Market Outlook

Geopolitical risk, economic resilience

Investment Backdrop

Growth
Positive

Inflation
Neutral

Policy
Negative

Geopolitics
Negative

Valuations
Neutral

Market Dynamics
Neutral

Indicators reflect a qualitative assessment of current macro conditions.

Middle East ceasefire falters

The fragile US-Iran ceasefire collapsed in early July. As yet, resumed strikes by both sides are limited, and precisely targeted, while background talks seem to be continuing, but we are reminded anew of today's geopolitical fragility. That said, we also remain aware that the most troubling humanitarian developments sometimes have little impact in the narrowly-focused, technical world of finance.

… but growth may continue

Oil prices have surged from around $70pb at the start of July to hit $100pb, before falling back (as we write) to $88pb. Reserves are reportedly at multi-year lows, and regional shortages of refined products have been biting.

Nonetheless, economic disruption may remain muted. The most recent forward-looking business surveys, if anything, suggest a small increase in momentum, and from respectable levels.

Again, the single most important driver of growth seems still to be US private demand: household spending, and capital outlays by businesses. Importantly, consumers and corporates together have so far been able to spend more without needing to borrow. For corporates at least this seems likely to change if spending on AI-related capacity surges further, as planned. Such spending could itself absorb much of the US corporate sector's remaining free cashflow. Meanwhile, it is still unclear just how profitable – and sustainable – such AI capacity will ultimately be.

Growth in Europe remains (as usual) more subdued, though local business surveys have also ticked higher and the long-awaited surge in defence spending seems poised to make itself felt. China remains the fastest-growing of the big economies, but it is slowing, with ongoing headwinds from earlier overinvestment.

Rates tilt upwards

Ongoing economic resilience may keep underlying inflation firm, even if oil prices stabilise. If unemployment stays low, core inflation rates seem unlikely to fall back to 2% targets and stay there.

At the start of the year we felt that interest rate expectations were too low. In place of that earlier profile of falling rates, money markets have been pricing-in rising rates during the rest of 2026. The ECB raised rates in June.

The catalyst for the change in views was the initial spike in oil prices back in March, but most recently markets have shared our view that there may be no room for cuts even in a world of lower oil costs. The new Chair at the US Federal Reserve has also been sounding more hawkish than his predecessor, underlining the shift in market expectations.

We didn't see things following this path, then, but interest rate expectations have ended up more or less where we thought they might. That said, the adverse impact on stocks remains smaller than we'd anticipated, because economic growth, and surging AI outlays in particular, has boosted corporate profitability.

Volatility contained

Even after the latest re-escalation, this does not look like the "biggest ever energy shock" which some proclaimed it to be. On a long-term view, the Strait of Hormuz and oil itself are becoming less important, and more quickly than was already the case.

Against this backdrop, and with US corporate results comfortably beating expectations for a second successive quarter, the relative stability of stock prices looks less remarkable. Our own appetite for risk remains higher than it was in April/May (even though the business case for much of that AI investment remains unproven).

The shift in interest rate expectations has been hurting both bonds and gold. Bonds are not expensive, but the gold price however remains historically elevated.

Important information