Currency Market Commentary

Insights
October 2026

FX markets navigate rising risks

High yields continue to support select currencies, but rising fiscal pressures, geopolitical uncertainty and shifting market dynamics highlight the need for greater selectivity and caution across FX markets. Tactically, we turned neutral on CAD, NZD, and EUR.

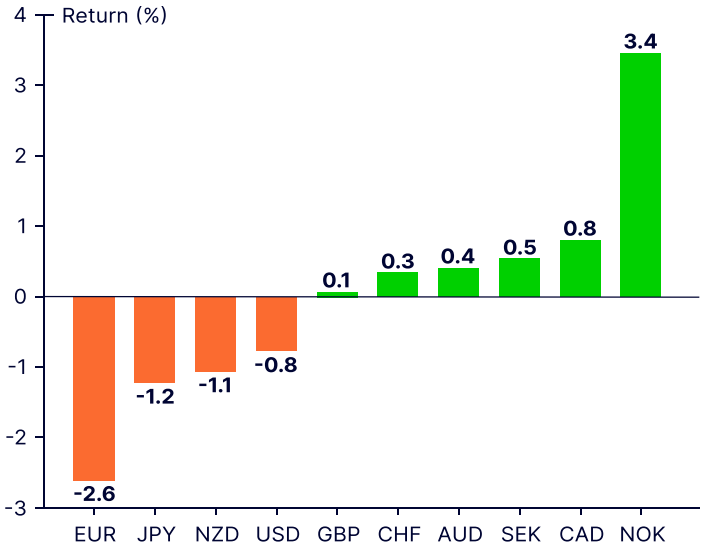
Investors are likely to continue to support currencies backed by higher yields and resilient, improving growth. But macro fragilities and the uneven nature of growth and asset price behavior mean that we are not in a simple "buy risk, go long carry" regime. The quality of growth and carry matters, and that defines a world in which specific country fundamentals matter.

The result is a mixed environment that is highly sensitive to news events and the evolution of local growth and monetary conditions. Our tactical systematic models reflect this mixed environment well, with eight of 10 G10 currencies scoring neutral, a rare occurrence.

Near-term volatility in the AI trade is likely to disadvantage the US dollar, limiting further gains. The US dollar has benefited greatly from the positive effects of the AI boom on capital inflows, earnings growth, GDP growth, and higher interest rates. Given this dependency, the US dollar is unlikely to fulfill its historical role as a safe haven in the face of an AI selloff.

Should the recent correction in AI stock prices morph into a deeper threat to current growth expectations and a broader equity correction, then we expect the Japanese yen, rather than the US dollar, to perform, as it could discourage further portfolio outflows from Japan. The Swiss franc also shows decent resilience.

Figure 1: October 2026 Currency Return vs. G10 Average



Source: Bloomberg and State Street Global Investment Management, as of 31 October 2026. **The performance data quoted represents past performance. Past performance does not guarantee future results.**

The ongoing Iran conflict and rumors that the US may restart its bombing campaign after the midterm elections present a significant risk. The front-month Brent crude futures price is already at $117, up from $72 at the end of Q2, while Dutch natural gas futures have broken above €100, up from only €43 at the end of Q2. More importantly, refined product prices remain extremely high.

Higher oil prices support the Norwegian krone and US dollar and, to a lesser extent, the Canadian dollar and Australian dollar, which are harder hit by the drag from refined product prices. But we are nearing levels at which those correlations may break down as energy prices threaten global growth and raise the risk of stagflationary conditions. Should the conflict re-intensify, there is the potential for oil to rise above $140. At those levels, markets should reorient to favor growth stability, with the US dollar and Swiss franc doing well.

Figure 2: November 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 October 2026.

The Japanese yen probably holds up, given the threat of intervention and the potential for a reduction in risk-seeking capital outflows from Japan. But Japanese yen upside should be limited due to Japan's heavy reliance on energy imports and its tendency to increase fiscal spending to help offset higher prices.

Fiscal and political risks are at the forefront, given the ongoing fiscal struggles in France and the US midterm elections next week. This biases the euro lower than otherwise and will keep investors vigilant and ready to punish any sign of fiscal largesse globally, with Brazil warranting caution. It's difficult to see French credit spreads tighten meaningfully before the presidential election next April, with deficits pushing 6% and debt-to-GDP near 120%.

US midterms are unlikely to make a material difference to US policy. Gridlock is the name of the game. Democrats appear highly likely to gain at least a slim majority in the House and have a chance at one in the Senate. However, they are unlikely to be able to pass substantive policy given President Trump's veto power.

Historically, markets like gridlock, but the initial reaction may be a bit negative as investors associate greater Democratic influence with the potential for restrained deregulation and a lack of fiscal support. Additionally, there is a meaningful risk that President Trump, constrained domestically by gridlock, redoubles his efforts internationally, whether in Iran, through tariffs (US dollar negative), or through some other action.

US Dollar (USD)

We are neutral with a mild positive bias toward the US dollar over the near term. Strong GDP, underpinned by 3.8% personal consumption growth and the AI capex boom, high yields, elevated energy prices, and robust corporate earnings growth provide a solid foundation for the US dollar.

However, there are serious headwinds that limit US dollar upside and create some two-way risk. We've seen some deceleration in job growth and real consumer spending, compounded by lingering concerns that high oil prices, the rapidly falling personal savings rate, and high interest rates may choke off growth outside AI-related sectors. With Congress likely to be divided or fully controlled by the Democratic Party after next week's midterm elections, 2027 is unlikely to see a repeat of the large tax and tariff refunds of 2026. In fact, President Trump may increase tariffs or intensify his efforts in Iran, sending energy prices higher again. We expect any renewed focus on tariffs to weigh on the US dollar.

Regarding AI, the theme had a tough October, weighing on the US dollar. While corporate earnings are truly impressive, recent tech earnings releases have been met with falling share prices. Indeed, it is very hard to see a repeat of the extent and pace of upward earnings revisions we've seen year to date. With so much good news priced in, investors are left worrying about the ultimate payoff from AI and broader risks to economic growth outside of AI if the theme were to falter. Should the AI selloff accelerate and threaten growth more generally, the US dollar is unlikely to behave as a safe haven. On a positive note, thus far, the recent AI wobble seems to be a repricing of the risk premium rather than a structural downgrade of the narrative, which suggests it won't trigger massive capital flight from the US at this point.

We retain our pessimistic multi-year US dollar view. Rising macro risks in the US from tariffs and other policies, high debt and deficits, and the current account deficit damage the US dollar's long-run attractiveness. The capex boom and AI frenzy will probably pay off, but they are unlikely to do so before we hit a few scary bumps in the road. Innovative companies and the dynamic, flexible US labor and capital markets underpin the US as a strong home for capital investment. But why not hold those companies alongside a partial US dollar hedge to offset some of these pronounced US macro risks?

Canadian Dollar (CAD)

We are neutral to slightly positive on the Canadian dollar over the near term. Positive momentum from October, supported by the Bank of Canada (BoC) rate hike, high oil prices, and AI jitters weighing on the US dollar, points to some additional upside going into November, with USD/CAD falling toward 1.38–1.385 from near 1.40. But we stick with our prior assessment that the Canadian dollar is in a tough spot.

The BoC rate hike is at odds with softening economic trends and core inflation at target. August GDP came in at 0% month over month, below expectations of +0.2%, with the advance estimate for September GDP at -0.1% month over month. The composite PMI has ticked up but remains below 50, signaling contraction. The economy lost 68,300 jobs in September, following a 41,700 loss the prior month, pushing year-to-date total job creation into negative territory.

The BoC rate increase from 2.25% to 2.5% helps the Canadian dollar in the near term, but it was highly proactive. The Bank of Canada is worried about the potential for second-round inflation effects from the energy price shock, combined with an expected pickup in fiscal spending next year. Current fundamentals provide scant evidence to support this concern. The lack of progress in US-Canada trade talks adds some upside risk to inflation via tariffs, but that is offset by the damage to consumer and business sentiment and spending intentions.

We expect USD/CAD to remain in a 1.38–1.42 range, with a break higher to 1.44 more likely than a break lower to 1.36, unless the AI selloff accelerates and drags the US dollar lower. Even then, because we see the AI selloff as temporary, rather than the start of a structural tech downtrend, a move to 1.36 would likely prove temporary.

Next year, we expect the relative Canadian story to improve on a more durable basis. We expect US growth, while healthy, to decelerate alongside inflation, while Canada begins to enjoy greater fiscal spending, lower refined energy prices, and the lagged benefits of low real interest rates. Ultimately, over a period of more than five years, under our US dollar bear market thesis, we see USD/CAD trading back toward 1.20.

Euro (EUR)

We shift from negative on the euro going into October to neutral with a mild negative bias going forward. The known European Union negatives appear better priced in. French spreads have widened substantially over the past few months as the euro has fallen. Structural growth problems have been known for years, and recent economic data has been a touch better than expected. Finally, investors have built negative positions in the euro, suggesting that a fair amount of pessimism is already priced in.

We have become less bearish but still see a negative skew. While GDP growth has surprised to the upside, it is highly uneven, with Spain growing well and France on the brink of recession. Energy prices continue to rise, providing an additional headwind. Dutch TTF natural gas futures are up almost 150% since the end of Q2. Beyond that, the mosaic of risks may be better priced after the recent euro selloff, but the problems are not going anywhere. Those risks include French debt sustainability, with elections looming large next April; competitive risks from China; the European Union's lagging role in AI; and the slow pace of reforms to address these issues.

Another one or two European Central Bank rate hikes are unlikely to provide much support in this context. They will add further challenges to growth and still fail to make the euro one of the highest-yielding G10 currencies. Next year may be a different story if energy prices come back to earth, the French election is resolved, US growth decelerates modestly, and the Federal Reserve wraps up its mini-hiking cycle. Until then, we expect the euro to remain depressed.

Over the long term, beyond five years, we remain more constructive on the euro versus the US dollar, driven primarily by US weakness rather than European Union strength, for the reasons listed in the US dollar section above. The case for European Union investors to pull back from their concentrated exposure to US assets, or at least implement higher average currency hedge ratios, is strong as the US becomes a less reliable trade and security partner.

The outlook against other G10 currencies is less optimistic. The euro is expensive versus the Japanese yen, Norwegian krone, Swedish krona, Canadian dollar, and Australian dollar and is likely to materially underperform those currencies over the coming years.

British Pound (GBP)

We are neutral with a mild negative bias on the British pound versus the G10. We are neutral because the UK enjoys yields in the top half of the G10, and growth data continue to outperform depressed expectations. The unemployment rate is down to 4.7% from 5.2% in January. The composite PMI for October came in at a healthy 53.1, supported by upside surprises in both the manufacturing and services PMIs. The autumn budget was uneventful, mostly kicking the can of fiscal consolidation down the road, but it was well received by markets. These improved growth metrics, alongside upside surprises in both headline and core consumer price inflation, are likely to put the Bank of England (BoE) back on a hiking cycle next week.

Better growth and the resumption of rate hikes are positive for the British pound, but not enough to recommend a long position. GDP is expected to grow in the low-to-mid 1% range over the next few years, hardly impressive on an absolute basis. The BoE should begin hiking again, but the market already prices in more than four rate hikes by September 2027, which is a bit too aggressive compared with our expectations. The Burnham government got a pass for kicking the fiscal consolidation can down the road while attention is more squarely focused on French fiscal risks. But that road is not endless. At some point, UK fiscal concerns are likely to reemerge, putting pressure on both the British pound and gilts.

In the long term, the story isn't as shaky, at least not against the US dollar and Swiss franc. Over a three-to-five-year horizon, we see GBP/USD peaking above 1.40. We also see the British pound outpacing the expensive, low-yielding Swiss franc over the coming years on a total return basis. Beyond the US dollar and Swiss franc, we see the British pound struggling against the rest of the G10 over the medium and longer term.

Japanese Yen (JPY)

We remain neutral on the Japanese yen, with a mild negative bias. On the plus side, the Bank of Japan followed its September rate hike with hawkish comments as energy prices rise and both headline and core inflation move back above 2%. A December rate hike to 1.5% is increasingly likely. At the same time, we see any meaningful downside risk to the Japanese yen as capped by the credible threat of joint US-Japan currency intervention.

The issue is that, with Bank of Japan expectations being repriced higher and intervention risk well known by investors, we do not see further yen-positive catalysts at this time. To the contrary, high global yields outside Japan, Japan's position as having the second-lowest short-end yields in the G10, and lackluster household spending in Japan all point to near-term Japanese yen weakness.

The prospect of capital repatriation is another potential support that has entered the conversation and would provide a basis for a large, persistent appreciation of the Japanese yen. But we think this may prove to be

more of a 2027 or even 2028 story, despite recent improvement in local demand for longer-maturity Japanese government bonds. Negative carry remains too large to induce a significant shift in hedge ratios, while strong international asset returns, particularly in equities, incentivize Japanese investors to hold international allocations steady.

That should change over time as we move through the current Federal Reserve hiking cycle and look toward future rate cuts. Also, at some point, global equity returns are likely to level off, at least for a time. Robust capex plans and AI opportunities in Japan should also favor greater domestic investment. It is also important to note that we don't necessarily need to see a large-scale repatriation of capital back to Japan for the Japanese yen to strengthen, just a material slowdown in the pace of portfolio and foreign direct investment outflows.

In the long term, we expect substantial upside against the US dollar, with USD/JPY likely to fall back into the 120–130 range over the next three to five years, consistent with our long-term US dollar bear market thesis.

Swiss Franc (CHF)

We are neutral on the Swiss franc against the G10 over the near term. The Swiss franc looks less attractive as global real and nominal yields rise relative to Switzerland's zero nominal and negative real policy rates. Even the defensive, low-yielding Japanese yen offers positive carry of more than 1.25% versus the Swiss franc, with that advantage rising. We prefer the Swiss franc as the funding currency for carry trades. This keeps us negative over the medium to long term on a total return basis, including the negative interest rate carry associated with the Swiss franc.

However, we see scope for near-term strength, or at least stability, due to surging domestic growth, core inflation rising back to 0.5% year over year and, most importantly, a safe-haven bid related to the widening in French credit spreads. Following the joint US-Japan intervention in the Japanese yen in July, we saw a rotation away from selling the Japanese yen and toward selling the Swiss franc as the funding currency for carry trades. That trade is now unwinding under these conditions.

If there is a further pickup in equity market volatility as we move through earnings season and/or global yields continue to correct lower, the safe-haven bid for the Swiss franc could be further amplified by a broader, temporary unwind of carry trades.

Norwegian Krone (NOK)

We remain constructive on the Norwegian krone but see it as risky. Higher-for-longer oil prices, resilient growth, and 4.5% yields point to additional Norwegian krone strength. The problem is that marginal changes in growth and interest rates are less supportive. Recently inconsistent retail sales, poor industrial production, and decelerating month-over-month core inflation offset the benefits of high oil prices. These data suggest that Norges Bank is likely at the end of its hiking cycle after raising rates from 4.25% to 4.5% in September.

Most importantly, the tight positive correlation between oil and the Norwegian krone seen in Q2 and early Q3 has become inconsistent. The 15% rise in oil during September failed to lift the Norwegian krone as investors worried about oil and interest rates choking off global growth. The positive correlation returned in October, with higher oil prices translating into a stronger Norwegian krone. This return to positive correlation was likely made possible by equity strength outside of AI and the pullback in global yields.

The point is that we are close to an inflection point at which rising energy prices and higher global yields threaten global growth and risk sentiment. This creates an underlying instability in the Norwegian krone, where another surge in interest rates or oil prices could once again flip correlations negative and send the currency lower despite Norway's higher oil revenues.

The long-term outlook is more durably positive. The Norwegian krone is historically cheap relative to our estimates of fair value and is supported by steady, albeit somewhat low, long-run potential growth, decent yields, and a strong balance sheet.

Swedish Krona (SEK)

We retain a negative tactical view on the Swedish krona due to its low interest rates, disappointing September GDP, negative sensitivity to rising energy prices, and poor September retail sales data. Against that backdrop, it is tough for the Swedish krona to build on its October strength in a market that favors higher yields and strong, dependable growth.

Despite current headwinds, we see positive signs that are worth watching over the medium term. The disappointment in recent growth data is likely to prove temporary as the recovery broadens, as evidenced by strong PMI data. Consensus growth expectations in the mid-2% range compare favorably with growth in the mid-1% range across Western Europe and should support the currency. The Riksbank is poised to deliver its first rate hike since 2023 next week, likely followed by one or two more hikes next year. That will only bring the policy rate to 2.25%–2.5%, but the trajectory is beneficial. Thus, we see scope for Swedish krona appreciation versus the G10 average over the medium term despite the near-term headwinds.

In the long-term, valuation also favors the Swedish krona, which is historically cheap on a real effective basis. Sweden also has a comfortable debt-to-GDP ratio of 33%, which should help in a world of excessively high fiscal burdens. We further expect Sweden to benefit from a gradual portfolio rebalancing under our long-term US dollar bear market thesis over a multi-year horizon. On balance, spillover risks from energy prices and European Union growth, along with low real yields, are likely to dominate the otherwise solid growth outlook, pushing the Swedish krona lower for now. However, we are watching these positive factors as potential catalysts for a medium-term turnaround in the currency.

Australian Dollar (AUD)

We are neutral on the Australian dollar, with a slight negative bias. Australia leads the G10 with a 4.6% policy rate. Another rate hike to 4.85% is likely at the next Reserve Bank of Australia meeting on 03 November, following the upside inflation surprise for Q3, with core consumer price inflation rising 1% quarter over quarter. The high yield, along with strong terms of trade and a stable-to-stronger Chinese yuan, provides a solid base for the Australian dollar.

While those factors form a strong base for the Australian dollar, the trajectory of the economy and risk sentiment point in the opposite direction, favoring a weaker currency. The unemployment rate has trended up from 4.1% in January to 4.7% in September, while both the manufacturing and services PMIs have dipped below 50, signaling contraction. Consumer sentiment is weak and unlikely to improve given the soft employment picture and steadily falling home prices.

The market may be pricing in another rate hike this week, with an 80% probability, which would be the fifth in this cycle, but that may be the last. The cumulative impact of that tightening appears to be materially slowing the economy, which is likely to help contain inflation. That, in turn, should put some downward pressure on the Australian dollar. If the Reserve Bank of Australia disappoints the market and keeps rates unchanged, as the Reserve Bank of New Zealand did last month, the Australian dollar should fall sharply, by 2%–3%.

Over a multi-year horizon, we are positive on the currency, especially against the US dollar and Swiss franc. Australian investors appear to have high levels of unhedged US dollar asset exposure. In accordance with our long-run US dollar bear market thesis, we believe the Australian dollar will be well positioned due to its high yields and the strong incentive for Australian investors to adopt higher currency hedge ratios or rotate outright away from the US into a more diversified global portfolio.

New Zealand Dollar (NZD)

We are neutral on the New Zealand dollar versus the G10 average, with a small positive bias. The Reserve Bank of New Zealand surprised markets by holding rates at a middling 2.75%, citing slightly lower-than-expected inflation and the fragility of the economic recovery. Inflation at 3.7% year over year is well above the Reserve Bank of New Zealand's 1%–3% range but was lower than its expectation and down from 4.1% year over year in the prior quarter. Meanwhile, the economic recovery is concentrated in the export and tourism sectors, while household demand remains weak amid elevated unemployment, subdued wage growth, and falling home prices.

Fragile growth and middling yields are not sufficient to support currency strength. However, NZD/USD is about 2.5% above its 10-year low, while AUD/NZD is back to levels last seen in 2013. The New Zealand dollar is cheap, reflecting the less-than-attractive mix of growth and yields. Because we expect further rate hikes over the coming quarters and continued economic recovery, albeit uneven, we believe we are near or past peak pessimism, limiting downside risks to the New Zealand dollar at these levels. In fact, we see a small positive bias.

In the long term, our outlook is mixed. Our estimates of long-run fair value suggest that the New Zealand dollar is cheap versus the US dollar and Swiss franc and has ample room to appreciate, but it is expensive against the Japanese yen and Scandinavian currencies.

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