TIAA-CREF Asset Management

2015 Fourth Quarter Economic and Investment Outlook

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Executive summary

- U.S. economic growth has been bolstered by healthy labor markets and lower oil prices, which together are beginning to drive increased consumer spending.
- We view China's economy as cyclically stable but in a slowing trend—a more optimistic outlook than current headlines suggest. Europe's recovery remains intact, with improved lending, manufacturing, sentiment, and spending.
- The summer correction in U.S. equity markets has created select buying opportunities in fundamentally strong companies. We expect market volatility to continue as we approach a Fed tightening cycle against a backdrop of global growth concerns; however, we anticipate a rebound in equity performance.
- For fixed-income investors, sector diversification and yield-curve positioning will remain key. We favor U.S.-centric holdings given the relative strength of the economy and the dollar.

Asset class preferences

Equities ↑	**Fixed income** ↓
U.S. Equities ↓	U.S. Treasuries ↓
International ↑	Corporate Bonds ↑
Emerging Markets ↑	High-Yield Bonds ↑
	Emerging Markets ↑

Data as of September 30, 2015. ↑ = overweight; ↓ = underweight. Please note the forecasts above concern asset classes only, and do not reflect the experience of any product or service offered by TIAA-CREF. These forecasts are for informational purposes only and should not be considered investment advice or constitute a recommendation to purchase or sell securities. Market forecasts are subject to uncertainty and may change based on varying market conditions, political and economic developments. Past performance is not an indicator of future results.

TIAA CREF
Financial Services

United States

Economy

The positive growth trajectory continues, and measures of consumer spending and inflation are beginning to tick up. Oil prices have stabilized, albeit at low levels, driven by ongoing demand and adjustments to supply made in response to the more than year-long decline in prices. While September's weak employment report could potentially affect the Federal Reserve's decision on whether to raise interest rates in December, the timing of the rate hike itself is less important to the economy than the ultimate pace of tightening.

Stocks

U.S. equity valuations appear fair. We look for growth to continue its multi-year outperformance versus value unless global economic growth accelerates meaningfully. Higher-yielding sectors such as Utilities and REITs might lag as interest rates move up.

Bonds

The impending Fed hike will likely be modest but nonetheless represents the start of a new rate cycle. Volatility has already spiked amid uncertainty about the timing of rate "liftoff," so spreads could actually stabilize when the Fed finally acts, particularly if the move is accompanied by dovish rhetoric. Heading into the fourth quarter, we favor diversified exposure, with emphasis on credit sectors offering a degree of protection from rising rates.

The Fed is likely to begin raising short-term interest rates later this year.

Get our perspective on how rising rates may impact bonds and stocks.

International

Economy

Both Japan and Europe remain focused on monetary stimulus to drive stronger growth and inflation, as well as longer-term economic reforms.

Stocks

We continue to find European valuations attractive on a relative basis, as profit margin improvement potential is greater than in the U.S., where margins are at peak levels and wage costs are creeping higher. Continued recovery in Europe would lead to significant earnings growth on margin expansion. In Japan, stocks may have entered a more volatile period but remain inexpensive.

Bonds

Diverging monetary policies between the Fed (moving to a tightening stance) and its international counterparts (ongoing and potentially expanded easing) will likely make it more difficult for foreign bonds to compete against U.S. fixed income on a yield basis.

Emerging markets

Economy

Headline focus on China's slowing "old line" economic sectors (industrial, manufacturing, and exports) masks healthier domestic and service-oriented areas of the economy. Many emerging markets remain vulnerable to the risk of declining oil prices and weak demand for exports.

Stocks

Emerging markets offer significant long-term upside potential, given valuations that have been pressured by China's slowdown, the prospect of a U.S. rate hike, and falling commodity prices. Stable or improving Chinese data could help spark a rally in these beaten-down markets.

Bonds

Emerging-market debt fundamentals are mixed—defaults may be on the rise, although a large portion of the risk appears to be priced in at current levels. Downside risk could have further to run if the dollar continues to strengthen. The likely impact of a stronger dollar is far from uniform across individual EM countries, however.