

Strategy

More challenges ahead despite US-China trade truce

Key message

1. The reduced US tariffs on Chinese imports remain high, and so bilateral trade is unlikely to return to normal.
2. Tariffs on semiconductor chips and global tariffs initially announced on April 2 have not been finalized yet, suggesting more policy uncertainty ahead.
3. Flip-flopping US trade policies have substantially hurt end-market demand, with downside risks looming.

Event

The US and China have agreed to temporarily reduce tariffs on each other. While this is indeed good news for the near term, we note that the lowered tariff rates are still high, and there are still uncertainties surrounding global trade wars, with elevated risk of end-demand contractions. Put simply, we expect more economic ordeals ahead.

Analysis

Taiex performance driven by Trump's erratic trade policies. The Taiex index has undergone some major swings in 1H25 by plunging by 28%, or 6,600 points, before spiking by 25%, or 4,400 points, as a result of Trump's flip-flopping trade policies. Although the US-China trade truce bodes well for investment sentiment, we note that the lowered tariff rates are still high, and the uncertainty surrounding global trade wars and the elevated risk of end-demand contractions all point to more economic challenges ahead, which will cap upside for the index, in our view.

US tariffs on Chinese imports are still above 37.5%, so bilateral trade is unlikely to return to normal. The US and China reached an agreement to reduce tariffs on each other for 90 days. However, we note that the applicable tariff rates for Chinese imports during the 90-day truce are still quite high, at 37.5-55.0%. Such high tariffs will leave general manufacturers unprofitable, and thus we find it hard for the two countries to resume a normal trade relationship.

Trade uncertainty continues as chip tariffs and blanket tariffs have yet to be finalized. The temporary trade truce between China and the US is not enough to eliminate all negatives stemming from US tariffs, as tariffs on semiconductor chips and the blanket tariffs announced on April 2, which are critical to Taiwan, have not yet been finalized. While Taiwanese semiconductor firms are capable of passing through additional costs to US clients if tariffs are imposed, we note that the US clients will also pass on the costs to consumers, resulting in waning consumption demand. The UK and China have sealed some sort of trade deals with the US, and the market is optimistic about global national tariffs landing between 10-30%, far below those of 20-50% announced on April 2. However, we believe these tariffs will weigh substantially on the global economy. According to the Peterson Institute for International Economics, a 10% universal tariff will affect US GDP by 0.4-0.8ppts, and the impact will likely persist for three years.

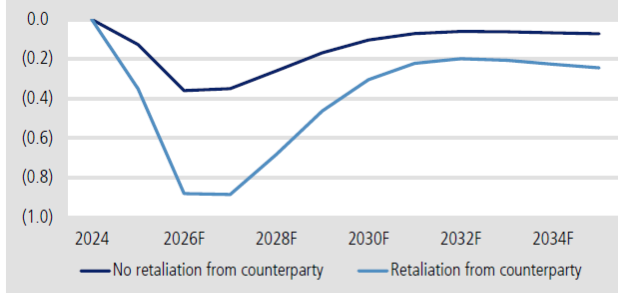
Flip-flopping trade policies have substantially hurt end-market demand, with downside risks looming. Although US tariffs have triggered early pull-in demand, allowing Taiwanese suppliers to defy weak seasonality in 1H25F, many fear that demand in the 2H25F peak season will turn out to be weaker than expected. Assuming that 1H25 positives will be offset by 2H25 negatives, the market has been revising down 2025-26F earnings forecasts for Taiex constituents since March. While the revisions are moderate, at only around 2%, we believe further earnings downgrades may be on the horizon, capping Taiex index performance, as tariff impacts on end-demand materialize and the competitiveness and profitability of Taiwanese firms are undermined by the appreciation of the NT dollar. Taiex earnings are highly correlated to the US economy. A substantial US economic slowdown will inevitably lead to earnings contractions for Taiex firms, and a deep economic recession will decimate Taiex earnings by at least 50%.

Conclusion & top picks

The US-China trade truce is indeed a near-term positive, but the reduced tariff rates between the two remain high, which, along with trade war uncertainty and downside risks for end-market demand, suggest more economic ordeals lie ahead. We believe the Taiex will stay afloat, between 20,000-22,000 in the near term, but the longer-term outlook is uninspiring, and it is hard to tell where the trough will be. Investors are advised to focus on AI stocks, which will benefit from resilient market demand, and avoid those that would fall victim to demand contractions, such as PC, handset, consumer electronics, apparel, footwear and bicycle plays.

Figure 1: A universal 10% tariff will hurt US GDP by 0.4-0.8ppts, and the impact would likely persist for three years

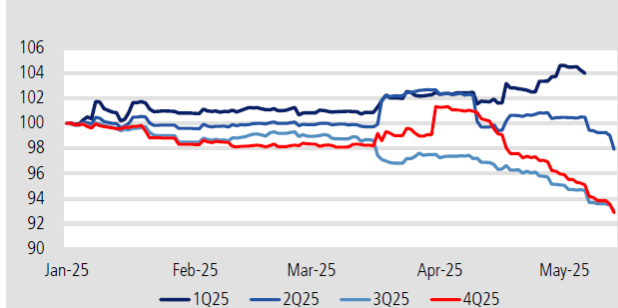
Impact of 10% universal tariff on US GDP, percent



Source: Peterson Institute for International Economics; KGI Research

Figure 3: Although US tariffs have triggered early pull-in demand in 1H25, many fear that demand in the 2H25 peak season will turn out to be weaker than expected

Taiex quarterly EPS forecasts, NT\$

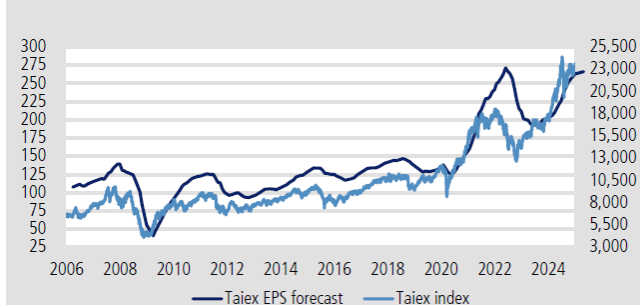


Source: Bloomberg; KGI Research

Note: We use the EPS forecast on January 1, 2025 as the base, at 100

Figure 5: Taiex index is highly correlated to earnings outlooks, and so further earnings downgrades, should they come to pass, will cap index performance

Taiex EPS forecasts, NT\$ (LHS); Taiex index, points (RHS)

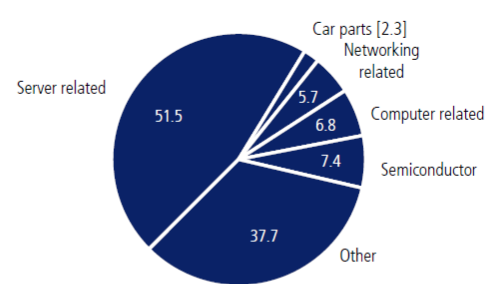


Source: Bloomberg; KGI Research

Note: We use the EPS forecast in January 2006 as the base, at 100

Figure 2: Taiwan's exports to the US amounted to US\$116.3bn in 2024. If a 10% tariff is to be paid by Taiwanese exporters, it will shave their EPS by 10%

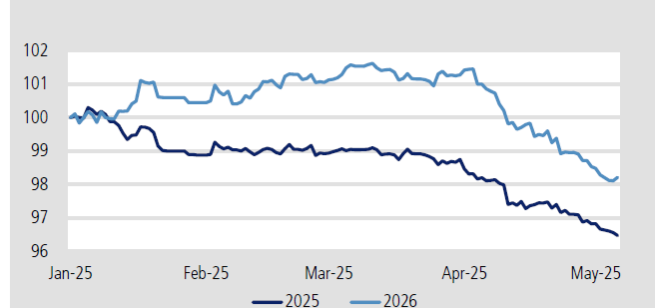
Top five Taiwan exports to the US in 2024, US\$bn



Source: Ministry of Economic Affairs; KGI Research

Figure 4: Assuming 1H25 positives will be offset by 2H25 negatives, the market has been revising down 2025-26F Taiex earnings forecasts since March

Taiex annual EPS forecasts, NT\$

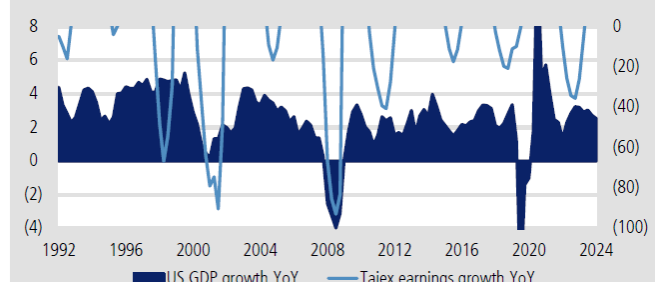


Source: Bloomberg; KGI Research

Note: We use the EPS forecast on January 1, 2025 as the base of 100

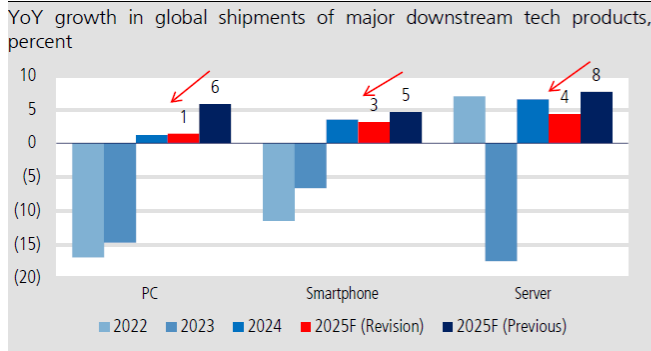
Figure 6: Taiex earnings are highly correlated to the US economy. A substantial US economic slowdown will inevitably lead to earnings contractions for Taiex firms, and a deep economic recession will decimate Taiex earnings, by at least 50%

US GDP growth YoY, percent (LHS); Taiex earnings growth YoY, percent (RHS)



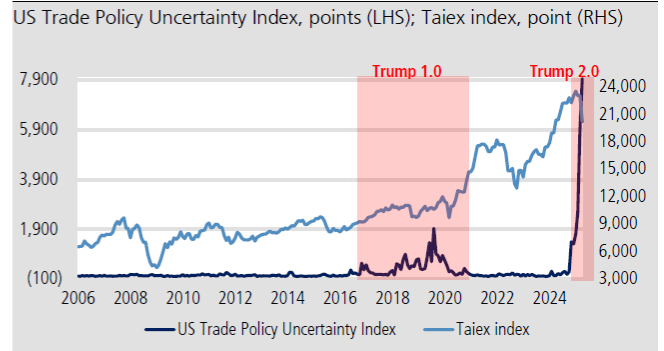
Source: Bloomberg; KGI Research

Figure 7: Given tariff uncertainties, we have revised down projected shipments of downstream tech products and further downgrades will be made if the US economy sinks into a recession



Source: KGI Research

Figure 8: Trump's erratic trade policies will squeeze market risk appetite



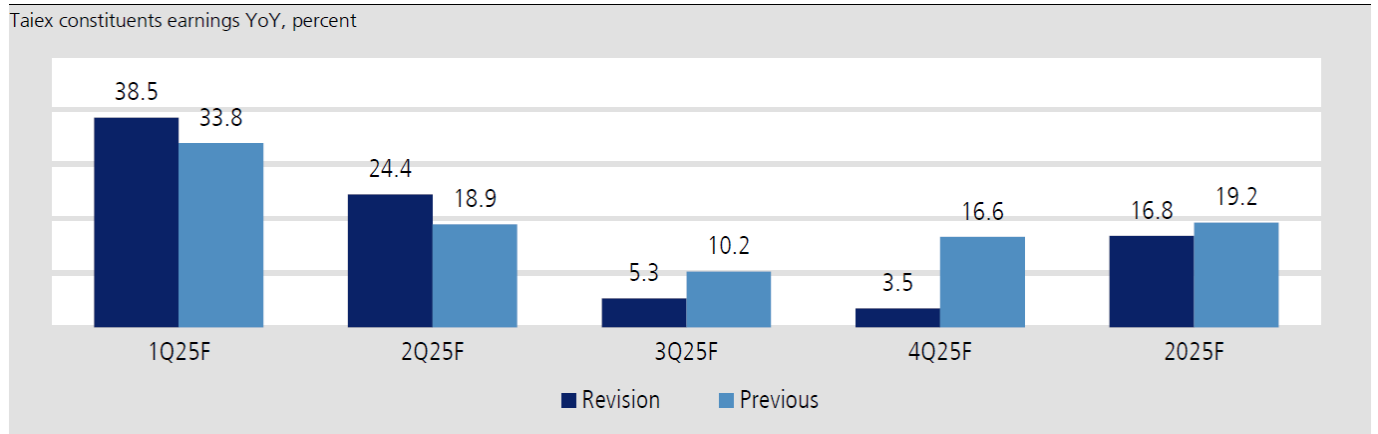
Source: Bloomberg; KGI Research

Figure 9: Earnings forecasts and valuations of Taixex constituents

P/E (x)	2021	2022	2023	2024	2025F
Taixex	17.8	18.5	26.0	18.5	15.9
Taixex excl. TSMC	13.2	16.0	23.8	16.9	15.3
Tech	25.5	22.7	28.7	21.3	17.4
Tech excl. TSMC	17.3	20.2	26.6	20.5	17.7
TSMC	43.4	25.5	30.9	22.1	17.0
EPS growth (%)	2021	2022	2023	2024	2025F
Taixex	78.1	(3.7)	(28.9)	40.5	16.8
Taixex excl. TSMC	97.4	(17.0)	(33.1)	40.8	10.9
Tech	51.7	12.2	(20.9)	34.8	22.4
Tech excl. TSMC	77.1	(14.2)	(23.9)	29.8	15.4
TSMC	15.2	70.4	(17.5)	39.9	30.0

Source: KGI Research

Figure 10: Taixex 1Q25 results were stellar, but 2H25F & 2025F guidance has been generally revised down



Source: KGI Research

Figure 11: Taix sensitivity analysis – 2025F earnings growth YoY vs. PE ratio

Taix (points)		Target PE (x)								
		10	11	12	13	14	15	16	17	18
2025 earning YoY (%)	(20)	9,400	10,340	11,280	12,220	13,160	14,100	15,040	15,980	16,920
	(10)	10,575	11,632	12,690	13,747	14,805	15,862	16,920	17,977	19,035
	(5)	11,162	12,278	13,395	14,511	15,627	16,743	17,860	18,976	20,092
	0	11,750	12,925	14,100	15,275	16,450	17,625	18,800	19,975	21,150
	10	12,925	14,217	15,510	16,802	18,095	19,387	20,680	21,972	23,265
	15	13,512	14,863	16,215	17,566	18,917	20,268	21,620	22,971	24,322
	20	14,100	15,510	16,920	18,330	19,740	21,150	22,560	23,970	25,379

Source: KGI Research

Figure 12: Our top picks

Company	Code	Investment rating	Target price (NT\$)	Mkt cap (US\$m)	Share price (NT\$)	Change +/- (%)	EPS (NT\$)		PE (x)		P/B (x)		ROE (%)		Cash yield (%)	
							2025F	2026F	2025F	2026F	2025F	2026F	2025F	2026F	2025F	2026F
QCI	2382 TT	Outperform	325.0	35,086	276.5	17.5	18.05	23.34	15.3	11.8	5.1	4.7	34.3	41.1	5.2	6.7
Wistron	3231 TT	Outperform	135.0	10,887	114.5	17.9	8.47	10.21	13.5	11.2	2.2	2.0	17.1	18.4	4.4	5.3
AVC	3017 TT	Outperform	725.0	7,766	609.0	19.0	36.26	45.78	16.8	13.3	6.5	5.2	43.2	43.4	2.8	3.6
GCE	2368 TT	Outperform	282.0	3,652	226.0	24.8	16.01	19.15	14.1	11.8	4.3	3.4	33.2	31.8	3.5	4.2
CTBC Holding	2891 TT	Outperform	46.0	26,213	40.6	13.3	3.80	4.09	10.7	9.9	1.6	1.4	15.5	14.7	5.7	6.2
E.S.F.H	2884 TT	Outperform	34.0	15,607	29.7	14.5	1.84	1.94	16.1	15.3	1.7	1.5	11.0	10.3	4.5	4.7
Uni-President	1216 TT	Outperform	92.0	14,653	78.5	17.2	4.32	4.86	18.2	16.2	3.1	2.9	17.7	18.7	3.8	4.0
EGAT	2645 TT	Outperform	155.0	1,354	110.0	40.9	5.15	7.24	21.4	15.2	3.1	3.0	14.5	20.1	4.2	5.9

Source: KGI Research

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