Currency Market Commentary

Insights
July 2026

Summary

The list of potential volatility triggers aside, we continue to expect a choppy, largely range-bound market through the rest of the summer due to the balance between positive and negative forces.

The resumption of open conflict with Iran, along with the potential expansion of hostilities to other countries, including Houthi attacks on Saudi Arabia, is likely to keep oil prices elevated. However, investor confidence that President Trump will back away from escalation if oil prices and bond yields become too high has, for now, helped mitigate the market response. In addition, stronger-than-expected second-quarter growth and inflation data suggest that the economic impact of the hostilities remains contained. We acknowledge that some of this calm may be misplaced. The longer the conflict with Iran persists, the further global oil inventories decline, and the broader the fighting becomes, the greater the risk of a more significant market dislocation. However, we do not appear to be at that tipping point yet.

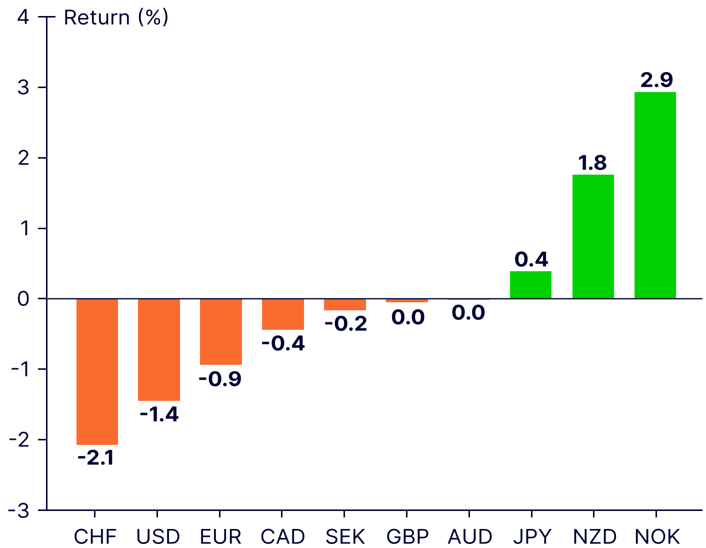
At the individual currency level, we also see a mix of positive and negative forces that point to a range-bound market. The marginal impulse for the US dollar is negative, given weaker-than-expected inflation, job creation, and a dovish reaction from the Federal Reserve. However, the economy remains at or near full employment, domestic demand is robust, interest rates are among the highest in the G10, and elevated oil prices provide additional support. Furthermore, Federal Reserve officials may reverse course and adopt a more hawkish tone.

Growth data in Europe, the UK, and Australia have all recently surprised to the upside. However, the euro remains constrained by below-average interest rates and its sensitivity to higher energy prices. The UK benefits from higher interest rates and stronger growth than we expected, but unemployment remains elevated, the economy is vulnerable to rising energy costs, and the new Burnham government is likely to encounter fiscal constraints. In Australia, household spending and labor markets remain resilient, and interest rates are among the highest in the G10 alongside Norway. However, the Reserve Bank of Australia has room to remain patient given softer-than-expected inflation and declining home prices.

Even the Japanese yen, supported by joint intervention and strong domestic growth, is likely to experience only limited appreciation unless the Bank of Japan follows through with a faster pace of rate hikes and the Takaichi government takes steps to ease fiscal concerns.

The broader point is that the current mix of positive and negative influences is likely to result in choppy market conditions. In that environment, we continue to favor a combination of attractive growth and carry opportunities while applying a penalty to assets

Figure 1: July 2026 Currency Return vs. G10 Average



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

exposed to global geopolitical risks and high sensitivity to investor sentiment.

This means keeping US dollar shorts tactical and avoiding excessive conviction, as additional long US dollar opportunities are likely to emerge. We view the euro as vulnerable due to chronically weak growth, below-average yields, high debt levels, and energy exposure, but we do not expect substantial gains from euro shorts in the near term. We have greater conviction in short Swiss franc positions given its near-zero yield, ultra-low inflation, the Swiss National Bank's willingness to intervene against excessive franc strength, and Switzerland's exposure to sluggish European Union growth. Given the Swiss franc's historical safe-haven status, it is probably best to express this view through long Japanese yen or US dollar positions for now. Following the resolution of the Iran conflict, however, long Swedish krona and/or Australian dollar positions are likely to become increasingly attractive.

The Norwegian krone benefits from high yields, but economic growth has been uninspiring and inflation has been weaker than expected. While high yields and elevated oil prices provide support, oil price volatility also makes it a riskier trade. Sustained Japanese yen strength is probably still several quarters away and more likely a 2027 story. Nevertheless, we expect follow-through from intervention efforts, and downside risks appear limited, making the yen attractive relative to the Swiss franc, where investors can earn carry while waiting for a more sustained appreciation.

For long-term investors who are less concerned about market volatility over the next few months, we see significant value in long positions in the Australian dollar, Japanese yen, Swedish krona, Norwegian krone, and Canadian dollar versus short positions in the US dollar, Swiss franc, and, to a lesser extent, the euro and British pound.

Figure 2: August 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 July 2026.

US Dollar (USD)

The US dollar enters August facing some downside pressure following weaker-than-expected employment, inflation, second-quarter GDP growth (+1.5% quarter-over-quarter annualized), and what markets perceived as a dovish Federal Reserve meeting on July 27. However, unless we see further weakness in employment and inflation during August, which remains a distinct possibility, we caution against anything more than a tactical short US dollar position. The US dollar continues to benefit from solid fundamentals, including final domestic demand growing at a 3.9% annualized pace, low unemployment, yields that remain among the highest in the G10, and Federal Reserve officials who are likely to adopt a more hawkish tone to restore credibility. In addition, ongoing risks related to the Iran conflict continue to provide support for the US dollar.

Looking beyond the summer, the US dollar could come under pressure as consumer spending loses momentum without the support of first-half tax refunds and World Cup-related spending, particularly against the backdrop of a softening labor market. The artificial intelligence capital expenditure story remains firmly in place for the foreseeable future, but slowing economic activity outside the artificial intelligence sector could weigh on growth and inflation later this year, posing a clear downside risk to the US dollar.

We maintain our pessimistic multi-year view on the US dollar but do not believe the risks associated with a sustained bear market are imminent. Innovative companies and the dynamic, flexible nature of US labor and capital markets continue to make the United States an attractive destination for investment. However, rising macroeconomic risks stemming from tariffs and other policy decisions, elevated debt and fiscal deficits, and the persistent current account deficit have reduced the US dollar's appeal. Against this backdrop, investors may consider increasing their US dollar hedge ratios as a way to mitigate growing macroeconomic risks while maintaining exposure to innovative US companies and other attractive investment opportunities. We believe this strategy will become increasingly compelling over the coming years.

As a result, we expect a gradual, multiyear increase in currency hedging on the US$33 trillion of foreign portfolio investments held in the United States. We also expect the United States to attract a smaller share of new portfolio inflows as investors seek more balanced global allocations. This shift is likely to contribute to a prolonged period of US dollar weakness or, at a minimum, significantly limit further US dollar appreciation.

Canadian Dollar (CAD)

A technical recession, defined as two consecutive quarters of negative growth in the fourth quarter of 2025 and first quarter of 2026, low policy interest rates of 2.25%, the threat of additional US tariffs outside the Canada-United States-Mexico Agreement (CUSMA), and below-target core inflation are all negative factors for the Canadian dollar. However, our models have turned positive. Growth may be weak and interest rates low, but conditions are improving.

May GDP increased 0.3% month-over-month, while April growth was revised higher to 0.6% month-over-month, supported by expansionary manufacturing PMI readings, stronger hiring, positive retail sales growth, and rebounding oil prices. The US decision not to renew CUSMA and its threats of additional tariffs are not positive developments and will continue to create uncertainty. However, this was our base case, and we believe it is already well priced by markets. Renewal would have been the most favorable outcome, but even a modest reduction in the tail risk of the US withdrawing from the agreement should help stabilize business expectations in export-oriented sectors. Over time, this could support capital expenditure and hiring plans, albeit modestly.

The recovery remains fragile, and low interest rates warrant caution toward long Canadian dollar positions. Nevertheless, we believe our models are identifying a genuine improvement in fundamentals that should, at a minimum, limit further downside.

We are more constructive over the medium term. Monetary policy is appropriately accommodative, and real policy rates near 0% are likely below their long-run equilibrium level, suggesting they should move higher once growth improves on a sustained basis. While greater clarity around the CUSMA negotiations is still needed, we do not expect a materially damaging increase in tariffs.

Looking ahead to 2027 and 2028, lower mortgage rates in Canada should become increasingly stimulative as mortgages originated near peak interest rates are reset at lower levels. At the same time, we expect US growth to remain healthy but gradually decelerate, alongside inflation, later this year and into next year. This should help cap Federal Reserve tightening expectations and allow the interest rate differential between the US and Canada to narrow.

Overall, we expect conditions to improve gradually, allowing USD/CAD to decline into the mid-to-high 1.30s by late 2026 or early 2027. Ultimately, given our long-term bearish US dollar thesis, we see USD/CAD returning to around 1.20 over the coming years. However, the Canadian dollar is likely to remain a laggard relative to the G10 excluding the US, as broad US dollar weakness may act as a headwind rather than a tailwind for Canadian dollar performance.

Euro (EUR)

We remain negative on the euro relative to the G10 average despite recent improvements in GDP and PMI data, unemployment near a record low of 6.3%, and indications from the European Central Bank (ECB) that it remains open to raising rates in September. The challenge is that the conflict with Iran and higher oil prices are likely to persist for some time, weighing on growth prospects. An additional one or two ECB rate hikes are unlikely to provide meaningful support for the euro, as they would also create further headwinds for growth while still leaving the euro short of being one of the highest-yielding currencies in the G10.

This mixed cyclical backdrop, combined with longer-term structural challenges including high debt levels, increasing competitive pressure from China, limited exposure to the artificial intelligence investment cycle, and slow progress on growth-oriented reforms, creates an unfavorable environment for the euro.

Over the long term, we remain constructive on the euro against the US dollar, driven primarily by expected US dollar weakness rather than European strength. As discussed above, there is a compelling case for European investors to reduce their concentrated exposure to US assets, or at least increase currency hedge ratios, as the United States becomes a less reliable trade and security partner. This shift should provide some support for the euro relative to the US dollar.

The outlook against other G10 currencies is less favorable. The euro appears expensive relative to the Japanese yen, Norwegian krone, Swedish krona, Canadian dollar, and Australian dollar, and we expect it to materially underperform those currencies over the coming years.

British Pound (GBP)

We are neutral on the British pound relative to the G10. Retail sales, employment, and both manufacturing and services PMI data have shown considerably more improvement than we had expected. Political risks have also temporarily eased, with presumptive Prime Minister Burnham pledging to adhere to fiscal rules.

However, several factors offset these recent improvements. The UK remains vulnerable to higher energy prices, unemployment is elevated, and the recent growth recovery remains fragile. In addition, we do not believe the Bank of England will deliver the 2.5 rate hikes currently priced into markets over the next year. Further, we expect the honeymoon period for the new government to end sooner rather than later as it confronts significant structural growth challenges, limited fiscal flexibility, and a highly vigilant bond market.

The longer-term outlook is somewhat more constructive, at least relative to the US dollar and Swiss franc. Over a three- to five-year horizon, we see GBP/USD rising above 1.40. We also expect the pound to outperform the expensive, low-yielding Swiss franc on a total return basis over the coming years.

Beyond the US dollar and Swiss franc, however, we expect sterling to struggle relative to the rest of the G10 over the medium to long term.

Japanese Yen (JPY)

The Japanese yen appears attractive across several dimensions, including valuation, economic growth, rising interest rates, moderating net cross-border portfolio outflows, strong domestic equity market performance, self-sustaining inflation at or above target, and currency policy through intervention. Joint US-Japan intervention to support the yen is a significant development and should prove more effective than previous intervention efforts. At the same time, the Bank of Japan has indicated that it may increase the pace of rate hikes from two per year, a move that US Treasury Secretary Scott Bessent would likely welcome.

The challenge is the timing of a sustained yen appreciation cycle. Joint intervention may already have lowered the trading range for USD/JPY, and we could see the pair move back toward 150 if it breaks below resistance around 155. However, despite indications that the Bank of Japan may accelerate the pace of tightening, short-term interest rates remain low and real policy rates remain well below zero. Markets also continue to worry that ultra-accommodative monetary policy and the Takaichi government's longer-term fiscal spending plans will continue to weigh on real interest rates and the yen.

As a result, while the yen offers substantial long-term upside potential, the scope for near-term appreciation appears more limited, although it remains relatively attractive, particularly against low-yielding currencies such as the Swiss franc. We are more cautious relative to higher-yielding currencies and do not yet see a sufficiently strong and sustained appreciation trend to offset carry costs without a more meaningful fundamental catalyst.

Potential catalysts could include greater clarity around Japan's fiscal outlook, stronger forward guidance from the Bank of Japan, a sharp global risk-off event that pressures equity markets and carry trades, and/or further yen appreciation that begins to create meaningful losses for underhedged Japanese investors with foreign asset exposure.

Over the longer term, we see significant upside for the yen against the US dollar. Consistent with our long-term bearish US dollar thesis, we expect USD/JPY to decline into the 120–130 range over the next three to five years.

Swiss Franc (CHF)

Our models have turned slightly negative on the Swiss franc relative to the G10 in response to weaker inflation and growth data. In addition, our short-term valuation model, which was positive last month, has shifted to neutral.

As was the case last month, we continue to see more substantial downside risks for the franc than our model scorecard implies. The franc also appears less attractive as global real and nominal yields rise relative to Switzerland's zero nominal policy rate and negative real policy rate. Importantly, the Swiss National Bank (SNB) has made it clear that it stands ready to intervene to prevent excessive franc strength, while core inflation of just 0.3% year-over-year gives policymakers the flexibility to keep interest rates at 0%.

This creates an unfavorable backdrop for the franc relative to currencies such as the US dollar, Australian dollar, Norwegian krone, and British pound, all of which offer policy rates above 3.6%. On a total return basis, after accounting for the increasingly negative interest-rate carry associated with long Swiss franc positions, it is difficult to see the franc outperforming the broader G10. Even against the US dollar, the franc would likely need to appreciate by another 10-15% over the next three to five years simply to offset the negative carry.

We also do not expect portfolio rebalancing away from the US dollar over the next one to three years to benefit the franc to the same degree as other currencies. Swiss investors already hedge a relatively large share of their foreign currency exposure, leaving less room for additional increases in US dollar hedge ratios. Put simply, we see less potential for sustained US dollar selling and Swiss franc buying than in many other major currency markets.

Overall, we believe the Swiss franc faces an unfavorable combination of low yields, accommodative monetary policy, intervention risk, and limited support from global portfolio reallocation trends, leaving it vulnerable to underperformance relative to much of the G10 over the medium term.

Norwegian Krone (NOK)

The Norwegian krone has closely tracked large swings in oil prices, making it the worst-performing G10 currency in June and the best-performing one in July. The conflict with Iran and disruptions to flows through the Strait of Hormuz appear likely to persist for some time. This should provide support for the krone, as should Norges Bank's attractive 4.25% policy rate.

However, this does not necessarily make the krone an attractive long position through the summer, given the potential for continued volatility. The intensity of the conflict with Iran is likely to fluctuate, resulting in ongoing two-way volatility in oil prices, which the krone tends to inherit. Meanwhile, domestic growth has remained soft, and June core inflation surprised to the downside, coming in at 2.7% versus expectations of 3.3%. This reduces pressure on Norges Bank to deliver additional rate hikes.

As a result, while the near-term backdrop is supported by higher oil prices and attractive yields, the combination of geopolitical uncertainty, oil price volatility, and softer domestic economic conditions argues for caution.

The longer-term outlook is more constructive. The krone remains historically cheap relative to our estimates of fair value and is supported by stable, albeit modest, long-term growth prospects, attractive yields, and Norway's strong fiscal and external balance sheet. These factors provide a solid foundation for appreciation over time, particularly once current geopolitical uncertainty begins to fade and market volatility subsides.

Swedish Krona (SEK)

We retain a negative tactical bias toward the Swedish krona, although we are seeing several encouraging developments that warrant close monitoring. In a market environment that we believe will become increasingly focused on growth and interest rate differentials, the krona still faces meaningful challenges. Most notably, the Riksbank's 1.75% policy rate is supported by core inflation of just 0.4% year-over-year and trend unemployment of 8.7%, well above the 2023 low of 7.2%. Expected GDP growth of around 2% this year compares favorably with many G10 peers but is unlikely to fully offset the drag from relatively low interest rates. In addition, Sweden remains dependent on energy imports and European Union demand, both of which are≈vulnerable to fluctuations in the intensity of the US-Iran conflict.

That said, there are several positive signs emerging. Both manufacturing and services PMI readings point to a strengthening expansion, and while core inflation remains low at 0.4% year-over-year, it has improved from 0.0% for the year ended April. Retail sales have also returned to positive growth. Despite its exposure to higher energy prices, the Swedish economy has proven relatively resilient. If these trends continue, the krona could be well positioned for a rebound once a more durable resolution emerges in the Middle East, although that process may take time.

From a longer-term perspective, valuation remains a meaningful advantage for the krona. The currency is historically inexpensive on a real effective exchange rate basis, while Sweden's public finances remain strong, with government debt equivalent to just 33% of GDP. This should prove beneficial in an environment where many developed economies face elevated fiscal burdens.

We also expect Sweden to benefit from gradual portfolio reallocation under our long-term bearish US dollar thesis. The substantial foreign asset holdings of investors in both Sweden and the broader European Union create significant potential for diversification away from US assets. Even if this shift occurs primarily through higher US dollar hedge ratios rather than outright asset sales, it should provide a meaningful long-term tailwind for the krona. Overall, while near-term challenges remain, the medium- and long-term outlook appears increasingly constructive.

Australian Dollar (AUD)

We remain constructive on the Australian dollar but maintain a neutral stance for now. The currency is inexpensive by our valuation measures and offers some of the highest yields in the G10. PMI data have returned to expansionary territory, labor market conditions remain strong, and inflation continues to run above the Reserve Bank of Australia's (RBA) target range.

The challenge is not the underlying growth or interest rate outlook. Rather, the marginal policy impulse has become more dovish. Inflation has come in below expectations, while housing prices are softening more rapidly than anticipated. As a result, the RBA is likely to be more patient regarding any additional rate hikes than markets previously expected.

Australia is also sensitive to refined petroleum product prices and broader global risk sentiment, both of which remain vulnerable to developments in the increasingly complex US-Iran conflict. These factors could contribute to near-term volatility and limit the Australian dollar's upside in the months ahead.

Over a multi-year horizon, however, we remain highly positive on the currency, particularly against the US dollar and Swiss franc. Australian investors appear to hold significant exposure to unhedged US dollar-denominated assets, which we believe could be subject to higher currency hedge ratios or a broader rotation toward more globally diversified portfolios.

Once markets fully adjust to the new tariff regime and global trade patterns stabilize, we believe the Australian dollar has the potential for a meaningful long-term appreciation. Combined with attractive valuations, relatively high yields, and solid economic fundamentals, this positions the Australian dollar as one of our preferred currencies over the longer term.

New Zealand Dollar (NZD)

We are tentatively positive on the New Zealand dollar relative to the G10 average. The economy is gradually recovering from its 2024-2025 recession, and both manufacturing PMI and consumer confidence have recently shown further signs of improvement. The Reserve Bank of New Zealand (RBNZ) raised interest rates by 25 basis points to 2.5% and signaled that additional increases remain possible. Markets are currently pricing in four more rate hikes by May 2027.

Despite these improvements, we remain cautious on the currency. Additional energy price shocks could undermine the recovery, while New Zealand's terms of trade have been on a steady decline since March. Core inflation remains within the RBNZ's 2%-3% target range, suggesting less urgency for further rate increases than markets currently anticipate, particularly if a resolution to the US-Iran conflict eases inflation pressures.

Although policy rates have moved higher, they remain low by G10 standards at 2.5%, especially for an economy that continues to run large and persistent current account deficits. The New Zealand dollar appears inexpensive from a valuation perspective, but the case for a full normalization of interest rates and a sustained acceleration in economic growth remains too uncertain to move us decisively off the sidelines.

Our longer-term outlook is more mixed. Based on our estimates of long-run fair value, the New Zealand dollar appears undervalued relative to the US dollar and Swiss franc and therefore has meaningful room to appreciate against those currencies. However, it appears relatively expensive against the Japanese yen and the Scandinavian currencies, suggesting more limited upside and the potential for underperformance in those currency pairs over time.

Overall, while the cyclical backdrop is improving and valuation is supportive, we believe investors should remain selective and patient until there is stronger evidence that the economic recovery and policy normalization cycle are becoming more firmly established.

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