Quarterly review

GBP Global Medium Portfolio

Market highlights

Q2 2025

Summary

Gains in global equities over the second quarter masked the extreme volatility experienced in early April when President Donald Trump unveiled his sweeping tariffs on so-called Liberation Day. The tariffs prompted sharp declines across equity and bond markets worldwide, although Trump's subsequent backtrack on tariffs along with a strong first quarter earnings season helped stocks and bonds recover. The dollar was the real victim of the quarter, as erratic policymaking from the US administration eroded confidence in the greenback.

Trump's sweeping tariffs, which included a baseline tariff of 10% on all countries and higher rates for certain regions, elicited strong reactions both domestically and internationally. Equities experienced a sharp risk-off response, with the S&P 500 posting its fifth biggest two-day decline since World War II. The equity market sell-off in April led investors to seek safety in gold as recession concerns mounted. The surprise Liberation Day tariffs triggered fears of higher inflation and economic disruption, rattling investor confidence in US Treasuries—normally a safe haven. This led Trump to make a U-turn and announce a 90-day pause on most tariffs.

The recovery in bond markets soon spread to equity markets. The tariff rollback combined with a robust set of first quarter corporate earnings in the US helped reverse many of April's losses. The S&P 500 rose 6.3% in May and 5.1% in June, ultimately ending the quarter up 10.9%,although given currency headwinds, the total return was 4.4% for sterling investors.

Stronger-than-expected macro data both in the US and Europe helped sentiment and alleviated concerns the US was facing an imminent recession. Stocks pushed higher as news of potential trade deals between countries filtered through, including frameworks between the US and the UK and the US and China. The deal between China and the US, which includes an agreement for Beijing to speed up exports of rare earth minerals, may help stabilise relations between the two countries following an escalating trade war where both sides slapped sky-high tariffs on each other's goods.

Following Germany's pledges to boost defence spending, NATO (North Atlantic Treaty Organisation) allies promised to raise defence spending to 5% of GDP by 2035, which sent European equities higher. Germany's DAX Index rose 7.9% in the second quarter and the Stoxx Europe 600 Index gained 3.3%. Performance in these markets is even more impressive in US dollar terms.

Asian equities saw large declines due to April's tariffs, although experienced strong rebounds once the tariffs were paused. Hong Kong's Hang Seng rose 5.8%, China's Shanghai Composite gained 4.2% and Japan's Topix returned 7.4% in the quarter.

After Trump's initial bold claims that he would broker a deal between Russia and Ukraine in one day, more than five months into his second term, this looks as far away as ever. Both Russia and Ukraine remain firmly entrenched in their positions on territorial disputes and sovereignty. Meanwhile Israel's attacks on three key Iranian nuclear facilities and subsequent twelve-day war led to a short-lived rise in oil prices in June, although Brent finished the quarter 10% lower at $67 a barrel.

Trump's aggressive trade and foreign policy rhetoric have further heightened global tensions and had a tremendous impact on the US dollar's safe haven status. As a result, investors have been diverting assets from the dollar—seen as the world's reserve currency—to other currencies and gold. This sent the dollar down 7% in the second quarter and down 10.7% so far this year, with the dollar index now having its worst first half performance since 1973. In the second quarter, the dollar lost ground against every other major G10 currency.

While equity markets ultimately ended the quarter in positive territory, the journey was anything but smooth. The sharp swings triggered by Trump's aggressive tariff policy—and his subsequent reversal—highlight how vulnerable global markets remain to unpredictable policymaking. Although investor confidence rebounded on the back of strong corporate earnings and resilient macro data, this quarter served as a reminder of how challenging forecasting has become.

Fixed Income

Across the quarter, government bond markets swung from a steep sell-off to a modest rally as global growth concerns, fiscal strains and shifting monetary-policy expectations drove demand. Following Liberation Day in early April, Sovereign bond markets experienced a heavy sell-off, with 30-year US Treasury yields surging to 4.9%, their largest daily jump since March 2020, and 10-year yields climbing to 4.5%, the highest since January. This reversal of early-month safe haven buying raised doubts over the Treasuries' role as a reliable market refuge, leading to Trump's U-turn.

May saw US bonds under further strain as Moody's downgraded US sovereign debt from Aaa to Aa1 amid mounting deficit fears. Sticky inflation and slowing growth compounded a stagflationary backdrop (concerns over slow economic growth coupled with rising inflation), while Trump's proposed extension of expiring tax cuts—the "big, beautiful bill"—exacerbated long-term debt projections. Consequently, 30-year yields breached 5% for the first time since October 2023, closing the month at 4.93% after a notable 25 basis-point rise. The Federal Reserve (Fed) held rates steady in a cautious, data-dependent stance, with Chair Powell highlighting the challenges of forecasting amid evolving policy risks.

Across the Atlantic, the Bank of England (BoE) cut its policy rate to 4.25% on 8 May—its fourth consecutive quarter-point reduction—but policymakers were split: two MPC members backed a larger 50 bp cut, while two preferred no change. Governor Bailey stressed there is no preset path for rates and cautioned against overstating trade frictions. In June, US yields retreated on softer economic data and dovish Fed signals, with markets fully pricing in a September rate cut. Late in the quarter, reports that President Trump may nominate a Fed chair successor by autumn drove yields down and lifted expected rate cuts to 64 bps for the rest of the year.

From a portfolio perspective, the fixed income component of the portfolio provided decent returns over the quarter. The portfolio's position in the 2035 UK Gilt was the best performer as yields at the belly of the UK yield curve fell by 35 bps. Our holdings in US Treasuries also contributed positively to performance, despite the value of the dollar depreciating by almost 6% for the quarter. Our US Treasury exposure is hedged to eliminate the risk of foreign exchange fluctuations eroding the diversification and income benefits of owning government bonds. Our position in the 3-7 Year US Treasury ETF added value as yields fell, and our inflation linked bonds holding was flat as the decline in nominal yields offset falling expectations for future inflation.

Turning to credit markets, credit spreads in both investment grade and high yield corporate bonds narrowed over the quarter, despite climbing significantly at the beginning of April. Liberation Day uncertainty sent the spread between US high yield bonds and their government bond counterpart to over 4%. As US trade policy uncertainty and inflation concerns abated over the quarter, spreads recovered their losses and ended the quarter on a positive note. Consequently, our position in AXA US Short Duration High Yield was the strongest performing credit position in the portfolio. Muzinich Global Tactical Credit, a strategic bond fund comprising mostly of investment grade credit, also yielded positive returns while protecting against the downside in early April.

Equity

The announcement of higher-than-expected trade tariffs on Liberation Day triggered a sharp sell-off in equity markets due to concerns they could give rise to a recession in the US. However, the subsequent 90-day pause on those tariffs and positive progress in US-China trade talks provided reassurance that a less extreme outcome was more probable.

Within the US, the S&P 500 ended the quarter at all-time highs in local currency terms although the weakness in the USD reduced returns for sterling investors. The strong recovery was led by growth stocks, particularly some of the largest Technology stocks.

Market enthusiasm towards Artificial Intelligence (AI) exposed companies returned as companies continued to invest significant amounts of capital in this area. However, the performance of the Magnificent Seven saw greater dispersion. Those companies which are already showing tangible revenue growth from AI such as Nvidia, Meta, and Microsoft outperformed whilst Apple and Alphabet lagged due to innovation concerns and potential competition from AI chatbots such as ChatGPT.

This divergence created opportunities for active managers, with strong performance seen from dedicated US managers such as T Rowe US Structured Research. The timely addition of PGIM US Growth to our portfolio, which increased the growth exposure and Technology allocation within the overall portfolio, captured the market rebound and benefitted from strength in its stock selection in Technology. The top holdings of the fund include Nvidia, Microsoft, Amazon and Meta.

In Europe, Ardtur Continental European, a fund added to the portfolio during the quarter, benefitted from its cyclical bias and the strong performance of its holdings in European banks Commerzbank, Deutsche Bank and BNP Paribas as they priced in a reduced economic impact of trade tariffs on the region.

Amongst our core global managers, the second quarter saw a reversal of the performance dynamic witnessed earlier in the year. Lazard Global Equity Franchise and Schroder Global Recovery were amongst the weakest performers. These funds have value or defensive biases which became detractors as the market shifted from value to growth and from defensives to cyclicals. Morgan Stanley Global Brands also struggled during this period as the fund suffered from poor stock selection with disappointing performance from Aon, Accenture and Coca-Cola. In comparison, Blackrock Global Unconstrained, which has a large Growth bias, benefitted from both style rotation and strong performance from some of its top holdings such as digital infrastructure provider Vertiv Holdings, US aerospace manufacturer Howmet Aerospace and Microsoft. This fund was the top performing equity fund during the quarter.

In Asia, markets demonstrated mixed performance across the region. Schroder Asia Total Return benefitted from its allocation to Financials and Technology including the strong performance of top holdings TSMC and Hong Kong insurer AIA. Whilst Morgan Stanley Asia Opportunities performance was more muted due to the impact from its greater allocation to China and specific weakness in Chinese consumer discretionary holdings Trip.com and Meituan. Japan's recovery was tempered by a slowdown in trade talks with the US which prolonged uncertainty for larger exporters, such as auto manufacturers.

Blackrock Natural Resources was one of two funds to deliver a negative return during the quarter. The escalation in the Iran-Israel conflict saw a brief spike in the oil price which the fund benefitted from, but this quickly reversed upon the brokerage of a ceasefire. The overriding driver of performance of the fund has been the fall in commodity prices due to a weaker demand outlook caused by trade tariffs and increased oil supply from OPEC+ nations.

Despite the challenges of the current economic environment, punctuated with bouts of volatility, the equity component of the portfolio was resilient during the quarter. We continue to believe that a consistent focus on building diversified portfolios with a targeted bias to quality is the best approach to achieving steady, long-terms equity returns.

Alternatives

The second quarter of the year ended with the Bloomberg Commodity Index down -4.06% in USD terms, this was primarily driven by conflicts in the Middle East which heighted volatility in oil and natural gas prices. Oil prices initially rose by $10/bbl in mid-June following Israel's attack on Iran. By late June however, it had fallen -15% from peaks as Trump announced a ceasefire. Gold prices have also dropped as market conditions improved, reducing demand for safe haven assets.

Within our portfolio, the trend-following strategy Winton Trend has been our most disappointing position in the portfolio. Over the medium- and long-term, trend following strategies are excellent portfolio diversifiers – delivering positive returns with little or no correlation to other asset classes. The strategy has struggled since purchase however, as markets continued to trade in a range with no clear upward or downward trend. Positioning wise, the fund's fixed income and currency exposure suffered as speculations around US interest rate expectations have been volatile, and commodities have oscillated around geopolitical tensions and OPEC production decisions. Despite a difficult period, we maintain our conviction that trend following has a place in a multi-asset class portfolio.

Elsewhere, Graham Macro fell in the second quarter despite gains within their fixed income holdings particularly towards the long end of the curve. Losses from long positions in the US dollar, sovereign bonds and soft commodities have dragged performance this quarter. Brevan Howard Absolute Return made gains as the team continues to trade actively and tactically, taking advantage of short-term changes within the fixed income and equity markets. The fund remains a good diversifier within our portfolio, offering differentiated returns in a complex and uncertain macro landscape.

Portfolio Changes and Asset Allocation

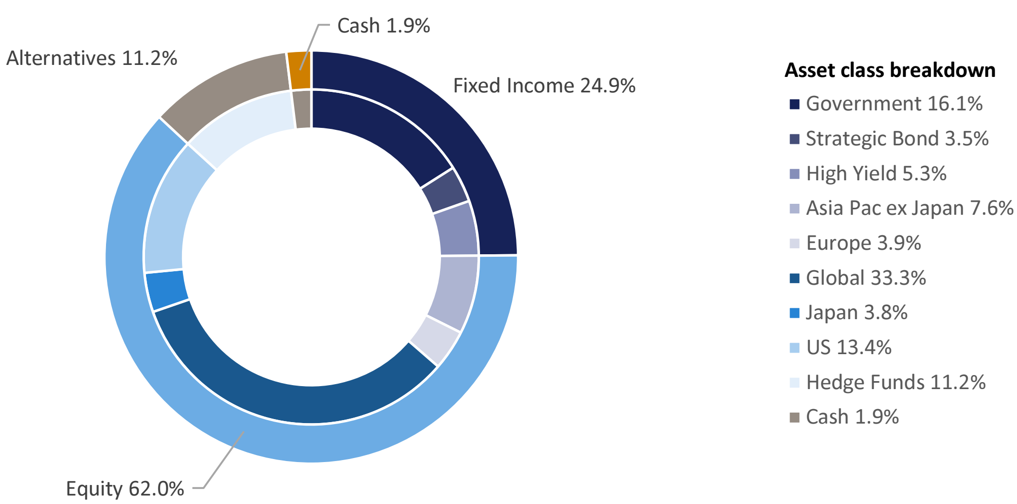
We increased our exposure to both Japanese and European equity markets on two occasions in the quarter, firstly close to their lowest points for the year in April, and then in June, reflecting our conviction in their improving fundamentals and attractive valuations. We sold our remaining position in US smaller companies, as US growth continued to slow.

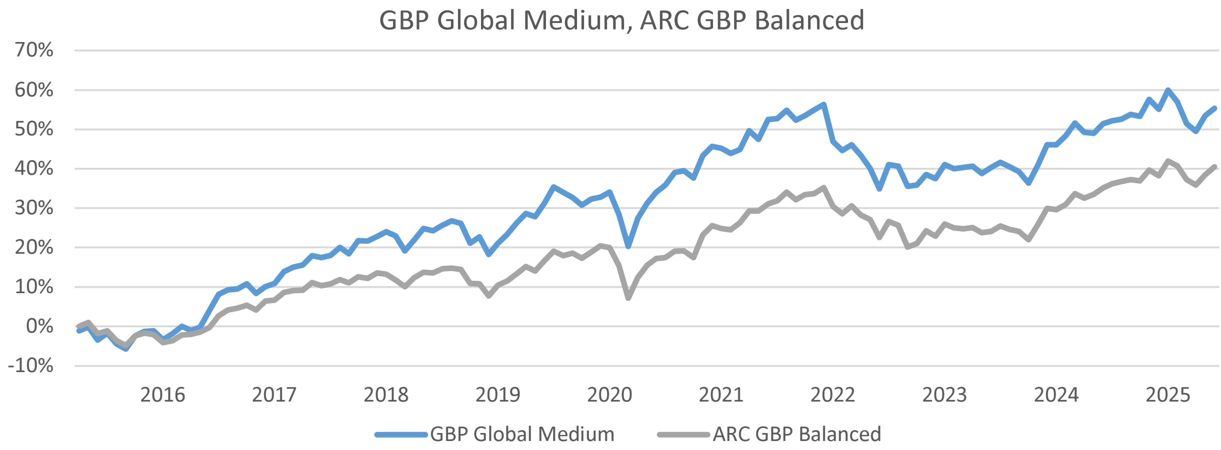
Our increased allocation to Japan reflects a market showing encouraging signs of economic normalisation after decades of stagnation. Japan benefits from real wage growth, rising inflation, a competitively valued currency and an inexpensive equity market. Reforms at the Tokyo Stock Exchange are driving improved corporate earnings and returns, underpinning our positive outlook. Furthermore, the potential for a US-Japan trade agreement remains a key catalyst, which we continue to monitor closely, mindful of the ongoing tariff risks.

We also expanded our position in Europe, building on the exposure initiated last quarter. After years of underperformance, the region appears poised for a turnaround. Our investment through the Ardtur Continental European Fund reflects strong valuation discipline and confidence in the manager's process. We believe this is the optimal vehicle to capture the benefits of fiscal easing and accommodative monetary policy across Europe. The recent German elections have reinforced Europe's improving competitiveness, and relative valuations versus the US remain compelling.

To fund the April purchases, we reduced our US High Yield holdings where pricing had remained resilient. For our June purchases we exited the remainder of our US small-cap position. Despite some positive catalysts such as deregulation in certain industries, we believe ongoing supply chain challenges, slow down in US economic growth and a weakening of private sector sentiment represent headwinds for smaller companies. Moreover, earnings growth in small caps continues to lag large-cap peers.

Portfolio Positioning





Conclusion

From a geopolitical perspective, the events which most significantly impacted the quarter were occurring in the Middle East. After several instances of heightened tension and conflicts over recent year investors have grown to learn that the impacts of international relations are not always necessarily relevant to the market. Current global instability shows no signs of abating but from the market's perspective, as long as the flow of oil and goods is not materially disrupted, then company earnings and interest rate expectations, two areas that have the strongest impact on the stock market, then the market should remain stable.

Recent years have seen a rise in global conflicts and unexpected events, reflecting a shift from a largely US-dominated world to a more complex, multi-polar international landscape. Such a transition can lead to greater uncertainty and geopolitical challenges. While this environment may increase market volatility and make investing more difficult, history shows that markets tend to deliver returns over the medium to long term despite geopolitical uncertainties.

Elsewhere the key questions for investors in the second half of the year will be around whether US tariffs are more impactful for growth or inflation, and whether the US dollar will truly lose its safe haven status. On the former, whilst we can see from tax receipt data that effective tariffs on US imports have increased, we are yet to see tariffs impact the US inflation data. Some of this will be the result of lag, but with US growth slowing, a looser labour market and a more modest (albeit still large) fiscal deficit, the situation ought to be quite different to the magnitude and persistence of inflation we saw in 2022. On the latter, the weakness of the US dollar has resulted in very different outcomes for euro and sterling investors, versus their US counterparts. Whether it's the economy losing momentum, concerns around fiscal policy or expectations around the next Fed chair, the dollar has had a series of headwinds this year. For sterling and euro investors this has meant global equity returns remain negative year to date and still over 5% from their 2025 highs.

Currency hedging a portfolio's bond allocation is prudent because their returns are largely fixed in local currency terms. For example, a US dollar bond yielding 5% will deliver that return in dollars, regardless of whether the dollar strengthens or weakens. Introducing currency exposure can distort that predictable outcome so we remove it where possible. The same applies to hedge funds, where we want the outcome to reflect manager skill, not random currency effects.

Equities are different. Companies often earn revenues globally, and their share prices naturally reflect movements in exchange rates. Whilst being opportunistic at extremes can add value, structurally hedging currency can actually interfere with this relationship, potentially reducing diversification and increasing complexity.

Further, the US dollar has traditionally been a risk-mitigator for sterling and euro clients. In the worst years for global equities, such as 2008 and 2022, the US dollar has appreciated considerably against the euro and the pound. This is because the dollar tends to appreciate in times of stress. The current charge is that this is no longer the case – the dollar is now a risk-on currency, meaning that it will move in lockstep with global equities. This may well be the case but from a portfolio strategy perspective we would need to see more evidence – just because the dollar behaved like a risk asset during (hopefully) peak US policy disorder in March and April does not mean that we should disregard a long history of it being a safe haven asset. Indeed, during the recent market sell off in relation to Israel and Iran, the dollar resumed its role of a risk-off currency.

The dollar's relationship with risk assets, along with whether tariffs will have more pronounced impact of inflation or growth are the two key questions for markets and portfolio strategy currently – these are our central focus over the coming weeks and months.