City National Rochdale®
AN RBC/CITY NATIONAL COMPANY

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On the Radar

FAQS ON THE MARKETS AND ECONOMY

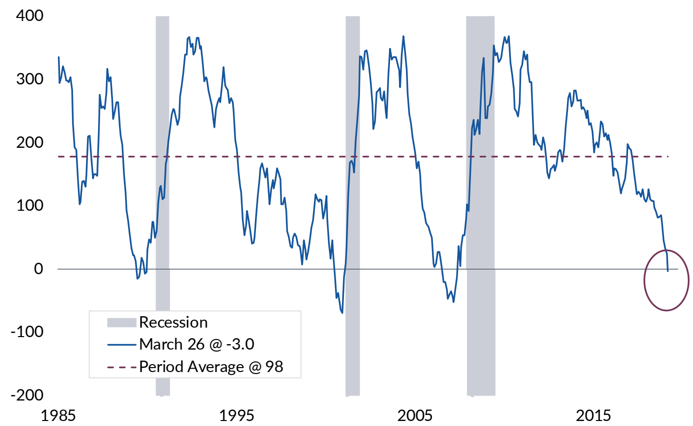
What does the inversion of the yield curve mean?

The yield on short-term investments now exceeds that of longer-term interest rates for the first time since 2007 (chart). Historically, an inversion is rare and noteworthy. It is often viewed as an indicator that precedes a recession and has proven to be a good one (although not perfect). This is because lower long-term rates can indicate that market perception for the future of economic growth is poor.

This time is a little different. The risk of a recession appears to be low. Economic fundamentals are strong, with very low unemployment rate and inflation. The Fed projects the economy to maintain an average growth rate of 1.9% over the next three years.

This time, longer-term interest rates have downward pressure due to lower global inflation. Foreign investors have been buying U.S. treasury securities because they yield more than their own sovereign debt. For comparison, the yield of the U.S. 10-year note is 2.43%, German -0.07%, and Japan -0.10%.

The Slope of the Yield Curve Has Gone Negative (Yield Difference Between 10-Yr. note and 3-Mo. bill, bps)



Source: Bloomberg. As of March 26, 2019.

KEY QUESTIONS

With the yield curve inverting, is it time to change my portfolio strategy?

Will housing rebound in 2019?

What's going on with Brexit?

With the yield curve inverting, is it time to change my portfolio strategy?

While the yield curve may be telling us that we are moving late into the cycle, we don't think its telling us it's time to sell risk assets. The recent inversion is certainly something to be watched, but it has not been a good indicator to use for timing changes to one's portfolio. In the past, when there has been a prolonged inversion, risk assets have tended to do quite well for a year or more.

We also think the recent curve inversion has primarily been driven by pressure from negative rates in Europe, as opposed to any significant deterioration in the U.S. economic outlook. Meanwhile, the Fed's more dovish stance is a strong support for the economy and markets. It lowers the risk of recession and is good for valuations.

This may be a time to be cautious, but there should be gains ahead as we move into the second half of the year and corporate profit results improve from their current weak patch. We have positioned for expected upcoming volatility by staying invested in quality U.S. assets and generally steering away from exposure to developed markets equities.

Yield Curve Inversion and Equities

Inversion Signal	Months to Recession	S&P 500 Return (NTM)
Sep-66	False Alarm	24%
Dec-68	12	-15%
Feb-73	9	-22%
Jul-78	18	8%
Sep-80	11	1%
May-89	14	12%
Sep-98	30	37%
Feb-06	22	13%
Average	**16.6**	**7.3%**
Median	**15.3**	**7.7%**

Source: FactSet. As of March 2019.

Will housing rebound in 2019?

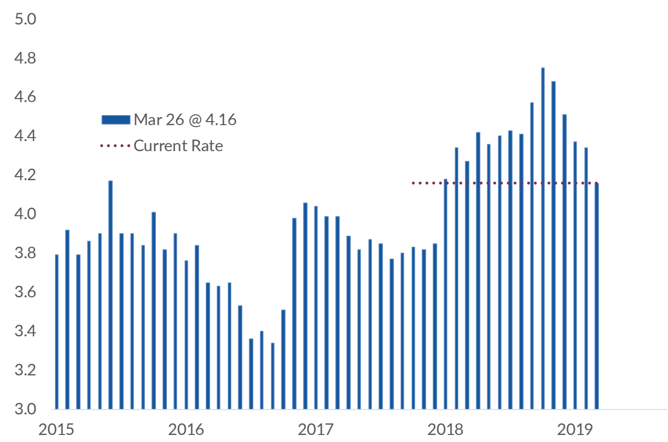
Following 2018, in which the housing market lost considerable momentum, the fundamentals are reversing direction and moving in the direction to make a more favorable environment for home buyers.

One of the major factors affecting housing demand is mortgage rates. The rate on the 30-year fixed rate mortgage has fallen 66 bps since a recent high back in November. It is at a rate not seen in over a year (chart).

Also, home prices have begun to moderate. In the past year, the national average of home prices is up 4.3%. In the period of 2012 (the lows of the market) though 2018, they averaged an annual growth rate of 5.6% and increased an aggregate of 53%.

Demand should pick up. For some time, housing starts have been plagued by bad weather. There were wildfires in the West in the summer, then Hurricanes Florence and Michael in the early autumn, horrendous fires in the West in November, and the polar vortex in the beginning of this year.

Mortgage Rates Are Moving Down (30-Year Fixed Rate Mortgage, %)



Source: Bankrate.com. As of March 26, 2019.

What's going on with Brexit?

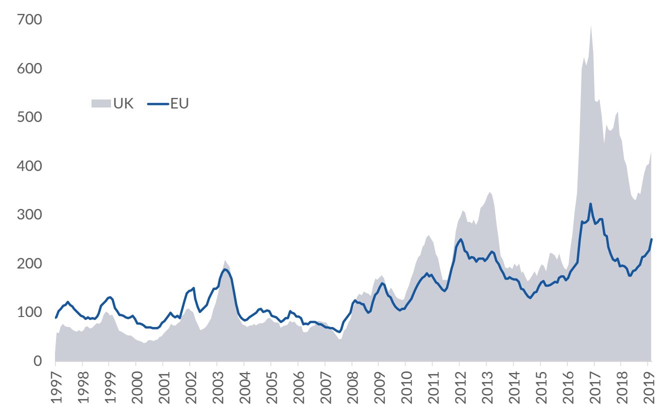
Nearly three years after the UK voted to leave the European Union, the deadline for Brexit is less than two weeks away and the British government is still scrambling to reach a consensus. After a week of stunning defeats in Parliament, British lawmakers will again try to find a way out of the impasse when they run a second vote on alternatives to Prime Minister May's deal on Monday. However, if Parliament has made one thing clear, it is that it is not prepared to leave the EU without a deal.

If no deal is reached this week, the UK will likely seek and the EU will accept a long Brexit delay conditional on participation in the upcoming European elections, ongoing budget contributions and a political process to break the impasse.

We still feel the odds are that the UK leaves the EU with a deal. Staying in the EU is the next most likely outcome and a no-deal Brexit the least. But Brexit is extremely complicated, making it impossible to predict exactly how and when this will all play out.

Most economists and business groups think a no-deal scenario would be disastrous, erecting customs checks, tariffs and other barriers between Britain and its biggest trading partner. In the meantime, uncertainty around the issue continues to weigh on what is an already weakening European economy. Our portfolio positioning, with a material underweight to European equities, reflects this reality.

Euro Economic Policy Uncertainty Remains High



Source: Policyuncertainty.com. As of March 2019.

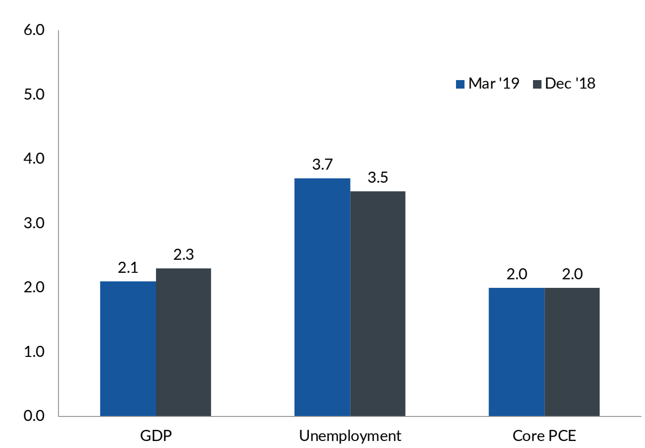
What did the Fed decide at their recent FOMC meting?

The Fed has downgraded their expectation of economic growth and they became more dovish on interest rates. Their projection for GDP growth dropped to 2.1% from 2.3% (chart), when they last meet in December. They have growing concerns about the pace of consumption in investments.

With the muted outlook on the economy, they changed their view to no interest rate hikes for this year, from their earlier projection of two hikes. This was a positive surprise to the markets. They held steady with their view of inflation, keeping it at 2.0%, which is also their target rate.

This move is a further extension of the dovish pivot Chairman Powell made in early January. With the weakness in the global economy and the softness in Q1 GDP growth (most of which was brought on by technical factors such as the government shutdown and the polar vortex), the Fed can continue to be patient, which should help the prospects of greater economic growth.

FOMC Projections for 2019



Source: Federal Reserve Bank. As of March 2019.

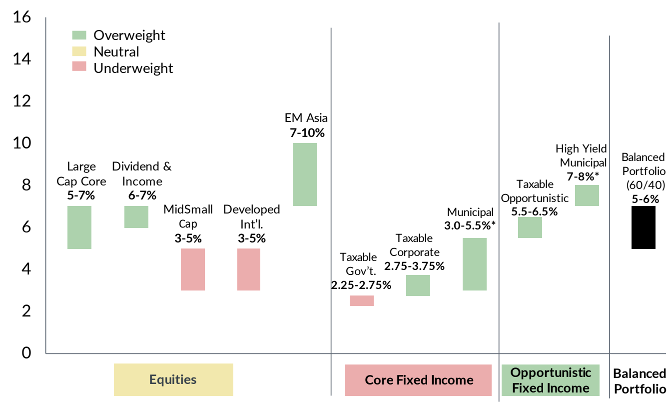
What is City National Rochdale's investment outlook for 2019?

Given our positive assessment of the fundamental backdrop, we remain bullish on equities in general for 2019 and continue to see attractive prospects in the opportunistic fixed income class. Still, we believe investors should prepare for more moderate returns in the year ahead and continued volatility.

The investment landscape has grown more challenging as investors adjust to more typical late-stage expansion conditions of higher inflation, rising interest rates and less accommodative monetary policy. Meanwhile, concerns over global growth, trade tensions and other geopolitical risks mean markets will likely continue to be subject to periodic swings in sentiment and potential pullbacks.

None of this means there are not more worthwhile gains ahead for investors, but it does highlight the value of active management and the need for investors to become more selective. Our equity and fixed income research teams have made deliberate risk-mitigating changes to help fortify client portfolios against the type of turbulence we have recently experienced while leaving them well-positioned to take advantage of opportunities should they present themselves.

One-Year Forecasted Returns (%)



Source: City National Rochdale. As of March 2019. Forecasted expected returns represent City National Rochdale's opinion for these asset classes, are for illustrative purposes only and do not represent client returns. The expected returns presented for these asset classes do not reflect any deductions for City National Rochdale fees or expenses. Actual client portfolio and investment returns will vary.

*Forecasted expected returns for HY Municipal and Municipal FI represent the taxable equivalent return at a 43.40% tax rate.

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

Investing in international markets carries risks such as currency fluctuation, regulatory risks, and economic and political instability.

Emerging markets involve heightened risks related to the same factors as well as increased volatility, lower trading volume, and less liquidity. Emerging markets can have greater custodial and operational risks, and less developed legal and accounting systems, than developed markets.

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.

Investments in below-investment-grade debt securities, which are usually called “high-yield” or “junk” bonds, are typically in weaker financial health, and such securities can be harder to value and sell and their prices can be more volatile than more highly rated securities. While these securities generally have higher rates of interest, they also involve greater risk of default than do securities of a higher-quality rating.

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.

Investments in emerging markets bonds may be substantially more volatile, and substantially less liquid, than the bonds of governments, government agencies, and government-owned corporations located in more developed foreign markets.

Indices are unmanaged and one cannot invest directly in an index. Index returns do not reflect a deduction for fees or expenses.

Returns include the reinvestment of interest and dividends.

Investing involves risk, including the loss of principal.

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

Past performance is no guarantee of future performance.

Index Definitions

The Standard & Poor’s 500 Index (S&P 500) is a market capitalization-weighted index of 500 common stocks chosen for market size, liquidity, and industry group representation to represent U.S. equity performance.