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Equities shrug off employment miss

Most broad-based indexes appreciated last week, with the S&P 500 enjoying its third consecutive week of gains and rising seven out of the past eight. The tech-heavy NASDAQ bucked the trend, falling nearly 1.5% as trading favored cyclicals over growth and defensives areas of the market. The DJIA added 2.7%, while the MSCI EM, EAFE, and ACWI ex-USA all rose between 0.1% and 2.6%.

HIGHLIGHTS

- **The U.S. added 266,000 new jobs in April – a huge miss relative to the one million that were expected. The unemployment rate ticked up to 6.1%.**
- **Additionally, employment numbers for both February and March were revised downward, with the three-month average sitting at 524,000.**
- **On a more positive note, initial jobless claims fell to 498,000, a new low in the pandemic recovery.**
- **Treasury yields were somewhat volatile, with the 10-year declining slightly for the week.**



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 the jobs data miss, the “reopening” trade regained momentum. Small caps and value recaptured leadership over their large cap and growth counterparts.*
- *Among sectors, energy appreciated the most, adding nearly 9% for the week on rising oil prices. Materials (5.9%) and financials (4.2%) were also notable winners, while consumer discretionary, utilities, real estate and information technology each lost between 0.4% and 1.2%.*
- *Outside of the weak employment numbers, U.S. economic data continue to skew positive, as durable goods and the Purchasing Managers’ Composite Index beat expectations. Outside of the U.S., Chinese exports and service data expanded, as did German exports and industrial production.*

Market drivers & risks

- **Jobs miss, but equities gain.** Despite last week’s jobs data, all 11 S&P 500 sectors rose on Friday.
 - Under normal economic conditions, a miss of 750,000 new jobs would have likely caused concerns about a potential recession. In our view, the numbers represent an issue of supply rather than demand, which is much less of a negative for the economy. Historic levels of stimulus, labor participation and COVID-related fears are just a few headwinds facing understaffed businesses. We expect these conditions to improve in the coming months as the pandemic and economy improve.
- **Growing pains.** While there are many potential explanations for April’s poor employment report, we believe it’s more of a hiccup than the start of a



We see solid long-term investments in value styles and select cyclical areas, as well as compelling opportunities in small caps.”

worrisome trend. We think a more important point is that the broader recovery remains intact and is being helped by continued strong demand.

- The current environment has made it challenging to accurately forecast economic and earnings data, resulting in missed expectations, both to the up and downside. While we remain confident in the ongoing economic recovery, we think a return to “normal” may take longer than some may have hoped. As a result, we continue to advocate a diversified investment stance, pairing high-quality growth companies with high-quality cyclicals levered to economic growth as we wade through the ongoing recovery.
- **Earnings growth reinforces strong demand.** With 88% of companies reporting, the S&P 500 is demonstrating earnings growth of 49.4%, which is more than double consensus estimates from the end of March. Should this trend continue, it would represent the highest year-over-year earnings growth rate since the first quarter of 2010 (55.4%).
 - Earnings growth remains broad based, with 10 of the 11 S&P 500 sectors now showing higher growth rates (or smaller declines) than at the end of March. Additionally, the 12-month forward P/E is currently 21.6x, down from a peak of 23.4x in September 2020. While that valuation level remains elevated compared to its five-year average, the change is incrementally better as we head into the period in which we expect to see peak earnings growth for the quarter, led by consumer discretionary (182%) and financials (134%).

Risks to our outlook

Given the magnitude of the miss in last week's employment data, investors have likely reset their expectations for the timing of the recovery. As a result, we expect a greater degree of volatility around future economic data, and expect investors may focus on those numbers rather than on Fed comments pertaining to the tapering of quantitative easing.

The debate over tax reform is heating up, as both political parties continue to express a willingness to negotiate. Any negativity surrounding these discussions, as well as the legislative battle for an infrastructure package, will likely create pockets of volatility.

New COVID-19 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

Increased economic reopening and recent underperformance have created opportunities in U.S. small caps. We 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. Tactical opportunities remain in technology and growth stocks, but with a high degree of selectivity, as the “shelter-in-place” trade may no longer provide a broad benefit to all companies. We also remain bullish on emerging markets over the long term, as efforts to stem the spread of the virus eventually take hold.

In focus

Tailwinds for emerging markets equities

Though global equities may appear overvalued when compared to their own history, relative valuations appear to favor emerging markets: Per FactSet, EM equities are currently trading at a 25% discount versus their historical relationship with U.S. equities. Several important tailwinds reinforce this point:

1. Strong growth from China
2. A weaker U.S. dollar
3. Possible incremental improvements in geopolitical outlooks.
4. A widening growth gap with EM earnings per share 10% higher than in the U.S.

It is also worth considering the duration and magnitude of the cyclical relationship between U.S. and EM equities. During the decade ending in 2019, U.S. equities outpaced EM by approximately 750 bps, on an average annual basis. In contrast, EM equities outperformed the U.S. by 1,250 bps per year during the prior decade (2000-2009). 2020 may have been a transition year, as emerging markets kept pace with the U.S. and outperformed significantly in the fourth quarter.

Though several EM countries continue to struggle amid the pandemic, we are optimistic that the global economy will eventually follow a similar path to recovery as the U.S. As a result, we believe this is a good time for investors to consider evaluating their exposure to emerging market equities given their solid prospects.

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.

For more information or to subscribe, please visit nuveen.com.

Sources

All market data from Bloomberg, Morningstar and FactSet

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A word on risk

All investments carry a certain degree of risk and there is no assurance that an investment will provide positive performance over any period of time. Equity investing involves risk. Investments are also subject to political, currency and regulatory risks. These risks may be magnified in emerging markets. Diversification is a technique to help reduce risk. There is no guarantee that diversification will protect against a loss of income.

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