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October 2025

Market Update

Performance Summary

It is pleasing to report that markets have continued to build on the gains mentioned in our second quarter update. All major stock markets have delivered positive gains year to date with the stand-out performers being Europe, Asia and the UK (markets we have felt were undervalued for some time) – all delivering percentage returns in the high teens or above. Technology stocks continued to drive strong returns from US markets, but as previously reported, continued US Dollar weakness meant returns were blunted somewhat in sterling terms.

However, stock market returns were eclipsed by the gold price which continued its upward trajectory past the psychologically important \$4,000/Oz mark, delivering a staggering return approaching 50% so far this year. The combination of lower US interest rates, a weaker US Dollar, fears over sticky inflation and geopolitical instability have been significant tailwinds for the precious metal which show little signs of abating.

In fixed income, returns from bonds have been far more pedestrian year to date which is reassuring on many levels. We favour high-quality government bonds, especially in the UK where we can lock in attractive yields to maturity as well as protect portfolios in economic downturns.

What does this all mean for portfolio returns? Year-to-date returns have been ranged from mid-to-high single digit total returns net of fees and charges, comfortably ahead of inflation. However, we must not be complacent and remain ever vigilant and prepared to act in your clients' best interests (more on this later).

Quarterly Recap

Three key themes influenced markets this quarter:

1. The Federal Reserve's (The Fed) interest rate cuts: signalling a shift towards easing financial conditions.
2. The U.S. economy: displaying 'Goldilocks' characteristics (not too hot, not too cold), but it was steady enough to inspire confidence.
3. The continued rise of artificial intelligence (AI): driving innovation, reshaping industries, and resulting in robust demand for its infrastructure. Importantly, many of the quality companies leading this trend have strong balance sheets, a competitive edge, and a track record of innovation through economic cycles – making them less vulnerable to broader macroeconomic headwinds.

These factors, alongside strong corporate earnings, have helped global stocks reach new highs. **But what does this mean for investments?**



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The third quarter saw major central banks begin to chart different courses. In the U.S., the Fed cut interest rates by 0.25% in September, paving the way for further reductions in 2025 and beyond. The Fed has prioritised supporting the jobs market, even as inflation remains above target. In contrast, the Bank of England (BoE) and the European Central Bank (ECB) have kept rates steady. The BoE is concerned by persistent inflation, while the ECB thinks inflation and interest rates are currently at a stable level. This divergence in central bank policies has important investment implications. The U.S. dollar is widely expected to weaken against sterling and the euro as the Fed reduces interest rates, while the BoE and ECB hold firm. Gold prices have risen to a record high, driven by expectations of a weaker dollar, Fed rate cuts, and growing concerns about fiscal sustainability.

The U.S. economy continues to tread a delicate path. True, there are signs of weakening, but it's far from entering a downturn. This fine balance has revived the 'Goldilocks' debate: can the U.S. sustain steady growth with stable inflation, even in an era of tariffs? The U.S. jobs market has undoubtedly softened in recent months as job gains slowed, vacancies fell and wage pressures eased. The slowdown in hiring could be part of a natural rebalancing after the post-Covid hiring surge, when job openings far exceeded the number of unemployed. It may also reflect temporary caution from companies amid lingering tariff uncertainty. While a weaker job market increases economic risks, it's not sinister enough to trigger a recession. Encouragingly household spending and retail sales remain resilient, showing that consumers are still confident. Wages continue to outpace inflation – historically an important condition for spending growth. Business optimism is improving, with forward-looking indicators like the Purchasing Manager Index (PMI) showing faster growth in order books.

Overall, the U.S. economy remains on solid footing, despite some weak patches of data. This 'temperate' economy is what economists call a 'Goldilocks' economy – not too hot to force the Fed to keep rates high, but not too cold to risk an economic contraction. This balance is positive for markets because there is plenty of room for future interest rate cuts, and real wage growth and tax cuts continue to support the case for a broadly resilient economy heading into 2026. Historically, this type of environment – where rates are falling but a recession is absent – has been bullish for markets.

It all comes down to corporate profits which have been stronger than expected this year despite tariff chaos. Technology continues to lead the way, with AI-related investments and infrastructure spending translating into real revenue and profit growth. Companies exposed to cloud services, semiconductors and enterprise software are reaping the rewards. In addition, we have seen broader market participation, while the largest technology companies dominate performance, the stock rally is spreading. Small and mid-cap U.S. companies have also reached record highs, reflecting optimism about Fed rate cuts and continued inflows into the U.S.



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Looking Forward

We are very comfortable with much of our portfolio positioning, and it has been pleasing to see areas where we feel offer compelling investment opportunities (Asia, Europe and the UK) producing very solid year-to-date returns. Valuations of companies in these markets are still attractive relative to that of their US peers and, as such, we are happy maintaining our exposure as we expect these investments to continue to deliver attractive returns. However, there is no doubt that valuations appear to be rich in large parts of the US market where technology companies dominate stock market indices.

There is much talk of a repeat of the late nineties dot-com bubble where huge amounts of capital flowed into companies with no track record and little or no earnings. Whilst we do not necessarily believe the current exuberance for AI exposed companies is history repeating itself – after all, these are amongst the most profitable companies in the world – there is no doubt that share prices are reflecting extremely high expectations that future profits will justify the enormous capital expenditure these companies are investing into AI. With this in mind, we feel it is prudent to take some profits from our US/technology exposed investments and hold as dry power in a Money Market Fund (currently yielding over 4%) for when markets (inevitably) question the status quo and provide us with an attractive entry point. We are currently in the process of repositioning portfolios accordingly.

Broadly speaking, the outlook remains balanced. Political, policy, and macroeconomic uncertainties are always part of the investing landscape. But markets don't need perfection to perform well. In a world full of noise, it's important to focus on the bigger picture, like fundamentals and secular drivers. Innovation, resilient corporate earnings, and easing financial conditions continue to provide reasons for long term optimism.

As always, we're here to navigate these opportunities and challenges, ensuring portfolios deliver solid returns but with a keen eye on the downside risks.

The Winchester Investment Team