

Q1 2025 Non-US Market Insights: Gains Amid Global Uncertainty

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Global equity markets experienced notable developments during the first quarter of 2025, with international equities delivering solid returns despite geopolitical turbulence and mixed signals from the United States. The MSCI ACWI ex-USA Index rose by 5.23%, underscoring broad-based optimism in key regions, though substantial challenges remained.

Northern Europe emerged as a standout, driven by strong gains in German equities. This optimism was fueled by Germany's announcement of a groundbreaking €1 trillion defense and infrastructure spending plan. The initiative marked a pivotal shift from the country's historically cautious fiscal approach, signaling a new era of economic policy. Equity markets in the region rallied on the prospect of higher spending, even as bond markets reflected unease over ballooning deficits. While the policy's long-term ramifications remain uncertain, differing fiscal realities across Europe may limit the degree to which other countries follow in Germany's footsteps.

Chinese equities also delivered robust returns, supported by advancements in artificial intelligence technology. The nation's new AI platform, DeepSeek, demonstrated its ability to rival US innovations at substantially lower costs, intensifying global competition in AI. President Xi Jinping appeared to recalibrate his stance toward the private sector, highlighting its critical role in driving China's economic growth. Despite these favorable developments, challenges persisted. Domestic consumption remained sluggish, and structural concerns in the real estate sector and adverse demographic trends continued to weigh on the outlook. Export strength offsets some of these pressures, but questions linger as to whether recent policy measures can sustainably invigorate consumer spending.

Elsewhere in Asia, results were varied. Japan's equity markets remained flat, while Australia and India posted modest declines. Australian equities struggled due to falling commodity prices, a sector vital to the country's economy. Meanwhile, India contended with slower consumer and government spending and a deceleration in IT sector hiring, further dampening performance.

Though non-US markets displayed resilience, developments in the US significantly impacted global sentiment. The US economy faced its first quarterly equity market decline since 2023, with tariffs announced by President Trump as part of "Liberation Day" creating uncertainty. The moves reshaped sentiment globally, as some countries negotiated with the US for better trade agreements, while others, including China, retaliated with their own tariffs. The US Federal Reserve held rates steady in March, acknowledging the inflationary pressures these policies could create, while simultaneously lowering its growth expectations for 2025. These dynamics weighed on the US dollar, which fell unexpectedly, likely reflecting broader market concerns about potential stagflationary risks.

Geopolitical uncertainties further shaped the global landscape. While there were tentative efforts to progress toward a minerals and mining deal between the US and Ukraine, a sustainable resolution to the Russian-Ukrainian conflict remained elusive, with continued resistance from Russian leadership. Instability in the Middle East also re-escalated, with fresh outbreaks of violence adding a layer of unpredictability to the global stage.

Amid heightened geopolitical risks and shifting trade policies, volatility in global markets was significant. However, such periods of dislocation often present opportunities for disciplined investors. For international equity markets, Q1 showcased the complexity of navigating regional dynamics while managing the ripple effects of US economic and political developments. While many challenges remain unresolved, the first quarter has reaffirmed our focus on identifying high-quality opportunities and maintaining a disciplined approach in uncertain environments.

MSCI ACWI ex USA Index measures the performance of large- and mid-cap stocks in developed (excluding the US) and emerging markets. The index is unmanaged, market capitalization weighted, includes net reinvested dividends, does not reflect fees or expenses (which would lower the return) and is not available for direct investment. Index data source: MSCI, Inc. See diamond-hill.com/disclosures for a full copy of the disclaimer.

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