Oxfordshire County Council Pension Fund

Quarterly Investment Report

Q2 2026

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Key Indicators at a Glance

Index (Local Currency)		Q2	YTD
Equities		**Total Return**	
UK Large-Cap Equities	FTSE 100	4.0%	7.6%
UK All-Cap Equities	FTSE All-Share	4.7%	7.2%
US Equities	S&P 500	15.2%	10.2%
European Equities	EURO STOXX 50 Price EUR	15.2%	11.1%
Japanese Equities	Nikkei 225	37.4%	40.3%
EM Equities	MSCI Emerging Markets	24.1%	23.8%
Global Equities	MSCI World	13.8%	9.7%
Government Bonds			
UK Gilts	FTSE Actuaries UK Gilts TR All Stocks	2.0%	0.1%
UK Gilts Over 15 Years	FTSE Actuaries Uk Gilts Over 15 Yr	2.3%	-1.9%
UK Index-Linked Gilts	FTSE Actuaries UK Index-Linked Gilts TR All Stocks	-1.1%	0.2%
UK Index-Linked Gilts Over 15 Years	FTSE Actuaries UK Index-Linked Gilts TR Over 15 Yr	-2.1%	-2.4%
Euro Gov Bonds	Bloomberg EU Govt All Bonds TR	1.9%	1.2%
US Gov Bonds	Bloomberg US Treasuries TR Unhedged	0.3%	0.3%
EM Gov Bonds (Local)	J.P. Morgan Government Bond Index Emerging Markets Core Index	4.2%	1.8%
EM Gov Bonds (Hard/USD)	J.P. Morgan Emerging Markets Global Diversified Index	4.6%	3.3%
Bond Indices			
IBOXX Sterling Corporates	IBOXX Sterling Corporates Overall Total Return Index	2.9%	1.0%
European Corporate Investment Grade	Bloomberg Pan-European Aggregate Corporate TR Unhedged	2.6%	1.4%
European Corporate High Yield	Bloomberg Pan-European HY TR Unhedged	3.4%	1.9%
US Corporate Investment Grade	Bloomberg US Corporate Investment Grade TR Unhedged	1.4%	0.9%
US Corporate High Yield	Bloomberg US Corporate HY TR Unhedged	2.5%	2.0%
Currencies			
GBP/EUR	GBPEUR Exchange Rate	1.4%	1.2%
GBP/USD	GBPUSD Exchange Rate	0.3%	-1.6%
EUR/USD	EURUSD Exchange Rate	-1.1%	-2.8%
USD/JPY	USDJPY Exchange Rate	2.4%	3.7%
Dollar Index	Dollar Index Spot	1.2%	2.9%
USD/CNY	USDCNY Exchange Rate	-1.6%	-2.9%
Alternatives			
Infrastructure	S&P Global Infrastructure Index	1.6%	10.0%
Private Equity	S&P Listed Private Equity Index	2.3%	-14.7%
Global Real Estate	FTSE EPRA Nareit Global Index TR GBP	7.8%	10.8%
Volatility		**Change in Volatility**	
VIX	Chicago Board Options Exchange SPX Volatility Index	-34.9%	10.0%
Commodities			
Brent Crude Oil	Generic 1st Crude Oil, Brent, USD/bbl	-38.4%	19.8%
Natural Gas (US)	Generic 1st Natural Gas, USD/MMBtu	13.6%	-11.2%
Gold	Generic 1st Gold, USD/toz	-13.1%	-7.0%
Copper	Generic 1st Copper, USD/lb	10.3%	9.0%
Gold	Spot gold price quoted in USD per troy ounce	-14.1%	-7.2%
S&P GSCI	Broad, production-weighted S&P GSCI commodity benchmark	-16.9%	12.9%
Sugar Futures	Front-month ICE Sugar #11 raw-sugar futures contract	-7.6%	-4.5%
Arabica Coffee	Front-month ICE Coffee "C" Arabica futures contract	4.3%	-10.8%
Sector Indices			
S&P500 Consumer Discretionary	S&P 500 Consumer Discretionary sector	9.1%	-1.1%
S&P500 Consumer Staples	S&P 500 Consumer Staples sector	-0.3%	6.7%
NASDAQ-100 Technology	Equal-weighted NASDAQ-100 Technology Sector	55.1%	45.6%
S&P 500 Health Care	S&P 500 Health Care sector	8.3%	2.6%
S&P 500 Financials	S&P 500 Financials sector	8.6%	-2.1%
S&P 500 Energy	S&P 500 Energy sector	-14.0%	18.0%
S&P 500 Industrials	S&P 500 Industrials sector	14.5%	19.5%
S&P 500 Utilities	S&P 500 Utilities sector	-1.2%	6.2%
S&P 500 Communication Services	S&P 500 Communication Services sector	8.1%	0.4%
S&P 500 Real Estate	S&P 500 Real Estate sector	7.6%	9.7%

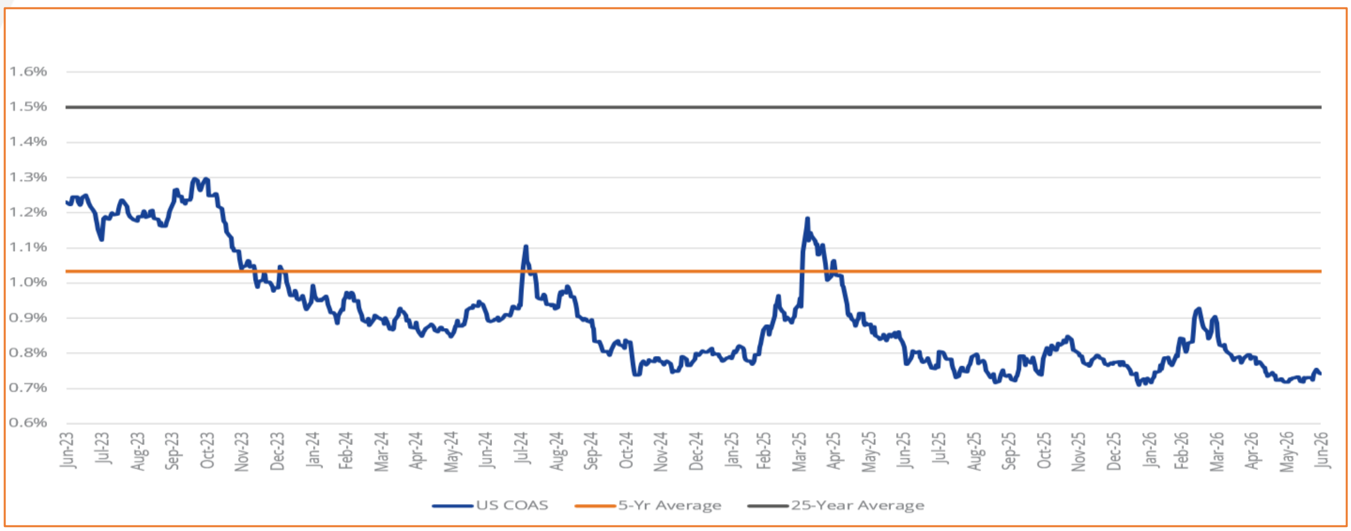
Source: Bloomberg. All return figures quoted are total return, calculated with gross dividends/income reinvested and in local currency.

Performance

The Fund returned 6.3% over the second quarter of 2026, underperforming the Fund benchmark by -1.7%. The rise is consistent with a strong market environment with Global Equities (MSCI World Index) up 13.8% in local currency terms and Bond prices rising between 0% and 5% over the period as the US and Iran reached a partial truce and oil started to flow through the Strait of Hormuz. We now know this to have been a temporary ceasefire and whilst something more lasting is ever hoped for, bringing together a fickle and unpredictable US president with a religious zealot would seem a hard task!

UK Gilts rose 2% erasing the falls of the last quarter with Emerging Market debt rising nearer 5%. Corporate credit outperformed Government debt marginally due to the higher yield as credit spreads remain historically tight (see Chart 1 below). The exception to the positive return environment was Index-Linked Gilts which continued to weaken slightly.

Chart 1: US credit spreads (yield on US High Grade Corporate Credit less the yield on the equivalent US Government Bond).



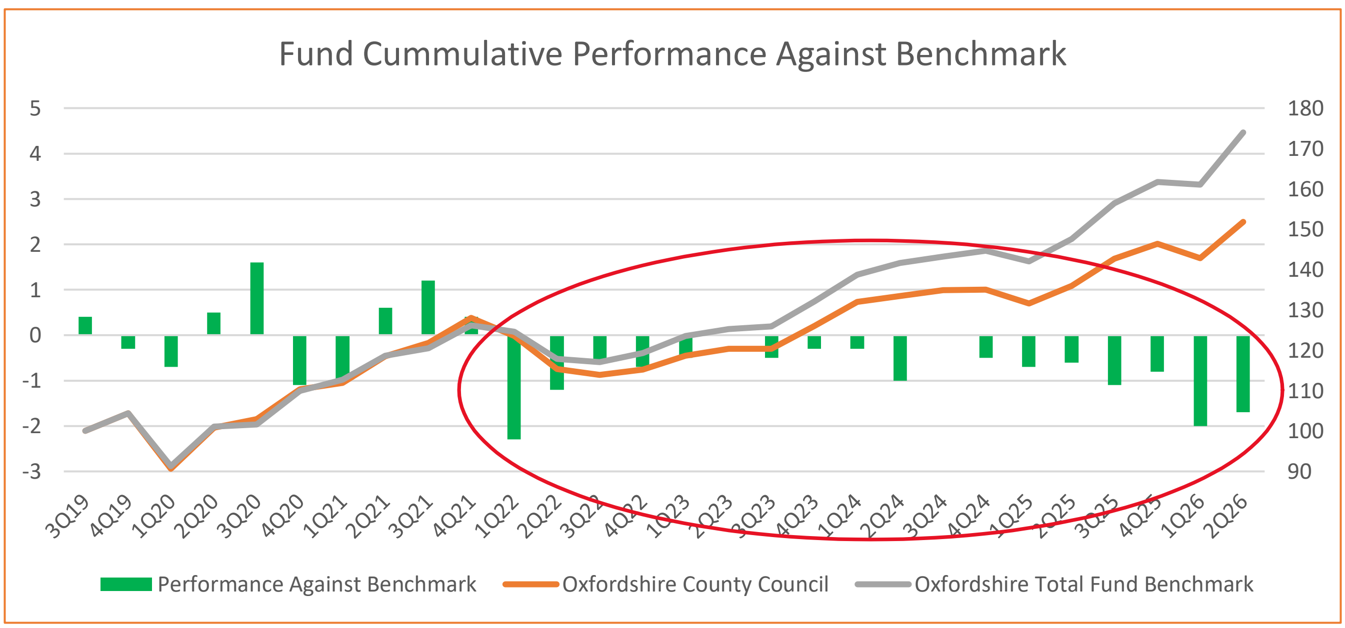
The Japanese Equity market was the strongest returning an exceptional 37% over the quarter driven by a weaker Yen, ongoing shareholder reforms and strong corporate earnings, in part through AI demand for Japanese precision engineering. The UK market returned 4% over the period as it has a high weighting to oil and energy stocks (Shell and BP) which fell over the quarter and limited exposure to IT and AI related demand.

Within Equity markets there was a noticeable sector rotation during Q2 back to the AI theme which led dominated stock performance in 2025, driven by strong earnings reports.

The Fund rose back above the £4bn mark to a valuation of £4.18bn. The underperformance against the benchmark was driven by poor returns from the Fund's Private Equity holdings, both those held directly through UK listed investment Trusts and those invested into more recently via Brunel. In each case the portfolios were pretty flat over the quarter when their benchmark (MSCI All World Equities) reflecting the quoted world equity market, rose over 14% in Sterling terms. With 10% of the Fund in Private Equity this equated to -1.5% of the Total Fund underperformance against its benchmark over the quarter. It is not unusual for Private Equity to lag a market which is rising or falling quickly as this is an illiquid asset class with minimal pricing points during a single quarter. However, Private Equity has performed poorly this year in particular as the hangover from rising interest rates continues to affect an industry when past returns were partly driven by high levels of indebtedness. The Fund's directly held Private Equity investments have now underperformed quoted World Equity markets over the past 5 years and are approximately in-line with quoted market returns over the last 10 years.

Longer term, the Fund has achieved a strong level of return, driven by a positive investment environment but has performed poorly against its benchmark, due to the poor performance of the main Brunel Equity portfolios of UK, Global High Alpha and Sustainable which account for over 40% of the Fund. Over 3 years the Fund has returned 9.1% p.a., -3.3% behind its benchmark, over 5 years 5.8% p.a., -2.7% behind its benchmark and over 10 years 7.8% p.a., -1.0% behind the benchmark.

Chart 2: Oxfordshire Pension Fund Performance



The chart above shows the cumulative performance of the Total Fund against its Strategic Benchmark, rebalanced to 100 (the lines) on the right-hand scale and the Fund's quarterly relative performance against its Strategic Benchmark (in blocks) on the left-hand scale. All the Fund's underperformance has occurred since the transfer of assets to Brunel and, in particular, since the Russian invasion of Ukraine in 2022 and the subsequent rise in inflation and then interest rates and it is partly this that has driven the poor performance of their selected managers, particularly within the main active equity portfolios.

This underperformance has come at a time when investors have had the benefit of strong returns with the Fund returning 7.8% p.a. over the last 10 years. This is above the Fund's actuarial discount rate assumption for future investment returns and will have helped improve the funding ratio between the triennial actuarial revaluations and remains a strong absolute rate of return over the long-term.

Over the last 5 years to end 31/3/26 the performance of the underlying managers selected by Brunel has been disappointing with approximately -1.7% p.a. of the Total Fund underperformance of -2.3% p.a. relative to the Strategic Benchmark coming from the poor performance of the main Equity portfolios: Sustainable, Global High Alpha and UK. However, I believe this to be heavily influenced by the strong environmental slant Brunel adopts when appointing investment managers which is a core part of their ethos. I continue to support this environmentally focused slant for the longer-term. Other LGPS Pools have also performed poorly across their equity mandates for much the same reason and 7 years after Pools started, we have no real proof that any of the Pools can add value through manager selection within quoted Equity markets! I would note in their defence, that it has been a very difficult period for any active managers to outperform.

Due to poor equity performance across each of the Pools' Equity portfolios, only 6 of the 63 LGPS Funds measured by PIRC outperformed their benchmark last year. Only one LGPS fund from this group has outperformed its benchmark over three years and only 6 over 5 years. But it is not just the Pools who have struggled to add value within Global Equity portfolios, the vast majority of active equity managers have underperformed due to market returns being driven by a small set of very large AI focused US technology companies. If/When this reverses and the ultra large US tech stocks underperform it will likely coincide with active managers outperforming passive for a period of time, possibly quite substantially.

During this quarter, the Fund completed the transition of the two main Global Equity portfolios from Brunel to new portfolios with new investment managers selected by LGPS Central (Central). (Global High Alpha and Sustainable.) In total over £1.3bn of the Fund's assets were transitioned to Central during the quarter. I have seen the Transition Report for the two Global Equity portfolio transitions which both show they were successful and achieved at a low cost. The Global High Alpha Equity portfolio has new managers under Central but is essentially the same mandate. The Sustainable Equity mandate has been replaced by three thematic Responsible Investment Mandates with new active equity managers selected by Central.

In addition, all other portfolios within Brunel were moved across to Central with the existing managers intact. This allows Brunel to be shut down and gives more time to manage the remaining transitions in due course.

Given the performance across both Liquid and Illiquid asset classes, there is no proof that Brunel has added value in performance terms over their 7 year history!

Asset Allocation

Table 1: The Fund's current asset allocation against the Strategic Benchmark

Asset class	Asset Allocation as at 31/12/25	Strategic Asset Allocation (SAA)	Position against the SAA	Deviation in cash terms
UK Equities	11.7%	**10%**	+1.7%	-£71m
Global Equities ex UK	43.6%	**41%**	+2.6%	-£109m
Fixed Interest	7.9%	**9%**	-1.1%	+£46m
Index-Linked Gilts	5.1%	**7%**	-1.9%	+£79m
Property	5.8%	**8%**	-2.2%	+£92m
Private Equity	10.0%	**10%**	+0.0%	-£0m
Secure Income	3.6%	**5%**	-1.4%	+£59m
Private Debt	2.5%	**5%**	-2.5%	+£105m
Infrastructure	3.7%	**5%**	-1.3%	+£54m
Cash	6.0%	**0%**	+6.0%	-£250m

These figures are taken from the State Street report. Figures may not add up due to rounding.

The current deviation from the Fund's SAA is within acceptable bounds. The high cash weighting should be seen as temporary and is associated with the transition from the Brunel pool to LGPS Central. The majority of this cash is awaiting drawdown into the Illiquid asset classes.

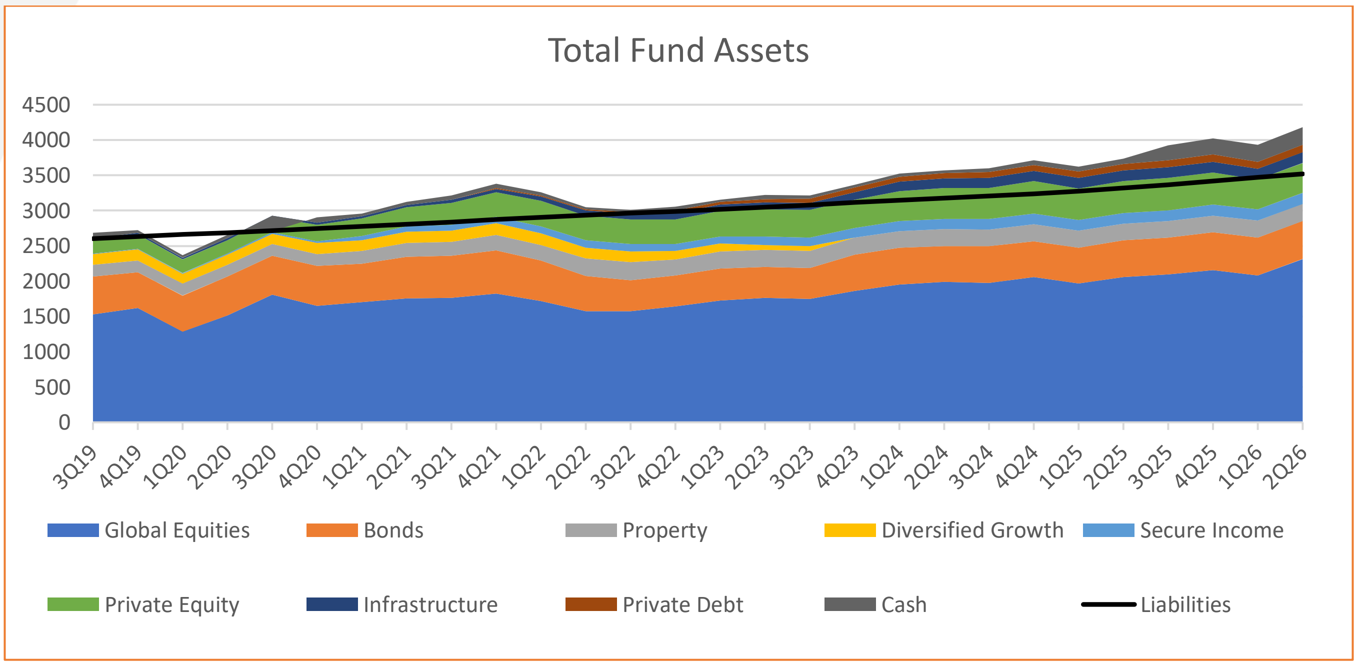
The Fund continues to progress with the agreed investment into two managers in the Social/Affordable Housing space, one investing across Shared Ownership, Affordable and Social rents and the other focusing on transitional housing to help combat homelessness. It is hoped that the new Prime Minister, Andy Burnham's focus on increasing social housing will not come at the cost of delaying further government grants to this sector.

At the December Pension Committee Meeting a new SAA was agreed which Central will use to guide the Fund's investments going forward, this included reducing the Equity exposure (UK plus Global) from 53% to 46% and reinvesting this money into Social Housing, Natural Capital and Index-Linked Gilts. This will increase the Fund's linkage to inflation which we see as a key risk for the next 10 years. In addition, the intention is to reduce Private Equity exposure via the directly held Investment Trusts and to reinvest this into Venture Capital which, although high risk, is targeting higher long-term returns.

Chart 3, on the next page, shows the assets of the Fund by asset class. I have also shown a black line which is the assumed valuation of the liabilities. Please treat this line with some caution, the liabilities are valued by the actuary every three years. At this time, they calculate the value of all earnt pension benefits plus the expected value of all future pension entitlements by the existing membership. This future liability is discounted back to today's value using a discount rate which reflects market conditions on the day of the valuation so, in essence, a snapshot once every three years. At the time of the actuarial revaluation, the actuary also calculates the future investment return which gives them the required probability of maintaining full funding into the future. To create the line in the chart, I have compounded up the actuarial valuation of the liabilities by the required investment return for each quarter.

As bond yields have risen between the 2022 and the 2025 actuarial revaluations, the actuary will have used a higher discount rate to value future pension liabilities when using the 31/3/25 data. This will reduce the current valuation of future pensions in today's money and, thereby, reduce the value of the liabilities and increase the funding level of the Fund, all else being equal; but, in addition, the actuary is likely to require a higher investment return going forward. There are also a number of other assumptions that the actuary makes when calculating the value of the pension liabilities including longevity and I have not made any estimation for these.

Chart 3: Oxfordshire Pension Fund Assets



Comment

Global markets staged a strong recovery in Q2 driven by a 'risk on' attitude among investors as progress was made between the US and Iran over a ceasefire deal which would reopen the strait of Hormuz allowing oil to flow once again. The price of oil (Brent) fell almost 40% to USD75 per barrel. This fall helped lower the outlook for inflation and hence interest rates expectations globally, giving investors more confidence. Obviously we now know this was relatively short lived! The current situation underlines how little trust there is between the US and Iranian negotiating teams and how difficult it will be to bring this to a final settlement.

The outstanding gains over the quarter were within the technology sector as investors, once again, concentrated on the outlook for AI. The NASDAQ 100 Technology index rose an exceptional 55% over the quarter reversing a softer Q1 whilst the S&P 500 energy index fell 14% in the US on the back of the falling oil price. All this feels like a return to the 2025 playbook with a focus on big Tech and AI related names driving equity markets higher lead by a small subset of the market.

However, earnings growth does remain strong in the US, partly driven by demand for AI related products and the massive investment into data centres, but this boom has also spread to banks (through higher trading revenue and fees from the Initial Public Offering (IPO) of SpaceX and potential IPO's of OpenAI and Anthropic) and those companies involved in the building and fitting out of data centres. Overall US earnings are expected to grow in the high teens in 2026 and 2027. Against this US wages are growing at 3.5% per annum, roughly in line with inflation.

The US, in particular, is going through an investment boom linked to AI. Capital investment (ex-defence and aircraft) remains strong and it is this which is driving the earnings growth rather than consumer spending which grew by 0.5% in Q1. The consultancy group McKinsey estimates that globally Companies are projected to invest nearly USD7 trillion into data centre infrastructure capital expenditures over the next five years. Of this global spending, the United States captures the largest share, with over 40% of the worldwide investment flowing into American projects.

Analysis by the St Louis Federal Reserve suggests that the recent investments in AI-related categories has contributed significantly to the real GDP growth in 2025. It has surpassed the contribution of IT components to the real GDP growth made during the Dot-com boom, both in levels and as a share of GDP. As firms continue integrating AI into their operations and building the infrastructure required to support it, these categories are likely to remain significant drivers of investment well into 2026 and beyond.

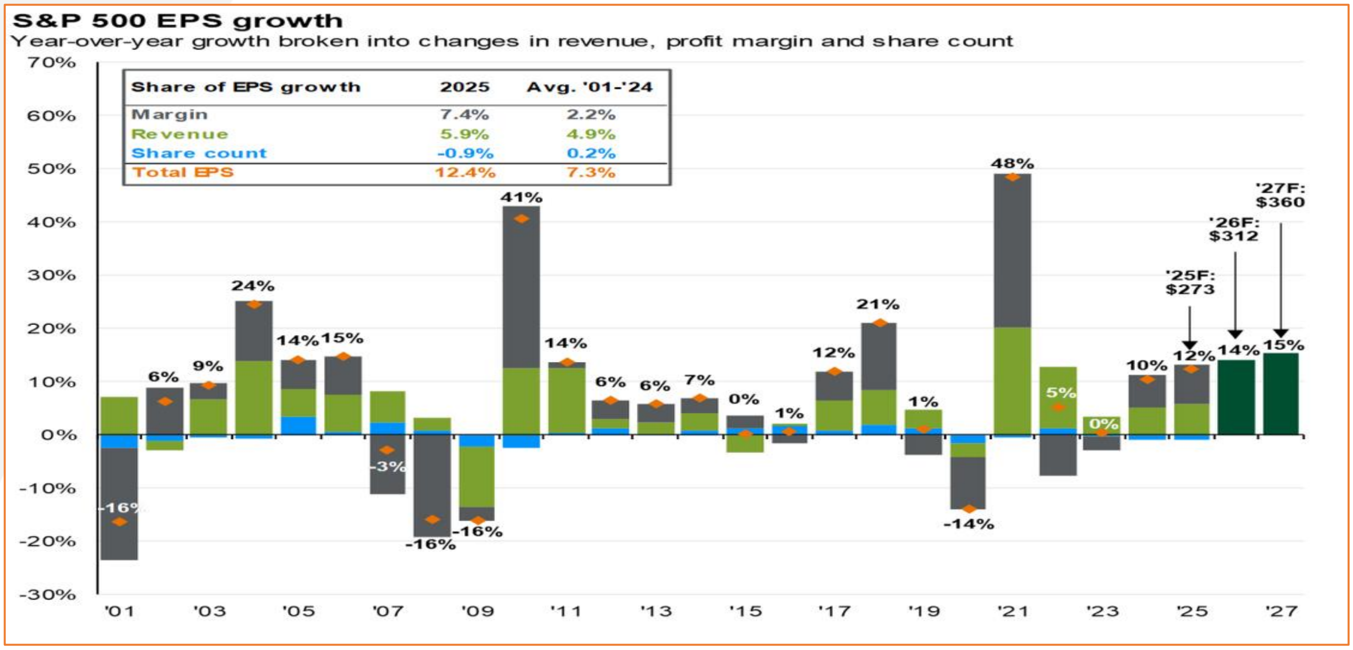
The chart below shows US manufacturing orders excluding Defence and Aircraft. The shaded areas are economic recessions. The recession in 2020 is Covid related but the recovery shown on the right hand side of the chart is strong and has had a second leg to it which would coincide with the investment boom for AI.

Chart 4: US Manufacturing orders

Source St Louis Federal Reserve

So the AI boom is real and the earnings being reported by companies involved in this sector are strong pushing US earnings growth into the mid-teens for the next two years. Some of this earnings growth is driven by revenue growth and some by further margin expansion. (See chart below.)

Chart 5: US Earnings growth



Source JP morgan

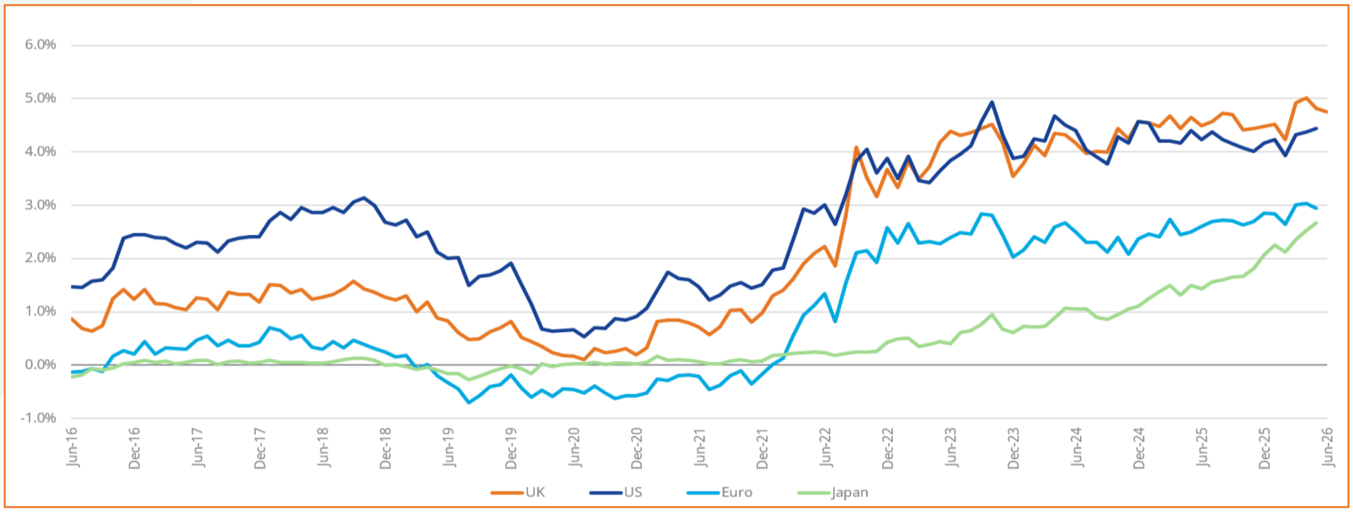
The questions remain: How much of this growth in Capital Spending is transitory? Is the US economy reaching a cyclical peak? Is the US equity market overvalued? Are US Tech stocks overvalued? How should a long-term investment portfolio be positioned in this environment?

It should be remembered that economic recessions usually only occur when interest rates are rising due to an inflationary event. We now have the economic and political backdrop to an higher inflationary environment from both long-term issues (falling demographics and global trade) and the shorter term issues of an unstable global political environment and oil price spikes. The US economy, in particular, is running hot driven by rising capital investment; corporate margins are high and rising at the expense of labour; equity markets are not cheap and in the US, arguably, expensive.

US 10 Treasury Yields are currently hitting new highs (prices falling) as the new chair of the US Federal Reserve (US Fed) is seen as playing it a bit loose with interest rates at a time of strong economic growth and signs of heightened inflationary pressure. It remains my belief that many Central Banks are quite happy with inflation running around 3% rather than their stated aim of 2% because the only way to bring down the high debt levels within most developed economies is to inflate it away over time. If we assume that inflation will average 3% over the medium term then a 10-year bond yield of 4.5% to 5% is fair value. The inflationary risks remain on the upside however and if any Central Bank admitted to targeting a 3% inflation level it would still frighten investors and lead to further weakness in bond markets.

The US breakeven inflation rate, which is the difference between a conventional 10-year Government bond and the 10-year index-Linked equivalent which gives insight into what investor's expectations are for future inflation, is at 2.2% as I write and has traded between 2.0% and 2.4% over the last 3 years. My expectation is this still needs to move higher and this will create a difficult investment environment at some stage in the future.

Chart 6: 10-year Government Bond yields

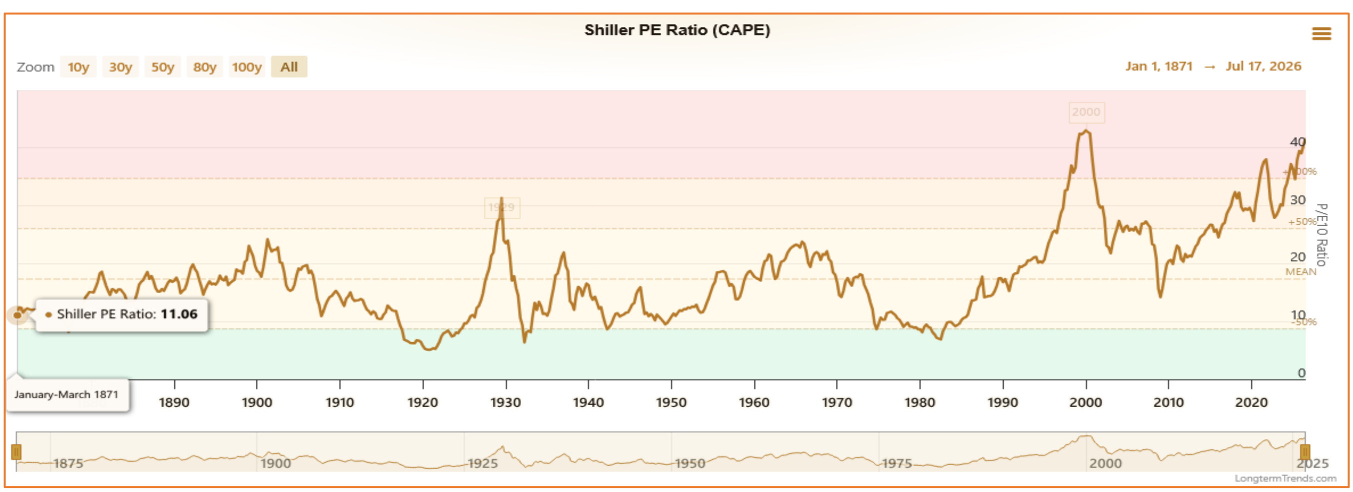


Source: Bloomberg

Notes: US Generic Govt 10 Year Yield (Ticker: USGG10YR Index); UK Govt Bonds 10 Year Note Generic Bid Yield (Ticker: GUKG10 Index); Euro Generic Govt Bond 10 Year (Ticker: GECU10YR Index); Japan Generic Govt Bond 10 Year Yield (Ticker: GJGB10 Index)

For equities, the situation is no easier. The chart below shows the Shiller or CAPE P/E for the US market over the ultralong term. The Shiller P/E divides the share price by the average of the last 10 years earnings per share and was developed by Nobel laureate Robert Shiller. This metric should, in theory, take out any economic cyclicality affecting earnings. As the chart on the following page shows, we are back at the level reached at the peak of the Dot.com bubble in 2000.

Chart 7: Shiller (CAPE) P/E



Source Longterm Trends

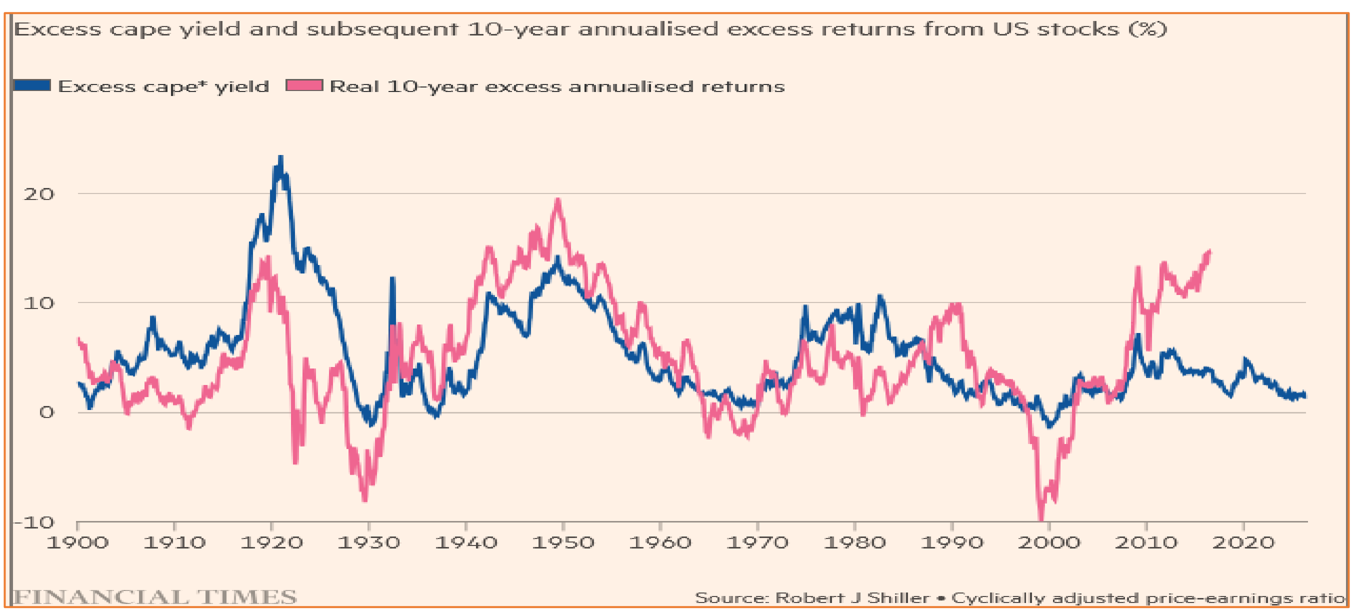
We do not know when the AI boom will end but history tells us that the stocks valued most highly at the peak are not the ones that gain from the technological advancement (think Railroads, the Industrial Revolution and the Dot.com bubble). The prime beneficiaries of AI may not have come to light yet! Profit margins in the US are at an all-time high. Margins are cyclical but there is an underlying structural change which suggests they could remain high for a prolonged period.

But, the companies included in the main US indices are much more tech and high margin focused than even 26 years ago. Therefore, shouldn't these be valued higher because each US Dollar of revenue translates into a greater percentage of cashflow and profit?

We know in the US, corporate margins are high and the equity market looks expensive when measured by the Shiller/CAPE P/E but we cannot tell when this measure should peak. Perhaps of more interest is a derivation called the Excess CAPE yield. As a valuation metric, Earnings Yield is used to look at the valuation of equities against long-term bonds and is the inverse of the P/E minus the yield on the 10-year Government Bond. In the Excess CAPE Yield the Earnings Yield is re-placed by the CAPE Yield, again removing any cyclicality.

The chart below attempts to look at the valuation of equity markets against the attractiveness of the yield on the 10-year Government Bond. Again this chart focuses on the US market as it is the most expensive and it is where we have the longest data series. The blue line is the Excess Cape yield where a low value suggests that equities offer poor value against bonds (because we are using the inverse of the Shiller/CAPE P/E). The red line is the subsequent 10 year excess return of the equity market over that provided by the 10-year Government Bond. The lines are very similar, only diverging from 2010. The chart suggests that when equities look expensive against bonds with a CAPE Earnings Yield of close to zero then the future 10-year return from equities usually falls in the range -10% to +3% over the subsequent 10-year period. We are now at that level.

Chart 8: Excess CAPE yield



This suggests that the US market, in particular, looks expensive despite the strong earnings growth. If that earnings growth slows then the US equity market will, most likely, fall. Hence the continuing focus on the prospects for AI and those companies investing the most in this area.

It should be remembered that the US equity market accounts for over 55% of the main Global Equity market index (MSCI World) with US Tech stocks accounting for over 20% of this index which is far above the weighting of all the quoted companies in Europe and the UK combined.

How should Funds react?

1. Increase exposure to assets which rise with inflation, this includes Real Estate and Social/Affordable Housing, Infrastructure and Index-Linked Bonds. **I would recommend the Fund investing into UK Index-Linked Bonds at this stage.** This could be done during the transition of the existing bond portfolios to new managers under Central. This is an area which should be discussed with Central because the UK Government Fit for the Future regulations only give 9 asset allocation buckets which LGPS Funds can use to inform their chosen Pool of their Asset Allocation strategy. These buckets do not differentiate between Conventional and Index-Linked Bonds despite their differing return characteristics.

2. Reduce exposure to US equities, particularly the US mega cap tech stocks. This can be done by moving to Global Equity indices which have a maximum caped weight for any one stock of 2%, thereby lowering the weight of the mega cap US tech stocks in particular and the US market more generally. A number of index providers offer this sort of passive index and it will be possible to link this with a Responsible Investment slant. This can be done quickly and simply. I would encourage members of the Pension Committee and officers to push Central to offer this type of vehicle in the near future.

Underlying Mandates

Rather than comment on each portfolio separately, duplicating the reporting from Brunel, the table below sets out each portfolio within the Fund with a note on my opinion of the management and performance using a traffic light system. Because of the transfer of assets to Central the main Global Equity portfolios have now changed managers making long-term performance data less relevant.

Given the transition of the two Global Equity portfolios from Brunel to Central this quarter, there is no continuous performance calculation for the period making commentary very difficult.

In the table on the following page I have marked any portfolio transitioned during the quarter as amber on performance and will keep this for the next three years until we have some idea of the underlying performance of the managers in each portfolio. This will not stop me from commenting verbally or in writing on these portfolios.

Table 2: Central portfolios

Portfolio	Benchmark	Inception	Performance	3-year rel p.a.	Comment
UK Equity	FT All-Share EX IT	09/18		n/a	Looks to have performed well over the quarter.
Global High Alpha	MSCI World Equity	11/19		n/a	Transitioned to Central
Global Sustainable	MSCI All World Equity	10/20		-n/a	Transitioned to Central
Global Paris Aligned	MSCI Paris Aligned	07/18		n/a	I do not see this as a particularly efficient way to adopt a more carbon neutral investment approach to investment.
UK £ Corporate Bond	£ Non-Gilt Credit	11/21		+1.7%	Credible performance in a strong credit environment.
Passive Index-Linked	FTSE >5-Year Index-Linked			n/a	Passive portfolio and so will match the index on performance. Returns from Index-Linked bonds have been very poor but may now be approaching attractive levels.
Multi Asset Credit	Cash + 2%	11/21		-0.0%	Performance behind the benchmark since inception by -3.1% p.a. with a poor Q1 26.
Property	Property benchmark	04/20		-0.4%	UK Performance has been acceptable outperforming since inception, but international property has been very poor.
Secure Income	Cash + 4%	07/20		n/a	These portfolios have failed to meet their inflation benchmarks suggesting issues with portfolio construction but more recent performance has improved.
Infrastructure	CPI	01/19		n/a	Drawdown has been slow; performance looks OK. Some concern over Wessex Gardens. Benchmark of CPI is an easy target.
Private Equity	MSCI All World Equity	01/19		n/a	Drawdown has been slow; was noticeably poor this quarter undermining longer-term returns. Direct Private Equity has been strong long-term but is now underperforming public equities over the last 5 years and has performed very poorly recently
Private Debt	Cash + 5%	08/17		n/a	Drawdown has been slow; performance looks good bar a noticeable fall this quarter.

Market Summary

Global markets staged a strong recovery in Q2 2026 as geopolitical and energy-security concerns eased and investor attention shifted towards resilient corporate earnings and the accelerating AI investment cycle. Brent crude retreated sharply as tensions between the US and Iran moderated and concerns over prolonged supply disruption through the Strait of Hormuz diminished.

Global equities responded strongly to improving risk sentiment. The MSCI World gained +13.8%, while the S&P 500 returned +15.2%, reversing their Q1 declines. Performance was led by technology, semiconductors and companies exposed to AI infrastructure and data-centre investment, supported by continued capital-expenditure commitments from major technology companies.

Market leadership remained concentrated, with growth stocks materially outperforming value. Emerging-market equities gained +24.1%, driven predominantly by South Korea and Taiwan, where semiconductor and memory-chip companies benefited from sustained AI demand. Japanese equities also performed strongly, while China and several commodity-producing markets lagged.

Sector dispersion was pronounced and represented a reversal of the Q1 pattern. The NASDAQ-100 Technology sector gained +55.1%, while industrials rose +14.5% and consumer discretionary returned +9.1%. In contrast, energy declined -14.0% as oil prices fell, while consumer staples and utilities were broadly flat to slightly negative.

Commodities reversed much of their Q1 strength as the geopolitical risk premium unwound. Brent crude declined -38.4%, while the S&P GSCI fell -16.9%. Gold also weakened, although copper gained +10.3%, supported by continued investment in AI infrastructure, data centres and electricity networks.

Fixed-income markets delivered modestly positive but uneven returns. Broad all-maturity UK gilts gained +2.0%, broad euro government bonds +1.9%, and broad US Treasuries +0.3%. Credit generally outperformed as spreads tightened and corporate fundamentals remained resilient, with emerging-market debt returning approximately +4.2% to +4.6%. Japan had the worst performing major bond market year-to-date, as yields rose from abnormally low levels and took account of the prime minister's ambitious spending plans. Emerging market debt was the best performing fixed income asset in Q2 at +4.0%.

Real assets benefited from the broader improvement in sentiment, with global listed real estate returning +7.8% and infrastructure gaining +1.6%. The VIX declined -34.9% during the quarter, although it remained +10.0% higher year to date, indicating that the Q1 volatility shock had not been fully reversed.

Economic conditions remained resilient but increasingly divergent. Business activity strengthened in the US and Japan, while momentum softened in the UK and eurozone. Inflation remained above central-bank targets following the earlier energy shock, resulting in continued caution and greater policy divergence between the major central banks.

Currency movements were moderate relative to other asset classes. The US Dollar Index rose +1.2%, while the Yen weakened 2.4% against the US Dollar. Sterling gained 1.4% against the Euro and 0.3% against the US Dollar, reflecting differing expectations for economic growth and monetary policy. Overall, Q2 represented a sharp reversal from the inflation-driven risk-off environment experienced in Q1. Falling oil prices, resilient earnings and renewed confidence in AI-related investment supported equities and credit. However, performance remained concentrated around technology and semiconductor beneficiaries, leaving markets vulnerable to changes in earnings expectations, geopolitical developments and monetary policy.

Regional Commentary

US equities gained approximately +15%, led by semiconductors, AI infrastructure and selected financials. Earnings were stronger than expected, although gains remained concentrated in technology-related sectors. Inflation reached around 4.2%, unemployment remained near 4.3%, and the Fed held rates at 3.50%–3.75%. Jerome Powell's term as chair of the Fed ended in May. He is replaced by Kevin Warsh whose target is to bring about significant reforms at the Fed and to shrink its balance sheet over time.

European equities rose approximately +15.2% supported by easing geopolitical risk, improving manufacturing activity and lower energy prices. Eurozone inflation increased to around 3.2%, while the European Central Bank (EC)B raised its deposit rate by 0.25% to 2.25% amid continued inflation concerns and weaker growth expectations.

UK equities, represented by the FTSE All-Share, gained approximately +5%, but underperformed the US, continental Europe and emerging markets. The market's defensive composition and larger exposure to energy and commodity companies limited participation in the technology-led recovery. UK gilts returned approximately +2.1%, benefiting from a more supportive political backdrop as the avoidance of a prolonged leadership contest eased uncertainty and provided a tailwind for gilt markets. CPI remained at 2.8%, while unemployment was around 4.9%–5.0%. The Bank of England maintained the Bank Rate at 3.75%.

Japan equities were the strongest-performing major regional market, with the Nikkei 225 rising +37.4% in Q2 and +40.4% year to date. Performance was led by technology, semiconductor-equipment and AI-related companies, supported by the rebound in global technology shares, strong demand across the semiconductor supply chain and a weaker Yen, with USD/JPY rising +2.4% during the quarter. However, the gains were concentrated among large technology-related index constituents and did not reflect uniformly strong performance across the broader Japanese market. The Bank of Japan (BoJ) raised rates by 0.25% to a still low level of 1%.

Emerging markets gained +24.1% in Q2, taking the year-to-date return to +23.9%, and materially outperformed developed markets. The advance was driven primarily by technology-heavy Asian markets, particularly South Korea and Taiwan, whose semiconductor and memory-chip companies benefited from accelerating AI infrastructure demand. Performance remained uneven, with China and commodity- and energy-sensitive markets in Latin America and the Middle East generally lagging as oil prices declined sharply. The strength of the index therefore reflected its growing concentration in the Asian technology supply chain rather than a uniform improvement across emerging economies.

Commodities declined as the geopolitical risk premium embedded in energy prices unwound. Oil fell approximately -38% over the quarter, while the broader commodity complex declined around -8%. Gold and precious metals also weakened by more than -10%, reversing part of their Q1 gains. Industrial metals performed comparatively better as investment in power infrastructure, data centres and technology supply chains supported demand.

Global listed real estate returned approximately +8.3%, supported by improving risk sentiment, greater stability in bond markets and signs of stabilising valuations. Elevated financing costs and divergent property-sector fundamentals remained key risks.

Volatility declined materially, with the VIX falling -34.9% during the quarter. However, it remained +10.0% higher year to date, indicating that the Q1 risk shock had not been fully reversed.