Mizuho Brief: FX Risks

Economics & Strategy | Asia ex-Japan

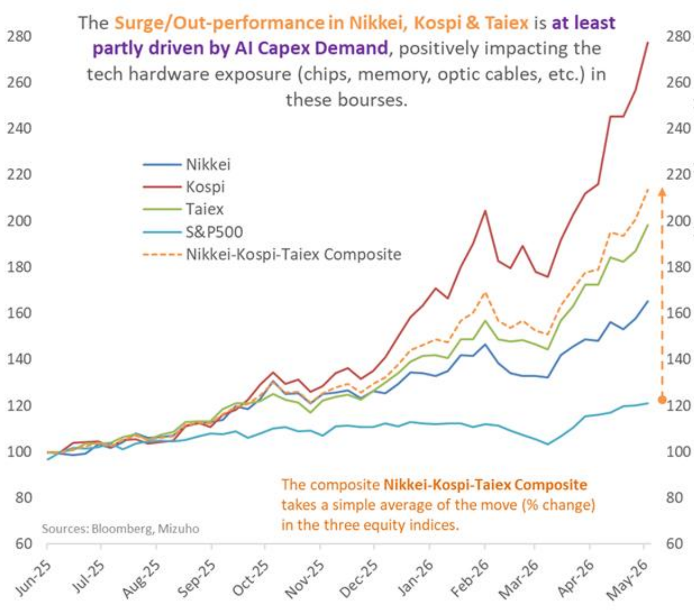
2 June 2026 |
Vishnu Varathan | Head Macro Research, Asia ex-Japan

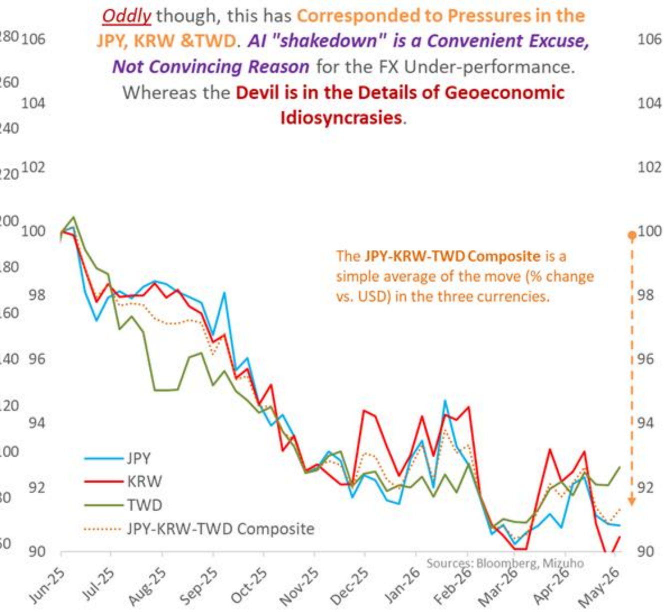
Dealing with the (Devil in the Details of) AI Equity-FX dissonance

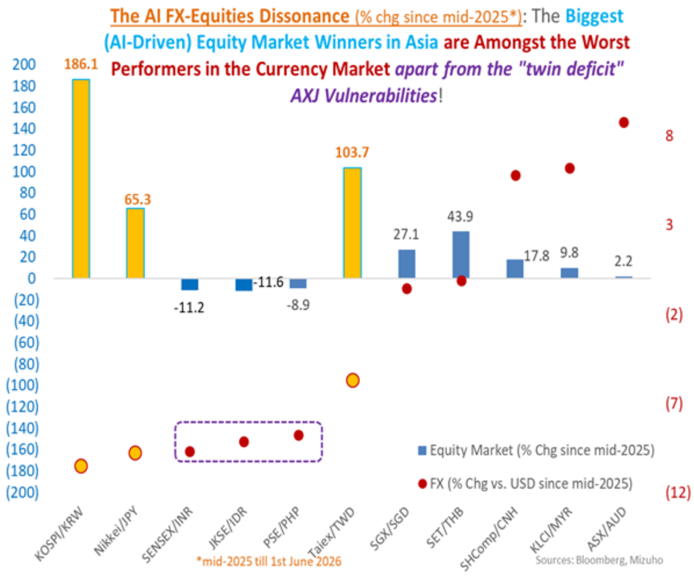
"There is nothing more stimulating than a case when everything goes against you" – Sherlock Holmes

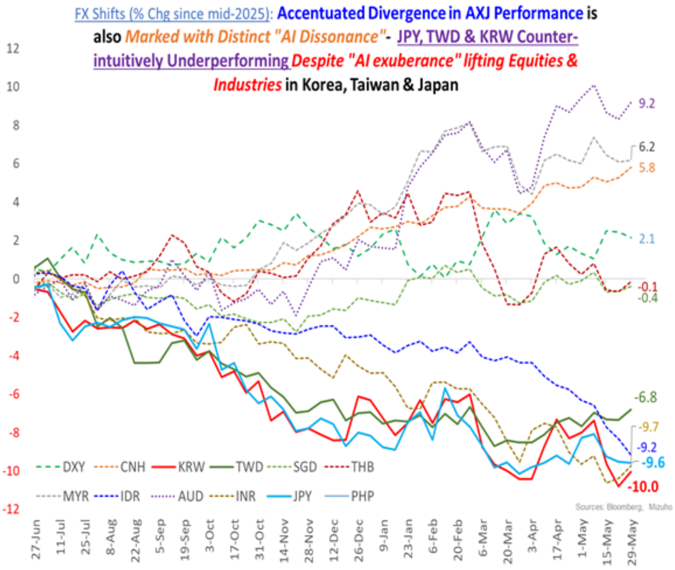
In a Nutshell:

- *Despite strong AI-driven equity gains in North Asia,* KRW, JPY, and TWD have underperformed in FX markets since mid-2025, diverging from the bullish equity narrative.
- Key factors for this **glaring equity-FX dissonance** include; i) *net foreign equity outflows* (notably from Korea and Taiwan); ii) *constrained current account dynamics* (Japan), as well as *political-fiscal risks* taking precedence.
- This has notably overwhelmed more hawkish policy expectations that ought to have supported respective currencies.
- ***Crucially***, the US' "**Pay America" capital extraction** has inflicted disproportionate pain on KRW, JPY and TWD.
- What's more, **supply-side shocks from the US/Israel-Iran crisis**, particularly the "Hormuz crisis," are hurting KRW, JPY and TWD given disproportionate energy reliance as well as risks of industrial input disruptions.
- Point being, the drivers of this **equity-FX dissonance** are *evolving, uneven* across, and *asymmetric* (with non-linear trajectory and impeded reversion).
- All said, ***as the conspiracy of geo-economic risks remain unresolved***, the stage is set for the stage for *extended equity-FX dissonance* and *entrenched AXJ divergence*.









- The **macro narrative of North Asia's out-performance on bullish AI theme**, *being in pole position to exploit the AI capex build-out of "hyper-scalers",* has **failed to express itself in FX markets**.
- In fact, **KRW**, **JPY** and **TWD** have ***distinctly under-performed*** the Asia FX space (since mid-2025) despite the obvious AI exuberance in equities.
- Notably, **similar under-performance elsewhere** in AXJ has been **attributable to significant headlines risks**.
- Specifically *geo-political stress confronting rupee* (hurt by exceptional and unexpected US trade antagonism) and *fiscal dominance/governance risks for the rupiah.*
- Whereas the **glaring underperformance in KRW, TWD** alongside the **JPY** sits in ***in stark contrast to*** corresponding, **exuberant surge in Kospi, Taiex & Nikkei**.
- Admittedly, **recent episodes* of stumbles in tech stocks and the March "risk off" on Iran** on AI "shakedown" may**, *albeit only partly,* **explain pockets of sell-off** (in JPY, KRW & TWD).
- ***But*** this **falls far short of convincingly accounting for** the **sustained** – in fact, even more ***accentuated*** – **divergence between equities and respective currencies**.
- Afterall, the mainly *"hardware" exposure of North Asia's AI exposures are predominantly still well-positioned to exploit robust capex by hyper-scalers.*
- And the upshot is that there is ***no one-size-fits-all macro/thematic drivers for counter-intuitive currency weakness*** (*at glaring odds with corresponding equity markets*).
- Instead, **AI Equities-FX dissonance** is **driven by** a **time-varying confluence of factors** – *peculiar to each currency* – as follow:

1. Net Foreign Investment flows
   - One of which is net foreign equity outflows, *despite (and in defiance of) the AI-driven surge* on the bourses.
   - This is **glaringly the case with Korea and, to a lesser extent, Taiwan –** partly explaining corresponding pressures on KRW and TWD.

- ***But* clearly not so for Japan** given the **languishing JPY**, ***despite*** **the surge of net foreign inflows into Japanese equities**.

Figure 1: Net Foreign Equity Flows

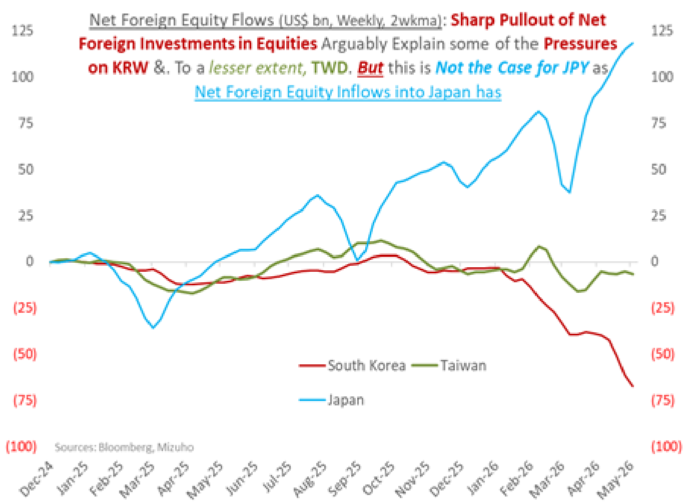
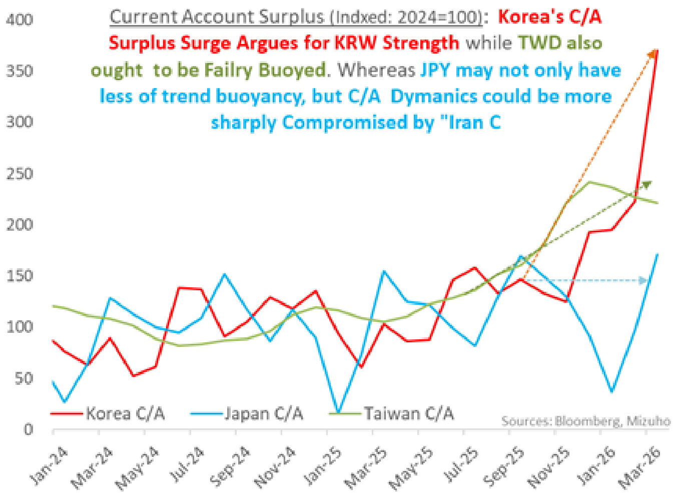


Figure 2: Current Account Dynamics



2. Nuances of Current Account (C/A) Shift:
   - Notably, shifts in Current Account trend dynamics – at least partly driven by AI capex build-out – ostensibly account for some of the marginal FX shifts.
   - But even here, it is **highly imperfect**, ***if not confounding***. For one, the script is flipped with **KRW** and **TWD** weakness **defying buoyancy suggested by C/A dynamics**.
   - Whereas JPY weakness *despite net foreign equity inflows* may partly squares with underlying soft spots in the C/A dynamics (outright drag from net goods and services trade deficit).

3. Policy Expectations & Political-Fiscal Risks:
   - The projection*** for relatively more hawkish BoJ and BoK policy rates into mid-2026 (of at least 2 hikes) vis-à-vis the Fed's single (25bp) hike expectations, ought to lift – and not depress – JPY and KRW.
   - **Even the CBC has hinted at tightening bias**, albeit refraining from overt allusions to imminent hikes, which *ought to be consistent with some degree of TWD backstop.*
   - Nonetheless, offsetting, if not overwhelming, confluence of (geo-)political and fiscal risks may be the more dominant force exerting FX pressures – as appears to be especially the case for JPY.

Figure 3: Net Foreign Equity Flows

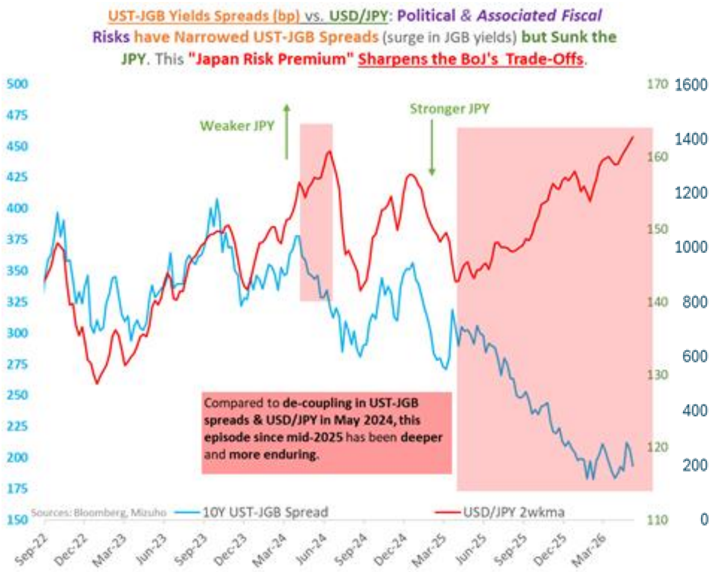
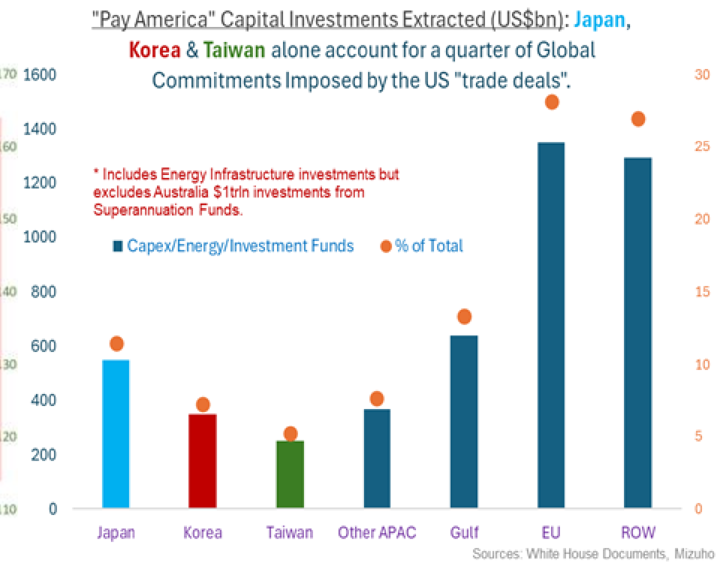


Figure 4: "Pay America" Capital Investments Extractions by the US



4. "Pay America" Capex Extraction:
   - A **pin-pointed source of geo-economic stress** hurting KRW, JPY and TWD despite the "AI boost" is the **"Pay America" extraction of capital** (investments) demand by the US (of these key trade partners/allies).
   - With Japan on the hook for $550bn, Korea for $350bn and Taiwan for at least $250bn – purportedly within Trump's term – the **anticipated capital outflows** (*expressed via FX market tools/behaviour^*) is **inevitably showing up in exchange rates**.
   - And this **extraordinary geoeconomic force** may be **overwhelming** (*and confounding* received wisdom associated with) the more conventional FX cogs.

5. US/Israel-Iran War Crisis
   - What's more, the **supply-side shocks induced by the "Hormuz crisis"** and ***amplified by industrial multipliers*** may be disproportionately hurting KRW, JPY and TWD.
   - Especially given *reliance on Persian energy* as well as *passage of wider industrial inputs* impacted, which imposes **cost pressures**, and **threatens to disrupt future production**.
   - To be sure, this (FX pressures) **could easily reverse if Iran risks are alleviated**.
   - *But amid the significant prevailing uncertainty* p**otential for downside remains pronounced**, and **attendant FX drag is hard to avert**.

- The **factors** listed for the glaring **FX-Equity dissonance** are **not exhaustive**. And could **continue to evolve**.
- Crucially, these factors **do not apply evenly across** the JPY, KRW and TWD, and perhaps not even cconsistently.
- Hence, the **response function of these currencies will vary with shifting headline risks.**, setting the stage for *extended equity-FX dissonance* and *entrenched AXJ divergence*.
- Moreover, *AI remains a rather asymmetric risk* for KRW, TWD and JY, which warns of *non-liner trajectories* with potentially *impeded reversion.*

- For one, the **“AI boost” may not only continue to elude for the associated currencies**, *if a positive turn in industrial multipliers is not realized.*
- What’s more, it **presents an additional layer of downside risk** *if the present euphoria gives way to overshooting (in equities) concerns.*

* The episodes – mostly in early-2026 (mostly pre-Iran) pertain to; *i) circular demand* (earlier) and; *ii) existential threats to certain (aspects of) industry*.

** Since April though markets have not only recovered from “Iran crisis” fears, but surged on AI rallies seemingly unfettered by Iran risks/”Hormuz crisis”.

*** Using market implied policy rate projection (as sourced from Bloomberg) alongside forecast polls.

^ Including Taiwan’s significant unhedged insurance outflows and reported hoarding of exports USD and Japanese/Korean banks buying USD (to prepare to fund capex into US).