nuveen
A TIAA Company

CIO Weekly Commentary
22 August 2022

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Energy primed to power through near-term uncertainty

Bottom line up top:

Slipping oil prices could cool inflation, but supply/demand dynamics remain hot. With energy one of the most volatile (and publicized) components of the CPI, this summer's pullback in prices (particularly gasoline) was the predominant factor for the July inflation moderation (Figure 1). In fact, U.S. average gasoline prices are back below $4 per gallon ($3.93 as of August 17), 22% lower than the mid-June peak of $5.01. This drop reflects a perception that demand for fuel will weaken amid expectations for higher prices and growing recession fears. Despite the conflict in Ukraine, Brent Crude has also traded lower in part due to China's zero-COVID policy and its shift to importing oil from Russia, which displaced Saudi Arabia in 2022 as China's top supplier of crude oil (China is the world's largest oil importer).

The trend of falling energy prices, however, could be poised to reverse in the U.S. Oil producers, wary of the pain overinvestment caused in prior cycles, did not significantly increase output as prices advanced earlier this year. U.S. rig counts remain below prior peaks, as capital discipline has been prioritized over increasing supply. While some North American energy companies stand to benefit from the buildout of clean energy generation and the shift towards renewables over time (a trend bolstered by the recent passage of the U.S. Inflation Reduction Act), this could mean less investment in the carbon economy.

Saira Malik, CFA
Chief Investment Officer

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.

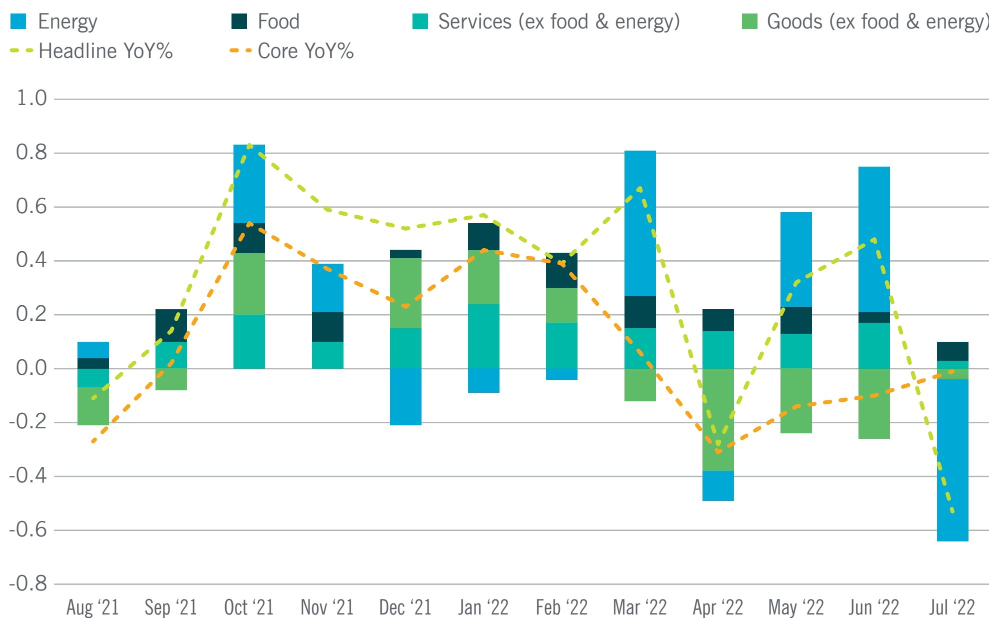
OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.
NOT FDIC INSURED | NO BANK GUARANTEE | MAY LOSE VALUE

We see a similar picture outside of the U.S. OPEC capacity utilization has recovered to a degree, but remains below pre-COVID levels (Figure 2). Energy scarcity is being felt more acutely in Europe, as prices for natural gas (which is primarily used for heating and generating electricity) are skyrocketing to record levels given diminished supply from Russia and continued logistical difficulties importing liquefied natural gas (LNG). Asia has also ramped up LNG imports in preparation for winter, further driving up prices. Energy security and its impact on fuel costs will remain a key theme in the years ahead, creating a stiff headwind to the efforts of lowering inflation back to pre-COVID levels.

Compelling supply/demand dynamics and an increased focus on renewables should spark tailwinds for the energy sector.

FIGURE 1: ENERGY SWINGS CONTINUE TO SPARK INFLATION

Change in year-over-year inflation rate and key sector contributions (%)

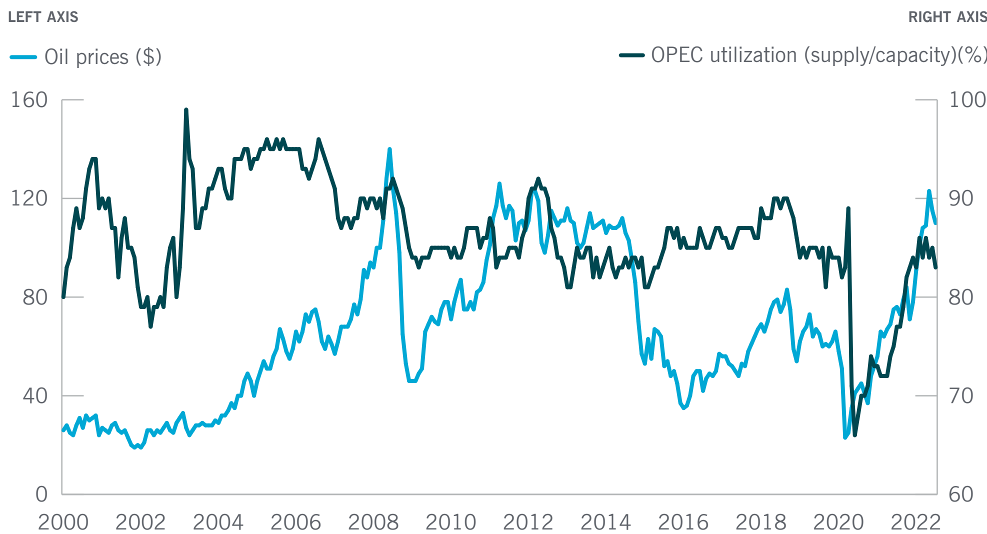


Data source: Bloomberg, L.P., Aug 2021 to Jul 2022. Monthly readings of the U.S. Consumer Price Index.

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

A focus on energy stocks could serve as a useful counterbalance to an otherwise defensive portfolio stance.

FIGURE 2: SUPPLY/DEMAND DYNAMICS REMAIN FAVORABLE FOR OIL PRICES



Data source: Bloomberg, L.P., Jan 2000 to Jul 2022. Monthly readings. Oil prices reflect Brent Crude.

Portfolio considerations:

High energy prices make the Fed's job harder, but not impossible. For example, the prices of goods ex-food and energy (21% of headline CPI) declined for a fifth consecutive month as retailers have cut prices to manage inventories. Softness in home prices has historically led a decline in owners' equivalent rent (24% of headline CPI), providing some optimism for the coming months. But energy prices (only 9% of CPI, yet a much more volatile component) have an outsized impact on the ultimate headline number. If energy supply constraints cause headline U.S. CPI to remain elevated, the U.S. Federal Reserve may have to tighten policy more aggressively to affect the core components of the real economy. Therefore, we believe the market's anticipation of a soft landing and a likely "Fed pivot" in 2023 toward easing may be overly optimistic. As such, **we think it makes sense to remain defensively positioned in portfolios.**

To prepare for a more uncertain path of further inflation, we favor **productive real assets like private real estate, infrastructure, and farmland** that have relatively stable values and cash flows that increase along with inflation. Within fixed income, we continue to advocate for a **moderately shorter duration profile**, but think it makes sense to maintain strategic allocations to investment grade bonds in case monetary tightening ultimately leads to a hard economic landing. **Higher quality is still key when it comes to equity positioning, but energy looks attractive** given free cash flow yields of around 15% for some U.S. companies. An energy overweight would also help balance an otherwise defensive positioning.

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

About Nuveen's Global Investment Committee

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.

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. **Past performance not predict or guarantee of 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

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. Investing in municipal bonds involves risks such as interest rate risk, credit risk and market risk, including the possible loss of principal. The value of the portfolio will fluctuate based on the value of the underlying securities. There are special risks associated with investments in high yield bonds, hedging activities and the potential use of leverage. Portfolios that include lower rated municipal bonds, commonly referred to as "high yield" or "junk" bonds, which are considered to be speculative, the credit and investment risk is heightened for the portfolio. Credit ratings are subject to change. AAA, AA, A, and BBB are investment grade ratings; BB, B, CCC/CC/C and D are below-investment grade ratings. As an asset class, real assets are less developed, more illiquid, and less transparent compared to traditional asset classes. Investments will be subject to risks generally associated with the ownership of real estate-related assets and foreign investing, including changes in economic conditions, currency values, environmental risks, the cost of and ability to obtain insurance, and risks related to leasing of properties. Socially Responsible Investments are subject to Social Criteria Risk, namely the risk that because social criteria exclude securities of certain issuers for non-financial reasons, investors may forgo some market opportunities available to those that don't use these criteria. Investors should be aware that alternative investments including private equity and private debt are speculative, subject to substantial risks including the risks associated with limited liquidity, the use of leverage, short sales and concentrated investments and may involve complex tax structures and investment strategies. Alternative investments may be illiquid, there may be no liquid secondary market or ready purchasers for such securities, they may not be required to provide periodic pricing or valuation information to investors, there may be delays in distributing tax information to investors, they are not subject to the same regulatory requirements as other types of pooled investment vehicles, and they may be subject to high fees and expenses, which will reduce profits. Alternative investments are not appropriate for all investors and should not constitute an entire investment program. Investors may lose all or substantially all of the capital invested. The historical returns achieved by alternative asset vehicles is not a prediction of future performance or a guarantee of future results, and there can be no assurance that comparable returns will be achieved by any strategy.

Nuveen provides investment advisory services through its investment specialists.

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