

Overview

At the start of the year it seemed that, after an interminable wait, we might have got past the uncertainty of the late-2025 UK Budget and markets were set fair for the coming year. Global economic growth was forecast to be positive, if modest. Inflation was clearly easing, and interest rates were generally forecast to fall. The impact of Trump's tariffs appeared to be modest, and even threats of legal action against the Chairman of the Federal Reserve Bank seemed relatively benign. The worst markets had to contend with were a US sortie into Venezuela to capture its President and the White House's irrational threats to take control of Greenland, upsetting NATO allies.

By the end of February most European equity markets were hitting record highs, with the UK (+10%) leading the way. Elsewhere, Japan (+17%) continued to reward a new Prime Minister following a successful snap election. US markets (+1%) were less buoyant as the technology sector, so influential over recent years, wobbled. Software companies tumbled on fears that artificial intelligence (AI) would negate their purpose. Geopolitical shenanigans had driven gold and oil prices up 21% and 18% respectively, with the former reaching nearly \$5,500 per troy ounce.

Then it was all change as the US and Israel attacked Iran with considerable force. There did not appear to be any co-ordination with allies in this action, and it was not clear what Trump's endgame looked like. What transpired was an Iranian regime able to withstand the attacks, even though many of its leaders were killed. It retained the ability to strike back against Gulf State neighbours' oil facilities and to assert very effective control over shipping through the Strait of Hormuz. With no knockout blow delivered by America, a highly volatile and unsettled situation has ensued.

The impact of the attacks on Iran, its resolute retaliation and the dramatic climb in the oil price (+70% over the quarter) has led to two specific fundamental changes in the outlook. First, the oil price rise is hugely inflationary, which reverses the expectations of a gentle decline. Second, the inflationary impact changes the outlook for interest rates. Prior to the attacks, rates were expected to fall during the year. Shortly afterwards expectations were for multiple increases over the remainder of 2026. Unsurprisingly, bond and equity markets sustained sharp reversals.

The following table sets out the market movements for the three months to 31st March 2026.

| Index | 31/12/2025 | 31/03/2026 | Change |
|--------------------------|------------|------------|--------|
| CBOE UK 100 | 994 | 1,015 | 2.1% |
| CBOE UK All Companies | 17,239 | 17,474 | 1.4% |
| CBOE UK 250 | 19,556 | 18,376 | -6.0% |
| ARC PCI – Steady Growth* | 350 | 348 | -0.6% |
| ARC PCI – Equity Risk* | 417 | 413 | -1.0% |

Markets

Away from geopolitics, two situations have had considerable influence on markets. Weakness in the private credit market – those providing finance to businesses outside of the mainstream banks – has raised questions about the possibility of a wider upset in the financial system. Separately, uncertainties over the likely winners and losers from the rapid expansion of AI saw software companies savaged in what seemed a “shoot first and ask questions later” approach by investors. The largest companies – the so-called “Magnificent Seven” – have weakened on reconsideration of the vast amounts they propose spending on AI. The technology-focused NASDAQ index fell 7% over the period.

Turning to the UK, at the end of February the main market indices had been leading most other mature global markets. By the end of March they still clung on to a narrow lead – but, once again, this came down to a concentration of performance from a few areas. The oil sector, principally BP and Shell, was up by a third, with both these companies significant contributors to the index. Among other large companies, AstraZeneca and HSBC both saw mid-single-digit percentage rises, while British American Tobacco was also up and usurped Unilever, which was weak, in the top six. Agreed bids for insurance company Beazley and investment manager Schroders brought modest relief.

Diversification, usually a positive risk-and-reward determinant, again proved less than helpful, with 48 stocks in the 100-share index falling by 5% or more than the average. Only 23, including those mentioned above, outperformed. Mid-and-smaller-sized companies, deemed more susceptible to economic and interest rate cycles, again underperformed. Far Eastern markets, which also enjoyed a positive start to the year, felt the pain of a stronger US dollar and higher oil prices following the start of hostilities in the Middle East.

Outlook

So where does this leave us heading into the rest of the year? Weaker economic numbers, as measured by Purchasing Manager Indices, are already coming through, although they still show signs of expansion. This weakness may stay the hand of central bankers in thinking they should raise interest rates. But higher inflation seems inevitable, even if the current two-week ceasefire extends into a more lasting peace, as it will take time to repair damaged oil and gas facilities. It is too early to see how events will impact corporate profits, but energy-intensive businesses will obviously be negatively affected.

In these circumstances, it is not surprising that, emotionally, one might want to head for the exits. However, signs of any resolution to the Middle Eastern situation have led to sharp recoveries in markets. As has often been written, research shows that missing the best 10 days of performance in a market can have a dramatic impact on the long-term performance of portfolios. Accordingly, we continue to believe that remaining invested in portfolios holding good-quality companies and collective investments, through thick and thin, will lead to good returns for clients over time.

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Notes

** ARC Private Client Indices (PCI) are benchmarks designed to assess the performance of discretionary private client portfolios across multiple asset classes, reflecting actual investor outcomes rather than model portfolios.*

Contact us

 +44 (0)20 7448 4700

 +44 (0)20 7256 5365

 support@fiskeplc.com

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