CITY NATIONAL ROCHDALE
AN RBC/CITY NATIONAL COMPANY

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ON THE RADAR

FAQs on the Markets and Economy

Has inflation started to respond to the Fed's interest rate hikes?

Not yet, inflation is still running hot.

The September's gain in Consumer price index (CPI) was up 0.4% Month-over-month (MoM) and 8.2% Year-over-year (YoY), down from 8.3% last month. Core inflation *(which excluded food and energy prices)* jumped to 6.6%, marking a 40-year high.

Core-service inflation continues to explode higher; prices rose 0.8%, the largest monthly increase of the cycle. This was driven by housing costs, which had their largest jump of the cycle. Although the market price in housing has turned a corner, the price data for CPI has built-in stabilizers for the CPI calculation and do not show the moderation. For example, since the pandemic's start, home prices are up over 40%, rents are up over 20%, and CPI rent is up only 11%. Another area for higher inflation has been with medical services responding to higher wages.

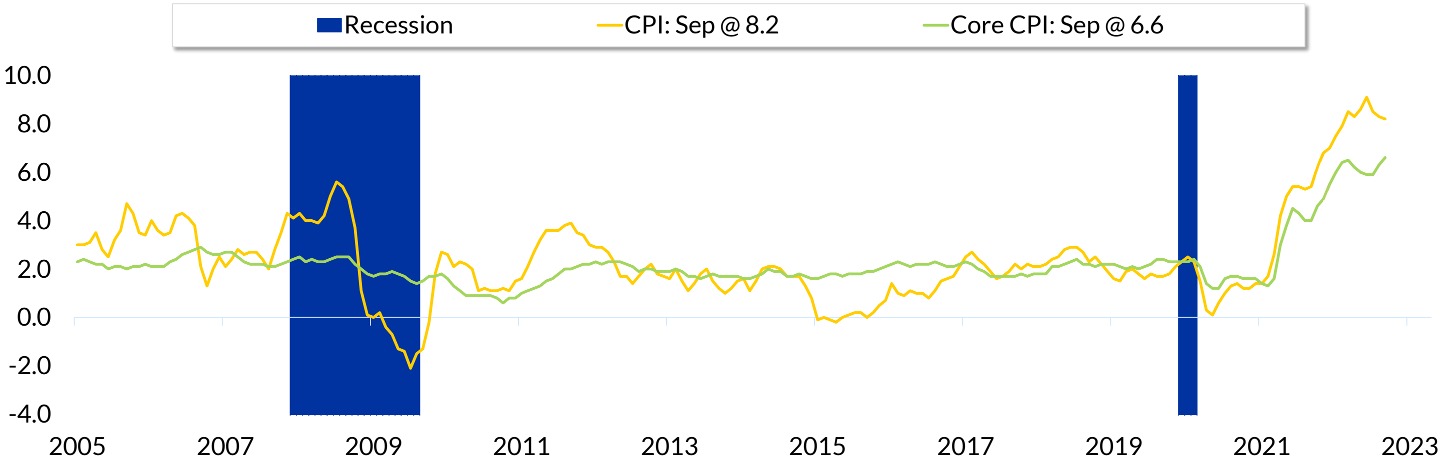
September's CPI gain was more substantial than expected. This report cements the need for a 75 basis points (bps) increase in the federal funds rate at the Fed's Nov 2 meeting *(that has been our base case for a while but wasn't fully priced into the market)*. There will be two more CPI reports before the December 14 FOMC meeting. It will give the Fed more information going into the meeting, in which they currently plan a 50 bps hike.

KEY QUESTIONS

- **Is the worst for markets behind us?**
- **Is the labor market responding to the Fed's raising of interest rates?**
- **Do we expect municipal credit deterioration from Hurricane Ian?**

CPI & Core CPI

% change YoY, not seasonally adjusted



Source: Bureau of Labor Statistics, September 2022

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

Is the worst for markets behind us?

Investors have had few places to hide in 2022, with both equity and fixed-income markets simultaneously recording three consecutive negative quarters for the first time in over four decades.

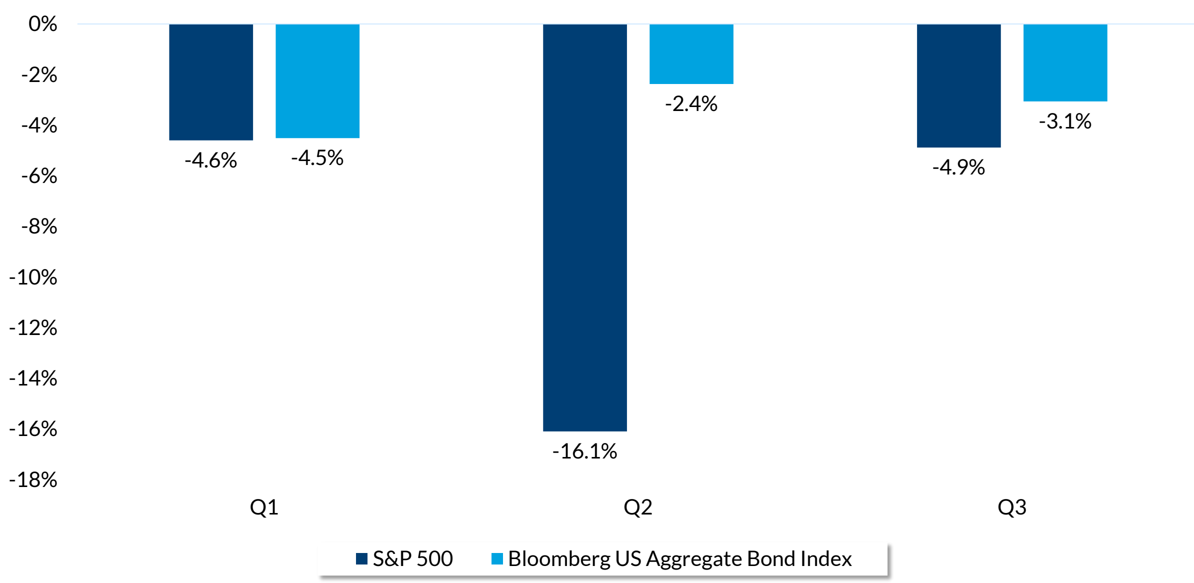
Unfortunately, we think volatility looks set to continue near term. Investors still have a long list of uncertainties to ponder, including slowing U.S. growth and overly optimistic earnings estimates, rising financial stress abroad, Europe's increasing energy crisis, and the ongoing Russia-Ukraine war. Most importantly, the persistence and breadth of inflation have provided an unwelcomed reminder to markets that rates may stay higher for longer than anticipated.

For some time now, CNR has maintained our above-consensus views on recession probability, the upward path of interest rates, and geopolitical risks. It is now clear that central banks around the world will raise interest rates even further than our above-consensus forecasts had implied, making the current tightening cycle the most aggressive in three decades. Given this, we now see the global economy entering a recession next year and the probability of recession in the U.S. rising to 60%.

The prospect of even tighter monetary policy in the near term points to the potential for a sharper slowdown in economic and corporate profit growth than is currently factored into market expectations. As a more challenging outlook for both the economy and corporate earnings is discounted, stock markets could continue to grind lower, even if government bond yields do not rise any further.

Historically, the S&P 500 has declined about 31% in a bear market, which means the current bear market low of about 25% is still well below average. Bottoming will likely be a process that could take some time to play out, with further swings in sentiment as investors gain greater clarity on the outlook. Looking forward, we continue to think that inflation and the response from policymakers will ultimately determine the direction of travel for markets ahead. Until a pattern of lower inflation readings is established, equities are likely going to have a hard time mounting a sustainable rebound, and bonds could remain under pressure.

2022 Asset Class Performance



Source: Bloomberg

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

Is the labor market responding to the Fed's raising of interest rates?

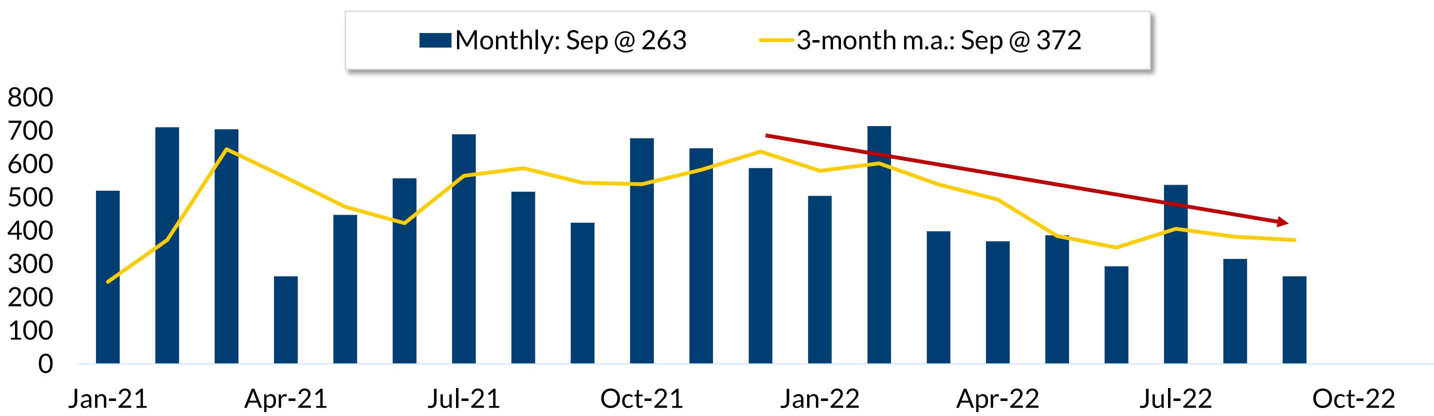
The Fed's goal of raising interest rates has been to slow down consumer demand, leading to lower price pressures.

Nonfarm payroll (NFP) development decelerated in September to 263,000 from 315,000. Consequently, there's an extension of the slowing down in labor need, bringing the three-month alter to 372,000 *(see chart)*.

Wage growth continues to decelerate, which is good news for the Fed. The monthly gain was just 0.3% for the second month. The yearly change dropped to 5.0% from 5.2%. For comparative purposes, most of the past expansion was between 2% - 3%. But the pace of wage gains has been slowing since March; the recent three-month change annualized is just 2.4%. But this decline is not consistent with the Employment Cost Index data or the Atlanta Fed Wage Tracker, which are better measurements of wages, so there is no victory to be declared yet.

Gradual improvements cannot be mistaken for a completed journey, and the Fed has yet to see significant weakness in the labor market from its rate hikes. This month's gain in NFP and the decline in the unemployment rate *(3.5%)* support the case for continued aggressive Fed hikes. The Fed's current plan implies a 75 bps hike in November and a 50 bps hike in December.

Nonfarm Payrolls
'000, seasonally adjusted



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

Do we expect municipal credit deterioration from Hurricane Ian?

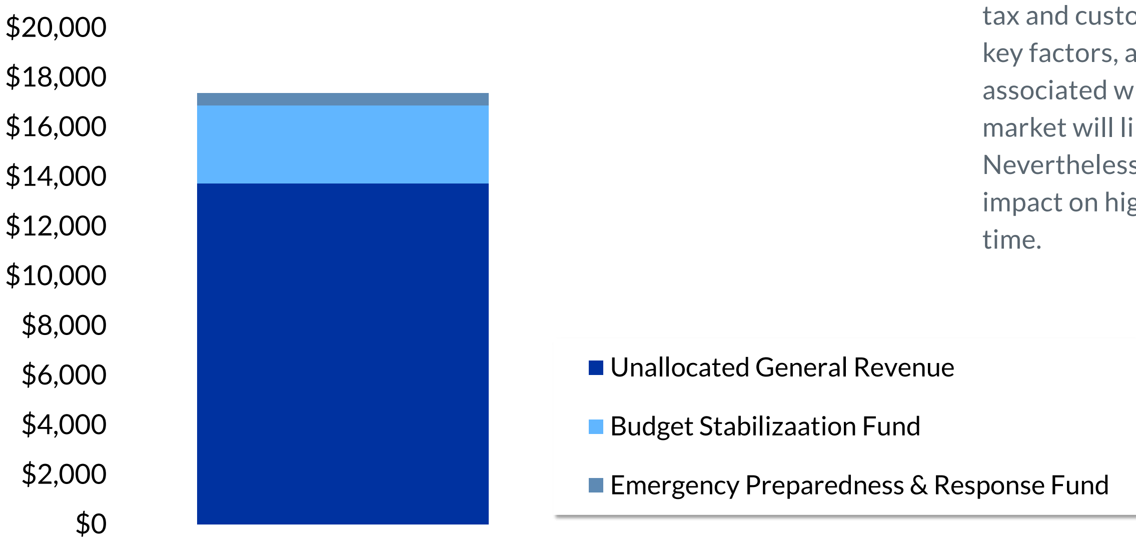
According to risk modelers, Hurricane Ian caused significant damage to property and infrastructure across parts of Florida that could reach tens of billions in insured losses.

While it is too early to determine the particular impact on the most affected issuers, the availability of federal/state aid, insurance proceeds, and other resources generally support credit quality. A federal disaster declaration will release FEMA funds to local governmental communities and enterprises *(LGs)*. FEMA relief funds reimburse at least 75% of eligible infrastructure repair and replacement storm-related costs. But due to timing lags in FEMA, in the near term, LGs will rely upon their internal liquidity and, more importantly, state assistance to fund emergency response, clean-up, and restoration needs. Favorably, given the storm-prone nature of Florida, over the years, many LGs developed planning practices and policies with contingencies to counter unforeseen circumstances. These efforts are critical in helping manage their credit quality.

The fiscal position of Florida State should guard its credit profile against potential economic and financial fallout from the storm but also enhances its ability to help its LGs. The revised financial outlook released in September 2022 shows general state reserves anticipated for FY 2022-23 of more than $17B *(with additional funds in various Trust accounts)*, providing ample flexibility. The state's $500 million allocation towards disaster response will assist with the aftermath. Recently, the Governor announced the state's commitment to subsidizing a significant share of the costs of LGs to alleviate financial pressure and accelerate rebuilding *(e.g., transportation/utility infrastructure)*. We expect LGs to lean on their internal cash balances and, in some instances, access bridge loans or short-term debt to meet their operational needs until aid and other support are received.

We will monitor the situation closely but don't expect material rating pressure for most issuers. It is unlikely that missed payments will occur from fundamental erosion in the capacity to pay debt service. According to Municipal Market Analytics, Florida has experienced only a single investment grade [safe sector] default in the last fourteen years *(the Santa Rosa Bay Bridge)*, which the Governor recently cured with a full repayment. Thus, the state demonstrates historical support for its LGs. Over the medium-to-longer term, economic tax and customer base changes are key factors, and the uncertainty associated with the state's insurance market will likely have implications. Nevertheless, we see limited credit impact on high–grade issuers at this time.

FY 2022-23 Anticipated Reserves ($milllions)



Source: State of Florida Long-Range Financial Outlook Fall 2022 Report, Pre Hurricane Ian

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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.

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.