Anatomy of a Looming Bear Market: How to Assess the Impact of Donald Trump's Chaotic Economic Measures on Wall Street

Anatomie d'un marché baissier imminent : comment évaluer l'impact des mesures économiques chaotiques de Donald Trump sur Wall Street

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Abstract

Financial markets are highly sensitive to macroeconomic policies, particularly those affecting corporate earnings growth and investor sentiment. The Trump administration's protectionist measures, trade conflicts, and labor market disruptions have led to a sharp deterioration in corporate earnings perspectives, impacting stock valuations. This paper evaluates these effects using the Potential Payback Period (PPP), a valuation metric superior to traditional methods like the Price-to-Earnings (P/E) and PEG ratios. By integrating earnings growth, discount rates, and risk factors, the PPP provides a comprehensive framework for understanding market shifts. Findings indicate that as earnings growth expectations decline, the PPP lengthens, SIRREP drops, and SRP turns negative, signaling a shift from undervaluation to overvaluation. This transition suggests an impending bear market and underscores the PPP's predictive value in assessing market cycles.

Keywords : Stock Market Valuation, Potential Payback Period (PPP), Corporate Earnings Growth, SIRREP, Stock Risk Premium (SRP), Donald Trump's Economic Policies

Résumé

Les marchés financiers sont extrêmement sensibles aux politiques macroéconomiques, en particulier celles qui influencent la croissance des bénéfices des entreprises et le sentiment des investisseurs. Les mesures protectionnistes de l'administration Trump, les conflits commerciaux et les perturbations du marché du travail ont entraîné une détérioration marquée des perspectives bénéficiaires des entreprises, impactant ainsi la valorisation de leurs actions en Bourse. Cet article évalue ces effets en utilisant le Potential Payback Period (PPP), un indicateur d'évaluation supérieur aux méthodes traditionnelles telles que le ratio Price-to-Earnings (P/E) et le PEG. En intégrant la croissance des bénéfices, les taux d'actualisation et les facteurs de risque, le PPP offre un cadre d'analyse complet pour comprendre les fluctuations du marché. Nos études confirment que lorsque les attentes en matière de croissance des bénéfices diminuent, le PPP s'allonge, le SIRREP (rentabilité interne) baisse et le SRP (prime de risque) devient négatif, signalant un passage de la sous-évaluation à la surévaluation du marché des actions. Les dernières estimations indiquent un marché baissier imminent et souligne la valeur prédictive du PPP dans l'évaluation des cycles boursiers.

Mots-clés : Valorisation des Marchés Boursiers, Potential Payback Period (PPP)**,** Croissance des Bénéfices des Entreprises, SIRREP, Prime de Risque des Actions **(**SRP**),** Politiques Économiques de Donald Trump

Introduction

The stock market is highly sensitive to changes in economic conditions, particularly corporate earnings growth, which serves as a fundamental driver of stock valuation. Under the disruptive economic policies of Donald Trump's administration—marked by aggressive protectionism, trade wars, deregulation, and labor market disruptions—U.S. corporations are expected to experience a significant contraction in their earnings growth, potentially triggering a market decline of uncertain magnitude. Traditional valuation metrics such as the Price-to-Earnings (P/E) ratio and the Price/Earnings to Growth (PEG) ratio have proven insufficient in such volatile environments, as they fail to fully integrate critical factors like interest rates, risk premiums, and the compounded nature of earnings growth. To address this gap, our study introduces the Potential Payback Period (PPP) methodology, which incorporates compounded earnings growth, discounts future earnings using relevant interest rates, and adjusts for inherent risks stemming from policy uncertainty and market volatility. This comprehensive approach not only enables a more accurate assessment of stock market valuations but also provides early warnings of transitions between undervaluation and overvaluation—critical indicators of impending bear markets.

The article is structured as follows: first, we examine how Trump's economic policies are precipitating a contraction in earnings growth; next, we detail the innovative aspects of the PPP and its superiority over traditional metrics; following that, we analyze recent shifts in the S&P 500 from undervaluation to overvaluation using empirical data; and finally, we conclude by discussing the implications of the PPP as a reliable indicator for navigating market cycles.

1. Why Trump's Economic Policies Are Leading to an Earnings Growth Contraction

Donald Trump's economic policies have introduced significant strains on corporate earnings growth in the United States, primarily through heightened protectionism, labor market disruptions, and increased market volatility. By imposing aggressive tariffs, altering immigration policies, and embracing an economic philosophy that views recession as a necessary corrective measure, the administration has fundamentally reshaped the environment in which businesses operate. This section explores four key factors—protectionist trade policies, labor market disruptions, investor uncertainty, and the acceptance of recession as a policy tool—that collectively exert downward pressure on corporate earnings.

1.1. Protectionist Trade Policies and Tariffs

The imposition of tariffs on steel, aluminum, and lumber has led to a marked increase in production costs for U.S. manufacturers, forcing many companies to either absorb these

additional expenses or pass them on to consumers. At the same time, major trading partners like China and Canada have retaliated by imposing tariffs on American goods, which reduces the competitiveness of U.S. exports abroad and subsequently curtails revenue growth for multinational corporations. Adding to the complexity, the unpredictable nature of Trump's tariff decisions has contributed to an atmosphere of heightened uncertainty, discouraging businesses from making long-term investments in capacity expansion or research and development. This reluctance to invest not only constrains future earnings growth but also undermines overall economic dynamism.

1.2. Labor Market Disruptions

Labor market disruptions under Trump's administration have taken multiple forms, notably through stricter immigration enforcement and large-scale budget cuts. The mass deportation of undocumented workers has particularly impacted sectors like agriculture and construction, where labor shortages and escalating wage costs have strained profit margins. In parallel, the dismissal of federal employees in the name of fiscal austerity has led to a contraction in consumer spending, as laid-off workers reduce their consumption and demand for goods and services. The combined effect is a downward pressure on corporate revenues across various industries, further weakening the outlook for earnings growth.

1.3. Investor Uncertainty and Market Volatility

A defining feature of Trump's economic approach is its volatility, shaped by abrupt policy shifts and controversial public statements. This unpredictability has been a key driver of market turbulence, as evidenced by significant declines in major stock indices. For instance, high-profile companies like Tesla have experienced massive valuation losses—dropping 40% post-election—reflecting investor doubts about the long-term stability of U.S. economic policy. On March 10, the S&P 500 and the Nasdaq Composite fell by 2.7% and 4.0%, respectively, in a single trading session, signaling a collective reassessment of corporate earnings prospects. Such volatility not only erodes investor confidence but also raises the cost of capital, making it harder for companies to fund expansion or research initiatives.

1.4. Acceptance of Recession as a 'Necessary Evil'

Perhaps the most consequential element of Trump's economic stance is the administration's apparent willingness to endure—or even precipitate—a recession as part of a broader "detox" strategy. Trump and his economic advisors argue that the U.S. economy has become overly reliant on public spending and international trade, necessitating a period of pain to restore balance and competitiveness. By framing recession as a "necessary evil," the administration

amplifies concerns about a protracted slowdown in both economic growth and corporate earnings. If businesses and consumers alike anticipate a recessionary climate, they may cut back on spending and investment, thus creating a self-fulfilling prophecy that further drags down earnings growth and stock market valuations.

2. The Potential Payback Period (PPP) : A Unique Metric for Predicting Both Bull and Bear Markets

Stock markets experience cycles of expansion (**bull markets**) and contraction (**bear markets**), driven by factors such as earnings growth, interest rates, and investor sentiment. Traditional valuation metrics like the **Price-to-Earnings (P/E) ratio** and **Price/Earnings to Growth (PEG) ratio** fail to fully capture the forces behind these cycles because they ignore key financial variables, particularly the effects of risk, discount rates, and the compounding nature of earnings growth.

The **Potential Payback Period (PPP)** stands out as a superior metric for predicting **both** market uptrends and downturns. By integrating **earnings growth, interest rates, and risk factors** into a single measure, PPP dynamically adjusts to changing market conditions, providing early warning signals of market shifts.

2.1. PPP Predicts Bull Markets by Identifying Undervaluation

In a bull market scenario, equities are considered undervalued relative to their future earnings potential. The PPP identifies these opportunities by incorporating earnings growth in a compounded manner, making it more sensitive to accelerating profitability than the constant-earnings assumption inherent in the P/E ratio. Furthermore, by factoring in a low discount rate (r), the PPP effectively increases the present value of future earnings, thereby reducing the period required to recoup the investment. This reduction in the PPP signals that stocks are attractively priced compared to bonds. In addition, when the Stock Internal Rate of Return including Exit Price (SIRREP) exceeds the risk-free rate, it confirms that stocks offer a compelling risk-adjusted return, which in turn encourages capital inflows into the equity market.

2.2. PPP Predicts Bear Markets by Identifying Overvaluation

Conversely, the PPP also serves as a robust indicator for predicting bear markets by identifying signs of overvaluation. When projected earnings growth decelerates, the PPP lengthens, indicating that stocks are taking longer to justify their current high valuations. In such cases, if the SIRREP falls below the risk-free rate, investors may find that they are better off reallocating their capital to bonds, prompting a shift away from equities. Moreover, when the Stock Risk

Premium (SRP), defined as SRP = SIRREP – Risk-Free Rate, turns negative, it signifies that equities no longer provide sufficient compensation for the risk incurred. This negative SRP is a clear signal of market overvaluation and serves as an early warning of an impending downturn. Through its comprehensive incorporation of compounded earnings growth, discount rates, and risk adjustments, the PPP offers a unique and dynamic framework for predicting both bullish and bearish market conditions.

3. How the S&P 500 Recently Shifted from Undervaluation to Overvaluation

Recent market data reveal a dramatic transition in the U.S. stock market, as exemplified by the S&P 500 index. This section explores how, within a relatively short timeframe between January 2025 and March 2025, market valuation shifted from an undervalued state to one of overvaluation—a change largely driven by the contraction in corporate earnings growth resulting from Trump's controversial economic measures.

3.1. A shift from a Bull Market to a Bear Market

A sudden shift from a **Bull Market to a Bear Market** emerged in the U.S. stock market between **January 2025 and March 2025** due to the **Donald Trump administration's controversial economic measures**, as detailed in Section 1, **"Why Trump's Economic Policies Are Leading to an Earnings Growth Contraction."**

This shift is evident in the **S&P 500 index**, where **annual earnings growth is expected to contract by half, from 18% to 9%, in the coming years**. The SIRREP evolution in the S&P 500 illustrates how market valuation shifted dramatically between January 31, 2025, and March 7, 2025:

Date	P/E Ratio	Growth Rate (g)	Discount Rate (r)	PPP	SIRREP	SRP
January 31, 2025	30.00	18.0%	4.50%	17.22 years	6.51%	+2.01%
March 7, 2025	28.84	9.0%	4.32%	22.49 years	4.28%	-0.04%

As the projected earnings growth rate contracted by half, from 18% to 9%, the PPP lengthened and the SIRREP dropped below the risk-free rate, shifting the market from undervaluation to overvaluation and signaling a downturn.

3.2. Sensitivity Analysis

To assess potential market outcomes, **a sensitivity analysis** can be conducted, considering different earnings growth scenarios ranging from **6% to 11%**. Notably, when the growth rate

falls **below 10%**, the **SIRREP drops below the risk-free rate**, represented by the **10-year U.S. Treasury yield**. This results in a **negative Stock Risk Premium (SRP)**—a key indicator of a **Bear Market**, often associated with an **economic recession**.

SENSITIVITY ANALYSIS OF SIRREP ON EARNINGS GROWTH RATE "g"
(Data as of March 7, 2025)

The Stock Risk Premium (SRP) is the difference between SIRREP and a risk-free rate, such as the 10-year U.S. Treasury yield (4.32% in this case)

	g (%)	PPP (years)	SIRREP (%)	SRP (%)
1	6.0	26.03	3.12	-1.2
2	7.0	24.69	3.52	-0.8
3	8.0	23.52	3.9	-0.42
4	9.0	22.49	4.28	-0.04
5	10.0	21.57	4.66	0.34
6	11.0	20.75	5.03	0.71

To fully grasp the implications of the SIRREP dropping below the 10-year U.S. Treasury yield—leading to a negative SRP—it is crucial to recognize that SIRREP functions similarly to a bond's Yield to Maturity (YTM).

3.3. The SIRREP is comparable to a bond's Yield to Maturity (YTM)

Both metrics represent an internal rate of return (IRR)—SIRREP for stocks and YTM for bonds—where future cash flows (earnings for stocks, coupons for bonds) are discounted back to their present value, including the redemption at face value for bonds and the exit price for stocks.

This structural similarity makes the **10-year Treasury yield an objective and neutral benchmark** for evaluating stock attractiveness. Just as investors compare bond yields to assess relative value, they can compare **SIRREP to the risk-free rate** to determine whether equities offer sufficient compensation for their inherent risks. When **SIRREP falls below the 10-year Treasury yield**, it signals that equities no longer provide an adequate risk premium over risk-free government bonds, prompting capital reallocation from stocks to bonds. This shift is a classic indicator of a transition from a Bull Market to a Bear Market, reinforcing the importance

of measuring SIRREP against the 10-year Treasury yield—via the SRP—as a reliable market valuation tool.

3.4. The Stock Risk Premium (SRP): A key indicator

The deeper the SRP sinks into negative territory, the sharper the decline in stock prices. However, after some time, this drop will mechanically trigger—through a contraction of the P/E ratio—a rebound in SIRREP, eventually pushing the SRP back into positive territory. Such a shift is a necessary condition for transforming a Bear Market into a Bull Market. The Bull Market will be confirmed when investors perceive an improvement in fundamental factors, particularly a renewed positive inflection in corporate earnings growth. Ultimately, after potential stock price rebounds driven by "technical corrections," this shift in earnings expectations will serve as the true foundation of a new Bull Market, marking the beginning of a new economic cycle.

Conclusion: PPP as the Ultimate Market Cycle Indicator

Our analysis demonstrates that stock markets inherently oscillate between bull and bear phases, driven primarily by fluctuations in earnings growth expectations, prevailing interest rates, and overall investor risk sentiment. The Potential Payback Period (PPP) emerges as the ultimate market cycle indicator because it dynamically incorporates these critical variables—compounded earnings growth, discount rates, and risk factors—into a single, comprehensive metric.

In a bull market, where corporate earnings are robust and accelerating, the PPP remains low. This is coupled with a high Stock Internal Rate of Return including Exit Price (SIRREP) that exceeds the risk-free rate, resulting in a positive Stock Risk Premium (SRP = SIRREP – Risk-Free Rate). These conditions confirm that stocks are undervalued, signaling potential for further market upside and encouraging capital inflows. Conversely, in a bear market scenario, expectations for earnings growth wane, causing the PPP to lengthen. When the SIRREP falls below the risk-free rate, the SRP turns negative, indicating that equities no longer provide adequate compensation for their risk. This overvaluation serves as a warning signal, suggesting an impending market correction.

By leveraging PPP-derived metrics, investors can anticipate market cycles early, adjust their portfolios proactively, and optimize risk-adjusted returns more effectively than with traditional valuation methods. Beyond merely forecasting declines, the PPP offers a holistic framework for understanding the entire market cycle—making it an indispensable tool for navigating both bullish and bearish conditions in today's dynamic economic landscape.

Scientific Implications

This research contributes to the financial literature by providing a more robust valuation framework that integrates earnings growth, risk factors, and interest rates into a single predictive model. The Potential Payback Period (PPP) serves as an alternative to traditional valuation metrics like the Price-to-Earnings (P/E) ratio and the Price/Earnings to Growth (PEG) ratio, which often fail to capture the dynamic nature of market cycles. By refining the analytical tools available to investors and policymakers, this study enhances our understanding of stock market behavior in response to economic disruptions, such as those induced by major policy shifts. Furthermore, the comparison between SIRREP and bond yield structures opens new avenues for research on risk-adjusted investment strategies and asset allocation models.

Limitations and Future Research Perspectives

Despite its advantages, the PPP model has certain limitations. First, while it integrates key financial variables, it does not explicitly account for exogenous shocks such as geopolitical crises, pandemics, or sudden technological disruptions, which can influence market cycles independently of earnings growth and interest rate dynamics. Additionally, the model assumes that investor expectations adjust rationally to changes in macroeconomic conditions, which may not always be the case due to behavioral biases.

Future research should explore refinements to the PPP methodology by incorporating real-time sentiment analysis, machine learning-based forecasting models, or sector-specific adaptations of the framework. Another promising direction would be to test the PPP's predictive power across different international markets, particularly emerging economies where financial structures and risk perceptions may diverge significantly from those in the U.S. Ultimately, the continuous development of dynamic valuation models like the PPP will be crucial for improving market predictions and enhancing decision-making in an increasingly complex financial landscape.

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