

Fed will keep cutting in 2026 while GCC credit looks well supported

16 December 2025 – Market Economics

- Divisions will be more apparent in Federal Reserve policymaking in 2026 amid mixed economic data.
- The composition of the Fed next year is in question and in particular its leadership which will likely lean more dovish.
- We expect the Fed to cut by another 75bps in total in 2026 with the front end of the US Treasury curve gaining while longer-term bonds reflect more concerns over the US government's fiscal path.
- After record volumes for issuances in 2025, GCC borrowers will take advantage of lower rates to meet borrowing needs amid lower oil prices

A divided Fed to start the year

2026 will see the Federal Reserve beset by internal debate and struggling to express a consensus view. Based on the Fed's summary of economic projections released at the December FOMC meeting, economic growth will accelerate in 2026 to 2.3% from an estimated 1.7% in 2025. The Fed projects a deceleration in PCE inflation to 2.4%, not yet at the Fed's 2% target level but ending the year at a much lower level than in the past few years. Unemployment is projected to be steady at about 4.4%.

Taken together, slowing inflation and modest unemployment levels are a good signal that the Fed will implement more cuts to policy rates and the median presented in the dots plot released in December is indeed for one more 25bps cut in 2026, following 75bs of easing 2025.

Consumer fears of inflation easing but jobs in focus



Source: University of Michigan, World Bank, Emirates NBD Research.

But the dispersion of views for where rates go in 2026 among Fed policymakers is wide. In the dots plot for 2026, seven participants projected no cuts and eight projected two or more cuts with one member proposing as many as six 25bps cuts. Comments from Fed speakers in the second half of

the year have reflected that wide range of views with some policymakers clearly wanting to stay cautious, worried about the risk that inflation will reaccelerate and erode incomes, while others have focused much more on the risks that the labour market will continue to weaken.

As economic data continues to be mixed with most momentum indicators suggesting good levels of activity albeit with weakening labour conditions and persistent price pressures, this divided Fed will characterize meetings for at least the first few months of 2026. That will mean that markets will have to digest more dissents at FOMC meetings, similar to the December FOMC when nine FOMC members voted for the 25bps cut, two supported keeping rates unchanged and one voted for 50bps of cuts.

Changes in Fed leadership in focus

Beyond the scale of disagreement on interpreting economic data, the Fed will go through a composition change in 2026 that could further frustrate messaging. The most critical change will be the appointment for a new Fed chair. Jerome Powell's term as chair will end in May 2026 and US President Donald Trump is finalizing his nominee for the next appointee. Of all the candidates proposed, from director of the National Economic Council Kevin Hassett to existing Fed governors Michelle Bowman or Christopher Waller, all appear publicly to support a more dovish tilt on policy than the Fed's current stance.

Powell's term as chair will end in May but he will still be a member of the Fed's board of governors until 2028. Should Powell choose to resign his governor position that will mean an additional vacancy on the Fed to be nominated by President Trump who clearly favours more dovish candidates.

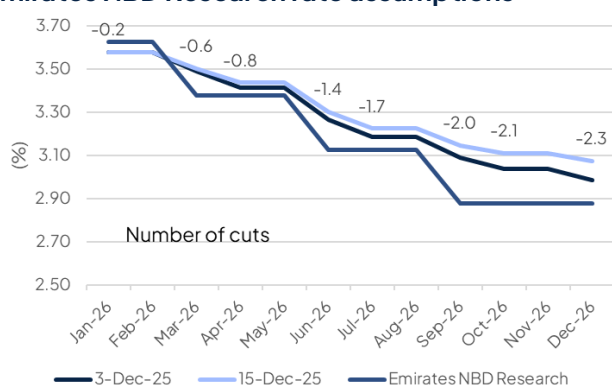
The approval process of the next Fed chair and next potential governor could also become caught up in political debate. Stephen Miran, who was nominated by President Trump to fill out the remainder of Andrea Kugler's term when she retired mid-way through 2025, was approved with a narrow 48-47 majority in the Senate.

The lack of a clear signal from economic data and divisions in Fed leadership will keep the outlook for rates in 2026 volatile. Markets oscillated sharply in their expectations for the December FOMC decision, pricing in less than a 30% probability of a cut as late as November 19 before sharply reversing to near 100% probability in the days leading up to the December 11 meeting. The interruption to data flow caused by the government shutdown will still linger into 2026 when data releases will be relatively stale.

Another 75bps of easing expected in 2026

We expect that the Fed will cut rates again in 2026 as worrisome signals from the labour market will need to be addressed even as inflationary risks remain in the background. Some Fed officials may take support from the fact that even as the Trump administration imposed tariffs across the US' trading partners this year, the pass-through to inflation has been relatively limited. Our forecast is for 3x25bps cuts from the Fed in 2026, taking the Fed Funds rate to 3% by the end of the year. Cuts will be more spaced out, rather than taking place at consecutive meetings as seen in H2 2025.

Emirates NBD Research rate assumptions



Source: Bloomberg, Emirates NBD Research.

For US Treasury markets we expect that the short-end will track the moves in the Fed Funds rate closely with about 70bps of decline in the 2yr UST yield. However, concerns over the longer-run fiscal path in the US will keep the longer-end of the curve

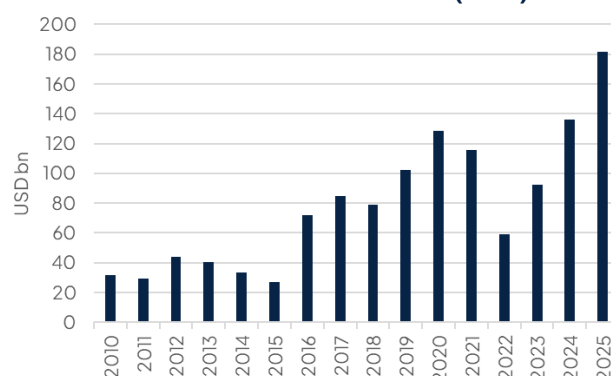
anchored and we expect far less movement on the 10yr UST yield.

GCC issued record volumes in 2025

Lower rates from the Fed will be followed by central banks across the GCC even if the downside risks to the labour market present in the US are not apparent across the regional economies. Lower rates will provide a tailwind to the robust non-oil growth in particular for markets like the UAE and Saudi Arabia.

Regional borrowing will also likely take advantage of the drop in rates. Bond and sukuk volumes in 2025 were on track to hit a record volume of more than USD 180bn, up from around USD 135bn in 2024, and with oil prices set for another decline in 2026, fiscal balances across the GCC will be slimmer.

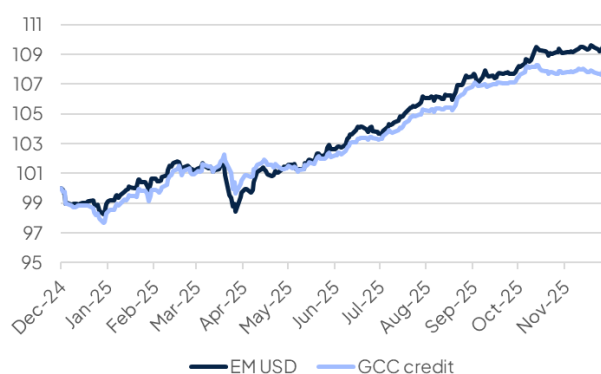
Total GCC bond and sukuk issuance (USD)



Source: Bloomberg, Emirates NBD Research.

Credit performance has been good for GCC bonds in 2025, tracking the broader move in emerging market USD bonds. While volumes will likely be large again as borrowing needs remain wide, strong credit fundamentals among large borrowers should keep the market well supported.

GCC bonds tracking EM

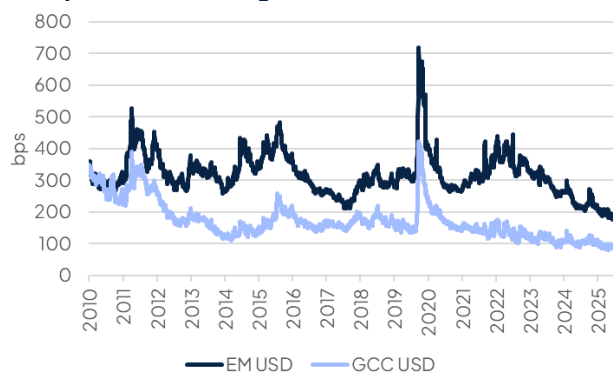


Source: Bloomberg, Emirates NBD Research



Regional credit spreads have tightened to record lows of less than 100bps over US Treasuries per a GCC wide US Dollar-denominated index and major moves this year reflected much more concern around trade and the imposition of US tariffs than geopolitical risks. Pricing has remained tight with the latest issues from Abu Dhabi in September raising a total of USD 3bn at just +10bps for a 3yr tranche and +18bps for a 10yr tranche.

GCC spreads much tighter than EMs



Source: Bloomberg, Emirates NBD Research

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