

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

What drove markets during the fourth quarter of 2025?

The December quarter saw growth assets outperform defensive assets. Several events helped shape market movements over the period:

1. Cooling US inflation and Fed easing pushed markets higher.

Global share markets went on a bull run to close the year, led by financials, materials and energy. Gold continued its record run and the S&P 500 flirted with record highs, though both experienced a slight dip in the last two trading days of the year. The rally, which erased earlier equities losses, meant the index was on track for its eight-straight up month – the longest positive run since 2018. The “Santa Claus rally” – a tendency for markets to rise in the last five trading days of the year – was due to a variety of factors including lower-than-expected inflationary figures out of the US and expectations that The US Federal Reserve (Fed) would cut rates twice in 2026. Traditional market rhythms have been thrown off by delayed reports from the US, a legacy of the shutdown.

The Fed cut rates at its final meeting of 2025, a decision that was widely expected. In justifying their decision, the Fed pointed to reasonably strong economic activity; economic activity has expanded at a moderate pace while job gains have slowed, and the unemployment rate edged up through September. US Inflation slowed to 2.7% per November data, which is below forecasts; the October data was not recorded due to the shutdown of the federal government.

2. Central banks diverge to end the year. Underlying inflation and unemployment figures sent central banks down divergent paths to end the year. In the United States, delayed jobs figures presented a mixed picture of the broader economy. Federal Reserve (Fed) officials delivered their third consecutive interest rate cut. The Bank of England (BoE) followed the US lead and reduced its Bank Rate by 0.25% to 3.75%, though the decision was a 5-4 split.

This was the fourth reduction of 2025.

The European Central Bank (ECB) kept all key interest rates unchanged at its policy meeting on 18 December, maintaining a data-dependent, meeting-by-meeting approach that is willing to make changes if warranted by conditions without establishing a fixed path forward.

The Reserve Bank of Australia (RBA) kept its cash rate steady at 3.60% to end the year. The move was not surprising however market observers had noted a recent uptick in inflation and unemployment figures might prompt the RBA to take proactive action to raise rates. The decision to hold rates, which was unanimous, relied on recent data that suggest risks to inflation have tilted to the upside though it will take longer to assess the persistence of the inflationary pressures. In post-meeting comments, RBA governor Michelle Bullock said the prospect of a rate cut was not discussed at the meeting, but they did consider the prospect of future hikes, which may be necessary to get inflation back to the RBA's 2.5% target.

Global shares made modest gains in the quarter, closing up 3.4%¹. Australian shares lagged, returning -0.89%. Volatility through October and November held markets back, while December saw strong growth that broke a multi-month skid. Positive performance in the markets was due in large part to material and resources companies, especially those tied to gold, rare earths and critical minerals that experienced significant growth through the quarter. Copper surged, reaching an all-time high in mid-December on strong demand from AI data centres and energy transition, along with supply disruptions from Central America. Global attention on tech, particularly around valuation, flowed through to Australian shares. NextDC, WiseTech Global and Xero values struggled as the companies face pressure from both the sector as well as regulators.

Energy shares were also underperformers, though a positive sentiment on future higher oil prices supported modest gains to end the month. Financials also saw a rise at the end of the year, led by gains in major banks before year-end trading became thin.

¹ Global shares measured by the MSCI World ex Australia Net Accumulation Index in AUD.

The Australian dollar (AUD) performed well in the December quarter, rising from US\$0.654 cents to start December to close at US\$0.667, peaking mid-month at US\$0.671. The Australian Trade-Weighted Index rose through the quarter, pointing to broad-based appreciation of the AUD both against the USD but also key partner currencies².

Interest rate sensitive assets were mixed, with global listed infrastructure, global and Australian listed property and Australian bonds recording negative growth over the period. Global bond values rose in markets where central banks were considering or executed rate cuts.

Credit spreads for both investment-grade and high-yield corporate bonds remained tight – or tightened – in the quarter. The tight spreads indicate concern about valuation, particularly in AI-related tech companies. Local currency emerging markets debt made strong gains on the back of further USD weakness. Hard currency emerging markets debt also performed well.

How did Russell Investments' active multi-asset portfolios perform in the December quarter? What was rewarded by the market and what wasn't?

Absolute returns. The Russell Investments Balanced Fund returned 0.42%³ for the quarter on a net of fees and tax basis. Absolute returns were driven primarily by the Fund's global equities exposures. Exposures to global listed infrastructure and private debt were also positive while Australian bonds and shares were negatives.

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:

- Stock selection amongst global equity manager, Sanders.
- An overweight to global equities versus the benchmark.

Negative contributors included:

- Stock selection from some of our Australian equity managers; notably aggressive growth manager Platypus.

What is Russell Investments' outlook for 2026? How is it impacting your active multi-asset positioning?

There have been many market drivers over the past 12 months; from Trump returning to office, to central banks cutting rates and global economies demonstrating resilience, however, one key theme that has been a strong contributor to equity price appreciation over this period has been the accelerating adoption of generative AI across different sectors, leading to increased productivity and profitability.

Looking to the year ahead, we see the tools expanding into new sectors and being used by new sectors – resulting in positive corporate results. There is also potential for reaccelerating US growth in the year ahead as policy drags that concerned investors through 2025 fade; we are seeing policy tailwinds building over coming quarters. There are still policy considerations that are weighing on the markets, including a hiring slowdown due to immigration restrictions and a cut back in government hiring – not due to firms reducing headcount because of a weak economy.

Despite many equity markets at or approaching all-time highs, along with valuations that are not cheap, our contrarian sentiment indicator (a measure of panic or euphoria in markets) is not showing unsustainable extremes of euphoria in markets, which we believe provides opportunity for markets to continue to move higher over the short term. Risks do exist, however, with a still uncertain geopolitical and a slowing US labour market - this highlights the value of building portfolio resilience across private markets, real assets, and diversified alternatives – an important point of distinction for active management.

We believe non-US developed equities are more attractively valued than US equities and could benefit from USD weakness; a dynamic we've seen in 2025. However, we're yet to see how large global themes like artificial intelligence play out, with US markets in particular likely to benefit from this.

In emerging markets, investors have become more optimistic on Chinese equities following a series of monetary and fiscal policy support; though sustained growth will depend on further fiscal initiatives, particularly in infrastructure and technology. For fixed income assets, we believe Australian government bonds offer reasonable value, versus the US which appears more fully valued. We expect that government bonds should act as portfolio diversifiers if the growth outlook deteriorates further from here. Private credit and infrastructure markets offer compelling alternative investment opportunities, with these assets benefiting from a differentiated opportunity set and their resilience in a higher interest rate environment.

In the currency space, the USD appears overvalued in real trade-weighted terms, though it has depreciated in recent months. We still see relative value in the AUD over the medium term.

² The trade-weighted index for the AUD is an indicator of movements in the average value of the AUD against the currencies of our trading partners. Source: Reserve Bank of Australia.

³ Source: Russell Investments. Past performance is not a reliable indicator of future performance.

QUESTIONS?

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