CITY NATIONAL ROCHDALE
AN RBC/CITY NATIONAL COMPANY

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ON THE RADAR

FAQs on the Markets and Economy

Has CNR's outlook for stocks changed?

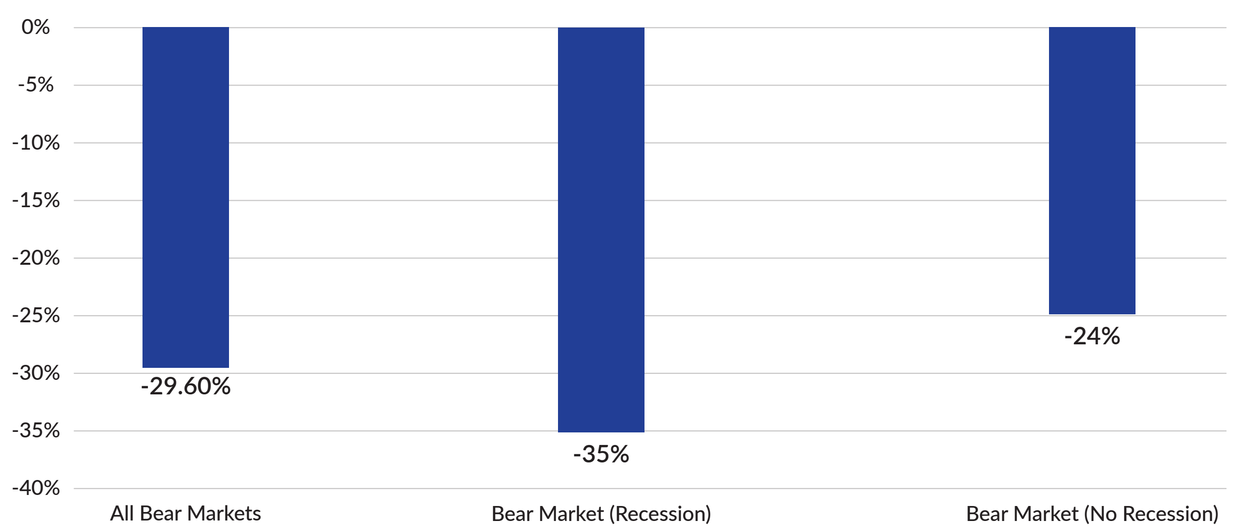
Investors are increasingly concerned about the risk of a recession as the U.S. stock market enters a bear market and the Fed's fight against inflation intensifies.

Regarding the outlook for the economy, we see both positives and negatives: U.S. fundamentals, especially those for households, are still broad and powerful and should provide some cushioning against rising headwinds. Conversely, inflation is more sustained than originally estimated and geopolitical uncertainty is increasing, slowing economic momentum and reducing consumer and corporate confidence from 30% to 50% in 2023. Executing a soft landing is difficult under the best of circumstances, and Fed officials have no standard playbook for the multitude of uncertainties that exist around today's outlook, raising the possibility of a policy mistake.

As risks have increased over the past few months, we have been proactively lowering our overall equity exposure in client portfolios and are now at a modest underweight. Although the S&P 500 has corrected roughly 20% so far, recessionary bear markets have historically declined 30-35% on average, suggesting further declines in stock prices are possible in coming months. Despite valuation adjustments, consensus earnings estimates have not yet discounted an increasing risk of an economic downturn.

Before a more durable bottom in markets is reached, we think investors will need better clarity on the path of inflation and Fed tightening, as well as the outlook for sustainable economic and earnings growth. In the meantime, we remain focused on holding high-quality, reasonably valued U.S. companies with durable franchises and strong management teams to help weather a recession should one occur.

Average S&P 500 Bear Market Drawdown



Source: FactSet, CNR Research

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Yields and Inflation: A Rough Rule of Thumb?

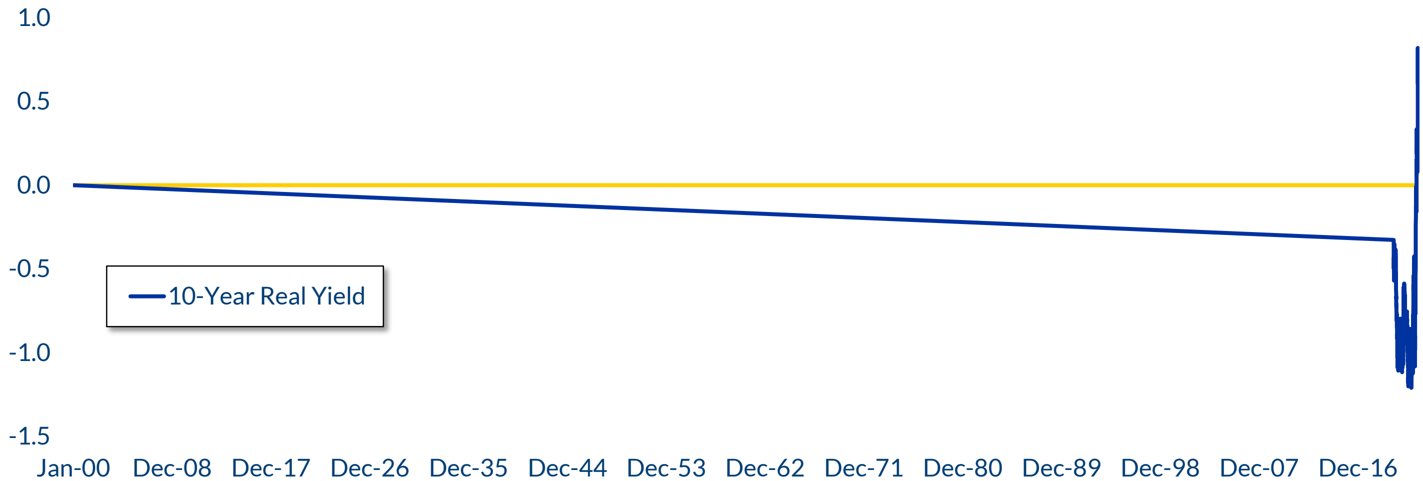
Over the past 20 years, interest rates have only been this volatile three times before today, according to the MOVE Index – a measure of implied volatility in U.S. Treasury options.

In environments like this, emotions run high, and fear grips the market. As investors, what can we do to look through the volatility and gauge longer-term results, especially when it comes to rates?

Inflation hasn't been around in 50 years, which means we need to break out old tools to understand how rates might behave and what the longer-term 10-year Treasury yield could average over the next 10 years. In that pursuit, we use a simple calculation to adjust yields for inflation and analyze this historically. Over 20 years, for pre-and post-quantitative easing as a policy tool, the average is about 1.4%. Compared to today's 0.70% level, the market is only half of the long-run average. There are two ways this number can increase. The first is from rising Treasury yields and the second is from falling long-term inflation expectations. Amazingly, longer-run inflation expectations have remained incredibly well anchored, with 10-year expectations only moving up 0.26%. As a result, most of the increase over time will come from rising Treasury yields.

This doesn't mean the market will not overshoot the long-term average or stay lower for longer, but by using this as an anchoring point, we should expect Treasury yields to eventually reach 4% beyond 2022, which is also consistent with the Federal Reserve's long-run estimates.

U.S. Treasury 10-Year Yield Adjusted for Inflation



Source: Bloomberg
Please note: Past performance is no guarentee for future results.

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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.

CalPERS: The California Public Employees' Retirement System, also known as CalPERS, is an organization that provides numerous benefits to its 2 million members, of which 38% are school members, 31% are public agency members and 31% are state members.

CPI: A consumer price index (CPI) is a price index, 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.

4Ps: The 4P analysis is a proprietary framework for global equity allocation. Country rankings are derived from a subjective metrics system that combines the economic data for such countries with other factors including fiscal policies, demographics, innovative growth and corporate growth. These rankings are subjective and may be derived from data that contain inherent limitations.

MOVE Index: Bloomberg Ticker "MOVE" – Statistic is computed by ICE BofA

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