13 March 2025

FUNDAMENTAL FLASH

Letting it Sink | Bracing for US Policy Shifts

Prepared by AHAM Asset Management

US equities are nearing correction territory this week, with the S&P 500 index falling over 8% from its peak 19 Feb 2025, wiping out more than USD 4 trillion in market value[1].

Tariff angst and fears of an economic slowdown have weighed heavily on sentiment, reversing much of the post-election optimism that had propelled markets higher following Trump's win last year.

Read more in our latest Fundamental Flash as we delve into the reasons behind this shift and what lies ahead.

A Pause in US Exceptionalism?

Several factors have contributed to the current sell-off:-

Tariff Uncertainty

The ongoing unpredictability in trade policy has created a challenging environment for businesses.

The frequent reversals in tariff announcements have left companies hesitant to commit to capital expenditures and hiring, slowing economic activity. Without greater policy clarity, businesses are likely to remain cautious, prolonging economic uncertainty.

Fiscal Tightening

The reduction in federal government spending through the newly set-up Department of Government Efficiency (DOGE) is also taking a toll on economic activity.

It is estimated that over 30,000 federal employees would be laid off. While this figure represents a small fraction of total US employment, the broader impact of spending cuts on economic activity cannot be ignored, particularly in sectors reliant on government contracts and public-sector demand.

Flashpoints

- US market selldown has intensified this week as tariff fatigue and fears of an economic slowdown weigh on sentiment.
- Uncertainty in US trade policy and government spending cuts have dampened business confidence, slowed investments, and put pressure on economic activity.
- The Trump administration appears to be front-loading economic pain early in his term, potentially paving the way for a policy shift toward growth measures ahead of the 2026 midterm elections.
- A weaker USD and lower global interest rates could provide support for Asian markets, with China and India positioned to benefit from policy stimulus and a shift in fund flows.
- While external and domestic factors have weighed on Malaysian equities, strong domestic fundamentals, policy execution, and FDI inflows could drive a recovery.

Short-Term Pain for Long-Term Gain?

We believe Trump is deliberately front-loading economic pain through tariffs and federal spending cuts through the DOGE by implementing unpopular measures early in his term. This phase of economic strain could last for a few quarters.

However, as the 2026 midterm elections approach, we expect a shift back toward pro-growth policies to align strategically with the US political calendar. By absorbing the short-term fallout early, the Trump administration can shift toward pro-growth measures closer to the election cycle, bolstering its political standing.

While certain spending cuts and government efficiency improvements could bring benefits over the long run, we would remain vigilant over potential unintended consequences. As with any major policy shift, trade-offs are inevitable.

What's Next?

We believe that the administration is unlikely to push the US economy into a full-blown recession, as doing so would carry significant political costs. If economic conditions deteriorate further, we expect policymakers to soften their stance, particularly on trade.

Additionally, any successful trade negotiations or even modest concessions from key trading partners could serve as a catalyst for markets to stabilise. Our base case is that tariffs are being used as a bargaining chip rather than a long-term strategy, suggesting room for potential relief.

If our current base case is right, the recent equity market weakness could be an opportunity for long-term investors.

Asia Stands to Benefit from Capital Shifts

The short-term disruption in the US from tariffs and government spending policies could create opportunities for Asian equity markets—provided it does not trigger a severe downturn in the US. A weaker US dollar and lower global interest rates would be broadly supportive of Asian economies, particularly as investors look beyond the US market in search of stronger earnings growth.

China and India stand out as potential beneficiaries of this shift. In China, policymakers have become increasingly supportive of private enterprises, particularly in the technology sector, in their quest to achieve artificial intelligence (AI) parity with the US. At the same time, measures to stimulate domestic consumption could help pull the economy out of a deflationary loop, providing a more sustainable path to growth.

Meanwhile, India has undergone a 5-month market correction amid slowing economic momentum, bringing valuations back in line with their 5-year average. Encouragingly, policymakers have already taken steps to support the economy, including income tax cuts, shoring up liquidity, and more accommodative lending policies.

Malaysia | Fundamentals to Prevail

Malaysia equities have been similarly weighed down by a combination of external and domestic factors. The lingering threat of US tariffs, concerns over a slowdown in data centre spending, and renewed strength in Chinese equity markets have all contributed to volatility.

Malaysia | Fundamentals to Prevail *(cont')*

However, we believe the market reaction has been overdone. Once the dust settles, investors are likely to refocus on Malaysia's strong domestic fundamentals, underpinned by ongoing policy execution and foreign direct investment (FDI) inflows.

Looking ahead, we see potential catalysts for a recovery. A liquidity injection from government-linked funds in 2Q'25 could help lift sentiment and provide support for the market. Against this backdrop, our portfolio remains centered on quality large-cap stocks, which we expect to recover first as foreign funds return.

Staying the Course

The shifting US policy landscape has introduced near-term headwinds, but it also sets the stage for longer-term adjustments that investors can capitalise for their portfolios.

Asia stands to benefit from capital flows seeking growth beyond the US, while Malaysia's strong fundamentals will come through as macro clarity improves. As sentiment stabilises, investors with a long-term perspective may find compelling entry points.

***

Correction

1. An earlier version of this article incorrectly stated that the S&P 500 index fell over 8% from its 2019 peak. The correct information is that the S&P 500 index fell over 8% from its 19 February 2025 peak, wiping out more than USD 4 trillion in market value. We apologise for the error.

Disclaimer