City National Rochdale®

AN RBC/CITY NATIONAL COMPANY

Quarterly Update

ECONOMIC AND INVESTMENT MANAGEMENT PERSPECTIVES

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THIS ISSUE

From the Desk of

Garrett D'Alessandro, CFA, CAIA, AIF®

A Mountain Too High

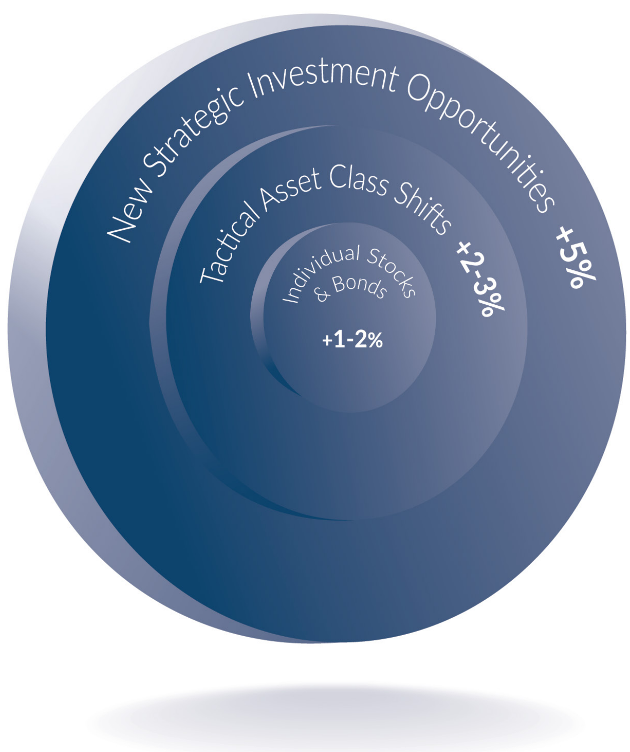
Investing in 2018 was like climbing to the top of Mount Everest, reaching the apex, then losing our footing and tumbling all the way down. The S&P 500 achieved a record high in September, with investors having earned approximately 11.2%, then fell to a net loss of about 4.38% for the year.

What matters is whether the U.S. economy and equity markets will regain their footing and produce good returns this year. We believe they will—during 2019, the markets should generate positive equity returns again. First we have to collect our senses, brush off the uncertainty, and regain our confidence. To do this, we need to get clarity on a few key issues, including: tariffs, interest rate concerns, and slowing growth in corporate earnings. Nonetheless, we are hopeful that the economy will remain solid enough for U.S. equities to generate returns of 6% to 8% in 2019. For fixed income investors, current yields are more appealing than a year ago—which we expect will remain modestly attractive.

Although 2018 returns were negative for equity investors and about flat for bond investors, City National Rochdale achieved positive results in several new strategic alternative asset classes through our purposeful expansion to our investment universe by focusing on new strategic opportunistic investing. Over the next two to three years, we seek to generate better returns and diversification by considering adding the addition of new opportunistic investment strategies to client portfolios.

We use a three-dimensional framework when structuring how we generate potentially superior returns.

OUR APPROACH TO SUPERIOR RETURNS



Source: City National Rochdale

City National Rochdale's investment outlook over the next two to three years indicates a likelihood of generating lower than average returns from traditional asset strategies. This is why our research team is dedicating more effort toward identifying and offering higher-returning opportunities to our clients.

Our goal is to create more wealth for our clients than what is achievable by only investing in traditional investment choices.

U.S. stocks have been among the world's best performing investments for over 8 years. However, over the next few years, we expect that U.S. equities may generate positive but somewhat lower returns. U.S. investment grade bonds, among the world's safest, have averaged a very respectable 5.3% since 2008. Here, too, future performance expectations are likely to be lower over the next few years.

While we expect individual stocks and bonds to remain a core representation for client portfolios, we believe the outermost circle—New Strategic Investment Opportunities—will offer clients unique return and diversification choices to meet their investment objects. City National Rochdale's extensive research enables us to find promising investment opportunities that can add sustainable strategic value to client portfolios. These are higher returning investments that are difficult to discover, have limited access, and require extensive intellectual research efforts.

After an unusual year in which bonds and U.S. core stocks were flat to negative, City National Rochdale clients can be reassured that our unique and differentiated research has been successful over many such cycles by focusing on quality companies and now adding New Strategic Investment Opportunities. The goal is simply to find investment returns wherever present.

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There Will Be Growth in the Spring

By Matthew Peron

2018 was the most challenging year for equity investors since the financial crisis. After climbing to a record high in September, a volatile fourth quarter left the U.S. stock market in the red for the first annual decline in a decade. The weakness was widespread, with nearly every global region and most stocks delivering negative returns. But it wasn't only equities that suffered. The risk-averse mentality of investors pervaded almost all asset classes. In fact, **last year was the first since 1972 when none of the major asset classes generated a total return greater than 5%.**

For some time now, we have deployed a defensive tilt in our strategies. **Our equity and fixed income research teams have made deliberate risk-mitigating decisions to help fortify client portfolios for later stage business cycle conditions and rising volatility, while also leaving them well positioned to take advantage of a continuing positive investment environment.**

The degree of the recent sell-off in equities was surprising, even to us. In contrast, corporate bond markets were relatively, and reassuringly, resilient. Indeed, with stock declines toeing the edge of bear-market territory in December, we couldn't help being reminded of the famous scene from the 1979 film *Being There*. Amid concerns about faltering economic growth, the movie's main protagonist, Chauncey, reassures the President: "As long as the roots are not severed, all is well."

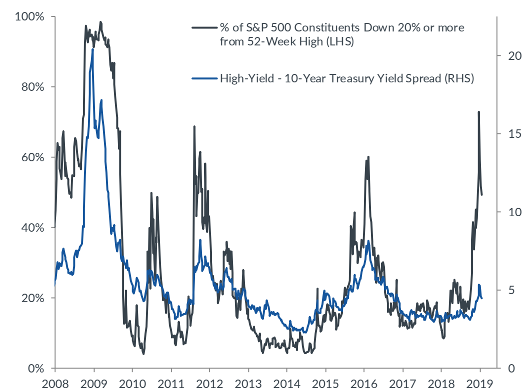
Markets now seem to have regained some of their footing, though it may be too soon to call the recent correction process over. Trade disputes, tighter Fed policy, political uncertainty, and weaker global growth have created a more balanced ledger of risks than we've experienced in many years. Yet, amid all the worries, we too find reassurance in that the economy's roots remain strong.

Market corrections can be very painful, trying the confidence of even the most hardened and seasoned investors. But it should not be forgotten that they are also normal. Since March 2009, we have experienced seven corrections, averaging a 13.0% decline. In fact, the recent drop is not uncharted territory for this expansion. Amid the Eurozone debt crisis and U.S. economic fears in 2011, stocks at one point fell 19.4%, only to rebound 33% over the next 12 months.

Similarly, **we believe the fundamental investment backdrop today is more favorable than recent equity moves and headlines might suggest.** Economic growth and corporate earnings may be slowing, but they are still growing and our most reliable leading indicators and

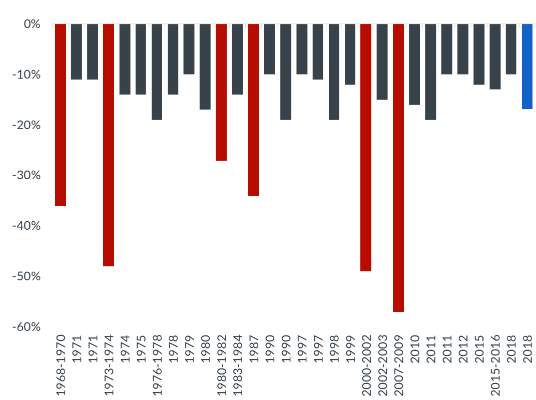
- Economic fundamentals remain positive
- Corrections are normal in bull markets
- City National Rochdale portfolio strategies have defensive tilt

Percent of S&P 500 Constituents Down 20% From Highs vs. High Yield Spread



Source: Dimson-Marsh-Staunton Dataset, FactSet, McKinsey as of 10/2018.

S&P 500 Corrections & Bear Markets



Source: FactSet as of 1/2018.

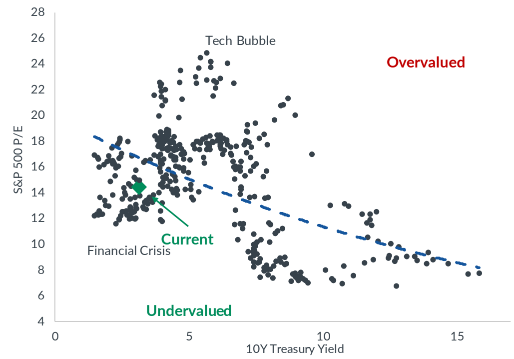
Speedometers℠ are signaling that they should keep doing so for at least the next several quarters.

Meanwhile, we believe markets have now priced in much of investor anxiety. Based upon consensus expectations for 2019 earnings growth, the S&P 500 was trading at 14.4 times earnings at year-end, a meaningful discount from the 15-year median of 16.5. Other valuation measures, including the relative attractiveness of stocks versus bonds, also appear much more favorable.

Although it can be difficult to remain calm in the midst of stock market action like we've seen recently, it is just these times when patience and discipline become more important than ever. More than 50 years ago, economist and investor Benjamin Graham observed: "In the short run the stock market is a voting machine, but in the long run, it is a weighing machine."

The unsettled markets carrying into 2019 are reacting to new economic and political realities, and expectations for global growth and corporate profits are being recalibrated. Our rigorous investment process has led us to stay the course over this normal weighing process and not overreact. It may take time but, as we have seen several times before in this cycle, markets eventually reconnect to positive fundamentals. To quote Chauncey one more time, as long as the roots are well: "There will be growth in the spring" (and beyond).

S&P 500 P/E vs. 10-Year Yield (1953-2018)



Source: FactSet as of 12/2018

U.S. Equity Outlook: The Battle Royale Continues

By Tom Galvin

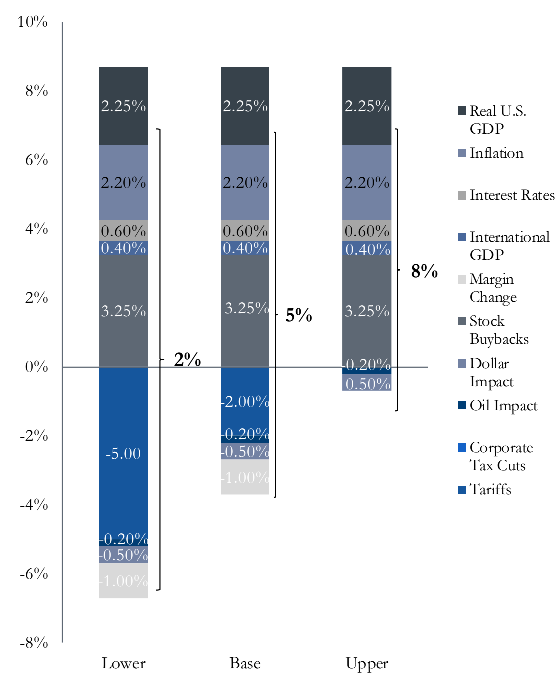
After undergoing a "healthy correction" in December, we believe U.S. equity markets are undergoing a multi-month corrective process driven by trade tensions, the path of Fed hikes, and the outlook for earnings. We have taken a conservative stance toward earnings growth in 2019 and have held a below consensus, base case forecast of 5%. **This earnings season is perhaps the most important one in years.**

Key things we are listening for to see if there is risk to our expectations include:

> **Any evidence of fundamental deterioration**. While economic activity is slowing both domestically and internationally, it is still growing. Revenue growth generally produces positive operating leverage, which should also be helped by lower input prices as many commodity prices have declined. Rising interest rates are also a modest positive as the balance sheet of the S&P 500 has more cash than debt. Increased labor costs are a potential headwind to margins. Corporation cash flows should remain solid. Net, we believe reported results will be choppy, but overall fine.
>
> **The tone and specifics of forward guidance from companies.** Results of the positive stimulus of tax cuts are beginning to fade, and concerns over the implications of trade tensions, Brexit, and Fed policy are impacting business decisions as evident by declining PMIs and declining global trade. Given this backdrop managements are likely to be cautiously optimistic and conservative in their commentary about the future. As a result the bottom-up earnings forecasts for many companies, which have been declining rapidly, could be reduced further, and our current base case assumption may have to be trimmed.

We have specific expectations for each of our holdings as it relates to revenues, earnings, and guidance. Should there be meaningful changes to our assumptions or our investment thesis, we will take appropriate action and maintain a solid pipeline of investment ideas. **We believe our focus on high-quality companies with solid earnings visibility will serve us well** as the Battle Royale continues.

2019 City National Rochdale Estimate Scenarios
S&P 500 Earnings Growth



Source: City National Rochdale estimates as of 1/2019.

- This earnings season may be the most important one in years
- We are listening for any evidence of fundamental deterioration
- Our focus on high-quality companies should serve us well

Conditions Favor Better Fixed Income Returns in 2019

By Gregory S. Kaplan, CFA

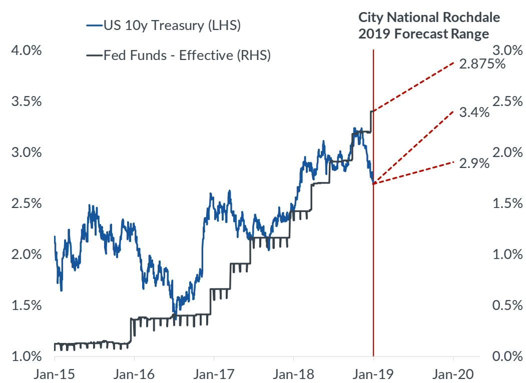
Fixed income returns were challenged in 2018 as rates rose in response to a combination of central bank tightening and strong economic growth spurred by fiscal stimulus. The bellwether 10-year Treasury yield began the year around 2.4%, peaked at 3.24%, and finished below 2.7% (see first chart). After tightening initially, credit spreads widened steadily after February on growth concerns, political turmoil, and monetary tightening. A less accommodative Federal Reserve raised rates four times and reduced its balance sheet by over $300 billion. While a headwind to longer rates, a tighter stance rewarded our liquidity management strategies as cash returned over 1.5%, and the curve flattened, playing into our core strategy of upgrading credit exposure, owning floating rate securities and taxable municipals, and establishing a maturity barbell.

With recession risk low in 2019 but deceleration in both U.S. and global economic growth already in motion, our previously unpopular call of a Fed pause in 2019 has become the consensus. This and softening inflation suggests that fixed income returns in 2019 should improve. **We expect longer rates to be range-bound, no more than two additional Fed hikes, and further credit volatility.** Security and sector selection will be increasingly important as manufacturing decelerates, volatility in the energy sector persists, and public pensions come under increasing scrutiny.

Fourth quarter volatility in risk assets improved valuations and made us more constructive on specific opportunities such as senior bank loans and their collateralized loan obligation (CLO) cousins. Domestic high yield, while cheaper, has not yet reached an entry point (see second chart). We also see value in specific maturities and issuers within the diverse emerging market debt space, including local currency exposure. These opportunities will likely lead fixed income returns in 2019 and serve as a valuable diversifier to other risk assets.

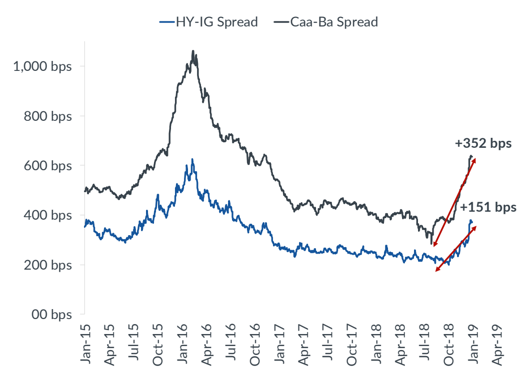
Overall we see a better year for fixed income, led by select opportunities and short-term liquidity management. Risks to our outlook include the pace of global economic deceleration, central bank surprises, and the political environment.

10-Year Treasury Yield and Fed Funds Rate



Source: Bloomberg as of 12/31/2018.

U.S HY-IG Corporate Spread and Caa-Ba Corporate Spread



Source: Bloomberg as of 12/31/2018.

- Muted but positive U.S. and global growth improves 2019 outlook
- Volatility has created opportunities in certain sectors
- Pause by Fed, mild inflation would aid fixed income returns

Dividend Growth Chugs Along Despite Market Jitters

By David J. Abella, CFA

Most major market indexes were negative for 2018 in a year marked by increased volatility, especially in the fourth quarter. Despite this, the stocks in City National Rochdale's High Dividend Income strategy continued their healthy performance. **Based on equity prices, one might expect slowing dividend growth rates or even dividend cuts, but operationally this was not at all the case for the companies in our portfolios.**

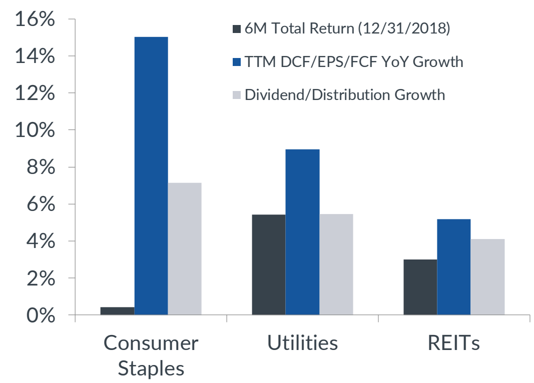
Looking more closely at our stocks in the Consumer Staple, Utility, and REIT sectors—all three being major dividend producing sectors—we see that the growth in free cash flow and in increased dividends exceeded the six-month total return in all of the sectors (see first chart). In other words, given market conditions, our stocks in three key income sectors accrued value as their yields and dividend growth increased more than their stock prices. In our view, this accrued valuation makes our names more compelling for investors looking for attractive yields that can rise with economic growth.

We believe it's important to focus on the growth rate of dividends, especially during choppy equity markets. As the U.S. economy continues to modestly advance, **the companies we hold have been able to increase their dividends near the higher end of our preferred range of 4-8%. Moreover, analysts currently project annual earnings growth of 9.5% for our stocks over the next two years** (see second chart). These cash flow streams enable us to project one-year forward returns of 6-8% for our holdings. While markets can be volatile, we have very high confidence in our estimates of aggregate yield and the growth of our companies' cash flows.

Our view is that **strong cash flows, coupled with solid growth rates, should help drive the attractive total returns the City National Rochdale High Dividend Income strategy has achieved in the past, especially given accrued values.** The key is identifying undervalued, high-quality companies with solid prospects for future dividend growth under most conceivable economic environments.

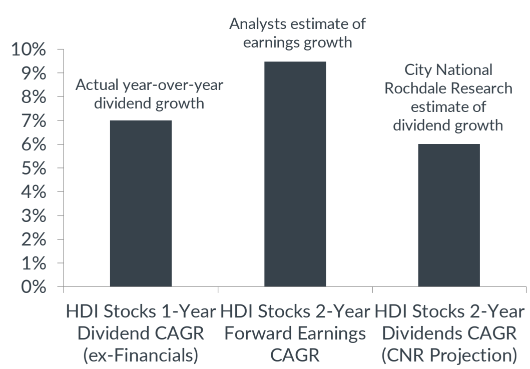
- Volatility can obscure strong company performance
- Earnings growth supports rising dividend yields
- Selectivity is key in identifying dividend growers

Growth Returns by Sector



Source: FactSet as of 12/31/2018.

Focus on Dividend and Earnings Growth



Companies that make up the universe of holdings in our D&I strategy grew their dividends, on average, 7.0% in the past year.

In addition, our companies have a projected growth in earnings of 9.5% and in dividends of 6% over the next two years.

Source: FactSet (based on published analyst estimates), based on City National Rochdale HDI strategy universe of stocks, as of 12/31/2018.

The projected growth rate in earnings is the aggregate average of all the published sellside analysts as reported through FactSet.

The projected dividend growth rate is the median of our projected range of 4-8%

Global Economic Outlook: Slowing, but Still Growing

By Steven Denike

The high-water mark for economic growth is probably behind us. The synchronized global expansion that began roughly two years ago has peaked, giving way to slower and more divergent GDP among the world's economies. **Evidence is mounting that the global expansion has entered the later stage of the business cycle, where growth slows, inflation picks up, interest rates rise, and asset returns become more volatile.** Still, gathering talk of recession appears premature.

U.S. economic momentum remains strong. Though we expect domestic GDP to slow gradually back to trend over the next year as financial conditions tighten and the impact of fiscal stimulus fades, healthy household balance sheets, robust job gains, and high confidence all remain important near-term tailwinds.

Policy mistakes on trade and interest rates are the major risks to the outlook. Uncertainty surrounding trade is weighing on overall economic activity and particularly on business investment, reducing some of the key expected benefits of corporate tax reform. Nevertheless, **the impact of trade disputes by themselves on the U.S. economy should be manageable, given the strength in underlying fundamentals.**

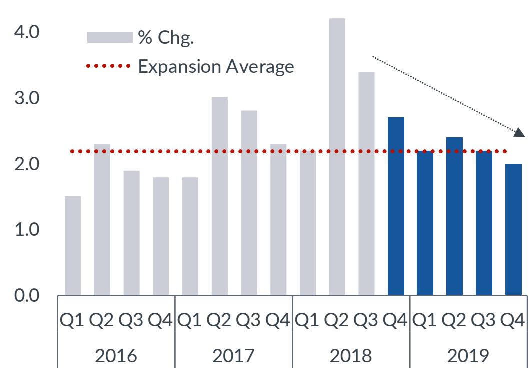
Far more important is the interest rate backdrop. Interest rates remain low by historical standards, but higher borrowing costs are already affecting rate-sensitive industries such as housing and automobiles. Importantly, **after five consecutive quarterly hikes, the Fed has signaled that it is mindful of the risks of overtightening.**

Overseas, there is even less appetite for tighter monetary policy. The ECB's bond buying program has ended but the Euro economy remains sluggish, with inflation still well below target. Uncertainty over Brexit negotiations has halted rate hikes by The Bank of England. Meanwhile, faced with structural strains in Japan and slowing GDP in China, Asian central bankers seem likely to keep policy loose.

Recent nervousness about the sustainability of growth is understandable—no expansion lasts forever. **Although the U.S. expansion is set to enter uncharted territory by becoming the longest on record this July, it is aging gracefully.** We still see few signs of overheating in sectors of the economy that have heralded some recessions in the past, or the credit excesses that have preceded others. Indeed, there's no reason late-cycle environments can't last a long time if major policy mistakes are avoided.

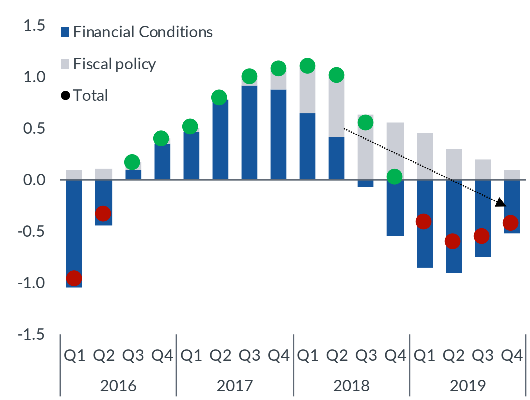
- Lengthy U.S. economic growth can continue
- Key risks are interest rate, trade policy errors
- Fears of recession in near future are unfounded

U.S. Real GDP Growth



Source: Bureau of Economic Analysis. Blue Chip Economic Forecasts as of 1/2019.

Percent Impact on Real U.S. GDP Growth



Source: Bureau of Economic Analysis. Blue Chip Economic Forecasts as of 1/2019.

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.

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

Important Information

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 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. 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.

Concentrating assets in the real estate sector or REITs may disproportionately subject a portfolio to the risks of that industry, including the loss of value because of adverse developments affecting the real estate industry and real property values. Investments in REITs may be subject to increased price volatility and liquidity risk; concentration risk is high.

Investments in Master Limited Partnerships (MLP) are susceptible to concentration risk, illiquidity, exposure to potential volatility, tax reporting complexity, fiscal policy, and market risk. Investors in MLPs are subject to increased tax reporting requirements. MLP investors typically receive a complicated schedule K-1 form rather than Form 1099. MLPs may not be appropriate investments for tax-advantaged accounts because of potential negative tax consequences (Unrelated Business Income Tax).

There are inherent risks with fixed-income investing. These risks may include interest rate, call, credit, market, inflation, government policy, liquidity, or junk bond. 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. 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 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.

Investments in emerging market 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. Emerging market bonds can have greater custodial and operational risks and less developed legal and accounting systems than developed markets.

As with any investment strategy, there is no guarantee that investment objectives will be met, and investors may lose money. Returns include the reinvestment of interest and dividends. Investing involves risk, including the loss of principal. Diversification may not protect against market loss or risk. Past performance is no guarantee of future performance.