

A more stable dollar

The US economy has held up better than expected though employment growth has slowed and unemployment has edged up, prompting the Fed to lower interest rates over the final months of last year. We expect it to cut by a further 50bps in 2026, in line with current market pricing. We also see the Bank of England lowering rates by another 50bps this year as inflation continues to head lower, while we expect the ECB to remain on hold through 2026. The dollar has been fairly stable recently, notwithstanding some further narrowing of relative US interest rate differentials. We are lowering our forecast range for EURUSD to \$1.14 to \$1.21, though we see significant risks to this relating largely to US monetary policy. We continue to expect EURGBP to trade in a range of £0.84 to £0.89.

Central Bank Rates (%)	Current	End-Q1'26	End-Q2'26	End-Q3'26	End-Q4'26
Fed	3.50-3.75	3.50-3.75	3.25-3.50	3.00-3.25	3.00-3.25
ECB	2.00	2.00	2.00	2.00	2.00
BoE	3.75	3.75	3.50	3.25	3.25

Exchange Rates	Current	Q1'26	Q2'26	Q3'26	Q4'26
€/\$	1.16	1.14-1.19	1.15-1.20	1.16-1.21	1.15-1.20
€/£	0.865	0.84-0.89	0.84-0.89	0.84-0.89	0.84-0.89
£/\$	1.34	1.32-1.37	1.32-1.37	1.33-1.38	1.33-1.38

Resilient global growth

The global economy has withstood the shock triggered by Trump's tariffs fairly well with the IMF expecting another year of solid if unspectacular growth (3.3%) in 2026. The US economy has also held up better than expected helped by a surge in AI-related investment, though employment growth has slowed and unemployment has edged higher. AI spending will again support growth in 2026, as will looser fiscal policy. Labour market conditions are expected to stabilise, while inflation is likely to moderate as the pass-through of tariffs to prices runs its course. The Euro area and UK economies look set to grow by a bit more than 1% this year, much the same as in 2025. Euro area inflation should remain close to 2%, while UK inflation is likely to fall back further given increased labour market slack.

Fed, BoE to lower rates further, ECB on hold

The Fed resumed lowering interest over the final months of 2025, in response to increasing downside risks to employment, and indicated some further policy easing is likely as inflation moves lower. We expect a further 50bps reduction this year, with the next cut coming in Q2, broadly in line with current market pricing. We also see the Bank of England MPC lowering rates by another 50bps as disinflation continues, while we expect the ECB to remain on hold through 2026.

Narrowing US-Euro area yield differentials

US and Euro area government bond markets diverged markedly in 2025. While US 2- and 10-year yields fell by around 80bps and 40bps over the year, equivalent German yields (the benchmark for the Euro area) were unchanged and 50bps higher respectively. UK bonds treaded something of a middle path with 2-year yields falling by 70bps and 10-year yields broadly flat, though the latter have been trending down since Rachel Reeves' budget in November. Looking to this year, short-dated yields should remain anchored as central banks hold or cut rates a little further, while yields out the curve might come under some modest upward pressure amid generally looser fiscal policy.

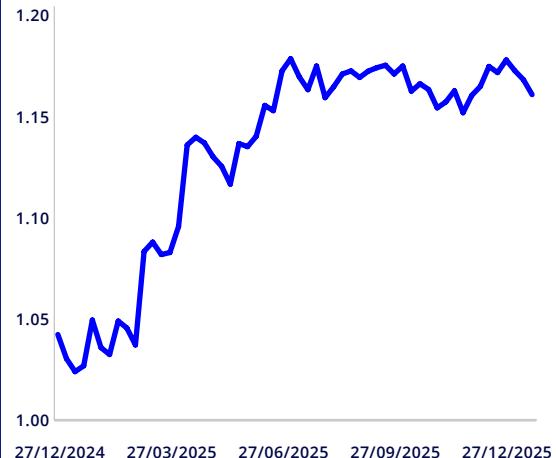
EURUSD forecast lowered

Falling US yields relative to German yields helps explain much of the dollar's decline against the euro in 2025. However EURUSD has been steady in recent months, notwithstanding Fed rate cuts and some further narrowing of yield differentials, suggesting the very negative sentiment towards the dollar evident in the middle part of last year has abated. With the Fed in rate cutting mode and the ECB on hold, there's still upside potential for EURUSD from current levels. However we are doubtful it will break decisively into the \$1.20-\$1.25 range we had expected, hence we see the pair trading mostly between \$1.15 to \$1.20 in 2026. There are significant risks around this though. Greater than expected Fed easing due to weakening labour market conditions, or in response to pressure on the new Fed Chair to lower interest rates, would increase the chances of more substantial gains for the euro, while a reassessment of the prospects for any further Fed rate cuts due to reaccelerating employment growth/declining unemployment would provide a substantial boost to the dollar. Other risks include escalating US-EU trade tensions, following Trump's latest Greenland-related tariff threat, and a US-led fall in asset prices, both of which we think would be dollar-negative.

Range of £0.84 to £0.89 for EURGBP

Sterling has recovered from its circa 2.5 year low of over £0.8850 against the euro since the UK budget in late November, with the increased 'headroom' the Chancellor has given herself to meet her fiscal rules seemingly reassuring investors. Concerns about fiscal policy are unlikely to disappear however, while further BoE rate cuts will also weigh on the pound. Hence we are leaving our forecast range for EURGBP at £0.84 to £0.89.

Euro-Dollar Exchange Rate



Source: Bloomberg

Economy

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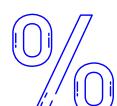
Steady global growth



Central Banks

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Fed to ease a little further



Markets

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Equity markets chalk up solid gains



Forecasts

GDP

GDP Growth*	2025(e)	2026(f)	2027(f)
Global	3.3%	3.3%	3.2%
US	2.1%	2.4%	2.0%
Euro area	1.4%	1.3%	1.4%
UK	1.4%	1.3%	1.5%

*Annual % change, constant prices

Source: IMF (January 2026)

Interest Rates

Central Bank Rates (%)	Current	End-Q1'26	End-Q2'26	End-Q3'26	End-Q4'26
Fed	3.50-3.75	3.50-3.75	3.25-3.50	3.00-3.25	3.00-3.25
ECB	2.00	2.00	2.00	2.00	2.00
BoE	3.75	3.75	3.50	3.25	3.25

Source: Bloomberg, Bank of Ireland Forecasts

Exchange Rates

Exchange Rates	Current	Q1'26	Q2'26	Q3'26	Q4'26
€/\$	1.16	1.14-1.19	1.15-1.20	1.16-1.21	1.15-1.20
€/£	0.867	0.84-0.89	0.84-0.89	0.84-0.89	0.84-0.89
£/\$	1.34	1.32-1.37	1.32-1.37	1.33-1.38	1.33-1.38

**Current Rate as of 19 January 2025

Source: Bloomberg, Bank of Ireland forecasts

Upcoming Events

January

EA CPI Dec (final)	UK CPI Dec	Fed Meeting
19 th	21 st	27 th -28 th
20 th	22 nd	30 th
UK Labour Market Sep-Nov	US PCE Inflation Nov & GDP Q3 (3rd est)	EA GDP Q4 (1st est) and Unemployment Dec
ECB and BoE Meetings	US CPI Jan	EA GDP Q4 (2nd est) & Employment Q4

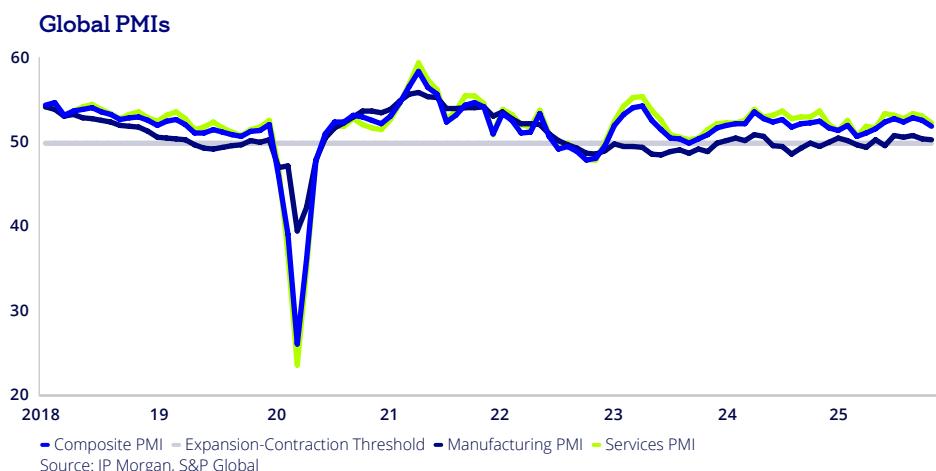
February

EA CPI Jan (flash)	US Payrolls Jan	UK GDP Dec and Q4	UK Labour Market Q4	US GDP Q4 (1st est) & PCE Inflation Dec
4 th	6 th	12 th	17 th	20 th

Economy

Steady global growth

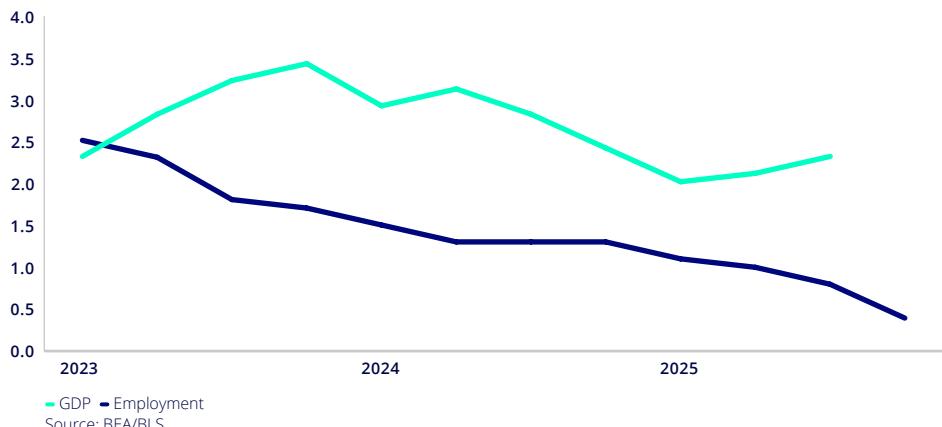
The global economy has withstood the shock triggered by Trump's tariffs fairly well. According to its latest (January) update, the IMF expects world GDP to have increased by 3.3% in 2025, broadly in line with its forecast at the end of 2024. While some of this resilience reflects the front-running of tariffs that boosted growth in the opening months of last year, the AI investment boom has supported global industrial production and trade, helping to counter the negative effects of higher tariffs. The IMF is forecasting growth of 3.3% again in 2026, and 3.2% in 2027 - both revised up slightly from its October projections - driven by continued investment in AI and supportive fiscal and monetary policy. It believes the risks to the outlook are 'tilted to the downside' however. A re-evaluation of productivity growth expectations about AI could lead to a decline in investment and trigger an abrupt correction in equity markets, eroding household wealth and spending; high public debt could raise long-term interest rates and, in turn, result in a broader tightening of financial conditions; while trade tensions 'could flare up, prolonging uncertainty and weighing more heavily on (economic) activity.'



US economy holds up better than expected

The US economy held up better than expected in 2025 notwithstanding the new administration's protectionist trade policy. GDP growth looks on course to average just over 2% for the year, down from 2.8% in 2024 but ahead of projections following Liberation Day in early April. A surge in AI-related capital expenditure made a significant positive contribution to growth, particularly over the first half of the year, offsetting weakness in other areas of investment (notably residential and non-residential construction), while consumer spending, albeit moderating gradually, has been supported by positive wealth effects associated with rising equity markets. Jobs growth slowed over the course of the year, exacerbated by a policy-driven decline in federal government employment. The unemployment rate has nudged up as a result, notwithstanding slower labour supply growth, but remains relatively low at 4.4%. The pass-through of higher tariffs to Inflation has been modest to date - core PCE inflation stood at 2.8% in September, up marginally from a 2025 low of 2.6% in April - with an increase in goods price inflation partially offset by a slight fall in services inflation.

US GDP and Employment Growth (% y/y)



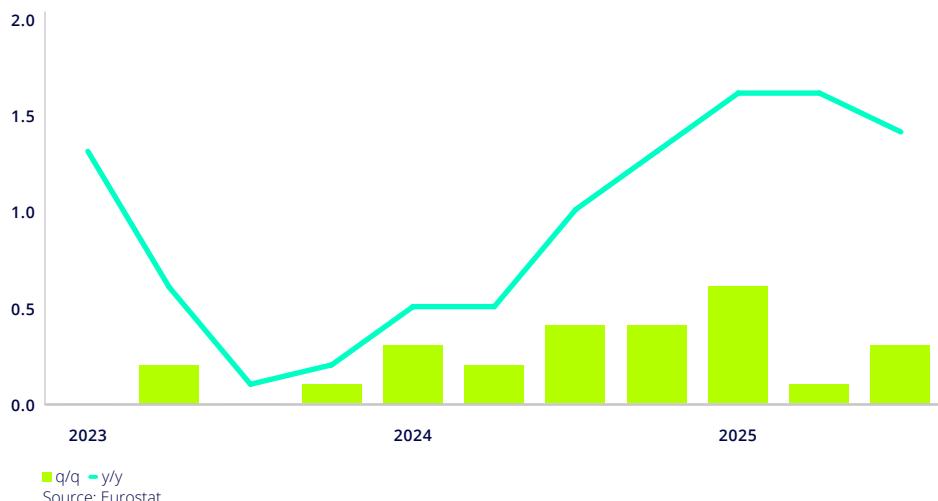
Economy

Looking at the prospects for the economy for the year ahead, AI-related investment is set to continue, albeit perhaps not at the rapid pace of last year, while consumer spending is likely to moderate further given softer employment / wage gains and some increase in the household saving ratio from its current low level. Fiscal policy will provide a modest boost to growth, with easier financial conditions also supporting activity. All told, GDP growth is expected to run close to 2% again in 2026, with the unemployment rate stabilising and inflation – while perhaps increasing further in the near-term - falling back over the course of the year.

Euro area economy proving relatively resilient

The Euro area economy proved reasonably resilient in 2025 despite the imposition of tariffs on goods exports to the US. While growth has eased from its well above-average pace in the first quarter of last year - when it was boosted by a jump in exports ahead of anticipated tariffs - it has come in ahead of expectations albeit still remaining relatively modest. Domestic demand has been the main driver of growth recently, offsetting a drag from net exports. Employment has continued to expand, helping to keep unemployment steady in a range of 6.3% to 6.4% over the past year. Headline inflation has been running broadly in line with the ECB's 2% target since early 2025. Core inflation has been relatively stable over the same period, albeit running slightly higher at just under 2.5%.

Euro area GDP Growth (%)



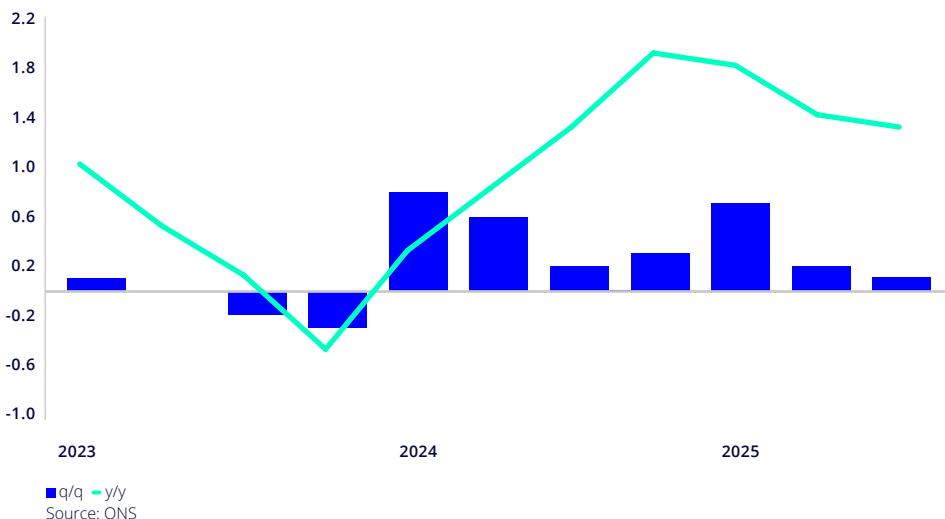
Generally, forecasts for GDP growth have been revised up recently. The economy is seen expanding by a bit more than 1% in both 2026 and 2027, much the same as in 2025 and broadly in line with economy's average (annual) rate of growth post the financial crisis. While higher tariffs and the recent appreciation of the euro are likely to weigh on exports, reduced uncertainty, positive real income growth, and easier financing conditions should support consumer spending and investment. Increased government spending on defence and infrastructure, notably in Germany, should also help to underpin growth. Given the outlook for growth, unemployment is expected to remain stable at its historically low level. With the economy and labour market both broadly in balance, and absent any unforeseen shock(s), inflation should continue to run close to 2%.

Economy

Hard grind for UK economy

Following a strong first quarter in 2025, GDP growth slowed to 0.2% and 0.1% q-o-q in Q2 and Q3 respectively, while another weak outturn seems likely in Q4. A range of factors weighed on the economy over much of last year, including heightened uncertainty related to trade and (domestic) fiscal policy, increased payrolls costs, which contributed to weaker labour demand, and a reacceleration in inflation, which weighed on household incomes. Unemployment has increased to a near 5-year high of just over 5%, while inflation accelerated to 3.8% in September from 2.5% at the end of 2024 before easing back to 3.2% in November.

UK GDP Growth (%)



Surveys published in December point to some modest improvement in consumer and business confidence post the November budget, which if sustained should support consumer spending and investment this year. The measures announced in the budget are expected to impart a modest boost to GDP growth over the next couple of years, both directly, via, increased government spending, and indirectly, via lower inflation (as a result of inter alia measures to reduce domestic energy bills) which will boost household real incomes and spending. Overall, GDP growth is expected to average a bit more than 1% a year in 2026-2027, with unemployment peaking at just over 5% and inflation declining towards the 2% target over the course of this year and into 2027.

Central Banks

Fed to ease a little further

The Fed has lowered interest rates by 75bps (to a range of 3.5%-3.75%) since resuming its cutting cycle in September in response to softening labour market conditions. This brings the cumulative reduction since September 2024 to 175bps and leaves the policy rate sitting just above the top of the Fed's estimate of the range (2.8%-3.5%) for the neutral interest rate. Following its third consecutive 25bps cut in December, the Fed said "this further normalization of our policy stance should help stabilize the labour market while allowing inflation to resume its downward trend toward 2% once the effects of tariffs have passed through". It also signalled some further reduction in rates is likely but indicated it may pause before easing policy again. Reflecting this, the market expects another 50bps worth of cuts in 2026 but is not pricing in the next quarter-point reduction until June/July. This seems a reasonable base case to us, though we think the risks surrounding it are considerable. A reacceleration in employment growth and/or a renewed fall in the unemployment rate, particularly if accompanied by stickier than expected inflation, would keep the Fed on hold for longer than expected. On the other hand, a further rise in the unemployment rate, particularly if driven by declining employment, would prompt the Fed to lower rates more quickly and by more than currently expected.

Central Banks

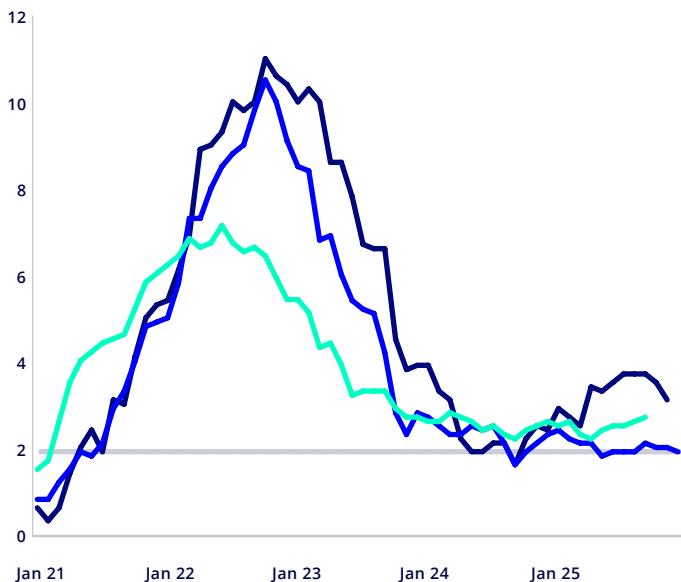
ECB to remain on hold

The ECB has left the deposit rate unchanged at 2% since its last 25bps cut in June 2025 - which brought the cumulative reduction since June 2024 to 200bps - including at its meeting in December. With inflation forecast to remain close to the 2% target over the next couple of years according to its latest projections, the ECB says monetary policy is in 'a good place', signalling it expects to keep the deposit rate on hold for a further extended period (although it continues to insist that all options regarding monetary policy remain 'on the table'). While it cites a number of upside and downside risks to its updated forecasts for growth and inflation, both of which were upgraded slightly for 2026, we think it would take a significant deviation from the current economic outlook to warrant a change in its monetary policy stance in either direction. Hence we expect the ECB to remain on hold through the end of 2026, in line with current market pricing, but think, on balance, that some firming of market expectations for rate hikes in 2027 is likely as we move through the course of this year.

Bank of England to cut some more

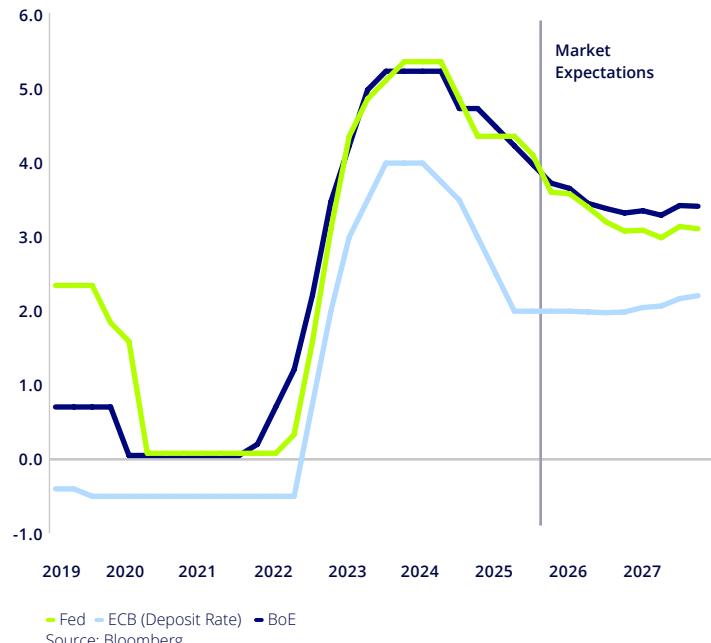
A larger than expected fall in inflation in October-November, alongside a further moderation in private-sector wage growth, saw the Bank of England Monetary Committee (MPC) cut interest rates by another 25bps to 3.75% at its December meeting (a bit earlier than it had anticipated when it previously lowered rates in August). The vote to do so was very tight though, with four of the nine MPC members preferring to stay on hold at 4%. Moreover, while the accompanying statement noted that interest rates are "likely to continue on a gradual downward path", it said "judgements around further policy easing will become a closer call". This is partly because, as the statement also noted, the restrictiveness of monetary policy has been reduced significantly as rates have been steadily lowered (by 150 basis points since August 2024) and are in the vicinity of the range for the neutral interest rate. With disinflation likely to continue in 2026, we continue to expect the policy rate to be cut by a further 50bps to 3.25%, with the next quarter-point reduction likely in April.

Annual Consumer Price Inflation (%)



— US (PCE) — EA (CPI) — UK (CPI) — Target
Source: BEA, Eurostat, ONS

Central Bank Policy Rates (%), End-Quarter



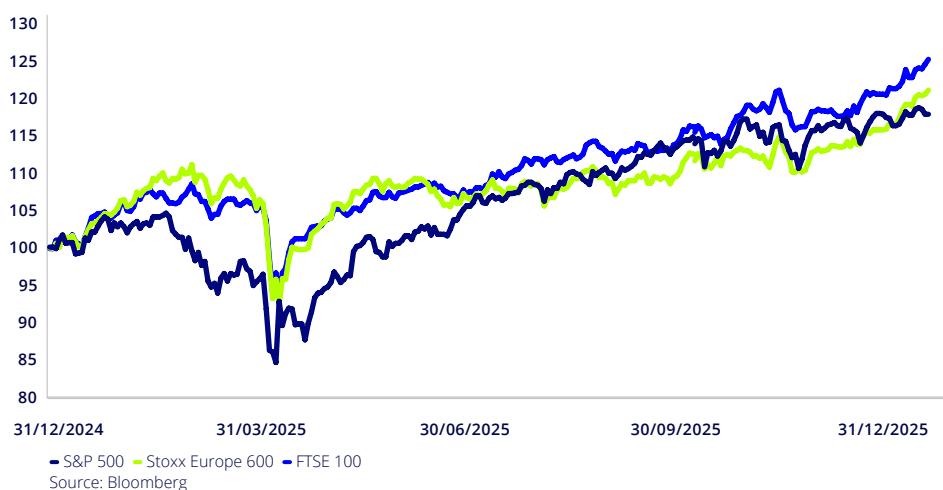
— Fed — ECB (Deposit Rate) — BoE
Source: Bloomberg

Markets

Equity markets chalk up solid gains

Equity markets recovered strongly from their post-Liberation Day slump in April to chalk up strong gains in 2025. AI-related optimism fuelled another year of double-digit gains for the S&P 500 (+16%) in the US, though its performance was far from exceptional relative to other markets, with the Stoxx Europe 600 gaining almost 17% and the German Dax, FTSE 100 in the UK and the Nikkei index in Japan all advancing by more than 20%. Emerging market equities also performed strongly last year, helped by a weaker US dollar. The outlook for equity markets generally in 2026 seems fairly benign against an expected backdrop of ongoing albeit modest global economic growth, declining inflation, low/falling interest rates in the major economies (Japan will be an exception) and strong corporate earnings growth, though concerns about stretched US valuations are likely to remain prominent again this year, while of course geopolitical uncertainties pose an ongoing risk to markets.

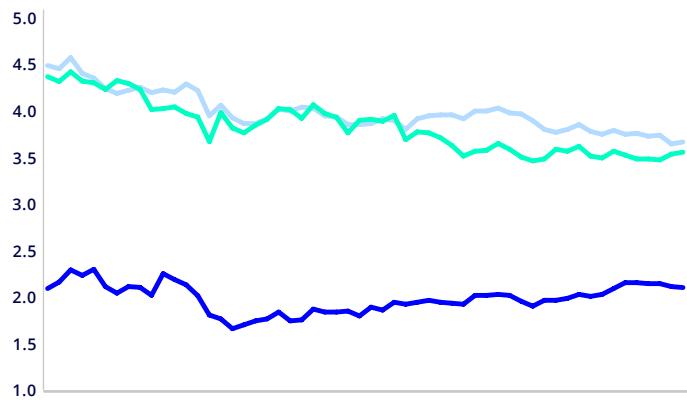
Equity Indices (End-2024=100)



Mixed bond market performance

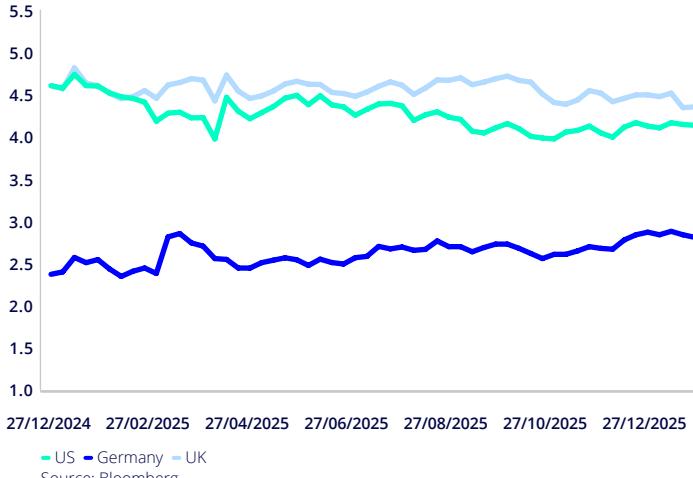
While curve steepening was a feature of both the US and Euro area government bond markets in 2025, yields in the two diverged considerably. In the US, 2-and 10-year yields fell by around 80bps and 40bps respectively (30-year yields were largely flat), hitting their lows for the year late in 2025 as the Fed resumed cutting interest rates. In contrast, German yields (the benchmark for Euro area yields) were largely unchanged on the year in the 2-year area, while 10-and 30-year yields rose by circa 50bps and 90bps respectively, reaching their highs for 2025 late in the year as it became clearer that the ECB's rate cutting cycle had (most likely) come to an end. The UK treaded something of a middle path between the US and Germany. 2-year yields fell by almost 70bps as the BoE cut interest rates but 10-year and 30-year yields were largely unchanged as fiscal policy concerns weighed on the long-end of the curve. The latter have been trending down since the UK budget in November though, with the increased 'headroom' the Chancellor has given herself to meet her fiscal rules seemingly reassuring investors. Looking to this year, yields at the short-end of curves should remain anchored as the main central banks hold (ECB) or cut interest rates a little further (Fed and BoE), while yields further out the curve might come under some modest upward pressure given generally looser fiscal policy in the main economies.

Government 2-Year Bond Yields (%)



Source: Bloomberg

Government 10-Year Bond Yields (%)



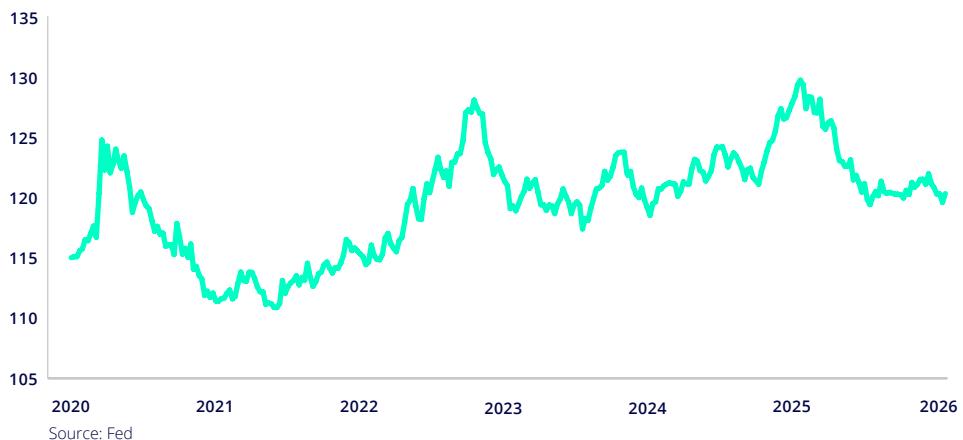
Source: Bloomberg

Markets

Limited upside now seen for EURUSD

The dollar fell quite sharply in 2025, shedding almost 6% on a trade-weighted basis over the course of the year, its largest decline since 2017. This included falls of 13% and 8% (or 14 cents and 10 cents) against the euro and sterling respectively, although it largely held its own against the Japanese yen.

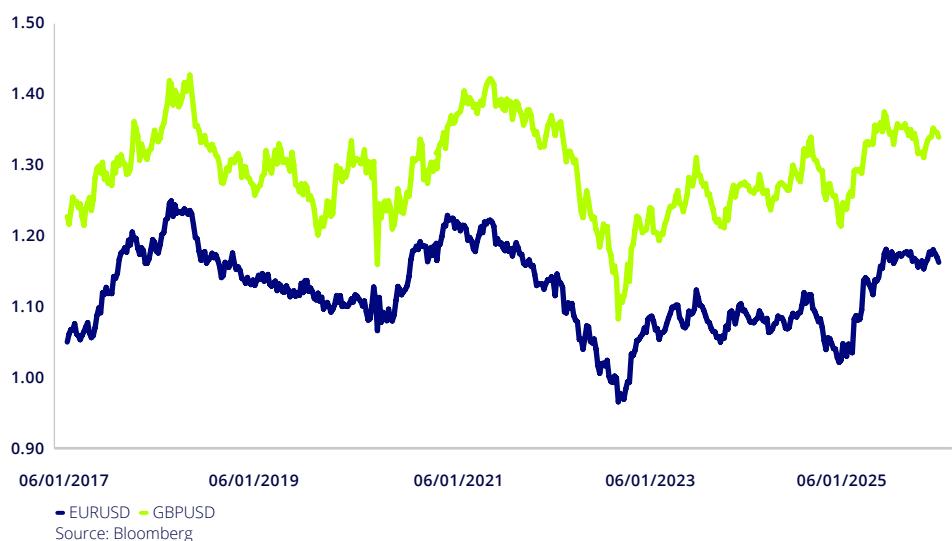
Dollar Trade-Weighted Exchange Rate



The sizeable fall in US bond yields relative to German yields helps to explain much, but not all, of the dollar's decline against the euro in 2025, with negative investor sentiment triggered by Trump's trade policy also weighing on the currency. EURUSD has been relatively steady in recent months, trading within the \$1.15 to \$1.20 range we had expected when we published our September Global Watch. However it has never seriously tested the top of this range notwithstanding the resumption of Fed rate cuts and some further narrowing of US-German yields differentials - which we thought would propel it above \$1.20 heading into 2026 - suggesting much of the negative sentiment towards the currency has largely abated. That said, with the Fed still in rate cutting mode and the ECB on hold, we believe there is still some upside potential for EURUSD from current levels. However we are now doubtful it can break decisively into the \$1.20-\$1.25 range we had expected in September, hence we are lowering our forecast range to \$1.14 to \$1.21 for 2026.

There are significant risks surrounding this forecast however. A greater than expected easing of Fed policy would increase the chances of more substantial gains for the euro, all the more so if some of the easing was because of political pressure on the new Fed Chair (due to be in situ in May) to lower rates. Against that, a reassessment of the prospects for any further Fed rate cuts could provide a significant boost to the dollar. Other risks include an escalation of US-EU trade tensions, following Trump's latest Greenland-related tariff threat, and a US-led decline in asset prices, due to over-optimism in relation to AI investment or heightened concerns about US deficit and debt levels, both of which we think would be dollar-negative.

Euro and Sterling versus Dollar

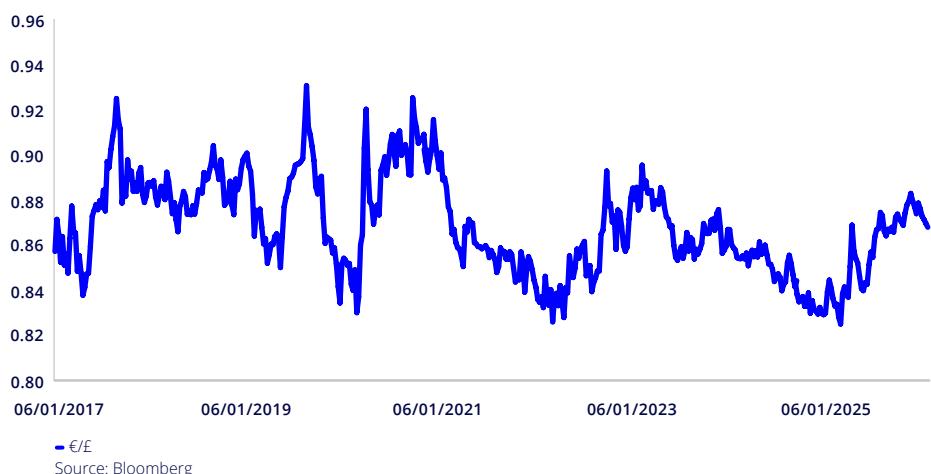


Markets

GBP to remain rangebound versus euro

Sterling has come under pressure at various times over the past year, often related to concerns over UK fiscal policy, most recently falling to a circa two and a half year low north of £0.8850 against the euro, and a seven month low of \$1.30 against the dollar, ahead of Rachel Reeves' budget in late November. The latter though seems to have reassured investors - mainly due to the increased 'headroom' the Chancellor has given herself to meet her fiscal rules - with the pound outperforming in recent weeks, rebounding to under £0.87 and \$1.34 respectively. Concerns about domestic fiscal policy are unlikely to disappear completely however (the budget is predicated on relatively optimistic forecasts for UK GDP growth), while further BoE rate cuts will also weigh on the pound, even as greater UK alignment with the EU in some areas potentially pulls in the opposite direction. All told, we are leaving our forecast range for sterling versus the euro unchanged at £0.84 to £0.89 - which is a subset of the broader range of circa £0.82 to £0.92 that has prevailed since 2017 - and are pulling down our forecast for GBPUSD to \$1.32 to \$1.38 (from \$1.35-\$1.40 previously) reflecting our less negative view on the dollar generally.

Euro-Sterling Exchange Rate



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