



Introduction

Financial markets generally performed well in August, helped by strong company profits and signals from major central banks that they may start lowering interest rates.

Investor confidence was buoyed by signs of stabilising inflation and the labour market slowing down.

Overall, technology companies continued to perform strongly, though their momentum slowed toward the end of the month amid cautious guidance from some major computer chip companies and concerns over whether AI projects would deliver expected results. Smaller companies did well as investors showed renewed interest in domestic businesses.

In the UK, defensive stocks performed better than others, while the Bank of England became more open to cutting interest rates. Japan's stock market performed very well, helped by a weak Japanese yen making Japanese goods cheaper abroad and strong company earnings.

Around the world, there were concerns about political interference in central bank decisions, adding complexity to the investment landscape.

Overall, August reflected a delicate balance between economic risks and investor optimism.

Markets

Stock markets around the world posted solid gains in August, with developed countries seeing their share prices rise. Emerging markets also advanced, particularly those in Latin America and China.

In the US, share prices climbed despite weaker employment data and ongoing concerns about trade tariffs. Powell's

Portfolio & Market Update

August 2025

speech at the Jackson Hole conference suggested the Federal Reserve might cut interest rates, which boosted investor expectations and helped offset inflation worries.

Companies in materials and healthcare sectors performed better than average, while technology companies lagged behind due to concerns about whether AI projects would deliver expected results.

European stock markets outside the UK edged higher, led by energy and automobile companies, though political uncertainty in France dampened overall sentiment. UK markets rose, with defensive companies leading.

Bond markets were mixed, with short-term US government bonds gaining value while longer-term bonds faced pressure due to concerns about government spending. Commodities saw modest declines overall, with oil prices weaker but gold supported by investors seeking safe investments.

US

US stock markets gained 2.0% in August, when measured in US dollars, though the performance was slightly negative when converted to British pounds due to the dollar strengthening.

While the economy's growth rate was revised upward and inflation remained elevated, the sharp slowdown in job creation and rising unemployment suggested the economy is slowing down.



Manufacturing data showed the sector was still contracting, with trade tariffs cited as a key reason for negative business sentiment.

Despite these challenges, investors remained optimistic, supported by resilient consumer spending and hopes for supportive government policies. However, high stock valuations and ongoing economic uncertainty suggest a cautious outlook for the autumn.

UK

UK stock markets delivered solid performance in August, with the main UK stock index rising by 1.22% in pound terms.

Large companies outperformed medium-sized companies, supported by strength in energy, basic materials, and telecommunications sectors. Technology companies lagged, mirroring the global sector weakness.

The Bank of England cut interest rates to 4.0%, though policymakers were cautious due to persistent inflation, which rose to 3.8% in July. Despite the rate cut, investors reduced their expectations for further rate reductions, as the domestic economic situation remained challenging.

Job market data showed signs of deceleration, while concerns about government spending ahead of the Autumn Budget added uncertainty.

Overall, sentiment was supported by resilient global demand and investors moving money into defensive sectors, but economic headwinds and policy uncertainty suggest a measured outlook for UK investments heading into the final quarter of 2025.

Europe

Continental European stock markets continued their gains in August, with the MSCI Europe (excluding UK) rising by 1.20%

Portfolio & Market Update

August 2025

in British pound terms. Investor sentiment was supported by resilient economic data and easing trade tensions.

Manufacturing companies saw new orders increase for the first time in 15 months, along with increased hiring. However, business confidence remained subdued due to concerns about US tariffs and broader economic challenges.

Energy and consumer discretionary companies led gains, while industrial and technology companies lagged. French stocks underperformed due to political uncertainty, weighing on the broader European index.

The European Central Bank kept interest rates unchanged. Despite elevated input costs and uneven sector performance, the region's resilience and improving demand conditions support a cautiously positive outlook for autumn.

Japan

Japanese stock markets posted solid gains in August, with the main Japanese stock index (MSCI Japan) up 4.5%. Market momentum improved mid-month, supported by strong company earnings, demand related to AI technology, and a potential improvement in liquidity conditions in the US.

Companies that export goods and those sensitive to global economic cycles benefited from a weaker yen and easing trade tensions. However, manufacturing activity remained subdued in the region,



with a key manufacturing indicator showing continued contraction.

Foreign sales fell sharply due to new US tariffs, while business sentiment weakened to a three-month low.

However, consumer confidence rose to its highest level since January, reflecting improved expectations for employment, income, and spending.

Inflation forecasts were revised higher, while economic growth expectations edged up slightly. Despite challenges in manufacturing and trade, stock markets were supported by optimism around AI infrastructure and signs of gradual economic recovery.

Asia & Emerging Markets

Emerging market stocks declined by 0.79% in British pound terms during August, underperforming global markets due to mixed regional dynamics and renewed tariff pressures. Latin America led gains, with Colombia, Chile, Brazil, and Peru supported by stronger currencies and improving inflation data.

China outperformed other emerging markets, helped by continued government support through its anti-monopoly policies and a 90-day pause in US tariffs.

However, broader emerging market sentiment was weighed down by weakness in Taiwan, Korea, and India.

Taiwan and Korea suffered from technology sector weakness and concerns about rising corporate taxes, while India faced pressure from increased US tariffs and foreign investors selling their holdings. The MSCI Asia (excluding Japan) posted modest gains, led by Singapore, China, and Malaysia.

Despite some positive company earnings, economic data remained weak, and investor sentiment was cautious.

Portfolio & Market Update

August 2025

Overall, emerging market performance was constrained by dollar strength, trade uncertainty, and uneven sector trends, reinforcing the need for careful selection and risk awareness.

Fixed Income

UK government bond yields rose in August, driven by another unexpected increase in inflation and reduced expectations that the Bank of England would cut interest rates further.

Short-term yields climbed as investors reassessed the likely path of interest rates, while long-dated government bonds underperformed, with the 30-year yield reaching its highest level since 1998 due to limited trading and concerns about government finances.

In the US, Treasury yields fell early in the month following weak job market data and signals from the Federal Reserve, though longer-term rates remained under pressure due to worries about government spending and political interference.

The yield curve steepened as markets priced in a higher likelihood of a September rate cut.

In Europe, bond yields drifted higher, supported by stable inflation and improving growth sentiment, though French bonds underperformed due to rising political uncertainty.



Commodities

Commodities delivered mixed performance in August, with the main commodities index (the S&P GSCI Index) posting a slight decline. Energy was the main drag, as oil prices fell mid-month following the International Energy Agency's lowered revision to 2025 demand forecasts and an increase in US crude oil inventories.

Gold continued to attract investors seeking safe havens, supported by expectations of a US interest rate cut and growing political pressure on the Federal Reserve.

Industrial metals were mixed, with iron ore and steel gaining due to infrastructure optimism, while copper faced headwinds from trade tensions.

Overall, commodity markets reflected a cautious tone amid shifting economic and geopolitical dynamics.

Outlook

As we move through late summer, markets remain cautiously optimistic, though high stock valuations and fiscal uncertainty continue to prevent overconfidence.

At Flying Colours, we maintain a measured approach to government bonds. While their valuations have improved, the surge in government debt issuance is testing market capacity, reinforcing our decision to keep government bond allocations below historical levels. Instead, we favour high-quality government debt from countries with disciplined spending.

Our bond investments remain diversified, including selective positions in emerging market debt where the fundamentals and valuations are compelling. We also retain exposure to alternative investment strategies, which we believe offer more effective diversification amid rising yields, policy uncertainty, and stretched stock valuations.

Portfolio & Market Update

August 2025

With economic risks still present, we continue to favour a globally diversified, balanced approach across different types of investments. Our investment philosophy is rooted in long-term thinking, focused on managing risk over time and delivering well-structured, risk-adjusted returns in the best interests of our clients.

Glossary

Tariff: A tax imposed by one country on imported goods and services from another.

Federal Reserve: Central bank of the United States.

MSCI Indexes: Stock indexes that track the performance of the stocks included in them. Often additional context is added in e.g. MSCI Europe ex-UK index covers Europe but excludes the UK.

European Central Bank (ECB): The central bank for the euro. Its main task is to maintain the euro's purchasing power.