

A low-angle, upward-looking photograph of several modern skyscrapers with glass facades. The buildings are set against a clear, bright blue sky. The perspective creates a sense of height and architectural grandeur. The buildings are reflected in a dark blue horizontal band that serves as a background for the text.

City National Rochdale®

 AN RBC/CITY NATIONAL COMPANY

# The **BOTTOM LINE**

Relevant Insights for the Savvy Investor

FEBRUARY 2021

## INFLATION, OR THE LACK THEREOF

There are many articles in the news about the risk of inflation. We continue to believe that inflation is not a severe risk to the economy in the next few years.

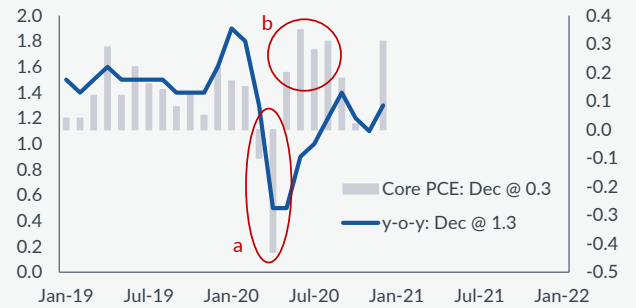
That said, for 2021, inflationary figures will be volatile. Inflation currently registers at 1.5% for the change in the past year. In the spring of last year, during the worst of the pandemic, there were a couple months of negative inflation as household buying plunged and producers/retailers had to drop prices (chart 1-a). Those monthly figures will soon drop off the year-over-year calculation, and the yearly change will increase. But in the past summer, when the economy reopened and demand for goods and services was strong, prices shot up (chart 1-b). When those increases drop off the yearly calculation, inflationary pressures will recede. By autumn 2021, the yearly change in inflation should normalize to show the real trend of price pressures.

The Fed will not be spooked by those events and will look past these factors as transitory and will not adjust monetary policy. The Fed will continue to focus on fundamental changes to the economy that may cause long-term price pressures. Based upon the Fed's recent projection for inflation, it does not think it will get to 2.0% until the end of 2023 (chart 2).

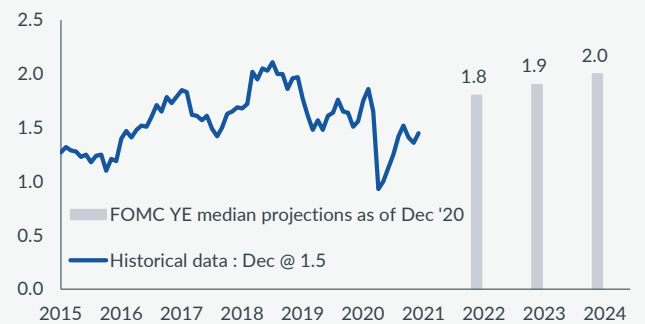
The Fed has signaled its plans to keep the federal funds rate low even if inflation moves above the 2.0% level. The Fed will delay raising interest rates as inflation starts to pick up because it is committed to ensuring that the economy gets back on track, and that the recovery is sustainable and inclusive.

We believe a few thresholds need to be passed before the Fed starts to respond to higher inflationary pressures: 1) inflation has to sustain a rate above 2.0% for about a year or more; 2) the unemployment rate needs to be below full employment (NAIRU – non-accelerating inflation rate of unemployment) (chart 3); 3) inflationary expectations have to sustain a level above 2.0% (chart 4); and 4) need evidence of an inclusive recovery.

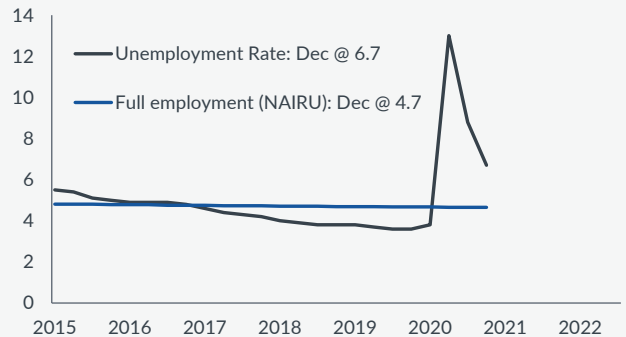
**CHART 1: Inflation: Core Personal Consumption Expenditure**  
% change, seasonally adjusted



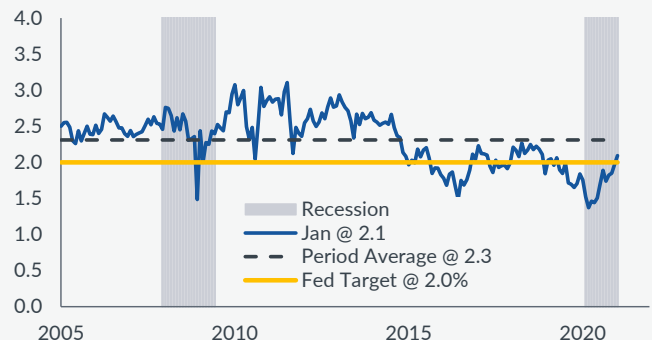
**CHART 2: Inflation & FOMC Projections**  
% change, year-over year, core personal consumption expenditures



**CHART 3: Labor Rates (%)**



**CHART 4: Inflation Expectations**  
5-yr./5-yr. Forward Breakeven (%)



Sources: Bureau of Labor Statistics, Federal Reserve Bank, Bureau of Economic Analysis, Congressional Budget Office, Bloomberg.

Investment management services provided by City National Bank through its wholly owned subsidiary City National Rochdale, LLC, a registered investment advisor.

Non-deposit Investment Products: ■ are not FDIC insured ■ are not Bank guaranteed ■ may lose value

# COVID-19

COVID-19 hospitalizations have begun declining and states are gradually reducing economic restrictions. The distribution of approved vaccines has accelerated, and positive data on multiple new vaccines indicates the potential for increased supply and reasonable effectiveness against new strains. Reduced virus spread and widespread vaccination should lead to economic normalization in mid-2021.<sup>1</sup>



## LABOR

After six months of declining monthly payroll growth, the January report reversed the trend. Combine that positive news with improving coronavirus news, and the outlook for labor appears good.<sup>2</sup>



## INFLATION

Inflation remained tame this past year despite the massive inventory shortages, shipping bottlenecks and rallies in many commodity prices. Inflation remains well below the Fed's goal and reflects an economy dealing with the pandemic's global economic slowdown.<sup>3</sup>



## THE FED

The Fed remains committed to keeping interest rates low to ensure the economy gets back on track, and that the recovery is sustainable and inclusive. Its current plan is to keep the short-term interest rate at the near-zero level until the end of 2023.<sup>4</sup>



## GDP

Economic output finished the final quarter up 4.0% and now stands just 2.5% below the previous peak. It has undergone a remarkable recovery from the pandemic due to the federal government's fast action (CARES Act) and the Fed dropping interest rates.<sup>5</sup>



## HOUSING

Home prices are up 9.1% year-over-year, which is more than twice the long-term average gain. Growing demand, low mortgage rates, and lack of supply are putting pressure on prices.<sup>6</sup>



## STOCK MARKET

Stocks have stumbled recently amid retail investor-driven volatility and signs of froth in more speculative areas of the market. Given the unprecedented rally from last February lows, a correction may be overdue, but we don't believe recent developments are a sign of an overall unhealthy market or a broader bubble.

Investment management services provided by City National Bank through its wholly owned subsidiary City National Rochdale, LLC, a registered investment advisor.

Non-deposit Investment Products:

■ are not FDIC insured

■ are not Bank guaranteed

■ may lose value

**Sources**

<sup>1</sup>Center of Disease Control

<sup>2</sup>Bureau of Labor Statistics

<sup>3</sup>Bureau of Labor Statistics

<sup>4</sup>Federal Reserve Bank

<sup>5</sup>Bureau of Economic Analysis

<sup>6</sup>S&P CoreLogic Case Schiller

**Important Disclosures**

The information presented does not involve the rendering of personalized investment, financial, legal, or tax advice. This presentation is not an offer to buy or sell, or a solicitation of any offer to buy or sell, any of the securities mentioned herein.

Certain statements contained herein may constitute projections, forecasts, and other forward-looking statements, which do not reflect actual results and are based primarily upon a hypothetical set of assumptions applied to certain historical financial information. Certain information has been provided by third-party sources, and although believed to be reliable, it has not been independently verified, and its accuracy or completeness cannot be guaranteed.

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

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.

Non-deposit investment products are not FDIC insured, are not bank guaranteed, and may lose value.

Investment management services provided by City National Bank through its wholly owned subsidiary City National Rochdale, LLC, a registered investment advisor.

Non-deposit Investment Products:

■ are not FDIC insured

■ are not Bank guaranteed

■ may lose value