

Our Multi-Asset team discuss Russell Investments' performance in the September quarter and their outlook for 2026.

What drove markets during the third quarter of 2026?

The September quarter was modestly positive for growth assets outside of rate sensitive areas. Defensive assets experienced significant volatility as bond yields rose significantly. Several events helped shape market movements over the period:

Sticky inflation sends bond yields soaring

Global bonds experienced a sell-off through most of September as central banks shifted expectations to rate increases to deal with persistently high inflation. Over the quarter, bond prices have experienced one of the largest sell-offs in years as bond yields have hit multi-decade highs across major global economies. The US 10-Year Treasury was around 5.24% at the end of the month, its highest level since 2007 while the 30-Year briefly touched its highest intraday level since 2004. In Germany, the 10-Year Bund reached 3.60%, its highest level in 17 years while the Japanese 10-Year exceeded 3.0%, which is the highest level in 30 years.

Persistently high inflation led the US Federal Reserve (Fed) to increase interest rates to curb inflation in September. Prior to the meeting, new Fed Chair Kevin Warsh primed markets for a potential increase in August, noting that the Fed would take whatever steps necessary to contain inflation. The increase of 25 basis points in September, from 3.75% to 4.00%, was the first rate increase in the US in three years. By late September, markets were already pricing in as many as two additional rate hikes this year including at the Fed's next meeting in late October. New York Fed President John Williams, meanwhile, made comments that the Fed could wait until December before again raising interest rates. William's comments carry weight because he is the vice chair of the Fed's Open Market Committee, which sets interest rates.

The Reserve Bank of Australia (RBA) has increased interest rates four times in the year and once in the quarter, increasing the cash rate by 25 basis points to 4.60% at the end of September. High and persistent inflation was cited as the reason. The consumer price index (CPI) in the year to August came in at 4.0%, led by increases in housing costs and transportation. While it was an increase over July (3.5%), it was below forecasts.

The Australian dollar (AUD) closed the quarter at a two-month low against the US dollar (USD) following the release of August inflation figures. The AUD was as high as US\$0.72 in mid-September before falling to US\$0.69 to end the month, around where it closed at the end of the previous quarter. Despite the intra-quarter volatility, the AUD finished flat against the USD across the quarter.

Equities end higher despite September volatility

Equities proved surprisingly resilient to the rates shock, supported by strong earnings and continued enthusiasm around AI investment and data-center capex. The S&P 500 gained around 2% in Q3 but headline strength concealed weakness underneath, with the S&P500 equal weight and Russell 2000 (which represents small companies), both generating negative returns. This suggests higher financing and discount

rates are increasingly affecting smaller and more leveraged businesses, while cash-rich mega-cap technology companies continue to benefit from AI-related earnings growth and investment, despite the significantly increased debt issuance from the hyperscalers.

Australian share markets were beset by volatility and significantly underperformed global equities during the period. A surge of growth on the final day of September prevented one of the worst monthly performances since March, with markets giving back gains after hitting an all-time high in August.

How did Russell Investments' active multi-asset portfolios perform in the September quarter?

Absolute returns

The Russell Investments Balanced Fund returned -0.18%¹ for the quarter on a net of fees and tax basis. Absolute returns were driven primarily by the Fund's equities exposures which delivered predominantly positive returns, however, exposure to Australian and international bonds and listed real assets were detractors.

Returns relative to fund benchmark

The Russell Investments Balanced Fund underperformed its strategic benchmark on a net of fees and tax basis.

Positive contributors included:

- Outperformance of the Australian Shares Fund, led by strong selections across healthcare – which was the best performing sector in the quarter.
- Manager outperformance in Australian shares including DFA and Numeric Investors.
- A general overweight to global equities, which generated positive returns during the quarter.

Negative contributors included:

- Domestic and international property and infrastructure exposures were significant detractors as rate increases and significantly higher bond yields pushed values down.
- Australian and domestic bond prices also fell (yields rose) on high inflation reports.

¹ Source: Russell Investments. Past performance is not a reliable indicator of future performance.

Russell Investments outlook

Over the quarter, markets were challenged with global bond yields rising and central banks turning hawkish. Oil prices have remained elevated due to lingering concerns about further escalation in the Middle East. In most regions, like the US, the increase in bond yields has mostly been driven by increased policy uncertainty and real yields from higher growth expectations. Inflation has picked up slightly and has been dominated by supply side effects and secular factors (tariffs, energy, AI). Conversely, in Australia, policy uncertainty has increased yields, but inflation has also been stickier. Despite this, equities and notably US mega caps remained resilient over the quarter supported by increasing economic growth expectations and strong corporate earnings. Small cap equities, high duration bonds (e.g. Government) and real assets struggled over the quarter with rising bond yields. Within credit, despite a significant increase in debt supply from US technology firms, credit spreads remained fairly stable as corporate balance sheets remained strong.

Our composite contrarian indicator, which measures pessimism and euphoria in markets, has remained fairly neutral. We still see the cycle as positive going forward, with recession risk at average levels, financial conditions still reasonably supportive and productivity gains likely to support future growth. We are conscious of possible risks to sticker inflation, notably a reignition of the middle east conflict weighing on global oil supply.

Our exposure to growth is modestly above benchmark, paired with exposure to diversifying assets such as hedge funds and unlisted growth. We are also now moderately overweight duration as we have added to global duration with increased bond yields. Regionally, we retain an overweight to US and Emerging Market equities. We are slightly underweight Australian equities as the growth outlook is more subdued and interest rate increases are weighing on the consumer and the property market.

For fixed income assets, we believe Australian government bonds still offer value versus global; however, given the convergence of yields, we added to global duration in late September. We expect that government bonds should act as portfolio diversifiers if the growth outlook deteriorates.

Within credit, we are slightly underweight as IG spreads remain tight and offer poor risk reward.

Private credit, infrastructure, and commodities are alternative investment opportunities that may benefit from their resilience if inflation becomes elevated.

In the currency space, we are close to our long-term targets as the spread between RBA & Fed hikes has reversed and AUD is near fair value.

Where to next?



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About Russell Investments

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(the "Transaction") pursuant to which Russell Investments will be acquired by a consortium led by B Capital Group Management, L.P. that includes California Public Employees Retirement System. The Transaction is expected to close by the end of Q1 2027, subject to the receipt of regulatory approvals and other customary closing conditions.

To the extent permitted by law, no liability is accepted for any loss or damage as a result of reliance on this information.

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