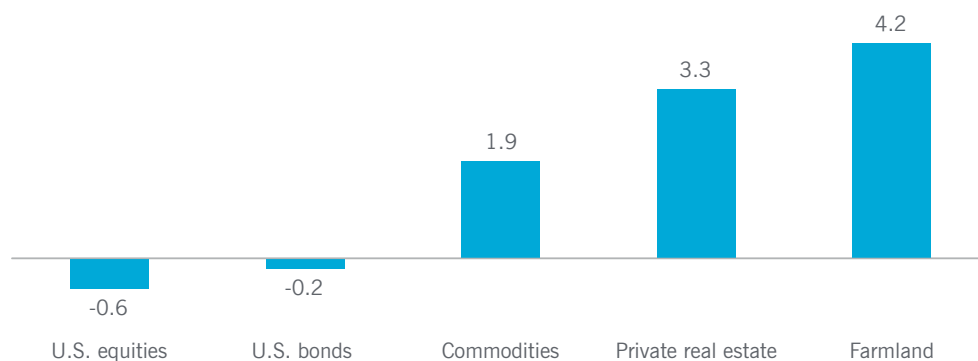
Data sources: Board of Governors of the Federal Reserve System (U.S.); FRED St. Louis Fed., 01 Jul 1954 - 06 Mar 2023. Performance data shown represents past performance and does not predict or guarantee future results.

Portfolio considerations:

Higher-for-longer interest rates are an important factor in portfolio construction. Inflation may top 3% annualized over the next five years, according to Moody’s Investor Service. Equities and bonds have experienced negative returns in such an environment (Figure 2). That does not make investing in public markets unattractive, but it requires more selectivity.

FIGURE 2: EQUITIES AND BONDS HAVE EXPERIENCED NEGATIVE RETURNS DURING PERIODS OF HIGH INFLATION

Average quarterly returns when inflation is greater than 3 (%)



Data source: Bloomberg, L.P., Data is from 29 Dec 2000 - 28 Feb 2023. Representative indexes: U.S. equities (S&P 500 total Return Index), U.S. bonds: Bloomberg U.S. Aggregate Total Return Index; commodities: Bloomberg Commodity Total Return Index; private real estate: NCREIF ODCE Total Return Index; farmland: NCREIF Farmland Total Return Index. Performance data shown represents past performance and does not predict or guarantee future results.

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Within equities, this environment favors areas that have historically thrived during periods of higher inflation, including industrials and the materials sectors that benefit from higher commodity prices. Historically, commodities have returned almost 2% each quarter when annual inflation is more than 3%. As for fixed income, investing in plus sectors such as senior loans and high yield will likely be required to earn a real yield, after inflation, inside a portfolio. High yield corporate bonds may provide an attractive total yield (the risk-free rate plus a spread for taking on credit risk). Senior loans offer investors a floating – rate yield that may protect a portfolio from further rate increases.

Inside alternatives, private real estate and farmland have performed well during higher inflationary periods. Thanks to their longer-term leases, farmland investments tend to hold their value in real terms and provide income stability.

***Looking ahead,
investing in
public markets
will require
more selectivity.***

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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