

The Fed remains on hold, but proceeding carefully

The U.S. Federal Reserve kept interest rates unchanged once more at the November policy meeting, as expected. The committee left open the possibility of one more hike later this year.

Tony Rodriguez
Head of Fixed Income Strategy

WHAT HAPPENED?

The U.S. Federal Reserve kept interest rates at 5.25% - 5.50%, remaining at their 22-year high. The policy statement contained minimal changes to key wording, and Chair Jerome Powell left the door open for another rate hike later this year.

The policy statement continued to characterize inflation as “elevated” and upgraded the language about growth to “strong” from “solid.” This was another incremental upgrade after the prior upgrade from “moderate.” The policy outlook language remained unchanged, discussing “additional policy firming that may be appropriate.” Finally, the statement added a reference to “tighter financial and credit conditions,” potentially signaling that the increase in Treasury yields over the last three months may substitute for more policy rate hikes.

In his press conference, Chair Powell emphasized that the Fed remains committed to decreasing inflation to the 2% target. He said that the FOMC can afford to “proceed carefully” and indicated that no decision has been made regarding the next policy meeting in December. Powell also said that the FOMC is not yet entirely confident that policy is

restrictive enough. This likely signals a possibility of one more rate hike, should growth remain strong and inflation elevated.

RECENT DATA HAVE BEEN SUPPORTIVE

Since the last Fed meeting in September, economic data have been broadly positive. Inflation has continued to moderate, with core PCE inflation down to +3.7% year-over-year, from +4.2% at the last meeting. Nevertheless, underlying trends were less favorable, as core PCE services excluding housing re-accelerated to near a 4% annualized rate, from a recent low earlier this summer closer to 3%. Wage inflation also remains elevated, despite some softening in the labor market over recent months.

On the growth side, third quarter U.S. GDP was extremely strong, expanding at an annualized rate of +4.9% quarter-over-quarter. Although around two percentage points of that headline number came from inventories and government, the data still showed strong growth for consumption and investment.

The labor market also remains healthy. The pace of job creation has been running around +250,000 per month, and the latest print was especially strong at +336,000. At the same time, leading indicators have softened, with the quits rate declining to pre-Covid levels and the unemployment rate edging higher.

The economic outlook remains healthy, with growth slowing but not collapsing. This is what the Fed wants, and it should be sufficient for inflation to decline through the end of the year. We continue to forecast a material growth slowdown over the coming quarters, with a year-end core inflation rate around 3.5%.

WHAT DOES THIS MEAN FOR INVESTORS?

With the Fed inching closer to ending rate hikes and the economic backdrop remaining uncertain, volatility will likely pick up again. We continue to believe Treasury yields should moderate and expect the curve to become less inverted, though policy rates are likely to remain elevated for some time.

In public fixed income markets, we believe a blend of taxable and non-taxable assets is attractive. On the taxable side, securitized assets and preferreds offer nontraditional income, with yields exceeding those of investment grade bonds. Opportunities within securitized assets include mortgage-backed and agency credit risk transfer securities (which are floating rate). In terms of non-taxable investments, AAA rated municipal bonds currently pay taxable-equivalent yields that exceed Treasury yields across all maturities. And with support from strong underlying fundamentals, high yield municipals also merit consideration.

Meanwhile, private credit offers an attractive risk-adjusted return profile, and its floating rate structure protects against potentially higher interest rates. Farmland can serve as a hedge against elevated inflation, and because farmland produces basic necessities, demand for the goods and services produced should be resilient during periods of economic weakening.

In equities, we're optimistic on information technology and health care. Tech stocks have strongly outperformed the broader market year-to-date, driven by the largest names. And their soaring share prices have been accompanied by a dramatic improvement in earnings before interest and taxes. Within technology, we remain constructive on less-cyclical select software companies — specifically

those whose revenue sources are tilted toward enterprises rather than retail consumers. Such companies tend to have resilient business models and inelastic demand.

Elsewhere, health care is a defensive play with the potential to outperform if the economic slowdown materializes as we expect. The sector has seen its share of consumer spending expand, largely a function of higher outlays for Affordable Care Act expenses (12% growth in 2022 and 35% growth over the past two years).

For more information, please visit us at nuveen.com.

Endnotes

Sources

Federal Reserve Statement, November 2023.

Bloomberg, L.P.

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. **Performance data shown represents past performance and does not predict or guarantee 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.**

Important information on risk

This report is for informational and educational purposes only and is not intended to be relied upon as investment advice or recommendations, does not constitute a solicitation to buy or sell securities and should not be considered specific legal, investment or tax advice or analysis. The analysis contained herein is based on the data available at the time of publication and the opinions of Nuveen Research.

The report should not be regarded by the recipients as a substitute for the exercise of their own judgment. All investments carry a certain degree of risk, including possible loss of principal, and there is no assurance that an investment will provide positive performance over any period of time. It is important to review investment objectives, risk tolerance, tax liability and liquidity needs before choosing an investment style or manager.

Nuveen, LLC provides investment solutions through its investment specialists.

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

NOT FDIC INSURED | NO BANK GUARANTEE | MAY LOSE VALUE