

Introduction

The final three months of the year brought positive results across global investment markets, with all major types of asset classes showing gains. Stock markets performed well despite challenges such as a US government shutdown, weaker employment figures, and questions about whether AI companies were overvalued.

Market trends shifted noticeably during this period. Growth-focused companies underperformed compared to value-oriented ones, while traditionally safer sectors posted impressive gains. In the bond market, falling interest rates and a steepening yield curve (where the gap widened between short-term and long-term interest rates) helped performance.

Overall, 2025 was a year marked by strength and durability. The S&P 500 rose over 9% and hit 39 new record highs, while the Global Equity Index surged nearly 20%, powered by substantial European economic stimulus and attractive pricing. The Aggregate Bond Index returned 7.3% as the Federal Reserve cut rates three times in the second half of the year.

The fourth quarter reinforced the advantages of spreading investments across different countries and asset types as market leadership shifted between regions and investment categories.

Markets & Portfolio Impact

Global stock markets posted strong fourth quarter gains, with Asian markets outperforming their developed-world counterparts. Alongside this, US indexes reached record levels, supported by another 0.25% interest rate cut from the Federal Reserve.

Additionally in the US, growth-oriented stocks outperformed value stocks, with large companies performing better than smaller ones, and technology stocks leading the rally.

European market prices moved slightly higher, lifted by energy and car manufacturing sectors, though political uncertainty in France continued to weigh on investor confidence.

Portfolio & Market Update

Quarter 4, 2025

UK stock markets rose, led by traditionally defensive sectors, as the Bank of England cut interest rates but remained cautious due to persistent inflation.

Our ProsperityBuild portfolio recorded positive returns, as our preference for growth-oriented equities, combined with targeted Asian exposure, contributed positively as these areas benefited from stronger earnings momentum and sustained investor demand. This positioning helped make the most of well-performing regions while maintaining diversification and risk management.

Bond markets benefited from easier financial conditions in the fourth quarter, with narrowing gaps between different bond types and strong investor demand.

Emerging market bonds outperformed, supported by improving economic fundamentals and favourable currency movements, while corporate bond markets remained resilient.

Government bond returns varied, reflecting differing government spending dynamics and central bank policies.

Our ProsperityShield portfolio navigated this effectively, as we maintained an underweighting in developed sovereign bonds and a tilt toward emerging market debt, areas that benefited from improving fundamentals and supportive currency trends.

US

US stock markets rose in the fourth quarter of 2025, though returns for UK investors were limited as a weaker dollar diminished gains when converted to pounds. This occurred despite the longest government shutdown on record and rising job losses.

The quarterly advance helped US markets deliver a third consecutive year of double-digit returns, with the S&P 500 ending 2025 nearly 18% up in dollar terms, though less in pounds, even after the sharp April sell-off following the Trump Administration's tariff announcements.

Late-year volatility in the market stemmed from investors taking profits rather than worsening economic fundamentals.

Market leadership remained concentrated in technology and communication services, though signs of broadening emerged. Both economically-sensitive and traditionally defensive areas, including industrials, financials, healthcare and utilities, recorded strong double-digit gains. Valuation concerns remained elevated, despite signals from monetary policy.

UK

UK stock markets delivered solid fourth quarter 2025 gains, with the FTSE 100 reaching a record high of 10,000 points, supported by its global, defensive composition.

Strength in financial companies, mining firms, defence contractors and precious metal producers reflected strong overseas earnings, resilient demand and a slightly weaker pound.

Medium and small-sized company stock prices lagged, as concerns over domestic economic growth, government spending cuts and weak consumer demand weighed on investor sentiment.

Policy developments shaped markets late in the quarter. Chancellor Rachel Reeves's Autumn Budget was viewed as credible, despite mid-month volatility in government bond markets, as tax rises and incentives were seen as fiscally manageable.

The Bank of England cut rates to 3.75% in December, signalling caution. While supportive for riskier assets, policy easing did not fully offset concerns.

Europe

Eurozone stock markets delivered positive but mixed returns in the fourth quarter, showing resilience despite an uninspiring economic backdrop.

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Major benchmarks finished near multi-year highs, supported by broad regional performance. Stock prices remained relatively reasonable, helping European equities outperform US markets when adjusted for currency effects, aided by euro appreciation against the dollar.

The European Central Bank held interest rates steady in December, after multiple cuts since mid-2024, signalling a cautious, gradual approach for 2026, and economic conditions remained uneven.

Manufacturing activity, particularly in Germany, stayed weak, while services activity and employment throughout the continent proved resilient. Financial companies performed strongly, benefiting from easier conditions, while healthcare and utilities attracted investors seeking defensiveness. Growth stocks lagged as valuation concerns re-emerged.

Overall, despite French government spending pressures, improved growth forecasts and easing inflation supported investor confidence.

Japan

Japanese stock markets continued to show strong performance in local currency during the fourth quarter, supported by improving company earnings, ongoing corporate governance reforms, and a constructive domestic policy backdrop.

Market leadership was broad, with strength across industrial companies, technology firms and defence contractors, reflecting global trends and improving investor confidence in domestic growth.

Investor sentiment was underpinned by the election of Prime Minister Sanae Takaichi and a new coalition government. In addition, the Bank of Japan raised interest rates in December and signalled further increases could follow in 2026.

While valuation concerns increased later in the quarter, solid corporate earnings momentum, rising shareholder returns and ongoing balance sheet discipline supported the Japanese market.

Asia & Emerging Markets

Asian and Emerging Markets delivered broadly positive returns, supported by easing US monetary policy and continued technology sector strength.

Performance in areas of Asia where investor enthusiasm around AI and the region's role in global supply chains underpinned sentiment.

South Korea and Taiwan benefited from strong demand for semiconductors, while several Latin American markets were supported by higher commodity prices and stronger currencies.

Returns were more mixed elsewhere. India performed broadly in line with the broader Emerging Market index as supportive economic conditions offset valuation concerns, while China gave back some earlier gains amid profit-taking, softer economic data, and renewed property sector stress.

Despite ongoing risks, Emerging Market equities remained resilient into year end.

Fixed Income

The rally in riskier assets during the fourth quarter extended into bond markets, with gaps between different bond types narrowing broadly and investor appetite remaining strong.

Emerging market bonds were a notable outperformer, supported by improving fundamentals, strong demand and favourable currency movements, particularly in Latin America.

Corporate bond markets performed well, with investment-grade assets benefiting from stable company balance sheets and easing financial conditions. While pockets of stress persisted in higher-risk areas, overall credit quality remained resilient.

Government bond markets showed greater divergence.

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UK government bonds outperformed as fiscal concerns eased and monetary policy turned more supportive. US Treasury bonds delivered muted results amid shifting rate expectations and changes in the yield curve, and Japanese bonds were sold off as policy tightening and fiscal expansion raised debt sustainability concerns. In Europe, bonds from peripheral countries outperformed those from core economies as economic prospects improved.

Overall, bond returns were underpinned by policy easing and stable growth expectations, despite ongoing regional differences.

Commodities

Commodities delivered mixed but positive performance, with precious metals the clear standout.

Gold and silver benefited from heightened geopolitical uncertainty, a weaker US dollar, moderating but still elevated inflation and global growth concerns. Strong investor demand and ongoing central bank purchases supported gold prices, while silver outperformed due to tighter supply and its growing role in renewable energy, electric vehicles and data centre infrastructure.

Industrial metals performed well, supported by supply constraints and rising demand linked to electrification, electricity grid investment and digital infrastructure, particularly in China.

Energy markets lagged, as oil prices declined amid global oversupply, expanding production and softer demand growth.

Strong precious metals gains helped offset weaker energy prices, lifting overall commodity returns.

Outlook

As we enter the new year, markets begin 2026 on more stable footing, with easing inflation pressures and interest rates appearing closer to their peaks. While this backdrop is constructive, we remain mindful that US stock market valuations are elevated and political and fiscal uncertainty persists across parts of Europe and the UK.

We continue to monitor geopolitical hotspots due to their potential market impact. Tensions surrounding Greenland's strategic importance, Iran's role in regional stability and energy markets and Venezuela's political-economic crisis could each influence asset prices and market sentiment.

At Flying Colours, we continue a selective approach to government bonds. Although yields are now more attractive, rising debt issuance and ongoing fiscal challenges mean we prefer to remain cautious, particularly where public finances appear stretched. Our focus remains on high quality sovereign issuers with strong fiscal discipline.

We continue to emphasise diversification beyond traditional fixed income, including carefully selected emerging market debt exposure, alongside alternative strategies that can help manage risk through different market environments.

We maintain a globally diversified and balanced portfolio approach, focused on preserving capital and delivering sustainable, risk adjusted returns for our clients over the long term.

Glossary

Growth-focused companies: Any company whose business generates strong cash flows or earnings that grow faster than the overall economy. These companies have profitable opportunities to reinvest their earnings back into the business, so they typically pay little to no dividends to stockholders.

Value-oriented companies: An established business whose stock price is considered cheap relative to its actual earnings, assets, or cash flow. These companies may be overlooked by investors because they're in mature industries or facing temporary challenges.

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Yield

curve:

Shows the relationship between yields and time to maturity.

Rally: A period of sustained increases in the prices of stocks, bonds or indices.

ProsperityBuild: A growth-oriented investment fund co-manufactured by Flying Colours Investment Management and Fidelity International, designed to provide global equity exposure.

ProsperityShield: A diversified, defensive investment fund co-manufactured by Flying Colours Investment Management and Fidelity International, designed to grow capital over the long term, while providing a smooth performance path for investors.