

Global Markets in Q2 2024: AI, Policy Shifts and Economic Divergence

Jun 2024

International equity returns were mixed in Q2 2024, with some market segments posting strong returns while others were weaker. The best-performing stocks came from areas that could benefit from the growth of artificial intelligence (AI) or country markets with a combination of low valuations and improving economic data. There were many notable elections in Q2, and the results of several drove local equity markets' performance depending on the perceived market-friendliness of the winning candidate or party. Additionally, some countries experienced stagnating economic recoveries or restrictive central bank policies that caused weakness.

The return of the MSCI ACWI ex-US Index was slightly positive in the quarter, up 0.96%. From a regional perspective, Asia Pacific ex-Japan had the most positive return in the quarter, driven by China, India, and companies in the semiconductor supply chain. Japan lagged the return of the international benchmark as higher interest rates and currency weakness weighed on US dollar returns. The performance of European equity markets was mixed. The United Kingdom was positive due to attractive valuations and an improving economic picture. France was a notable laggard as stagnating economic growth and surprising results in European Parliamentary elections caused concern.

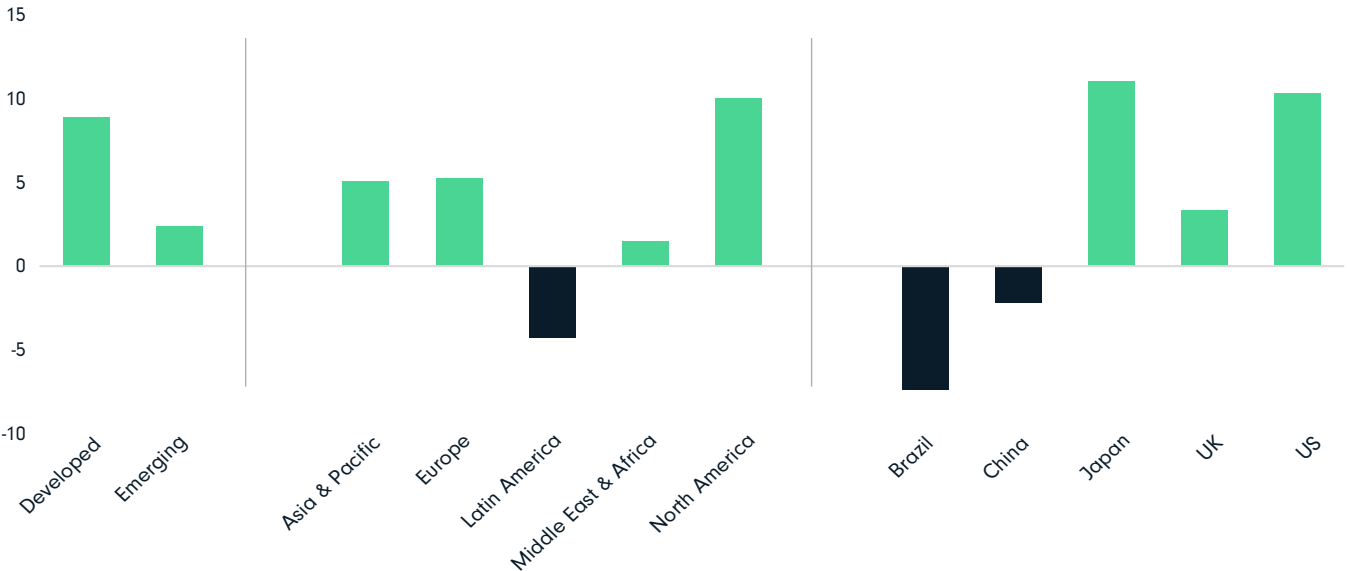
As has been expected for several months, monetary policy among major central banks diverged in Q2 as the European Central Bank cut rates while the Bank of England and the Federal Reserve held. Further, Fed chair Jerome Powell maintained his position that US rates are likely to remain higher for longer, signaling that there is expected to be only one rate cut before the end of the calendar year. Given the US's economic resilience — exemplified by resilient employment numbers — and inflation's ongoing stickiness, Powell's commitment is not particularly surprising. What naturally remains to be seen is how durable the economic data prove to be in the coming months.

Meanwhile, in the wake of finally exiting its protracted negative interest-rate regime, the Japanese Central Bank (JCB) faces ongoing challenges maintaining the yen's value, which has continued sliding relative to the dollar as US interest rates remain high. Though inflation in Japan has finally ticked up, which should give the JCB room to contemplate rate hikes, domestic consumer sentiment has been fragile as a weak yen has translated into high import and fuel costs. The JCB undoubtedly faces a delicate balancing act in the months and quarters ahead as it seeks to finally end decades of economic malaise.

Similarly, the ongoing global monetary policy and macroeconomic mix continues complicating the picture for a Chinese government which is seeking to boost its economy while facing growing trade tensions with Western countries — especially the US and the European Union, both of which have been ratcheting up restrictions related to electric vehicles and technology more broadly. Positively, Chinese GDP grew 5.3% year over year in Q1 — beating expectations and incrementally better than Q4's 5.2%. However, much of the growth has been attributable to the economy's supply side, which the government has provided ample support, while the demand side and the country's consumers continue struggling to recover from a deep real estate crisis that has crimped wealth and led many to cut back on spending.

It's been hard to miss the recent performance of AI-related stocks — which has contributed to an increasingly narrow market in the US and has also driven some of the best performing areas of international markets, albeit without the concentration of US indices. We will be selective in how or if we add exposure to this area and strictly adhere to our time-tested, fundamental approach to identifying high-quality, underappreciated companies.

Exhibit 1 – Q2 2024 Total Returns for Major Markets (USD) (%)



Source: FactSet, as of 30 Jun 2024.

As bottom-up, value-oriented investors, we thrive in times of volatility and disruption. It’s during these periods that great businesses often become mispriced, presenting us with exceptional investment prospects. Our excitement lies in continuously searching for and uncovering the best ideas amidst change.

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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