

Strategy

Taiex rebound could be nearing an end

Key message

1. US intervention in the Middle East conflict will be critical to the performance of stock markets near term.
2. The Taiex rally could be nearing an end.
3. We recommend investors focus on defensive plays in 3Q25 and shift in stages to the AI sector in 4Q25.

Event

Escalation of the Israel-Iran military conflict has disrupted the recent Taiex rebound.

Analysis

US intervention in the Middle East critical to the performance of stock markets near term. Over the past week, the Taiex rebound came to an end and switched into consolidation mode, mainly due to escalation of the Israel-Iran military conflict, which has led to foreign capital outflows from the Taiex. Going forward, we believe US involvement in the war will be a major swing factor for market performance. Looking back at 22 major international wars or terrorist attacks since World War II, historical data shows that when the US gets involved, it often triggers larger market corrections; when the US stays out, markets tend to remain relatively stable. Markets also typically take longer to recover when the US gets involved, and vice versa. Of the 22 major military events, the US became directly involved in the Pearl Harbor attack, the Korean war, the Cuban missile crisis, two Vietnam wars, Iraq's invasion of Kuwait, the September 11 attacks, and airstrikes in Syria. During these events, the S&P 500 index saw maximum drawdowns ranging from 2% to 20%, and took 18-307 days to recover.

Taiex rally could be nearing an end. Since late-April, the Taiex has seen a strong rally driven by three major catalysts, namely the easing of trade wars, strong AI demand, and foreign capital inflows chasing appreciation of the NT dollar. However, we believe these catalysts have largely been priced in and are beginning to reverse, making it difficult for the market to gain further upside momentum.

According to the Yale Budget Lab, the effective tariff rate imposed by the US may have declined from the April 2 peak of 25% to 18%. While this easing of tariff wars has indeed fueled the recent Taiex rally, consensus seems to have underestimated the economic impact of tariffs, which is just about to unfold. The current effective tariff rate represents the highest rate since 1934 and it is expected to have a significant impact on the economy. According to the Peterson Institute for International Economics (PIIE), tariffs of 10-20% would reduce US GDP growth by 0.9-1.8ppts and increase inflation by 1.1-2.2ppts, signaling a rising risk of stagflation.

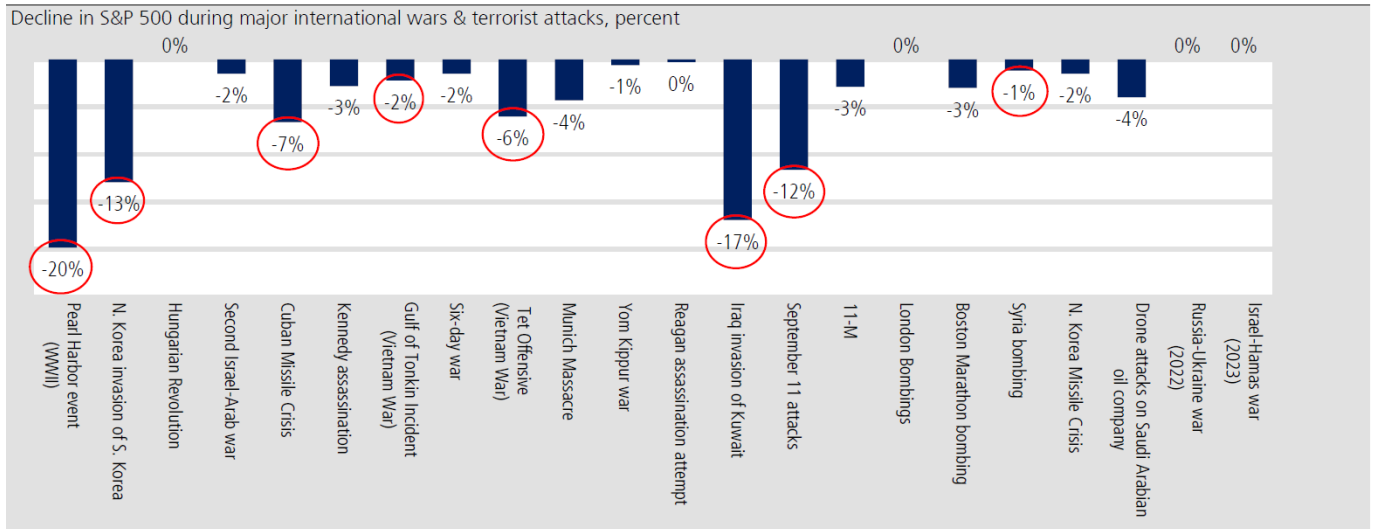
While AI-related demand remains undeniably strong, the recent surge in the Taiex has driven stock prices and valuations across the supply chain to elevated levels.

Finally, the liquidity rally fueled by NT dollar appreciation against the US dollar appears to be nearing an end. The NT dollar has strengthened by up to 10.7% during this cycle, approaching the typical rally fulfillment point (a peak of 8–12%). This, coupled with escalating geopolitical risks, suggests that the NT dollar rally may be entering its final phase, undermining the sustainability of the liquidity-driven market rally.

Conclusion & top picks

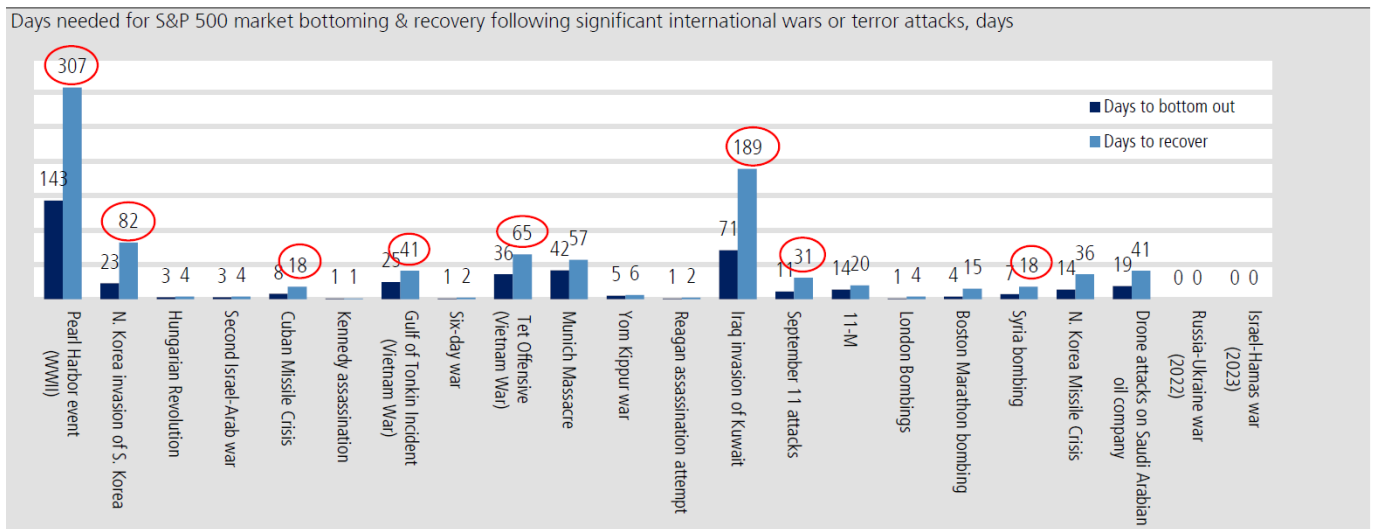
Since late-April, the strong rebound in Taiwan equities has been driven by easing tariff tensions, robust AI demand, and the spillover effect of capital inflows driven by international hot money chasing NT dollar appreciation. However, we believe these catalysts have largely been priced in and are beginning to show signs of reversal. As such, we believe the current rally is losing momentum. We recommend that investors adopt a defensive stance in 3Q25, steering clear of overheated valuations and heightened systemic risks, and gradually accumulate positions on dips in 4Q25.

Figure 1: Historically, when the US gets directly involved in major international wars or terrorist attack responses, stock markets undergo sharper corrections; when the US stays out, market reactions are generally more subdued



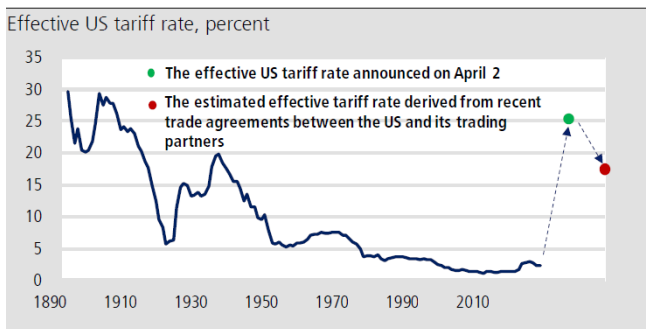
Source: Bloomberg; KGI Research

Figure 2: Historically, when the US gets directly involved in major international wars or terrorist attack responses, stock markets take longer to recover; when the US remains uninvolved, markets typically rebound more quickly



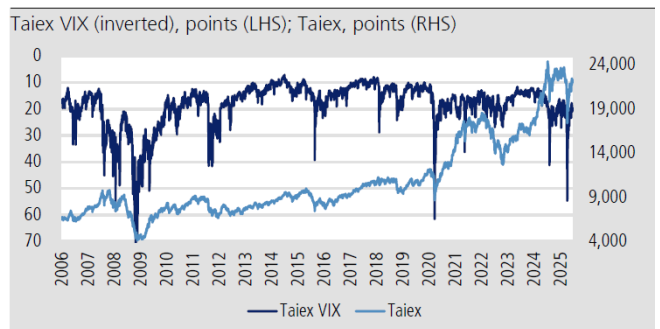
Source: Bloomberg; KGI Research

Figure 3: Effective US tariff rate has declined from peak of 25% (announced April 2) to 18%; the easing of trade tensions has been a key catalyst of the strong Taieix rebound



Source: Yale Budget Lab; KGI Research

Figure 4: Taiex Volatility Index (VIX) at historically low levels, suggesting the market may be underestimating tariff-related risks, particularly the potential economic impact of renewed trade tensions



Source: Bloomberg; KGI Research

Figure 5: Maximum impact on US GDP growth could reach 0.9-1.8ppts if Trump imposes 10-20% universal tariff on global imports

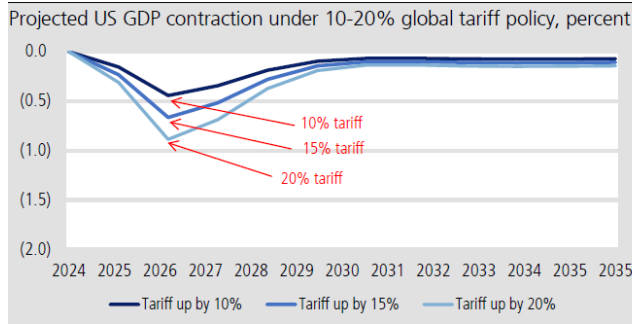


Figure 6: US inflation could rise 1.1-2.2ppts if Trump imposes 10-20% universal tariff on global imports

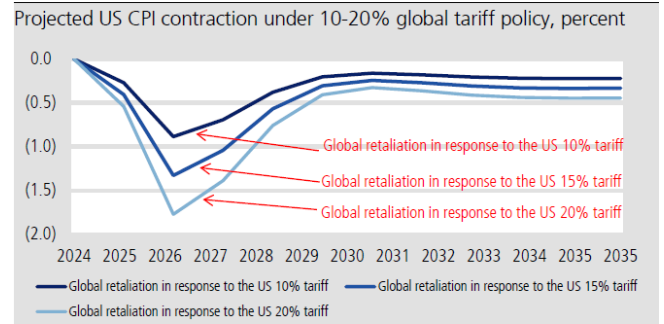


Figure 7: Since late-April, FINI have significantly increased Taix holdings by around NT\$240bn, partially reflecting a liquidity surge driven by international hot money chasing NT dollar appreciation

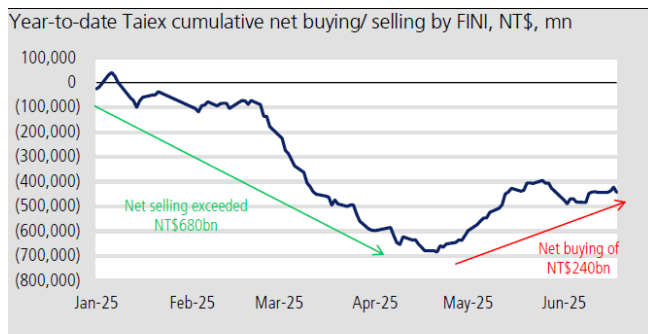


Figure 8: NT dollar has appreciated as much as 11%, nearing the fulfillment level of past rallies; with escalating geopolitical risks, the liquidity-driven rally fueled by NT dollar appreciation may be approaching final stages

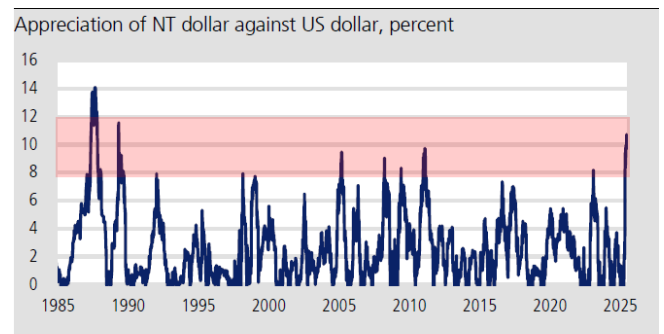


Figure 9: Earnings forecasts & valuations of Taix sectors

Tech	Earning YoY (%)					Forecast PE (x)		Non-tech	Earning YoY (%)					Forecast PE (x)	
	2022	2023	2024	2025F	2026F	2025F	2026F		2022	2023	2024	2025F	2026F	2025F	2026F
Server EMS	(1.7)	3.7	24.8	21.4	27.8	14.7	11.0	Cement	(50.7)	8.4	27.9	(6.7)	17.7	17.3	14.2
Thermal	34.5	20.5	54.0	69.5	28.7	19.7	14.7	Food	(13.6)	6.8	12.7	18.7	12.4	18.0	16.0
Power supply	15.1	2.4	(1.7)	26.5	17.3	19.9	17.0	Petrochemicals	(62.6)	(51.0)	(80.8)	20.6	74.0	49.5	23.3
ABF	102.5	(68.1)	(70.1)	140.2	75.5	22.3	12.2	Apparel	32.1	(11.0)	17.3	(0.9)	4.9	15.5	14.9
Optical communication	-	63.4	20.5	139.6	-	20.4	-	Footwear makers	100.0	(45.2)	18.0	(9.1)	5.4	21.1	20.0
IC design and service	94.8	5.3	29.9	5.1	51.1	34.8	24.0	Auto parts	113.5	25.1	44.3	15.3	9.6	10.8	9.6
Networking PCB	56.1	(22.8)	59.1	40.2	19.6	16.6	13.9	Industrial automation	5.2	(14.2)	6.6	11.0	18.1	26.1	20.9
Networking	77.3	15.2	15.3	51.1	-	15.0	-	Bicycle	(12.7)	(44.8)	(88.9)	813.6	20.6	13.6	11.3
CCL	(7.7)	8.2	74.5	42.1	8.3	21.4	19.8	Container shipping	19.7	(94.4)	631.6	(52.2)	(15.0)	8.7	11.8
Tier-one foundry	70.4	(17.5)	39.9	26.5	17.0	18.4	15.8	Steel	(75.4)	(89.0)	(41.0)	562.0	50.2	52.2	25.3
Second-tier foundries	56.3	(30.1)	(22.6)	(13.4)	9.5	14.6	13.4	Tourism	(46.5)	176.4	2.7	7.7	16.0	12.9	10.7
Handset components	11.4	(40.3)	44.0	8.1	8.0	11.0	9.7	Food	(40.3)	144.6	(11.9)	24.1	21.5	15.6	12.6
Telecom	2.6	13.7	13.6	7.1	2.7	27.1	26.4	Aerospace	127.3	26.8	(0.3)	(3.7)	23.1	22.4	17.9
IC design (handset/consumer electronics)	(2.9)	(32.6)	29.8	12.1	11.1	15.9	14.7	Airlines	(37.8)	185.5	52.7	(29.1)	(40.2)	11.1	19.8
Handset EMS	(26.5)	4.1	7.4	(5.4)	9.8	12.6	11.5	Heavy electrical	30.4	23.3	67.9	14.0	(4.0)	24.3	20.5
Cloud digital	16.3	17.1	13.1	22.8	16.7	19.0	16.2	Green energy	56.9	85.5	26.8	101.7	42.3	21.9	12.1

Source: KGI Research estimates

Figure 10: Earnings forecasts & valuations of Tailex constituents

Earning (NT\$bn)	2021	2022	2023	2024	2025F	2026F
Tailex	3,917	3,771	2,682	3,769	4,402	4,851
Tailex excl. TSMC	3,320	2,755	1,844	2,595	2,918	3,115
Tech	1,914	2,147	1,698	2,249	2,768	3,247
Tech excl. TSMC	1,317	1,130	860	1,075	1,284	1,511
TSMC	597	1,017	838	1,173	1,484	1,736
EPS growth (%)						
Tailex	78.1	(3.7)	(28.9)	40.5	16.8	10.2
Tailex excl. TSMC	97.4	(17.0)	(33.1)	40.8	12.4	6.7
Tech	51.7	12.2	(20.9)	32.4	23.1	17.3
Tech excl. TSMC	77.1	(14.2)	(23.9)	25.1	19.4	17.6
TSMC	15.2	70.4	(17.5)	39.9	26.5	17.0
P/E (x)						
Tailex	18.1	18.8	26.4	18.8	16.1	14.6
Tailex excl. TSMC	13.1	15.8	23.5	16.7	14.9	13.9
Tech	26.2	23.4	29.5	22.3	18.1	15.4
Tech excl. TSMC	17.3	20.2	26.5	21.2	17.8	15.1
TSMC	45.9	26.9	32.6	23.3	18.4	15.8

Source: KGI Research estimates

Figure 11: Our top picks

Sector/ theme	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
High-yield and undervalued stocks	MediaTek	2454 TT	Outperform	1700.0	67,660	1250.0	36.0	72.29	85.05	17.3	14.7	5.1	4.7	29.2	33.1	5.4	5.8
	Uni-President	1216 TT	Outperform	92.0	14,959	77.9	18.1	4.32	4.86	18.0	16.0	3.1	2.9	17.7	18.7	3.9	4.1
	PCSC	2912 TT	Outperform	300.0	9,030	257.0	16.7	11.98	13.51	21.4	19.0	5.9	5.3	28.4	29.4	3.5	3.5
	CTBC Holding	2891 TT	Outperform	45.0	28,523	43.0	4.8	3.32	3.95	12.9	10.9	1.6	1.4	13.5	13.8	4.9	5.6
	E.S.F.H	2884 TT	Restricted	N.A.	17,190	31.8	N.A.	1.84	1.94	17.2	16.4	1.8	1.6	11.0	10.3	4.2	4.4
	Asustek	2357 TT	Outperform	800.0	17,144	683.0	17.1	53.29	54.46	12.8	12.5	1.8	1.8	14.4	14.3	6.2	6.4
AI supply chain	Alchip	3661 TT	Outperform	4020.0	7,651	2800.0	43.6	75.82	129.66	36.9	21.6	5.2	4.4	14.5	21.7	1.4	2.3
	MPI	6223 TT	Outperform	1005.0	2,761	867.0	15.9	33.40	40.34	26.0	21.5	7.2	5.4	30.2	28.5	2.1	2.5
	ASEH	3711 TT	Outperform	168.0	21,597	144.5	16.3	10.29	12.96	14.0	11.2	1.8	1.7	13.2	15.4	3.1	4.2
	Hon Hai	2317 TT	Outperform	205.0	73,003	155.5	31.8	12.85	14.46	12.1	10.8	1.2	1.2	10.6	11.3	4.4	4.9
	QCI	2382 TT	Outperform	320.0	36,485	279.5	14.5	17.75	19.82	15.7	14.1	4.6	4.3	29.9	31.4	5.1	5.7
	Wistron	3231 TT	Outperform	135.0	12,593	118.5	13.9	8.47	10.21	14.0	11.6	2.3	2.0	17.1	18.4	4.2	5.1
	AVC	3017 TT	Outperform	725.0	9,629	734.0	(1.2)	36.26	45.78	20.2	16.0	7.9	6.2	43.2	43.4	2.3	3.0
	DELTA	2308 TT	Outperform	428.0	35,114	400.0	7.0	17.03	20.20	23.5	19.8	4.0	3.6	18.0	19.0	2.1	2.5
	BHI (Bizlink)	3665 TT	Outperform	788.0	4,915	765.0	3.0	37.97	45.74	20.1	16.7	3.4	3.0	18.4	19.2	2.4	2.9
	ELASER	3450 TT	Outperform	300.0	1,056	214.5	39.9	6.50	10.01	33.0	21.4	6.3	5.4	20.2	27.3	1.4	2.1
	GCE	2368 TT	Outperform	282.0	4,430	266.5	5.8	16.01	19.15	16.6	13.9	5.0	4.0	33.2	31.8	3.0	3.6
	Accton	2345 TT	Outperform	950.0	13,521	713.0	33.2	37.99	N.A.	18.8	N.A.	8.7	N.A.	51.8	N.A.	2.9	N.A.

Source: KGI Research

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