AmBank Economics

#WhatWeThink

FX update – Policy rates shift higher; minimal impact assessed for FX

16 October 2026

Executive Summary

A summer of resurgent US-Iran tensions has pushed oil prices up, and product prices even higher. With inflation set to remain higher for longer, global bonds have weakened in anticipation of more rate hikes ahead by central banks. Nevertheless, we assess the impact to be minimal on major currencies, given similar inflation profiles and expected monetary-tightening cycles. Instead, risks to our projections ahead are predicated on idiosyncratic, domestic developments for each country/currency.

A summer of war, escalations, and reprisals

After a trough around end-June, crude oil prices have steadily rebounded, with Brent remaining well above USD100/bbl since early September. US-Iran peace negotiations in late June were not only derailed, but the conflict is also now spreading beyond the Persian Gulf region and involving attacks on Saudi Arabia's East-West pipeline. Gains were even sharper for petroleum product prices (see Exhibits 3-5), supported by a potent mix of catalysts – some of which reinforce each other: 1) refinery attacks in West Asia, and some unplanned refinery disruptions elsewhere due to unsustainably high refinery run rates earlier, 2) Supply chain disruptions + higher fuel oil and diesel costs for transportation, 3) Ukraine-Russia escalations into strikes on ports and energy infrastructure, and 4) the smaller stockpile of oil products (prior to the war) relative to crude oil. With the US and Iran largely at a military/economic stalemate and trust in meaningful talks low, we think energy prices are set to remain elevated for longer. Fluid peace-war events (dialogues, escalations, successful transits, etc.) are also expected to fuel continued market volatility.

Central banks turn hawkish as fresh inflation risks loom

With higher energy prices set to drive inflation higher, most major central banks (the Fed, ECB, BOJ, and RBA) have hiked their respective policy rates in their recent September meetings, while market expectations of global central bank policy rates have shifted even more hawkish over the past few months (see Exhibits 8 – 12). As of end-June 2026, the greatest shift was observed for the ECB, BOJ, and Fed, with markets pricing in policy rates of 3.07%, 1.85%, and 4.74% by mid-2027 (prior: 2.40%, 1.21%, and 4.18%, respectively). In comparison, shifts for the RBA were relatively subdued (see Exhibit 12), though we qualify that the RBA had been persistently hawkish even before the outset of the US-Iran war, with three rate hikes already done between September 2025 and May 2026. Meanwhile, for the BOE, expectations for the first BOE rate hike have continuously been deferred, owing to tempered comments by Governor Bailey, subdued core inflation readings in the UK, and risks of spillover towards financial market instability – with new PM Burnham and Chancellor Healey set to announce their first Autumn Budget on 28 November.

Exhibit 1: AmBank currency forecasts

	4Q26	1Q27	2Q27	3Q27	4Q27
USDMYR	4.08	4.07	4.05	4.05	4.05
DXY	102.1	103.1	101.8	101.3	100.6
EURUSD	1.12	1.10	1.12	1.13	1.14
GBPUSD	1.32	1.33	1.34	1.34	1.35
AUDUSD	0.68	0.67	0.67	0.69	0.70
USDJPY	158	159	160	160	160

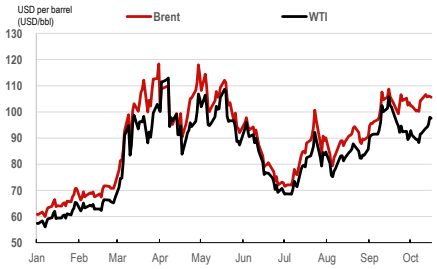
Sources: AmBank Economics, Bloomberg

Exhibit 2: AmBank policy rate forecasts

	4Q26	1Q27	2Q27	3Q27	4Q27
OPR	2.75	2.75	2.75	2.75	2.75
US FFR (UB)	4.25	4.25	4.50	4.50	4.50
ECB	2.75	3.00	3.00	3.00	3.00
BOE	4.00	4.25	4.25	4.50	4.50
RBA	4.60	4.60	4.60	4.85	4.85
BOJ	1.50	1.50	1.75	1.75	1.75

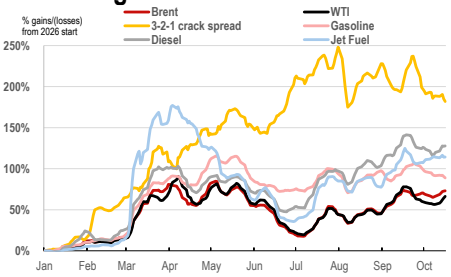
Source: AmBank Economics, Bloomberg

Exhibit 3: While the increase in upstream crude oil prices has been significant…



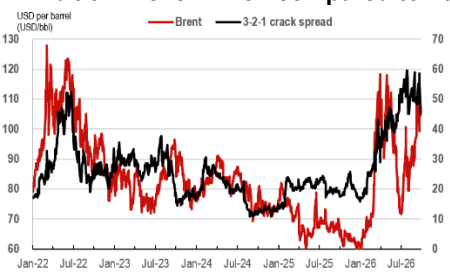
Source: AmBank Economics, Bloomberg

Exhibit 4: … the impact on oil product prices has been greater and stickier…



Source: AmBank Economics, Bloomberg

Exhibit 5: … even when compared to 2022



Source: AmBank Economics, Bloomberg

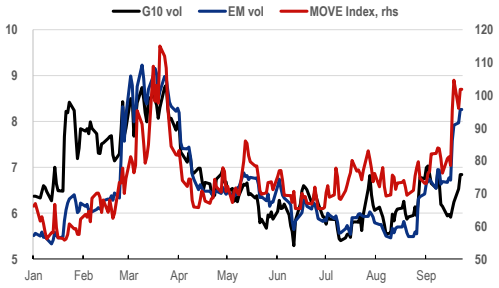
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DM currencies stable despite bond market weaknesses

Despite the recent upward shift in policy rate expectations (which was among the driving forces behind bond market weakness), contagion into FX markets appears to be limited to EM currencies, while volatility among G10 currencies was contained (see Exhibit 6). Developed economies tend to experience similar macroeconomic shocks together (i.e. higher energy prices and inflation risks), of which major central banks tend to respond similarly. Hence, with yields on major bonds rising in tandem, these bonds remain equally attractive/unattractive to investors, resulting in little arbitrage opportunities via currency valuations. Meanwhile, central banks of EM economies must respond to additional considerations beyond inflation risks, including shifts in market sentiment, capital flows, currency stability, and trade account dynamics. As such, the risk of monetary policy divergence exists. Market adjustments to higher UST yields are also reflected in higher bond yields for other DM countries; while anchored policy rates and front-end bond yields for EM economies mean the burden of adjustment is borne by their respective currencies instead (see Exhibit 7).

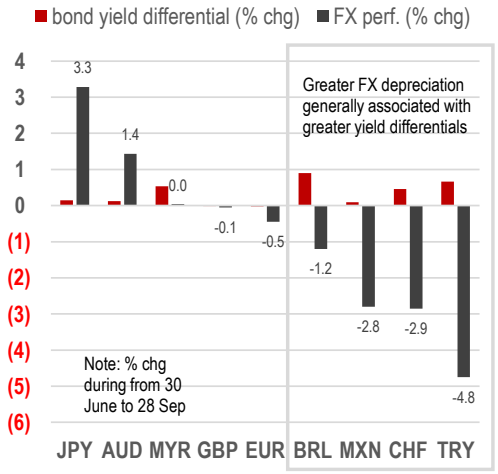
Hence, despite an overall upward shift in our policy rate expectations (compared to our previous update on 13 August), our currency forecasts show little accompanying change in this report. Our assessments of the risks ahead include: 1) Differing pathway of inflation ahead for each country due to differing local labour markets, trade account, and executive policy measure dynamics (for example: Energy-related subsidies, restriction of oil product exports, an unexpectedly tight/weak labour market, etc.), 2) Central bank independence + fiscal dominance risks (particularly for the BOJ, but also the US and the UK), 3) Political cycle risks in the US this year (mid-term elections), and the Eurozone (France, Italy, and Spain) and Malaysia next year, and 4) A slowdown in current AI infrastructure development (with impact on the US and Malaysia expected to be greater than the Eurozone/UK/Japan/Australia). While intermittent escalations in US-Iran tensions may lead to temporary spikes in energy prices and a brief repricing of central bank rate expectations, we expect these effects to prove short-lived. As such, we estimate the implications for our FX forecasts to be minimal (as per our earlier assessment on 13 August).

Exhibit 6: Volatility in G10 currencies remains tame relative to its 2026 peak in March



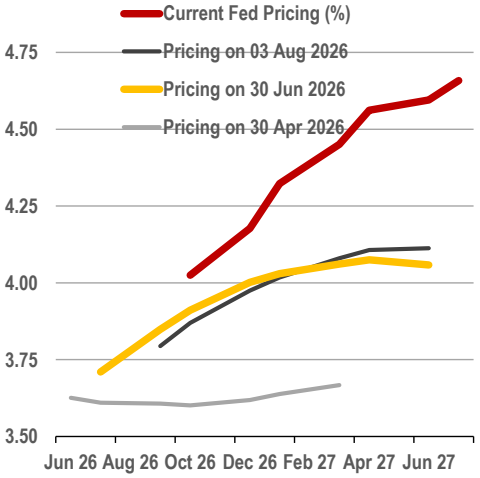
Source: AmBank Economics, Bloomberg

Exhibit 7: Depreciation of the BRL, MXN, CHF, and TRY amid a widening of front-end yield differentials



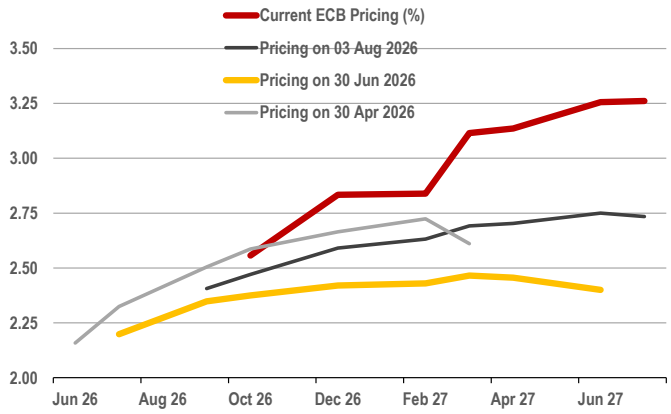
Source: AmBank Economics, Bloomberg

Exhibit 8: Fed policy rate expectations



Sources: AmBank Economics, Bloomberg

Exhibit 9: ECB policy rate expectations



Sources: AmBank Economics, Bloomberg

Exhibit 10: BOE policy rate expectations

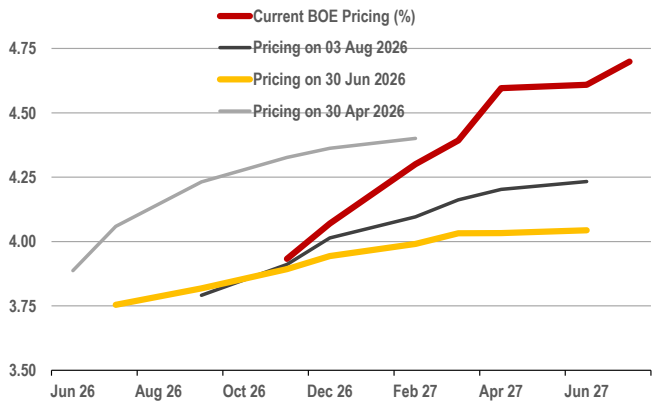
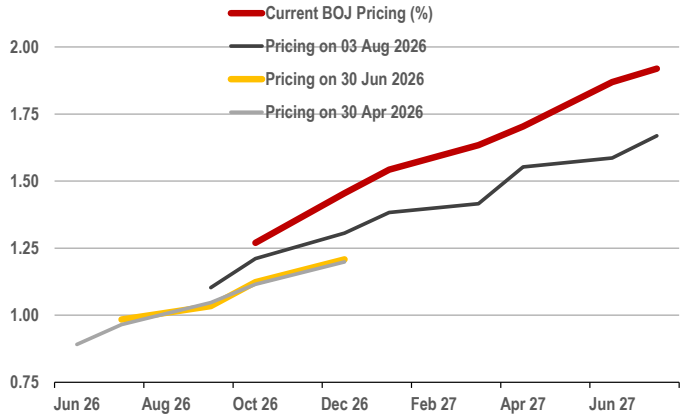


Exhibit 11: BOJ policy rate expectations



Sources: AmBank Economics, Bloomberg

Exhibit 12: RBA policy rate expectations

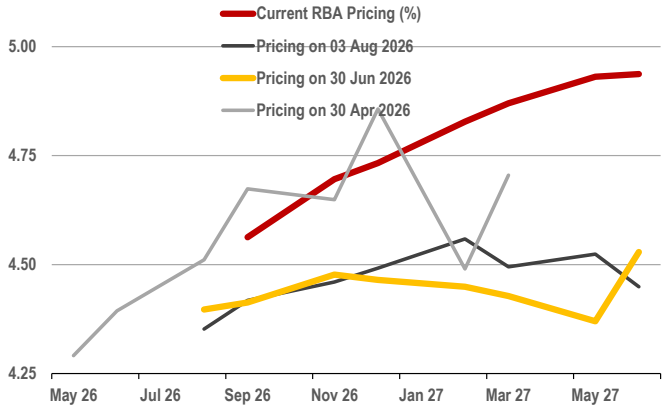


Exhibit 15: FX vs. oil price moves in 2026

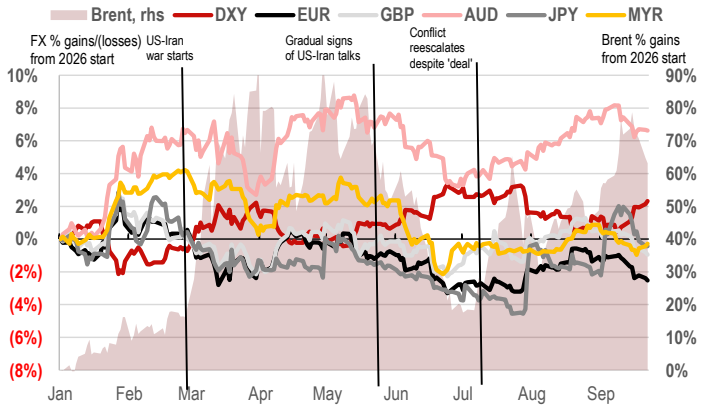
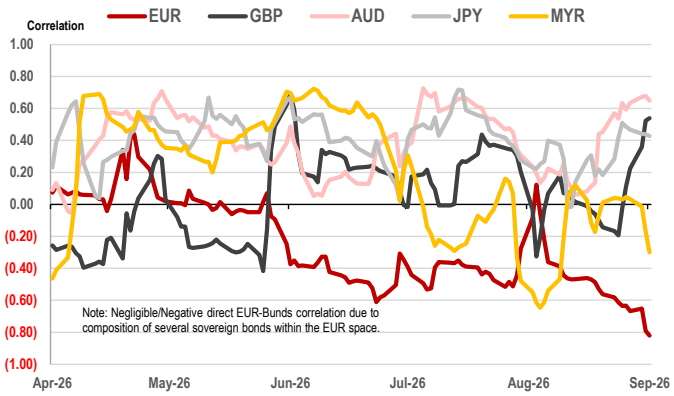


Exhibit 16: Correlation (10-day moving average) of FX vs. yield differentials



Sources: AmBank Economics, Bloomberg

Exhibit 17: The JPY remains sharply undervalued relative to positioning, while also suggesting significant downside for the JPY if bearish positionings are reinstated

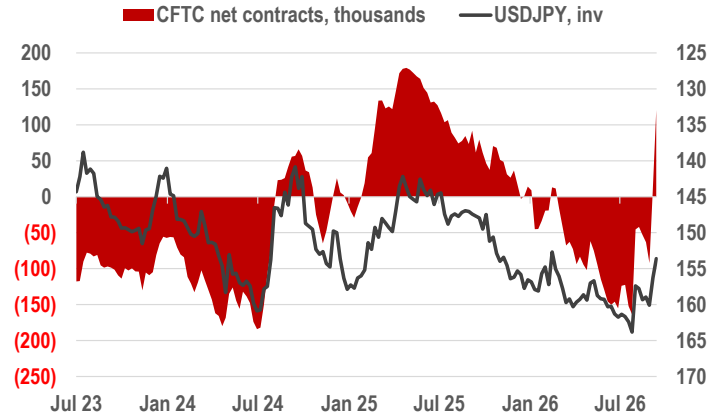
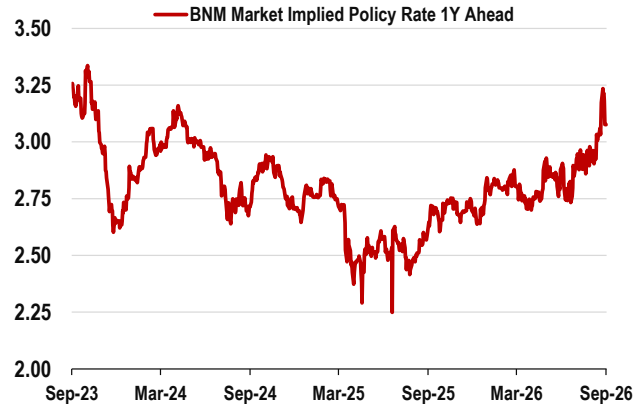


Exhibit 18: Swap markets are pricing in an OPR hike ahead after BNM's September MPC meeting



Sources: AmBank Economics, Bloomberg

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