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Weekly Investment Commentary

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Markets need better economic and trade news to keep rising

Since the summer, investors have grown significantly less pessimistic about the global economy and financial markets. Stock prices have been rising as investors have been moving money into equities. In contrast to conditions a few months ago, financial markets now appear priced for a much better economic environment, and investors are anticipating more progress on a U.S./China trade deal. We think the macro environment is solid enough to sustain the current risk-on trade, but we are increasingly concerned that stocks may have gotten ahead of themselves.

HIGHLIGHTS

- **Fueled by the consumer sector, the global economy has stabilized and the outlook appears brighter today than it did one year ago.**
- **Trade issues, however, represent a significant threat and could potentially derail equity markets.**
- **We remain constructive toward stocks heading into 2020, but are concerned that valuations already reflect high levels of optimism.**

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Senior Portfolio Manager and Chief Equity Strategist

Bob Doll serves as a leading member of the equities investing team for Nuveen, providing reasoned analysis through equity portfolio management and ongoing market commentary.

Economic growth has been stabilizing (for the most part)

The global economic environment seems to be healthier than it was a year ago. Notably, we see evidence of more solid growth around the world, and not just in the U.S. as was the case through much of 2018. The consumer sector in particular has been quite strong and has propelled the broader economy.

One year ago, investors were highly worried about a global recession, but those risks appear to have faded. In fact, if anything, we think investors may have grown too optimistic over prospects for stronger growth, as reflected by rising stock prices. We think risks remain, especially regarding the manufacturing sector and global trade levels. We don't think it will happen, but weak manufacturing and trade could act as a drag and significantly slow down global economic momentum. We think it is more likely that the strong consumer and service sectors could help provide a lift to manufacturing data. But so far evidence of that scenario has been scant.

Trade woes represent a significant risk

The main culprit behind any economic weakness continues to be the rise in protectionism and broad trade policy uncertainty. Trade issues have clearly hurt global manufacturing levels, caused a downshift in business sentiment and depressed capital expenditure spending. If protectionism persists and new tariffs continue to be enacted, this damage could deepen.

We see some glimmers of hope, however. While the latest rounds of negotiations over the U.S./China phase one trade deal have stalled, we think prospects remain for a limited agreement and new tariffs could likely be delayed. Even as tariffs have been in place and as economic data from the eurozone has been spotty, Chinese export levels have been picking up, which is a critically important indicator of broader global trade levels. It is too early to say whether this improvement is a harbinger of better things to come, but it is clearly an optimistic signal.

At present, equity prices reflect a better trade environment, and we hope those signals are correct. A reduction in tariff levels (or even an easing in trade tensions and more clarity around future policy) would be bullish for stocks. If corporate management teams had a better sense of where trade issues were heading, they would be more willing to invest in their businesses, which would be a positive for corporate earnings and profits.

Monetary policy may have run out of steam

Part of the reason we have a cautious outlook toward the economy and global financial markets is that monetary policy may have exhausted its ability to provide a tailwind for stocks. Global monetary policy remains extremely accommodative, but central banks, including the Federal Reserve, now appear in a holding pattern.

The drop in interest rates over the course of 2019 has been a positive for stock markets. But at this point, we have a hard time seeing additional cuts without also seeing notable economic weakness. And such weakness would be a negative for stocks and would probably outweigh any additional benefits arising from even lower rates.

In contrast, if economic growth does pick up (perhaps due to better news on the trade front), policymakers will come under increasing pressure to once again raise interest rates. We don't see that happening in the near term given how cautious central bankers have been, but monetary policy is less clear now than it was earlier in the year.

We remain mildly constructive toward stocks

We are hopeful that a modest improvement in economic growth will take hold, and we see prospects for better trade conditions from here. A slow recovery in manufacturing and trade would probably cause interest rates to rise modestly, but not to the point that rising rates would damage equity markets. At the same time, corporate profits could grind slowly higher in 2020. All told, such an environment causes us to be mildly constructive toward stocks.

The risks, however, appear skewed to the downside. The problem is those risks are more about political issues and policy decisions rather than economic fundamentals. Politics and policy mistakes are much harder to handicap than issues such as economic weakness or credit fundamentals, making them particularly tough to plan for.

Additionally, we think that valuations for equities and other risk assets have gotten full over the past few months. At this point, most of the good news appears already baked into prices. That means that economic growth and trade clarity will need to deliver in order for prices to continue moving higher.

2019 PERFORMANCE YEAR TO DATE

	Returns	
	Weekly	**YTD**
S&P 500	1.0%	27.6%
Dow Jones Industrial Avg	0.8%	23.1%
NASDAQ Composite	1.7%	31.9%
Russell 2000 Index	2.3%	22.0%
Euro Stoxx 50	0.4%	22.9%
FTSE 100 (UK)	1.2%	15.7%
DAX (Germany)	0.5%	20.7%
Nikkei 225 (Japan)	0.1%	19.8%
Hang Seng (Hong Kong)	-1.0%	5.7%
Shanghai Stock Exchange Composite (China)	-0.4%	15.4%
MSCI EAFE	0.5%	18.8%
MSCI EM	-0.8%	10.6%
Bloomberg Barclays US Agg Bond Index	0.2%	8.8%
BofA Merrill Lynch 3-mo T-bill	0.0%	2.1%

Source: Morningstar Direct, Bloomberg and FactSet as of 29 Nov 2019. All index returns are shown in U.S. dollars. Past performance is no guarantee of future results. Index performance is shown for illustrative purposes only. Index returns include reinvestment of income and do not reflect investment advisory and other fees that would reduce performance in an actual client account. All indexes are unmanaged and unavailable for direct investment.

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The **S&P 500 Index** is a capitalization-weighted index of 500 stocks designed to measure the performance of the broad domestic economy. The **Dow Jones Industrial Average** is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the *Nasdaq*. The **Nasdaq Composite** is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market. The **Russell 2000 Index** measures the performance approximately 2,000 small cap companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks. **Euro Stoxx 50** is an index of 50 of the largest and most liquid stocks of companies in the eurozone. **FTSE 100 Index** is a capitalization-weighted index of the 100 most highly capitalized companies traded on the London Stock Exchange. **Deutsche Borse AG German Stock Index** (DAX Index) is a total return index of 30 selected German blue chip stocks traded on the Frankfurt Stock Exchange. **Nikkei 225 Index** is a price-weighted average of 225 top-rated Japanese companies listed in the First Section of the Tokyo Stock Exchange. **Hong Kong Hang Seng Index** is a free-float capitalization-weighted index of selection of companies from the Stock Exchange of Hong Kong. **Shanghai Stock Exchange Composite** is a capitalization-weighted index that tracks the daily price performance of all A-shares and B-shares listed on the Shanghai Stock Exchange. **MSCI EAFE Index** is a free float-adjusted market capitalization weighted index designed to measure developed market equity performance, excluding the U.S. and Canada. The **MSCI Emerging Markets Index** is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. **Bloomberg Barclays U.S. Aggregate Bond Index** covers the U.S. investment grade fixed rate bond market. The **BofA Merrill Lynch 3-Month U.S. Treasury Bill Index** is an unmanaged market index of U.S. Treasury securities maturing in 90 days that assumes reinvestment of all income.

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