Markets in correction mode: A rebound, but volatility may persist

Multi Asset Solutions Team

Key points

- The market correction began with an AI-related expectations reset before spreading more broadly, amplified by policy uncertainty, tighter export controls, hawkish central-bank commentary and crowded positioning.
- Markets subsequently rebounded following the reinstatement of the Chief Executive Officer (CEO) at a leading US chip designer, easing some immediate concerns about leadership continuity. However, wider questions around AI valuations, regulation and policy remain.
- Economic and corporate fundamentals remain relatively supportive, suggesting the sell-off is still more consistent with a valuation adjustment than a broad deterioration in the outlook.
- Further market rebounds are possible after sharp declines, but lower seasonal liquidity and continued policy uncertainty may keep volatility elevated.
- Government bonds have benefited from demand for perceived safe-haven assets, while a more durable equity recovery may require some easing in financial conditions.
- Investors should prepare for continued market fluctuations by maintaining diversification, managing concentration risks and keeping portfolios aligned with their objectives and tolerance for risk.

From AI enthusiasm to a broader reset

Global markets entered a period of correction after a strong run led by artificial intelligence and related technology shares. The initial weakness reflected a reassessment of elevated valuations and the significant capital spending needed to sustain AI growth. Investigations involving a leading US chip designer, together with expectations of tighter US controls on exports of advanced chip technology, added uncertainty. More hawkish comments from the US central bank also weighed on investor sentiment.

As prices fell, the correction broadened beyond technology. Crowded and leveraged positions appear to have magnified the move, as some investors reduced risk or sold assets to meet margin requirements. This combination of changing expectations and technical selling helps explain why market declines became sharper and more widespread than the initial news might have suggested.

Markets have since staged a rebound following the reinstatement of the CEO at the leading US chip designer. The development helped to ease some immediate concerns about leadership continuity at a company that plays an important role in the AI ecosystem. Nevertheless, the rapid shift in sentiment, from a sharp sell-off to a subsequent recovery, illustrates how sensitive markets remain to company-specific developments and changing headlines.

Importantly, this does not necessarily imply that the long-term AI investment theme has ended. Demand for computing capacity remains strong, while investment in data centres, cloud infrastructure and advanced semiconductors continues. However, investors are becoming more demanding. Companies will increasingly need to show that substantial AI spending can generate sustainable revenue, cash flow and returns on investment. This is likely to create greater differentiation between businesses and reduce the appeal of treating all AI-related companies as a single investment theme.

Fundamentals offer support, but volatility may persist

The broader backdrop remains relatively constructive. Corporate earnings have generally been resilient, technology earnings revisions have remained positive, and recession risks appear contained. Credit markets have also held up comparatively well. Together, these signals suggest that the correction has so far been driven more by

lower valuations and an expectations reset than by evidence of widespread economic or financial stress.

The market rebound is encouraging, but it should not be interpreted as confirmation that the period of volatility has ended. Following a sharp sell-off and increasingly oversold market conditions, further near-term gains are possible. Nevertheless, investors should be prepared for additional swings. Trading volumes and liquidity are often thinner around the US Thanksgiving period, which can amplify market movements in either direction. Uncertainty over technology regulation, AI-related capital spending and monetary policy could also continue to trigger abrupt changes in sentiment.

A more durable equity recovery may depend on financial conditions becoming less restrictive. Hawkish central-bank rhetoric can place upward pressure on borrowing costs and valuation discount rates, particularly for growth companies whose expected profits lie further in the future. By contrast, expectations of lower interest rates or declining bond yields could provide a more supportive environment.

Implications across asset classes and regions

Government bonds have benefited from safe-haven demand as investors sought more defensive assets. If economic growth remains resilient, however, the path for bonds may be uneven because persistent inflation or hawkish policy guidance could limit the scope for yields to fall.

Within equities, the correction reinforces the case for selectivity. Businesses with sustainable earnings, healthy balance sheets and a credible path to monetising investment may be better placed than companies whose valuations rely mainly on optimistic long-term assumptions. Defensive and income-oriented sectors may also provide diversification when highly valued growth shares are under pressure.

The speed of both the sell-off and the rebound also highlights the risks of concentrated exposure to individual companies or investment themes. A diversified allocation across sectors, regions and asset classes may help portfolios manage periods when market leadership changes rapidly. Diversification does not eliminate losses, but it can reduce dependence on a single source of return.

In Asia, policy-led stabilisation measures in South Korea, Taiwan and China have offered some support to equity sentiment. Even so, the region remains sensitive to global technology demand, US trade policy and potential restrictions on advanced semiconductor exports.

What this means for investors

Corrections can be uncomfortable, but they are a normal feature of investing. They may also create opportunities when sound long-term fundamentals remain intact and valuations become more reasonable. At the same time, the recent rebound should not encourage investors to overlook the possibility of renewed volatility.

Rather than reacting to short-term headlines, investors should review whether their portfolios remain aligned with their objectives, investment horizon and tolerance for risk. Maintaining diversification across asset classes, regions, sectors and investment styles can help reduce reliance on any single market theme.

Preparing for volatility may include reviewing portfolio concentration, maintaining an appropriate balance between growth and defensive assets, and avoiding investment decisions driven solely by sharp daily market movements. Investors should also ensure that the level of risk in their portfolios remains suitable for their financial circumstances and ability to withstand potential losses.

In the current environment, discipline and selectivity remain especially important. A sustained recovery may take time, and markets could experience further setbacks along the way. Staying focused on long-term objectives while actively managing portfolio risks may place investors in a better position to navigate both the opportunities and uncertainties ahead.

Important information

Manulife Investment Management is the global wealth and asset management segment of Manulife Financial Corporation. The information and/or analysis contained in this material have been compiled or arrived at from sources believed to be reliable but Manulife Investment Management does not make any representation as to their accuracy, correctness, usefulness or completeness and does not accept liability for any loss arising from the use hereof or the information and/or analysis contained herein. Neither Manulife Investment Management or its affiliates, nor any of their directors, officers or employees shall assume any liability or responsibility for any direct or indirect loss or damage or any other consequence of any person acting or not acting in reliance on the information contained herein.

This material was prepared solely for educational and informational purposes and does not constitute a recommendation, professional advice, an offer, solicitation or an invitation by or on behalf of Manulife Investment Management to any person to buy or sell any security. Nothing in this material constitutes investment, legal, accounting or tax advice, or a representation that any investment or strategy is suitable or appropriate to your individual circumstances, or otherwise constitutes a personal recommendation to you. The economic trend analysis expressed in this material does not indicate any future investment performance result. This material was produced by and the opinions expressed are those of Manulife Investment Management as of the date of this publication, and are subject to change based on market and other conditions. Past performance is not an indication of future results. Investment involves risk, including the loss of principal. In considering any investment, if you are in doubt on the action to be taken, you should consult professional advisers.

Proprietary Information – Please note that this material must not be wholly or partially reproduced, distributed, circulated, disseminated, published or disclosed, in any form and for any purpose, to any third party without prior approval from Manulife Investment Management.

This material has not been reviewed by, are not registered with any securities or other regulatory authority, and may, where appropriate, be distributed by Manulife Investment Management and its subsidiaries and affiliates.