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Capital markets will likely be choppy

Equities finished lower for a second straight week, with the S&P 500 Index down 2.1% and suffering back-to-back weekly declines of more than 1% for the first time since late August.¹ Energy was the worst performer for a fourth straight week as growth concerns stemming from the coronavirus weighed heavily on oil. Outsized weakness in industrial metals, chemicals, paper and packaging put pressure on Materials. Utilities performed best, as defensive sectors tended to fare better. Consumer discretionary also finished positive for the week, thanks to strong earnings from Amazon.

HIGHLIGHTS

- **U.S. economic data has softened slightly, but global data is generally improving.**
- **Escalating concerns over the coronavirus have dampened the reasonably hopeful investment backdrop at the beginning of the year.**
- **Cyclical economic conditions are poised to improve only modestly this year, and any upturn may be delayed by the impact of the virus, especially in China.**



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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.

Weekly top themes

1

It appears that fourth-quarter earnings will end up positive by 2 to 3%, with nearly half of S&P 500 companies reporting. The expected growth rate for 2020 now stands at 9.1%, down from 9.4% earlier in the year. Our guess remains plus 6%. Most companies have indicated the macro backdrop is healthy and have viewed the phase-one trade deal as a modest positive on margins.

2

Real GDP beat expectations, increasing 2.1% quarter-over-quarter and 2.3% year-over-year. Capex was down 1.5%, but tech capex increased 6%.²

3

The period since the December Fed meeting has been dominated by three developments: 1) softer U.S. data but generally better global data, 2) an extension of the fourth quarter market “melt up” that triggered Fed unease that balance-sheet expansion may be fueling risk-taking and 3) the coronavirus that drove a swing back to risk off. It is too soon to tell how serious the economic impact of the virus will be, but it could put a short-term drag on Chinese growth that would weigh on global stabilization.

4

The combination of very low put-call ratios, aggressive ETF flows and widespread overbought conditions posed a tactical risk for markets. However, a spark to catalyze a correction was missing. While the Iranian situation quickly faded and impeachment hasn't hit bullish sentiment, the sudden emergence of the coronavirus appears to have struck at the foundation of the market's upturn.

5

Last year's decline in mortgage rates has helped generate a meaningful recovery in the housing market. Provided long-term interest rates rise in an orderly manner, housing's recovery should persist and provide a basis to extend the economic expansion. Importantly, a recession has never started while housing has been expanding.

6

We expect global manufacturing to pick up in 2020, thanks to the delayed tailwind from the synchronized global easing cycle that pushed global short rates to a new expansion low. Unfortunately, the coronavirus is a new, potentially significant headwind that is impossible to forecast.

7

House Democrats released an infrastructure plan. While it has little chance of becoming law before the election, it provides guidance on what Democrats might do if they win in November.

Concerns over the coronavirus dampen investor sentiment

The investment backdrop at the start of the year was reasonably hopeful. Closely watched manufacturing indicators pointed to a potential cyclical uptrend after a two-year slowdown. Monetary policy was highly accommodative and destined to stay that way, at least through the U.S. election in November. Prior political and policy concerns had abated, with the U.S./China phase-one trade agreement, the decisive outcome of the U.K. election and somewhat diminished anxiety about a U-turn in economic policy after the results of the upcoming U.S. election.

However, the escalation of the coronavirus has detoured these positive developments. It's unclear how the health crisis in China will evolve, but investors will remain jittery until the virus is contained. That said, risk assets were overheated by mid-January and vulnerable to any negative news. We caution reading too much into investors' reactions so far. A further global equity correction of 3% to 5% would still leave the underlying uptrend intact.

While we optimistically assume the coronavirus will soon be contained, markets were overdue for a reality check. Cyclical economic conditions are poised to improve only modestly this year and signs of an upturn may be delayed by the impact of the virus, especially in China. Equity and credit valuations are already full by historical standards following major rewritings in 2019.

The U.S. election remains a wild card, and there's potential for setback as the U.S., China and U.K./EU strategic relationships are negotiated. Our base-case scenario continues to call for choppy capital markets this year. By mid-January, markets had already discounted much of 2020's anticipated economic and earnings improvement. So resetting expectations was due. Present and anticipated conditions do not warrant aggressive positioning until we see more clarity or more attractive valuation entry points.

2020 PERFORMANCE YEAR TO DATE

	Returns	
	Weekly	YTD
S&P 500	-2.1%	0.0%
Dow Jones Industrial Avg	-2.5%	-0.9%
NASDAQ Composite	-1.8%	2.0%
Russell 2000 Index	-2.9%	-3.2%
Euro Stoxx 50	-3.2%	-3.9%
FTSE 100 (UK)	-3.1%	-3.8%
DAX (Germany)	-3.9%	-3.1%
Nikkei 225 (Japan)	-1.8%	-1.5%
Hang Seng (Hong Kong)	-5.8%	-6.4%
Shanghai Stock Exchange Composite (China)	-	-1.6%
MSCI EAFE	-2.5%	-2.1%
MSCI EM	-5.1%	-4.7%
Bloomberg Barclays US Agg Bond Index	0.6%	1.9%
BofA Merrill Lynch 3-mo T-bill	0.0%	0.1%

Source: Morningstar Direct, Bloomberg and FactSet as of 31 Jan 2020. 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.



Present and anticipated conditions do not warrant aggressive positioning until we see more clarity or more attractive valuation entry points.

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

1 Source: Bloomberg, Morningstar Direct and FactSet

2 Source: Credit Suisse

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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