

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Post-Jackson, it's time to start filling duration holes

Bottom line up top

Jackson Hole in one word: Hawkish. Fed Chair Jerome Powell's opening remarks at last week's Jackson Hole symposium reaffirmed the central bank's determination to keep a tight rein on inflation. While year-over-year headline CPI has fallen sharply from its June 2022 peak of 9% to about 3%, and core CPI has eased to 5%, these levels remain too high for the Fed's comfort. "We are prepared to raise rates further if appropriate," Powell stated, clearly implying that the current rate hiking campaign is likely not over. He added that the Fed intends to "hold policy at a restrictive level until we are confident that inflation is moving sustainably down toward our objective."

Shelter from the storm. One particularly encouraging disinflationary trend has been the recent moderation in shelter prices. After peaking above 8% in March, shelter inflation dipped to 7.7% in July, contributing 340 basis points to the overall core CPI rate. Because of how it's calculated, shelter inflation data tends to lag actual moves in rents and housing prices by several months. We anticipate the metric will continue to ease over the coming quarters, which should allow inflation to continue to moderate (Figure 1).

Economy more likely to simmer than sizzle. We're increasingly confident that peak inflation is behind us. And despite continued strength in the Federal Reserve Bank of Atlanta's GDP Now Tracker, which as of last week signaled the U.S. economy expanding at an annualized rate of 5.9%, we believe growth is poised to decelerate during the remainder of 2023 and into 2024. This anticipated slowing should be accompanied by a partial retracing of the steep rise in U.S. Treasury



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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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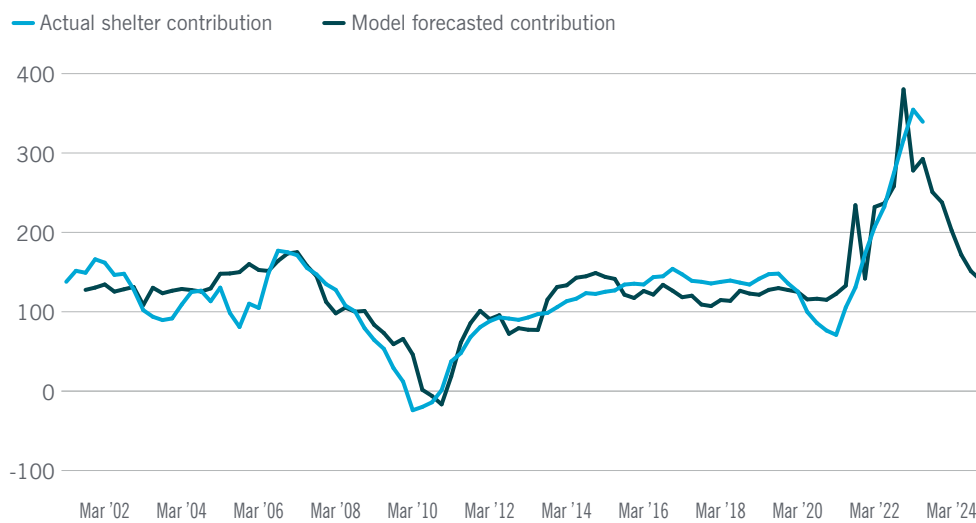
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yields that began after Memorial Day. Historically, the 10-year yield has peaked within the last few months of the final rate hike in a tightening cycle. We expect this hike will occur at either the September or November Fed meeting, and that the 10-year yield will decline through year-end. Given this softer outlook for inflation, growth and interest rates, investors still on the sidelines holding cash and money market funds may want to take advantage of opportunities to add duration to their portfolios sooner rather than later.

We expect both inflation and economic growth to moderate over the coming quarters.

FIGURE 1: MODERATING SHELTER PRICES COULD SIGNAL A BROADER EASING OF INFLATION

Actual and forecasted shelter contribution to core U.S. CPI in basis points



Data source: Bloomberg, L.P., Mar 2021 to Jan 2024. Data depicts the contribution of shelter to the overall core Consumer Price Index in basis points. The model calculates a forecasted shelter contribution based on nominal GDP and home prices. Data from Bloomberg.

Portfolio considerations

With the anticipated end of the U.S. rate hiking cycle as a backdrop, we analyzed the returns of the broad bond market versus short-term Treasuries during historical periods when the Fed paused (Figure 2). The broad market typically experienced a strong relief rally immediately after the Fed pause and mostly outperformed the following year. This lends further credence to our view that overallocating to cash or short-term government debt could be a mistake — and that investors may want to start closing their duration underweights.

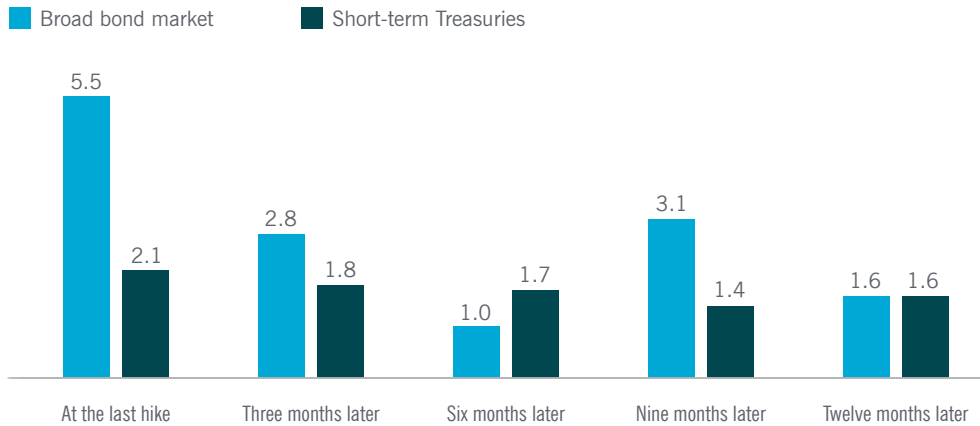
In particular, we believe allocating to investment grade corporate bonds, which offer a longer duration and a yield approaching 6%, could prove beneficial. We're also finding attractive portfolio opportunities in other credit categories and suggest a diversified approach rather than targeting a single specific sector. Our preference is for issuers with durable free

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cash flow and solid balance sheets in high yield corporates, senior loans, emerging markets debt and preferred securities. Mid-quality segments (rated BBB and BB) look the most compelling.

FIGURE 2: BONDS HAVE HISTORICALLY OUTPERFORMED CASH WHEN RATE HIKES STOP

Average rolling three-month returns (%) starting at the following timeframes



Data source: Bloomberg, L.P. Data reflects average performance during all Federal Reserve rate-hiking cycles since 1990 (1995, 2000, 2006 and 2018). Performance data shown represents past performance and does not predict or guarantee future results. Representative indexes: Broad bond market: Bloomberg U.S. Aggregate Bond Index; Short-term Treasuries: Bloomberg U.S. Treasury 1-3 Year Index.

Although yields on cash may look tempting, we believe overallocating to cash or short-term debt could be a mistake.

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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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