2023 Outlook: A Deep Dive into CNR’s Economic and Investment Outlook

Summary of December 15 Market Update Webinar

Evaluating Recession Risks during a Bear Market & Inflation
For most of 2022, City National Rochdale had predicted that economic volatility would remain higher for longer periods of time. While maintaining our "higher for longer" thesis during our December market update, there was also a note of optimism for 2023.

CNR still anticipates lower GDP, lower earnings and a lower S&P 500 fair value compared to some other forecasts. We also have higher-than-consensus expectations for inflation, interest rates and volatility, said Garrett R. D'Alessandro, CNR CEO.

However, D'Alessandro also anticipates that 2023 will be a “tale of two years," with the first half likely to see a mild recession and continued market volatility, and the second half seeing return to positive territory for both equity and fixed income investments.

Looking Back at the 2022 Economic Picture
Reviewing 2022, D'Alessandro explained that this was one of the most challenging markets experienced in years, with the traditional 60/40 balanced portfolio seeing its worst returns in half a century.

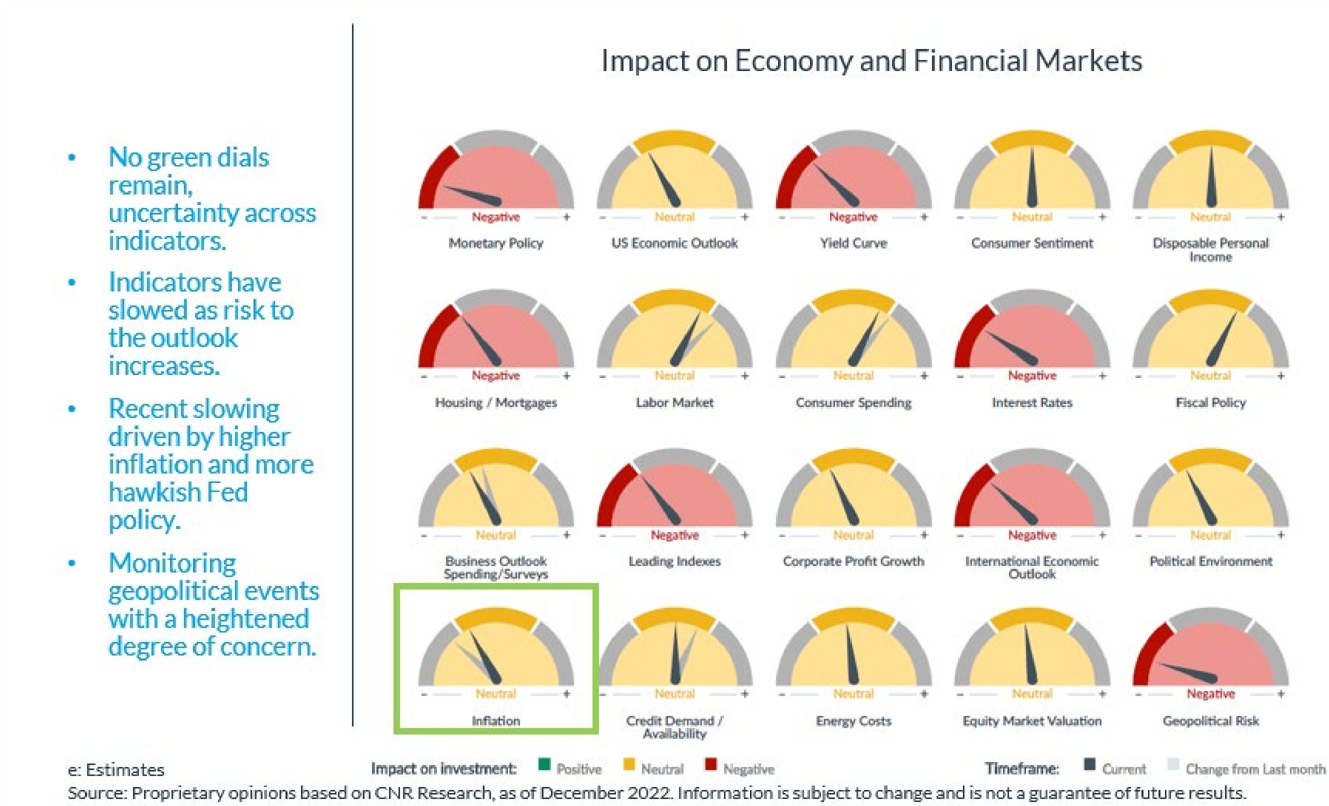
The CNR team was able to predict several important trends in 2022, such as anticipating the equity correction, and we de-risked portfolios by selling non-U.S. equities and focusing on quality U.S. stocks.

In addition, CNR avoided investing in speculative tech and cryptocurrency but included other alternative investments. We didn't anticipate the pace of inflation and interest rate increases, but neither did other analysts across the financial industry.

Also unexpected were the aggressive actions taken by Russian President Vladimir Putin and the magnitude of negative fixed income returns.

What's Ahead for the 2023 Economy?

CNR Speedometers®, our forward-looking indicators for the next six to nine months, are all yellow or red this month. However, our team provided reassurance that these outlooks aren't as negative as they first appear.



“There's no green on this page of Speedometers because of uncertainty about monetary policy, uncertainty about consumers, uncertainty about interest rates and uncertainty about corporate profits," said D'Alessandro. “They're not necessarily overwhelmingly negative, the yellow indicators just tell you we're uncertain."

He also pointed to an encouraging note: The Speedometers inflation dial has moved from red to yellow, reflecting CNR's belief that inflation has peaked. While still elevated, the inflationary trend over the next year will likely be lower, he said, making it less of a headwind to economic growth.

- Household and business fundamentals still solid but slowing.
- Inflation pressures to remain elevated, but moderating.
- Fed remains tight to slow economy and wages.
- We have below-consensus expectations for GDP and earnings growth.
- We have consensus estimates for interest rates.

City National Rochdale Forecasts		2022e	2023e
Real Annual GDP Growth		1.0% to 2.0%	-1.25% to 0.75%
Corporate Profit Growth		5.0% to 6.0%	-6.5% to 1.5%
Headline CPI Year End		6.6%	2.6%
Core CPI Year End		5.6%	3.1%
Interest Rates	Fed Funds Rate	4.25% to 4.50%	5.00% to 5.25%
	Treasury Note, 10-Yr.	3.50% to 3.75%	3.5% to 4.25%

Sources: Bloomberg, CNR Research, as of December 2022. Information is subject to change and is not a guarantee of future results.

The CNR team anticipates GDP to pivot around zero for 2023 but believes the strong fundamentals in household and business balance sheets will help the economy weather what they anticipate to be a 60% chance of a mild recession.

Global Economic Outlook

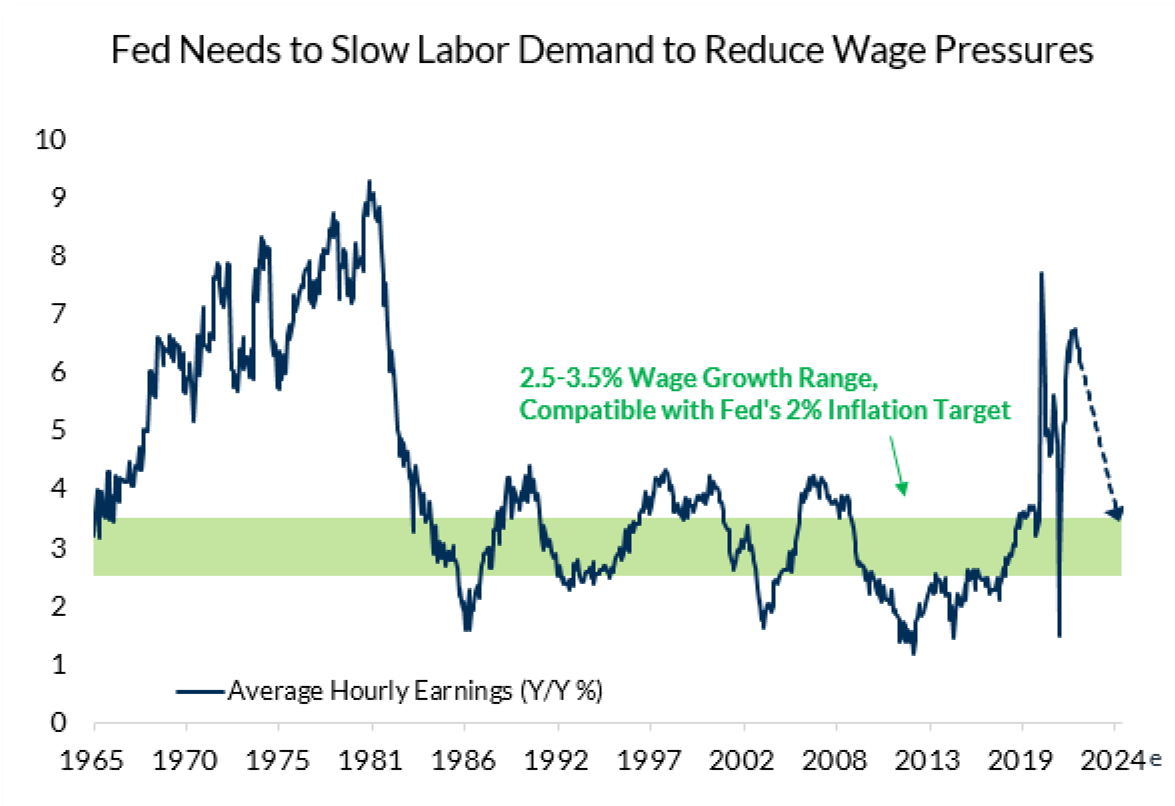
US	• Offers the most favorable opportunity set • Strength in real income & household balance sheets • Favorable labor market dynamics • Corporate resilience, stronger productivity and competeviness • Health of banking system
Europe	• Recession underway amidst high unemployment, double digit inflation • Ukraine war, high energy and commodity costs • ECB tightening cycle lagging Fed • Weaker outlook for earnings growth • Long term structural challenges: aging population, declining productivity, and diminishing global competitiveness.
China	• Increasing state control, decrease in private sector independence. • Questionable corporate governance and lack of shareholder protection. • Return on equity and levels of profitability trending down • Reopening expected to be bumpy, stressing healthcare system. • Property sector bubble. Slowing global demand impacting exports.

The U.S. currently has the strongest economy in the world, which is one reason CNR has pulled all allocations from Europe. CNR's concern is that Europe will continue to experience high inflation, high unemployment and high energy costs. China's increasing state control, property bubble and difficulties with COVID-19 policies contribute to the concern about investing there.

The Fed's Battle With Inflation Continues

While inflation has shown signs of cooling recently, a prime contributor that has concerned the U.S. Federal Reserve is wage growth.

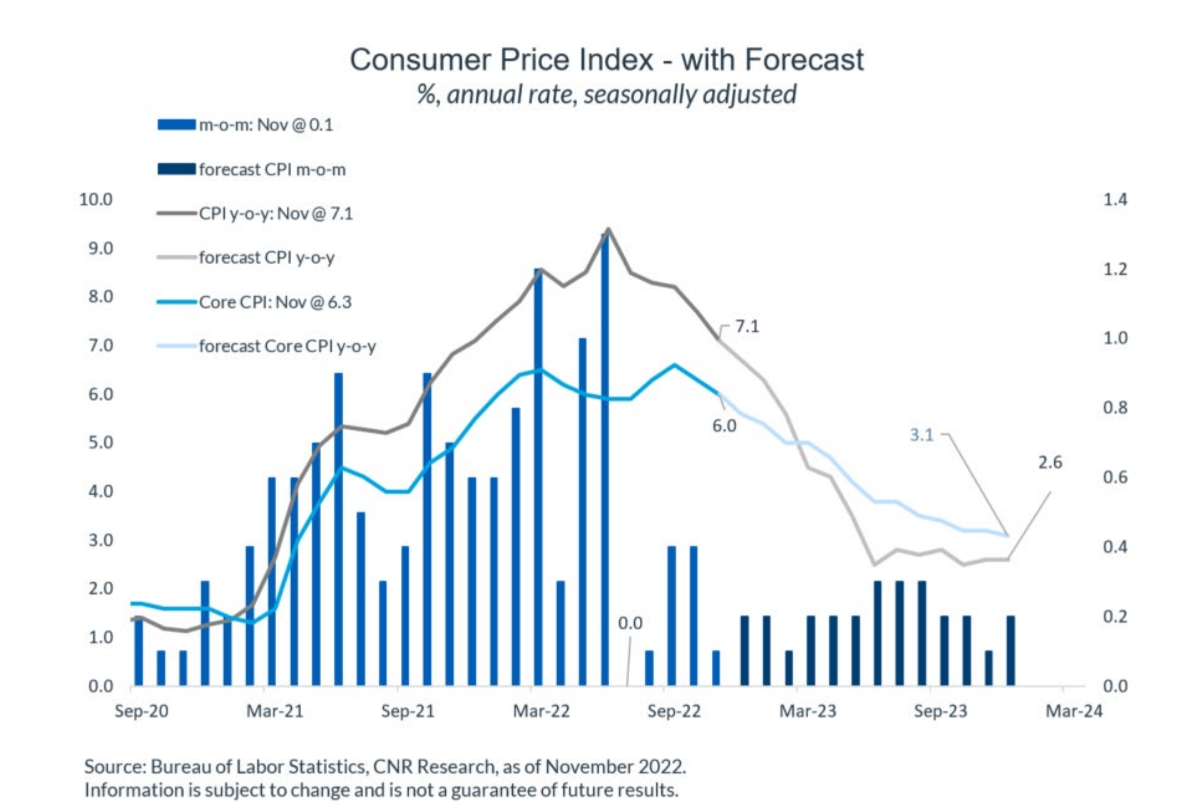
“The Fed has been very transparent that they want wages to come down to a range that's consistent with their inflation target of 2%," said Paul Single, CNR managing director, senior economist and senior portfolio manager. “If the labor market doesn't soften, the Fed will keep rates higher for longer."



Sources: Bloomberg, CNR Research, as of December 2022. Information is subject to change and is not a guarantee of future results. e: Estimates

Inflation pressures are expected to moderate in 2023, especially with food inflation coming down. Higher prices and higher financing costs are likely to slow consumer spending, too.

“Our view is that inflation is heading in the right direction, but it will take time to come down enough," said Single.

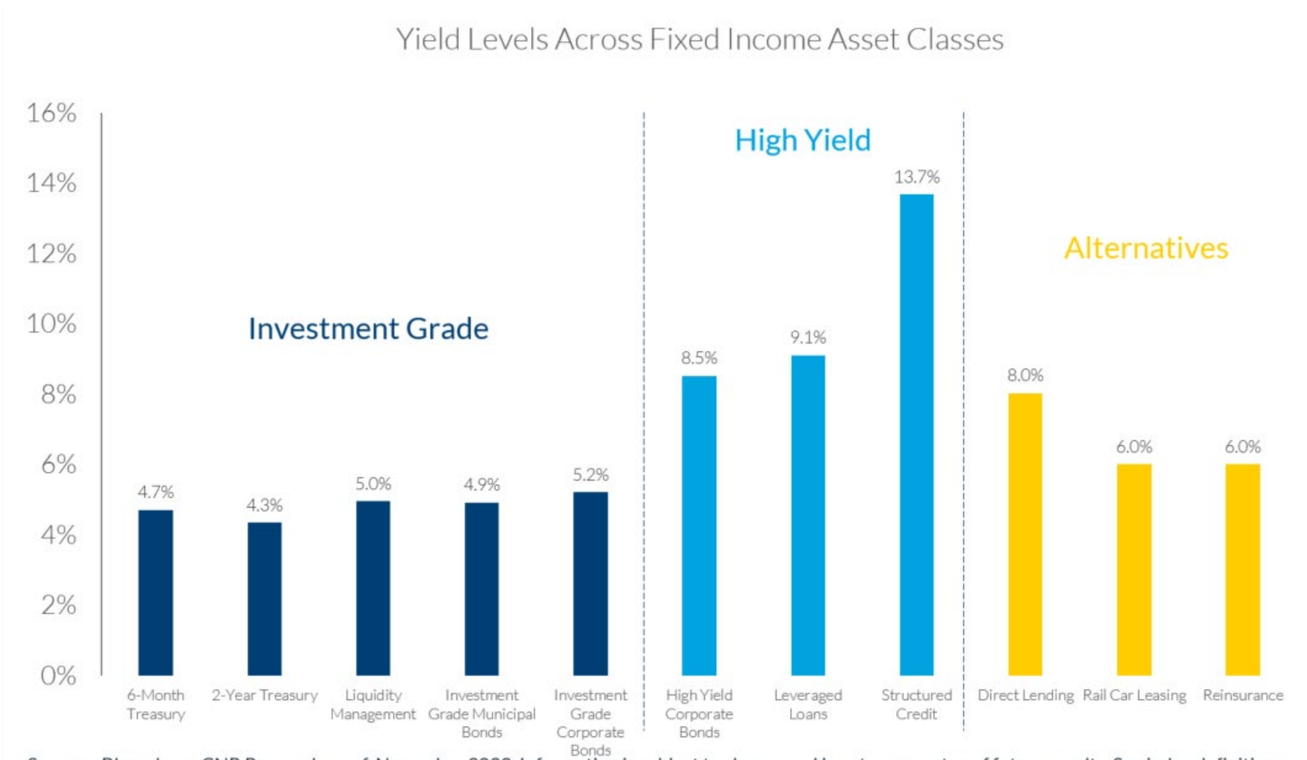


Investment Opportunities Exist Amidst Volatility

Investors have found some opportunities over the past year that should extend into 2023. Yields have been substantially higher on some fixed income assets. Investors can take advantage of higher short-term rates on investment grade bonds that have been close to 5% for a year and provide income with less risk, said Charles Luke, managing director and co-director of fixed income for City National Rochdale.

Owning high yield bonds is still beneficial over time, too, Luke said. CNR's team has also found success investing in alternative assets for more yield, such as direct lending, rail car leasing and reinsurance contracts, all of which are typically more stable than some other investments.

“What we're illustrating here is that opportunities for investors in bond markets have significantly improved through the year," said Luke. “With these elevated returns, we do expect bond returns to increase over the next three to five years."



Sources: Bloomberg, CNR Research, as of November 2022. Information is subject to change and is not a guarantee of future results. See index definitions for more information.

Specific asset allocation decisions will depend on whether the U.S. economy is in a slow growth period or a mild recession. But over the long term, high-yield bonds are more appealing, Luke said. In a mild recession, short-term bonds and two-year Treasury notes are options to consider.

Research from Bloomberg and City National Rochdale show that fixed income investments can offset volatility and generally move higher as economic growth bottoms out. Fixed income yields will generally outperform the 10-year average if interest rates are more stable.

More Liquid

All High Net Worth Investors With No Minimums

Asset Class	Income Focus	Volatility	Structure	Liquidity
Reinsurance	Low (Periodic)	Low	Interval Fund	Quarterly
Collateralized Loan Obligations ("CLOs")	High (7-9%)	High		
Direct Lending	High (5-8%)	Medium		

Eligible for Qualified Purchasers With $250k or More

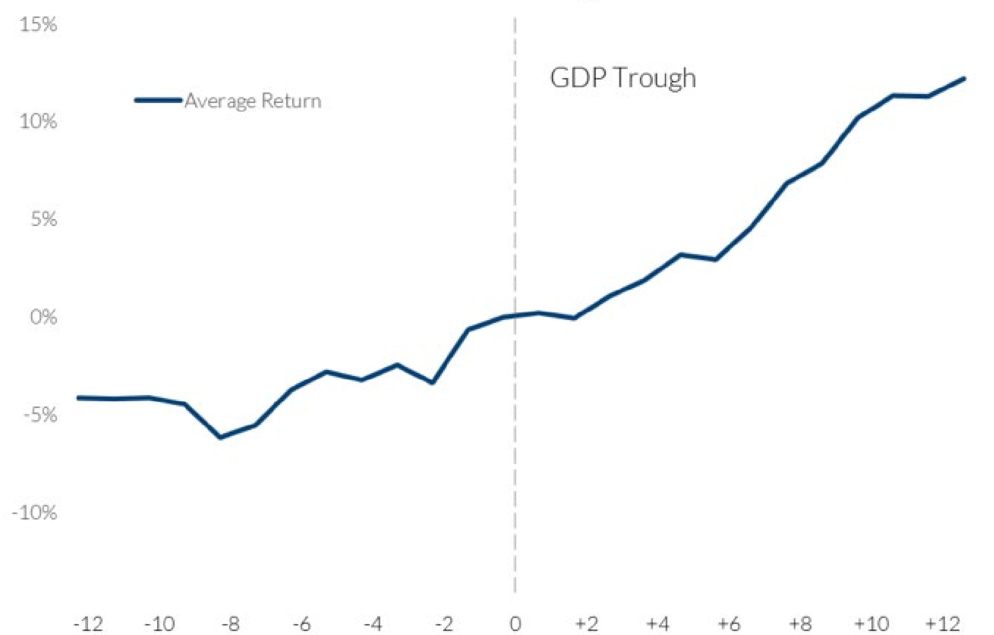
Asset Class	Income Focus	Volatility	Structure	Liquidity
Private Equity Co-Invest/Secondaries	Low (Periodic)	Medium	Tender Offer Interval Fund	1-year lock-up
Capital Leasing Rail Cars	Medium (9%+)	Low	Open Ended Partnership	2-year lock-up
Event Driven Legal Catalyst	Low (No Distributions)	High	Evergreen Hedge Fund	1-year lock-up
Capital Leasing Marine Transport	High (10%+)	Low	Open Ended Partnership	2-year lock-up

Less Liquid

Sources: Bloomberg, CNR Research, as of December 2022. Information is subject to change and is not a guarantee of future results.

Investment Risks in 2023

Bloomberg U.S. Aggregate Index Performance Before & After GDP Troughs



[1] Covers performance periods with GDP troughs in 1970, 1973, 1981, 1990, 2001 and 2008
Sources: Bloomberg, CNR Research, as of December 2022.

While equity valuations have adjusted, consensus earnings estimates still are not reflecting a more challenging economic outlook and negative revisions to forecasts could be a source of further downside in the near term.

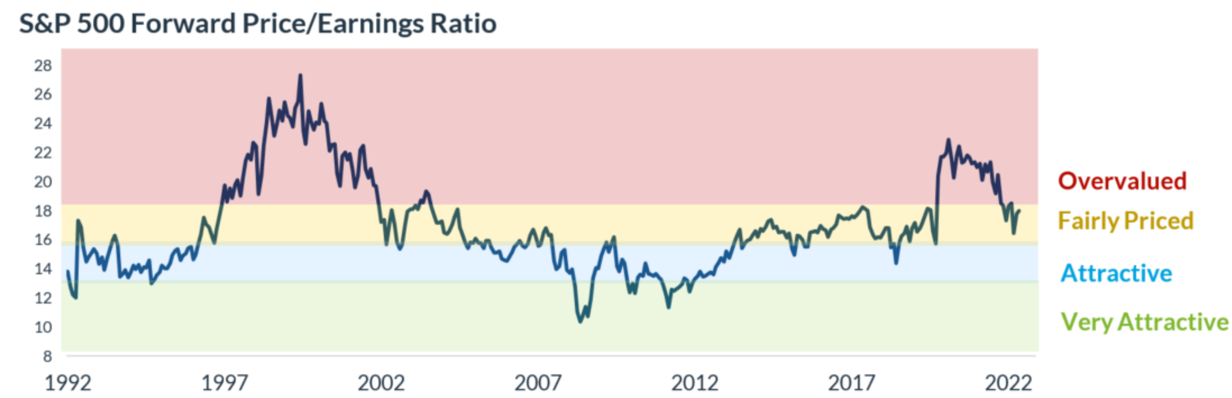
Among the other critical issues CNR is watching, that could have a negative impact on equity markets in 2023, is the possibility that interest rates go even higher and the potential for further exogenous shocks.

“We believe our core equity strategy is well-positioned for a mild recession and we've proactively lowered our exposure to companies and industries that are most at risk," said Tom Galvin, chief investment officer for City National Rochdale. “Conversely, we've increased our exposure to companies and industries that are more steady growers."

Mild Recession Likely in 2023

2023 Critical Issues to Watch

	Earnings	P/E Multiple
Positive	• Inflation moderation	• Valuation correction
	• Dollar headwind abating	• Earnings yield favorable vs. Fixed Income
	• Mild recession	
Negative	• Margins still elevated	• Absolute PEs still not attractive
	• Consensus earnings estimates too high	• Downside risk if real rates go higher
	• Risk of exogenous shocks remain	• Risk of exogenous shocks remain



Sources: FactSet, CNR Research, as of November 30, 2022. Information is subject to change and is not a guarantee of future results.

Among three likely 2023 scenarios - slow growth, a mild recession, or a normal recession - CNR believes a mild recession is the most likely. The leadership team is particularly watching labor and wages as an indicator for the economy in 2023, along with geopolitical risks.

“For the Fed to succeed in its battle against inflation, we need to see a sustainable decline in wage growth to about 2.5% to 3.5% wage growth," said Galvin. "If this proves challenging, the tightening process may have to be sustained and go higher."

While history and research provide optimism about future returns, investors should expect volatility and perhaps further downside risk in the near term.

"Rest assured, if a severe recession risk goes up, as fiduciaries with a prudent responsibility to manage your capital, capital preservation is still as important as capital appreciation and we have a plan," said Galvin.

	Slow Growth	Mild Recession	Normal Recession
Probability	25%	60%	15%
Economy	Below trend	Contract-to-flat	Contract
Consumption	Moderate	Weak-to-moderate	Weak
Labor	Pace of hiring slows, "Job gap" narrows	Moderate job losses	Significant increase in unemployment
Inflation	Remains elevated	Gradually eases	Falls faster
Interest Rates	Elevated but range bound	Lower	Curve inversion persists, Long-end meaningfully lower
Fed Policy	Tightening continues well into 2023	Pause	Potential rate cut 2H of 2023
Geopolitical Risk	China reopens successfully, Ukraine resolution	Slow progress in China, Ukraine stalemate continues	China COVID setbacks, Ukraine War escalates

Source: CNR Research. Information is subject to change and is not a guarantee of future results.

Any opinions, projections, forecasts, and forward-looking statements presented herein are valid as on the date of this document and are subject to change.

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.

As with any investment strategy, there is no guarantee that investment objectives will be met and investors may lose money.

Diversification does not ensure a profit or protect against a loss in a declining market. All investing is subject to risk, including the possible loss of the money you invest.

Returns include the reinvestment of interest and dividends.

Indexes are unmanaged and investors are not able to invest directly into any index.

The mention of a specific security is not a recommendation to buy, or solicitation to sell such security.

Quality ranking: City National Rochdale Proprietary Quality Ranking is the weighted average sum of securities held in the strategy versus the S&P 500 at the sector level using the below footnoted formula. 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).

Dividend Quality ranking: City National Rochdale Proprietary Dividend Quality Ranking is the weighted average sum of securities held in the strategy versus the S&P 500 at the sector level using the below footnoted formula. City National Rochdale Proprietary Dividend Quality Ranking formula: 15% Free Cash Flow Yield, 15% Free Cash Flow Margin, 10% Free Cash Flow Growth, 10% Dividend Growth (1-year and 5-year), 20% Dividend Payout Ratio, 15% Leverage (debt to equity ratio), 15% Return on Equity.

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.

Muni Bond: A municipal bond is a debt security issued by a state, municipality or county to finance its capital expenditures, including the construction of highways, bridges or schools. These bonds can be thought of as loans that investors make to local governments.

Bloomberg Barclays U.S. Corporate High Yield Bond Index: measures the USD denominated, high-yield, fixed-rate corporate bond market.

Dow Jones Select Dividend Index: The Dow Jones U.S. Select Dividend Index looks to target 100 dividend-paying stocks screened for factors that include the dividend growth rate, the dividend payout ratio and the trading volume. The components are then weighted by the dividend yield.

The Intercontinental Exchange (ICE): The Intercontinental Exchange (ICE) is an American company that owns and operates financial and commodity marketplaces and exchanges.

The Bloomberg Aggregate Bond Index: "the Agg" is a broad-based fixed-income index used by bond traders and the managers of mutual funds and exchange-traded funds (ETFs) as a benchmark to measure their relative performance. U.S. Treasury Yield Curve: refers to a line chart that depicts the yields of short-term Treasury bills compared to the yields of long-term Treasury notes and bonds.

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.

Bloomberg Barclays US Aggregate Bond Index: The Bloomberg Aggregate Bond Index or "the Agg" is a broad-based fixed-income index used by bond traders and the managers of mutual funds and exchange-traded funds (ETFs) as a benchmark to measure their relative performance.

MSCI Emerging Asia PE: The MSCI Emerging Markets Index is a selection of stocks that is designed to track the financial performance of key companies in fast-growing nations. It is one of a number of indexes created by MSCI Inc., formerly Morgan Stanley Capital International.

Global Equity Markets: a global market in which shares of companies are issued and traded, either through exchanges or over-the-counter markets.

6M T-Bills: The 6 Month Treasury Bill Rate is the yield received for investing in a US government issued treasury bill that has maturity of 6 months.

2-Year Treasury Notes: negotiable debt obligations issued by the U.S. Treasury Department (other than a Stripped Treasury Security) having a remaining maturity of more than one year but not more than two years.

Liquidity Management: The liquidity index calculates the days required to convert a company's trade receivables and inventory into cash.

Investment Grade Municipal Bonds: Investment-Grade Municipal Bond Investment-grade municipal bonds are debt securities, issued by state and local governments carrying the lowest credit risk that a bond issuer may default.

Investment Grade Municipal Bonds: Bloomberg Municipal Bond Inter-Short 1-10 Year Total Return Index.

Investment Grade Corporate Bonds: Investment grade corporate bonds are low-risk bonds. Because they are bonds, they are not tied to equity. Instead, they are like debt notes issued by a corporation. Investment Grade Corporate Bonds: Bloomberg Intermediate Corporate Bond Index.

High Yield Corporate Bonds: “U.S. High Yield Corporate” is represented using the U.S. High Yield Index.

High Yield Municipal Bonds: Bloomberg 60% Tax-Exempt HY / 40% LB Municipal Investment Grade Total Return Index.

Leveraged Loans: S&P LSTA Leveraged Loan Index, 6m T-Bills – ICE BofA 6-Month Treasury Bill Index, U.S. High Yield Corporate: 1-3 Years – ICE BofA U.S. High Yield 1-3 Year Index, Intermediate Municipal – Bloomberg 1-15 Yr Municipal Index, U.S. High Yield Corporate – Bloomberg U.S. High Yield Corporate Index, Intermediate IG Corporate – Bloomberg Intermediate Corporate Index, High Yield Municipal – Bloomberg 60% Tax-Exempt HY/40% LB Municipal Index.

Speculative Technology: Companies in early stages of business development with negative net income that provide technology products or services.

Digital Revolution: Companies that provide technology products or services, and/or use technology products and services in a manner that enhances their business.

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