

Currency Market Commentary

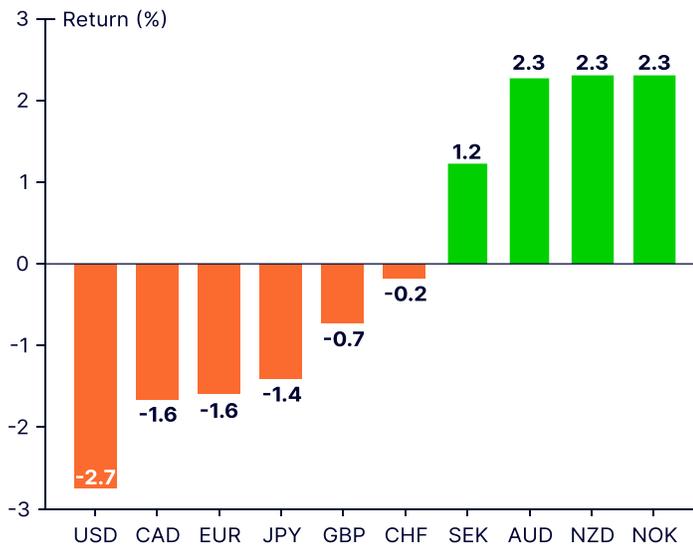
Insights
February 2026

Summary

Politics are likely to play a larger role in driving currency movements going forward, although relative growth and monetary policy will remain important. This marks a shift from our view at the start of the year, when we anticipated a period of greater clarity regarding tariff and trade policy.

We see room for the currently oversold dollar to rebound at least through the first half of February. The nomination of Kevin Warsh for Fed Chair appears to have avoided the market's worst concerns, and US growth is likely to remain strong. In our view, fears of a broad, multi-country coalition led by the US intervening to weaken the dollar are overstated.

Figure 1: January 2026 currency return vs. G10 average



Source: Bloomberg and State Street Global Investment Management, as of 31 January 2026. **Past performance is not a reliable indicator of future performance.**

We believe the threatened yen intervention was a specific, targeted move to limit further yen weakness rather than a signal of a coordinated effort to depreciate

the dollar. Ultimately, fundamentals will drive currency performance, and they continue to point to the yen remaining at depressed levels for now.

Figure 2: February 2026 directional outlook

	Tactical outlook	Strategic outlook
USD	↗	↘
CAD	↗	—
EUR	—	↘
GBP	↘	—
JPY	—	↗
CHF	↘	↘
NOK	↗	↗
SEK	↘	↗
AUD	—	—
NZD	—	—

Note: All individual currency views in the table above are relative to the G-10 average.
Source: State Street Investment Management, as of 31 January 2026.

The threat of new tariffs and non-tariff barriers further undermines confidence in the reliability of US policy and should limit any potential upside in the dollar. Investors are now more likely to react disproportionately to negative US developments, putting additional downward pressure on the currency. This skews near-term dollar risks to the downside, while our long-term view remains for a pronounced 3–5 year dollar bear market.

We generally favor higher-yielding, stable-growth, and commodity-sensitive currencies supported by strong government balance sheets, such as the Norwegian krone and the Australian dollar. The Swedish krona is also well positioned as its economy continues to recover and it benefits from EU fiscal stimulus; however, after a strong one-year rally, it appears overbought and is likely to retrace over the next 1–2 months.

Canada also benefits from firm commodity prices, a broadly sound fiscal position, and a stabilizing growth outlook. As a result, the Canadian dollar screens well in our model, though we see significant headline risks ahead of this summer's United States–Mexico–Canada Agreement (USMCA) renegotiation and therefore limited room for appreciation.

The British pound looks vulnerable as fiscal austerity, soft labor markets, and renewed disinflation increase the likelihood of more aggressive Bank of England policy easing, which should keep the pound subdued through 2026. The Swiss franc continues to struggle with near-zero inflation, zero interest rates, and the risk of intervention. The Swiss National Bank (SNB) is likely to rely on currency operations to limit further appreciation pressures from safe-haven flows.

The euro screens better and should be relatively resilient during an equity-market correction. However, growth remains sluggish, and uncertainty around the speed and composition of German fiscal stimulus persists. We expect the euro to have difficulty breaking higher over the next 1–2 months and to continue underperforming the G10 average.

US Dollar (USD)

We see room for the currently oversold dollar to rebound at least through the first half of February for several reasons.

1. Fed Chair nominee Kevin Warsh's longstanding commitment to low and stable inflation has eased market concerns about a potential erosion of central-bank independence.
2. US growth is likely to remain firm.
3. Although the administration's new tariff threats may exert a lasting drag on investor sentiment, most of these threats—often referred to as the TACO trade—have not yet been implemented.
4. The fears of a coordinated, multi-country “Mar-a-Lago accord” aimed at weakening the dollar appear misplaced. The threatened yen intervention seems targeted specifically at limiting further depreciation in that pair rather than signaling an effort to engineer a sustained yen uptrend.

While the US dollar may extend its recovery from the January lows in the near term, our outlook is best described as neutral with a clear downside risk bias. The threshold for initiating new long-dollar positions continues to rise amid elevated policy uncertainty. In response, we expect a gradual increase in currency hedges on the roughly USD 33 trillion in foreign portfolio assets held in the US. We also expect the US to capture a smaller share of incremental global portfolio flows as investors pursue more balanced geographic allocations.

Accordingly, we maintain our call for a multi-year US dollar bear market, with the currency likely to decline at least 15% over the next 2–4 years. The US remains an attractive destination for capital investment, supported by innovative companies and flexible labor and capital markets. However, rising macro risks—policy uncertainty, high debt levels, and a widening current account deficit—have eroded the dollar's upside potential and its historical reliability as a safe-haven asset during periods of economic or geopolitical stress. We also expect US economic outperformance to be meaningfully smaller over the next 10–15 years than it was over the preceding decade and a half.

Canadian Dollar (CAD)

Our models favor the Canadian dollar, supported by firm commodity prices, strong local equity performance, and early signs of growth stabilization following a difficult 2025. The cumulative impact of lowering the policy rate from 5% to 2.25% over the past 18 months should also begin to provide a meaningful boost to the domestic economy.

However, we are less optimistic than our models suggest and see the Canadian dollar constrained in a 1.36–1.40 range versus the US dollar. The improving economic narrative faces near-term risks from renewed US tariff threats and the upcoming renegotiation of the USMCA (or CUSMA in Canada). We expect intensifying rhetoric and tough negotiating tactics from the US in the coming months, which are likely to weigh on consumer and business confidence in Canada and act as a headwind to growth.

Our medium-term view is more constructive. The Canadian dollar screens as cheap on our long-run fair-value metrics, and we expect the North American tariff dispute to ultimately culminate in a renegotiated USMCA that largely preserves North America's

favorable relative tariff structure versus the rest of the world. Canada also retains greater capacity than the US for rapid monetary and fiscal stimulus, and it has significant room for both regulatory reform and expanded trade with markets outside North America. As these factors come into play, we see scope for USD/CAD to move into the low 1.30s by late 2026.

Over the longer horizon, our broader US dollar bear-market thesis implies that USD/CAD could eventually return to, or even fall below, 1.20. That said, the Canadian dollar is likely to remain sluggish versus the G10 ex-US, as a weaker US dollar will act as a structural headwind.

Euro (EUR)

We maintain a neutral to slightly negative stance on the euro. Q4 gross domestic product (GDP) surprised to the upside, but the European Union (EU) remains stuck in a low productivity growth regime and continues to face pressure from US tariffs and rising competition from China. The European Central Bank (ECB) has likely completed its rate cutting cycle; however, its 2% policy rate sits in the lower half of G10 yields and is unlikely to attract meaningful capital inflows. Fiscal expansion—led by Germany—is supportive, but this is already largely priced into the currency, and the marginal risks now tilt toward concerns about slower or less effective implementation.

The most constructive factor for the euro in the near term is its role as a hedge against weakness in risk assets. Beyond that hedging function, we prefer the Australian dollar and Norwegian krone, both of which offer higher yields and a more compelling near term growth profile. We expect EUR/USD to remain broadly rangebound, with most of the movement within the range driven by US economic and monetary policy developments.

Over the medium term, we remain constructive on the euro versus the US dollar. The case for EU investors to scale back their concentrated exposure to US assets—or at least adopt higher average hedge ratios—is strong as the US becomes a less reliable trade and security partner. We see scope for EURUSD to move toward 1.30+ over the next 3–5 years.

The outlook against other G10 currencies is less favorable. The euro screens expensive relative to the Japanese yen, Norwegian krone, Swedish krona,

Canadian dollar, and Australian dollar and is likely to materially underperform those currencies in the coming years once tariff related growth risks ease and equity market volatility moderates.

British Pound (GBP)

We are negative on the pound over the near term. Every indicator in our tactical scorecard ranks the pound below the G10 average, including measures of growth momentum, short term value, relative equity performance, and commodity market impacts.

Sterling rests on a fragile foundation of high public debt, persistent current account deficits, and structurally weak productivity growth. Recent data paint a sluggish picture: growth has been soft, the labor market continues to weaken, retail sales have disappointed, and inflation is likely to drift lower.

Together, these point toward easier monetary policy and a weaker currency. Concerns around fiscal stability, ongoing political risks to Prime Minister Starmer's government, and the UK's inability to meaningfully improve its long run growth prospects are also likely to weigh on UK and pound sentiment.

The Bank of England's relatively high 3.75% policy rate offers some support, but that support is limited by the fact that rates are high for unhealthy reasons, constraining the BoE's ability to stimulate demand.

The longer term story is less challenging—at least against the US dollar and Swiss franc. While the pound appears structurally weak versus most of the G10, we see it stabilizing in the mid 1.30s against the US dollar this year. Over a 3–5 year horizon, we see scope for GBP/USD to reach the 1.40–1.45 range.

We also expect the pound to outperform the expensive, low yielding Swiss franc on a total return basis over coming years. Beyond the US dollar and Swiss franc, however, we expect the pound to struggle over the medium term.

Japanese Yen (JPY)

We view the yen as very cheap relative to our long run fair value estimates, supported by improving interest rate differentials—both real and nominal. While the credible threat of coordinated US Japan intervention

to support the yen is unlikely to unlock that underlying value on its own, it should help establish a floor under the currency and limit further depreciation. In the near term, however, the yen is likely to remain soft until we move past the February lower house election and market concerns around fiscal slippage and a behind the curve Bank of Japan begin to ease.

Over time, we expect a sustained period of negotiated wage growth, alongside an improvement in growth and inflation supported by robust fiscal spending, to bring the BoJ back to the table with higher policy rates—providing a durable tailwind for the currency. A key assumption behind this medium term yen strength is the eventual moderation of investor fears around fiscal sustainability. In our view, the government's fiscal plan is unlikely to generate a destabilizing volume of new issuance, and Japan's large, persistent current account surplus ensures a high share of domestically funded debt, reducing the risk of abrupt capital flight.

Taken together, these factors support a move in USD/JPY back toward the **140–145** range by end 2026. We therefore maintain a medium term bullish view on the yen, even as we acknowledge that the current period of softness may extend into early 2026.

Looking further ahead, we see additional upside. Over a 3–5 year horizon, we expect the yen to return to the **120–130** range against the US dollar, consistent with our broader long term US dollar bear market thesis.

Swiss Franc (CHF)

We acknowledge that the Swiss franc has benefited from its traditional safe haven status as investors focus on risks related to currency debasement, high government debt burdens, tariff uncertainty, and elevated geopolitical tensions. This support may persist in the near term, but ultimately, we expect the franc to materially underperform the G10 going forward. While the franc retains attractive defensive characteristics, at current yields and valuations it is an exceedingly expensive risk hedge.

Fundamentally, the franc screens as the most overvalued G10 currency based on our long run fair value measures. It also offers the lowest yields and the lowest inflation rate in the group. Inflation is likely to remain uncomfortably close to zero, and growth is set to remain below trend. Against

this backdrop, we expect the Swiss National Bank to be more willing to intervene directly in currency markets to limit undesired franc appreciation. When accounting for the increasingly negative carry associated with long franc positions, the total return outlook for the franc versus the rest of the G10 is weak. Even against the US dollar, the franc would need to appreciate an additional 10–15% over the next 3–5 years simply to offset the negative interest rate carry embedded in the currency.

We also do not expect the global portfolio rebalancing away from the US dollar over the next 1–3 years to benefit the franc as much as it may benefit other currencies. Swiss investors already hedge a high proportion of their foreign currency exposures. As a result, there is limited room for additional increases in US dollar hedge ratios. Put more simply, there is less scope for US dollar selling and franc buying from Swiss institutional portfolios compared with other markets.

Norwegian Krone (NOK)

We retain a positive tactical bias on the Norwegian krone, supported by cheap long run valuation, firm oil prices, high local yields, a pristine sovereign balance sheet, and broadly positive equity market sentiment. While domestic growth has been sluggish, it has had limited impact on the Norges Bank's policy stance given persistent inflation pressures and the outsized role of global macro conditions in driving the currency.

Our hesitation stems from krone's well known vulnerability to volatility in both oil and equity markets. Fears of an oil supply glut that weighed on sentiment last year have eased amid improved global growth expectations and renewed concerns over Iranian supply. However, the more constructive oil backdrop is not without risk. The US appears to be making progress toward a negotiated solution with Iran, and the recent rise in oil prices could induce additional supply, particularly from Saudi Arabia and US producers. Equity markets continue to push to new all time highs, but valuations are full, and pullbacks may become more frequent even if global growth proves solid in 2026. For these reasons, we see scope for substantial periods of krone volatility, even as our overall bias remains positive.

Over the long term, we hold a more confident positive view. The krone is historically cheap relative to our estimates of fair value and is underpinned by steady

long run potential growth and an exceptionally strong national balance sheet. Norway also maintains significant fiscal and monetary flexibility, giving policymakers ample capacity to cushion the economy and the currency from the current tariff related shock. These features reinforce the krone's appeal once near term volatility subsides.

Swedish Krona (SEK)

We shift from a neutral to a negative stance on the Swedish krona in the near term. After leading the G10 in 2025 and delivering a solid 1.2% gain in January, we see the krona running out of momentum. Interest rates remain low at 1.75%, translating to almost -0.5% in real terms. While Bloomberg consensus growth forecasts have ticked up to 2.4% and PMI data still signal firm activity across manufacturing and services, recent hard data have been disappointing. December retail sales fell -0.7% MoM, and Q4 GDP increased just 0.2% QoQ versus expectations of 0.5%. For the next one to two months, the Swedish recovery narrative appears somewhat overpriced in the currency.

Beyond these near term concerns, we take a more constructive medium term view. The broader trend in Federal Reserve policy points toward easing, while the Riksbank appears likely to remain on hold for an extended period. This setup should lead interest rate differentials to shift steadily in Sweden's favor. Moreover, despite recent softness, Sweden's economy is clearly recovering from the difficult 2023–2024 period. Public finances remain exceptionally strong, with debt at only 33% of GDP, and Sweden has meaningful exposure to the defense sector, one of the main beneficiaries of planned EU fiscal expansion.

Valuation also supports the krona. On a real effective basis, the Swedish krona remains historically cheap. Over a multi year horizon, Sweden should benefit from a gradual global portfolio rebalancing consistent with our long term US dollar bear market thesis. With both Sweden and the broader EU holding significant foreign assets, an increase in US dollar hedge ratios—even a modest one—should create a meaningful, sustained tailwind for the krona.

Australian Dollar (AUD)

We continue to view the Australian dollar as one of our preferred currencies in the G10. High inflation, improving

consumer spending, and strong gains in home prices support a solid 2026 growth outlook, keeping the Reserve Bank of Australia biased toward tighter policy, even after its 0.25% rate hike on 04 February. The Q4 US–China tariff ceasefire and recent appreciation of the Chinese yuan remove a key headwind that weighed on the Australian dollar throughout much of 2025. In addition, Australia has ample fiscal space and the ability to deploy more meaningful stimulus should a negative global growth shock materialize, an enviable position in a world where government debt levels are already stretched.

That said, we do see some near term considerations that temper our enthusiasm. After a strong six month rally, the Australian dollar appears somewhat ahead of itself and is vulnerable to a 2–4 week pullback. Our multi factor model indicates that the Australian dollar is temporarily overbought. Medium term challenges also remain, including lackluster business investment, high household debt service burdens, and structurally low productivity growth. The currency is additionally sensitive to global equity market volatility, which appears more likely following the sharp rally since April 2025.

Over the long term, however, our conviction is stronger. Australian investors appear to hold high levels of unhedged US dollar denominated assets, which we believe will be subject to increased hedge ratios or a broader rotation into more diversified global portfolios. Once markets fully adjust to the new tariff regime, we see considerable room for a sustained long term rally in the Australian dollar.

New Zealand Dollar (NZD)

We maintain a slightly positive near term outlook for the New Zealand dollar. After experiencing a recession in 2024 and a difficult start to 2025, the economy is now transitioning toward a period of more stable growth, with activity expected to exceed 2% in 2026. Both manufacturing PMI and consumer confidence indicators have risen sharply, reaching levels last seen in late 2021. At the same time, the broad based rally in commodities has lifted New Zealand's terms of trade toward the upper end of its three year range. The US–China trade truce and modest improvement in China's growth outlook are also supportive, given China's role as a key trading partner.

The New Zealand dollar may still exhibit bouts of volatility due to its historically high sensitivity to global

risk sentiment, a notable concern amid today's elevated policy uncertainty. Its large current account deficit and relatively low short end yields also present near term headwinds. However, unlike the Australian dollar, the New Zealand dollar is not overbought. Following a weak second half of 2025, the currency remains depressed and appears to be in the early stages of a recovery, which reinforces our modestly constructive bias.

Over the longer term, our view is more mixed. On our estimates of long run fair value, the New Zealand dollar screens cheap versus the US dollar and Swiss franc, offering meaningful room for appreciation. However, it screens expensive relative to the Japanese yen and the Scandinavian currencies, implying a more challenging long term path against those crosses.

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