CITY NATIONAL ROCHDALE
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ECONOMIC & INVESTMENT MANAGEMENT PERSPECTIVES

Q2 UARTERLY UPDATE

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SECOND HALF OF 2025 OUTLOOK: A MARKET BALANCING ACT AFTER AN EVENTFUL START

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The first half of 2025 delivered no shortage of volatility, testing investor resolve while ultimately rewarding investors who maintained composure and stayed in the market.

The equity market drawdown that bottomed in April — nearly breaching bear market territory with a peak-to-trough decline of over 19% — was triggered by the Trump administration's announcement of reciprocal tariffs. Markets also endured the sustained geopolitical friction in Eastern Europe and weathered a re-escalation of Middle East tensions and military actions. The global policy backdrop, once again unsettled, challenged assumptions around inflation persistence, supply chain resilience and earnings durability.

And yet, just as sentiment appeared to be unraveling, markets staged a notable reversal. The S&P 500 rallied sharply into midyear, finishing June up 6.2% year to date, lifted by better-than-expected inflation and employment data, as well as increased policy clarity from Washington. Treasury yields stabilized, credit spreads narrowed, volatility moderated, and many of the worst-case scenarios embedded in asset prices proved too dire.

Still, the rally has left investors facing a familiar puzzle: How much optimism is already priced in, and what risks remain underappreciated?

A SHIFT IN POLICY — AND ITS MARKET IMPLICATIONS

The centerpiece of the policy landscape heading into the second half of the year is the passage of the "One Big Beautiful Bill" (OBBB), which was signed into law on July 4, the president's deadline. While the political theater surrounding the bill's path was no small contributor to earlier market volatility, its final form delivered more continuity than upheaval. Most notably, the OBBB makes the individual tax cuts enacted in the 2017 Tax Cuts and Jobs Act (TCJA) permanent, thereby avoiding what would have amounted to a large, broad-based tax hike on businesses and consumers starting in 2026.

Corporate provisions, including extensions to bonus depreciation and R&D incentives, could bolster investment spending, particularly among capital-intensive industries. In that sense, the bill may modestly support earnings growth over the next 12 to 18 months. However, markets will also have to reckon with its longer-term implications: The legislation lifts the debt ceiling to $40 trillion and raises questions about upward pressure on yields as fiscal borrowing accelerates.

The net impact of the bill is still to be determined, but at a minimum, it removes a significant source of uncertainty. As a result, financial conditions have eased, and investor focus has pivoted toward the traditional levers of growth and valuation.

MARKETS: CAUGHT BETWEEN MOMENTUM AND MATURITY

Equity markets enter the third quarter on strong footing but also on stretched valuations. The S&P 500 is trading at 22.3 times forward earnings — well above historical averages — while optimism has returned in force, particularly around the technology and communication services sectors. Despite the continued rally, late-June market activity flashed overbought signals, particularly if earnings or macro data disappoint. There's plenty of potential for the equity market to finish higher this year, but we doubt it will be a straight line.

So which tailwinds remain? Corporate earnings in the second quarter are expected to show modest year-over-year growth, and while some compression in margins is likely, especially in the consumer-facing sectors with sensitivity to imports, many large-cap companies continue to benefit from productivity gains and pricing power, even with pressure on input costs from pending tariffs. The breadth of the market remains narrow, with outsize contributions from mega-cap names in

AI and software, which have staged a rally of over 30% from the bottom in April. However, a gradual broadening could occur if the economic backdrop continues to stabilize.

Earlier in the year and relative to international markets, U.S. equities underperformed, but since market lows in early April, the gap is narrowing, with the U.S. outperforming developed markets. Trade tensions and geopolitical instability remain key risks abroad, particularly in Europe and parts of Asia. Emerging markets could benefit from the current level of the dollar, but that tailwind has moderated. The U.S. dollar, after declining meaningfully through the second quarter, appears to have found a near-term floor, supported by relative growth differentials and the Federal Reserve's cautious posture. After all, the U.S. continues to have one of the highest 10-year yields across the developed world.

INFLATION, LABOR MARKETS AND THE FED: POLICY PATIENCE IN FOCUS

On the macro front, inflation remains a central focus. The disinflationary trend has continued, albeit unevenly, with the May consumer price index and producer price index both surprising to the downside. Yet supply chain disruptions and tariff-related pass-through effects have reintroduced upside risk. Our base case calls for inflation to end the year between 3% and 3.75%, slightly above the Fed's comfort zone.

The labor market remains resilient on the surface, but signs of softening are beginning to emerge. June's unemployment rate fell, but underlying data — such as reduced federal workforce participation and weaker private hiring intentions — suggests some cooling. While this is not yet cause for concern, it does reduce the urgency for further rate hikes.

Accordingly, the Fed has adopted a holding pattern. The July 30 meeting is expected to leave rates unchanged, as policymakers evaluate the full impact of tariffs and fiscal policy. Markets are pricing in the potential for one or two rate cuts before year-end, but the bar remains high. Any cut will require either a material deterioration in the labor market or a sustained drop in inflation closer to the target.

LOOKING AHEAD: A CONSTRUCTIVE BUT UNSETTLED PATH

The outlook for the second half of 2025 remains constructive but still very unpredictable. Investors must navigate a landscape defined by sharp reversals — both in price and policy — and maintain flexibility in positioning. The supportive forces of continued easing financial conditions, fiscal stimulus and still-decent earnings must be weighed against valuation risk, uncertain global trade policy and the potential for inflation to reassert itself.

For diversified portfolios, U.S. equities — particularly high-quality large caps with pricing power and balance sheet strength — remain a core allocation. Fixed income, bolstered by attractive yields and modest credit risk, offers ballast. International exposure, despite its significant first-quarter 2025 outperformance, still requires more selectivity given uneven macro conditions and currency volatility.

Above all, while many of the early-year fears have not materialized, new questions are emerging. The path forward may not be as smooth as the recovery from April's lows, but neither is it likely to be as treacherous. As always, those who stay focused on fundamentals, policy context and long-term goals will be best equipped to weather what comes next.

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EQUITIES IN TRANSITION: RECOVERY, RESILIENCE AND ONGOING UNCERTAINTY

KEY POINTS:

- Tariff volatility dominated early-quarter momentum.
- A technology sector revival drove recovery performance.
- The Federal Reserve maintained cautious policy amid uncertainty.

The second quarter of 2025 witnessed a remarkable recovery in U.S. equity markets following the tariff-induced volatility that defined the period's opening.

The S&P 500 surged nearly 11% during the quarter as stocks recovered from an early-April swoon sparked by concerns about tariffs. This dramatic rebound showcased the market's resilience amid policy uncertainty and geopolitical tensions.

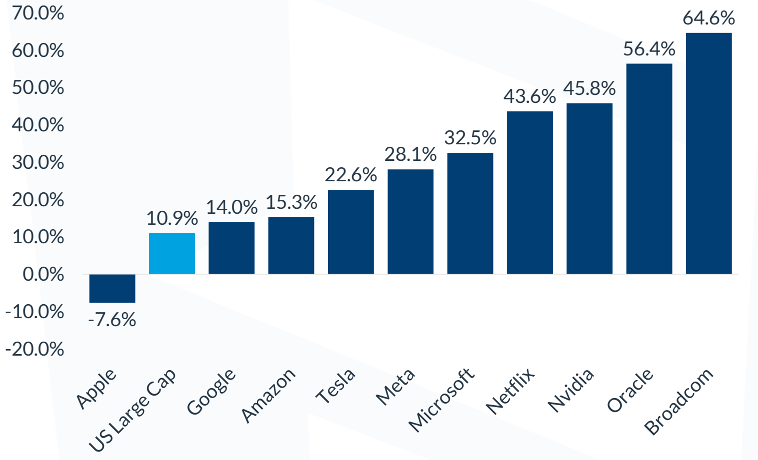
The quarter began with significant turbulence, as President Trump's "Liberation Day" tariff announcement on April 2, 2025, triggered a global market sell-off and reignited recession fears. Markets initially plunged into correction territory, with the S&P 500 falling over 18% from February peaks (Feb. 19–April 8), before staging an impressive recovery through May and June. The S&P 500 and Nasdaq both closed the quarter at record highs, marking a stunning reversal from the April lows.

Technology sectors led the recovery with exceptional performance, demonstrating renewed investor confidence in growth and innovation themes. Information technology led the pack with just over a 23% quarterly gain, followed closely by communication services sectors, which benefited from strong earnings and investor enthusiasm. This represented a dramatic sector rotation from first-quarter 2025, when defensive sectors like energy and healthcare had outperformed, while technology stocks struggled under tariff uncertainty.

Geopolitical events provided additional market volatility, particularly the Israel-Iran conflict that erupted in June. The 12-day conflict, which included U.S. strikes on Iranian nuclear facilities, caused oil prices to rise from $70 to $81 per barrel, though the market impact proved more contained than historical precedents. Markets demonstrated resilience, as the conflict was contained by late June.

Corporate earnings remained robust throughout the period, with first-quarter 2025 results showing 12.7% earnings growth for the S&P 500, marking the second consecutive quarter of double-digit growth. The Magnificent 7 technology companies reported particularly strong first-quarter earnings growth of 31.8%, supporting the sector's second-quarter recovery.

CHART 1: 2025-Q2 "MAGNIFICENT" STOCK RETURNS



Source: Bloomberg, CNR Research as of June 30, 2025, starting March 31, 2025 Past performance is no guarantee of future results.

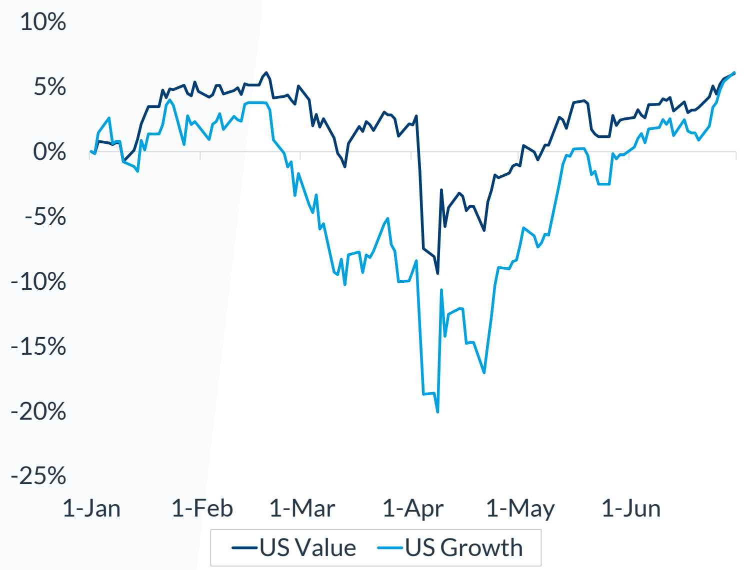
2025-Q2 Stock returns of selected technology and consumer discretionary companies

The Magnificent 7 Stocks include Alphabet, Amazon, Apple, Meta Platforms, Microsoft, Nvidia, and Tesla.

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.

For the first half of 2025, U.S. equity markets delivered positive but modest returns, with the S&P 500 gaining 6.2%. The performance reflected a year of two distinct halves — early volatility followed by strong recovery, ultimately leaving major indexes near record levels despite significant policy and geopolitical headwinds.

CHART 2: 2025-H1 CONVERGENCE BETWEEN GROWTH & VALUE



Source: Bloomberg, CNR Research as of June 30, 2025, starting December. 31, 2025, cumulative returns over time. Indices used: U.S. Value: Russell 1000 Value Index, U.S. Growth: Russell 1000 Growth Index.

Past performance is no guarantee of future results.

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INVESTMENT GRADE FIXED INCOME: BONDS KEEP THEIR COOL AHEAD OF SUMMER

KEY POINTS:

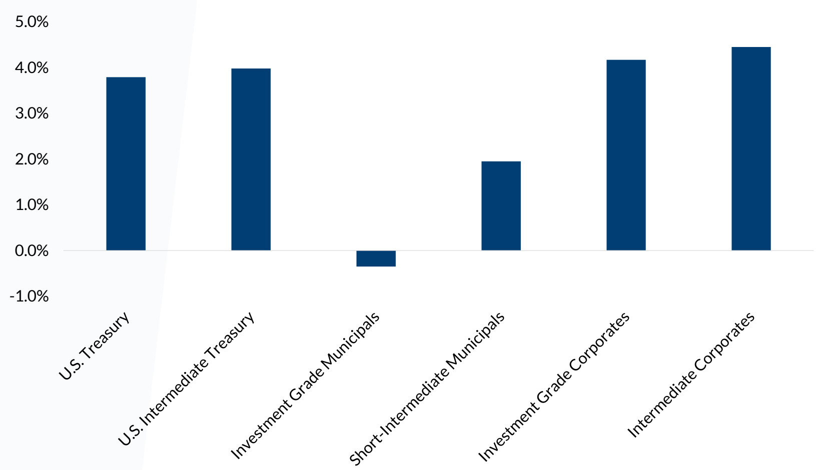
- The potential for attractive yields and enhanced income offer opportunities.
- Market technicals a potential tailwind for near-term performance.
- Credit fundamentals provide relative stability for active managers.

Investment-grade (IG) fixed-income returns were mixed to end the first quarter. While all pockets of the financial market confronted elevated volatility, uneven performance developed toward the final weeks of the first quarter.

The U.S. Treasury Index outpaced other IG asset classes, rewarding investors with a 2.92% total return versus a loss of 22 basis points (bps) for IG municipal bonds and 2.31% for IG corporate bonds, per Bloomberg indexes. Front and center was the uncertainty over U.S. trade policy, particularly the impact of tariffs, as well as escalating geopolitical and economic risks. These events pushed inflation expectations up and growth down and pulled consumption forward as businesses and consumers dashed to get ahead of implementation. The results were lower rates and wider credit spreads. The bellwether 10-year U.S. Treasury bond declined a cumulative 37 bps during the first quarter, reflecting more periods of risk-off investor sentiment. While the Federal Reserve left its overnight lending rate unchanged at its March meeting, it faces potentially difficult policy choices ahead with a tug-of-war between mitigating rising prices and staving off disruptions to employment. That being said, easing rates may not cure imbalances, but time perhaps will.

A key observation during the first quarter was the change in valuations and risk pricing across IG bonds. Credit spreads on the Bloomberg U.S. Corporate Investment Grade Index widened between +14 bps and +94 bps, hitting its highest level since August 2024. While

CHART 1: YEAR TO DATE TOTAL RETURN



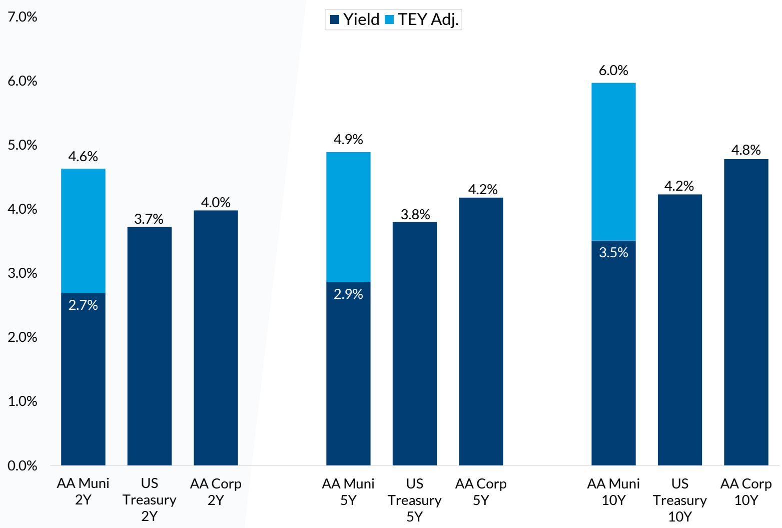
Source: Bloomberg, as of June 30, 2025. Past performance is no guarantee of future results.

Indices used: US Treasury Index, US Intermediate Treasury Index, Municipal Bond Index, Municipal Short-Intermediate Bond Index, US Corporate Bond Index, US Intermediate Corporate Bond Index.

close monitoring of corporate fundamentals is warranted as economic headwinds swirl, IG corporate borrowers should continue benefiting from mostly healthy balance sheets, stable leverage and favorable cash flow generation. The magnitude and duration of policy shifts associated with trade and economic factors could further weigh on credit spreads and pricing. In municipals, the ratio of the 10-year AAA benchmark municipal bond versus a comparable Treasury bond is a key valuation metric. This metric increased meaningfully in the final weeks of the first quarter, as Treasury rates held steady and municipal yields rose (i.e., municipals underperformed), making municipal bonds more attractive at levels not seen in at least two years. Valuations coupled with mostly durable credit conditions, albeit normalizing for issuers given policy shifts, offer compelling value for market investors and could continue as volatility increases in the near term.

One theme that fixed-income investors have continually embraced is income. At quarter-end, the yield to worst of IG municipal bonds and IG corporate bonds, per Bloomberg, was 3.85% and 5.15%, respectively. Attractive yields provide good cash flow and may act as a buffer to rate volatility. Moreover, higher yields benefit forward-return potential. As we progress through the next few months, staying engaged in the markets when dislocation surfaces can add value to long-term investors, but adhering to sound active management and security selection will be crucial to navigating economic uncertainty.

CHART 2: FIXED INCOME YIELDS



Source: Bloomberg, as of June 30, 2025. Past performance is no guarantee of future results.

Indicies used: AA Municipal Bond Revenue Curve, US Actives Treasury Curve, US AA Corporate Bond Revenue Curve.

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HIGH YIELD FIXED INCOME: COMPELLING INCOME BUFFERS TIGHT VALUATIONS

KEY POINTS:

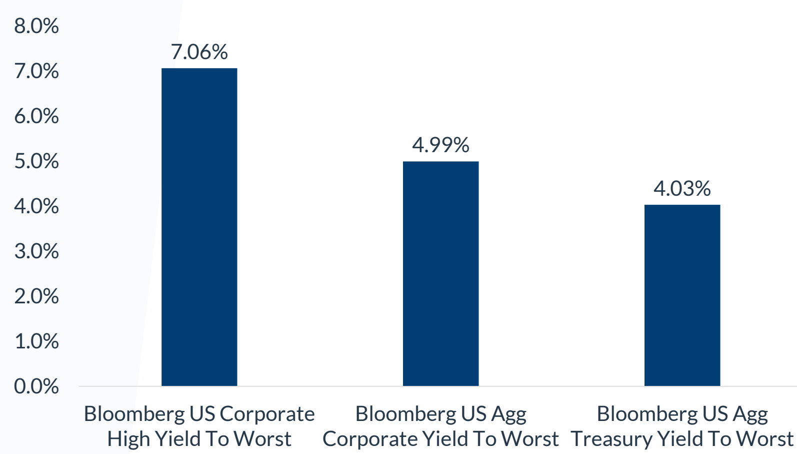
- Income a return driver despite elevated market volatility.
- Issuer fundamentals remain solid.
- Full valuations warrant careful security selection.

High yield (HY) bonds delivered positive total returns in the second quarter, as investors continued to seek attractive levels of income and relative value opportunities.

Despite market ebb and flow, attainable yields and cash flow provided a strong incentive for capital deployment into risk assets vs. other bond types. Geopolitical pressure remained a moderate backdrop for credit markets during the quarter, with Middle East tensions, including threats to shipping routes in the Red Sea, contributing to broader investor caution. But these events had a limited direct impact on U.S. and emerging market corporate HY spreads. Given these dynamics, our focus has remained on corporate emerging market HY rather than sovereign debt to reduce exposure to international risks and developments. From a positioning standpoint, credit investors continue to prioritize fundamental earnings strength and balance sheet wherewithal over macro-driven risks during the quarter. Within the HY municipal bond market, the yield-to-worst of the Bloomberg Municipal High Yield Index has remained steady for most of this year, with current levels at about 90% of their 5-year range. The taxable-equivalent yield (i.e., adjusts tax-exempt municipal yield for federal taxes) of HY municipal is currently about 10%[1], which is compelling vs. its fixed income peers.

With a policy environment in flux and global economic projections less certain, most companies that are issuing high yield bonds continue to

CHART 1: HIGH YIELD BONDS OFFER ATTRACTIVE INCOME



Source: Bloomberg, as of June 30, 2025. Past performance is no guarantee of future results.

[1] taxable equivalent yield is 37% fed + 3.8% Medicare Surcharge, 40.8%.

maintain healthy balance sheets and produce stable earnings. While there have been isolated defaults, the overall distress level remains below their longer-term averages. According to Pitchbook/LCD research, the net debt-to-EBITDA (earnings before interest, taxes, depreciation, and amortization) ratios declined to 4.2x from 4.7x over the past quarter, demonstrating profitability and cash flow support. The average ratio over the past 10 years has been approximately 5x, according to LCD. Similarly, first-time municipal bond issuer defaults are at their lowest year-to-date since 2021, per Municipal Market Advisors (MMA)[2]. However, uneven economic conditions and project-specific factors may lead to an uptick in some areas of the asset class. After several years of favorable growth in operational activities, many sectors of the HY municipal bond market remain reasonably positioned for potential headwinds.

A notable observation during the quarter and on the year has been credit spread trends. The extra yield that high yield bonds offer over safe-haven government securities has tightened YTD and remains below recent years' averages. With a more fully priced HY market, investor sentiment or shifts in fundamental credit conditions could influence risk compensation and security valuations. We continue monitoring these dynamics and remain conservative in our credit research process, with a focus on security selection and diversification. The Fed will likely drive market performance into year-end. While our base case is 1–2 FOMC rate cuts, slightly below market consensus, this suggests only modest relief for fixed rate bonds and loans, with carry remaining the primary source off total returns.

CHART 2: BLOOMBERG US CORPORATE HIGH YIELD AVERAGE OPTION-ADJUSTED SPREAD (OAS)

Source: Bloomberg, as of June 30, 2025. Past performance is no guarantee of future results.

The option-adjusted spread (OAS) is the measurement of the spread of a fixed-income security rate and the risk-free rate of return, which is then adjusted to take into account an embedded option.

[2] Municipal Market Advisors (MMA) data as of June 30, 2025.

THE FED OUTLOOK: CLEAR AS MUD

PAUL SINGLE
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KEY POINTS:

- The recent economic data is what central banks dream of.
- The Fed has repeatedly said that it wants greater clarity on the impact of policy changes before making its next move.
- CNR has expected the tariffs to slow economic growth compared to last year. We expect these to slow growth, not derail it.

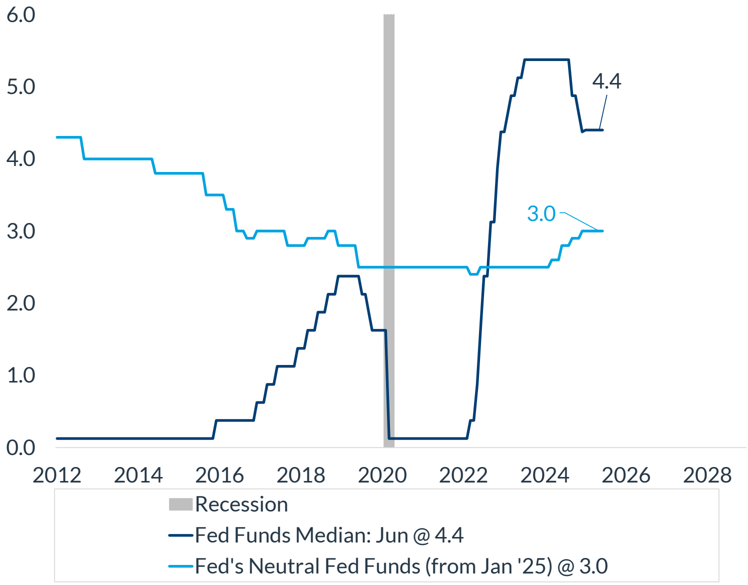
The recent economic data is what central banks dream of. In the past three months, the unemployment rate has averaged just 4.2%, and the annualized rate of CPI was 2.4%.

These are excellent levels. Economists generally view full employment as an unemployment rate within the range of 4.0% to 4.5%, and the Fed's target inflation rate is 2.0%. This data is enough information for the federal funds futures market to expect two interest rate cuts this year, of 25 bps each.

In the past, the Fed would analyze that data to establish its forecast. However, at this time, making forecasts that carry a high level of confidence has become far more difficult for the Fed.

To the Fed, the level of uncertainty about the future remains highly elevated, primarily due to the federal government's planned polices that may have a powerful impact on the economy. The most notable is its tariff policy. What will the tariff rate be? How much of that tax will be absorbed by businesses, which would impact corporate profitability? How much will be passed on to consumers? The answers to these questions will impact inflation and inflation expectations. But the answers are difficult to discern, since the tariff increases that are expected to occur have not happened since the 1930s, so there is no recent data to compare them against. The Fed has repeatedly said that

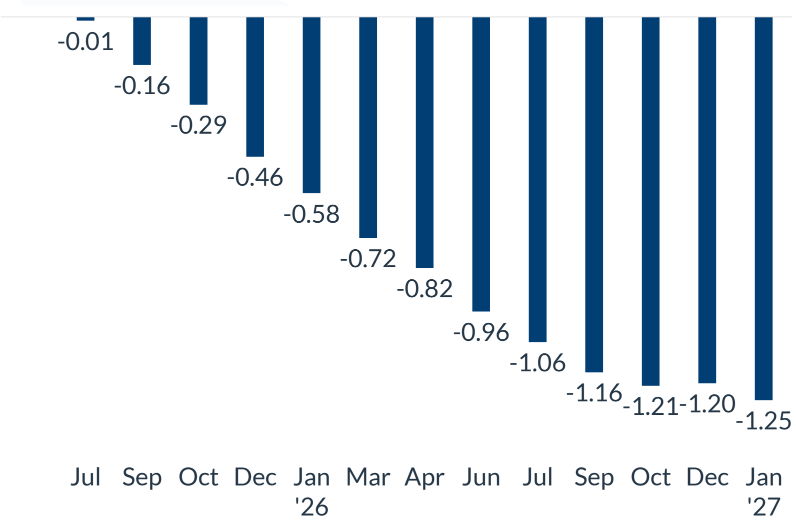
CHART 1: FEDERAL FUNDS & FED'S LONGER-TERM RATE
%, NOT SEASONALLY ADJUSTED



Source: The Federal Reserve, as of July 2025. Past performance is no guarantee of future results.

CHART 2: FEDERAL FUNDS FUTURES: CHANGE FROM CURRENT LEVEL

%, AS OF JULY 22, 2025



guarantee of future results.

it wants greater clarity on the impact of policy changes before making its next move.

In addition to unknown tariff impacts, there will be economic impacts from the mass deportations of migrants, the increase in layoffs of federal workers, stimulus from the new budget, and planned reductions in federal regulations.

With that background in mind, CNR continues to believe the Fed will return to its easing of monetary policy that it started last September. It had reduced the federal funds rate by 100 bps in the fourth quarter of 2024. Since December, the Fed has stood on the sidelines as it awaited finalization of the administration's policies.

Since the beginning of the year, CNR has expected the tariffs to slow economic growth compared to last year. These will slow growth, not derail it. The federal funds rate is considered restrictive by the Fed's definition (Chart 1). That gives the Fed room to lower interest rates to restimulate the economy (Chart 2).

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.

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 Dow Jones Industrial Average (DJIA) tracks thirty of America's biggest and most established companies, acting like a quick temperature check of the U.S. economy.

The MSCI USA Large Cap Index is designed to measure the performance of the large cap segments of the US market. The index covers approximately 70% of the free float-adjusted market capitalization in the US.

The Bloomberg Investment Grade Corporate Bond Spreads refer to the spreads between investment grade, fixed-rate, taxable corporate bonds.

The Russell 1000 Value Index measures the performance of the large-cap value segment of the US equity universe. It includes Russell 1000 companies with lower price-to-book ratios, lower expected and historical growth rates.

The Russell 1000 Growth Index is a stock market index that measures the performance of the large-cap growth segment of the U.S. equity universe. It includes large and mid-cap companies that exhibit growth characteristics, and it is published and maintained by FTSE Russell.

The U.S. Treasury Index is an index that reflects recent auctions of actively traded U.S. government securities and is often used as a benchmark by lenders when establishing interest rates.

The Bloomberg U.S. Treasury: Intermediate Index measures US dollar-denominated, fixed-rate, nominal debt issued by the US Treasury.

The Bloomberg Municipal Short-Intermediate Bond Index is a measure of the US municipal tax-exempt investment grade bond market.

The Bloomberg US Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by US and non-US industrial, utility, and financial issuers.

The Bloomberg U.S. Intermediate Corporate Bond Index is a measure of the investment grade, fixed-rate, taxable corporate bond market.

The Bloomberg AA Municipal Bond Revenue Curve index is a measure of the US municipal tax-exempt investment grade bond market. It includes general obligation and revenue bonds, which can be pre-refunded years later and get reclassified as such.

The Bloomberg US Treasury Actives Curve is a curve that relates the yield on a security to its time to maturity.

The Bloomberg US Corporate AA Corporate Bond Revenue Curve represents the effective yield of the ICE BofA AA US Corporate Index, which tracks the performance of US dollar-denominated investment-grade rated corporate debt publicly issued in the US domestic market.

Bloomberg US Corporate High Yield To Worst refers to the yield to worst of the Bloomberg U.S. Corporate High Yield Bond Index.

The Bloomberg US Agg Corporate Yield To Worst is a measure of the lowest yield the Bloomberg US Aggregate Bond Index (Agg) has ever had while its effective duration is at its highest.

The Bloomberg US Agg Treasury Yield To Worst is an index that measures the yield of US Treasury bonds.

DEFINITIONS

The “core” Personal Consumption Expenditures (PCE) price index is defined as prices excluding food and energy prices. The core PCE price index measures the prices paid by consumers for goods and services without the volatility caused by movements in food and energy prices to reveal underlying inflation.

The Producer Price Index (PPI) is a measure of the average change over time in the selling prices received by domestic producers for their output.

A leveraged loan is a type of loan that is extended to companies or individuals that already have considerable amounts of debt or poor credit history.

Yield to worse (YTW) is the lowest potential yield that an issuer can pay on a bond without defaulting.

The option-adjusted spread (OAS) is the measurement of the spread of a fixed-income security rate and the risk-free rate of return, which is then adjusted to take into account an embedded option.

The Magnificent 7 refers to a group of major tech companies with stock growth that far outpaced the high-performing S&P 500 in recent years. Coined in 2023, the group consists of Alphabet, Amazon, Apple, Meta Platforms, Microsoft, Nvidia, and Tesla

Nasdaq is a global electronic marketplace for buying and selling securities. Its name was originally an acronym for the National Association of Securities Dealers Automated Quotations.

IMPORTANT INFORMATION

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