The Investment Institute
by UniCredit

Market Spotlight

Market Spotlight is our publication that looks at key market drivers

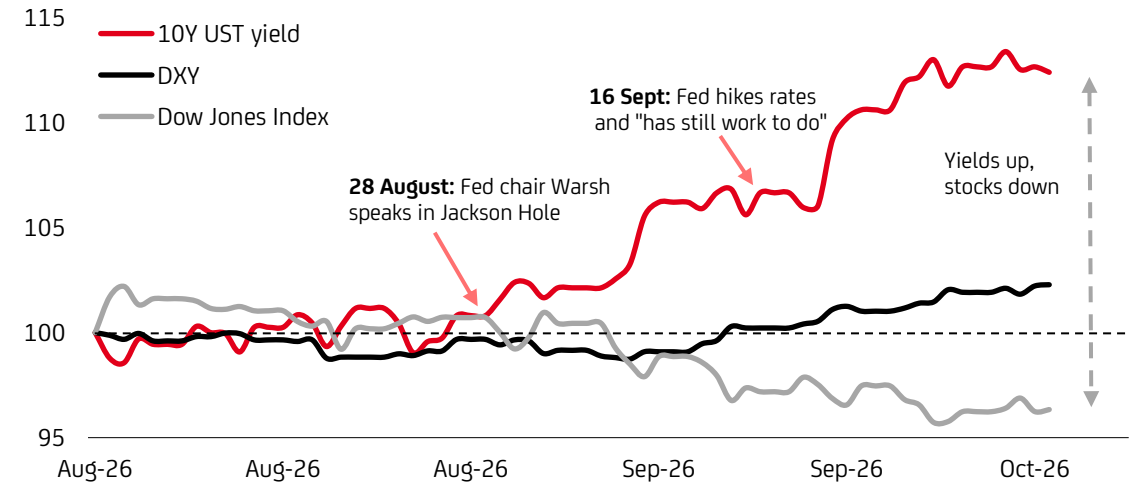
What in FX if market turmoil becomes a self-fulfilling prophecy?

9 October 2026

Investors' attempts to treat current market levels as an irresistible buying opportunity are clashing with reality as the 10Y UST yield reached a 24Y high of 5.3675% before retreating to 5.25%. With equities and bonds falling simultaneously, market turmoil risks intensifying as selling pressure feeds on itself. If this self-fulfilling sell-off takes hold, the USD may remain quite firm, supported by high US yields and its safe-haven role until markets calm down.

CHART: MARKET REACTION FOLLOWING FED CHAIR KEVIN WARSH'S SPEECH IN JACKSON HOLE AND RATE HIKE

10Y UST YIELD, DOW JONES INDEX AND THE US DOLLAR INDEX (DXY)



Source: LSEG, The Investment Institute by UniCredit
Note: all three series are indexed to 100 on 3 August 2026

THE NOISE ...

The price action seen this week has been quite instructive regarding the prevailing mood among investors. Early attempts to view current yield levels as an irresistible opportunity to buy back bonds clashed against reality, as the minutes of the September FOMC meeting showed that some participants were concerned about a possible demand-led increase in price pressures, rather than

one driven solely by higher energy costs. Consequently, under this scenario, the nearly 80bp worth of tightening priced into the US forward curve over the next 12 months could be even justified. And in this case, bond yields could still rise further before bonds are definitively viewed as a buying opportunity. Unsurprisingly, the 10Y UST yield hit a 24Y high of 5.3675% on Wednesday before retreating to around 5.25% ahead of the Columbus Day holiday in the US on Monday, confirming that fluctuations also in bond yields remain large at present.

… AND THE SIGNAL

But the ongoing market turmoil could intensify. Price action shows that equity markets worldwide are falling alongside bonds. There is a risk that a bearish self-fulfilling prophecy could emerge, whereby, in the absence of the intervention of an external agent (namely, central banks), investors adopt the logic that "we sell because markets are falling and markets are falling because we sell".

The chart on the previous page shows movements in the 10Y UST yield, the Dow Jones Index and the US Dollar Index (DXY) since August, highlighting the escalation in market tensions, especially on the yield front, following Fed Chair Kevin Warsh's speech in Jackson Hole on 28 August and the 25bp rate hike delivered at the 16 September FOMC meeting, at which Warsh indicated that the US central bank still has work to do.

Unfortunately, central banks have remained largely silent until now, especially in the US. Remarks by Banque de France Governor Emmanuel Moulin that the situation in the country is serious but does not require ECB action, and comments by other ECB officials that repricing of yields could impact future stance and higher yields could materially impact the economy, are probably too tepid to halt the ongoing market situation, let alone definitively reverse it. The current crisis originated in the US, probably because of an overly aggressive Fed stance on monetary tightening, as we discuss in more detail in our *Short View* – The USD between soaring UST yields and buying opportunities, 7 October. Hence, any solution needs to come through the US and the Fed.

In the meantime, the implications for the FX market are straightforward: the USD is set to remain quite firm, benefiting from soaring US yields. Its safe-haven status could provide additional support if the bearish self-fulfilling prophecy materialises or geopolitical tensions in the Middle East escalate significantly again. However, US President Donald Trump has ultimately denied talks that he will attack Iran before the US midterm elections on 3 November. Given the current situation and widening yield spreads across the eurozone due to creeping political risk, EUR-USD's ability to hold the line at around 1.12 appears to be a sign of resilience rather than weakness. The CHF and the JPY may also benefit, probably more against the euro than against the greenback.

Of course, a bullish self-fulfilling prophecy may also emerge if sentiment turns, markets recover on their own and stocks and bonds rally together. A drop in the 10Y UST yield back to 5.00% or even 4.80%, the level prevailing early in September before market turmoil began and more in line with our scenario, may suggest that the crisis is over. The USD would then lose some of its strength as UST yields decline. However, even in this case, a recovery in EUR-USD to 1.16, its level one month ago, would remain very difficult if political tensions across the eurozone persist.

Author
Roberto Mialich, FX Strategist – Global (UniCredit Milan), roberto.mialich@unicredit.eu

Editor
Edoardo Campanella, Director & Editor-in-Chief of The Investment Institute (UniCredit Milan),
edoardo.campanella@unicredit.eu

UniCredit S.p.A.
The Investment Institute by UniCredit, Piazza Gae Aulenti, 4, I-20154 Milan
the-investment-institute@unicredit.eu

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