WATTERSON
FINANCIAL PLANNING

Market Update

July 2026

TITAN SQUARE MILE

The Macro

The second quarter of 2026 was unsettled. Investors faced three key issues: uncertainty around central bank policy, inflation that is proving slow to fall, and economic growth that is slowing but not collapsing.

In the UK, inflation remains above target. While headline inflation held steady in May, more persistent areas like services inflation picked up again(1). This matters because it suggests inflation pressures are not fully under control. The Bank of England kept interest rates unchanged in June, but some policymakers voted for a further increase(2). This highlights a shift in thinking - from when rates might fall to whether they may need to stay higher for longer.

Markets were volatile during the quarter. Energy prices, driven by tensions in the Middle East, played a central role. Oil and gas costs remained elevated compared to pre-conflict levels(2), increasing pressure on inflation and consumer confidence.

UK economic growth has been modest but remains positive overall. GDP grew over the three months to April, although there was a small decline in the latest monthly reading(3). In simple terms, the economy is holding up, but higher costs are starting to weigh.

Inflation data in May added to the complexity. While headline inflation remained stable, transport and services costs increased(1). Fuel prices and airfares were key driver(1), meaning the headline number looked stable, but underlying pressures remain.

In Europe, inflation also rose while growth weakened(4). The European Central Bank responded by raising interest rates in June, linking the move directly to energy-related inflation pressure(5).

In the US, the Federal Reserve held rates steady. It noted that economic growth remains solid but inflation is still above target(6). Its projections show moderate growth but continued inflation pressure(7).

Towards the end of June, there was some relief. Oil prices fell as supply concerns eased and shipping conditions improved(8). This helped sentiment, but confidence has not fully recovered.

Bond Markets

Bond markets had a challenging quarter. Initially, weaker growth concerns pushed bond yields lower, but this reversed as investors reassessed how long interest rates might stay high.

In the UK, government bond yields rose as investors demanded higher compensation for inflation and fiscal risks. However, falling oil prices later in the quarter helped yields stabilise, leaving modestly positive returns(9).

Corporate bonds were more resilient. Credit spreads remained relatively tight, and demand for new issuance was strong(10). Investors continue to find yields attractive, and company balance sheets remain generally healthy. New bond issues were often heavily oversubscribed(11).

Emerging market debt experienced more volatility. Higher US yields, a stronger dollar at times, and energy uncertainty weighed on performance. Yields rose and spreads widened over the quarter(12).

Equity Markets

Equity markets started the quarter cautiously, reflecting concerns over energy prices, inflation and central bank policy. The key fear was a “stagflation” scenario—where growth slows while inflation remains high.

Markets recovered gradually. As energy fears eased and oil prices stabilised, confidence improved. By June, global equity funds saw strong investor inflows.

The US remained the strongest market, led by large technology companies and the continued interest in artificial intelligence. This supported returns but also increased concentration risk.

UK equities were steadier but less dynamic. The market's exposure to sectors like energy, financials and healthcare proved supportive in a higher-rate environment.

Europe delivered mixed performance. Banks benefited from higher rates, while weaker growth weighed on cyclicals. Defensive sectors held up well during periods of volatility.

Emerging markets and Asia were more uneven but benefited from the global technology rebound, particularly where companies are linked to AI infrastructure and digital growth themes.

Outlook

Looking ahead, three key questions will shape markets in Q3:
• How quickly will energy prices feed into inflation?
• Will growth weaken enough to bring inflation down?
• How long will central banks keep rates elevated?

The Bank of England has made clear that policy decisions will depend on how persistent inflation proves to be, particularly in services and wages(2).

In Europe, the ECB faces a difficult balance between controlling inflation and supporting weak growth(5).

In the US, the Federal Reserve is likely to remain data-dependent. Growth is holding up, but inflation remains above target(6,7).

Energy prices and geopolitical risks remain critical. If oil prices stay stable, inflation pressures should ease. If not, volatility could return quickly.

What this means for Portfolios:

The investment environment has stabilised slightly but remains uncertain.
• Bonds now offer more attractive income, but volatility remains.
• Equities still provide growth potential, but leadership is narrow and valuations are tighter.
• Diversification remains essential.

A balanced approach - focusing on quality investments, maintaining liquidity, and ensuring diversification across regions and asset classes—remains the most effective way to navigate current markets.

Date of data: 30 June 2026.

Research Sources

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Important Information