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European Market Update

European stock markets have delivered a robust performance in 2025 YTD, outpacing their U.S. counterparts amid shifting global dynamics. As of March 26, the STOXX 600, a pan-European benchmark, was up 7.8% YTD, propelled by a 13% gain in Q1 alone—the strongest quarterly performance in two years (Reuters, 2025a). National indices have shone brighter: Germany's DAX rose 16.2%, Spain's IBEX 35 climbed 10.5%, Italy's FTSE MIB gained 11.9%, and France's CAC 40 advanced 5.3% (Newsweek, 2025). This rally, which contrasts with the S&P 500's -5.1% YTD decline, stems from four key drivers: anticipated European Central Bank (ECB) rate cuts, positive economic surprises (e.g., Germany's Ifo Business Climate Index hitting a nine-month high in March), improving earnings momentum, and a fiscal pivot toward defense and infrastructure spending (Invesco, 2025; T. Rowe Price, 2025). Defense stocks, like those in the MSCI EMU Aerospace and Defense Index, soared nearly 40% YTD, fueled by Germany's €1 trillion defense pledge and a broader EU "rearm Europe" plan (Schwab, 2025; CNBC, 2025a).

However, March has seen volatility, with the STOXX 600 down 1.4% for the week ending March 28—its worst weekly drop since December—erasing some gains as tariff fears resurfaced (Reuters, 2025b). Last week's losses included a 0.7% Friday decline, driven by a U.S. core PCE inflation reading of 2.8%, stoking global risk-off sentiment (Reuters, 2025b). Despite this, European markets remain attractive, trading at 14 times forward earnings versus the S&P 500's 21, offering a 37.5% valuation discount (Reuters, 2025c).

This week, three issues will dominate. First, Trump's "Liberation Day" tariff rollout on April 2 threatens European exports, particularly autos, with a 25% levy on non-U.S.-made cars already rattling markets—Volkswagen and Stellantis fell 3-5% last week (Reuters, 2025d). Posts on X suggest a "sharp decline" is expected Monday as investors brace for broader levies (X Post, @tEconomics, 2025). Second, the ECB's April rate decision looms; softer-than-expected March inflation in France (0.9%) and Spain (2.2%) bolsters bets on a 25-basis-point cut, potentially lifting equities but pressuring yields (CNBC, 2025b). Third, Germany's unemployment rose sharply in March—the fastest since October 2024—hinting at economic fragility that could dampen sentiment if jobs data worsens (Reuters, 2025b). With U.S. markets volatile and gold near $2,900 as a safe haven, European stocks face a pivotal week balancing tariff risks against domestic resilience (Yahoo Finance, 2025).

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