

Hymans Robertson Investment Services (HRIS)

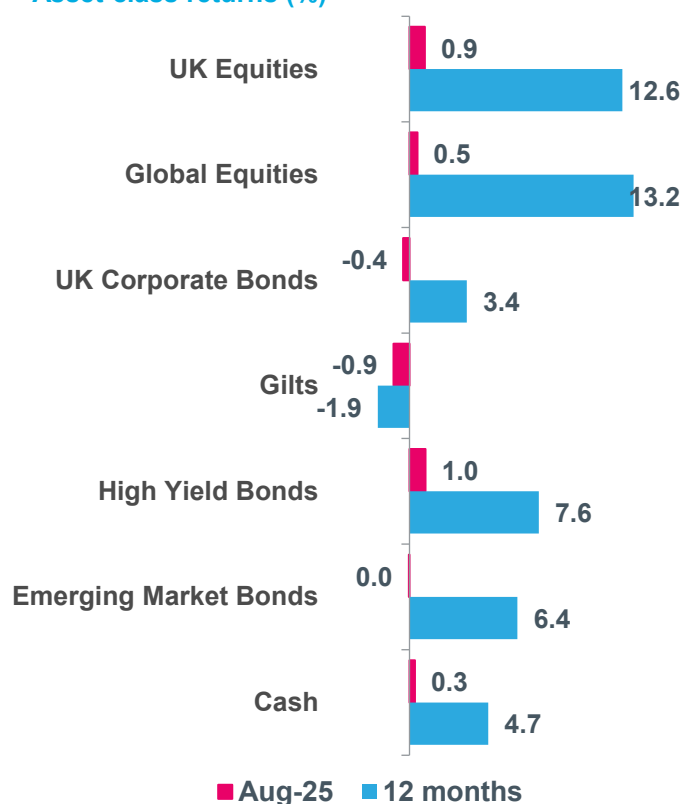
Market digest

August 2025

Monthly highlights

- Equities generated a small positive return over the month despite early signs of labour market weakness in the US.
- Government bond markets struggled, as concerns over government spending continue to grow.
- On page 3 of this document, we provide market commentary to cover the 12 months to 30 June 2025.

Asset class returns (%)



Source: Morningstar. Figures to 31 August 2025. Returns in sterling terms except high yield bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.

Market summary

- Our model portfolios typically invest in a combination of the asset classes shown in the left-hand chart.
- Equity markets eked out small gains for investors in August. Corporate earnings, on average, beat expectations however future uncertainty over the impact of tariffs, as well as signs of a weaker US labour market tempered investor confidence.
- Japan was the strongest performing equity region, while US markets were flat as a weaker dollar offset market gains.
- The Bank of England reduced interest rates to 4% in August but signalled that the bar for another cut has risen, lowering expectations of further cuts this year.
- Bond markets struggled, especially gilts. Long-dated bond yields rose (bond prices fall as yields rise) as widespread concerns over government debt levels continued.
- High-yield bonds continued to perform well as US corporates delivered good earnings.
- With equities outperforming bonds in August, higher risk portfolios typically performed better than lower risk portfolios, over the period.

Outlook and topical market themes

- Long-term government bonds yields have been steadily rising, even as central banks cut interest rates. This points to investors' concerns over a potential supply/demand imbalance. At the same time, higher yields may provide an attractive entry point for investors.
- The Federal Reserve look set to cut interest rates in September for the first time this year. Despite this, President Trump has stepped up his pressure on Fed independence.

Why long-term bond yields are rising and what it means for investors

Since last summer, the Bank of England (BoE) has lowered interest rates from 5.25% to 4.0%. Yet, contrary to expectations, long-term bond yields have risen. The yield on 20-year gilts is more than 1% higher over the past year, recently reaching its highest level since 1998 (see chart below). This highlights the limited control the BoE's interest rate policy has on longer term borrowing rates. Instead, long-term bond yields are influenced more by investors' expectations for inflation and economic growth, as well as how much debt the government is issuing and investors' appetite for buying it.

The trend isn't unique to the UK. Bond markets across Europe as well as the US and Japan are seeing similar moves, but the UK faces additional challenges. Inflation here seems more persistent than in other major economies, which makes investors demand higher returns to hold gilts. This is coming at a time when the government is issuing a lot of debt while at the same time, the BoE is selling their gilt holdings. Meanwhile, traditional buyers of these bonds, in particular UK pension schemes, are stepping back. This means the UK is relying more on overseas investors which can make yields increasingly volatile. For bond investors, although rising yields can push down bond prices in the short-term, the high yields offer potentially attractive forward-looking returns and opportunities for investors. Furthermore, a globally diversified exposure to bonds can help spread portfolio risk and capture a range of opportunities.

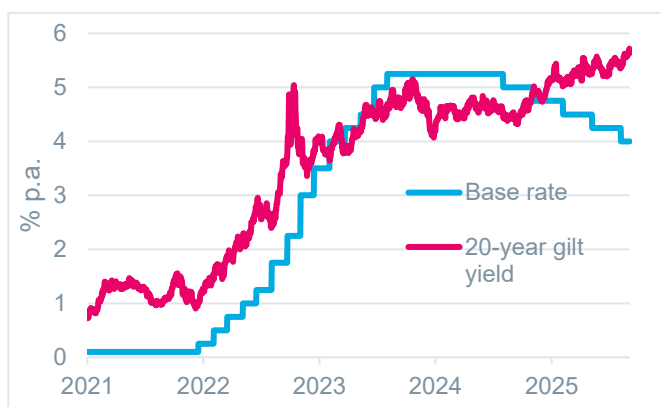
The Federal Reserve (Fed) is set to cut in September

Just as the BoE seems to be pausing its rate-cutting cycle, the Fed looks set to cut interest rates in September, for the first time this year. In a recent speech, Fed chairman Jerome Powell mentioned a shifting balance of risks i.e. the Fed is starting to become more concerned around economic growth than inflation.

This is happening against a backdrop of intense political pressure to cut from President Donald Trump, who has increased his criticism of the Fed and its leadership since returning to office. In recent weeks he has tried to fire a member of the Fed's Board – something that has never happened before. These actions have called the Fed's independence into question. Currently it still looks challenging for President Trump to gain full control of the Fed, but his efforts have raised questions about how independent the central bank will remain. For investors, the key takeaway is that the Fed is beginning to shift its focus towards supporting growth. If rate cuts continue, this could be supportive for both bond and equity markets.

Chart of the month

Long-term government bond yields continue to rise through the BoE rate-cutting cycle



Source: Bank of England

The chart shows the Bank of England's base rate alongside the yield on a 20-year UK government bond (gilt).

While the base rate has been falling since 2024, gilt yields have continued to rise. This divergence highlights the limits of central bank policy in influencing long-term borrowing costs. Instead, factors like expectations for inflation, economic growth, government borrowing and investor demand play a much bigger role in shaping long-term bond yields.



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Annual market summary: covering the 12 months to 30 June 2025

The second half of 2024 focused more on the re-election of Donald Trump rather than how quickly central banks could and would cut rates. A close election was expected, but what we got was an emphatic victory for Trump. Markets quickly pivoted towards 'Trump trades' reflecting the expected winners and losers from Trump's expected policy agenda.

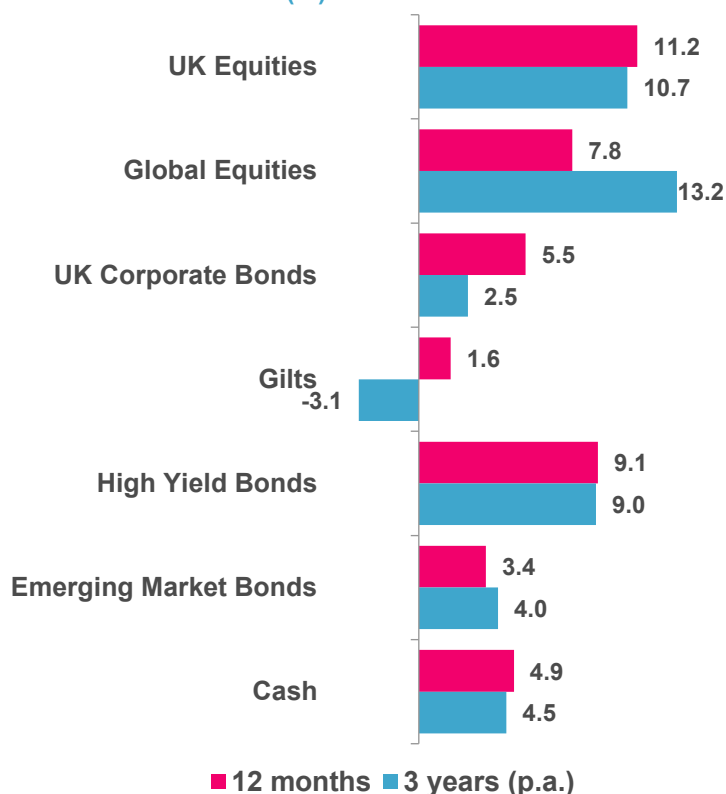
However, investors' early enthusiasm for President Trump's policy agenda started to wane in early 2025, and then completely evaporated, as Trump prioritised implementing heavy tariffs on trade partners, as opposed to working on the more market friendly policies such as tax cuts and deregulation. "Liberation Day" at the start of April further disrupted markets with no economy seemingly safe from Trump's tariffs. Postponement of the announced tariffs and indications of positive trade talks helped markets recover in May and June, but volatility persisted throughout the period.

Central banks started their path towards lower interest rates. The Bank of England cut by 1% over the period to 4.25%, as did the US Federal Reserve (to 4.5%). One difference is that the Federal Reserve stopped cutting rates after December and have adopted a more wait-and-see approach to assess the impact of tariffs, whereas the Bank of England has cut rates more steadily over the period.

Overall, the 12 months to June 2025 were positive for equity performance, despite the tariff driven volatility. The UK equity market ended the period as the top performing region, after the US market fell heavily in Q1 25.

Bond performance was strong across the different asset classes, buoyed by the falling interest rate environment. Heightened geopolitical uncertainty in June prompted investors to increase demand for safe-haven assets such as government bonds, increasing their price. Corporate bonds outperformed government bonds over the period with fundamentals still strong e.g. earnings growth forecasts. High yield bonds delivered even stronger 12 month returns as yields fell over the period (bond prices rose) and some emerging market bonds benefitted from a weakening of the US dollar.

Asset class returns (%)



Source: Morningstar. Figures to 30 June 2025. Returns in sterling terms except High Yield Bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.

Risk warning

The value of your investments and the income from them may go down as well as up and neither is guaranteed. Investors could get back less than they invested. Past performance is not a reliable indicator of future results. Changes in exchange rates may have an adverse effect on the value of an investment. Changes in interest rates may also impact the value of fixed income investments. The value of your investment may be impacted if the issuers of underlying fixed income holdings default, or market perceptions of their credit risk change. There are additional risks associated with investments in emerging or developing markets. The information in this document does not constitute advice, nor a recommendation, and investment decisions should not be made on the basis of it. The material provided should not be released or otherwise disclosed to any third party without prior consent from HRIS.