THE FUTURE IS YOURS

AIP

4th October 2025

Looking through the shutdown

The US government shutdown is a potential near-term risk for markets. **A 2-3- week shutdown, which is likely to have limited market impact. A shutdown lasting beyond 2-3 weeks, coinciding with stretched investor positioning, could cause a short- term pullback in risk assets.** For tactical investors, it is prudent to lock in gains on excessively concentrated positions. Longer-term investors should consider using any pullback to add to preferred equity markets (US and Asia ex-Japan) and US technology, communications and healthcare equity sectors which are backed by a strong earnings outlook. Gold remains a reliable hedge during a government shutdown and a structural bullish story. In bonds, lock in current yields in 5-7-year maturities as a slowing US job market points to more Fed rate cuts in the next 12 months. Further downside in USD/JPY amid rising prospect of a BoJ rate hike.

Duration of shutdown matters

A brief US government shutdown is likely to have limited impact on the economy and markets. However, a prolonged shutdown, lasting beyond 2-3 weeks, remains a non-negligible risk, given the Democrats want to use the opportunity to force the Trump administration to undo the planned ending of some healthcare subsidies for millions of Americans by the year end. **Republicans will agree on an extension of the healthcare subsidies**, helping end the government shutdown. Any delay would hand the Democrats a political win over the sensitive issue ahead of next year’s mid-term elections.

Stretched investor positioning is a near-term risk.

The shutdown coincides with US equity market investor positioning that has become more stretched. US equities scaled new record highs. **Combined investor positioning in the US equity market has risen close to extreme (1.65 standard deviation above its historical mean).** At these levels, US equity returns over the following three months have more often been negative. The last time positioning was above 1.6 (Dec 2024), the next 3-month return was -8.1%. However, the risk of a deep correction is low, other short- and long-term quantitative models, based on factors such as momentum, implied volatility, economic surprises and macro risk.

Opportunity to add to preferred sectors

Any shutdown-driven market drawdown as an opportunity to add to preferred equity markets – the US and Asia ex-Japan. The structural AI-driven growth story driving the technology sector in the US, Europe and China will remain in place regardless of the length of the government shutdown. The sector is supported by upward earnings revisions, with US Q3 earnings growth now estimated at 8.8%, up from 8% at the start of Q3. Meanwhile, the US healthcare sector has caught a tailwind from recent agreements between some sector leaders and the Trump administration that alleviates tariff concerns.

Gold remains a key hedge

The precious metal has been resilient during past US government shutdowns. It is also likely to keep benefitting from structural demand from central banks amid elevated global policy uncertainty. Gold miners as a tactical opportunity. The sector is seeing rising profit margins as the gold rally in recent years has driven prices far above the all-in production cost which remains below USD 2,000/oz.

Lock-in yields on medium-maturity bonds

A government shutdown, combined with a weakening job market, raises the chance of two more Fed rate cuts this year and a total 100bps of cuts to 3.25% over the next 12 months. Value in high quality bonds in the 5-7-year maturity space, especially with the US 10-year government bond yield currently above 4%.

Downside risk for USD/JPY

A US government shutdown beyond a few weeks will likely push USD lower. Downside for USD/JPY, with a test of 145 support, especially if Agriculture Minister Koizumi wins the ongoing leadership race for Japan's ruling Liberal Democratic Party in a run-off. Koizumi backs BoJ rate hikes and supports policy normalisation. There is an increasing chance of the BoJ hiking rates on 30 October.

DISCLAIMER

Information provided in this document is indicative and has no contractual value. It is subject to frequent changes, especially due to evolutions in the legislative and regulatory environment. This information does not constitute an investment, legal, accounting or tax advice. Before any implementation the recipient of this document must consult an independent professional advisor in order to determinate if his objectives are compatible with proposed operations and to obtain all financial accounting legal and tax information necessary to allow him to appreciate characteristics risks and suitability of each intended operation and cannot be held responsible for any consequences especially financial as the result of operations which would be realized based on this only document.
Information provided in this document are coming from the best sources. Nevertheless, Arabian International Partners LLC (AIP), its subsidiaries and employees, cannot be held responsible for any financial or other consequences that may arise from the use or distribution of this document.

This confidential document is exclusively intended for the person to whom it is given and may not be communicated to third parties (except for external advisers under the condition they respect this confidentiality undertaking) and may not be reproduced, copied or circulated without prior authorization of Arabian International Partners LLC (AIP).

THE FUTURE IS YOURS AIP

Corporate Finance
Structured Debt
Debt Capital Markets
Financial Sponsor Coverage
Advisory

arabianipl.com