City National Bank

Private Banking & Wealth Management

Economic and Market Overview

Second Quarter 2026

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Update: Geopolitical Events / Military Actions

The first half of the second quarter continued to be dominated by the conflict involving Iran. The disruption of trade through the Strait of Hormuz and concerns regarding global energy supplies initially drove oil prices sharply higher and increased market volatility. However, by late Q2, signs of a tentative ceasefire and progress toward reopening shipping routes significantly reduced investor anxiety. Markets ultimately shifted their focus away from geopolitical events and back toward economic fundamentals, corporate earnings, and artificial intelligence-related investment themes. Energy prices declined drastically from their peak levels, improving both inflation and growth expectations. However, as energy costs retreated, sentiment regarding AI spending's contribution to inflation began to grow. While geopolitical risks remain elevated, the quarter demonstrated that markets often recover quickly once uncertainty begins to diminish.

Economic and Market Overview

Second Quarter 2026

The US Economy

The U.S. economy regained momentum during the second quarter. After growing only 0.5% in Q4 2025, first-quarter 2026 GDP expanded at an annualized 2.1%, supported by resilient consumer spending, AI-related business investment, and continued labor market strength. Nonfarm payrolls increased by 172,000 in May following a gain of 179,000 in April, while unemployment remained stable at 4.3%. Inflation, however, moved higher during the quarter. The Personal Consumption Expenditure (PCE) Price Index increased 3.8% year-over-year in April while Core PCE rose 3.3%. Elevated energy prices tied to Middle East tensions contributed significantly to the acceleration in inflation and complicated the Federal Reserve's policy outlook.

The Federal Reserve maintained the federal funds target range at 3.50%-3.75%. New Federal reserve Chair Kevin Warsh made his first appearance this quarter, naming inflation as his number one priority, signaling the possibility of rate hikes later in the year.

Economic and Market Overview

Second Quarter 2026

U.S. Economic Conditions and Policy Outlooks

GROSS DOMESTIC PRODUCT (GDP)

Economic activity improved meaningfully during Q2. Consumer spending remained the largest driver of growth, supported by a stable labor market and continued income gains. Corporate profitability remained strong, aided by productivity improvements and significant investment in artificial intelligence infrastructure and semiconductor capacity. The first-quarter GDP growth rate of 2.1% represented a notable rebound from the slowdown experienced in late 2025. While inflation remains elevated, **underlying economic conditions continue to support moderate expansion**.

HOUSING

Existing home sales increased 3.2% during May to a seasonally adjusted annual rate of 4.17 million units. Home prices continued rising, with the median existing-home price reaching $429,300. Inventory increased to approximately 4.5 months of supply. Builder sentiment can best be described as cautious. The NAHB Housing Market Index declined to 35 in June, reflecting ongoing affordability concerns, elevated mortgage rates, high construction costs, and weaker buyer traffic.

U.S. Economic Conditions and Policy Outlooks

EMPLOYMENT

The labor market remained resilient throughout the quarter. Payroll growth averaged approximately 175,000 jobs per month during April and May. The unemployment rate remained steady at 4.3%, while labor force participation held near 61.8%. Wage growth continued but moderated slightly, with average hourly earnings growing 3.4% year-over-year.

Employment gains were concentrated in healthcare, leisure and hospitality, government, and social assistance sectors. Despite weakness in portions of financial services, **overall labor market conditions remain consistent with continued economic growth**.

FEDERAL RESERVE POLICY

The Federal Reserve maintained the federal funds rate at 3.50% - 3.75% during the June meeting.

The most significant change during Q2 was the shift in Fed messaging under new Chair Kevin Warsh. Policymakers sharply increased their inflation projections for 2026, raising expected PCE inflation from 2.7% to 3.6%. Unlike earlier expectations for rate cuts, the Committee now projects policy rates ending 2026 closer to 3.8%, implying that tightening may be a possibility.

The Fed's focus has clearly shifted toward restoring price stability, making inflation the primary policy focus entering the second half of 2026.

Asset Class Overview

US FIXED INCOME MARKETS

Fixed income markets faced pressure from higher inflation expectations and a more hawkish Federal Reserve. Treasury yields moved higher during most of the quarter, with the 10-year Treasury reaching as high as 4.67% before finishing June at approximately 4.47%, compared to 4.32% at the end of Q1.

Despite rising rates, fixed income returns across major sectors were positive due to attractive starting yields and resilient credit fundamentals.

Municipal bonds remain particularly attractive from a tax-equivalent yield perspective for higher-income investors.

Economic and Market Overview

Second Quarter 2026

The table below shows the total return for the full 2025 year, Q2/2026, and YTD 2026 across the US Fixed Income Market.

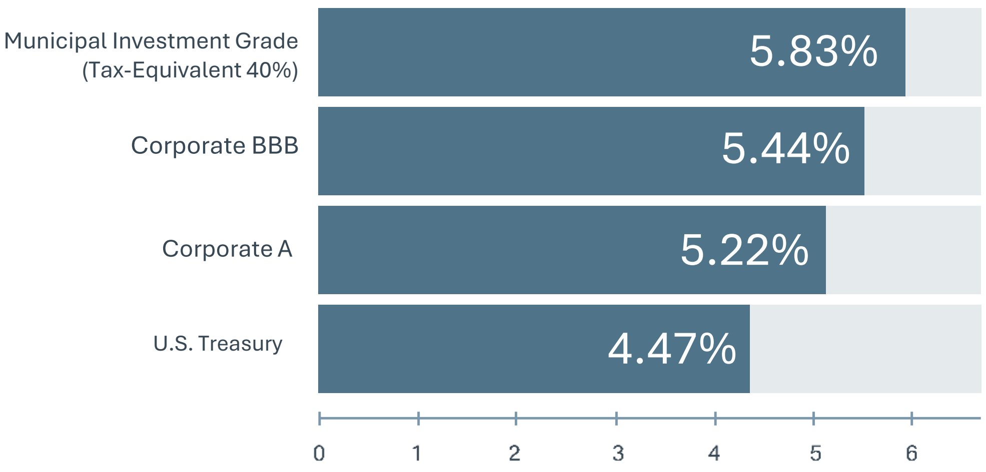
US Fixed Income Market	2025 Total Return	Q2 2026 Total Return	2026 YTD Total Return
US Aggregate Bond Index	7.1%	0.38%	0.28%
Bank Loans (Morningstar LSTA)	5.9%	2.19%	1.69%
High Yield Bonds (ICE BofA)	8.5%	2.02%	1.92%
Short Term Investment Grade Corp Bonds (ICE BofA)	5.7%	1.15%	1.15%
Intermediate Investment Grade Corporate Bonds (Bloomberg)	7.2%	0.32%	0.42%
Short Duration Municipal Bonds (S&P)	3.7%	0.9%	1.07%
Intermediate Duration Municipal Bond (S&P)	4.2%	0.11%	0.51%

2Q 2026 returns reflect total return in U.S. dollars from January 1 through July 9, 2026. S&P Dow Jones Indices, FTSE Russell, Bloomberg, FactSet. Index performance is shown for illustrative purposes only and does not represent the performance of any specific investment.

The table below shows the current yields across taxable and municipal investment grade bonds, with 10-year maturities. We again note the compelling tax equivalent yield of intermediate investment grade municipal bonds.

10- Year Yield Comparison

(Tax Equivalent Basis, 40% Federal Tax rate)



10-Year U.S. Treasury Yield, Source: Envestnet — 10-Year Corporate A Yield, Source: ICE BofA US Corporate Index Effective Yield — Municipal Tax-Equivalent Yield, Source: FMS Bonds Municipal Market Yield — 10-Year Corporate BBB, Source: ICE BofA BBB US Corporate Index Effective Yield

Economic and Market Overview

Second Quarter 2026

US Equity Markets

U.S. equities delivered an exceptionally strong recovery during Q2. Corporate earnings continued to exceed expectations, with 84% of S&P 500 companies reporting earnings above consensus forecasts. Artificial intelligence-related investment spending emerged as the dominant market theme, driving powerful gains in technology and semiconductor companies.

Index	2025 Total Return	Q2 2026 Total Return	2026 YTD Total Return
S&P 500	17.4%	14.5%	10.2%
NASDAQ (Composite)	20.2%	12.76%	21.86%
Russell 1000 Growth Total Return Index	18.5%	10.55%	4.55%
Russell 1000 Value Total Return Index	15.9%	22.01%	18.11%
Dow Jones Industrial Average total return Index	14.9%	14.1%	9.2%
Rusell 2000 Total Return Index	12.8%	20.4%	21.3%
S&P Small Cap	6.02%	14.62%	19.11%

US Equity Markets

HISTORIC EARNINGS GROWTH CONTINUES

Corporate earnings have remained a key driver of market performance, supported by the continued strength of many of the largest companies in the U.S. While technology leaders such as NVIDIA, Microsoft, Amazon, and Meta have delivered exceptional growth in recent years, earnings momentum has increasingly broadened across the wider market. Overall, the outlook suggests that the historic earnings growth achieved by U.S. companies in recent years is expected to continue, providing a strong foundation for future corporate profitability and market performance.

Index	2024 Earnings Growth	2025 Earnings Growth	2026 Q1 Expected Earnings Growth	2026 Q1 Actual Earnings Growth	2026 Projected Earnings Growth
S&P 493	4%	10%	10%	17.4% **(best since Q4, 2021)**	17.9%
MAG 7	40%	22%	22.5%	63.2% **(highest since Q2 2021, all 7 beat estimates)**	34.9%

International Equity Markets

International equities continued to show strength through the second quarter after a very strong 2025. The performance of major international equity market indices can be seen in the table below.

Index	2025 Total Return	Q2 2026 Total Return	2026 YTD Total Return
MSCU ACWI ex US Total Return Index	32.6%	14.06%	12.86%
MSCI World Index	21.6%	11.94%	10.30%
MSCI Emerging Markets Total Return Index	34.0%	20.72%	20.62%
MSCI EMU Total Return Index (Eurozone)	18.9%	12.79%	8.59%
MSCI AC Asia ex Japan Total Return Index	31.5%	22.03%	22.73%
MSCI EM Latin America Total Return Index	52.3%	-3.33%	11.37%

Alternative Investments

Alternative investments produced mixed results during the second quarter as investors navigated shifting inflation expectations, declining energy prices, and changing geopolitical conditions. Commodities faced headwinds as oil prices reversed sharply lower following signs of a resolution to Middle East supply disruptions. Publicly traded real estate generated strong positive returns, supported by resilient economic growth, healthy corporate fundamentals, and continued investor demand for income-producing assets.

Alternative	2025 Total Return	Q2 2026 Total Return	2026 YTD Total Return
Bloomberg Commodity Index Total Return (BCOMTR)	15.7%	-8.1%	14.36%
S&P GSCI Gold Total Return Index	62.5%	-13.3%	-5.5%
FTSE Nareit All Equity REITs Total Return Index	2.3%	9.42%	13.22%

Economic and Market Overview

Second Quarter 2026

AI Continues to Fuel Growth, but Inflation Remains a Challenge

Semiconductor demand, resilient economic activity, and higher input costs may keep Federal Reserve policy restrictive despite continued earnings growth

Buildout of artificial intelligence infrastructure has triggered a sharp increase in demand for advanced semiconductors, particularly the high-performance chips required for data centers and cloud computing. These higher costs are likely to filter through the broader technology ecosystem over time. Consumer products such as laptops, smartphones, tablets, and other connected devices rely on many of the same supply chains and core manufacturing resources, sustained demand will contribute to higher hardware costs for consumers.

Newly appointed Federal Reserve Chair **Kevin Warsh** adopted a notably hawkish tone, emphasizing that returning inflation to the Fed's 2% target is the Committee's highest priority. While the Federal Reserve kept the federal funds rate unchanged at 3.50%–3.75%, updated projections now suggest policymakers are willing to keep rates for longer.

In effect, the AI investment boom that is supporting economic growth and corporate earnings may also become another source of persistent inflation, reinforcing the Federal Reserve’s and Chair Kevin Warsh's commitment to maintaining a restrictive policy stance until price pressure eases.

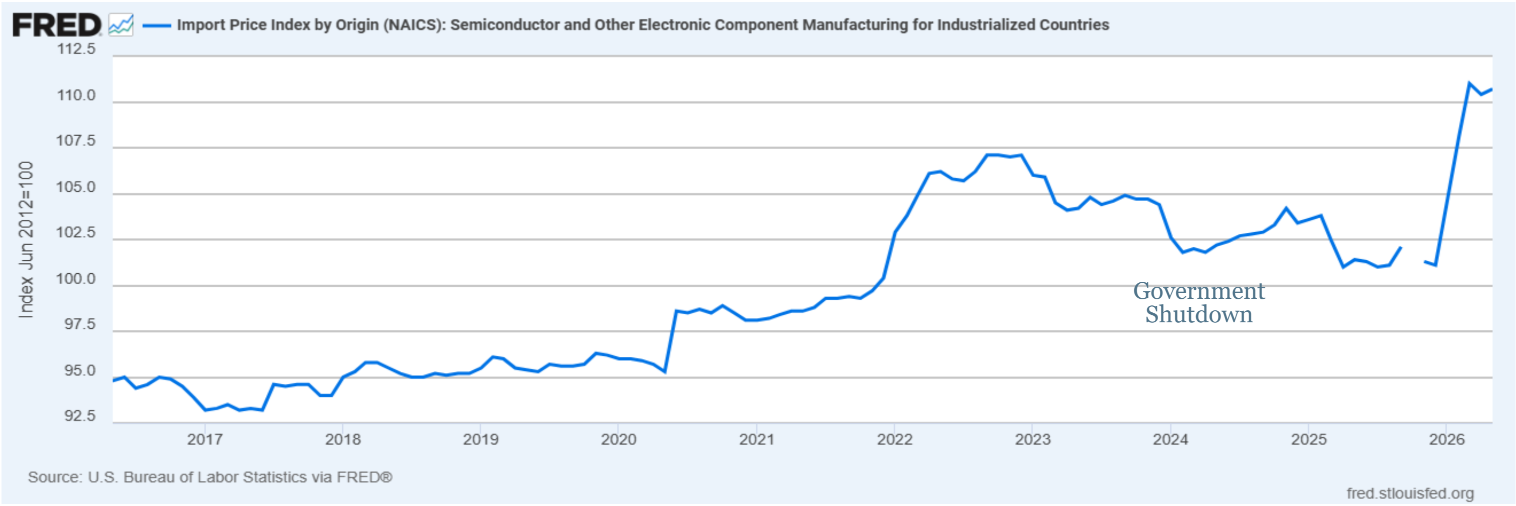


Chart measures changes in U.S. import prices for semiconductors and electronic components sourced from industrialized countries

Our Investment Positioning for 2026

FIXED INCOME, we continue to favor intermediate-duration exposures and high-quality corporate credit. Despite a more hawkish Federal Reserve and higher inflation expectations during the quarter, yields remain attractive from both an income and total return perspective.

MUNICIPAL FIXED INCOME, our highest conviction remains investment-grade municipal bonds. Tax-equivalent yields remain highly attractive for investors in higher tax brackets and continue to compare favorably with many investment-grade taxable alternatives.

ALTERNATIVE INVESTMENTS, gold and publicly traded real estate remain holdings within our alternative allocations. While gold experienced some volatility during the quarter, real estate continues to perform consistently.

U.S. EQUITY, we maintain a constructive view on U.S. equities, supported by resilient economic growth, strong corporate earnings, and continued investment in artificial intelligence infrastructure. While mega-cap technology remains an important component of equity allocations, we increasingly favor broader market participation including small- and mid-cap companies, which demonstrated improving performance during the second quarter.

INTERNATIONAL EQUITY, we maintain a modest overweight allocation to international equities. International, developed, and emerging markets delivered strong returns during the second quarter and continue to offer attractive diversification benefits and valuation opportunities. Developed international markets remain our preference, while selective emerging market exposure may benefit from improving global growth trends and technology-related investment themes.

Risks are Ever Present

It is rarely possible to predict the outcome of geopolitical events, inflationary pressures, or monetary policy decisions. The current environment is one where economic growth has remained resilient, but inflation, Federal Reserve policy, and geopolitical developments continue to create uncertainty.
We know risks are ever present and we manage through those risks dynamically, using all our extensive capabilities.

Our portfolios are customized to each one of our clients' individual goals and objectives. Levels of liquidity have been defined as part of the investment guidelines which we manage to. For many, diversified portfolios with an emphasis on quality, balanced and growth exposure, and disciplined rebalancing amid ongoing market uncertainty will prove to be resilient

We hope that the information provided in this document is of value and provides context. Should you wish to have a deeper conversation, we look forward to meeting with you.

Important Disclosures

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Not FDIC	Not Insured by Any Federal Government Agency	Not Deposits
Not Bank Guaranteed	Subject to Investment Risk	May Lose Value

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INDEX OVERVIEW

The **Dow or DJIA** (Dow Jones Industrial Average) is an unmanaged index of 30 common stocks comprising 30 actively traded blue chip stocks, primarily industrials, and assumes reinvestment of dividends. The **NASDAQ Composite** is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market. The **S&P 500 Index** is an unmanaged index comprising 500 widely held securities considered to be representative of the stock market in general. The **DJ US Select REIT Index** is a subset of the Dow Jones Americas Select RESI and includes only REITs and REIT-like securities (The Dow Jones US Select Real Estate Securities Index (RESI) represents equity real estate investment trusts (REITs) and real estate operating companies (REOCs) traded in the US). The **Bloomberg Commodity Index** is a broadly diversified commodity price index that tracks prices of futures contracts on physical commodities on the commodity market and is designed to minimize concentration in any one commodity or sector. The **MSCI EAFE Index** is recognized as the preeminent benchmark in the US to measure international equity performance. It comprises the MSCI country indices that represent developed markets outside of North America: Europe, Australasia, and the Far East.

The **MSCI Emerging Markets Index** is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. The **MSCI ACWI Index** is a free float adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets. The MSCI ACWI consists of 46 country indices comprising 23 developed and 23 emerging markets country indices. The **MSCI Emerging Markets** (EM) Eastern Europe Index captures large and mid cap representation across four emerging markets (the Czech Republic, Hungary, Poland, and Russia) countries in Eastern Europe. With 52 constituents, the Index covers approximately 85% of the free float-adjusted market capitalization in each country. The **MSCI EM** (Emerging Markets) Latin America Index is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of emerging markets in Latin America. The **MSCI ACWI Ex-US Index** is a market-capitalization weighted index maintained by Morgan Stanley Capital International (MSCI) and designed to provide a broad measure of stock performance throughout the world, with the exception of US-based companies. The **MSCI China Index** captures large and mid cap representation across China H shares, B shares, Red chips, and P chips covering about 85% of this China equity universe. The **Bloomberg Municipal Bond Index** is an unmanaged index comprising investment-grade, fixed-rate municipal securities representative of the tax-exempt bond market in general. The **Bloomberg Global Aggregate ex-US Index** is a market-capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most US-traded investment-grade bonds are represented. Municipal bonds and Treasury Inflation-Protected Securities are excluded, due to tax treatment issues. The Index includes Treasury securities, government agency bonds, mortgage-backed bonds, corporate bonds, and a small amount of foreign bonds traded in the US.

Economic and Market Overview

Second Quarter 2026

The **Bloomberg US 5 10 Year Corporate Bond Index** investment return of US dollar measures the denominated, investment rate, taxable securities issued by industrial, utility, and financial companies, with maturities between 5 and 10 years. Treasury securities, mortgage grade, fixed backed securities (MBS), foreign bonds, government agency bonds, and corporate bonds are some of the categories included in the Index. The **Bloomberg US 5 7 Year Treasury Bond Index** is a market capitalization weighted index and includes Treasury bonds issued by the US with a time to maturity of at least 5 years, but no more than 7 years. The market capitalization **Russell 1000 Index** is a weighted benchmark index made up of the 1000 largest US companies in the Russell 3000 Index (which comprises the 3000 largest US companies). The **Russell 2000** Index is an unmanaged index considered representative of small cap stocks. The **Russell 3000** Index an unmanaged index considered to be representative of the US stock market and measures the performance of the largest 3,000 US companies representing approximately 98% of the investable US equity market. **The Russell Midcap Index** is a subset of the Russell 1000 Index. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership.

The monthly survey of The **Housing Market Index** (HMI) is based on a monthly survey of **NAHB** members designed to take the pulse of the single-family housing market. The survey asks respondents to rate market conditions for the sale of new homes at the present time and in the next six months, as well as the traffic of prospective buyers of new homes. Builders rate current sales, future sales expectations (next six months), and prospective buyer traffic. The HMI is a weighted average of these three components, with a score above 50 indicating a positive market outlook and below 50 indicating a negative one. Bond Index The **JPMorgan Emerging Market** (EMBI Global) tracks total returns for traded external debt instruments in the emerging markets and is an expanded version of the JPMorgan EMBI+. As with the EMBI+, the EMBI Global includes US dollar is denominated Brady bonds, loans, and Eurobonds with an outstanding face value of at least $500 million. The **CBOE Volatility Index** the (VIX) is an up to minute market estimate of expected volatility that is calculated by using real time S&P 500 Index option bid/ask quotes. The Index uses nearby and second nearby options with at least 8 days left to expiration and then weights them to yield a constant, 30 day measure of the expected volatility of the S&P 500 Index.

DEFINITIONS

The **Federal Open Market Committee** (FOMC) is the monetary policymaking body of the Federal Reserve System. The **federal funds rate** is the interest rate at which a depository institution lends funds maintained at the Federal Reserve to another depository institution overnight. The **European Central Bank** (ECB) is the central bank for Europe's single currency, the euro. The ECB's main task is to maintain the euro's purchasing power and thus price stability in the euro area. The euro area comprises the 19 European Union countries that have introduced the euro since 1999. The **Gross Domestic Product** (GDP) rate is a measurement of the output of goods and services produced by labor and property located in the United States. The **Bureau of Labor Statistics** (BLS) is a unit of the United States Department of Labor. It is the principal fact-finding agency for the U.S. government in the broad field of labor economics and statistics and serves as a principal agency of the U.S. Federal Statistical System. The **Bureau of Economic Analysis** (BEA) is an agency in the U.S. Department of Commerce that provides important economic statistics, including the gross domestic product of the United States.
It is a governmental statistical agency that collects, processes, analyzes, and disseminates essential statistical data to the American public, the U.S. Congress, other Federal agencies, state and local governments, business, and labor representatives. The **PCE** (Personal Consumption Expenditure) Index of Prices is a U.S.-wide indicator of the average increase in prices for all domestic personal consumption. Using a variety of data, including **U.S. Consumer Price Index** and Producer Price Index prices, it is derived from personal consumption expenditures and is essentially a measure of goods and services targeted toward and consumed by individuals.

Sector performance is represented by the **Global Industry Classification Standard** (GICS) sectors, developed by Standard & Poor's and MSCI Barra.
The **Consumer Price Index** (CPI) measures the monthly change in prices paid by U.S. consumers. The Bureau of Labor Statistics (BLS) calculates the CPI as a weighted average of prices for a basket of goods and services representative of aggregate U.S. consumer spending. The **Federal Funds** (fed funds) Rate refers to the interest rate that banks charge other institutions for lending excess cash to them from their reserve balances on an overnight basis.