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by UniCredit

Market Spotlight

Market Spotlight is our publication
that looks at key market drivers

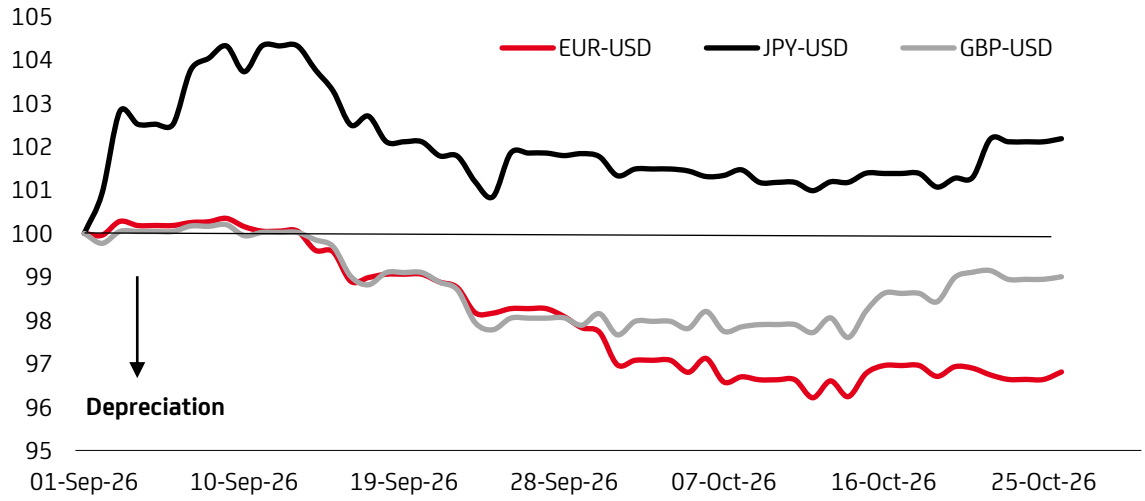
EUR, JPY, and sterling: a moment of truth

26 October 2026

The next eight days will be critical in shaping the outlook for the euro, the yen and sterling. Central banks, in particular, will have to provide answers. Market participants expect convincing guidance to help shape their strategies. Otherwise, these three currencies are likely to come under renewed pressure, benefiting the USD and the CHF.

THE EUR HAS BEEN PENALISED THE MOST SINCE SEPTEMBER COMPARED TO THE JPY AND STERLING

EUR, JPY, AND STERLING AGAINST THE USD



Source: LSEG, the Investment Institute by UniCredit
Note: all exchange rates are indexed to 100 on 1 September 2026. The JPY is expressed in terms of quantity of dollars per yen.

THE NOISE ...

The next eight days will be decisive in shaping the financial-market landscape, including FX. Central banks, in particular, will have no choice but to provide answers; they will be compelled, however reluctantly, to lay their cards on the table. Otherwise, tensions are likely to resurface, particularly in bond markets, pushing long-term bond yields higher and widening yield spreads over Bunds across the eurozone.

Central banks are expected to offer guidance to help investors shape their future strategies. Otherwise, the euro, sterling and even the JPY may suffer, while the USD and the CHF may benefit further.

… AND THE SIGNAL

Five key events will shape the FX outlook, with a sixth to follow next week:

1. **Tomorrow, the elections in Israel** will feature a contest between Bibi Netanyahu's Likud party and the Yashar party, led by Gadi Eisenkot. Yet, the outcome of the vote is unlikely to alter Israel's foreign policy, particularly towards Iran. The race between the two parties is very close, and neither is projected to reach the 61-seat threshold required for a majority in the 120-member Knesset. Coalition negotiations are therefore likely, with new elections possible if they fail. The resulting uncertainty may keep the USD on bid.
2. **On Wednesday**, **the Fed** – along with its Chair Kevin Warsh – is expected to clarify whether it intends to proceed with a rate-hiking cycle that carries the risk of over-tightening. Markets have already begun to adjust to their expectations following less aggressive remarks from influential Fed officials such as John Williams and Michelle Bowman. We expect the Fed to stay on hold at this meeting and to hike in December. However, what will matter is how hawkish Warsh will sound in his overall assessment of the economic outlook. Less hawkish signals would likely keep the 10Y UST yield below 5% and put further downward pressure on the USD. Conversely, a reaffirmation of the Fed's hawkish stance would push the 10Y UST yield back towards its recent 24-year peak of 5.3475%, reinvigorate the US unit and drag EUR-USD towards or even below its recent low of 1.1114.
3. **Also on Wednesday, the UK will unveil its autumn budget**. This will be the first significant test of the new Burnham government's fiscal strategy. In the past, concerns about the UK's potentially spiraling public finances, specifically regarding the cost of borrowing and rising debt levels, weighed on sterling, even as gilt yields climbed. The government has committed to honoring the 2024 manifesto promise not to increase the main rates of Income Tax, employee National Insurance, or VAT. However, economic pressures from rising gilt yields and global energy volatility have reduced Treasury fiscal buffers down to an estimated GBP12bn/20bn, leaving the Chancellor balancing strict fiscal rules with pressure for spending.
4. **On Thursday, the ECB**, beyond preparing markets for the anticipated tightening in December, will face scrutiny regarding whether and how it intends to address widening government bond yield spreads within the eurozone, particularly in France. An overly tepid response risks intensifying pressure across the eurozone and weighing on the EUR against both the USD and the CHF.
5. **On Friday, the BoJ,** while likely keeping interest rates steady at 1.25%, despite inflation in Japan recently reaching the 2% target, will raise its inflation projections, but more critically will need to clarify the extent to which it intends to accelerate the normalization of monetary policy. An increase to 1.50% in December is already all but certain. The BoJ must also address whether, and by how much, it might raise its policy rate above 2% by 2027 – a level that now appears to be the minimum expected endpoint and could easily be exceeded by 2028. The JPY may benefit from the BoJ continuing to sound hawkish, while fears of renewed Japanese and US intervention may limit any JPY retreat.

All of this is taking place as we await the outcome of the US midterm elections on 3 November. There is a possibility that US President Donald Trump might respond to a likely defeat by testing his emergency powers even further, while resuming attacks on Iran.

According to reports in the US press, renewed attacks have already been coordinated with Israel, regardless of the outcome of Tuesday's elections. The impact on the USD remains difficult to predict, as a potential "sell America" reaction due to democratic backsliding could be offset by safe-haven demand for the currency if global risk aversion escalates.

Lastly, markets are likely to brace for a big sell-off in Brazilian assets today, including the BRL, which may even exceed pre-election values against the greenback beyond 5.20-5.30, after Luis Inácio Lula da Silva was re-elected president of Brazil with 51.8% of the vote ahead of Flávio Blosonaro (48.2%).

Bolsonaro has said he will seek to have the election annulled, calling the last-minute extensions of voting hours ordered by the Supreme Court "unacceptable". Yet, the risks outlined above are likely to have broader implications for markets.

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