



Q3 2025 - TARIFF TURBULENCE

Global markets reached record highs this quarter before experiencing volatility due to the sequencing of President Trump's election pledges - tariffs, tax cuts and deregulation - that's come in a painful manner for investors.

Trumps Tough Love

Markets are coming to terms that Trump's second iteration as President is becoming distinctly different from Trump's first when the share market performance was his political scoreboard.

Trump focus on reshaping global trade agreements to support domestic manufacturing is likely to lead to higher inflation and lower global growth. Despite tougher trade sanctions, economies remain supported by high government spending and solid consumption, with full employment and wage increases.

However, business and consumer confidence are waning, which could eventually impact economic data, company earnings, and forward guidance.

Less Exceptional

US equities began the year trading on elevated market multiples, that left little room to absorb any major shocks, and this has pressured risk assets. The S&P 500 fell by 4.5%, ending a five-quarter winning streak, while the 'Magnificent 7' major tech stocks saw significantly greater declines.

Growth and momentum trades, particularly in Artificial Investments (AI), reversed as Chinese AI startup DeepSeek challenged market expectations with its low-cost offerings.

Consequently, both large- and small-cap equities, especially growth stocks, suffered. The Dow Jones Industrial Average fared better, down just over 1%, while the Nasdaq shed 10%, wiping out more than half of last year's gains.

The Small Cap Russell 2000 fell by around 10% as investors shunned risk. The upcoming US quarterly earnings season is expected to be the weakest of the year, with a stronger recovery in later quarters.

Resilient Australian Market

Australia's labour market remains strong, with unemployment at 4.0%, near a 50-year low. Inflation is now within the Reserve Bank of Australia's 2-3% target band, leading to a cash rate

cut to 4.10% in February, the first cut since November 2020. The S&P/ASX 200 index declined by less than 3%, performing better than many developed market peers. However, business and consumer confidence are waning, which could eventually impact economic data and company earnings.

The domestic mid-cap earnings season in May and major banks report half-year results, will be a critical test for sentiment particularly towards the lagging small caps.



European and Chinese Markets Surge

Europe emerged as a standout performer, with the Euro Stoxx 600 rising by 5%, driven by fiscal spending plans, particularly in defence.

Chinese shares rose by 15%, boosted by the emergence of AI and potential further stimulus to offset tariffs. Japanese stocks, however, fell by 10% due to concerns over US tariffs impacting its export-reliant economy.

Defence is the new Offence

Investors have turned to defensive assets like gold, cash, and fixed-rate bonds to protect their portfolios during times of uncertainty. Gold rallied by 19% in the first quarter, benefiting from trade war fears, weaker global growth, and elevated risk. This was its best quarterly performance since the third quarter of 1986.

Gold equities outperformed and delivered outsized returns as cash flows surged and the M&A cycle is just heating up.

Market Multiples Compress

Equity valuations have been de-rated due to uncertainty. The upcoming reporting season will reveal if current valuations are justified. The de-rating has been driven by price rather than earnings.

Historical data shows that during the last four US recessions, the trough forward P/E ratios were significantly lower than current levels, suggesting potential further downside if economic conditions worsen.

China's Response

China's incremental stimulus and a weaker US dollar have supported commodities, particularly iron ore.

The size and magnitude of China's stimulus plans remain a swing factor for the Australian economy.

Iron ore looks relatively defensive among commodities, given China's policy flexibility and potential to lift infrastructure spending to counter tariffs.



Australian Economy

Australia has limited direct trade exposure to the US, which may help avoid a recession. A lower Australian dollar could make exports more competitive, and cheaper imports from redirected Chinese exports could benefit consumers.

This could help discretionary stocks, with recent trading updates from retailers being broadly encouraging despite weaker consumer sentiment.

A Bland Federal Budget

The Federal Budget focused on cost-of-living relief measures, such as energy rebates and reduced medicine costs, with minor fiscal deficit increases providing a small economic boost. This should permit further RBA interest rate cuts post-election.

With only subtle policy changes between both major parties, polling is likely to be tight, and a minority government is looking more likely.



Opportunities amidst the Noise

US recession risks have increased, with some probability now priced into equities. Markets are expected to remain volatile as tariff policies evolve and earnings revisions catch up.

While it may be too late to sell many stocks given the sharp pullback, investors may find opportunities to add to equities over the coming months.

Sanity is likely to prevail on tariffs, as Trump's policies have significantly impacted US households' personal wealth, and the next year's midterm elections could pose challenges for his party if the market malaise continues.



Lost amongst the tariff noise is Trump has far more market positive agendas to pursue such as tax cuts and deregulation later in the year which are likely to come with lower interest rates.

Despite the volatility, there are significant opportunities for those willing to navigate the uncertainty. Many stocks have fallen more than the broader market correction, presenting potential for active investors to seek out significant mispriced opportunities.