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Weekly Equities Commentary

19 April 2021

Equities reach record high on strong economic data

Stronger-than-expected economic news propelled stocks to new highs last week. Lower Treasury yields helped drive the outperformance of growth and momentum styles after those areas of the market meaningfully lagged value in the first quarter. The biggest sector winners this week were utilities, materials and health care, which each gained 3% or more. No sectors posted negative returns for the week.

HIGHLIGHTS

- **Inflation ticked up, with March's U.S. headline Consumer Price Index rising 2.6% year-over-year and 0.6% month-over-month. Core inflation rose a more moderate 1.6% and 0.3%, respectively.**
- **Retail sales rose sharply by nearly 10% in March, as continuing jobless claims showed a steep decline from February to March.**
- **Reversing a trend that had been in place for much of 2021, the 10-year Treasury yield dropped significantly, ending the week at 1 .59%.**

Saira Malik, CFA
CIO of Nuveen Equities

Saira Malik oversees the equities strategic direction for Nuveen as chair of the Equities Investment Council (EIC) and a member of Nuveen's Global Investment Committee (GIC). She has responsibility for equity portfolio management, equity research, equity trading, target date, quantitative and index strategies, as well as portfolio management responsibilities for global equity strategies.

Weekly overview

- *Despite rising global COVID-19 case counts, the bullish narrative for equities remains unchanged: Fiscal and monetary stimulus, vaccine distribution and solid market inflows have all been pushing equities higher.*
- *Utilities (3.7%), materials (3.3%) and health care (3.0%) led, while communication services (0.0%), energy (0.3%) and industrials (0.6%) were relative laggards. Large caps outperformed small caps last week.*
- *Per Bank of America, equity markets saw an additional $25.6 billion of inflows in March, bringing the total to over $600 billion over the past five months. Large caps and value styles were the largest beneficiaries, while small caps and growth experienced outflows.*

Market drivers & risks

- **Economic lift off?** Retail sales, unemployment and manufacturing data were all positive last week and surpassed expectations
  - The market reaction to the positive news was counterintuitive: Cyclical equities lagged and bond yields fell. Our interpretation is that a confluence of dovish Fed policy, ample liquidity and strong confidence levels has created a "melt-up" effect, prompting investors to buy anything that looks inexpensive. We believe this to be a short-term phenomenon and continue to favor economically sensitive areas of the market, which should do well when investors focus on earnings.

> ***We see solid long-term investments in value styles and in select cyclical areas, as well as compelling near-term growth opportunities."***

- **Earnings results could argue for diversification.** This earnings season may be one of the most highly anticipated in recent history given the increasingly high level of expectations paired with lingering pandemic-driven uncertainty. We think results will be solid, but expect peak earnings growth to occur in the second quarter, reflecting the positive economic data we anticipate over the next several months.
  - Historically speaking, accelerating earnings growth tends to favor value and cyclical areas. This trend should be amplified by rising interest rates. However, these expectations may be already priced into the markets to some degree, leading us to favor a more diversified approach by focusing on high-quality growth and cyclical opportunities.
- **Bank earnings look particularly solid.** In early reporting, the first quarter earnings growth rate for the S&P 500 stands just below 30%. This is in line with our full-year expectations, which are slightly above consensus estimates.
  - This uptick in growth has been largely due to bank results. Goldman Sachs, JPMorgan, Wells Fargo and Bank of America all reported strong results last week thanks to solid reserves and elevated trading revenues. Though fiscal and monetary stimulus have both been boosting results, we also think factors such as improved loan growth point to future strength for the industry.

Risks to our outlook

Headline economic data may create pockets of volatility, as inflationary shocks caused by short-term global supply chain disruptions and year-over-year comparisons will be difficult for investors to ignore.

Though recent Fed comments have seemingly settled investors' nerves, many remain wary about possible rate increases or asset purchase tapering. The central bank's messaging will remain one of the most significant near-term risks.

With the clock started on the legislative battle for an infrastructure package, investors should expect news related to its progress to move markets.

New COVID cases and varying vaccination rates across the globe could also create volatility for global equity markets. On a related note, incrementally better news out of the U.S., combined with incrementally worse news elsewhere, has led to a recent strengthening of the U.S. dollar. This is likely to create near-term headwinds for emerging markets.

Best ideas

We see continued tactical opportunities in growth and technology stocks, as investors with lofty expectations may be unimpressed by first quarter earnings. In the near term, we continue to favor consumer service sectors, especially in areas where unemployment remains elevated, and we are keeping an eye on industrials that could benefit from publicly funded infrastructure investments. We remain bullish on U.S. small caps, emerging markets and cyclicals for the longer term as the economy reopens, but think those areas could be subject to volatility over the coming months.

In focus

Higher inflation has arrived … temporarily

Annual U.S. inflation readings have moved higher, thanks largely to comparisons with last year's recessionary environment. Monthly inflation has also climbed, primarily as a result of higher energy prices, with gasoline rising 9.1% in March alone. The year-over-year comparison effect will likely be even more powerful in April's reports (especially for energy), which will almost certainly push headline inflation above 3% and core inflation above 2%. But this will almost certainly be transitory.

Monthly inflation data could remain elevated, however, as surveys of both large and small businesses indicate that pricing pressures are a concern. While half of March's inflation is attributed to gasoline, the other half is largely due to service industries: hotel stays, sporting event admission, car insurance and public transportation have all seen cost increases above historical averages. However, these prices are still below their pre-pandemic peaks. We think we are in a reflationary environment as demand slowly returns to normal, rather than in one of exploding inflation. We expect inflation to recede, possibly by the start of the fourth quarter.

In this environment, we prefer areas of the market that are strongly levered to the economy and interest rates, such as financials, industrials and consumer services. We would avoid companies that have already priced in a recovery or that lack quality fundamentals.

About the Equities Investment Council:

The Nuveen Equities Investment Council (EIC) includes the firm's senior equity portfolio managers averaging three decades of investing experience. The group brings global expertise across different styles of equity investing and provides value-added insights to Nuveen's investment process by refining and delivering the firm's collective equity market outlook, including key risks and drivers, to clients. Led by Saira Malik, CIO & Head of Equities, the team shares best global equities ideas, while focusing on individual areas of expertise to help generate alpha.

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Sources

All market data from Bloomberg, Morningstar and FactSet

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