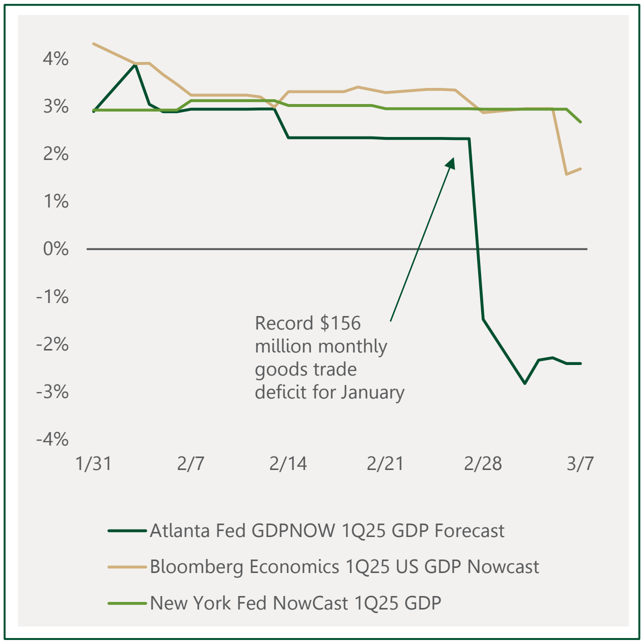
MARKET REVIEW
MARCH 2025

RCB BANK
Trust & Wealth Management

The Atlanta Fed's Projection is an Outlier
1Q25 U.S. GDP Real-Time Forecasts



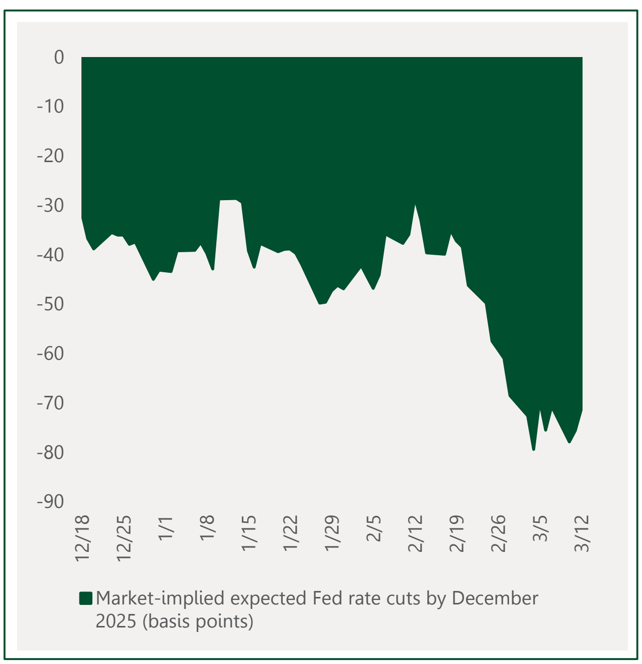
Source: Bloomberg. Past Performance does not guarantee future results.

In recent weeks, the Atlanta Fed GDP Nowcast, a widely known real time estimate of GDP growth for the current quarter, has significantly diverged from other estimates. The Atlanta Fed Nowcast now calls for real GDP to decline in the first quarter, but the driver of the divergence between estimates is a result of net exports.

Net exports, one of the four major components of GDP, represents the trade balance by subtracting total imports from exports. In January, the U.S. trade deficit widened to a record $156 billion, caused by a surge in imports. Due to differing statistical methodologies, the deficit widening had an outsized impact on the Atlanta estimate versus similar real-time growth projections from the New York Fed and Bloomberg.

The increase in the deficit during January appears to have been inflated by a surge in gold imports, a financial asset that does not impact production. The other three components of GDP are positively contributing to the Atlanta Fed GDP Nowcast. Thus, it is likely a temporary outlier that should stabilize upward in coming weeks as monthly import figures for February normalize.

The market now expects 0.75% of Fed cuts in 2025
Fed funds futures-implied policy cuts (basis points)



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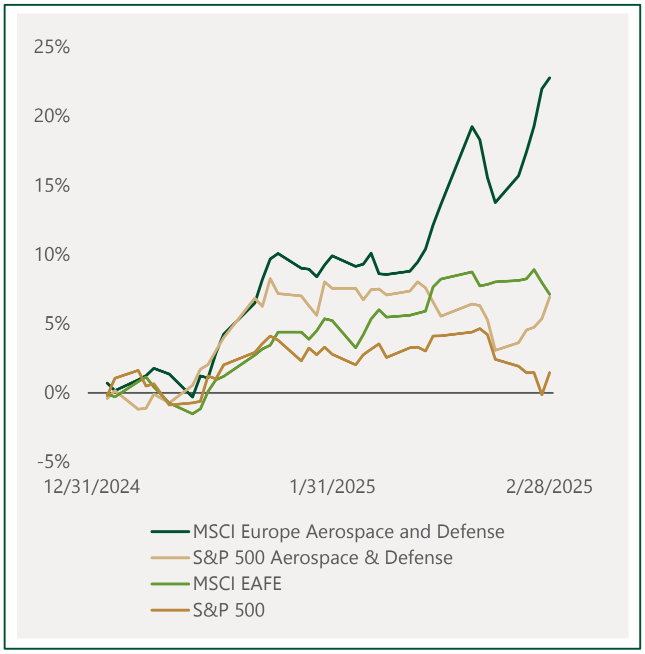
At the start of the year, the Federal Reserve was primarily concerned about stalled progress on inflation amid policy uncertainty and following 100 basis points (bps) of interest rate cuts in the prior four months. As a result, the market broadly expected the Federal Reserve to take a conservative approach to cutting interest rates throughout 2025. Only one 25-bp cut was fully priced by markets as recently as February 12.

In recent weeks, the market has been forced to reprice expectations, as concerns about economic growth have come into focus even as inflation has remained firm. Subsequently, the market is now pricing in about 75 bps of cuts by the end of 2025. This would take the policy rate to a range of 3.5%-3.75%.

A mix of inflationary fears and slowing growth puts the Fed in a difficult position. If the economy were to fall into a contraction, the central bank would likely move forward with significant rate cuts to help stimulate demand. Yet this could come at the risk of not getting inflation all the way back to 2%, especially if tariffs prove to be inflationary.

Europe Defense Stocks Outperform
Year To Date Return



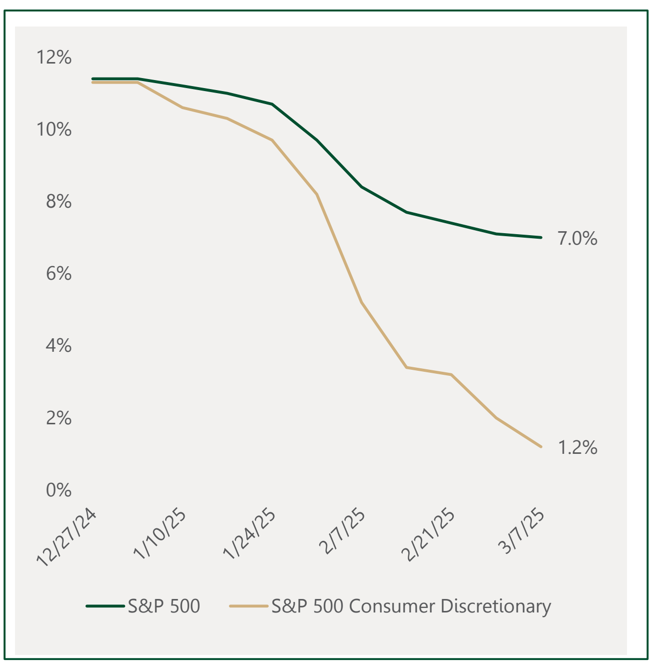
Source: Bloomberg. Past Performance does not guarantee future results.

The S&P 500 fell for the third time in the last five months. The index's 1.30% monthly decline in February was driven by softer economic data and concerns about inflation's persistence. Uncertainty surrounding President Trump's proposed tariffs also weighed on investor sentiment. Defensive and interest rate sensitive sectors outperformed with the consumer staples sector rising 5.70% and real estate sector up 4.22%.

After leading the stock market the last two calendar years, Magnificent 7 stocks have underperformed this year and are near correction territory since their peak on December 24th. The cohort fell 5.30% in February, led by double digit declines in Tesla TSLA (-27.59%), Alphabet GOOGL (-16.54%), and Amazon AMZN (-10.69%). Meta Platforms META was the only Mag 7 stock with a positive return in the first two months of this year (+14.12%).

European stocks outperformed the U.S. for a second consecutive month, led by European defense stocks which are among the best performers in the world this year. The MSCI Europe Aerospace and Defense index's over 20% gain this year was bolstered by European leader comments to increase defense spending amid growing uncertainty about U.S. support for Ukraine.

Consumer Discretionary Estimates Revised Lower
First Quarter Earnings Growth Forecast



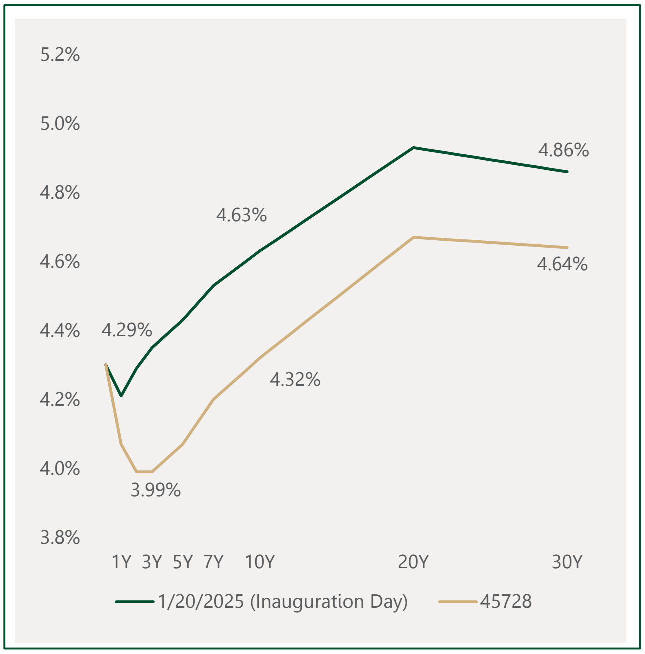
Source: Bloomberg. Past Performance does not guarantee future results.

The S&P 500's fourth quarter earnings were stronger than expected with 14.3% growth that almost doubled analysts' forecast for 7.3% growth. This was the index's strongest earnings growth since the fourth quarter of 2021. Excluding the Magnificent 7, earnings growth of 9.3% was nearly triple the 3.1% analyst estimate. Double digit earnings growth in the financials and health care sectors were the strongest areas outside the Magnificent 7 heavy sectors including technology, communications, and consumer discretionary sectors which posted earnings growth of 19.7%, 29.9%, and 24.8%, respectively.

Analysts project earnings growth deceleration to 7% and 8% in the first and second quarters of this year, respectively. Magnificent 7 earnings growth is forecasted to moderate to under 20% each quarter this year after growing 34% in 2024.

The decline in consumer sentiment and mounting tariffs have led to downward analyst revisions for the consumer discretionary sector's earnings. Analysts project a meager 1.2% first quarter earnings growth for the sector, down from 11% forecast at the start of the year. The sector is projected to have a modest 3% earnings growth in the first half of the year and 6% decline when excluding Amazon (AMZN) and Tesla (TSLA).

Yields Move Lower in Trump's First 50 Days
U.S. Treasury Yield Curve: 1/20 vs. 3/12



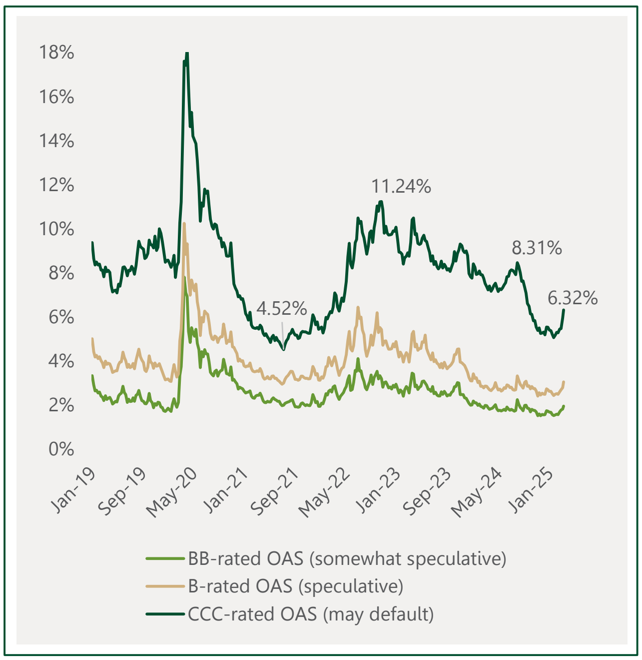
Source: Bloomberg. Past Performance does not guarantee future results.

After reaching a 13-month closing high of 4.79% on January 14, yields on the 10-year U.S. Treasury note moved briskly lower over the next two months and registered a year-to-date low of 4.15% on March 3 (the day before the original March 4 deadline for U.S. tariffs on Canada and Mexico).

The 2-year Treasury note yield (widely viewed as a proxy for the Fed's expected policy rate in 12-24 months) sank below 4% in the first week of March for the first time since mid-October. If the messaging from Fed officials becomes dovish in coming weeks, we would expect the 2-year yield to dip toward 3.5%.

The move lower in yields has come as bond market participants have reset their expectations for growth, inflation, government spending, and the Trump administration's fluid trade policy. For several days in the first week of March, the entire yield curve became inverted again with the upper bound of the fed funds rate (4.5%) eclipsing the 30-year Treasury bond yield. A string of weak business activity readings from various regional Federal Reserve Bank and purchasing managers surveys have dampened 1Q25 U.S. growth expectations.

No Signs of Major Credit Market Stress
U.S. High Yield Option-Adjusted Credit Spreads



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Credit markets have reacted in a more muted fashion to the current policy uncertainty than what we have seen in the U.S. equity market. Yield premiums on a Bloomberg index of highly speculative CCC-rated corporate bonds have widened to about 6.3% in the second week of March from a three-year low near 5.1% in late January.

These spread levels are about 100 basis points lower than a year ago and well below the average weekly credit spread of 8.7% for the CCC-rated index from March 2022 (the beginning of the Fed's last rate hike cycle) to August 2024 (last summer's growth scare).

Corporate issuers have generally enjoyed strong demand for their new debt over the last 12 months as investors remain comfortable with trends in earnings growth, leverage, and interest coverage. The demand for below-investment grade issues could face a test in the second half of 2025 and early 2026 due to a wave of 5-year term refinancings from debt originally issued at historically favorable terms in 2021.