City National Rochdale®

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On the Radar

FAQS ON THE MARKETS AND ECONOMY

What explains the disconnect between the economy and stock market?

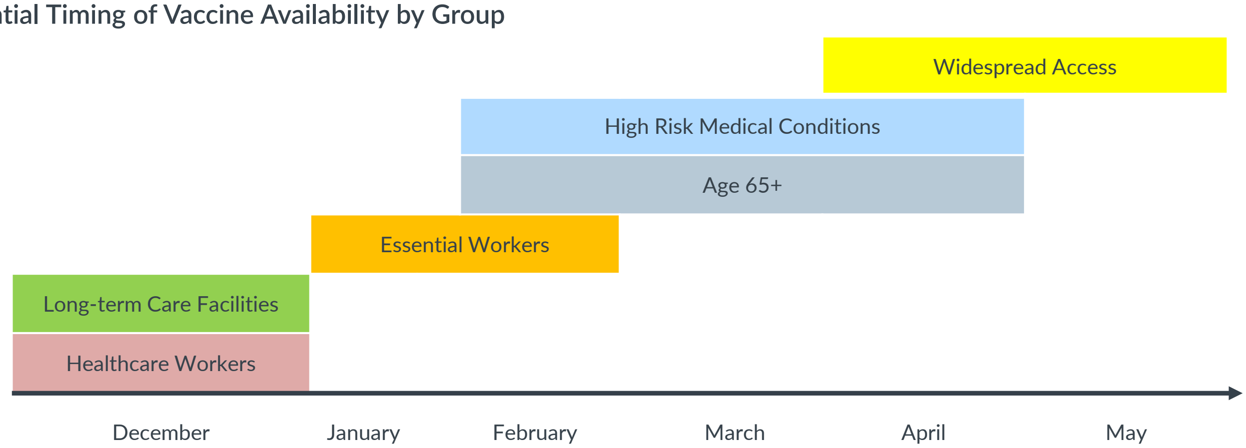
The recovery in the equity markets has confounded some, given the damage to the economy caused by the COVID crisis. However, it's important to remember that stock prices are forward-looking in nature. In other words, investors have continued to look past the near-term struggles facing businesses and consumers, and, instead, they have begun to eye prospects of widely available vaccines by next spring, which should allow for a return to more normalcy in economic activity and support a rebound in corporate profits.

Another thing to keep in mind is that the stock market is not the economy. Not only are the hundreds of thousands of nonpublic businesses still enduring hardship not counted in major stock indexes, but the market is also heavily weighted toward technology companies, which have actually benefited from societal changes forced by the pandemic.

For example, the technology sector comprises 39% of the S&P 500, but only 6.9% of U.S. GDP. In contrast, the service industries most impacted by the crisis (retail, restaurants, hotels, transportation, tourism, and entertainment) amount to 19% of GDP, yet these same industries represent only about 7% of S&P 500 earnings.

Finally, policy actions have played a leading role in the market recovery. Fiscal relief from Washington has, so far, been effective in helping fill the income gap created by the historic spike in unemployment. Meanwhile, the Fed and other global central banks have implemented unprecedented monetary-policy stimulus, which has lowered interest rates driving investors into stocks, and provided confidence that policymakers will do whatever is necessary to support the economic recovery and functioning of financial markets.

Potential Timing of Vaccine Availability by Group



Source: S&P 500.

KEY QUESTIONS

What did we learn from the monthly labor report?

What did the Fed's Beige Book tell us about the current state of the economy?

Are dividend and income equities attractive?

What did we learn from the monthly labor report?

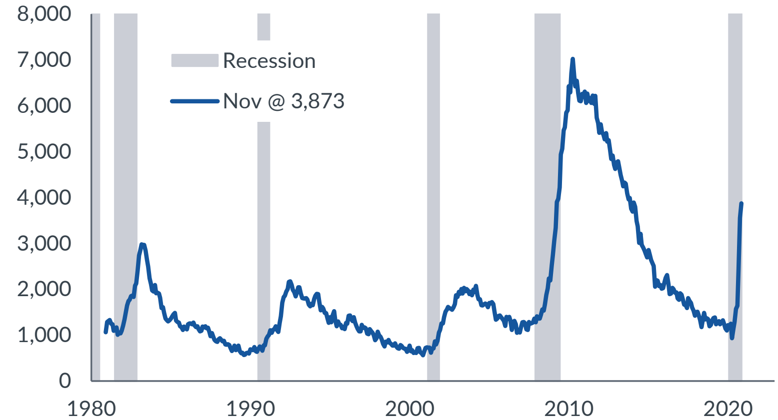
The pace of job gains is weakening. The November jobs report was disappointing to the downside, with payrolls increasing just 245,000, well below the expectation of 460,000. Job gains have slowed for the past five months after peaking at 4.8 million back in June. Hiring was concentrated in just a few industries.

The unemployment rate, which is calculated by another survey, fell to 6.7% from 6.9%. It fell for the wrong reason; it fell because the number of people working or looking for jobs fell by 400,000.

Employment stands 9.8 million below the pre-pandemic levels. The number of those out of work for more than six months has grown to 3.9 million, the highest level since 2013 (see chart). This group makes up more than a third of all unemployed. When someone is unemployed for a long period of time, they tend to lose skills and relationships, making it difficult to easily return to the workforce.

Number of Unemployed for 27 Weeks & Over

not seasonally adjusted



Source: Bureau of Labor Statistics as of November 2020.

What did the Fed's Beige Book tell us about the current state of the economy?

The economic recovery remains at a moderate pace for most of the country, but is slowing in areas where the number of coronavirus cases is exceptionally high. This is especially true for the Midwestern states, which have recently been hit particularly hard with the virus. Overall, the report had a weaker tone than the previous publication in October.

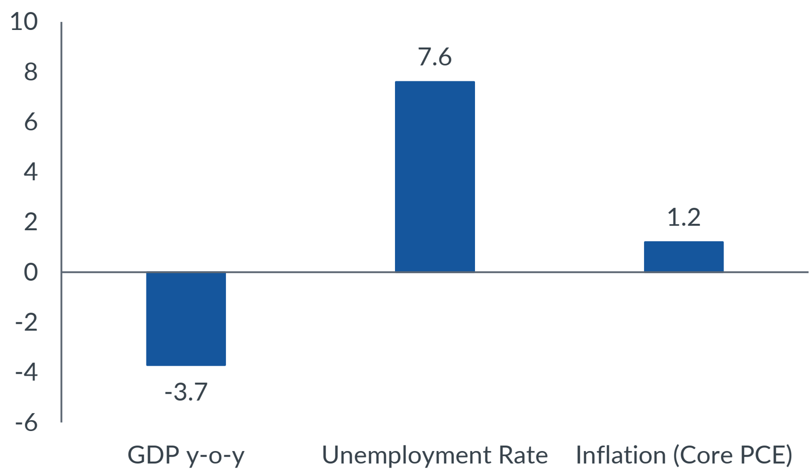
Living in a pandemic continues to be a challenge. It was noted that virtual schooling and childcare continue to pose challenges for many parents. This is a concern for women who want to return to the workforce, since they are more apt to stay at home to care for the children. The labor force participation rate for working-age women (25-54) stands at 74.6%, below men of the same age, at 87.9%. The gap between the two has widened 1.0 ppt. since the beginning of the recession.

The Beige Book is published eight times a year, just before the FOMC meeting. It is a compilation of anecdotal information on the current economic conditions.

The Fed will be updating its economic projections at its upcoming meeting on December 16. This chart shows the recent outlook from September. In some aspects, the economy has performed better than the Fed thought; back in September, they thought year-end unemployment would be 7.6%; it currently stands at just 6.7%.

FOMC Economic Projections

%, September 2020



Source: Federal Reserve Bank as of September 2020.

Are dividend and income equities attractive?

In the context of this year's rally, we believe dividend and income equities offer some of the most attractive remaining value for investors. Dividend stocks are priced attractively, not only in relation to history, but also in relation to growth stocks, which have seen a dramatic increase in valuations throughout the COVID crisis.

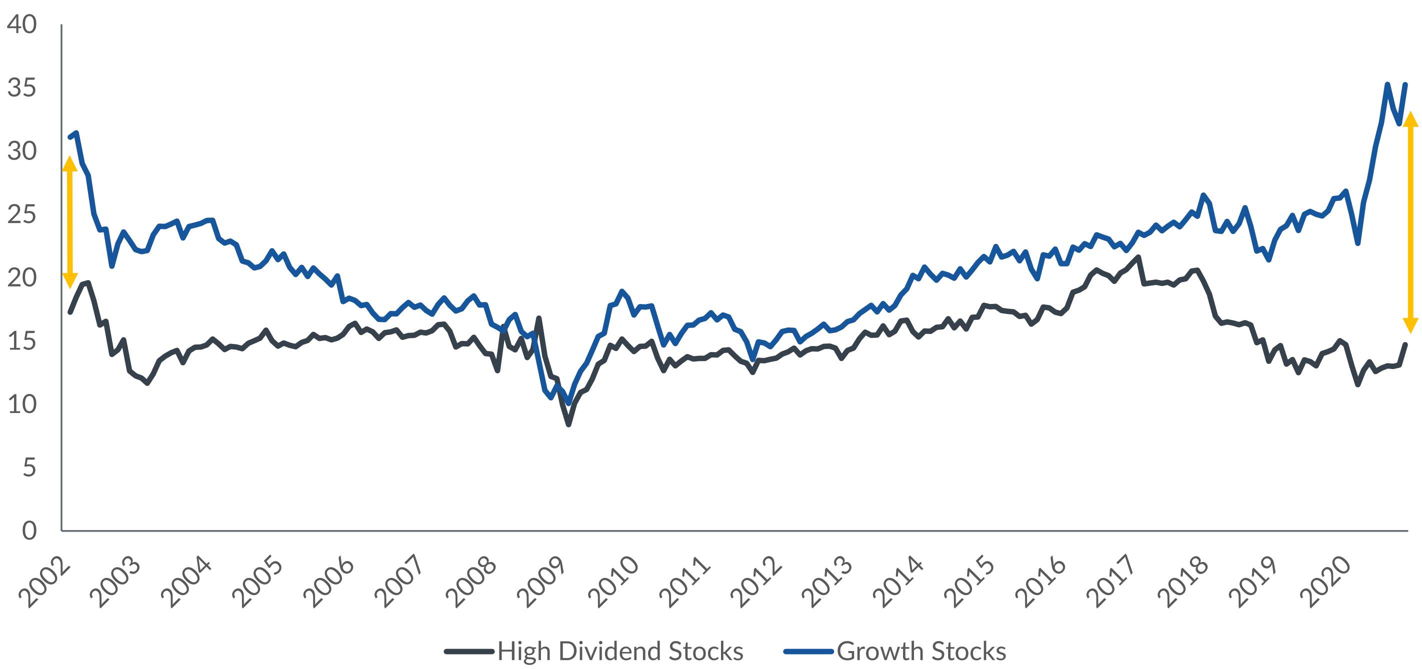
Going forward, the mass distribution of a vaccine sometime next year should allow for economic activity to return to more normal levels, proving a boost to the economically sensitive value sector, including many of our dividend stocks, which have lagged the recovery.

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 we believe can maintain their dividends through the economic uncertainty ahead, we are increasingly focusing on companies that may have 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



Source: CNR Research, Bloomberg. Growth Stocks: S&P 500 Growth Index. High dividend stocks: Dow Jones U.S. Select Dividend Index.

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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.

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.

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

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.

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.