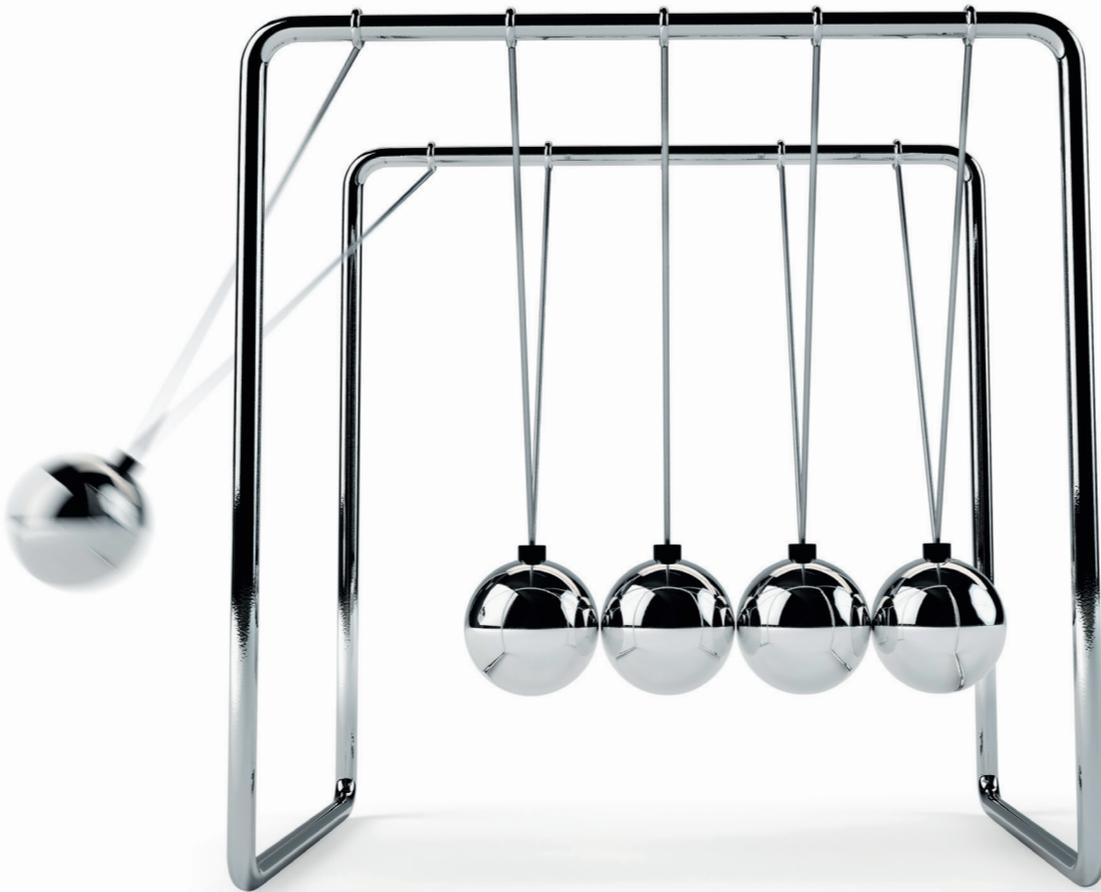


TRADE-OFF

2018 Global Market Outlook – Q4 update



Synopsis

Trade wars, the U.S. Federal Reserve (the Fed), China stimulus and the direction of the U.S. dollar dominate our near-term outlook. At this juncture, U.S. recession risks appear low. We believe that European growth can improve over the next couple of quarters. We view emerging markets as oversold, but see a bounce as dependent on the next move in the ongoing trade wars between the U.S. and other countries.

Key market themes

The S&P 500® Index has been the best performing regional equity market this year, but U.S. equities remain very expensive, with a Shiller cyclically adjusted price-to-earnings ratio of 33 times as of mid-September. While we see momentum as continuing to favor U.S. equities, some of our contrarian over-bought indicators are beginning to trigger. In addition, a December Fed funds rate hike looks likely, as do three or four more hikes in 2019, which would take the rate to 3.3%. A shift to a more aggressive outlook would put upward pressure on the U.S. dollar and Treasury yields. It also would add to the stresses in emerging markets.

We like the idea of leaning into eurozone equity exposure after its recent underperformance. In particular, Italian risk looks to be dissipating, corporate earnings are still robust and the industry consensus has become too pessimistic about the economic outlook. Trade-war risk, however, tempers our enthusiasm for this region as a whole.

UK equities continue to look slightly cheap on our scorecard. At 1.5%, 10-year gilts are still long-term expensive.

However, given the near 20 basis-point rally in yields we've seen over the third quarter, we no longer classify government bonds as very expensive—just expensive.

One of the top stories in Asia Pacific has been Australian growth, which has been impressive so far in 2018. However, we believe that this economy may have seen a peak in growth for the next couple of years, as the headwind of falling housing prices continues to grow and uncertainty around the strength of the Australian consumer remains. Meanwhile, in New Zealand, our outlook for the country is deteriorating as uncertainties around government policy are likely to slow the economy and damage business confidence.

Canadian valuations continue to improve, but we see them as more attractive on a relative basis, especially compared to U.S. equities. We are generally neutral in absolute terms, but remain modestly positive toward Canadian equities relative to the U.S.

Economic indicators

- Corporate earnings growth in the U.S. has exceeded industry analysts' expectations and, according to International Monetary Fund (IMF) estimates, fiscal stimulus is adding 0.7% to GDP growth this year and will add 0.8% in 2019.
- We believe the hurdle for U.S. earnings to surprise on the upside is now very high. The impact of corporate tax cuts on earnings will soon disappear, and both borrowing costs and wages are headed higher. A slowdown in earnings growth will take away one of the main supports for U.S. outperformance relative to other markets.
- We view China stimulus as more likely to resemble *stepping off the brake* than *pushing on the accelerator*, as President Xi Jinping focuses on deleveraging and structural reform while balancing the need for policy stimulus to counteract the impact of U.S. tariffs.
- We see an escalation in trade wars between the U.S. and other nations as a threat to emerging markets and global trade.

Asset class views

Equities: Broadly neutral

We're neutral global equities for now, with a small preference for non-U.S. markets. The pessimism on eurozone equities looks overdone. We're waiting for more clarity on trade wars, the Fed and China stimulus before leaning into oversold emerging markets.

Fixed income: Reasonable value at 3% in the U.S.

Ten-year U.S. Treasury yields near 3% offer reasonable value amid the current uncertainty. Over the medium term, however, the cycle forces of inflation pressures and central bank tightening look to put global government bond markets under pressure.

Currencies: Japanese yen undervalued

We like the defensive qualities of Japanese yen exposure. It's 20% undervalued relative to purchasing power parity, is getting cycle support at the margin as the Bank of Japan moves less dovish and has solid sentiment support from sizeable net short positions. The added benefit, in our view, is that it also performs well as a safe haven. We see it as a defensive diversifier on portfolio construction grounds.

We also see more upward pressure on the U.S. dollar in 2019, as we think the risks are shifting toward a slightly more aggressive Fed than the market is pricing.

Please visit russellinvestments.com to read the complete 2018 Global Market Outlook – Q4 update.



IMPORTANT INFORMATION

The views in this Global Market Outlook report are subject to change at any time based upon market or other conditions and are current as of September 21, 2018. While all material is deemed to be reliable, accuracy and completeness cannot be guaranteed.

Please remember that all investments carry some level of risk, including the potential loss of principal invested. They do not typically grow at an even rate of return and may experience negative growth. As with any type of portfolio structuring, attempting to reduce risk and increase return could, at certain times, unintentionally reduce returns.

Keep in mind that, like all investing, multi-asset investing does not assure a profit or protect against loss.

No model or group of models can offer a precise estimate of future returns available from capital markets. We remain cautious that rational analytical techniques cannot predict extremes in financial behavior, such as periods of financial euphoria or investor panic. Our models rest on the assumptions of normal and rational financial behavior. Forecasting models are inherently uncertain, subject to change at any time based on a variety of factors and can be inaccurate. Russell believes that the utility of this information is highest in evaluating the relative relationships of various components of a globally diversified portfolio. As such, the models may offer insights into the prudence of over or under weighting those components from time to time or under periods of extreme dislocation. The models are explicitly not intended as market timing signals.

Forecasting represents predictions of market prices and/or volume patterns utilizing varying analytical data. It is not representative of a projection of the stock market, or of any specific investment.

Investment in global, international or emerging

markets may be significantly affected by political or economic conditions and regulatory requirements in a particular country. Investments in non-U.S. markets can involve risks of currency fluctuation, political and economic instability, different accounting standards and foreign taxation. Such securities may be less liquid and more volatile. Investments in emerging or developing markets involve exposure to economic structures that are generally less diverse and mature, and political systems with less stability than in more developed countries.

Currency investing involves risks including fluctuations in currency values, whether the home currency or the foreign currency. They can either enhance or reduce the returns associated with foreign investments.

Investments in non-U.S. markets can involve risks of currency fluctuation, political and economic instability, different accounting standards and foreign taxation.

Bond investors should carefully consider risks such as interest rate, credit, default and duration risks. Greater risk, such as increased volatility, limited liquidity, prepayment, non-payment and increased default risk, is inherent in portfolios that invest in high yield ("junk") bonds or mortgage-backed securities, especially mortgage-backed securities with exposure to sub-prime mortgages. Generally, when interest rates rise, prices of fixed income securities fall. Interest rates in the United States are at, or near, historic lows, which may increase a Fund's exposure to risks associated with rising rates. Investment in non-U.S. and emerging market securities is subject to the risk of currency fluctuations and to economic and political risks associated with such foreign countries.

The S&P 500, or the Standard & Poor's 500, is a stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ.

Performance quoted represents past performance

and should not be viewed as a guarantee of future results.

Indexes are unmanaged and cannot be invested in directly.

Yale Professor Robert Shiller calculates a Cyclically Adjusted P/E Ratio (CAPE) based on stock price divided by prior 10-year earnings. The U.S. stock market is represented by an index created by Professor Shiller. The stocks included are those of large publicly held companies that trade on either of the two largest American stock market exchanges: the New York Stock Exchange and the NASDAQ. Prior to 1926 his data source was Cowles and Associates Common Stocks Index, after 1926 his source has been the S&P 500.

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