Mizuho Brief: USD

Economics & Strategy | Asia ex-Japan

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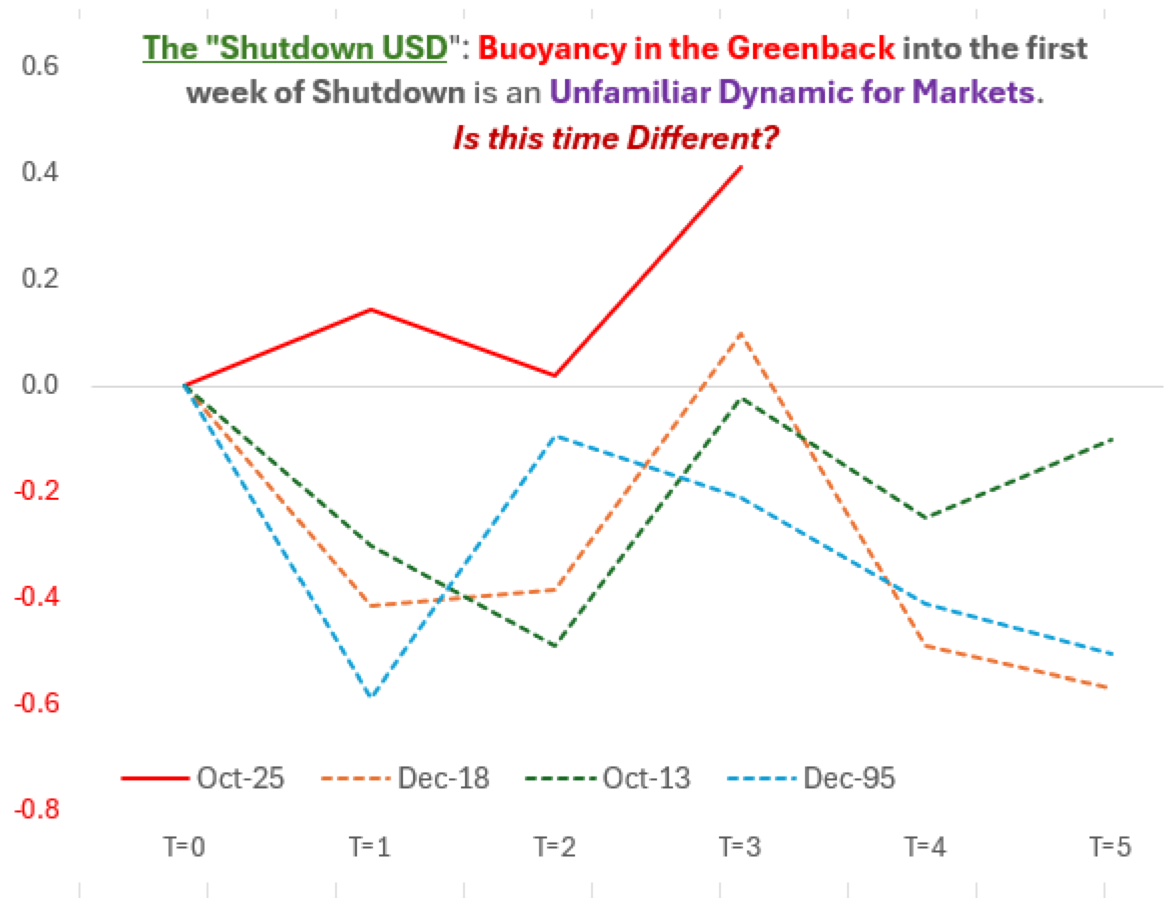
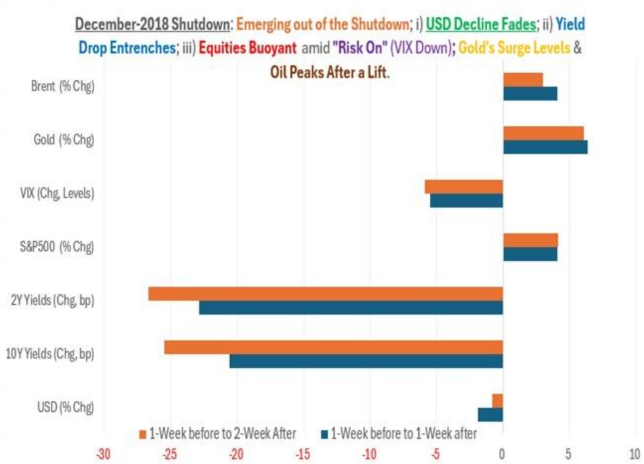
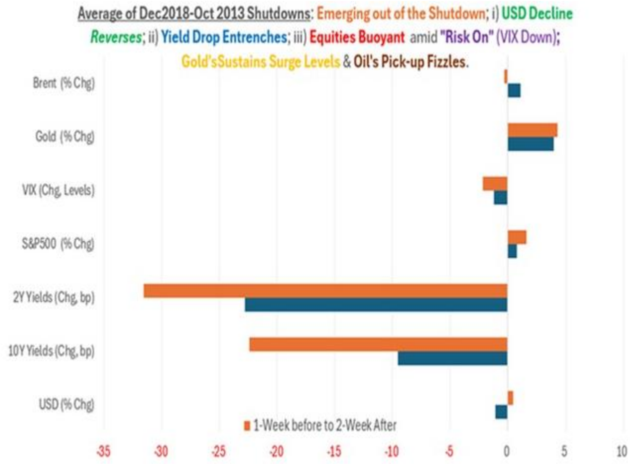
Why USD has Dismissed the Shutdown



- Buoyant USD Defying Shutdown: A **buoyant USD despite the US shutdown** has probably wrong-footed some and intrigued many insofar as it **flies in the face of received wisdom that the USD weakens into shutdowns**. Point being, and as keen observers will rightly suggest, US shutdowns typically result in a softer USD (alongside a drop in yields and a rise in equities).
- Shutdown (USD) Sell-off Exaggerated: But while a **decline in the USD during the shutdown is by and large true**, **assuming enduring USD weakness** resulting **from a shutdown is misguided**. In fact, evidence of fading USD weakness suggests that USD sell-off narratives may be exaggerated looking past the actual shutdown.
- Less Compelling to be Aggressively Bearish on USD: Specifically, recent **evidence from comparable** (and meaningfully longer) **shutdowns** in December 2018 and October 2013) suggest that **USD declines were considerably reversed within 2 weeks out of the shutdown** (see Charts below). And so, the ***case to go big on bearish USD bets is less compelling***.



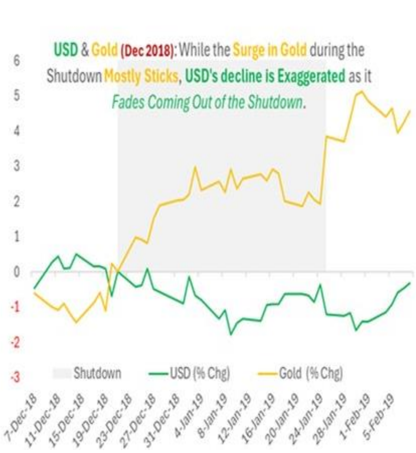


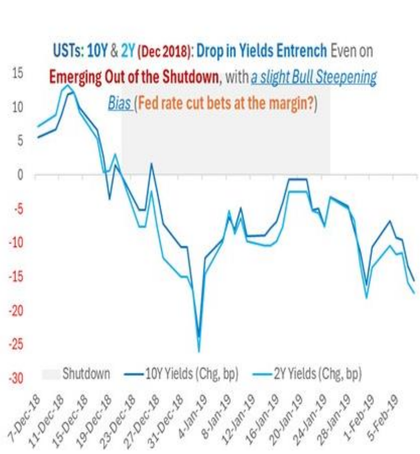
- Specific USD Buoyancy Factors for 2025 Shutdown: Crucially, there are **specific** ***"this time it's different"*** **factors at work**, which conspire to provide **grounds for the Greenback to defy expectations of a pullback from the shutdown**.

i. Lack of "Risk On" Dollar Drag: Given **more precarious geoeconomic risk sentiments** amid **more deeply entrenched US political risks**, **prospects for a more unimpeded "risk on"** into, and emerging from, the shutdown may be **compromised**. And consequently **hobbling "risk on" pullback in the Greenback**.

ii. Coincident EUR & JPY Woes Propping Up USD: What's more, coincident headwinds to JPY (from a conspiracy of loose fiscal and monetary policy expectations after LDP elections) and EUR woes on French political upheaval also lend relative buoyancy to the USD.

iii. Counterintuitive Dial-Back in Imminent Fed Easing: Finally, and crucially, the **knee-jerk to associate shutdown disruptions with a more dovish (at the margin) Fed** is now **turned on its head** – thereby **backstopping, if not buoying the USD**. Specifically, compelling evidence of a *surge in equities and bonds* (significantly softer yields) following a *shutdown suggest easier financial conditions,* which is perversely, ***consistent with diminished case for imminent easing***. **Especially as the Fed struggles to find evidence to justify deeper cuts sooner**. Delayed data releases also add to the case for deferred cuts.





Latent Volatility on Jobs Risks: But hat said, there may **be far more pronounced latent two-way volatility in the USD hinging on risks to US federal jobs**. Specifically, *if Trump seizes the opportunity to pull off a "DOGE 2.0" to permanently cut government jobs* and **flips the policy risk from deferred easing to front-loaded cuts**. This could ***sink yields*** (in emphatic bull steepening fashion) and ***drag the USD down*** more forcefully.

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