City National Rochdale®
AN RBC/CITY NATIONAL COMPANY

JANUARY 20, 2021

On the Radar

FAQS ON THE MARKETS AND ECONOMY

What is CNR's outlook for equity markets?

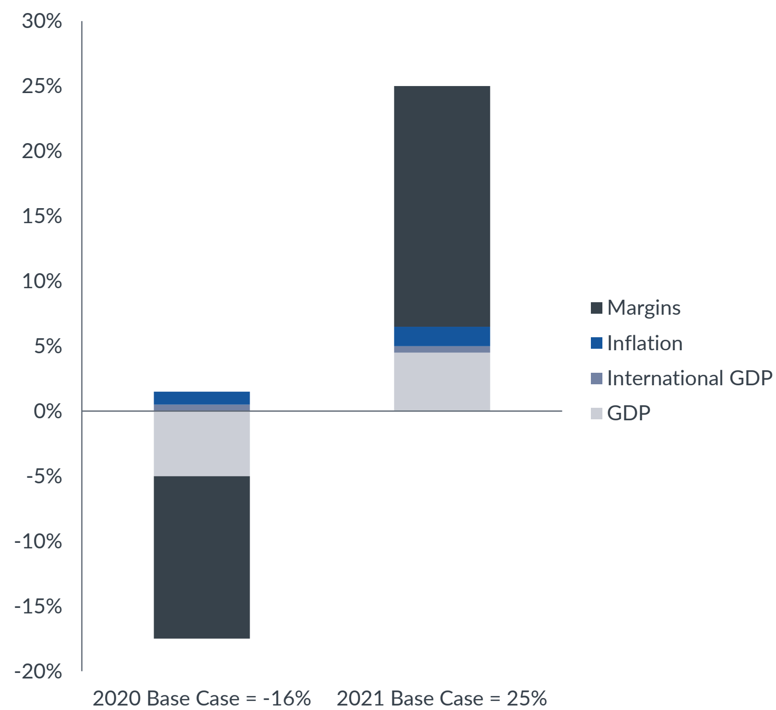
U.S. stock markets continue to build on optimism of a vaccine-driven return to normalcy and corporate profit recovery, with expectations for greater fiscal stimulus under Democrat-controlled government.

To a large extent we think the market reaction has been justified. The visibility of economic growth in the medium term has improved recently now that the election is behind us, while vaccine development has been much better than expected, and with it the confidence in the outlook for corporate profit growth has improved.

However, with stocks now up nearly 70% from last year's low, investors should prepare for moderate returns going forward. We don't think the gains are exhausted, but this rally has priced in expectations for a fairly sturdy recovery this year.

While we expect that to come to pass, inevitable periods of disappointments and policy anxiety could produce more volatility compared with the past several months. Market valuations have been stretched, leaving less cushion for error, and an expected recovery in earnings will likely be key for markets to take the next step higher.

S&P 500 Earnings Growth Forecast: 2020 and 2021



Source: CNR Research.

Overall, we continue to prefer U.S. stocks over non-U.S. developed markets and EM Asia over other emerging markets. While valuations in S&P 500 stocks appear full, other areas, especially in the high dividend paying stocks look attractive to us. We remain focused on high-quality companies with strong business models selling at reasonable valuations.

KEY QUESTIONS

What is CNR's outlook for inflation?

What is causing the yield on the benchmark 10-year to move up?

Are dividends and income equities attractive?

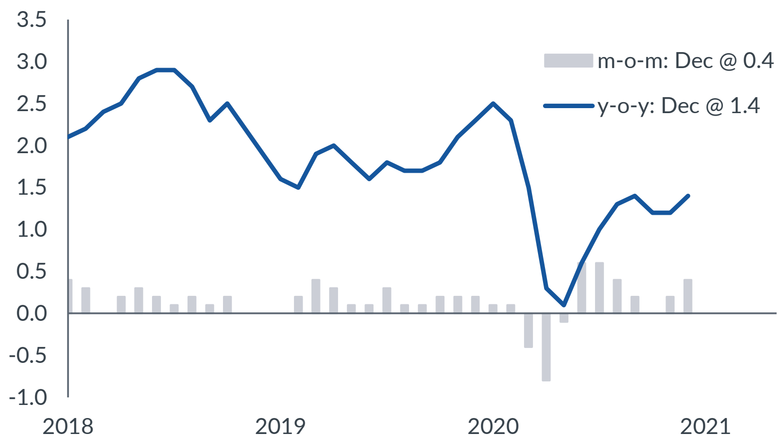
What is CNR's outlook for inflation?

We do not think inflationary pressures will be severe enough for the Fed to adjust monetary policy.

Inflation this year will be a roller coaster ride. As the year progresses, the year-over-year calculation will be volatile as months from last year drop off the measure. In the spring of 2020, there were several months of negative inflation due to the lockdown and a severe oil price decline. As those drop off the yearly calculation, the yearly change will increase. In the past summer, the large increases in inflation as the economy reopened will drop off and cause the yearly calculation to recede.

The jump in inflation will not spook the Fed during the spring. Instead, they will look past these one-time adjustments. They will continue to focus on fundamental changes to the economy that may cause long-term price pressures. The Fed has signaled that they plan to keep the federal funds low even if inflation moves above 2.0%.

Consumer Price Index (%)



Source: Bureau of Labor Statistics as of December 2020.

What is causing the yield on the benchmark 10-year to move up?

The yield on the 10-year Treasury note is currently 1.09%' it moved above the 1.0% threshold on January 6. Back in August, the yield hit a 2020 nadir of 0.51% due to the coronavirus's seriousness and uncertainty and the lack of agreement in the federal government to provide another fiscal relief package.

The recent upward movement is based on the assumption of a more robust economic growth rate this year due in part to increased government spending. Back in December, the federal government approved a $900 billion fiscal aid package. With a new Congress, there is a greater chance of more federal spending on pandemic relief.

Another cause of higher interest rates is a growing belief that inflation may increase over the next decade. This can be seen in the "TIPS breakeven" yield, which measures the market's expected average inflation rate. It is derived from the difference between the nominal yield and the yield of inflation-protected securities of like maturities. We do not believe inflation will get out of control; please see the question "What is CNR's outlook for inflation?"

10-year Treasury Yield (%)

Source: Bloomberg as of January 15, 2021.

Are dividends and income equities attractive?

We believe dividend and income equities offer some of the greatest remaining value for investors. Not only are dividend stocks priced attractively relative to history, but also relative to growth stocks, which have seen a dramatic increase in valuations over the COVID-19 crisis.

Going forward, the mass distribution of a vaccine by the second half of 2021 should allow for economic activity to return to more normal levels, providing a boost to the economically sensitive value sector, including many of our dividend stocks, which have lagged the recovery.

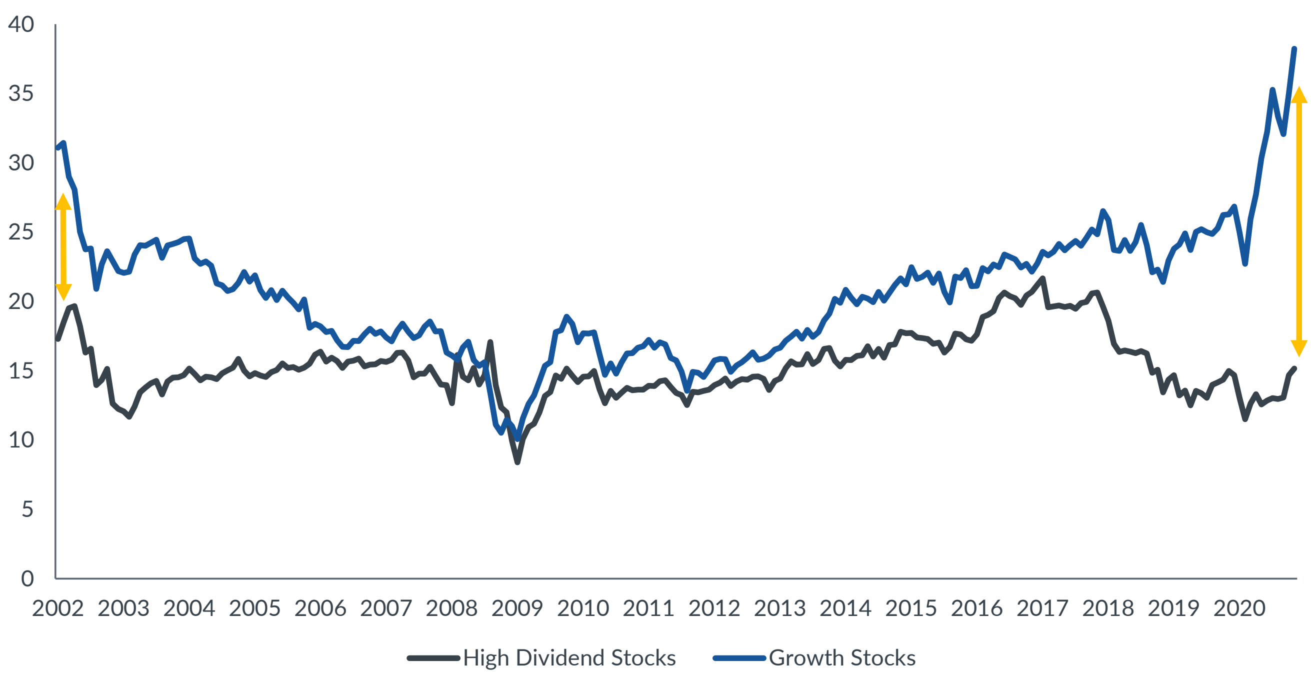
Meanwhile, with interest rates so low and likely to remain that way for a prolonged period of time, we feel fixed income investors will continue to find solid dividend names as an attractive alternative. The income opportunity is there. Spreads for the three main equity income assets (consumer staples, utilities, and REITs) are at the highest levels in the past 10 years.

We believe having a solid portfolio yield that is as stable as possible will be the critical factor that can generate positive returns over time. This would include being invested in steady cash flow businesses that have much of their revenue tied to "essential services." In addition, strong balance sheets with reasonable payout levels are important.

While the CNR dividend research team continues to emphasize owning stocks that can maintain their dividends through the economic uncertainty ahead, we are increasingly focusing on companies with the ability to grow their dividends in order to take advantage of an improving economic outlook and help drive a higher expected total return.

Valuations: High Dividend Stocks vs. Growth Stocks

Price/Earnings Ratio



Source: Bloomberg. High Dividend Stocks: Dow Jones U.S. Select Dividend Index. Growth Stocks: S&P 500 Growth Index.

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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.

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Past performance is no guarantee of future performance.

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Index Definitions

S&P 500 Index (S&P500) is a stock market index that tracks the 500 most widely held stocks on the New York Stock Exchange or NASDAQ. It seeks to represent the entire stock market by reflecting the risk and return of all large-cap companies.

The Consumer Price Index (CPI) is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food, and medical care.

Dow Jones US High Dividend Yield Index serves as a benchmark for income seeking equity investors. The index is designed to measure the performance of 80 high yield companies within the S&P 500 and is equally weighted to best represent the performance of this group, regardless of constituent size.

S&P 500 Growth Index measures growth stocks using three factors: sales growth, the ratio of earnings change to price, and momentum. S&P Style Indices divide the complete market capitalization of each parent index into growth and value segments.