US strategy

Hesitant on US equities despite improved market sentiment due to new semiconductor & pharmaceuticals tariffs & weakening US fundamental

Key message

1. Leading survey indicators (soft data) are likely to drag down US real economic data (hard data) in the future; it is unrealistic to expect an aggressive or immediate Fed rescue.
2. Downward revisions to earnings forecasts since the beginning of the year will continue.
3. The sectors most vulnerable to US-China tariffs are likely to be consumer discretionary plays and industrials, while cybersecurity stocks could deliver relatively decent performance.

Event

Although tariff negotiations between the US and other countries seem to have progressed, significant uncertainties remain in the coming months — particularly regarding the new tariffs on semiconductors and pharmaceuticals. We have not yet turned long on US equities, given weakening US fundamentals.

Analysis

Survey data from reports (soft data), which are leading indicators, are expected to drag down US actual economic data (hard data) in the coming months. It is unrealistic to expect an aggressive or immediate Fed rescue. At present, there are few reasons for optimism regarding the U.S. economy—whether from the corporate front or personal consumption. On the corporate front, investment sentiment has turned conservative due to tariff-related uncertainties (Figures 1 & 2). This is also reflected in order data, where manufacturing order surveys — both those compiled by regional Fed banks and ISM PMI — show a sharp decline, particularly the former (Figure 3). On the personal consumption side, a noticeable slowdown in job openings has led to weaker income growth and declining consumer confidence, resulting in more conservative spending (Figures 4–6). In summary, soft data has already signaled economic slowdown, though hard data has yet to show a broad-based downturn (Figure 7). Real economic indicators will be eventually dragged by forward-looking survey data. More concerning is that the threshold for a Fed rate cut remains quite high, on stalled disinflation in the US. We believe it is rash to expect the US Fed to come to the rescue without signs of a severe recession or systemic financial risk.

Downward revisions to earnings forecasts since the beginning of the year to continue. With the 1Q25 earnings season coming to an end, the market has updated its outlook on future earnings. Overall, downward revisions to earnings forecasts since the beginning of the year have been the trend. Consensus expected earnings growth of nearly 15% at the start of the year, but this has been cut to around 9% (Figure 8), while sales forecasts have remained relatively stable. The same pattern applies to 2Q25 forecasts. Although consensus was already bearish about the second quarter, earnings growth forecasts for 2Q25 have been revised down from approximately 12% to 7%, which is even lower than the actual 1Q25 figures. Given the current fundamental trends, we believe downward revisions in earnings forecasts are not yet over, and further downgrades are likely to be seen in the future (Figure 9).

The sectors most vulnerable to US-China tariffs are likely to be consumer discretionary plays and industrials, while cybersecurity stocks could deliver relatively decent performance. We analyze US-China trade impacts from a US sectoral standpoint, as US tariffs on Chinese goods are still among the highest on any country, despite recent reductions. In terms of import exposure, consumer discretionary plays, industrials, and tech sectors have relatively high import shares from China. Notably, the consumer discretionary sector accounts for 28.6% of total imports, with over two-thirds of them coming from China (Figures 10 & 11). Before Donald Trump's second term, many of the tariffs imposed during the first US-China trade war remained in place. Utilities, energy and tech sectors face tariffs above 20% on Chinese imports, while consumer discretionary imports face average tariffs of around 17.5%, which does not particularly stand out among all sectors (Figure 12). However, the average tariff rate on consumer discretionary imports from countries outside China is the highest among all sectors, at around 6%. This suggests that although the sector has high exposure to Chinese imports, the relative tariff burden it faces is not the most severe. Although tariff rates have changed meaningfully during the second Trump administration, the big picture remains largely the same, as tariffs are imposed on all products. However, from a profitability standpoint, the consumer discretionary and industrial sectors have relatively low net margins (Figure 13), making them more vulnerable to cost pressures from rising tariffs. We were previously positive about an earnings rebound and attractive valuations for industrial plays from late-2024 to early-2025. However, recent analyses suggest a reassessment of our view is necessary.

Are there any preferred sectors? We believe that software stocks, which are relatively less affected by tariffs and economic cycles, may be worth considering. Among them, information security plays stand out as a potential investment vehicle for two main reasons: (1) increased geopolitical risk. Amid a tariff war, geopolitical tensions tend to rise, often leading to a surge in cyberattacks. This, in turn, boosts demand for information security solutions; and (2) AI as a long-term theme. The development of AI will boost demand for information security, benefiting the sector (Figure 14). Our recommended ETFs are CIBR and HACK.

Conclusion

Despite optimistic market sentiment following the joint statement on tariffs issued by the US and China on May 12, the absolute tariff rate imposed by the US on Chinese goods remains high. Upon closer examination, the anchoring effect of this joint statement on tariff negotiations is likely to be limited in duration. The US has reduced tariffs on Chinese goods to just an additional 30% for 90 days, which follows the same logic as the tariff reductions applied to other countries after April 9, where rates dropped to 10% for 90 days, though without requiring any formal statements or negotiations. However, the temporary reduction does not provide much guidance as to what the tariff rates for other countries will be after the 90-day period. Therefore, it cannot be ruled out that the rates may not stay at or below 10%.

We believe that although trade tensions have eased, their impact on financial markets should not be underestimated - especially for individual equities, which are more immediately affected than the broader economy. In fact, while exports account for only a little more than 10% of the US economy, overseas sales make up 41% of total S&P 500 sales, so there is a much higher level of international exposure for the stock market than for the economy overall. Moreover, products more affected by tariffs represent nearly half of the US equity market, well above the 22.4% for the overall economy (Figure 15). Therefore, the recent pullback on the probability of a US recession should not lead to an underestimation of the stock market's vulnerability. The S&P 500 has surpassed the 5,800 points level it reached in mid-March, before markets began pricing in the April 2 tariff announcements. This rise is reasonable, given the recent positive developments involving the UK and China, as expectations for new tariffs on other countries were already unlikely to be below 10%, making the news a genuine positive. However, a return to the highs seen in mid-February would be unjustified. Given that the market rebound appears to have peaked, and with upcoming tariffs on semiconductors and pharmaceuticals, along with a confirmed economic downturn, we currently maintain a more cautious stance on US equities. Now is not the right time to turn bullish across the board.

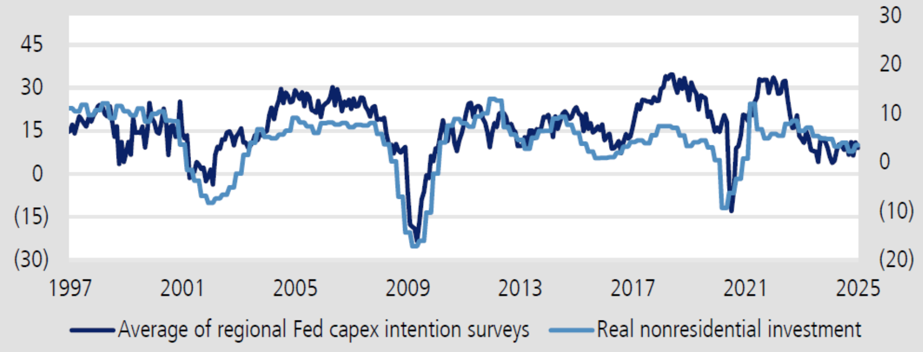
Figure 1: Low corporate expansion confidence

NFIB SME survey – "Good time for expansion" in the next three months, percent

Note: Shaded areas are NBER-defined US recession
Source: Bloomberg; KGI Research

Figure 2: Poor capex expectations surveyed by Fed branches bode ill for corporate non-residential investment

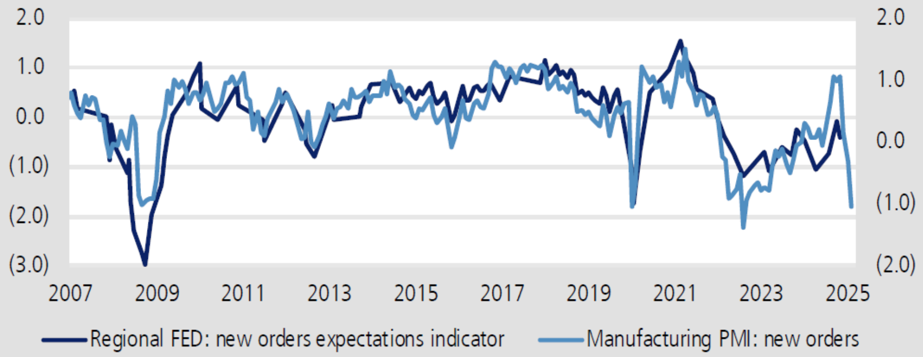
Average capex intention surveyed by Fed branches, points (6 months in advance; LHS); real non-residential investment, percent (RHS)



Source: Bloomberg; KGI Research

Figure 3: New orders depletion to speed up manufacturing sector downturn

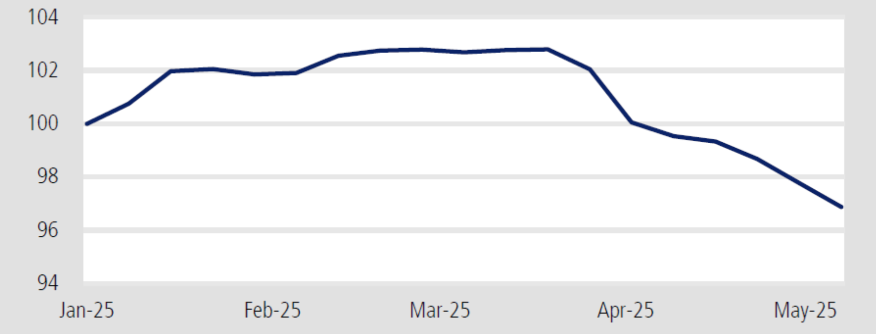
Regional FED: new orders expectations indicator,points (6 months in advance; LHS); Manufacturing PMI: new orders,points (RHS)



Source: Bloomberg; KGI Research

Figure 4: Job openings have nosedived since mid-March

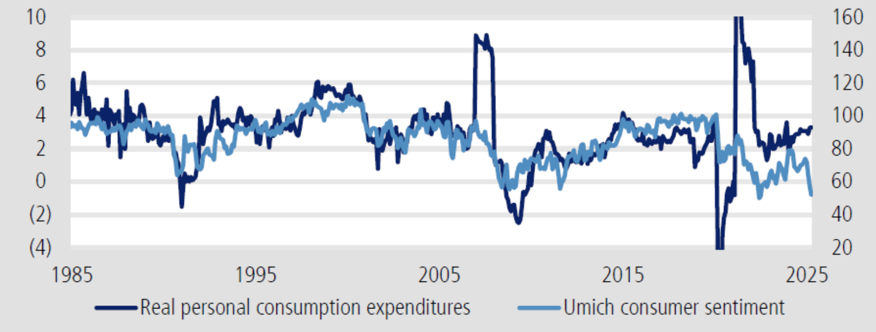
LinkUp job openings trend since 2025 (January 2025 = 100)



Source: LinkUp; KGI Research

Figure 5: Weakening consumer confidence will affect consumer spending

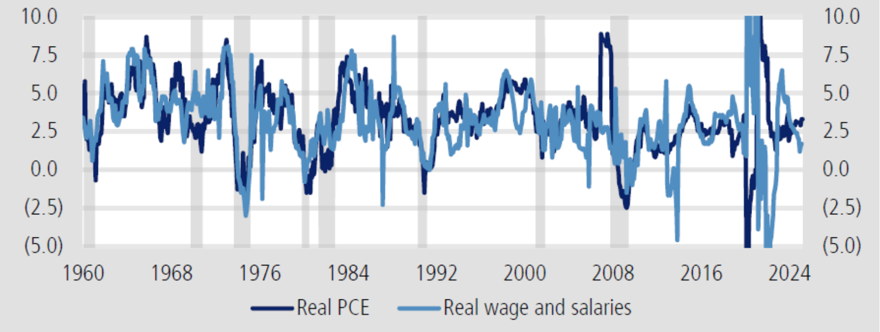
Real personal consumption spending change YoY, percent (LHS); University of Michigan consumer sentiment index, points (RHS)



Source: Bloomberg; KGI Research

Figure 6: Spending falling along with wages

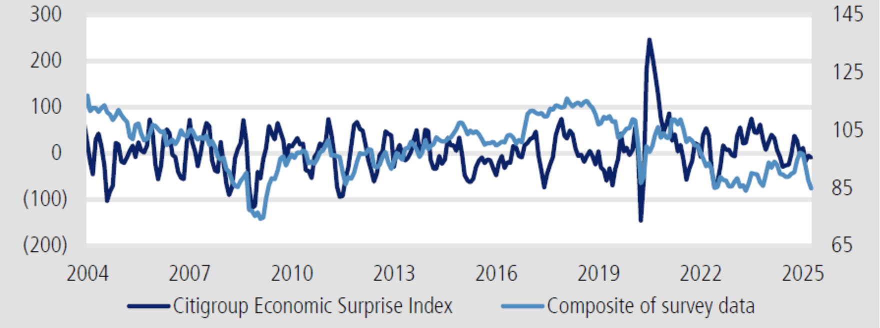
Real personal consumption spending, percent (LHS); real wage, percent (RHS)



Note: Shaded areas are NBER-defined US recessions
Source: Bloomberg; KGI Research

Figure 7: Falling survey data will drag down real data

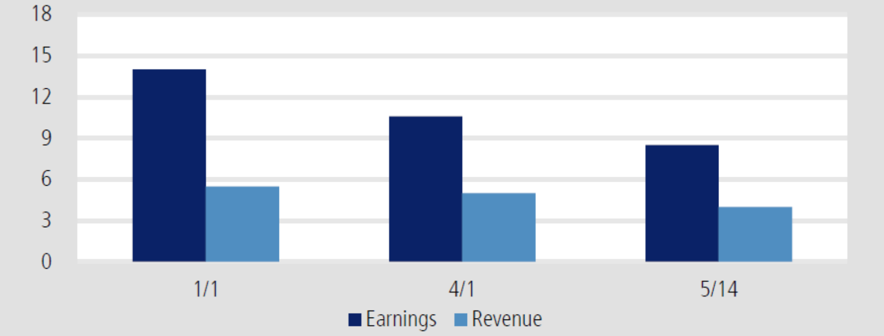
Citi economic surprise index, points (LHS); composite surveyed data, points (RHS)



Note: Surveyed data includes the ISM manufacturing index, NFIB small business optimism index and the University of Michigan consumer sentiment index (January 2003 = 100)
Source: Bloomberg; KGI Research

Figure 8: US corporate earnings forecasts have been cut since early 2025

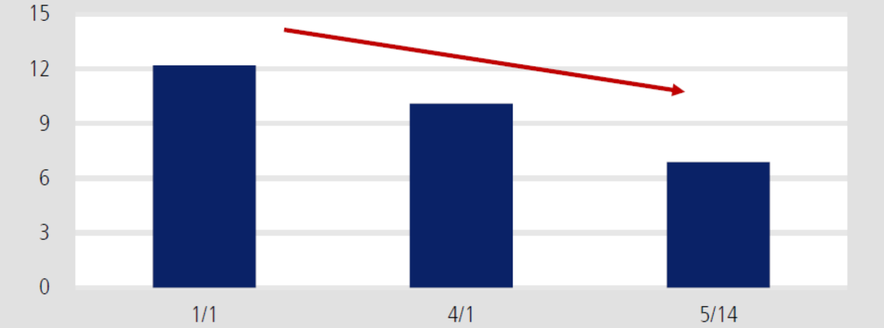
S&P 500 sales and earnings forecast change YoY in 2025, percent



Source: LSEG; KGI Research

Figure 9: 2Q25F earnings also being revised down

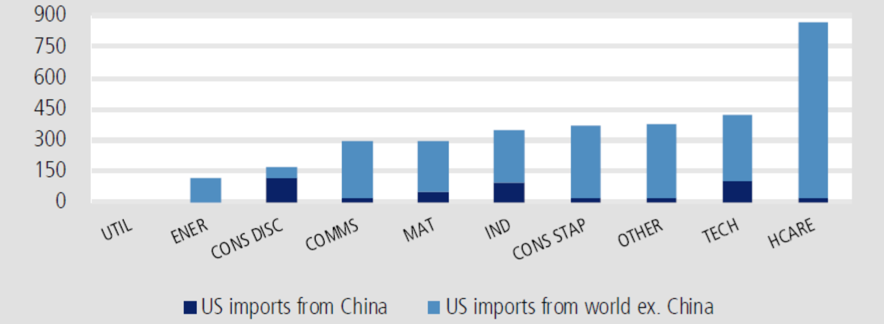
S&P 500 earnings forecast change YoY, percent



Source: LSEG; KGI Research

Figure 10: Weighting of the consumer discretionary sector highest amongst US imports from China

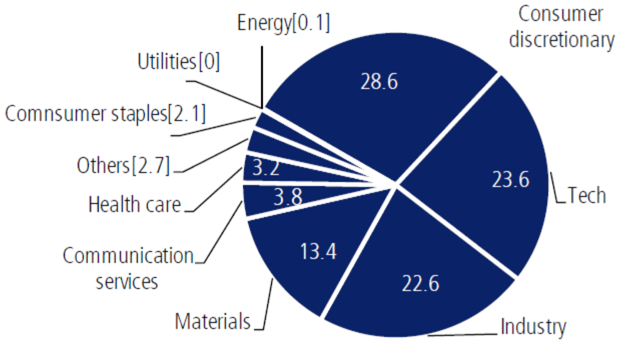
Imports from China and other countries in 2024, US$bn



Source: USITC; KGI Research

Figure 11: Consumer discretionary, tech & industrial plays have the highest weighting in Chinese imports

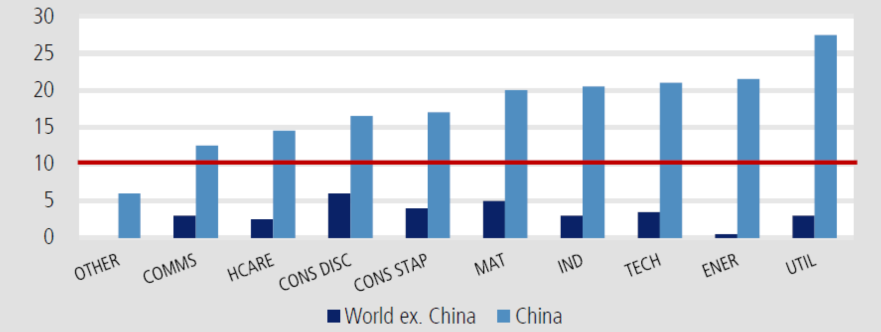
Weighting of Chinese exports to US by sector, percent



Source: USITC; KGI Research

Figure 12: Tariff rates on utilities, energy & tech products, imported from China to the US, are the highest

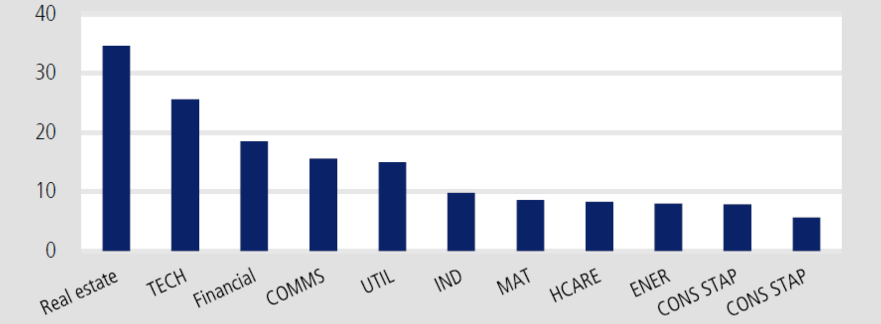
3-month median return by investment style during economic downturn and recession (relative to broader market), percent



Source: USITC; KGI Research

Figure 13: Discretionary consumer & industrial sectors more vulnerable to tariff rises due to low net margins

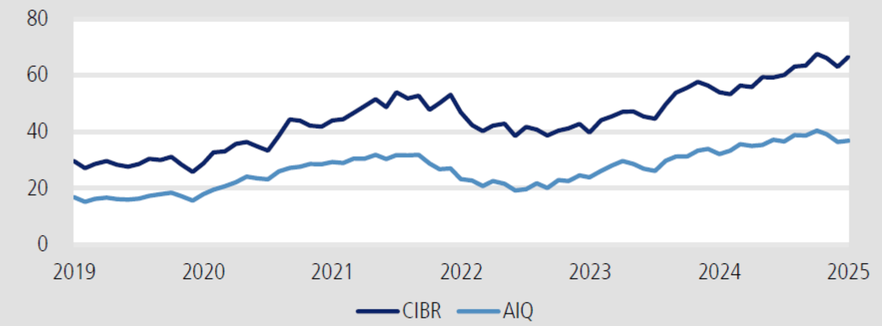
Net margin by US sector, percent



Source: FactSet; KGI Research

Figure 14: Information security a potential bright spot, as it will be more important as AI proliferates in the long-term

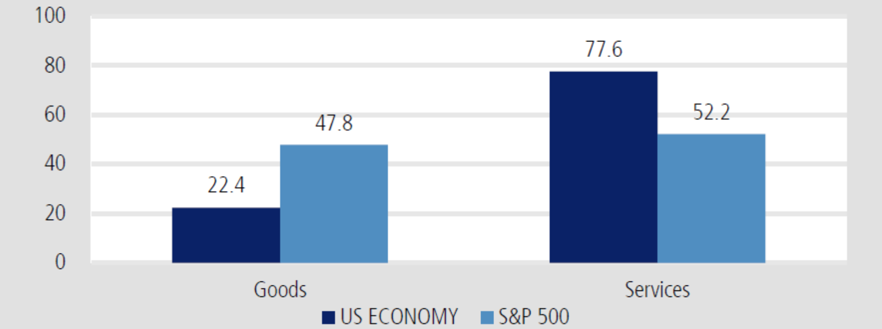
CIBR and AIQ share price, NT$



Source: Bloomberg; KGI Research

Figure 15: US equities more affected by trade wars than the overall economy, as goods have a higher weighting in US stock market than in the overall economy

Goods and services weightings in the US economy and stock market, percent



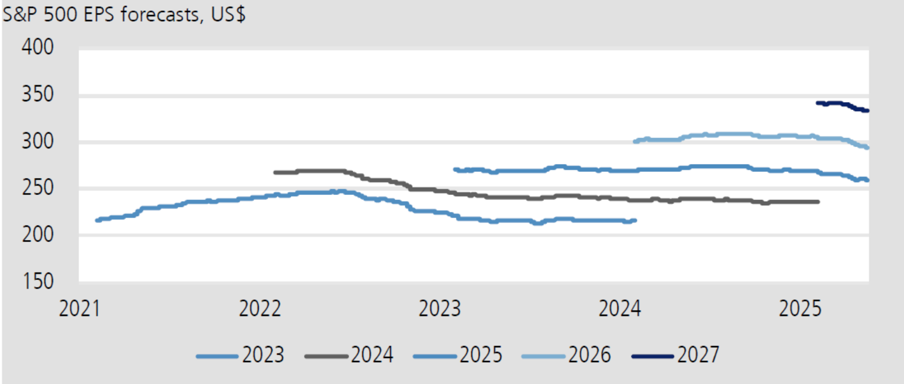
Source: FactSet; KGI Research

Figure 16: Major international political & economic events over next quarter

Date	Major event	Possible effect
6/5	ECB monetary policy meeting	The market expects over 80% chance of a 25bps rate cut; may further widen the yield gap with the U.S.
6/15-17	51th G7 summit	Theme: "Building the Economy, Combating Climate Change, and Managing New Technologies"
6/16-17	BOJ monetary policy meeting	Low probability of a rate hike
6/17-18	Fed FOMC meeting	The market expects a low probability of a 25 bps rate cut, while the trade wars have just begun, and the impact is uncertain

Source: KGI Research

Figure 17: S&P 500 EPS forecasts



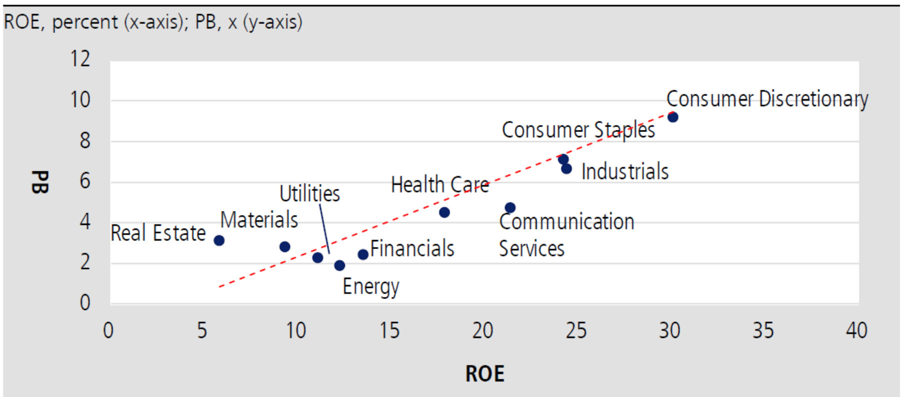
Source: Refinitiv; KGI Research

Figure 18: S&P 500 EPS growth forecasts by sector

	4Q24	1Q25	2Q25	3Q25	4Q25	1Q26	2024	2025	2026
S&P 500	17.1	14.3	5.9	8.0	6.2	10.0	12.1	8.5	13.6
Consumer Discretionary	28.5	9.5	(3.3)	(1.2)	(2.9)	10.2	20.2	0.3	15.2
Consumer Staples	1.5	(5.2)	(2.0)	2.0	5.6	7.3	4.0	0.2	7.9
Energy	(29.3)	(16.6)	(24.4)	(11.0)	(2.5)	4.9	(20.1)	(12.8)	20.0
Financials	35.1	7.0	1.9	8.1	3.2	11.7	18.9	4.7	12.9
Health Care	14.3	46.3	5.7	8.5	9.9	7.9	5.2	15.8	10.8
Industrials	8.0	11.1	2.5	20.2	1.0	11.3	2.4	8.3	16.2
Materials	2.0	0.9	(4.2)	17.3	13.6	17.6	(6.3)	2.4	16.7
Real Estate	15.3	(7.0)	2.8	20.0	1.2	15.5	3.2	4.5	9.2
Information Technology	19.8	19.3	17.5	16.1	13.8	16.6	21.5	16.5	17.2
Communication Services	31.5	31.2	31.0	1.9	4.1	(3.4)	26.2	15.2	9.5
Utilities	12.5	6.1	0.5	(0.8)	8.4	12.1	16.5	5.1	8.0

Source: Refinitiv; KGI Research

Figure 19: S&P 500 PB by sector versus ROE



Source: Bloomberg; KGI Research

Key US economic data

Indicators		Units	2021	2022	2023	2024	May-24	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25
GDP	GDP QoQ SAAR	QoQ %, SAAR						3.0			3.1			2.4			(0.3)	
	GDP YoY	YoY %	6.1	2.5	2.9	2.8		3.0			2.7			2.5			2.0	
Consumer prices	CPI	YoY %	4.7	8.0	4.1	3.0	3.3	3.0	2.9	2.5	2.4	2.6	2.7	2.9	3.0	2.8	2.4	2.3
	Core CPI	YoY %	3.6	6.2	4.8	3.4	3.4	3.3	3.2	3.2	3.3	3.3	3.3	3.2	3.3	3.1	2.8	2.8
	PCE price index	YoY %	4.1	6.6	3.8	2.5	2.6	2.4	2.5	2.3	2.1	2.3	2.5	2.6	2.6	2.7	2.3	
	Core PCE index	YoY %	3.6	5.4	4.2	2.8	2.7	2.6	2.7	2.7	2.7	2.8	2.8	2.9	2.7	3.0	2.6	
Labor market	Labor force participation rate	%	62.0	62.3	62.5	62.5	62.6	62.6	62.7	62.7	62.7	62.5	62.5	62.5	62.6	62.4	62.5	62.6
	Unemployment rate	%	5.4	3.6	3.6	4.0	4.0	4.1	4.2	4.2	4.1	4.1	4.2	4.1	4.0	4.1	4.2	4.2
	Non farm payrolls	'000	7,233	4,555	2,594	2,012	193	87	88	71	240	44	261	323	111	102	185	177
	Net Change In total employment in labor force	'000	6,124	4,555	2,594	2,012	(331)	(9)	64	206	377	(346)	(273)	478	2,234	(588)	201	436
	Challenger job cut announce	YoY %	(1.2)	(1.7)	2.1	(0.9)	(20)	20	9	1	53	51	27	11	(40)	103	205	63
	Opening/ hiring	x	1.56	1.75	1.58	1.43	1.42	1.46	1.38	1.46	1.29	1.42	1.51	1.40	1.45	1.39	1.33	
	Avg. hourly earnings	YoY %	5.0	4.9	4.1	4.0	4.1	3.9	3.6	4.0	3.9	4.1	4.2	4.0	3.9	3.9	3.8	3.8
Economic activity & business condition	Industrial production	YoY %	4.4	3.4	0.2	(0.3)	0.0	0.9	(0.5)	(0.1)	(0.7)	(0.4)	(0.9)	0.4	1.7	1.4	1.3	1.5
	Durable goods orders	YoY %	18.4	8.8	3.7	(1.7)	(0.2)	(9.8)	2.2	(1.0)	(1.8)	4.8	(5.1)	(3.4)	3.5	(0.1)	9.4	
	Core capital goods orders	YoY %	13.4	8.6	(2.5)	(0.6)	(2.8)	(4.0)	(0.6)	(1.8)	0.5	0.2	(1.1)	1.9	3.3	(0.9)	1.5	
	Total business inventory/ sales ratio	x	1.29	1.34	1.37	1.37	1.37	1.38	1.37	1.37	1.37	1.37	1.37	1.35	1.36	1.35	1.34	
	Manufacturing inventory/ sales ratio	x	1.49	1.53	1.59	1.58	1.59	1.58	1.57	1.58	1.58	1.58	1.58	1.58	1.57	1.57	1.57	
	Retail inventory/ sales ratio	x	1.14	1.23	1.27	1.31	1.30	1.32	1.31	1.33	1.33	1.32	1.31	1.29	1.31	1.31	1.29	
	ISM manufacturing index	Point	60.6	53.5	47.1	48.2	48.5	48.3	47.0	47.5	47.5	46.9	48.4	49.2	50.9	50.3	49.0	48.7
	ISM non-manufacturing index	Point	62.4	56.1	52.7	52.4	53.5	49.2	51.4	51.6	54.5	55.8	52.5	54.0	52.8	53.5	50.8	51.6
	ISM manufacturing index: new orders	Point	64.3	51.6	46.0	48.7	46.3	48.9	47.6	45.6	46.7	47.9	50.3	52.1	55.1	48.6	45.2	47.2
	Chicago Fed National activity Index	Point	0.38	(0.00)	(0.13)	(0.15)	0.15	(0.17)	(0.30)	(0.05)	(0.21)	(0.50)	(0.04)	0.37	(0.26)	0.24	(0.03)	
	Conference board leading index	YoY %	7.1	0.4	(7.5)	(4.8)	(5.0)	(4.5)	(4.7)	(4.6)	(4.3)	(3.7)	(3.0)	(3.0)	(2.7)	(3.0)	(3.6)	(4.0)
	C&I Loans for large/medium - tightening lending standard	%	(15.1)	11.8	43.9	9.5			7.9			0.0			6.2			18.5
	C&I Loans for large/medium - stronger demand	%	(1.2)	12.4	(42.3)	(18.2)			0.0			(21.3)			9.4			(20.3)
Housing market	Building Permits	'000, SAAR	1,735	1,684	1,516	1,474	1,407	1,461	1,436	1,476	1,434	1,428	1,508	1,480	1,460	1,454	1,481	1,412
	Housing starts	'000, SAAR	1,603	1,552	1,421	1,371	1,316	1,327	1,265	1,391	1,357	1,352	1,295	1,514	1,358	1,490	1,339	1,361
	New home sales	'000, SAAR	770	637	666	684	672	672	707	691	726	623	676	720	654	674	724	
	Existing home sales	mn, SAAR	6.1	5.1	4.1	4.1	4.1	3.9	4.0	3.9	3.9	4.0	4.2	4.3	4.1	4.3	4.0	
	NAHB housing market index	Point, SA	81	59	44	45	45	43	41	39	41	43	46	46	47	42	39	40
	S&P/Case-Shiller 20-city composite home price index	YoY %	18.7	4.9	6.4	4.6	6.8	6.5	5.9	5.2	4.6	4.3	4.4	4.6	4.8	4.5		
Consumption	Personal expenditures	YoY %, SA	8.8	3.0	2.5	2.8	2.8	2.9	2.9	2.9	3.2	3.1	3.1	3.1	3.1	2.9	3.3	
	Retail sales	YoY %	18.1	9.1	3.5	2.6	2.6	2.0	3.0	1.9	2.0	3.1	3.9	4.6	4.6	3.9	5.2	5.2
	Retail sales ex-autos	YoY %	17.2	10.6	3.3	2.8	2.9	3.4	3.4	2.2	2.5	3.0	3.1	3.7	4.4	4.3	4.4	4.2
	Domestic vehicles sales	mn, SA	179.2	164.8	185.2	189.3	15.9	15.3	15.8	15.1	15.8	16.0	16.5	16.8	15.6	16.0	17.8	17.3
	Conference board consumer confidence	Point	112.7	104.5	105.4	104.5	101.3	97.8	101.9	105.6	99.2	109.6	112.8	109.5	105.3	100.1	93.9	86.0
	Michigan Consumer Sentiment Index	Point	77.6	59.0	65.4	72.5	69.1	68.2	66.4	67.9	70.1	70.5	71.8	74.0	71.7	64.7	57.0	52.2
Fiscal	Budget balance	As % of GDP	(10.4)	(5.3)	(6.3)	(6.9)	(6.0)	(5.4)	(5.4)	(7.0)	(6.2)	(6.9)	(7.1)	(6.9)	(7.2)	(7.2)	(7.0)	(6.8)
Int'l balance	Current account balance	As % of GDP	(3.7)	(3.9)	(3.3)	(3.9)		(3.3)			(3.6)			(3.8)				
	Net foreign securities transactions	US $bn	907	1,321	1,005	761	(4.1)	21.6	102.3	95.0	208.9	118.5	49.9	46.7	(42.1)	112.9	161.8	
Monetary & financial	Federal funds rate	%	0.25	4.50	5.50	4.50	5.50	5.50	5.50	5.50	5.00	5.00	4.75	4.50	4.50	4.50	4.50	4.50
	10-Year treasury yield	%	1.51	3.87	3.88	4.57	4.50	4.40	4.03	3.90	3.78	4.28	4.17	4.57	4.54	4.21	4.21	4.16
	Dollar index	Point	95.7	103.5	101.3	108.5	104.7	105.9	104.1	101.7	100.8	104.0	105.7	108.5	108.4	107.6	104.2	99.5

Source: Bloomberg; KGI Research

Key Taiwan economic data

Indicators		Units	2021	2022	2023	2024	May-24	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25
GDP	GDP YoY	YoY %	6.7	2.7	1.1	4.6		4.9			4.2			2.9			5.4	
Consumer prices	CPI	YoY %	2.0	3.0	2.5	2.2	2.2	2.4	2.5	2.4	1.8	1.7	2.1	2.1	2.7	1.6	2.3	2.0
	Core CPI	YoY %	1.9	2.7	2.4	1.7	1.8	1.8	1.9	1.8	1.8	1.6	1.7	1.7	2.3	1.0	1.7	1.7
Labor market	Unemployment rate	%	3.7	3.6	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	
Economic activity	Industrial production	YoY %	14.7	(1.7)	(12.5)	11.6	16.0	13.3	13.2	13.1	11.8	8.9	10.6	19.8	4.9	18.2	13.7	
	Markit Taiwan manufacturing PMI	Point			46.3	50.9	50.9	53.2	52.9	51.5	50.8	50.2	51.5	52.7	51.1	51.5	49.8	47.8
	NDC monitoring light signal						Yellow-red	Red	Yellow-red	Red	Yellow-red	Yellow-red	Yellow-red	Red	Yellow-red	Yellow-red	Yellow-red	
	NDC monitoring indicators	Point	39.0	24.2	14.4	34.0	36.0	38.0	35.0	39.0	34.0	32.0	34.0	38.0	35.0	37.0	34.0	
	NDC composite leading index	YoY %	4.8	(3.2)	(1.6)	2.0	3.3	4.3	5.1	5.5	5.7	5.6	5.4	5.2	5.0	4.7	4.1	
	NDC composite coincident index	YoY %	8.5	(1.5)	(8.9)	6.3	8.7	9.3	9.4	9.4	9.2	9.2	9.5	9.9	10.3	10.6	10.8	
Consumption	Retail sales	YoY %	3.3	7.4	9.7	3.3	2.6	3.9	3.1	1.1	3.4	(0.5)	2.2	3.1	5.5	(3.8)	0.4	
Trade	Exports	US$bn	446.6	479.7	432.6	475.3	37.4	39.9	39.9	43.6	40.6	41.3	41.1	43.6	38.7	41.3	49.6	48.7
	Imports	US$bn	381.3	428.1	352.1	394.7	31.3	35.2	35.1	32.1	33.5	34.4	33.2	37.5	28.7	34.8	42.6	41.5
	Trade balance	US$bn	65.3	51.6	80.5	80.5	6.1	4.7	4.8	11.5	7.1	6.9	7.9	6.1	10.0	6.6	7.0	7.2
	Export growth	YoY %	29.4	7.4	(9.8)	9.9	3.4	23.4	3.1	16.8	4.5	8.4	9.7	9.1	4.4	31.4	18.6	29.9
	Import growth	YoY %	33.4	12.3	(17.8)	12.1	0.5	33.9	15.8	11.6	17.3	6.0	19.7	30.4	(17.2)	47.5	28.8	33.0
	Export orders	US$bn	674.1	666.8	561.0	589.5	48.9	45.6	50.0	50.2	53.8	55.5	52.3	52.9	47.0	49.5	53.0	56
	Export order growth	YoY %	26.3	(1.1)	(15.9)	5.1	7.0	3.1	4.8	9.1	4.7	4.9	3.3	20.8	(3.0)	31.1	12.5	19.8
Monetary & financial	M1B	YoY %	12.8	4.1	3.1	4.0	5.0	5.2	5.2	4.1	4.1	4.9	4.6	4.0	4.4	3.1	1.8	
	M2	YoY %	8.0	7.1	5.3	5.5	6.0	6.3	6.2	5.8	5.6	5.8	5.5	5.5	5.5	5.2	4.4	
	Foreign reserves	US$bn	548.4	554.9	570.6	576.7	572.8	573.3	571.7	579.1	577.9	576.9	578.0	576.7	577.6	577.6	578.0	582.8
	Rediscount rate	%	1.1	1.8	1.9	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
	Exchange rate	USD/TWD	27.7	30.7	30.7	32.8	32.4	32.4	32.8	32.0	31.7	32.0	32.5	32.8	32.7	32.8	33.2	32.0

Source: Bloomberg; KGI Research

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