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Geopolitical risks, resilient growth, and AI investment shape markets

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Global markets in August remained resilient despite a challenging backdrop of persistent geopolitical tensions, renewed trade frictions, and uncertainty surrounding the path of US monetary policy. The US-Iran conflict and continued disruption around the Strait of Hormuz remained important drivers of sentiment, with Iran maintaining demands for compensation and sanctions relief while Washington intensified economic and military pressure. Prospects for a diplomatic breakthrough weakened as the month progressed, with the US preparing additional sanctions against countries and businesses supporting Iran before renewed military exchanges brought geopolitical risks back into focus toward month-end. Persistent shipping disruptions kept energy-security concerns elevated and continued to support oil prices.

Economic conditions nevertheless remained broadly resilient across the major economies. Flash PMI readings pointed to continued expansion globally, with US business activity reaching its strongest level in more than four years, while the UK, Eurozone, Japan, India, and Australia also recorded positive growth momentum. In the US, however, the picture remained mixed. Second-quarter GDP was confirmed at 1.5% annualised, while concerns over fiscal sustainability intensified after public debt exceeded USD40tn for the first time. Inflation initially showed signs of moderation, with both CPI and PPI easing, but underlying price pressures remained elevated toward month-end, with PCE inflation at 3.7% YoY and core PCE at 3.3%.

The shifting inflation backdrop complicated expectations for Federal Reserve policy. Earlier signs of softer inflation reinforced expectations that the Fed could remain on hold for the remainder of the year. However, Chair Warsh subsequently signaled that further tightening remained possible if inflation failed to moderate, bringing monetary-policy uncertainty back into focus. Outside the US, inflation pressures remained visible in several economies, including Japan and Germany, while UK inflation accelerated amid higher household energy costs, highlighting continued divergence in global inflation dynamics.

Across Europe and Asia, economic signals were mixed but generally constructive. Germany's business sentiment improved toward the end of the month, while China introduced additional measures to support its struggling property market. Chinese manufacturing conditions also improved marginally, with the PMI rising to 49.8, although activity remained below the threshold separating expansion from contraction. Japan recorded a record current-account surplus despite softer GDP growth, while broader Asian growth remained supported by relatively resilient external demand.

Trade tensions added another layer of uncertainty. US-Canada relations deteriorated after negotiations collapsed and Canada announced retaliatory tariffs on US goods, with tensions intensifying further toward month-end. At the same time, the prospect of additional US sanctions linked to Iran raised the risk that geopolitical tensions could increasingly spill over into global trade and economic relationships.

Artificial intelligence remained an important counterweight to these macro and geopolitical risks. AI-related investment continued to attract significant capital, with financial institutions exploring a funding package exceeding USD500 billion for AI infrastructure, while strong earnings from AI-related companies reinforced confidence in the structural investment cycle. The persistence of AI-driven activity provided an important source of support for markets despite uncertainty surrounding geopolitics, inflation, and monetary policy.

Overall, August was characterized by a balance between resilient global economic activity and increasingly complex policy and geopolitical risks. Persistent tensions around the Strait of Hormuz, renewed trade disputes, elevated underlying US inflation, and more hawkish Federal Reserve signals kept uncertainty high, while solid global activity and continued AI investment helped support market sentiment. The outlook remains sensitive to the evolution of US-Iran tensions, the inflation trajectory, and the Federal Reserve's policy response.

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