ON THE RADAR

FAQs on the Markets and Economy

DECEMBER 8, 2022

What is the Fed thinking going into year-end?

The Fed will conclude its final meeting of the year on December 14 and they are expected to raise the federal funds rate by 50 bps at that meeting.

This will be a step down from their unprecedented series of four 75 bps hikes in the past four meetings. A slowdown in the pace of rate increases is needed because the Fed needs more time to see how past increases have impacted the economy. It takes time for the full effects of those rate increases to ripple through the economy.

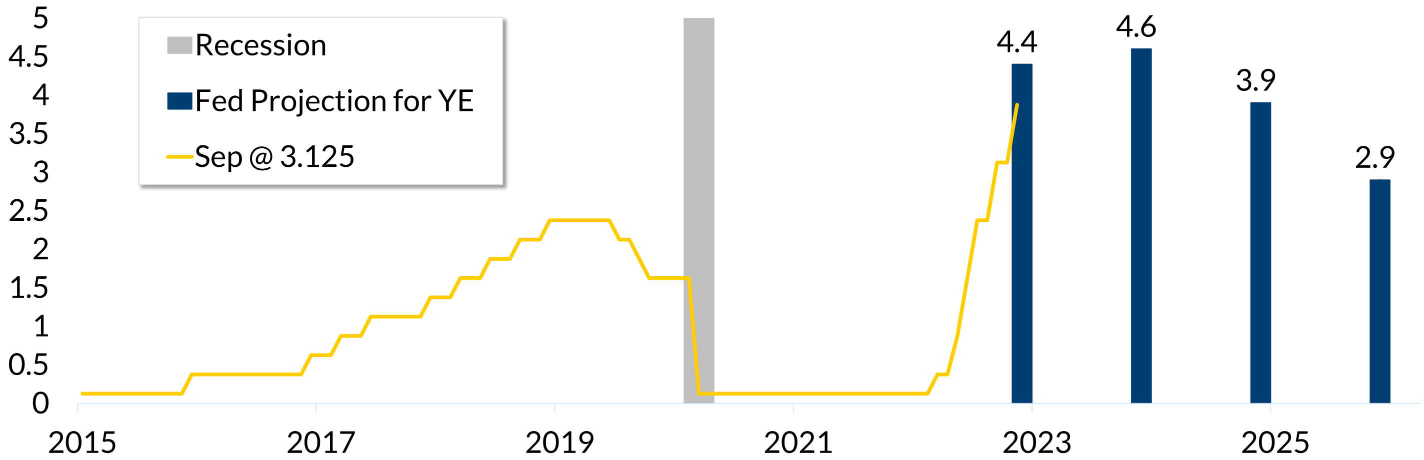
One thing is clear: The Fed does not want to overtighten. Because that would mean they would have to cut interest rates soon. They do not want to cut rates soon because they want time to find the correct level of interest rates. That will help ensure a continuation of economic growth.

Fed Chair Jerome Powell has stated that although the Fed plans to slow the pace of interest rate increases, the Fed may increase the terminal rate of the federal funds rate above the Fed's previous forecast of 4.6%.

KEY QUESTIONS

- What does the recent labor report mean for Fed action?
- Is the current market rally sustainable?
- Are yields still attractive?

Federal Open Market Committee (FOMC) Projections — Federal Funds
%, mid-point



Source: Federal Reserve, November 2022

Please note: Information is subject to change and is not a guarantee of future results.

What does the recent labor report mean for Fed action?

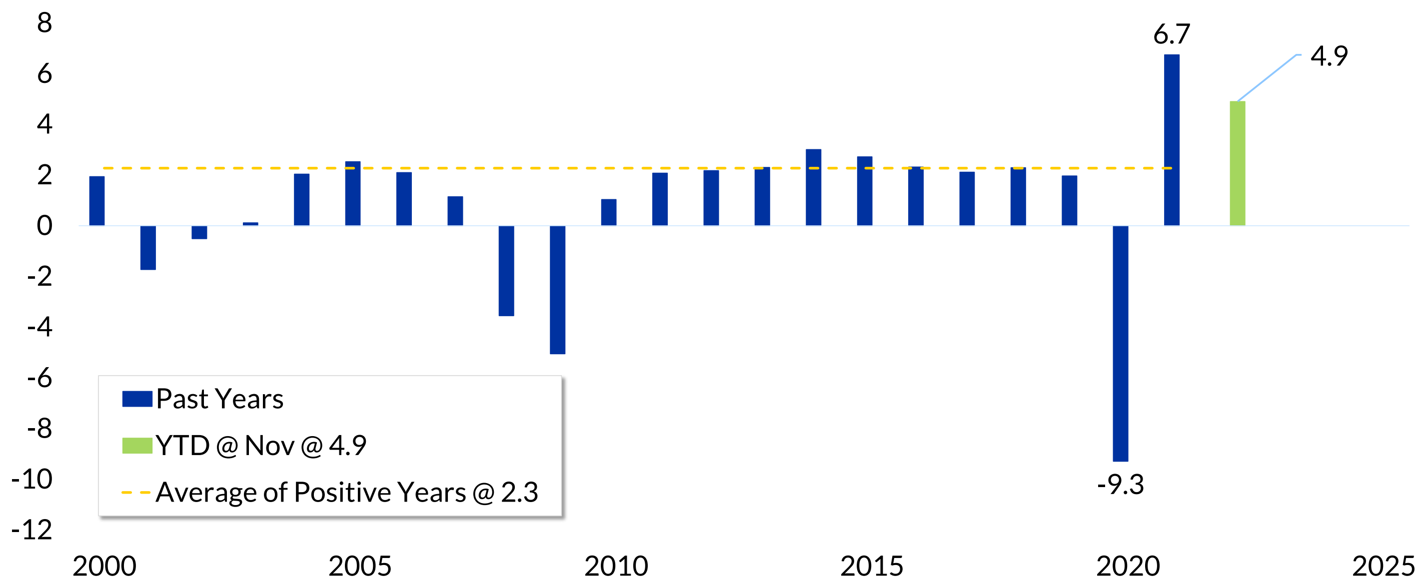
The November report showed that payroll employment slowed only modestly, and hourly earnings re-accelerated.

Nonfarm payrolls increased by 263,000 in November with the unemployment rate remaining at 3.7%, and average hourly earnings jumped to 5.1%.

The labor market has remained resilient this year, with 4.9 million people hired, which is about twice the strength of the average good year *(see chart)*. This is despite the Fed's aggressive interest rate hikes, record low levels of consumer sentiment, and fears of a recession. There have been layoffs in some sectors of the economy (technology, entertainment, and real estate), yet the demand for workers in other parts of the economy remains strong. The need for workers continues to outpace the number of people looking for a job (education, hospitality, and healthcare). Even as workers are being laid off, they are being scooped up by other businesses as job openings remain well above the pre-pandemic levels. Sectors that report shortages of workers are education, healthcare, and hospitality. Many companies are mainly avoiding layoffs because demand for goods and services remains solid. In addition, many companies are reluctant to lay off workers because they found it hard to rehire when the economy rebounded from the pandemic.

For the Fed, payroll growth is not falling fast enough, and wages aren't slowing as quickly as they did during the summer. The strength of this report plays into CNR's belief of the federal funds rate being "higher for longer." This will keep the Fed raising interest rates as it pursues its quest to slow the pace of economic growth. We believe the Fed will raise the fund's rate by 50 bps at its next meeting on December 14. At that meeting, they will probably, in our view, announce a higher terminal rate compared to the September forecast of 4.6%.

Nonfarm Payrolls — Yearly Change
millions, seasonally adjusted



Source: Bureau of Labor Statistics, November 2022
Please note: Information is subject to change and is not a guarantee of future results.

Is the current market rally sustainable?

Fueled by signs of moderating inflation and growing expectations of an easing in the pace of Fed tightening policy, the latest equity market rally has gained steam with the S&P 500 recording its first back-to-back monthly gains in over a year.

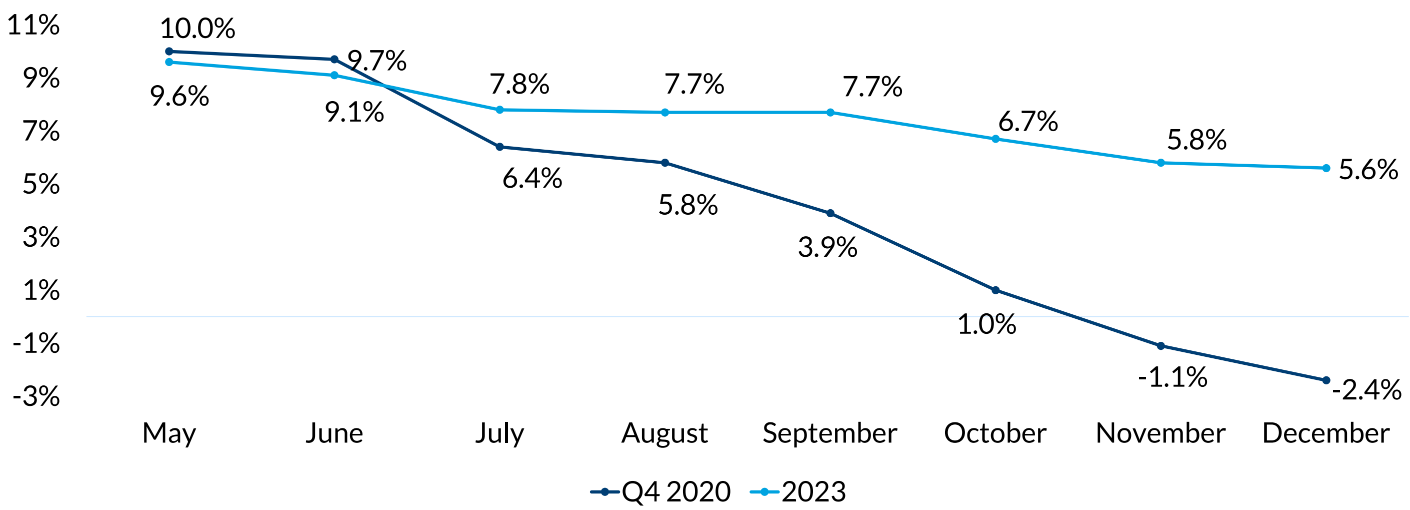
While we agree that recent developments are encouraging, it's important to remember that rallies are common features of bear markets, and history suggests the path to a Fed pivot could be volatile for stocks due to elevated inflation and interest rate risk.

Though Fed Chair Powell last week signaled smaller interest rate hikes ahead amid improving inflationary conditions, overlooked by many investors was his reiteration that the Fed has "a long way to go in restoring price stability" and that this will likely require "holding policy at a restrictive level for some time." Coupled with November's much-better-than-expected jobs report, including continued evidence of strong wage pressures, this is a reminder that policymakers may have to keep interest rates higher for longer.

In the meantime, incoming data continues to point to slowing economic momentum with higher interest rates and rising costs finally hitting the bottom lines of Corporate America. Consensus expectations for Q4 earnings have been cut by 6.4% since the end of last quarter, and estimates for 2023 have started to come down as well. For some time, we have argued that earnings estimates would likely have to be revised lower to reflect the more challenging macroeconomic backdrop ahead and rising recession risk. In a scenario where the economy enters a mild recession next year, we would expect earnings growth to stagnate or even contract.

Given this, we believe it remains too early to signal the all-clear sign. Bottoming will be a process that could take some time to play out, and further swings in sentiment are likely as investors gain greater clarity on the outlook, particularly with rate hikes and inflation, and weigh their implications for the economy and corporate profits. In particular, we suspect further downward earnings revisions could be a catalyst for additional market declines before a sustainable recovery in equity prices can begin.

Evolution of Consensus S&P Earnings Growth Estimates



Source: FactSet

Please note: Information is subject to change and is not a guarantee of future results.

Are yields still attractive?

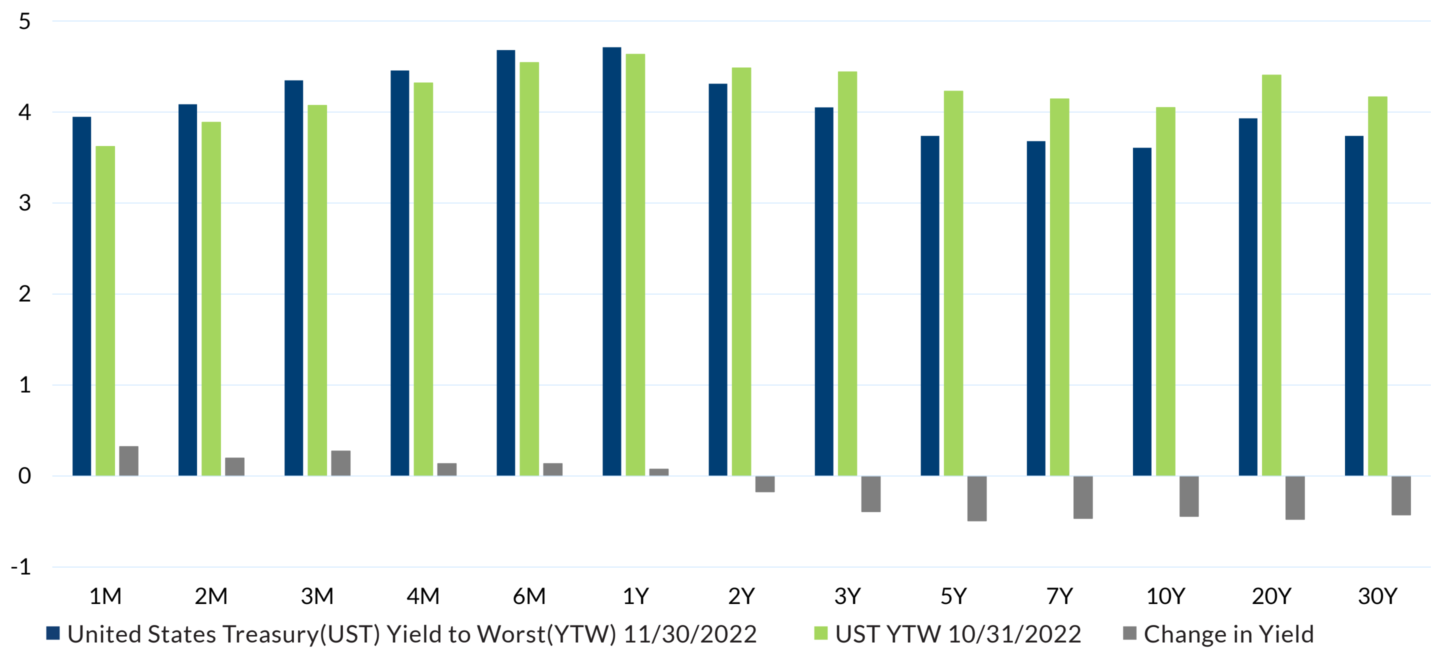
Fixed-income markets have struggled with higher inflation and super-sized interest rate hikes.

Returns for most bonds are negative this year. However, for November, be it fleeting or an early holiday gift, bonds with high-interest rate exposure generated mid-single-digit positive returns. The Bloomberg Treasury 20+ Year Index rose 7.28% for the month while the Bloomberg Long Corporate Index returned 9.08%.

Given the brisk adjustment in rates, fixed-income investors are wondering if they have missed the peak in yields. We do not think so as the high end of our forecasts continues to incorporate yields above 4.0%. CNR's approach is always to take a long-term view of asset allocation and portfolio strategy, and we believe investors should take advantage of the highest treasury and investment-grade corporate yields in over a decade. We recommend a steady shift over the next several months into high-quality bonds to lock in exceptional risk-adjusted returns and increase income.

Looking forward, recessionary forces will build, the Federal Reserve is expected to pause interest rate hikes, and the market is pricing in potential cuts to interest rates in late 2023 and 2024. Taken all together, CNR expects the cumulative effects of these forces to push yields lower than what is available today.

Despite a Twisting of the Yield Curve, Opportunities Remain



Source: Bloomberg, November 2022

Please note: Information is subject to change and is not a guarantee of future results.

IMPORTANT DISCLOSURES

The information presented does not involve the rendering of personalized investment, financial, legal, or tax advice. This presentation is not an offer to buy or sell, or a solicitation of any offer to buy or sell, any of the securities mentioned herein.

Certain statements contained herein may constitute projections, forecasts, and other forward-looking statements, which do not reflect actual results and are based primarily upon a hypothetical set of assumptions applied to certain historical financial information. Certain information has been provided by third-party sources, and although believed to be reliable, it has not been independently verified, and its accuracy or completeness cannot be guaranteed.

Any opinions, projections, forecasts, and forward-looking statements presented herein are valid as of the date of this document and are subject to change.

There are inherent risks with equity investing. These include, but are not limited to, stock market, manager, or investment-style risks. Stock markets tend to move in cycles, with periods of rising prices and periods of falling prices.

Investing in international markets carries risks such as currency fluctuation, regulatory risks, and economic and political instability.

There are inherent risks with fixed-income investing. These may include, but are not limited to, interest rate, call, credit, market, inflation, government policy, liquidity, or junk bond risks. When interest rates rise, bond prices fall. This risk is heightened with investments in longer-duration fixed-income securities and during periods when prevailing interest rates are low or negative.

Investing involves risk, including the loss of principal.

This material is available to advisory and subadvised clients, as well as financial professionals working with City National Rochdale, a registered investment adviser and a wholly owned subsidiary of City National Bank. City National Bank provides investment management services through its subadvisory relationship with City National Rochdale.

Readers are cautioned that such forward-looking statements are not a guarantee of future results and involve risks and uncertainties, and actual results may differ materially from those statements.

Indices are unmanaged, and one cannot invest directly in an index. Index returns do not reflect a deduction for fees or expenses.

All investing is subject to risk, including the possible loss of the money you invest. As with any investment strategy, there is no guarantee that investment objectives will be met. Diversification does not ensure a profit or protect against a loss in a declining market. Past performance is no guarantee of future performance.

Any opinions, analysis, and expectations mentioned herein are as of December 8, 2022, unless otherwise noted or sourced.

INDEX DEFINITIONS

S&P 500 Index: The S&P 500 Index, or Standard & Poor's 500 Index, is a market-capitalization-weighted index of 500 leading publicly traded companies in the U.S. It is not an exact list of the top 500 U.S. companies by market cap because there are other criteria that the index includes.

Bloomberg Barclays U.S. Corporate High Yield Bond Index measures the USD-denominated, high-yield, fixed-rate corporate bond market.

Moody's Investors Service, often referred to as Moody's, is the bond credit rating business of Moody's Corporation, representing the company's traditional line of business and its historical name. Moody's Investors Service provides international financial research on bonds issued by commercial and government entities.

CPI: A consumer price index (CPI) is a price index, i.e., the price of a weighted average market basket of consumer goods and services purchased by households. Changes in measured CPI track changes in prices over time.