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CITY NATIONAL ROCHDALE
AN RBC/CITY NATIONAL COMPANY

July 2024

ECONOMIC & INVESTMENT MANAGEMENT PERSPECTIVES

QUARTERLY UPDATE

Market Update: Bending, Not Breaking

Charles Luke, CFA
Chief Investment Officer

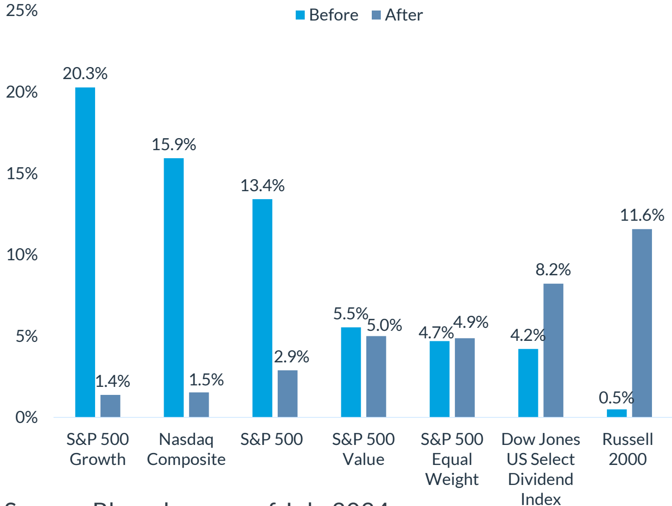
As the current expansion enters its fifth year, the US economy is clearly downshifting. Economic growth over the first half of 2024 averaged 2.1%, roughly a percentage point lower than the pace recorded in the second half of 2023.

Companies are hiring fewer workers and consumers are exercising more caution as high interest rates put pressure on spending. While those dynamics might seem worrying on paper, the current trajectory suggests a normalization to a slower but more sustainable rate of growth is occurring, as opposed to the beginning phases of a recession.

At the midpoint of the year, equity markets are experiencing an uptick in volatility and a shift in market leadership. Value and cyclical parts of the market, including small- and mid-cap stocks, have rallied over the past month, while growth stocks, especially the mega-cap tech names responsible for the lion's share of market gains over the first half of the year, have lagged. There have been many factors at play behind this rotation, ranging from a broadening in earnings growth and better relative valuations outside of tech to expectations of U.S. election–driven policy shifts.

Chart 1: 2024 Market Performance

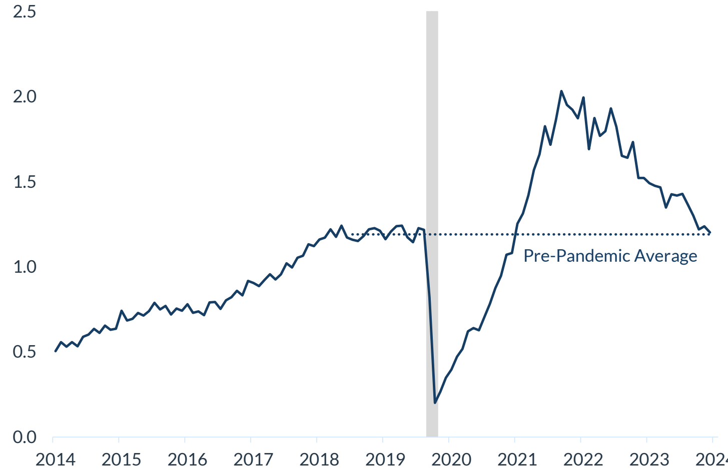
Before & After May CPI Data Release on 6/12/24



Source: Bloomberg, as of July 2024.

Past performance is no guarantee of future results.

Chart 3: Jobs Available Per Unemployed Worker

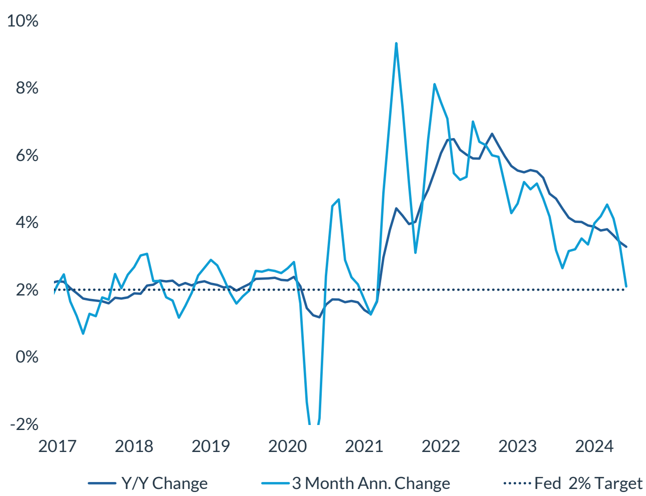


Source: St. Louis Fed, as of June 2024.

Past performance is no guarantee of future results.

Above all, it has been a series of better-than-expected inflation readings that have assured investors that Fed rate cuts are around the corner. Entering 2024, it was not clear that the Fed would risk cutting rates as signs of an overheating economy and stubborn inflation were evident. But these issues now appear to be solved. Measures of labor market tightness have fallen sharply and are now only slightly above pre-pandemic levels, on average. Meanwhile, since peaking at a 40-year high of 6.6% two years ago, the three-month annualized rate of change in core CPI inflation has slowed to just 2.1% – the lowest level since March 2021 and not far from the Fed's 2% target.

Chart 2: Core CPI Inflation



Source: St. Louis Fed, as of June 2024.

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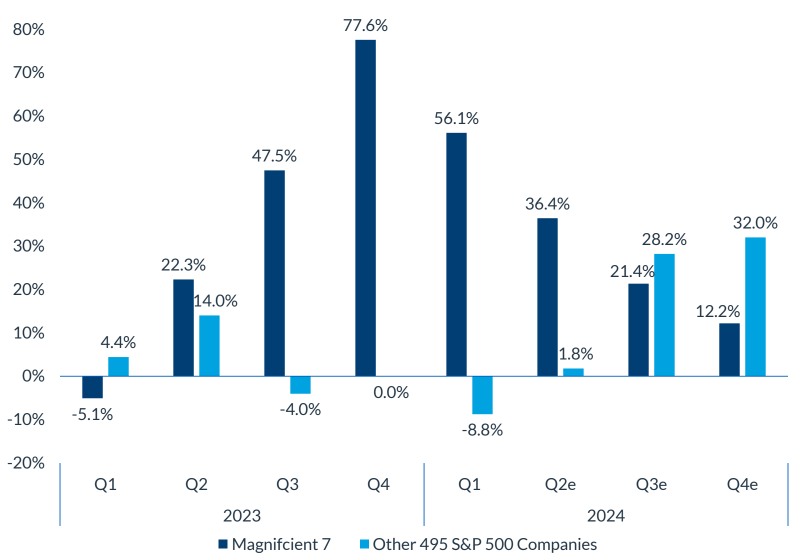
After the upheaval of the past few years, the most aggressive Fed tightening cycle in decades seems to be having the intended effect by bringing supply and demand into better balance. Evidence continues to build for a soft landing, and parts of the economy will continue to struggle against higher rates, including manufacturing, housing and lower-income households. But at this point, the economy has survived tighter Federal Reserve policy without any major signs of severe macroeconomic vulnerabilities. Most notably, and so far absent this cycle, is the development of excess leverage that can create over-investment and spark the type of extended credit cycles that have historically presaged recessions.

For the Fed, this means the tradeoffs are shifting. We have revised our expectations for Fed rate cuts, as incoming inflation and labor data now support a case for an initial rate cut in September and possibly another before the end of the year. We continue to believe officials will be content to take it slow, seeking to reduce rates enough to prevent unnecessary weakness in the economy, while trying to avoid reigniting inflation pressures and the need to keep rates high. Still, the bigger backdrop of a Fed rate-cutting cycle is broadly supportive of sustained economic growth and favorable investment conditions.

After such a strong rally in the equity market, value- and income-oriented stocks that have been dormant are springing to life as investors seek investments that have more room for valuation expansion and that could benefit from lower interest rates. One of the keys coming into 2024 was the expansion of the market rally outside of technology, and it is now clear this is happening after Q1 earnings season and projections for Q2 show a broadening resurgence in earnings.

While technology sectors appear to have stretched valuations and could be due for a correction, a combination of defensible earnings streams and long-term AI growth prospects will remain a tailwind for that group. We believe that the development of AI technology and its impact across the economy is a long-term trend that remains in the early phases. That said, we think the market rotation underway reflects what could be a more durable trend in which lagging sectors and segments market play catch-up, fueling additional gains. The rate of technology- and growth-oriented companies is moderating, while profitability among the rest of S&P 500 is forecasted to accelerate in coming quarters.

Chart 4: S&P 500 Consensus Y/Y Earnings Growth



Source: Factset, as of June 31, 2024.

Indices are unmanaged, and one cannot invest directly in an index. Past performance is not a guarantee of future results.

For the moment, we continue to be positioned well for this move with exposure to income-oriented and mid-cap stocks, alongside high-yield credit exposure, which has benefited from higher treasury rates and resilient economic growth. But, as investors continue to reset expectations within a longer-term market advance, more divergence is likely, which should create tactical opportunities. We will be looking for these pivot points in the months ahead to add quality investments to portfolios and to diversify allocations to participate in the broadening of market returns.

Core Equity: Staying the Course on Long Term Secular Growth

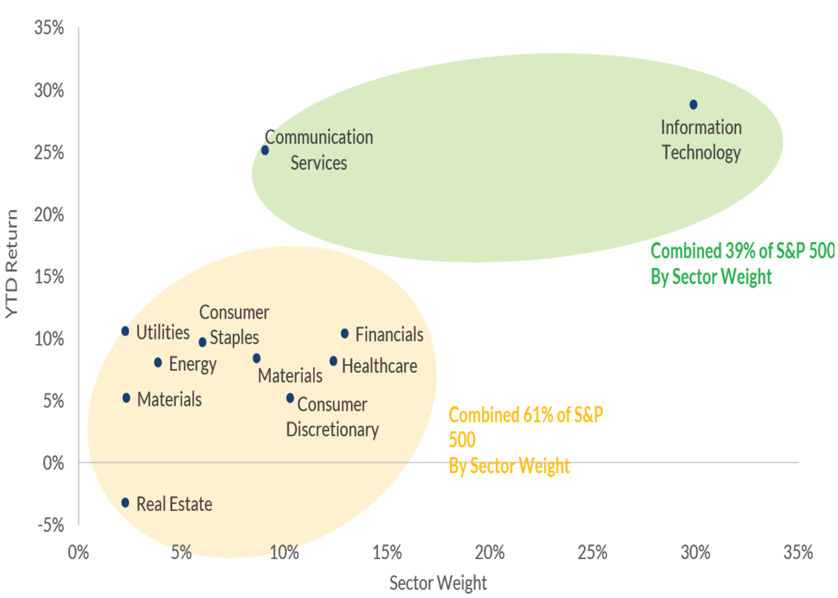
Amy Chen, CFA
Director, Senior Equity Analyst

The S&P 500 finished the first half of 2024 near record highs and up 15.3%. While the advance has continued to be driven by growth stocks, especially tech-related, more sectors are participating in the rally this year, delivering solid to strong returns overall year to date.

Given high valuations, the Core Equity strategy remains balanced and continues to favor secular growth and high-quality companies, which exhibit above-average margins, earnings growth, and return on invested capital.

In Q2, Core Equity returned 4.93%, 65 bps ahead of S&P 500, net of fees. Healthcare, Consumer Staples, and Industrial sectors led performance. Within Healthcare, we prefer biotech pharmaceutical companies over healthcare service providers, as we see greater financial benefits from drug development and fewer policy risks. Companies with exposure to weight loss, cancer, chronic pain, and gene therapy drugs make up the majority of our exposure. In Consumer Staples, two of the companies we own won additional market share by being the price leaders in the industry. EDLP (everyday low price) has gained popularity, as low-end consumers struggle with inflation and high borrowing costs. In the Industrials sector, companies leveraging the benefits of AI, particularly within the data center, electricity, and HVAC businesses, had strong performance.

Chart 1: YTD S&P 500 Return vs Sector Weight



Source: FactSet, as of June 2024.

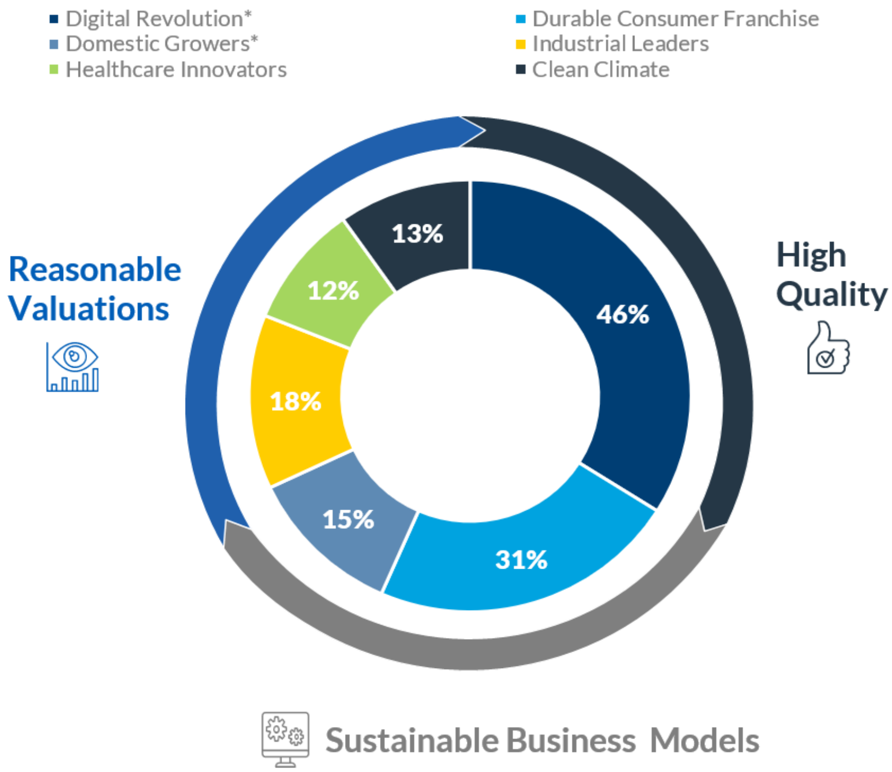
Information is subject to change and is not a guarantee of future results. Indices are unmanaged, and one cannot invest directly in an index.

Using quantitative and fundamental research, the Core Equity portfolio is structured by layering quality and valuation metrics over long-term secular themes of Digital Revolution, Durable Consumer Franchises, Healthcare Innovators, Domestic Growers, Industrial Leaders, and Clean Climate, while minimizing risk. During Q2, portfolio tracking error fell from 2.4% to 2.2%, and positioning continued to shift toward the AI mega trend with increases in semiconductor, hyperscale cloud operator, and digital media platforms, and reductions in traditional industries like cable networks, cellular carrier, and payment companies.

KEY POINTS

- Continue to focus on high-quality companies.
- Balanced exposure between cyclical and defensive sectors.
- Positioning toward AI mega trend and beneficiaries.

Chart 2: Thematic Research Focus



Source: CNR Research, as of July 2024.

*Some stocks are included in more than one theme. Information is subject to change.

Equity Income: Concentrating on Dividend Stocks

David Shapiro
Senior Portfolio Manager, Equity Income

Tony Hu, CFA, FRM
Senior Portfolio Manager, Equity Income

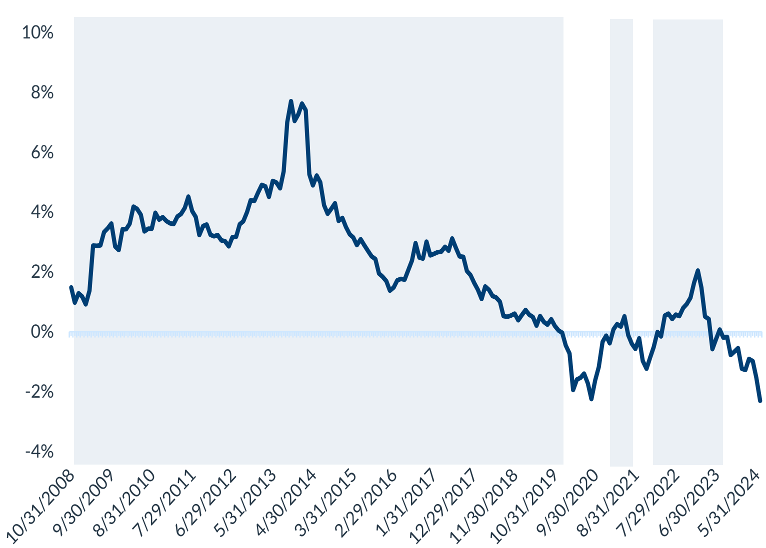
By now it's been well covered by our colleagues and elsewhere that the market has been powered to new highs by the gains of a small number of mega-cap stocks.

Market concentration is back to peaks last seen during the Tech Bubble 25 years ago. **And market breadth has been weak – the average stock has meaningfully underperformed the market.** As of mid-year, the market cap-weighted S&P 500 has outperformed the equal-weighted S&P by more than 10%.

We thought it would be interesting to see how the relative performance of our dividend universe compares to market breadth. The accompanying chart shows 5-year rolling relative returns of our dividend stock universe vs. the S&P 500. The highlighted portions are periods during which the 5-year rolling returns of the equal-weighted S&P outperformed the cap-weighted S&P. In addition to showing that over this medium-term time frame both the equal-weight and dividend stocks have tended to outperform, it also demonstrates that **dividend stock returns tend to outperform when the broader market outperforms.**

And why would this occur? Well, for one thing, **both operate on a "buy low/sell high" basis.** They both rebalance. The equal weight index has to sell its top performers (and buy the losers) to stay equal weight, while our dividend index does the same to maintain yield. **They both therefore will underperform a cap-weighted index when its performance is dominated by mega-caps that are allowed to run. And they should outperform when mega-cap gains have run their course, for whatever reason, as we have seen in the past.**

Chart 1: Dividend Stock Outperformance and Market Breadth



Source: FactSet, as of 6/30/2024.

Past performance is no guarantee of future results.

DJDVP vs. S&P 500 rolling trailing 5-year returns. The shaded portion covers when equal weight S&P 500 (RSP) vs. S&P 500 rolling trailing 5-year returns are positive.

What could cause that? A number of things, all of which are hard to time, but which ultimately, in the past, have proven to be important. Relative valuation. High-yielding dividend stocks are value stocks. Inflections in relative earnings growth. Macro-economic conditions. Competitive forces, further technological shift, regulatory scrutiny. Dynamics that have helped put an end to eras of mega-cap market dominance in the past.

We do think the time will come when we see an ebb in market concentration, and when the diversification benefit of a portfolio of attractive yielding stocks to moderate volatility will come into play. **Until it does, we are happy to continue to collect our portfolio income and watch our portfolio income (and value) compound at its historical +MSD dividend growth rate.**

KEY POINTS

- Concentrated markets impact attractive dividend stock relative performance.
- Dividend stock outperformance appears correlated with periods of market breadth.
- History suggests we will see a return to both broader market strength and dividend stock outperformance at some point.

Taxable Strategies: Changes on the Horizon?

Michael Taila, CPWA®
Managing Director, Head of Fixed Income

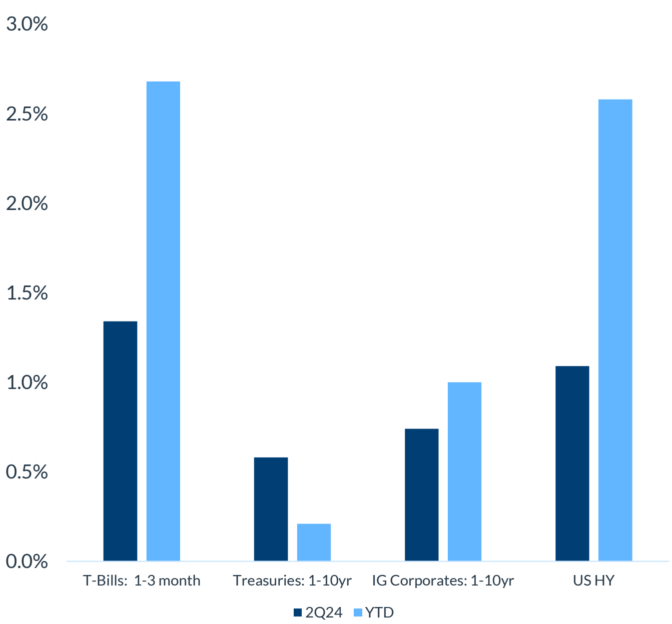
David Krouth, CFA
Director, Senior Portfolio Manager

Macroeconomic and monetary policy sentiment shifted during the second quarter as leading indicators fell from February highs, and downward progress on inflation was evident, but slower than expected.

This led the market to believe the higher-for-longer interest rate outlook gained a foothold. The change in market perception dampened expectations for Fed rate cuts to as few as 0-to-2 by year-end. The volatility that developed resulted in increased Treasury yields. For example, the 10-year U.S. Treasury bond increased about 60 bps to 4.7% by late April, but because of weaker-than-expected data (e.g., consumer spending and CPI), yields settled at 4.4% by quarter-end. As confidence emerges, a loosening of policy could be warranted (chart 1). City National Rochdale currently has a 10-year U.S. Treasury range of between 4.1% and 4.6%.

Most taxable asset classes closed out 1H2024 in positive territory (chart 2). Interestingly, longer maturity bonds are beginning to outperform shorter tenors, including T-Bills. As prevailing yields remain attractive across many segments of the taxable fixed income markets and confidence re-emerges on rate cuts this fall, we are positioned neutral to our

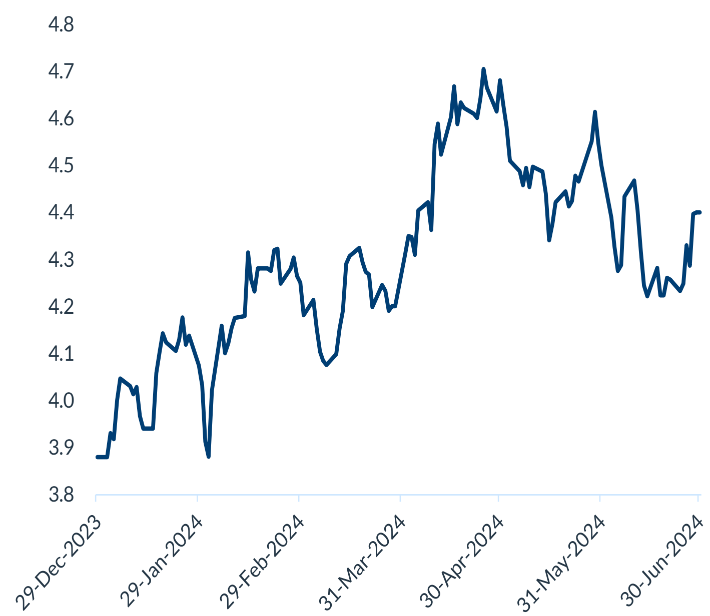
Chart 1: Q2 and YTD Returns



Source: Bloomberg, as of June 30, 2024.

Past performance is no guarantee of future results.Indexes are unmanaged and do not reflect a deduction for fees or expenses. Investors cannot invest directly in an index. Information is subject to change and is not a guarantee of future results.

Chart 2: 10-Year Treasury Yield



Source: Bloomberg, as of June 30, 2024.

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various benchmarks. Should geo-political risk or fluctuating data impact the market, we maintain the flexibility to respond. Selectively adding duration by pushing further out on the curve into longer maturity strategies could add value to investor portfolios. Rotating from T-Bills, for example, which have elevated reinvestment risk, into medium-term bonds could lock in compelling yield for an extended period and potentially provide enhanced total return.

The technical and fundamental backdrop has led to U.S. investment grade (IG) and high yield corporate (HYC) quality spreads remaining near multi-decade lows. Continued, albeit moderating, economic growth has supported issuer credit profiles so far this year. For example, interest coverage ratios, which are a standard measurement of debt serviceability, are healthy, while default experience among HYC is running slightly below long-term averages. With gross issuance up roughly 25% YoY through Q2 and total fixed income bond flows positive, this supply and demand balance has helped support bond prices. Within the IG space, option-adjusted spread as a % of total yield is below historical averages and reflects net demand for bonds. We expect current conditions to persist in the short run, but an unexpected drag on the economy, coupled with volatility as the November elections near, could lead to spread widening. Thus, research due diligence is critical, but we would see market dislocation as a potential entry point for investors.

KEY POINTS

- April may have been the near-term peak in Treasury yields.
- Extend portfolio maturities to capture income and increase forward-return potential.
- Credit fundamentals remain sound.

Tax-Exempt Strategies: Taking the Temperature on Municipals as Summer Heats Up

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Managing Director, Head of Fixed Income

William D. Black, CFA
Managing Director, Senior Portfolio Manager

Michael Korzenko, CFA
Director, Senior Analyst, Municipal Credit Research

Investment grade municipals (IGM) closed out the second quarter in a neutral position as losses during April and May were offset by the strongest June monthly performance since 2016, per the Bloomberg Municipal Bond Index.

Year to date, IGM delivered a respectable -.4% total return versus -.86% for U.S. Treasuries. Longer maturity and lower quality bonds were among the best performing areas of the municipal bond market. One bright spot in fixed income is the stellar performance of high yield municipal bonds (HYM). According to the Bloomberg Municipal High Yield Bond Index, the YTD total return was above 4% through 1H2024. The relative strength of IGM and HYM bonds this year is attributed, in part, to absolute yields that remain attractive despite the volatility in the financial markets. The value of the tax exemption tends to increase as yields rise. With currently available yields in IGM and HYM bonds bouncing around levels still higher than in years prior, taxable equivalent basis on these

Chart 1: Municipal Bond Yields Remain Compelling

Source: Bloomberg, as of June 30, 2024.

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segments of more than 6% and 9%, respectively, are quite enticing for longer-term investors.

The technical backdrop for municipal bonds has turned very exciting so far this year. On the supply side, gross sales of more than $240 billion during 1Q and 2Q (about a 40% increase YoY) has provided investors with ample bond choices to put cash to work in portfolios. As issuers pull forward deals ahead of election uncertainty and feel more comfortable in the current interest rate environment (vs. 2023), supply is projected to remain strong at least in the near term. The absorption of supply is due to healthy demand for the asset class. Municipal bond mutual fund flows have continued to improve from the record outflows of 2022. On the year, net inflows have helped support the market, leading to more fully valued bonds and tighter credit spreads. The interplay between supply and demand could weaken after the summer as the election comes more into focus. Thus, our positioning is in line with respective benchmarks but with flexibility within our strategies to take advantage of rate scenarios.

Municipal credit trends remain stable for most issuers of the market, but waning stimulus and economic moderation is beginning to impact revenue production for some state and local governments (SLGs). The ratio of upgrades to downgrades remains positive, but the margin has thinned over the past two quarters. However, we expect IGM quality to remain intact but focusing on more issuer-specific factors in discerning risk with an emphasis on the forward-looking view of individual credits. Robust reserves and liquidity should act as a buffer should budget imbalances surface. Within HYM bonds, we expect distress to remain low in comparison to the size of the market, but monitoring operating risk within certain sectors, like senior living.

Chart 2: Gross Municipal Bond Issuance, in $Billions

Source: Bloomberg as of June, 30 2024; projected = Bank of America and JPM revised forecasts Indexes are unmanaged and do not reflect a deduction for fees or expenses. Information is subject to change and is not a guarantee of future results.

KEY POINTS

- Value in the tax exemption provides an advantage.
- Balanced technicals continue supporting prices.
- Credit resilience is increasingly important in security selection.

The Fed: The Fed Getting Ready to Cut Interest Rates

Paul Single

Managing Director, Senior Economist,
Senior Portfolio Manager

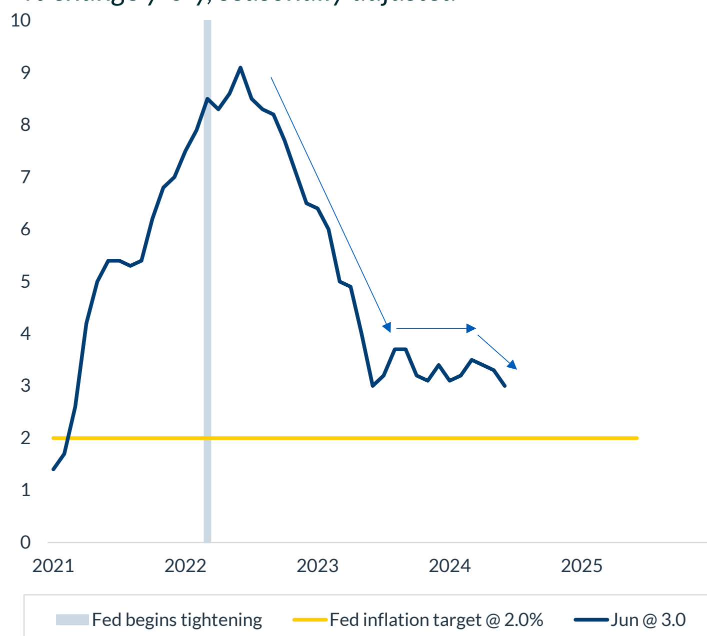
The Federal Reserve Bank is getting ready to start cutting interest rates. **We expect that the first cut will be 25 basis points at its September 18 meeting.**

For well over a year, the pace of economic growth has been slowing from its breakneck pace. However, inflationary pressures have not declined enough to warrant the lowering of interest rates. **Since shortly after the Fed began its tightening of monetary policy, back in March of 2022, inflationary pressures have been declining (Chart 1).** This was the result of increasing financing costs and the resolution of most post-pandemic logistical snarls. Inflation fell quickly to 3.0% in June 2023, following its peak of 9.1% in the previous June. For the rest of 2023, the inflation rate stabilized in the 3.0% to 3.5% range, frustrating the Fed. Then, in the first quarter of this year, it started to move back up, with an annualized rate of 4.6%, further disappointing the Fed, since the federal funds rate was at the highest level in more than two decades.

But, in the second quarter, inflation has returned to its downward trajectory, increasing at just a 1.1% annualized rate. **This has given the policymakers greater confidence that inflation is heading down to the central bank's target of a sustainable 2.0% rate.**

Chart 1: Consumer Price Index

% change y-o-y, seasonally adjusted



Source: Bureau of Labor Statistics, Federal Reserve Bank, as of June 2024.

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

This is happening at a crucial time as the economy continues to move into a more mature business cycle phase. The pace of consumer spending has been moderating, and, more importantly, the pace of payroll gains has slowed. The average monthly gain for the past three months (data can be volatile on a month-to-month basis) is 177,000, down almost 100,000 from a year ago (Chart 2). Although it's still at a solid pace, and well above the approximate pace of population growth, the Fed is growing wary about the cooling pace.

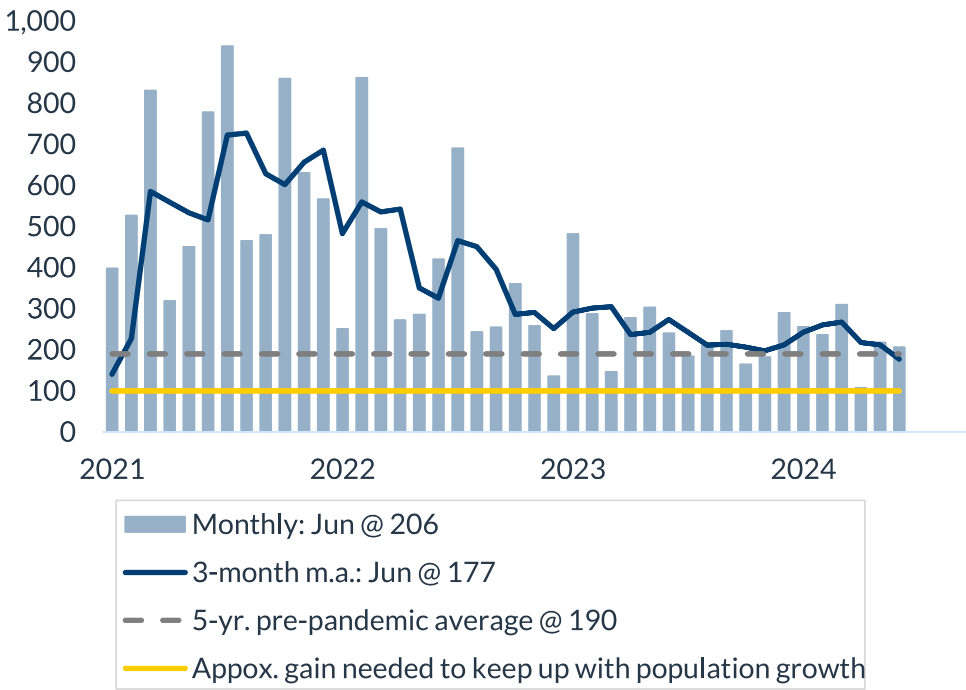
KEY POINTS

- The Federal Reserve Bank is getting ready to start cutting interest rates.
- Inflation has returned to its downward trajectory, increasing at just a 1.1% annualized rate (in the second quarter).
- The pace of consumer spending has moderated, and, more importantly, the pace of payroll gains has slowed.

The Fed has a dual mandate, seeking maximum employment and price stability. For the past year, its focus has been battling inflation, since it was too high, and labor demand was strong. But now, the mandate is more balanced, so the Fed needs to start lowering interest rates to ensure continued economic growth.

Chart 2: Nonfarm Payrolls

'000, seasonally adjusted



Source: Bureau of Labor Statistics as of June 2024.
Information issubject to change and is not a guarantee of future results.

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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, and investors may lose money. Diversification may not protect against market risk or loss. Past performance is no guarantee of future performance.

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

There are inherent risks with fixed income investing. These risks may include interest rate, call, credit, market, inflation, government policy, liquidity, or junkbond. When interest rates rise, bond prices fall.

Bloomberg risk is the weighted average risk of total volatilities for all portfolio holdings. Total Volatility per holding in Bloomberg is ex-ante (predicted) volatility that is based on the Bloomberg factor model.

Municipal securities. The yields and market values of municipal securities may be more affected by changes in tax rates and policies than similar income-bearing taxable securities. Certain investors' incomes may be subject to the Federal Alternative Minimum Tax (AMT), and taxable gains are also possible. Investments in the municipal securities of a particular state or territory may be subject to the risk that changes in the economic conditions of that state or territory will negatively impact performance. These events may include severe financial difficulties and continued budget deficits, economic or political policy changes, tax base erosion, state constitutional limits on tax increases and changes in the credit ratings.

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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 US It is not an exact list of the top 500 US companies by market cap because there are other criteria that the index includes.

S&P 500 Growth: The S&P 500 Growth Index is a stock index administered by Standard & Poor's-Dow Jones Indices. As its name suggests, the purpose of the index is to serve as a proxy for growth companies included in the S&P 500.

S&P 500 Value: The term S&P 500 Pure Value Index refers to a score-weighted index developed by Standard and Poor's (S&P). The index uses what it calls a "style-attractiveness-weighting scheme" and only consists of stocks within the S&P 500 Index that exhibit strong value characteristics. The index was launched in 2005 and consists of 120 constituents, the majority of which are financial services companies.

S&P 500 Equal Weight: The S&P 500® Equal Weight Index (EWI) is the equal-weight version of the widely-used S&P 500. The index includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight - or 0.2% of the index total at each quarterly rebalance.

DJDVP: The Dow Jones U.S. Select Dividend Index aims to represent the U.S.'s leading stocks by dividend yield.

Bloomberg Municipal Bond Index: The Bloomberg US Municipal Bond Index measures the performance of investment grade, US dollar-denominated, long-term tax-exempt bonds.

Bloomberg Municipal High Yield Bond Index: The Bloomberg Municipal High Yield Bond Index measures the performance of non-investment grade, US dollar-denominated, and non-rated, tax-exempt bonds.

Bloomberg Investment Grade Index: The Bloomberg US Investment Grade Corporate Bond Index measures the performance of investment grade, corporate, fixed-rate bonds with maturities of one year or more.

The Nasdaq Composite Index is a market capitalization-weighted index of more than 2,500 stocks listed on the Nasdaq stock exchange.

The Russell 2000 Index is a stock market index that measures the performance of the 2,000 smaller companies included in the Russell 3000 Index.

The Bloomberg Magnificent 7 Total Return Index is an equal-dollar weighted equity benchmark consisting of a fixed basket of 7 widely-traded companies classified in the United States and representing the Communications, Consumer Discretionary and Technology sectors as defined by Bloomberg Industry Classification System (BICS).

Indexes are unmanaged and do not reflect a deduction for fees or expenses. Investors cannot invest directly in an index.

Definitions

Yield to Worst (YTW) is the lower of the yield to maturity or the yield to call. It is essentially the lowest potential rate of return for a bond, excluding delinquency or default.

P/E Ratio: The price-to-earnings ratio (P/E ratio) is the ratio for valuing a company that measures its current share price relative to its earnings per share (EPS).

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.
MSCI Emerging Markets Asia Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the Asian emerging markets.

The Magnificent Seven stocks are a group of high-performing and influential companies in the U.S. stock market: Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA, and Tesla.

City National Rochdale Proprietary Quality Ranking formula: 40% Dupont Quality (return on equity adjusted by debt levels), 15% Earnings Stability (volatility of earnings), 15% Revenue Stability (volatility of revenue), 15% Cash Earnings Quality (cash flow vs. net income of company) 15% Balance Sheet Quality (fundamental strength of balance sheet).
*Source: City National Rochdale proprietary ranking system utilizing MSCI and FactSet data. **Rank is a percentile ranking approach whereby 100 is the highest possible score and 1 is the lowest. The City National Rochdale Core compares the weighted average holdings of the strategy to the companies in the S&P 500 on a sector basis. As of September 30, 2022. City National Rochdale proprietary ranking system utilizing MSCI and FactSet data.