Market outlook | Q3 '26

Higher for longer

Markets adjust to a new rate reality

The oil shock fades

As tensions ease, markets reset

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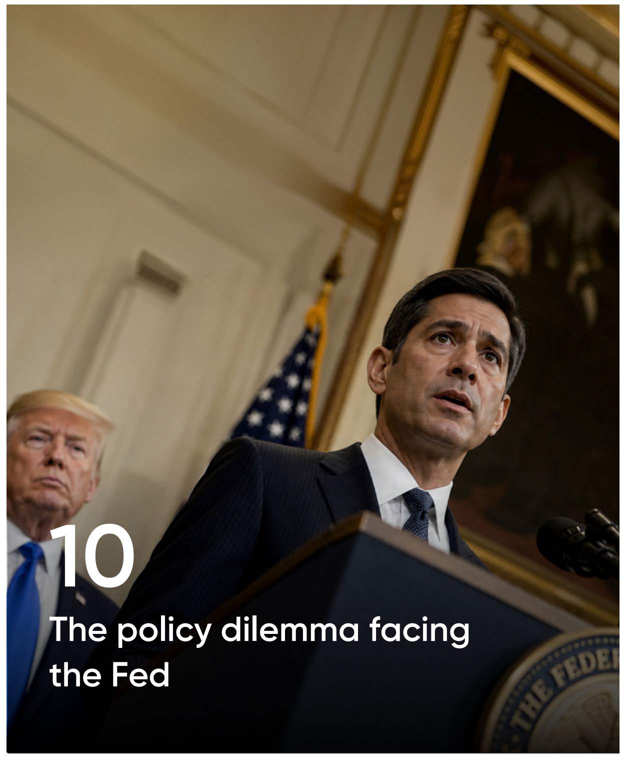
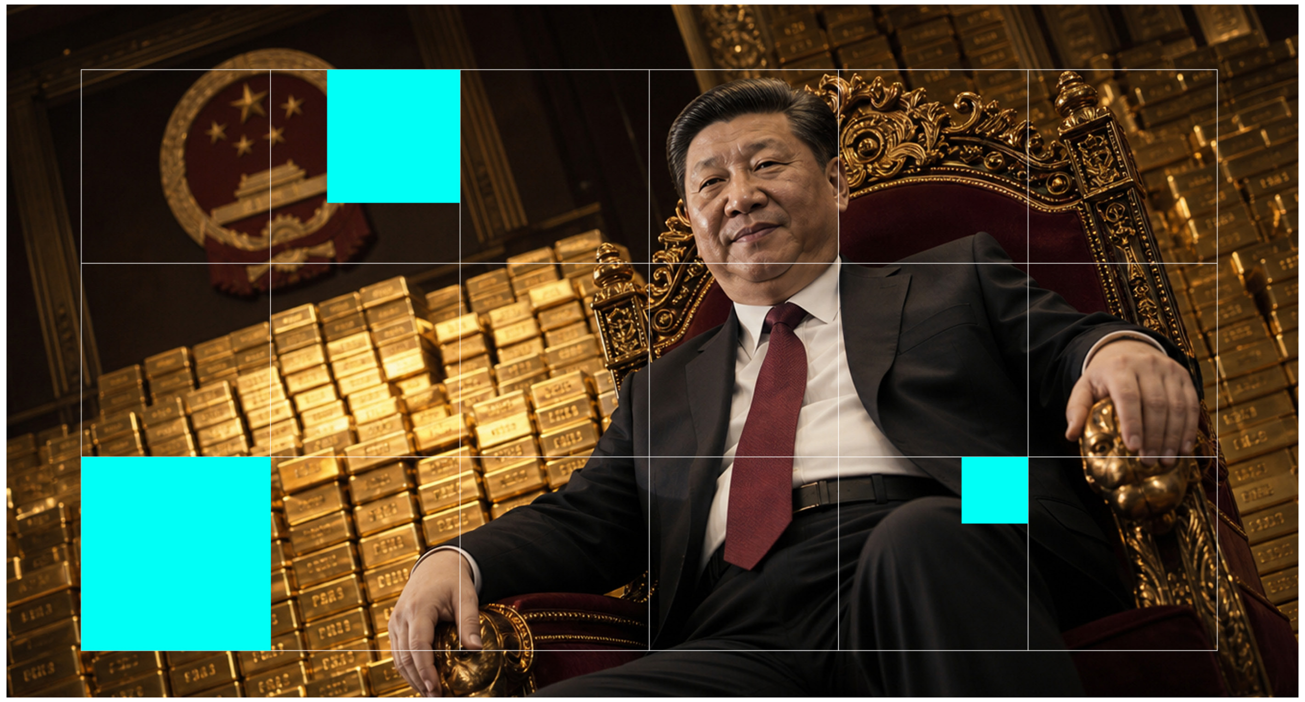




Gold after the correction: Recovery or downside?

Gold enters the third quarter at an important turning point. After reaching record highs earlier this year, the precious metal has undergone one of its sharpest corrections in recent history as shifting interest-rate expectations reshaped investor sentiment. Central Bank demand continues to provide long-term support, markets will be watching closely to see whether easing monetary policy expectations and technical price action can sustain the recent recovery.

From record highs to a sharp correction

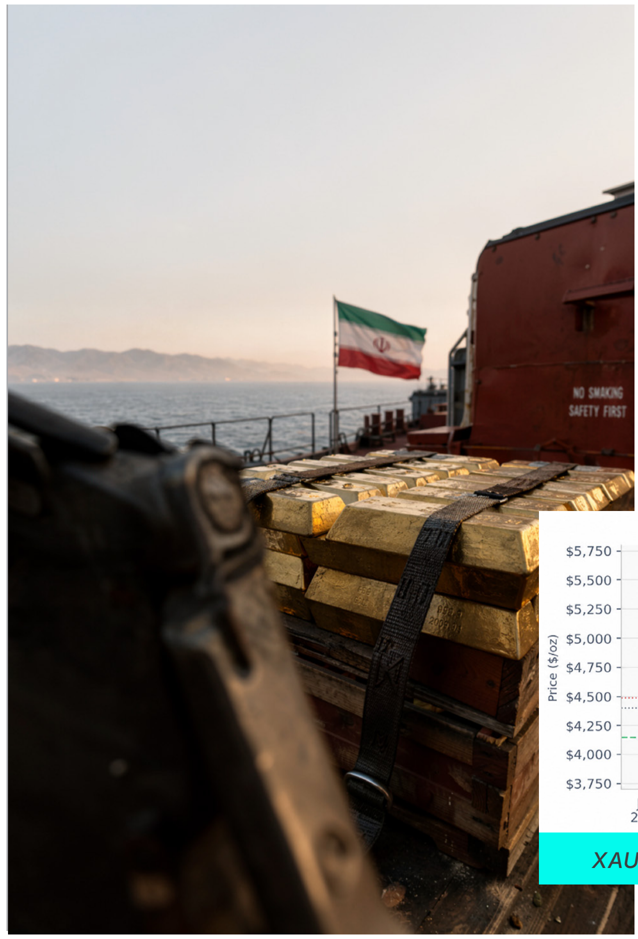
Gold entered 2026 with exceptional momentum. The metal had risen by roughly 45% over the previous 12 months, driven by a powerful mix of elevated structural demand from central banks, the repositioning of major global financial institutions in the Western Hemisphere away from dollar-denominated assets, and a geopolitical risk premium that surged after the United States and Israel launched military operations against Iran in late February. On 28 January 2026, XAU/USD touched an intraday record of $5,589 an ounce, a level that, in hindsight, appears to have marked the peak of market sentiment rather than the start of a sustained breakout.

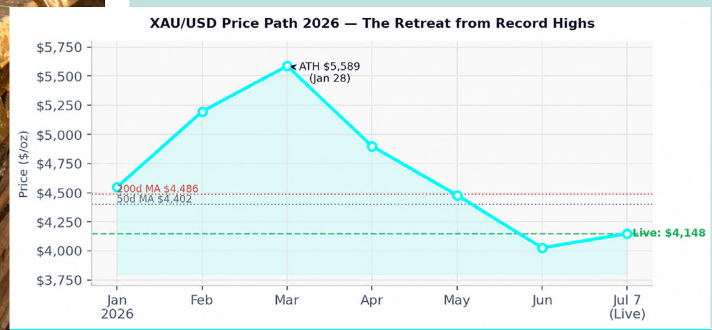
What followed; one of the sharpest corrections gold has seen in modern history. By June, metal fell below $4,000, a decline of more than $1,500 from peak to trough in five months.

Changing rate expectations drove the sell-off

The reversal was not caused by a collapse in structural demand. Central banks, which the World Gold Council estimates bought 244 tonnes in the first quarter of 2026 alone, continued to accumulate gold throughout the sell-off.

The real driver was the repricing of the expected monetary policy path. The same conflict that initially lifted gold and oil triggered an inflation shock that forced markets to reassess the Federal Reserve's policy trajectory under its new chair, Kevin Warsh. Energy price spikes from Strait of Hormuz disruptions fed directly into US CPI, complicating the Fed's data-dependent path. Market pricing quickly shifted from 50 basis points of cuts to a 25-basis-point hike, a 75-basis-point swing in policy expectations. This shift hit gold. As real yields spiked and the dollar strengthened, ETF investors who bought into gold's 2025 rally began trimming exposure to manage the rising opportunity cost of holding the non-yielding asset.





XAU/USD's path in 2026: the retreat from record highs.

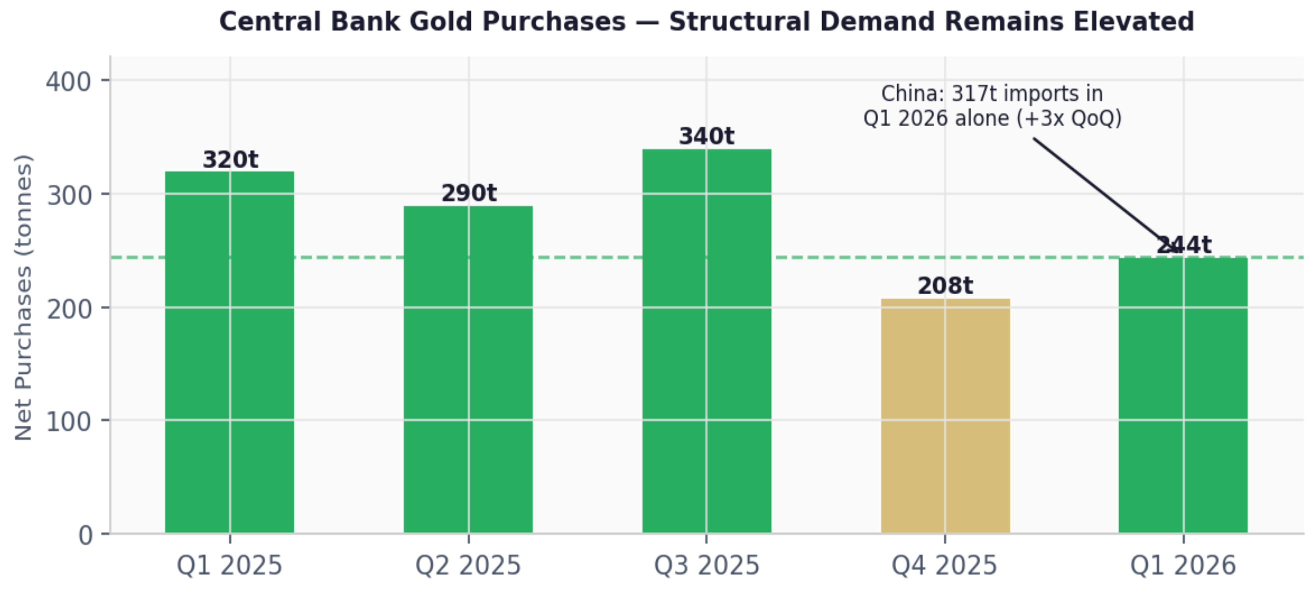
Can gold's recovery continue?

The turning point came on 2 July, when the US jobs report for June showed that the economy added only 57,000 jobs, roughly half the 110,000 expected, while the previous two months were revised lower by a combined 74,000. The weaker-than-expected data reduced the case for further monetary tightening. The probability of a September rate hike, according to the CME FedWatch Tool, fell from 66% to around 50% within hours.

Gold responded immediately, rising more than 2% during the 3 July session, its strongest daily performance since mid-June, before extending its recovery to around $4,148 by 7 July.

The key question for the third quarter is whether this rebound marks a genuine trend reversal or merely a countertrend move within a broader corrective structure.

From a technical perspective, caution is still warranted. XAU/USD is currently trading below both its 50-day moving average at $4,402 and its 200-day moving average at $4,486, a configuration that remains technically bearish regardless of momentum in any single session. The 20-day moving average, near $4,156, acted as resistance throughout June's decline and is now the first short-term support level. A weekly close above the 50-day moving average would provide the first credible sign that selling pressure is easing. Until then, the broader structure remains an unproven rebound.



Central-bank gold purchases, in tonnes.

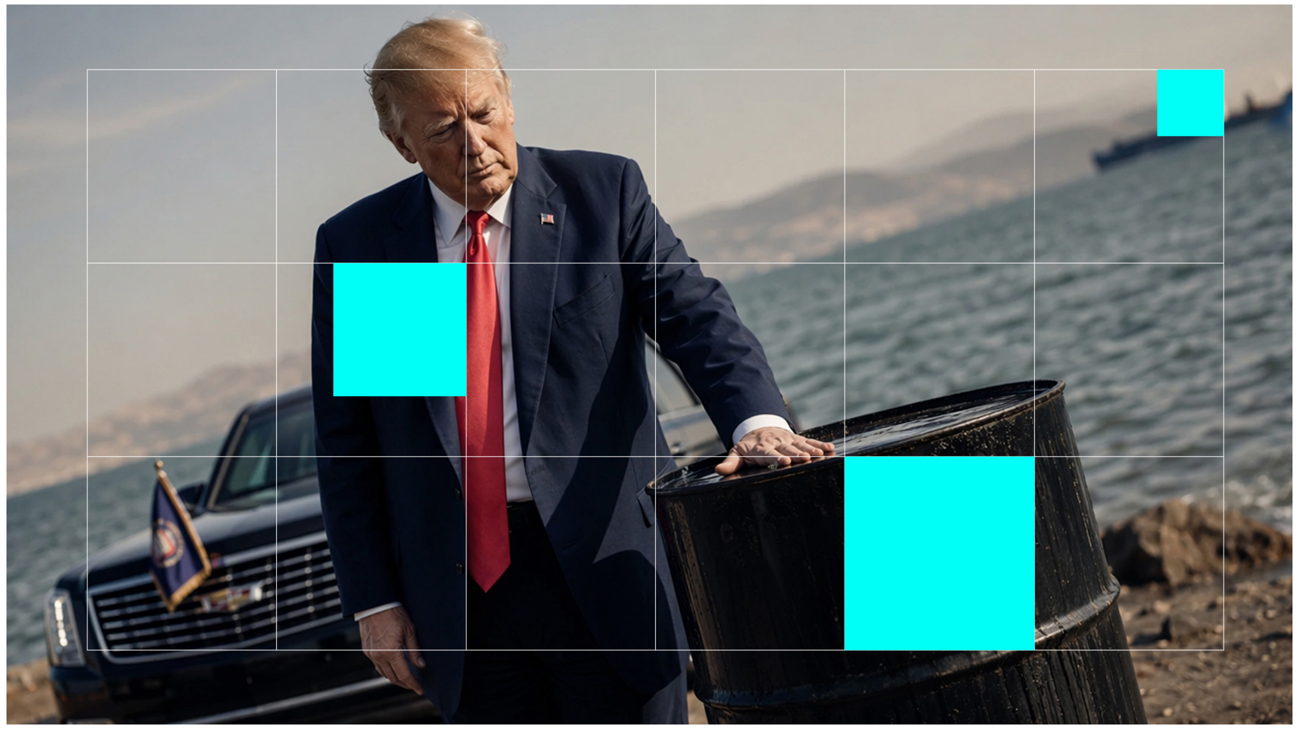
Central banks and market expectations remain key drivers of gold

Beyond technical factors, central-bank behaviour remains one of the strongest structural drivers of gold prices. Reported net purchases totalled 244 tonnes in the first quarter of 2026, while flows through the over-the-counter market and unreported purchases are estimated to have been significantly higher. The World Gold Council's 2026 survey also found that 89% of central-bank reserve managers expect global gold reserves to increase over the next 12 months, a record figure. China also continued reducing its reliance on dollar assets for strategic reasons, importing 317 tonnes in the first quarter of 2026, nearly three times the level recorded in the fourth quarter of 2025. The freezing of Russia's central-bank assets in 2022 also reshaped how many emerging-market central banks approach reserve management.

Institutional forecasts for the third quarter remain broadly constructive, despite considerable uncertainty. Price targets range from $4,300, the base-case forecast from Deutsche Bank and ING, to $6,300 in JPMorgan's bullish scenario, with Goldman Sachs targeting $5,400 by year-end and Morgan Stanley forecasting $5,200. TD Securities believes a move below $3,900 is unlikely unless an early rate hike becomes a realistic possibility, identifying $4,280 as the nearest likely resistance level. Overall, the wide range of forecasts reflects uncertainty over the path of Federal Reserve policy rather than disagreement over gold's long-term structural outlook.

For traders, the third-quarter framework remains finely balanced. Downside risk continues to be supported by central-bank buying, which has historically provided a floor around the $3,900-$4,000 area, while renewed geopolitical tensions involving Iran or the Strait of Hormuz could quickly revive safe-haven demand. The upside case, however, still requires confirmation. Either the Federal Reserve needs to signal a clear pause, allowing real yields to fall and ETF investors to return, or a fresh geopolitical shock needs to reignite the risk premium. In the absence of either catalyst, the World Gold Council's expectation of a volatile, range-bound market remains the most likely scenario.

Raed AlKhedr
Chief Market Analyst



Oil's rapid reversal after the Strait of Hormuz crisis

Oil enters the third quarter in a very different position. After surging past $120 a barrel on supply disruption fears, prices fell sharply as geopolitical tensions eased and core market fundamentals re-emerged. The focus now shifts to whether recovering supply, inventory levels, and global demand will keep prices under pressure.

A market that has gone full circle

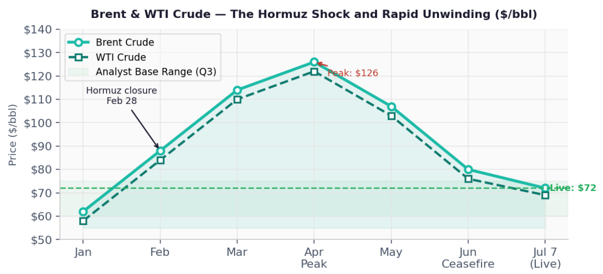
Few markets have seen a bigger turnaround than crude oil in the first half of 2026. Brent opened the year near $62 a barrel, elevated compared with previous yearly openings but still consistent with the structural oversupply that defined 2025, when OPEC+ was managing excess production through voluntary cuts while struggling with weak compliance.

Within six weeks of the United States and Israel launching air operations against Iran on 28 February, Brent had climbed above $100 for the first time since 2022 and peaked above $126 in April. The Strait of Hormuz, the waterway through which roughly 20% of global seaborne crude oil and liquefied petroleum gas trade passes, was closed to most tanker traffic. The largest disruption to global energy supply since the crises of the 1970s had arrived without warning.

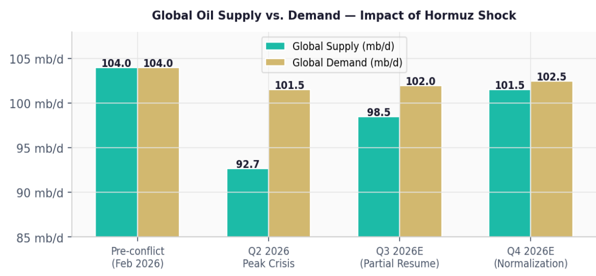
By 7 July 2026, Brent was trading near $72 a barrel, not far from where it started the year. That full reversal, completed in roughly 22 weeks, is one of the clearest examples of how quickly commodity markets can reprice. It also highlights how geopolitical shocks, market mechanics and structural supply forces interact once acute disruption begins to fade. Understanding why oil has now given back its conflict-related risk premium is more useful for assessing the third-quarter outlook than simply knowing where prices peaked.

Why did oil prices fall so quickly?

The drop from $126 to $72 was driven by several factors. The US-Iran ceasefire framework, signed in mid-June, which included a 60-day ceasefire and the reopening of the Strait of Hormuz, removed the catastrophic risk that had kept prices elevated. Even before the ceasefire, demand destruction was accelerating faster than the US Energy Information Administration (EIA) had projected. The agency revised its global oil demand forecast from growth of 1.2 million barrels per day in February to a contraction of 1.1 million barrels per day in June, a swing of 2.3 million barrels per day in just four months.



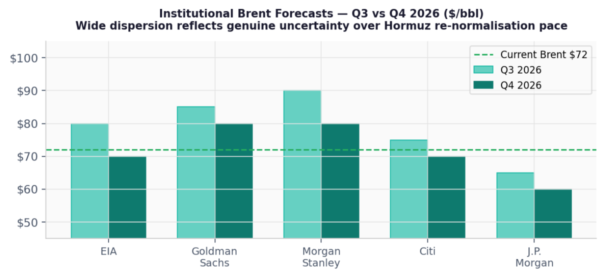
At the same time, Atlantic Basin producers moved quickly to fill the gap left by Middle Eastern exporters. The International Energy Agency (IEA) raised its 2026 supply growth forecast for the Americas by more than 600,000 barrels per day, with the United States reaching record production of 13.6 million barrels per day alongside rising output from Brazil and Canada. The structural oversupply that defined 2025 never disappeared. The conflict merely masked it for a few months.



Supply is returning faster than expected

As of 7 July, the recovery in the Strait of Hormuz is progressing faster than many institutions expected in their June forecasts. At least eight Japanese vessels have exited the strait via a route near Iran, including five very large crude carriers capable of transporting up to 2 million barrels each.

Saudi Aramco's exports are approaching pre-war levels, and the company cut the August price of its Arab Light grade for Asian buyers by $11 a barrel to a discount of $1.50 against the regional benchmark. That pricing structure has not been seen since the oil price wars of 2020 and 2015, signalling that Riyadh is prioritising market share over price defence. OPEC+ has also approved an additional quota increase of 188,000 barrels per day for August, its fourth consecutive monthly increase, bringing cumulative production increases since April to roughly 800,000 barrels per day.



What traders should watch next

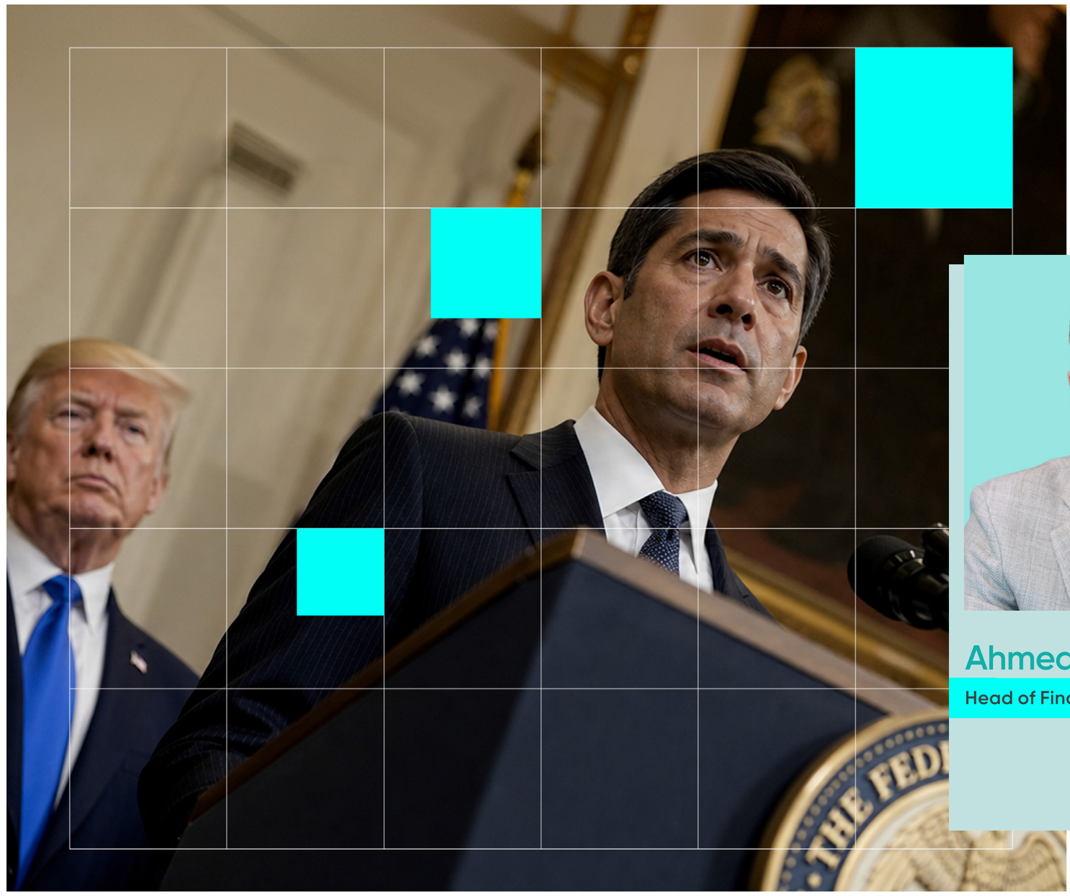
For traders, the third-quarter outlook remains structurally bearish, but with meaningful upside risks tied to geopolitical events. The base case, continued recovery in Hormuz, OPEC+ gradually unwinding its production cuts and a partial recovery from demand destruction, points to Brent trading within a $68 to $80 range during the quarter. The main downside risk is a faster-than-expected inventory rebuild, which could accelerate a move back towards the pre-conflict $60 area.

The clearest upside risk is a breakdown of the US-Iran ceasefire framework. That possibility cannot be dismissed. Formal negotiations have already been frozen once, and Iran was linked to an attack on a vessel in the Gulf of Oman after the memorandum of understanding was signed. Markets have now removed almost all the geopolitical risk premium from oil prices. That also means any credible sign of renewed escalation would likely be priced in quickly. Traders holding short positions should keep that risk firmly built into their position management.

Raed AlKhedr
Chief Market Analyst

Would higher interest rates really bring down US inflation?

The US enters the third quarter facing a familiar but increasingly complex challenge. Inflation remains above target, while economic growth and the labour market have stayed resilient enough to keep the prospect of further interest-rate increases on the table. The key question is whether tighter monetary policy would meaningfully reduce inflation or simply add pressure to an economy already dealing with supply-driven price shocks.



Ahmed Azzam
Head of Financial Market Research

The policy dilemma facing the Fed

Inflation is keeping rate hikes on the table. Growth and the labour market are giving the Federal Reserve just enough room to consider them. That is the policy dilemma shaping the start of the third quarter.

Inflation remains above target, the economy has not collapsed, and the labour market is cooling without breaking. On paper, this gives the Federal Reserve, led by Kevin Warsh, room to argue that policy may need to remain restrictive for longer or even tighten further if inflation proves stubborn. The case for higher interest rates, however, is far less convincing. The real question is not whether the economy can absorb tighter policy, but whether tighter policy would address the kind of inflation the US is facing.

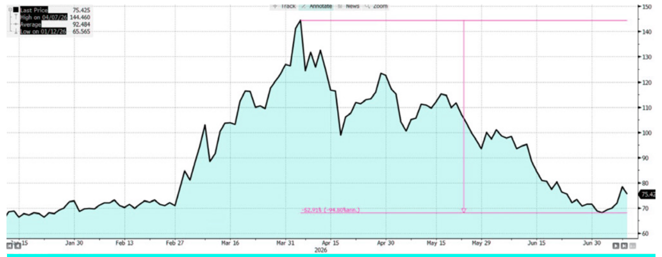
The latest inflation shock still appears to be driven more by supply constraints than overheating demand. Price pressures have been fuelled by energy market volatility, geopolitical risk and higher costs across oil-linked commodities, rather than by a broad acceleration in domestic demand.

That distinction matters. Higher interest rates can cool spending, weaken credit conditions and slow hiring. They cannot produce more crude oil, lower fertiliser prices, ease shipping disruptions or remove geopolitical risk from the Strait of Hormuz. This is why tightening into the current shock carries a different risk. It could do little to address the underlying drivers of inflation while adding pressure to an economy already absorbing higher input costs.

Inflation is still sticky, but the worst may be behind us

Headline inflation appears to have peaked in May, with both CPI and PCE inflation likely to ease in June as the earlier surge in energy prices fades. While renewed geopolitical tensions show the backdrop remains fragile, the inflation outlook does not depend entirely on a lasting ceasefire.

For headline inflation to reach a new high, oil would likely need to return to extreme price levels. That remains outside the baseline scenario unless geopolitical tensions escalate significantly. The energy shock is real, but it does not yet appear large or persistent enough to recreate the inflation spiral that followed the Russia-Ukraine conflict in 2022.



Source: Bloomberg

The broader commodity spillover also appears more contained this time. Prices for jet fuel, fertiliser, plastics, aluminium, polymers, natural gas and other oil-related inputs have already peaked in most cases and are now moving lower. Steel remains the main exception. That suggests the second-round effects of the latest energy shock are fading more quickly than they did in 2022.

This does not make inflation harmless. It makes the policy response more complicated. If the shock is already reversing, additional rate hikes risk responding to yesterday's inflation pressures rather than tomorrow's inflation trend.

The Fed needs to respond to inflation, not just react to it

Energy inflation is never harmless, even when it starts outside the core basket. The Fed learned that lesson earlier in the decade. A shock in oil or gas prices can quickly feed through transport costs, utilities, imported goods and corporate margins. Companies facing higher costs eventually must choose between absorbing the hit or passing it on to consumers.

The difference this time is that the pass-through still appears contained. Core inflation is running below headline inflation at 2.9% versus 4.2%, inflation expectations remain broadly anchored, and the labour market has not generated the kind of wage-price spiral that would force the Fed into a more aggressive tightening cycle. That gives policymakers room to be patient, even if it does not give them room to be dovish.

Source: Bloomberg

The US economy remains resilient, but it is not overheating. Real GDP is expected to grow by around 2.1% in 2026 before easing to an average of about 1.9% in 2027 and 2028. That is neither a boom nor a recession. The labour market tells a similar story, with unemployment at around 4.3%: high enough to show cooling, but not high enough to force rate cuts. This is the uncomfortable middle ground. The economy is too strong to give the Fed a clear reason to cut rates, but the inflation shock remains too supply-driven for higher interest rates to look like a straightforward solution.

Are markets expecting the wrong outcome?

Market pricing of a brief hiking cycle followed by tentative rate cuts next year looks misplaced. If the Fed raises rates into the later stages of a temporary supply shock, the disinflationary benefit could be limited. The cost, however, would likely emerge later through a weaker labour market in 2027 and 2028. That leaves the third-quarter baseline looking less like the start of a renewed tightening cycle and more like an extended pause. The Fed may prefer to keep rates steady while monitoring inflation expectations, especially if oil prices continue to retreat and the latest energy shock fades.

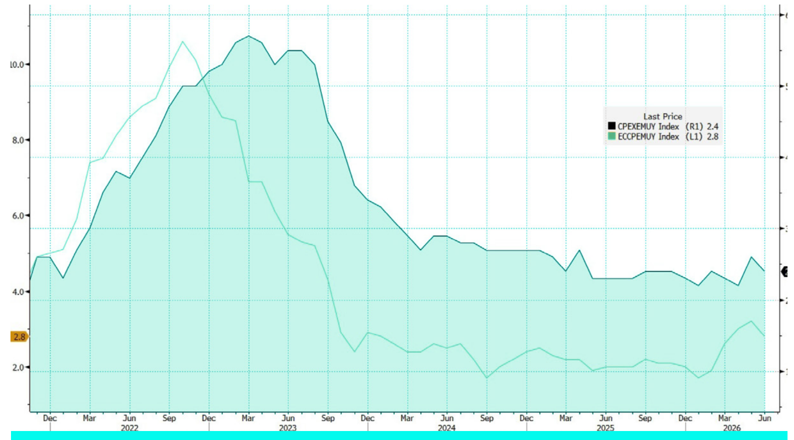
The risk scenario is different. The Fed could still follow a path similar to the European Central Bank by delivering one rate hike before returning to a data-dependent stance. Such a move would shift market attention towards the labour market's ability to withstand higher rates for longer.

Either way, the Fed's dilemma will remain one of balance. Even if policymakers choose a more restrictive path, they will still need to weigh inflation risks against the lagged effects of tighter policy on growth, credit and hiring. That is where the third-quarter tension may become most visible: in the gap between market pricing and the Fed's reaction function. If that gap widens, financial assets could face sharper swings as investors reprice the path for rates, growth and inflation.

The ECB faces a difficult third quarter

Noureldeen AlHammoury
Chief Market Strategist

The European Central Bank enters Q3 facing one of the toughest policy balancing acts among the world's major central banks. After raising interest rates by 25 basis points in June, the ECB is no longer focused solely on the final stage of bringing inflation down. It is now dealing with a fresh energy-driven inflation shock linked to the Middle East conflict, while growth across the euro area remains fragile. With the ECB's next monetary policy meeting scheduled for July 22-23, incoming inflation, energy, PMI and wage data will be closely watched by markets.

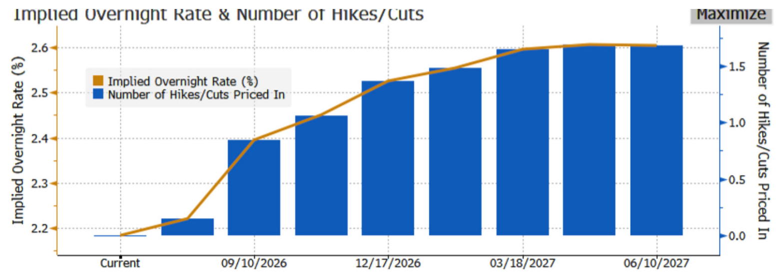


Source: Bloomberg

Inflation remains the ECB's biggest challenge

The ECB's June decision marked a clear shift. Policymakers raised key interest rates by 25 basis points, citing higher energy prices and the need to keep medium-term inflation anchored around its 2% target. The latest Eurosystem staff projections forecast headline inflation averaging 3.0% in 2026, 2.3% in 2027 and returning to 2.0% only in 2028. Core inflation is also expected to remain sticky, averaging 2.5% in both 2026 and 2027 before easing to 2.2% in 2028.

However, the case for another immediate rate hike is less clear. Eurozone inflation eased to an estimated 2.8% in June from 3.2% in May, while the services PMI improved but remained weak at 49.4, still signalling contraction. The composite PMI rose to 50.0, pointing to stabilisation rather than a strong recovery. Together, these figures suggest the euro area economy is not overheating but instead absorbing an external energy-driven price shock.



Source: Bloomberg

Why the ECB is likely to remain cautious

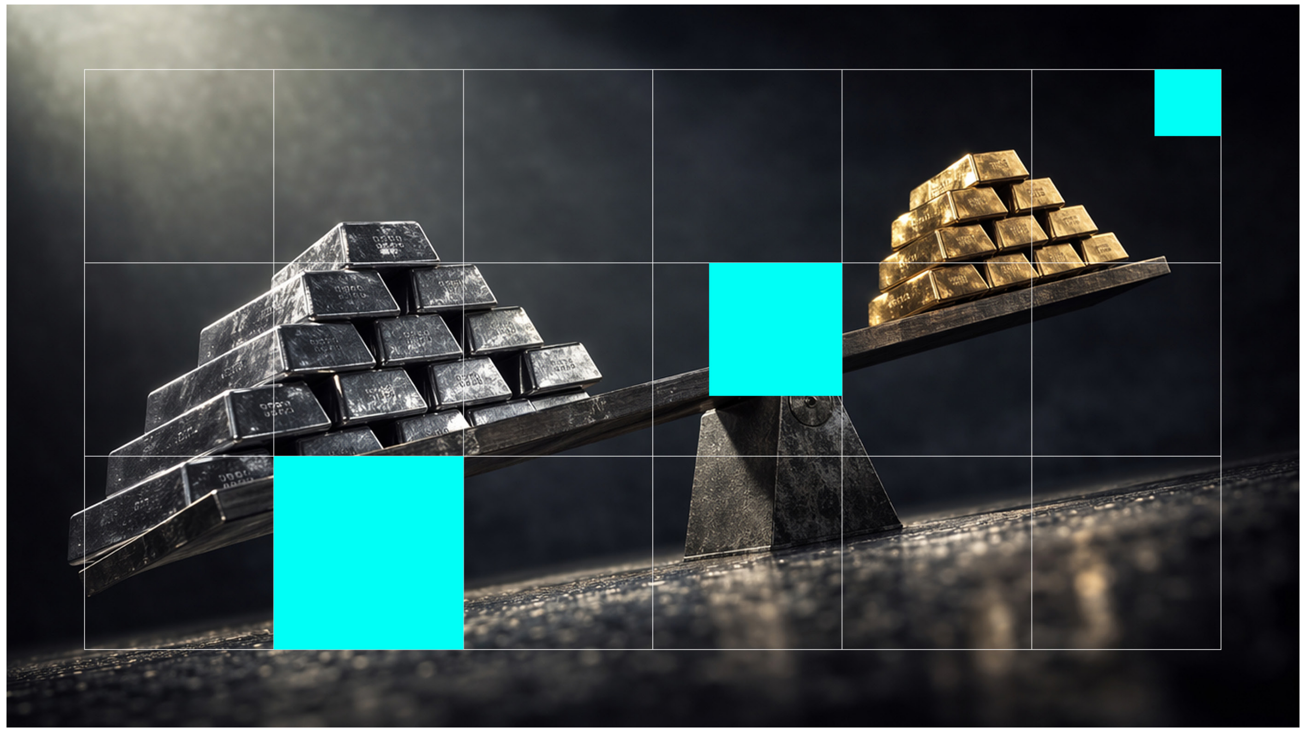
This is where the policy challenge becomes more nuanced. The ECB is unlikely to react to the headline inflation rate alone. Instead, it will focus on how broad and persistent the inflation shock proves to be. A temporary rise in oil or gas prices reduces consumers' real incomes and weakens demand. Raising interest rates too aggressively in response risks deepening the slowdown without increasing energy supply.

This was also the central argument in the Bloomberg Opinion piece, which warned that Europe is already facing higher energy costs and that tightening policy too quickly could worsen the demand shock, particularly for manufacturers already under pressure from the loss of cheap Russian gas and Chinese overcapacity. The analysis also noted that longer-term inflation expectations remained close to the ECB's 2% target, supporting a cautious rather than automatic tightening response.

What should traders watch?

The ECB's real test in Q3 is not whether inflation is above target, it clearly is. The bigger question is whether the energy shock begins to feed into wages, services prices and longer-term inflation expectations. If those expectations remain anchored and core inflation continues to moderate, the ECB could justify pausing after June's rate hike. But if gas prices remain elevated, food prices rise further or wage settlements accelerate, policymakers may be forced to raise rates again despite weak growth.

Our base case is that the ECB will maintain a tightening bias while avoiding any pre-commitment to another rate hike in July. The likely message is one of data dependence and vigilance. For markets, this means the euro could remain supported by interest rate differentials during periods of hawkish repricing. However, European equities, particularly industrials and other rate-sensitive sectors, remain vulnerable if investors conclude that the ECB is tightening into a stagflationary shock rather than responding to genuine demand-led inflation.



Silver is at a turning point

After a volatile first half of the year, silver enters Q3 at an important turning point. Prices have retreated sharply from their January highs, yet physical supply remains tight and investment demand is showing early signs of improvement. The key question is whether these factors can drive a recovery as interest-rate expectations and broader market sentiment evolve.

From rally to correction: Silver's dramatic reversal

Silver had a volatile first half of 2026. After climbing 68% during Q1, prices reversed sharply following the US-Israel-Iran conflict. The metal fell more than 22% in Q2 and is now trading around 18% below where it started the year, and roughly 51% below its January peak.

Despite the correction, one key indicator suggests the market may be approaching a turning point. The COMEX delivery coverage ratio, which measures how many futures contracts could stand for delivery relative to the amount of silver available in exchange warehouses, currently stands at 17.7%, a level considered tight. If physical supply remains constrained, it could provide the foundation for a recovery during Q3.

Big banks remain divided on silver

After one of the most volatile first halves in silver's history, institutional forecasts for the rest of 2026 vary widely. Price targets range from around $60 an ounce on the bearish end to more than $300 under the most bullish scenarios, highlighting uncertainty over whether macroeconomic headwinds or structural supply shortages will have the greater influence during the second half of the year.

J.P. Morgan recently lowered its forecast to $60-$65 an ounce from its previous target of $81, citing softer industrial demand and weaker investor

interest following the sharp correction.
Goldman Sachs continues to see upside from electrification, solar demand, AI infrastructure and a more supportive macroeconomic environment if monetary policy begins to ease. The bank expects silver to reach $85–$100 by year-end.
Citigroup forecasts $110 an ounce during the second half of 2026, arguing that persistent physical supply shortages could drive another leg higher.
HSBC has raised its forecast to $75 an ounce but believes silver remains fundamentally expensive after its early-2026 rally and expects further gains to become more limited.
Bank of America maintains a base case of $56-$65 an ounce, while its bullish scenario ranges from $135 to $309.
A clear divide emerges across institutional forecasts. The bearish outlook largely depends on the Federal Reserve keeping interest rates higher for longer. With Kevin Warsh now leading the Fed and several policymakers still projecting at least one rate hike this year, higher yields could continue to weigh on silver demand by making bonds more attractive.
The bullish case is driven by a different set of factors, including resilient industrial demand, ongoing market shortages and persistent constraints on mine supply.

The gold-silver ratio remains in focus

Many institutional forecasts begin with gold rather than silver. Banks typically estimate a gold price before applying an expected gold-silver ratio to calculate silver's potential value. As a result, movements in the ratio can provide an important indication of how analysts expect silver to perform relative to gold.
The ratio currently stands at 69.9:1. While that is slightly above its long-term average, it is not historically extreme. This suggests silver remains relatively inexpensive compared with gold, leaving room for outperformance if precious metals continue to strengthen. However, any sustained narrowing of the ratio is likely to depend on improving industrial demand, stronger investor sentiment and a broader recovery in the precious metals market.

Positioning has improved without becoming crowded

One of the more encouraging developments heading into Q3 is the recovery in COMEX open interest following the sharp washout earlier this year. According to the latest CFTC Commitments of Traders data for 30 June 2026, total COMEX silver futures open interest has recovered to around 109,000 contracts. While this is up modestly from late June, it remains more than 40% below levels seen at the start of the year. Combined futures and options open interest stands near 134,000 contracts, compared with more than 220,000 at the beginning of 2026.
The sharp decline in open interest during the first half of the year suggests much of the speculative excess has already been cleared from the market. Unlike previous rallies, which were driven largely by leveraged positioning, the current market is being supported more by physical demand and structural supply shortages.
Although positioning has started to recover alongside silver's rebound from its June lows, it remains well below historical highs. That leaves room for fresh speculative capital to return if macroeconomic conditions become more supportive. Physical demand also remains healthy. The July COMEX delivery month has already seen more than 27 million ounces of silver stand for delivery, while the September contract currently has more than 83,000 open contracts, equivalent to roughly 415 million ounces of notional silver exposure ahead of first notice day.
Overall, positioning appears supportive rather than stretched. The market is no longer crowded with speculative long positions, reducing the risk of another large liquidation while still leaving room for additional investor participation if sentiment improves.

Investment demand is recovering, but risks remain

Investment demand has improved during 2026 but remains well below the exceptional levels seen during previous bull markets. Exchange-traded products have returned to net inflows after several years of outflows, reflecting improving investor sentiment as expectations for lower interest rates and ongoing supply shortages strengthen. At the same time, physical investment demand for coins and bars has remained resilient despite higher prices, although demand has moderated from the record buying seen between 2022 and 2024.
Futures positioning tells a similar story. While speculative interest has recovered following the sharp sell-off earlier this year, participation remains well below historical peaks, suggesting the market is not yet overcrowded. That leaves room for further institutional and retail inflows if the Federal Reserve adopts a more dovish stance or geopolitical risks increase.
Investment demand remains one of silver's biggest potential catalysts this quarter. A sustained decline in real yields, renewed ETF inflows or further compression in the gold-silver ratio could encourage another wave of buying and support higher prices.
The main downside risk is that interest rates remain elevated while the US dollar stays firm. In that environment, investment demand is likely to recover more gradually, even if the market continues to face structural supply shortages.

Rufas Kamau
Regional Financial Market Analyst

The UK balancing inflation, interest rates and the pound

The UK enters Q3 facing a difficult economic backdrop. Inflation remains too sticky, while growth is no longer strong enough to give the Bank of England unlimited room to keep policy restrictive. As a result, markets will be watching every data release closely, because the next move in interest rates, gilt yields and the pound will depend on whether inflation continues to cool without the economy losing too much momentum.

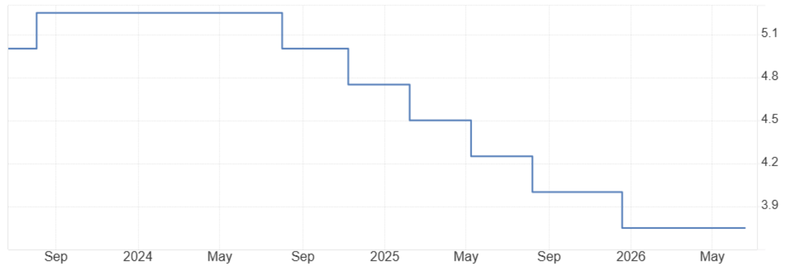
Yazeed Abu Summaqa
Market Analyst

Higher for longer? The BoE's next challenge

The Bank of England is not navigating a straightforward easing cycle. Growth is slowing, but inflation has not yet returned comfortably to target. That is the challenge. If policymakers cut rates too early, they risk keeping inflation expectations too high. If they keep policy tight for too long, they risk placing unnecessary pressure on households, businesses and credit conditions.

This is why the BoE's messaging has become more cautious. Markets may still expect policy easing over the coming quarters, but the Bank cannot commit to a fixed path while wage growth and services inflation remain sticky. Headline inflation still matters, but it is no longer the whole story. The BoE is paying closer attention to domestic inflation pressures because they are harder to reverse than energy-driven price shocks.

The majority within the Bank of England believe a weaker economy could help bring inflation under control without the need for further tightening. As demand slows and labour market conditions soften, companies become less able to pass higher costs on to consumers, particularly as spending becomes more cautious. This gave the Bank of England reason to keep the policy rate at 3.75% during Q2 rather than move towards further tightening.



Source: BoE

Why inflation remains the UK's toughest challenge

The UK's inflation challenge has become increasingly driven by domestic pressures. While energy prices triggered the initial shock, services, wages and housing costs are now slowing the pace of disinflation.

Services inflation remains stubborn because it is closely linked to labour costs. Many service-sector businesses rely heavily on staff, so when wages rise, operating costs increase as well. Those costs are often passed on to consumers through higher prices, making inflation slower to fall. Weaker growth may reduce pricing pressure, but it is unlikely to bring prices down quickly while labour costs remain elevated.

Housing adds another layer of complexity. A shortage of supply continues to support rental costs, while higher borrowing costs have not resolved the shortage of homes. This leaves the Bank of England in a difficult position. Monetary policy can cool demand, but it cannot solve supply constraints.

That is why the Bank remains cautious. Cutting rates while core inflation remains elevated could damage credibility. But waiting too long could deepen the economic slowdown.

GBP's next move depends on growth, not just rates

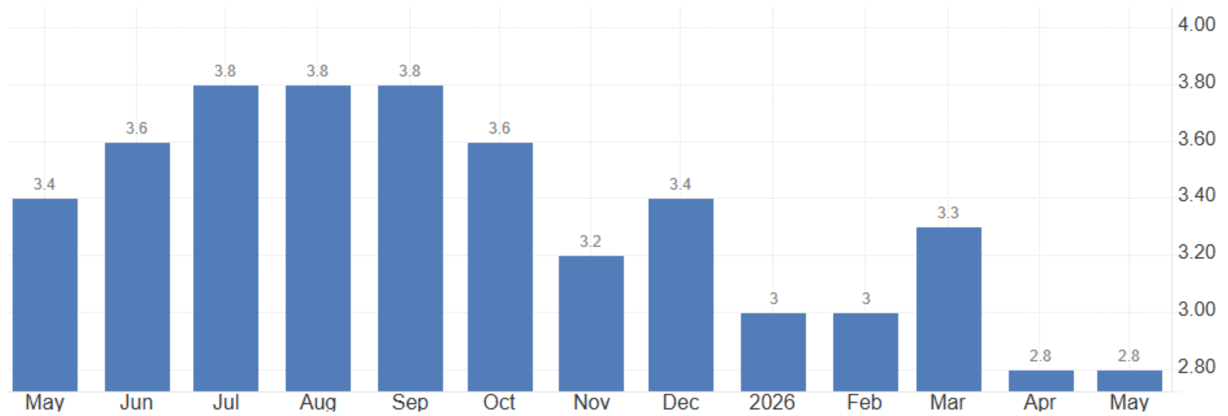
Expectations for the pound will depend on how the UK's policy path differs from that of the US and the eurozone.

In the rate divergence scenario, inflation keeps the Bank of England on hold while the Fed and the ECB move towards easing. That could support the pound, as UK interest rates would remain relatively more attractive.

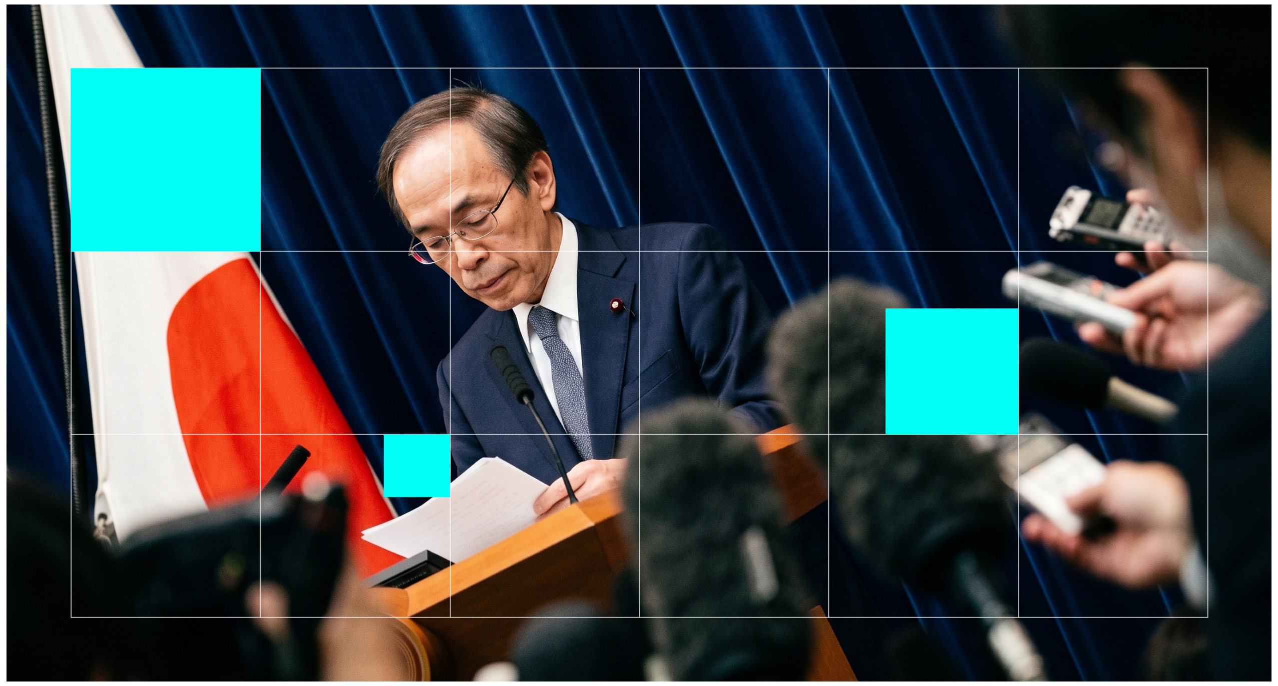
The second scenario is that higher borrowing costs begin to weigh more heavily on economic activity, leading to a sharper slowdown and forcing the BoE to cut rates. In that case, the pound could come under pressure as markets begin pricing in weaker growth, rather than focusing solely on the interest rate gap.

The stagflation scenario is the most challenging. The economy slows while inflation remains high, leaving monetary policy with few good options. Cutting rates could damage credibility, while keeping them high could place even greater pressure on growth. In this scenario, sterling volatility could increase and investors may demand a higher risk premium for holding the currency.

The BoE will possibly maintain a higher-for-longer policy stance throughout Q3 and will not rush into rate cuts after the first positive inflation reading. Inflation may ease further as energy pressures continue to fade, but that alone is unlikely to trigger a clear easing cycle while services inflation and wage growth remain stubborn.



Source: Office for National Statistics



Could Japan's credit squeeze spark the next carry trade shock?

Japan's exit from ultra-loose policy is no longer only a domestic rates story. It's starting to change credit pricing, yen funding and the risk of a disorderly carry trade unwind. The Bank of Japan is trying to normalise policy gradually, but markets are already testing what happens when an economy built around cheap money begins to face higher funding costs.

Credit risk is returning to Japan

After raising its policy rate to 1% in June, the Bank of Japan is making borrowing less effortless than it once was. Officials including Naoki Tamura are still arguing that rates should move gradually toward a neutral level near 2%, meaning companies can no longer assume capital will stay extremely cheap.

The pressure is already showing. Between January and June, 45 Japanese companies declared bankruptcy due to currency depreciation. That was a 32.3% increase from a year earlier and the highest first-half total in four years.

This is not a broad corporate crisis yet, but it is a clear warning. A weaker yen is lifting import costs, while higher rates are making refinancing more expensive. Smaller firms, importers and highly indebted borrowers are likely to feel the squeeze first. That is usually how credit stress begins. Not with the strongest companies, but with firms facing thin margins, weak pricing power and limited access to cheap refinancing.

Q3 will test how much tightening Japan's weaker borrowers can absorb. If the BoJ hikes again while the yen stays under pressure without intervention, credit risk could move from a slow repricing into a more visible market concern.

The end of easy yen funding

For years, the yen made the carry trade straightforward. Investors could borrow cheaply in Japan and invest that money in higher-yielding markets overseas. It worked because Japanese interest rates stayed close to zero and global appetite for risk remained strong.

That backdrop is starting to change. Japanese yields have reached 30-year highs, while the US-Japan 10-year yield spread has narrowed to around 1.69%, its lowest level since 2022. As that gap shrinks, borrowing in yen and taking currency risk elsewhere becomes less attractive. A gradual unwind would likely be manageable. But if the yen strengthens quickly or markets start pricing in another BoJ rate hike more aggressively, leveraged carry trades could unwind much faster.

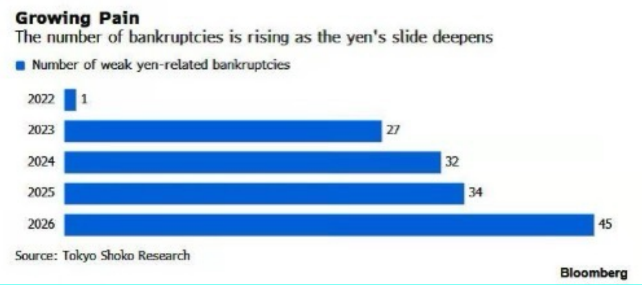
Japanese pension funds, insurers and asset managers also play an important role. As domestic yields become more attractive, more capital could stay in Japan instead of flowing overseas. That would reduce demand for the global bonds and risk assets that have benefited from years of cheap yen funding.

Currency intervention risk is rising

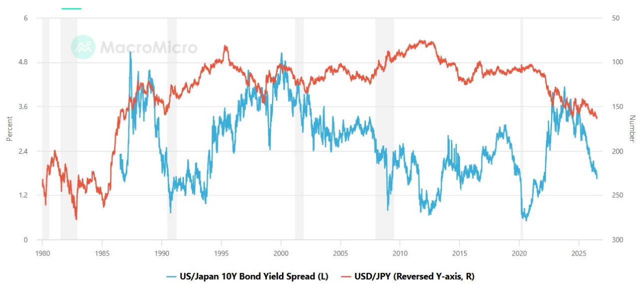
A weaker yen supports exporters, but it also raises import costs and puts more pressure on households and smaller businesses. If the currency weakens further, especially towards levels officials consider excessive, the risk of intervention will rise again. Policymakers would likely begin with verbal warnings, but markets know Japan can step in directly if volatility becomes disorderly.

The opposite risk matters too. A sharp rally in the yen, driven by a carry trade unwind, could tighten global financial conditions quickly. That would not be a normal currency move. It would be a forced adjustment in funding markets.

Q3 is likely to bring another BoJ rate hike to around 1.25%, while the US-Japan 10-year yield spread is likely to remain under pressure. There is also a growing likelihood of real FX intervention, rather than just verbal warnings. If yen weakness continues to push up import costs and add to credit stress, policymakers may have little choice but to tighten policy while also stepping into the currency market. That combination would increase the risk of a sharper carry trade unwind, especially if leveraged investors are forced to cut yen-funded positions quickly.



Source: Bloomberg



Source: MacroMicro

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Market Analyst

What's next for cryptocurrencies? The key themes shaping Q3

After a sharp pullback, cryptocurrencies enter Q3 searching for direction. Bitcoin is trading near a key technical level, institutional demand has weakened and ETF flows continue to point to cautious investor sentiment. With risk appetite still fragile, the market's next move may depend on how investors respond to economic uncertainty, equity market volatility and increasing regulatory pressure.

Bitcoin spot ETFs see outflows as institutional confidence weakens

After months of heightened volatility, the cryptocurrency market is approaching a critical point. The total market capitalisation is around $2 trillion, placing the market at a level where it could either recover or decline further. Meanwhile, Bitcoin is trading near $60,000, a significant technical zone that previously acted as key resistance in 2021. Investor flows tell a similar story. Bitcoin-linked spot ETFs have shown gradual outflows since the end of 2025 and have not yet seen a meaningful recovery. Total spot Bitcoin ETF holdings have declined by approximately 57% from their peak in October 2025, according to Glassnode's US Spot ETF Balances metric (as of 1 July 2026). This trend suggests weakening institutional investor confidence amid ongoing global economic and geopolitical uncertainty, which has affected investment in higher-risk assets such as cryptocurrencies. The chart below shows how selling pressure on Bitcoin

Figure 1. Bitcoin Price vs Bitcoin Spot ETF Net Flows (2024–2026). Source: Own analysis using data from the CBOE, NASDAQ, and NYSE Arca Exchanges.

spot ETFs has intensified since May 2026, with only limited net inflows observed.

Bitcoin and the S&P 500 move more closely during volatile markets

Historically, there has been considerable discussion about the correlation between cryptocurrencies and the stock market, particularly US equities. This hypothesis is mainly based on the fact that both markets are considered higher-risk assets due to their elevated volatility. However, statistical evidence

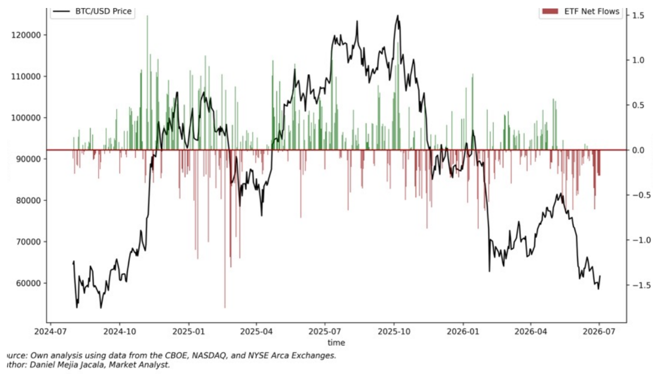

Figure 2. Bitcoin vs S&P 500 Values and Dynamic Correlation (2019–2026).

Source: Own analysis using data from the CBOE and Coinbase Exchanges.

shows that, although periods of high correlation do occur, the relationship is not always as strong or consistent as many market participants expect. A rolling correlation analysis of Bitcoin's weekly returns and the S&P 500's weekly returns, using a six-month comparison window, shows that periods of high and statistically significant correlation (r > 0.40) mostly coincide with declines in both markets. This timeframe is intended to balance long-term dynamics with shorter-term market movements. The findings suggest that Bitcoin prices may be negatively affected if stock markets fall, representing a significant risk, particularly given the sensitivity of equity markets to concerns about the potential overvaluation of companies associated with artificial intelligence. The chart below illustrates this relationship.

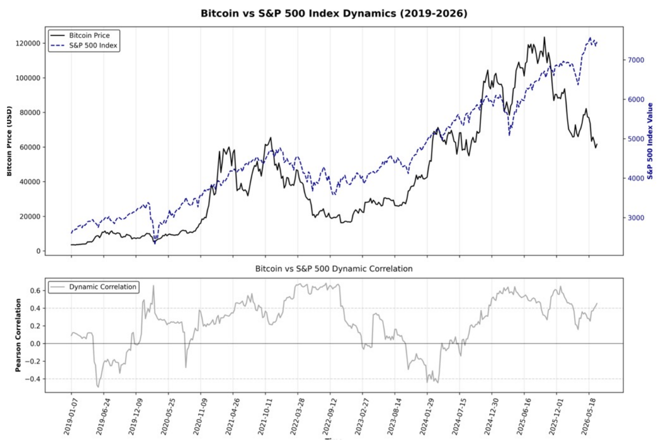

Figure 3. Bitcoin's Historical Drawdown (2018–2026). Source: Own analysis using data from the Coinbase Exchange.

Bitcoin tests a key support level after a 50% decline

History shows that sharp market corrections are a recurring feature of the cryptocurrency market. Bitcoin has experienced drawdowns of more than 50% on several occasions, including a maximum drawdown of 84.27% in 2019. Currently, Bitcoin is trading around $60,000, which represents a drawdown of approximately 51.6% from its peak of around $124,000 in October 2025.
Understanding this history helps traders assess the risk-reward ratio of their positions more clearly. While cryptocurrency prices may fall further, given their history of deep drawdowns and high volatility, they have also demonstrated significant return potential over time. The key is to define an appropriate risk tolerance and investment horizon based on individual objectives, whether short term or long term.

Finally, it is important to recognise the key risks facing cryptocurrencies. Geopolitical and economic uncertainty can increase risk aversion, encouraging investors to shift towards defensive or safe-haven assets. At the same time, cryptocurrencies face growing competition from other risk assets, including companies linked to artificial intelligence and technological innovation, as illustrated by investor interest in high-profile companies such as SpaceX. The regulatory environment is also evolving, particularly in the United States and Europe, where the continued development of tokenisation and central bank digital currencies (CBDCs) may reshape the competitive landscape.

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Q3 Market outlook 2026

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