Forex and Interest Rate Outlook

AIB Treasury Economic Research Unit

17th November 2026

- Global economy has been robust in the face of geopolitical shocks, but downside risks to the outlook remain elevated
- US economy continues to outperform, with the Eurozone and UK dented by higher energy prices and policy uncertainty
- Markets anticipate further rate hikes from central banks. However, the outcome could differ if inflation undershoots expectations
- Higher rate expectations supporting the dollar, with Fed policy guidance recently tilting more hawkish
- Euro to remain on defensive in near term, but could regain strength in 2027

David McNamara
Chief Economist

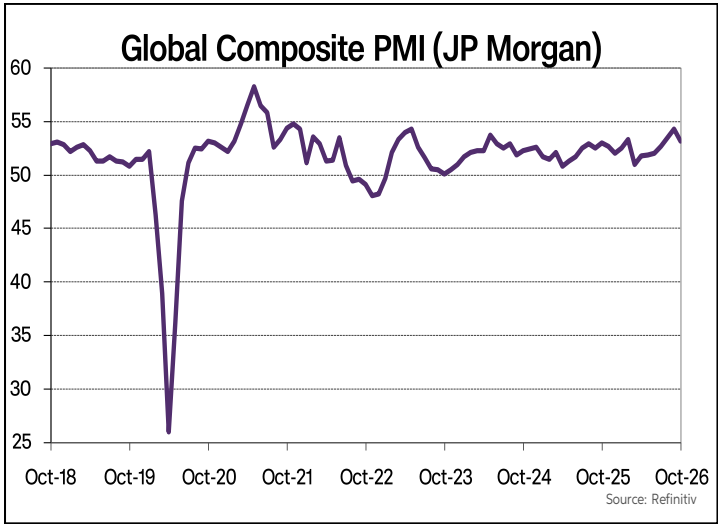
John Fahey
Senior Economist

Daniel Noonan
Economist

https://aib.ie/investorrelations/economic-research-unit

Global Economic Outlook

	Oil price fall but outlook highly uncertain
Energy prices have eased back in recent weeks	Following the US midterms and signs of a détente in hostilities between the US and Iran, oil prices have eased to a $90-100 per barrel range from a near-$120 peak. Oil supply remains below pre-war levels, but is recovering from the nadir reached in the spring. Nevertheless, the supply of oil and other commodities from the region remain constrained amid rising demand heading into the winter period.
Oil prices trading between $90 -100, natural gas prices remain elevated	The recent oil price surge was similar to 2022, reaching a recent peak close to $120/barrel in March/April, and again in October. However, European natural gas prices remained at a fraction of the highs reached in 2022. In recent weeks, gas prices have ranged between €85-90/kWh, compared to a peak of €350/kWh in 2022. In recent weeks European demand has pushed up prices ahead of the heating season.
Central banks remain weary of second round effects	At the last round of central bank meetings in October/November, energy and second-round inflationary effects were the key themes, with most policymakers conceding there are few signs of broadening price pressures beyond energy goods. Indeed, second-round effects have yet to materialise to any great extent in the Eurozone and the UK, with the elevated core inflation rate in the US a legacy of the previous inflationary shock, underpinned by the exceptional growth in the US economy and the labour market of late.
	Spluttering AI trade driving market volatility
AI trade begins to wobble	Alongside energy prices, sharp swings in tech/AI sector valuations have also spilled over to forex and bond markets. Indeed, the tech-heavy NASDAQ essentially hit a peak in May of this year, and has treaded water since then, struggling to sustain the exceptional upward momentum of the previous 12-18 months. The NASDAQ 100 is nearly 11% lower since the beginning of the quarter, exacerbated by company-specific issues at NVIDIA, one of the largest companies in the US by market cap.
Safe-haven flows to sovereign bonds and the dollar	While the AI trade has seemed impervious to fundamentals over the past few years, the rising cost of capital is also a factor in the current slump. US swap rates have risen sharply since the war in the Middle East began, while long-end yields have surged on both inflationary and fiscal sustainability concerns. Nonetheless, the retreat in equity prices has seen a flight to safety in recent weeks, with the US 10-year Treasury yield at 5.1%, off its recent peak of c.5.3%. The dollar has also strengthened versus the other majors.
US regulatory changes post midterms could blunt AI build-out	The AI-trade wobble has also been driven by fears of a policy lurch towards increased regulation of AI and related infrastructure. Most notably, several state-level ballot measures and candidates in the US midterms that sought to curtail data centres were successful. This has triggered a re-assessment of the AI trade, with firms most exposed to the build-out seeing the sharpest hit to valuations.



GDP (Vol % Change)

	2024	2025	2026 (f)	2027 (f)
World	3.5	3.5	3.1	3.4
Advanced Economies	1.9	2.0	2.1	1.8
US	2.8	2.3	2.3	2.3
Eurozone	1.0	1.2	1.1	1.2
UK	1.0	1.2	1.3	1.2
Japan	-0.2	1.2	0.7	0.7
Emerging Economies				
China	5.0	5.0	4.5	4.0
India	7.1	7.8	7.0	7.0
World Trade Growth (%)	3.7	5.0	4.6	4.7
Inflation -CPI				
Advanced Economies (%)	2.6	2.5	3.1	2.7

Sources: IMF Economic Outlook Update, October 2026

Interest Rate Outlook

Central Banks hike and markets expect more rate rises

Central banks raise rates in response to energy price shock

The energy price shock arising from the war in the Middle East has seen all the main central banks raise rates. The surge in energy prices has resulted in a notable move higher in headline inflation. However, so far, second-round effects appear to be muted. Nonetheless, central bankers are very attentive to upside risks to underlying inflation, and in turn, to achieving their price stability targets. Hence, the policy tightening implemented over recent months from the Fed, ECB, BoE and BoJ. Meanwhile, with energy prices remaining elevated and amid hawkish rhetoric from monetary policy officials, the market is anticipating further rate increases from all the main central banks.

Fed looks likely to hike again before year end

The Fed left its policy rate unchanged at 3.75–4.00% in October, with two FOMC members favouring a 25bps hike. The most recent policy change from the Fed came at their previous meeting in September, when they decided to hike rates (for the first time since July'23) by 25bps. Chair Warsh maintained an inflation-focused, moderately hawkish tone, stressing the need for further data before determining the appropriate policy stance. Remarks from a raft of Fed officials over the last week indicated an increasingly hawkish FOMC. This combined with higher than anticipated October CPI data has seen a significant hardening in US rate expectations. The market is fully pricing in a 25bp hike next month and is now factoring in around 90bps of additional tightening in total by end-2027. We believe the extent of further rate hikes will be more limited and envisage an additional 50bps of tightening.

ECB suggests December is a 'live' meeting for another rate hike

The ECB left its key interest rates unchanged in October, with the deposit rate remaining at 2.50%, following September's 25bp hike. President Lagarde (who is leaving her role early, in Feb'27) indicated that December is a "live" meeting, revealing that the Governing Council debated a hike in October but ultimately judged itself "well positioned" to hold for now. The ECB continues to emphasise a data-dependent, meeting-by-meeting approach, with incoming data expected to provide greater clarity. Markets currently price around an 85% probability of a 25bps December hike and roughly 50bps of further tightening in 2027. While a December increase appears reasonable, we expect the deposit rate to peak at 2.75%, as tighter financial conditions and limited second-round inflation effects should reduce the need for significant additional tightening next year.

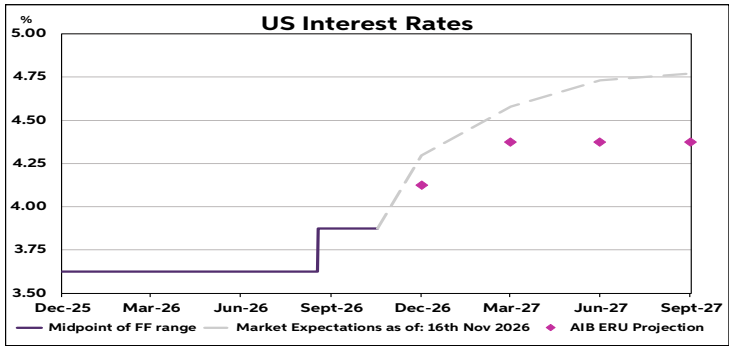
BoE hikes in November but Gov Bailey suggests relatively limited tightening cycle

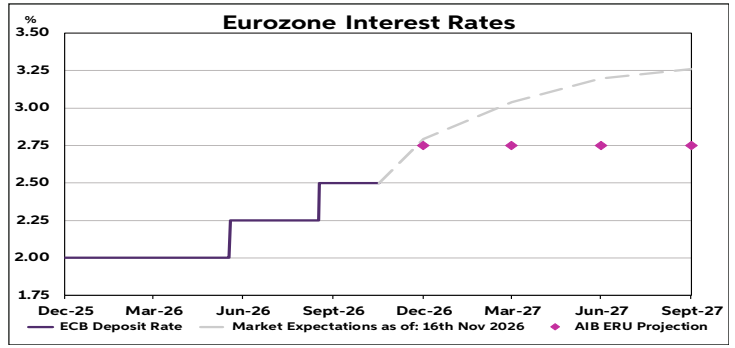
The BoE raised the Bank Rate by 25bps to 4.00% in November, its first increase since August 2023, with the MPC voting 8:1 in favour (Catherine Mann preferred a 50bp hike). The minutes indicated that six members believe further tightening could be warranted, particularly if the Middle East conflict persists and second-round inflation pressures emerge. However, Governor Bailey stressed that the increase should not be viewed as the start of an inevitable sequence of hikes, reinforcing the MPC's meeting-by-meeting approach. The market is factoring in another hike in December and circa 100bps in total of additional tightening by end-2027. We continue to view market expectations as excessive, forecasting one further 25bp increase, which would see Bank Rate peak at 4.25%, compared with the market-implied 4.75-5.00%.

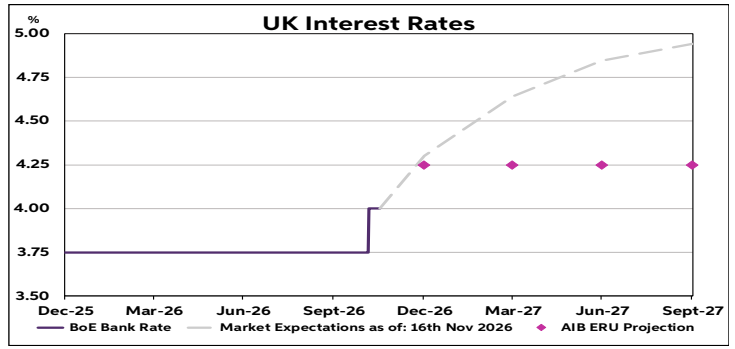
Interest Rate Forecasts

	Current	End Q4 2026	End Q1 2027	End Q2 2027	End Q3 2027
Fed Funds	3.875	4.125	4.375	4.375	4.375
ECB Deposit	2.50	2.75	2.75	2.75	2.75
BoE Repo	4.00	4.25	4.25	4.25	4.25

Current Rates Reuters, Forecasts AIB's ERU







Forex Market Outlook

AIB Treasury Economic Research Unit

Dollar has been in the ascendancy recently

Dollar has benefitted from current conflict and higher market interest rates

The dollar has gained ground over the course of the final quarter of 2026, with the trade-weighted DXY index up 1.3%. Against the euro, the dollar has appreciated even more, up over 2%. While the dollar benefitted somewhat from the terms of trade boost of higher oil prices in recent months, it appears the rise in interest rate expectations and ongoing economic outperformance have also benefitted the greenback.

An enduring conflict could be a boost to dollar, but this risk has diminished

While Middle East oil flows are now close to pre-war levels, oil prices remain elevated at c.$95 per barrel. Surging winter demand and a catch-up in strategic reserves are boosting oil demand globally, underpinning continued elevated oil prices. A more adverse scenario of a sustained war and energy price shock would likely be a boost for the dollar in the short term, but this risk appears to have diminished for now.

Dollar strength expected near term, and unwinding in 2027

The policy trajectory of the Fed will be a key driver of the dollar, with Chair Kevin Warsh setting out a hawkish outlook in recent months. However, the big picture is Warsh is a relatively dovish Chair, but his longer term view is being hampered by sticky core inflation and a relatively hawkish FOMC. However, following a couple of further rate hikes, we expect Warsh to reassert his dovish credentials next year. This could spur a more sustained rise in EUR/USD in 2027, reflected in a top end of our forecast range being $1.17 for Q3 2027.

Europe more exposed to energy shocks, fiscal risks mounting

Europe highly exposed to energy shock, but underlying inflation muted

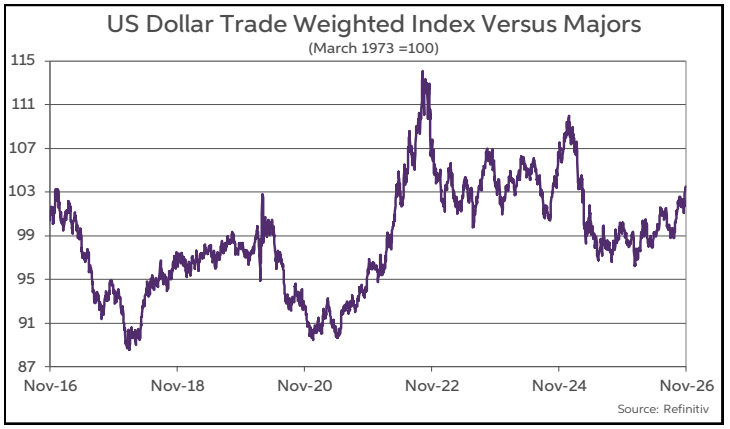
With most Eurozone countries net importers of energy, the shock to oil prices has fed through quickly to consumer prices, with inflation peaking at around 3.5% across the Eurozone. In that context markets have priced in circa 75bps in total by end-2027. However, with underlying inflationary pressures muted and the economy weak, we expect just one further hike from the ECB, which could weigh on the currency in the near term.

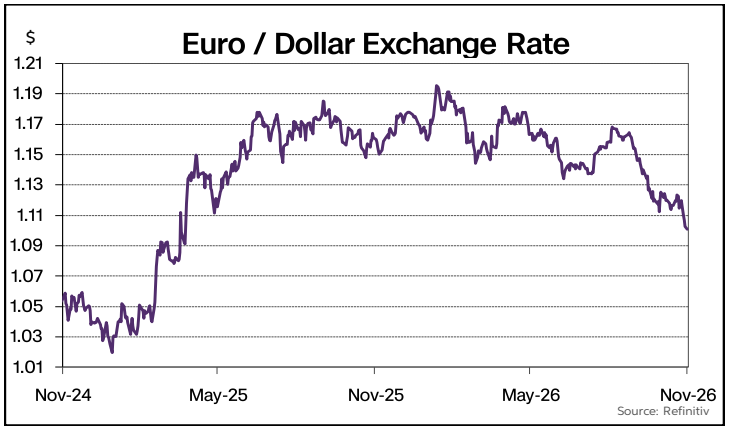
Political uncertainty to weigh on Euro

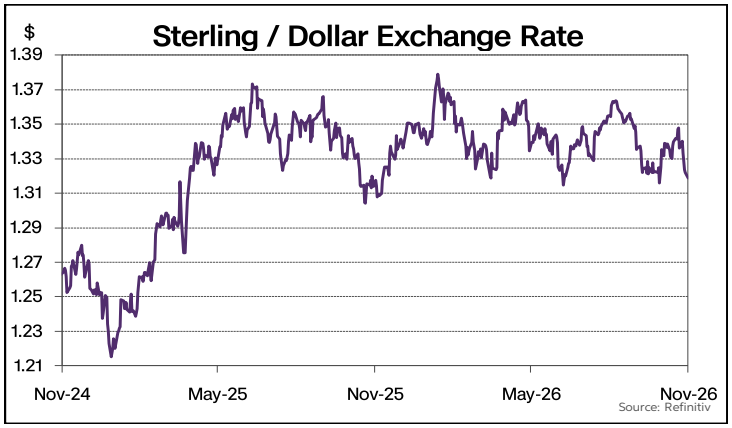
With a series of elections on the horizon in Spain, France and other Eurozone countries, and fiscal risks crystalising in major economies, the currency has been on the defensive. We expect this to continue in the near term, with some relief as energy price begin to normalise in 2027.

Euro to make modest gains against the dollar in 2027

We anticipate the euro to remain under pressures versus the dollar over the remainder of 2026, but for the Euro to regain some ground in 2027. We expect the pair to remain in the current $1.10-1.12 range, before recovering gradually to $1.14 by Q3 2027. However, risks are clearly to the downside if we see a more prolonged shock to energy prices, which would likely boost the dollar further.







Forex Market Outlook

Sterling has gained ground, but move may not be sustained

UK gilts and sterling more cyclical amid geopolitical risks

Sterling and gilts have proved volatile in the current geopolitical environment. Meanwhile, the available hard data point to a solid UK economy, and the budget in October proved a non-event in terms of market moving news. More broadly, sterling has been boosted by higher rate expectations, and relative political calm versus its European neighbours, boosting sterling against the euro to an 18-month high in recent weeks. A more conciliatory tone towards the EU from PM Burnham has also provided a helpful backdrop for sterling.

BoE set for modest rate hiking cycle, limiting any potential sterling upside

The BoE belatedly hiked rates in November. On the inflation front, while member's views diverged, the majority still view the risks of second-round inflation as being relatively muted compared to the last price shock in 2022. Our expectation is for the BoE to hike just once more in this cycle, which is more dovish than the market is currently pricing in. This, combined with weak GDP growth prospects, could act as a drag on sterling in the near term, particularly against the dollar.

Sterling to remain close to current levels in the near term, risks to downside

Sterling is expected to be modestly lower through the remainder of 2026 versus the euro. However, the pair is likely to remain largely range-bound as relative macro fundamentals are unlikely to drive a notable break-out from the current range. EUR/GBP could move towards 85p by Q3 2027. We see the potential for GBP/USD to hold at around $1.34-1.36 through to Q3 2027.

Yen volatile, but FX interventions and rate hikes to provide support

The yen has been volatile in 2026

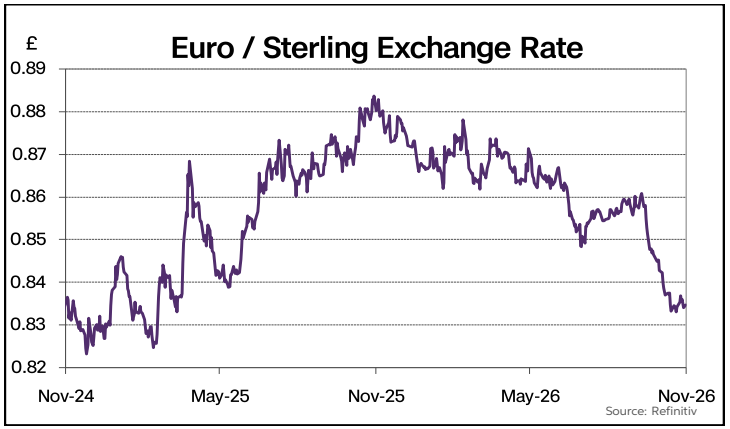
The yen had been exceptionally volatile in 2026. With USD/JPY trading above the 'pain point' of ¥160, authorities intervened to support the currency, alongside a first US intervention since the late-1990's earlier this year. This pushed the pair to c.¥156, but the currency has lost ground of late, settling at c.¥159 in recent weeks. The upshot is an expectation that Japan will tighten both fiscal and monetary policy to sustain the yen below the ¥160 threshold.

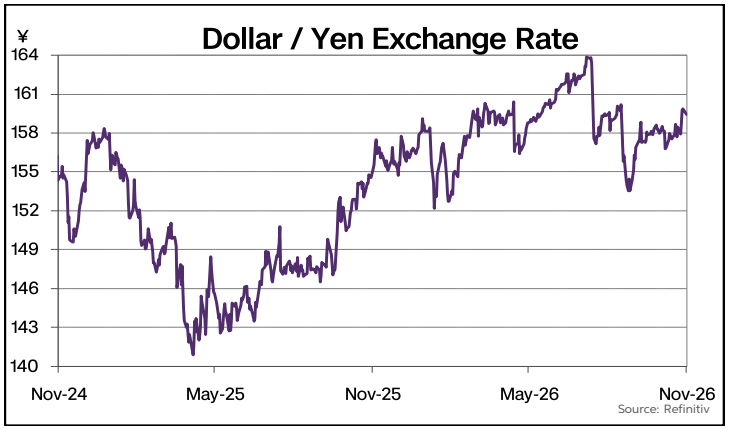
Further central bank hikes should be supportive to the currency

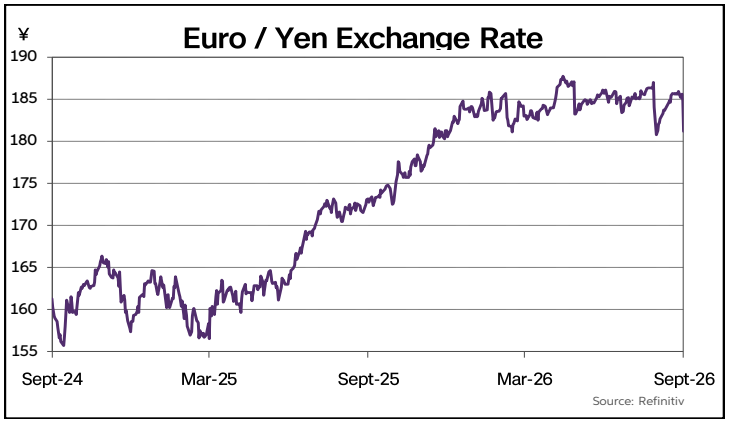
Markets are pricing in a further 75bps of hikes by the Bank of Japan (BoJ) by end-2027, which should provide a supportive backdrop for the yen. Around 25bps in total is priced in before the end of 2026, with circa 50bps priced in throughout 2027. The BoJ may move faster than is currently priced in, front-loading its interventions given the recent pressure on the yen.

Yen expected to strengthen slightly in the near term

The yen is expected to appreciate modestly in the near term. We see the yen staying within ¥156-162 during Q4 versus the dollar, but falling to around ¥155 by Q3 2027. Versus the euro, the currency is expected to remain relatively static, trading in the ¥174-180 range for the remainder of the year and into 2027. BoJ rates will be a key catalyst, with current sticky inflation raising the risk of faster rate hikes than is currently priced in.





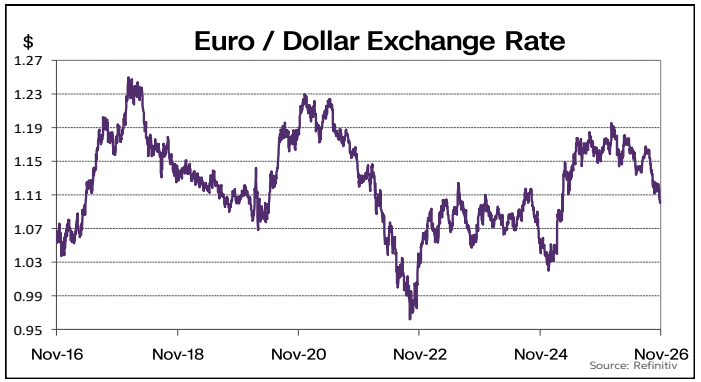


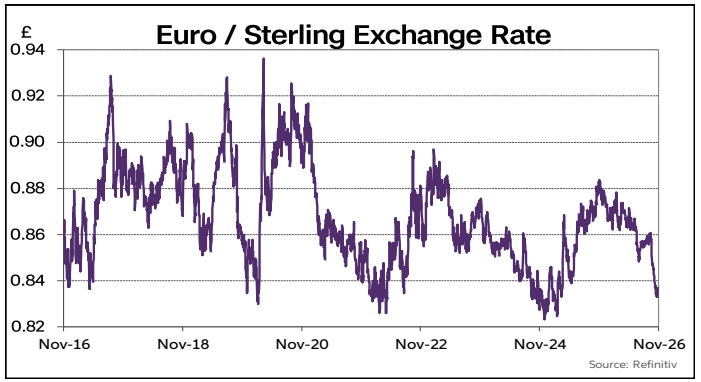
AIB Treasury Economic Research Unit

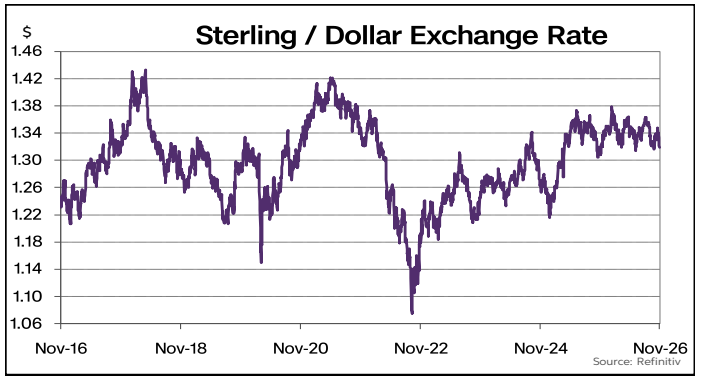
Summary of Exchange Rate Forecasts

("Spot" Forecasts for end Quarter can be taken as Mid-Point of expected Trading Range)

	Current	Q4-2026	Q1-2027	Q2-2027	Q3-2027
Euro Versus					
USD	1.099	1.08-1.14	1.09-1.15	1.10-1.16	1.11-1.17
GBP	0.833	0.81-0.87	0.81-0.87	0.82-0.88	0.82-0.88
JPY	174.8	174-180	174-180	174-180	174-180
CHF	0.92	0.92	0.93	0.94	0.94
US Dollar Versus					
JPY	159.0	156-162	155-161	154-160	152-158
GBP	1.319	1.29-1.35	1.30-1.36	1.30-1.36	1.31-1.37
CAD	1.43	1.40	1.40	1.40	1.40
AUD	0.67	0.69	0.70	0.71	0.71
NZD	0.55	0.56	0.57	0.59	0.61
CNY	6.67	6.70	6.80	6.80	6.80
Sterling Versus					
JPY	210	210	210	209	208
CAD	1.89	1.85	1.87	1.86	1.88
AUD	1.96	1.91	1.90	1.87	1.89
NZD	2.40	2.36	2.33	2.25	2.20







AIB Treasury Economic Research Unit

This publication is for information purposes and is not an invitation to deal. The information is believed to be reliable but is not guaranteed. Any expressions of opinions are subject to change without notice. This publication is not to be reproduced in whole or in part without prior permission. In the Republic of Ireland it is distributed by Allied Irish Banks, p.l.c. In the UK it is distributed by Allied Irish Banks, plc and Allied Irish Banks (GB). In Northern Ireland it is distributed by Allied Irish Bank (NI). In the United States of America it is distributed by Allied Irish Banks, plc. Allied Irish Banks, p.l.c. is regulated by the Central Bank of Ireland. AIB (GB) and AIB (NI) are trade marks used under licence by AIB Group (UK) p.l.c. (a wholly owned subsidiary of Allied Irish Banks, p.l.c.), incorporated in Northern Ireland. Registered Office 92 Ann Street Belfast BT1 3HH. Registered Number NI 018800. Authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. In the United States of America, Allied Irish Banks, p.l.c., New York Branch, is a branch licensed by the New York State Department of Financial Services. Deposits and other investment products are not FDIC insured, they are not guaranteed by any bank and they may lose value. Please note that telephone calls may be recorded in line with market practice.

AIB, 10 Molesworth Street, Dublin 2 Tel: 353-1-6600311 https://aib.ie/investorrelations/economic-research-unit