Garry White, Chief Investment Commentator, Charles Stanley

Market Snapshot

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A deterioration of the situation in the Middle East and renewed tariff threats combined with some mixed corporate earnings to unsettle investors and increase volatility. Equity markets have retreated from recent highs, with US stocks led lower by sharp falls in technology shares after disappointing reactions to results from Tesla and Alphabet. The FTSE 100, however, proved relatively resilient.

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Bond markets sold off as investors pared back expectations of interest-rate cuts, with oil-driven inflation concerns pushing yields on government borrowing higher. US Treasury yields climbed to their highest levels since early 2025, while markets interpreted the ECB's latest comments as relatively hawkish.

Investor confidence proved one of the market's strongest tailwinds in the second quarter, helping push equities to new highs despite a challenging backdrop. Patrick Farrell, our CIO unpacks the key trends, risks and opportunities for investors heading into the second half of the year in his CIO mid-year perspective.

The FTSE 100 was up 0.6% over the week by mid-session on Friday, with the more UK-focused FTSE 250 trading 0.4% ahead

Middle East

The April ceasefire agreement between Iran and the US appears to be over. Oil prices hit the $100 a barrel level for the first time since May this week causing investors to reassess the inflation outlook once more. While a return to full-scale conflict is not inevitable, recent developments have increased the risk of further escalation and the associated economic consequences. Investors are therefore paying closer attention to the military, political and supply-chain pressures that could shape the next stage of the crisis.

In a significant new development, the Iran-backed Houthi movement in Yemen has opened what could become a second front in the regional confrontation by threatening and attacking shipping routes in the Red Sea, including vessels linked to Saudi Arabia near the Bab el-Mandeb Strait – the southern gateway to the Suez Canal. The timing is notable because it complements Iranian pressure on the Strait of Hormuz, potentially giving Tehran and its regional proxies influence over two of the Middle East's most strategically important maritime trade routes.

The longer these disruptions and complexities persist, the greater the potential economic impact. While supply chains can absorb short-term shocks, prolonged restrictions to major shipping routes could result in more meaningful inventory drawdowns and supply shortages. Over time, this would increase the risk of upward pressure on both energy prices and broader inflation.

European gas prices rose sharply, with the Dutch TTF benchmark climbing above €60/MWh, a four-month high, as traders worry about the security of global liquified natural gas (LNG) supplies ahead of next winter. The main driver has been renewed tensions involving Iran, which have raised concerns over LNG shipments through the Strait of Hormuz, a key route for Qatari exports to Europe. At the same time, Europe's gas storage facilities remain significantly less full than at the same stage last year, leaving the market more sensitive to any supply disruption. The combination of geopolitical risk, lower-than-normal storage levels and Europe's continuing reliance on imported LNG following the reduction of Russian gas imports has pushed a substantial risk premium back into the market.

Tariffs

President Trump intensified his trade agenda this week by announcing a series of new tariff measures, most notably imposing 50% tariffs on a wide range of Canadian goods, including products linked to the auto, dairy and alcohol sectors. Mr Trump said these were aimed at countering what the administration described as Canada's discriminatory treatment of US exports. The duties, which are due to take effect in 30 days, represent a significant escalation because they would apply to many goods that had previously qualified for preferential treatment under the US-Mexico-Canada trade agreement.

The president also imposed duties of between 10% and 12.5% on imports from 60 trading partners that account for roughly 99% of US imports, including the United Kingdom (UK), European Union (EU), China, Canada, Mexico, India and Japan. The measures, which take effect as a temporary 10% global tariff expires, are being justified on the grounds that affected countries have failed to do enough to block goods produced with forced labour from entering their markets.

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Mr Trump also announced plans for future tariffs on imported generic drugs as part of a broader effort to encourage manufacturing to move back to the US. The latest actions reflect Trump's continued use of tariffs as a tool to pressure trading partners, protect domestic industries and encourage reshoring of production.

UK politics

Government bond markets have remained relatively calm after new prime minister Andy Burnham publicly committed to maintaining the fiscal rules introduced by former chancellor Rachel Reeves. These rules were designed to ensure that the public finances remain sustainable while still allowing borrowing to support long-term investment.

In their current form, the rules require day-to-day government spending to be funded through tax revenues rather than borrowing, while public debt is expected to be falling as a share of national income over a defined period. Their purpose is to reassure investors that the government will manage the public finances responsibly, helping to keep borrowing costs lower and maintain confidence in UK assets. Financial markets scrutinise adherence to these rules closely when assessing the sustainability of government spending plans, and any perceived weakening of fiscal discipline could result in higher gilt yields and increased borrowing costs for the state.

The appointment of John Healey as Mr Burnham's chancellor came as a surprise to many observers, with markets having viewed Shabana Mahmood as the most likely candidate and Ed Miliband as an outside possibility. Mr Healey is nevertheless seen as a credible choice given his previous Treasury experience. However, investors are likely to monitor his approach to fiscal discipline carefully, particularly as he resigned as defence secretary after pushing for higher levels of defence spending than were ultimately agreed.

Economics

UK inflation eased more than expected in June, strengthening the case for further interest rate cuts from the Bank of England. Data from the Office for National Statistics showed the Consumer Prices Index (CPI) rose 2.6% year-on-year, down from 2.8% in May, while CPIH, which includes owner-occupiers' housing costs, slowed to 2.8% from 3.0%. The decline was driven primarily by lower transport costs and a moderation in food price inflation, although underlying price pressures remained evident, with core inflation unchanged at 2.6% and services inflation only edging down to 3.6%. While inflation remains above the Bank of England's 2% target, the softer-than-expected reading boosted expectations that policymakers could continue easing monetary policy in the coming months if the downward trend is sustained.

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The European Central Bank (ECB) left interest rates unchanged at its July meeting, as policymakers opted to assess the impact of recent policy tightening and ongoing energy-market volatility. In her post-meeting press conference, ECB president Christine Lagarde stressed that the central bank remained data-dependent and was "not pre-committing" to any particular path for interest rates, while warning that higher energy prices linked to Middle East tensions could still feed through into broader inflation. Although eurozone inflation eased to 2.8% in June, Lagarde said price growth was likely to remain above the ECB's 2% target for some time.

As heatwaves become more frequent and intense, they are disrupting productivity, infrastructure and supply chains and create risks investors can no longer afford to ignore.

Company news

Alphabet delivered a strong set of second-quarter results that underscored both the resilience of its advertising business and the growing commercial impact of AI. Revenue rose 24% year-on-year to $119.8bn, comfortably beating expectations, with Google Cloud emerging as the standout performer as sales surged 82% to $24.8bn on the back of strong demand for AI infrastructure and enterprise AI services. Search revenue increased 17%, YouTube advertising rose 13% and operating income climbed 30%, highlighting the continued strength of Alphabet's core franchises even as it pours vast sums into AI. The company also raised its capital expenditure guidance to as much as $205bn this year, reflecting an industry-wide race to build computing capacity.

For the wider technology sector, the results reinforce the view that AI investment is translating into real revenues rather than remaining a speculative theme. Alphabet's accelerating cloud growth suggests demand for data centres, semiconductors, networking equipment and AI software remains exceptionally strong, providing a positive read-across for companies such as **Nvidia**, **Microsoft**, **AMD** and a range of infrastructure suppliers. At the same time, the sharp increase in capital spending highlights how the biggest technology groups are engaged in an increasingly expensive battle for AI leadership, raising the competitive bar for smaller rivals and signalling that demand for AI computing power continues to outstrip supply.

Ahead of next week's results from **Microsoft**, **Meta Platforms**, **Apple** and **Amazon**, the key theme for investors will be whether strong AI-driven demand continues to justify elevated levels of investment. Following **Alphabet's** strong results, demand for AI infrastructure and services remains clear, but markets are becoming increasingly focused on the pace of monetisation and the scale of capital expenditure required to support future growth. We expect management commentary on AI adoption, cloud demand and investment plans to be at least as important as the headline earnings numbers themselves. More broadly, as AI reshapes the technology landscape, identifying the companies best positioned to convert investment into sustainable earnings growth will remain critical for investors. companies can translate AI investment into sustainable revenue and earnings growth, rather than treating the sector as a single theme.

Tesla reported record second-quarter revenue of $28.2bn, up 26% from a year earlier and comfortably ahead of Wall Street expectations, as vehicle deliveries rose 25% to a record 480,126 units and growth continued in its energy storage and services businesses. However, investors focused on a much weaker profit performance, with adjusted earnings per share of $0.33 missing forecasts by a wide margin and operating income plunging 57% as spending on artificial intelligence, robotaxis, Optimus humanoid robots and other long-term projects drove a 47% increase in operating expenses. Margins also came under pressure. Shares in the Elon-Musk-controlled group fell about 11% following the statement.

Mitie's board has recommended shareholder take up a £3.1bn cash takeover by facilities management rival **OCS**, which is owned by US private-equity firm **Clayton, Dubilier & Rice**. Under the terms of the deal, Mitie shareholders will receive up to 221.6p a share, including a final dividend, representing a premium of about 47% to the company's previous closing price. The deal is the latest example of overseas buyers and private equity investors snapping up UK-listed companies as they exploit what many view as a persistent valuation gap in the London market. Relatively weak share prices, a shortage of domestic equity investment and concerns over the attractiveness of London's stock market have left many British companies trading at discounts to international peers, making them attractive targets for foreign acquirers. Mitie joins a growing list of UK takeover targets, reinforcing concerns that undervalued British businesses are increasingly being acquired by overseas investors able to pay substantial premiums while still securing assets they believe are worth significantly more than their market valuations suggest. FTSE 100 bid targets this year include **easyJet**, **Intertek**, **Beazley**, **Schroders** and **Segro**. In the FTSE 250 there is **Senior**, **Gamma Communications**, and **Advanced Medical Solutions**.

Defence shares rose as investors remained optimistic about a sustained increase in global military spending and as the Farnborough International Airshow has put the sector firmly in the spotlight. The event, where defence companies make up around half of a record 1,600 exhibitors, has featured announcements and discussions around combat aircraft, drones, missile defence, artificial intelligence and other next-generation military technologies. Major defence contractors with a presence at the show include **BAE Systems**, **Leonardo**, **Boeing**, **Airbus** and **Saab**, all of which are seeking to position themselves for increased procurement spending from governments responding to heightened geopolitical tensions and security challenges.

Segro announced that it has requested and been granted an extension to the 'put-up-or-shut-up' deadline for **Prologis** to make a firm offer for the UK Real-estate investment trust (Reit) or walk away, as it said it would be minded to recommend the US logistics giant's final approach. Prologis has made a "best-and-final" $18.7bn bid.

Low-cost carrier **easyJet** reported a sharp decline in third-quarter profits as higher fuel costs and disruption linked to the Iran conflict weighed on earnings. However, the airline still beat analysts' expectations and struck an optimistic note on summer trading. Profit for the three months to 30 June fell to £85m from £286m a year earlier as fuel costs surged by £105m, but management said consumer confidence was improving and demand for late bookings remained strong, prompting the company to maintain its full-year capacity guidance. The results came against the backdrop of an increasingly complex takeover battle, with easyJet backing a £7.15-a-share, £5.7bn cash proposal from US investment firm Apollo after withdrawing support for rival bidder Castlelake's lower offer. However, the situation has been complicated by reports that the European Union could tighten airline ownership rules, potentially creating hurdles for non-European buyers seeking control of the carrier. Apollo has until 7 August to make a firm offer, while Castlelake faces a 3 August deadline.

Compass Group delivered another strong set of results, with organic revenue growth driven by robust client retention, new business wins and continued demand across its education, healthcare and business & industry divisions. Management said volume growth remained positive and reiterated confidence in the group's full-year outlook, underpinned by strong cash generation and margin expansion.

BT Group reported a mixed but solid start to its 2026 financial year, with first-quarter revenue falling 3% to £4.9bn as weaker handset sales and challenging conditions in its international business offset growth from fibre broadband services. Management highlighted strong operational progress, with its full-fibre network now reaching more than 19 million premises and record Openreach fibre take-up helping connected premises rise to 7.1 million. Consumer broadband and mobile customer numbers both increased, while cost-saving initiatives helped offset higher wage and national insurance costs.

3i Group delivered a solid second-quarter performance, with its majority-owned discount retailer Action maintaining positive like-for-like sales growth and helping lift the investment group's net asset value (NAV) despite adverse foreign exchange movements. The listed private equity group's NAV per share increased to 3,131 pence as of 30 June, delivering a total return of 3% over the three-month period.

RELX reported strong financial results for first half of 2026, with revenue reaching £4.87bn, representing underlying growth of 7%. Management reaffirmed its full-year outlook, expecting continued strong underlying growth in revenue, adjusted operating profit, and adjusted earnings per share.

Roche reported resilient first-half results despite a strong Swiss franc weighing on headline numbers. Although reported sales and earnings were lower in Swiss franc terms because of currency movements, the Swiss pharmaceuticals group reaffirmed its full-year guidance for mid-single-digit sales growth and high-single-digit growth in core earnings per share. Chief executive Thomas Schinecker said Roche remained well positioned for further expansion thanks to a robust pipeline of new medicines, with investors increasingly focused on the rollout of recently launched treatments and the potential of the company's late-stage drug portfolio to drive the next phase of growth.

Nestlé said it expects to raise around €3bn from a joint venture with investment firm Platinum Equity for its water and premium beverages business, a long-awaited deal it has been courting since 2024. The company's second quarter results disappointed as profit margins were squeezed by high coffee and cocoa prices. New chief executive Philipp Navratil and chair Pablo Isla, the former Inditex boss, have simplified the group's sprawling organisational structure and sold off parts of its portfolio. The company also posted slightly better than expected second-quarter organic sales growth as prices and sales volumes increased. The world's biggest packaged food company said it now expects full-year organic sales to grow 3% to 4%, instead of its previous target of "around 3%".

Otis Worldwide reported solid second-quarter results, with revenue rising 7% to $3.9bn as strong demand for maintenance, repair and modernisation services offset weakness in its new equipment business. The elevator and escalator maker posted organic sales growth of 6%, driven by a 9% increase in service revenue – matching the fastest pace since the company was spun off – while modernisation orders rose 9% and backlog increased sharply, providing visibility for future growth.

US life sciences company **Thermo Fisher** unveiled better-than-expected second-quarter figures, with revenue, organic growth, margins and earnings all ahead of forecasts. The standout was organic growth of 5%, significantly ahead of the 3% expected by Wall Street analysts, with strength evident across all major segments. Analytical Instruments was the biggest positive surprise, delivering 7% organic growth and suggesting improving demand for capital equipment, while Lab Products & Biopharma Services also exceeded expectations, indicating continued recovery in pharma and biotech spending.