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CBUAE–FED Currency Swap Line

A precautionary backstop proposal, Not a distress signal

CONTEXT: A US media outlet earlier this week reported that the Governor of Central Bank of UAE (CBUAE) had raised the idea of a USD–AED currency swap line with US Treasury Secretary Scott Bessent and Federal Reserve (FED) officials during recent IMF/World Bank meetings in Washington. On 21st April, US President Donald Trump said the currency swap with the UAE is under consideration. Some media outlets have framed this as a sign that the UAE is facing acute liquidity stress, which is factually not true. Hence, in this note we try to provide a more realistic, data-backed analysis.

Swap line is precautionary, not crisis driven

Discussing a Fed swap line is a prudent contingency measure – not an indication that the UAE is running out of dollars or under peg pressure.

Bilateral CCY swaps are a common tool for stability

Central bank swap lines are a normal liquidity tool, also used by stable economies and allies. They help ensure dollar liquidity during rare pressures without depleting reserves.

AED peg remains solid

The UAE's dirham (AED) is firmly pegged at 3.6725 per USD since 1997 and remains credibly supported by ample reserves and assets and the fact that a significant portion of its trade (including oil) is in USD.

Banking system liqudity is still ample

While USD demand in the sytem has gone up at the peak of war, which is a natural phenomenon, banking sytem liquidity continues to be resilient supported by CBUAE initiatives.

What is a cross-currency swap line between two central banks?

- A central bank cross-currency swap line **is a bilateral agreement** under which two central banks exchange agreed amounts of their respective currencies for a defined period, with a commitment to reverse the exchange at the same rate on a fixed future date.
- **It is not a loan** – no debt is incurred and no interest is paid in the conventional sense. The FED would hold dirhams as collateral; the CBUAE receives dollars.
- The purpose is to *ensure that in periods of heightened demand for a specific currency (in UAE's case the USD), a central bank can supply it to domestic financial institutions without having to liquidate existing assets*.
- The FED maintains permanent standing swap arrangements with five peers – the Bank of England, Bank of Canada, Bank of Japan, European Central Bank, and Swiss National Bank – and has extended temporary facilities to other central banks during episodes of global stress (e.g., COVID-19 in 2020). Please refer to the charts on page 6 about global central banks swap lines.

Does seeking a currency swap line necessarily signal financial distress?

- **The answer is 'No':** The historical record makes this clear. Many countries with robust balance sheets have sought or utilized currency swap lines purely as a precautionary measure. UAE officials have characterized this latest swap discussions explicitly as 'preliminary and precautionary', and **no formal request has been made yet.**
- The existence of a swap line in practice reduces the probability that a country will ever need to use it, since markets know a backstop exists.

- A swap line would act as a safety net to ensure UAE banks can get USD liquidity without draining national FX reserves if the Iran conflict worsens and there is a significant demand for USD, which is currently under control.
- During severe geopolitical stress, it is quite common for investors and residents to often seek haven assets like the USD, and capital flight or extra cash withdrawal pressures can emerge as people convert local assets or deposits into dollars. This dynamic is currently not evident in the UAE, but officials are cautiously preparing for 'what if' scenarios.
- By arranging a swap line now, the CBUAE would have a "dollar liquidity insurance policy" in place. This pre-emptive step helps calm markets and ensure that even if the conflict or risk aversion escalates, the UAE can meet any spike in USD demand without delay. In short, given the remote possibility of a severe dollar crunch, if the Iran war intensifies, the swap line idea centers on being prepared in advance, rather than scrambling in an actual crisis.

Consider the following cross-currency swap deals and their objectives:

- South Korea, Singapore and Australia are all investment-grade sovereigns and have activated FED swap lines during the 2008 and 2020 crises not because of insolvency but to prevent dollar funding gaps from impacting domestic liquidity. ***Indeed, Treasury Secretary Scott Bessent yesterday (22nd April) said many other Gulf allies and a number of Asian nations have requested foreign exchange swap lines with the US.***
- Saudi Arabia maintains the riyal's dollar peg and holds substantial FX reserves, yet simultaneously operates a cross-currency swap agreement with the People's Bank of China to facilitate CNY–SAR trade flows for its largest bilateral trade relationship. Swap lines are instruments of bilateral economic management, not signals of weakness.
- In 2025, Türkiye's central bank (CBRT) and CBUAE signed a $4.9bn currency swap deal and the objective was to deepen the financial cooperation between the two countries to enhance trade and economic relations.

How would a FED–CBUAE swap line actually work, and would it also benefit the US?

- If activated, a swap line would let the US FED provide USD liquidity to the CBUAE in exchange for UAE dirhams, instantly bolstering dollar supply locally.
- This mechanism is extremely useful in a crisis scenario. Rather than the UAE having to sell its foreign assets or draw down reserves to raise dollars, the FED would temporarily supply dollars (creating them as needed) and hold an equivalent value of dirhams as collateral.
- The CBUAE could then lend those dollars to UAE banks or institutions facing high demand as this would ease any critical situation without depleting the UAE's own USD reserves.
- Crucially, **it prevents forced fire-sales of USD assets, which indeed delivers a scope of benefit to the US**. For instance, UAE authorities and sovereign funds hold large amounts of US Treasury bonds and other dollar investments. In a dollar squeeze, selling those en masse for cash could negatively affect both the UAE (by crystalizing losses) and the US (by pushing up US interest rates). A swap line avoids that scenario – UAE entities wouldn't need to liquidate their USD assets hastily because the central bank can swap dirhams for dollars from the FED on the back of the agreement.
- The **FED has a self-interest here too**. Historical FED policy shows they offer swap lines in part to protect US financial markets from destabilizing asset sell-offs abroad. In essence, a USD–AED swap would act as a bilateral financial safety valve – ensuring the UAE banking system can access dollars to meet customer needs, while also safeguarding the value of the UAE's substantial dollar investments (like US Treasury bonds) by removing pressure to sell them.
- **Both countries benefit**: The UAE economy stays liquid and stable, and US markets avoid turmoil that could arise if a major holder of USD assets faced a cash event. The ***swap arrangement is therefore a bilateral backstop that protects both the integrity of the UAE's financial system and the stability of US dollar asset markets.***

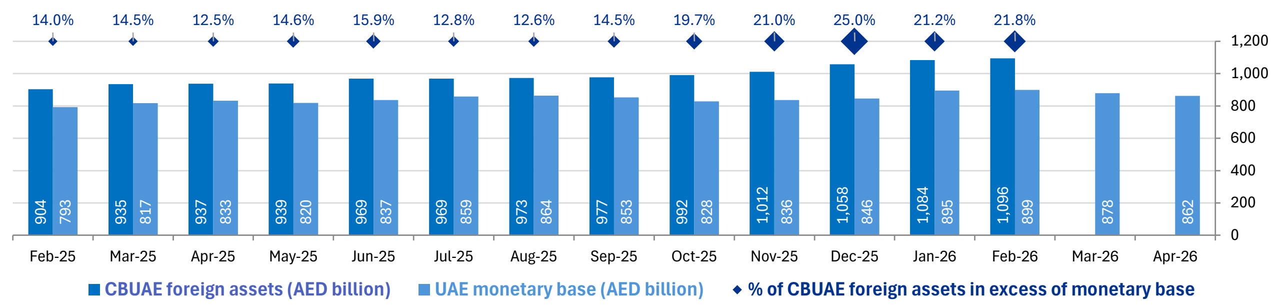
Does this mean UAE is moving away from the dollar toward the yuan as reported by some media outlets?

- **The answer is 'No':** In our opinion, any speculation about de-dollarization overstates the situation materially. The dirham has been pegged to the USD at 3.6725 since 1997 and is **backed by CBUAE's substantial foreign assets**.
- The growing focus of the UAE and other GCC states to facilitate more CNY/RMB flows is due to the fact that China is the top trading partner for most GCC states. Total China-Arab trade is estimated to have exceeded USD450bn in 2025. Settling in local currency reduces 'double conversion' costs (Local → USD → RMB).
- Amidst the ongoing regional conflict, GCC states are seeking 'non-Western' payment rails like CIPS and mBridge to insulate their economies from the geopolitical disruptions to the USD-based banking system.
- Irrespective of the above initiatives taken in the past few years, any massive shift to RMB settlement creates a currency mismatch risk on national balance sheets that are still functionally dollar-denominated.
- Market Liquidity: The RMB share in global trade finance still lags far behind the USD in terms of global FX liquidity and as a reserve asset.
- Corporate Inertia: Many private sector firms in the GCC still prefer USD for its stability and global ubiquity, as seen in recent surveys showing that while trade exposure to China is high, RMB-denominated debt remains relatively low.
- Security & Military Ties: The Gulf's primary security architecture remains deeply tied to the United States. Shifting the 'petrodollar' foundations too aggressively carries profound geopolitical risks.

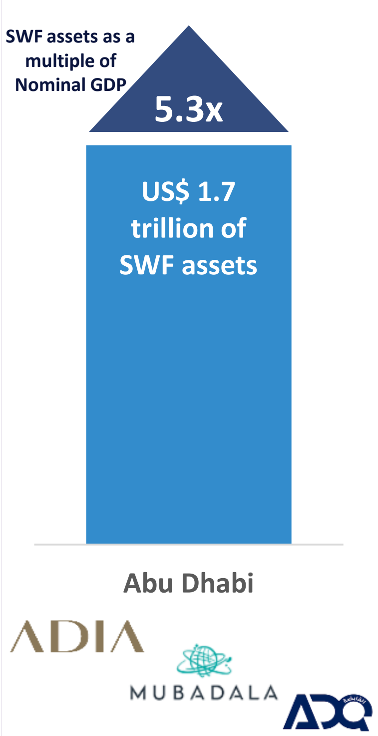
How strong are the UAE's own dollar buffers and financial fundamentals?

- **Exceptionally strong:** Even before any swap line, the UAE has huge financial ammunition to support its currency and economy. The Central Bank's foreign reserves have more than doubled over the past few years, reaching about AED 1.09 trillion ($298bn) in February 2026.
- In fact, foreign reserves now exceed the UAE's monetary base by ~22% at the end of February 2026 – a very high coverage ratio that underpins the peg's credibility.
- Moreover, the UAE is backed by massive sovereign wealth funds (SWFs). As of 2025, the UAE's various SWFs (such as ADIA, Mubadala, ADQ, ICD, etc.) collectively manage on the order of ~$2.35 trillion in assets – one of the largest sovereign wealth stockpiles in the world. These external assets provide an enormous cushion. They could be mobilized, if absolutely necessary, to defend the currency or support the banking system, though there is no indication such drastic action will be needed.
- The UAE's external position is very robust, as it entered the current challenging geopolitical situation with significant balance sheet strength. In the past five years, UAE's banking-sector total assets have grown by 65% to AED 5.47 trillion ($1.5 trillion), and of these, foreign assets represent more than 38% as of February 2026.
- Even the share of more flight-prone money in the banking system is relatively limited. As of February 2026, only about 10% of UAE bank deposits are held by non-residents, so the exposure to sudden foreign withdrawal is not excessive. In short, the UAE has ample firepower (both in official reserves and broader sovereign assets) to meet dollar needs. The exploratory swap line would simply add an extra layer of assurance to an already strong foundation.

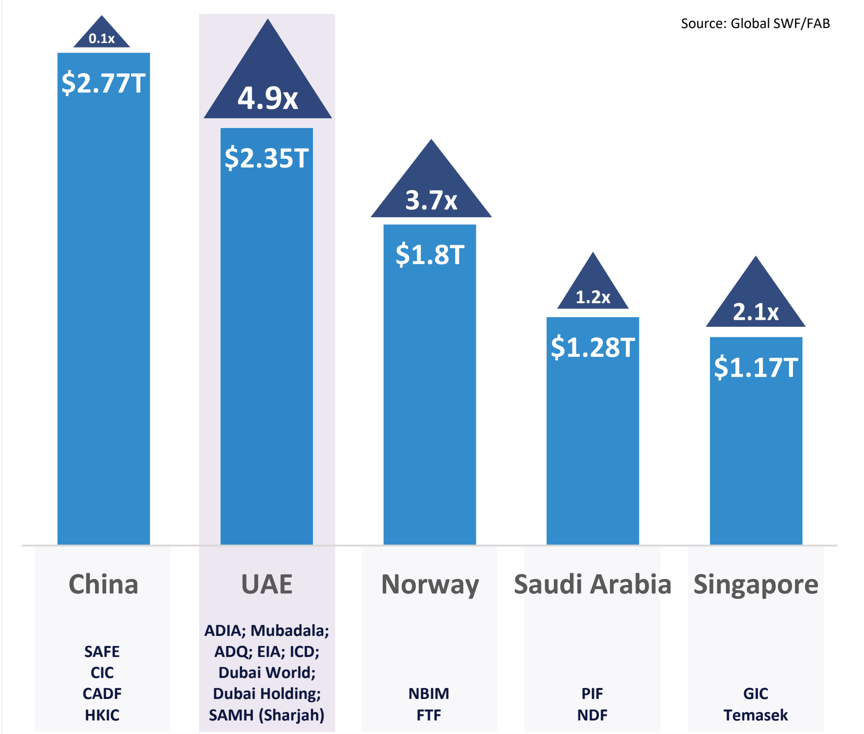
CBUAE foreign reserves exceed UAE's monetary base with a very high coverage ratio that underpins the Dirham's peg credibility



Abu Dhabi's SWF assets are 5.3x of its GDP



Top 5 countries with total SWF assets of more than US$ 1 trillion



Sources for the charts: CBUAE; Global SWF FAB

What measures has the CBUAE taken domestically to support liquidity during the conflict?

The CBUAE has already deployed a comprehensive "Financial Resilience Package" of emergency measures (announced in March 2026) to fortify the banking system's liquidity in both dirham and dollars. These steps are preemptive and temporary, aimed at ensuring banks can continue operating smoothly through the Iran war's uncertainty. Key elements of this package include:

(1) **Monetary Policy Measures**: Enhanced access to central bank funds – banks can tap up to 30% of their CBUAE reserve balances and can access new AED & USD liquidity facilities.

(2) **Liquidity & Funding Relief**: Temporary easing of liquidity and stable funding ratios – e.g. Liquidity Coverage Ratio (LCR), Net Stable Funding Ratio (NSFR) – to give banks more flexibility in managing short-term funding.

(3) **Capital Buffer Relief**: Temporary release of capital buffers – Countercyclical Buffer (CCyB) and Capital Conservation Buffer (CCB) – letting banks dip into these reserves and increase banks' lending capacity and shock absorption.

(4) **Credit Risk Management Flexibility**: Regulatory forbearance on loan classification – banks may delay classifying certain crisis-affected loans as non-performing.

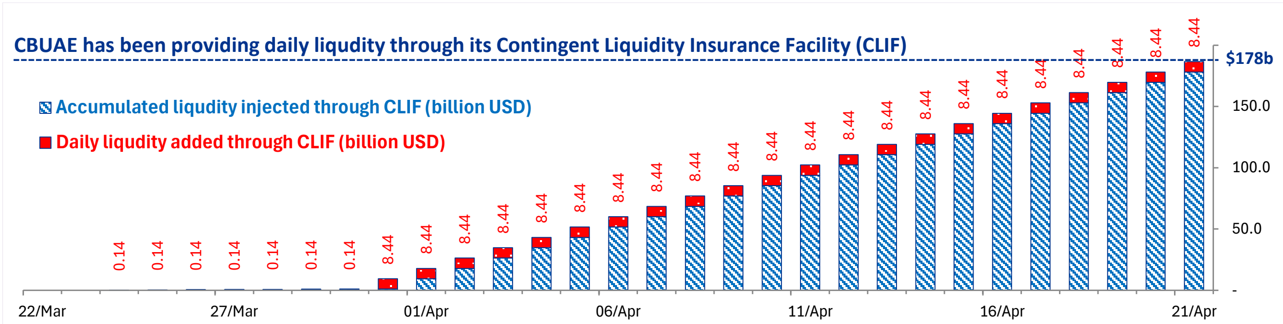
(5) **Additional Support**: CBUAE urged banks to continue lending and providing financial services to support customers and the broader economy despite the challenging conditions.

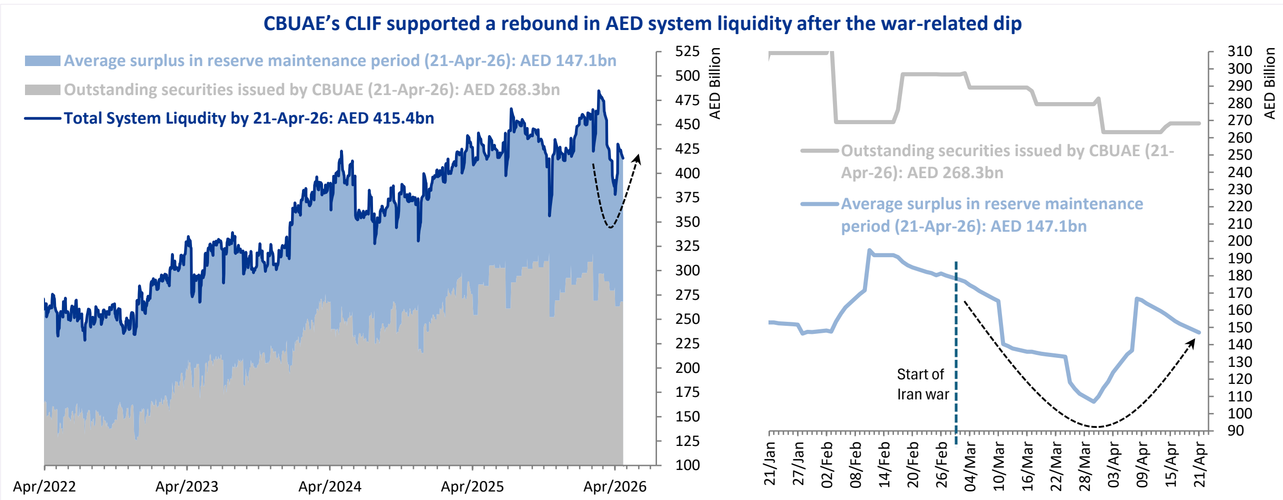
Critically, the central bank underscored that there has been no material impact on banks' health or payment systems so far. These measures are precautionary buffers. They are backed by the CBUAE's own formidable resources (over AED 1.1 trillion in FX reserves) and by the fact that UAE banks collectively hold substantial liquid assets (around AED 920 billion with the central bank).

The message is that domestic liquidity is well-managed: Local banks have access to central bank funding and can even tap into regulatory reserves if needed. The CBUAE has activated a special liquidity tool – **CLIF (Contingent Liquidity Insurance Facility)** – which was first introduced in 2022.

- Unlike standard credit lines, the CLIF facilities act as a liquidity backstop, ensuring that if a bank or NBFI cannot meet its short-term obligations due to market-wide "shocks," it has guaranteed access to cash.
- Eligible counterparties can access CBUAE reserves for term settlement by pledging securities as collateral via a repurchase agreement for conventional funding or via a Collateral Management Agreement (CMA) for funding in accordance with the Islamic Shariah rules.

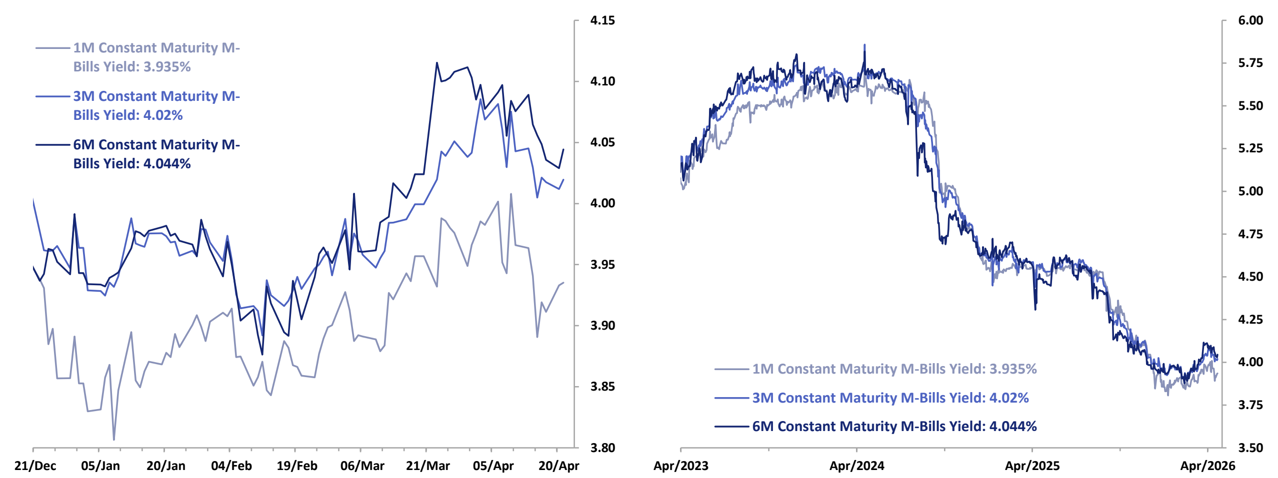
According to the data released by the CBUAE, around AED 685.5bn ($178bn) of liquidity has been injected since 24th March. This has indeed helped to boost the AED system liquidity after experiencing some drop after the onset of the war.



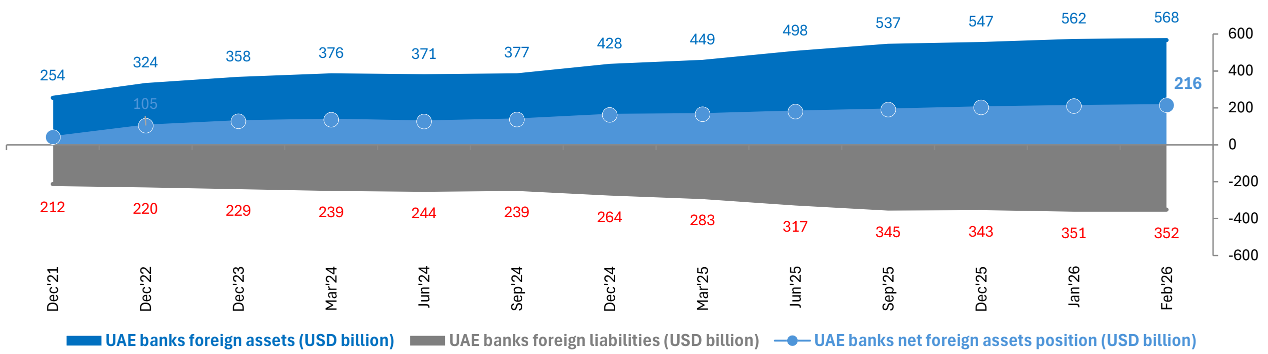


Source for the charts: CBUAE; FAB

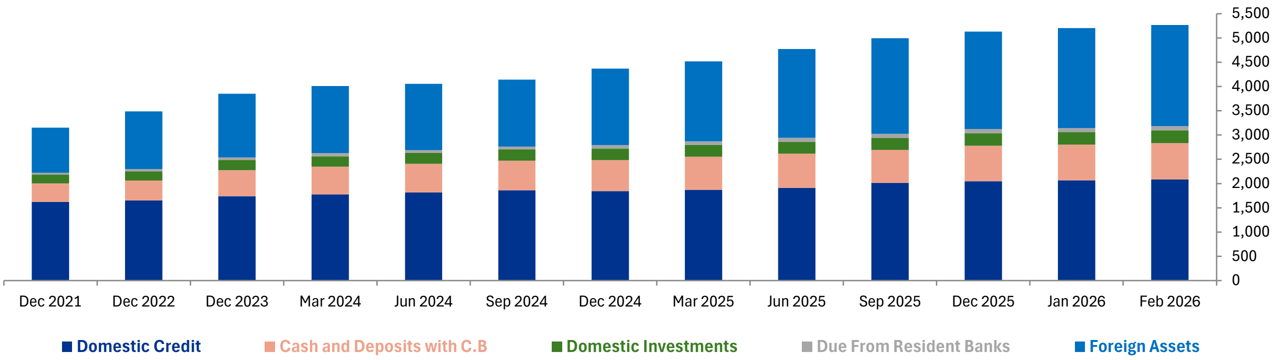
The movement in UAE M-Bill yields also indicate that there is no material liqudity pressure in the banking system



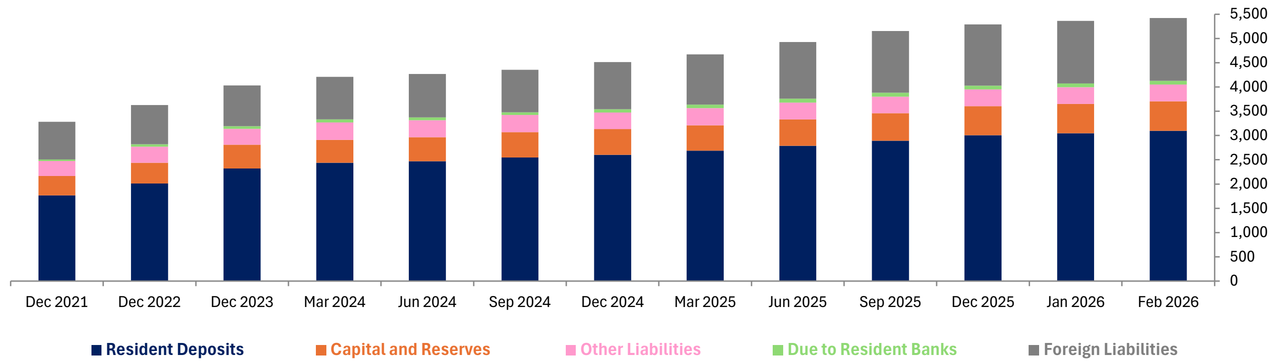
UAE banks' net foreign assets position has more than doubled to USD 216 billion in past three years



Aggregated Balance Sheet of UAE Banks - Assets (AED billion)



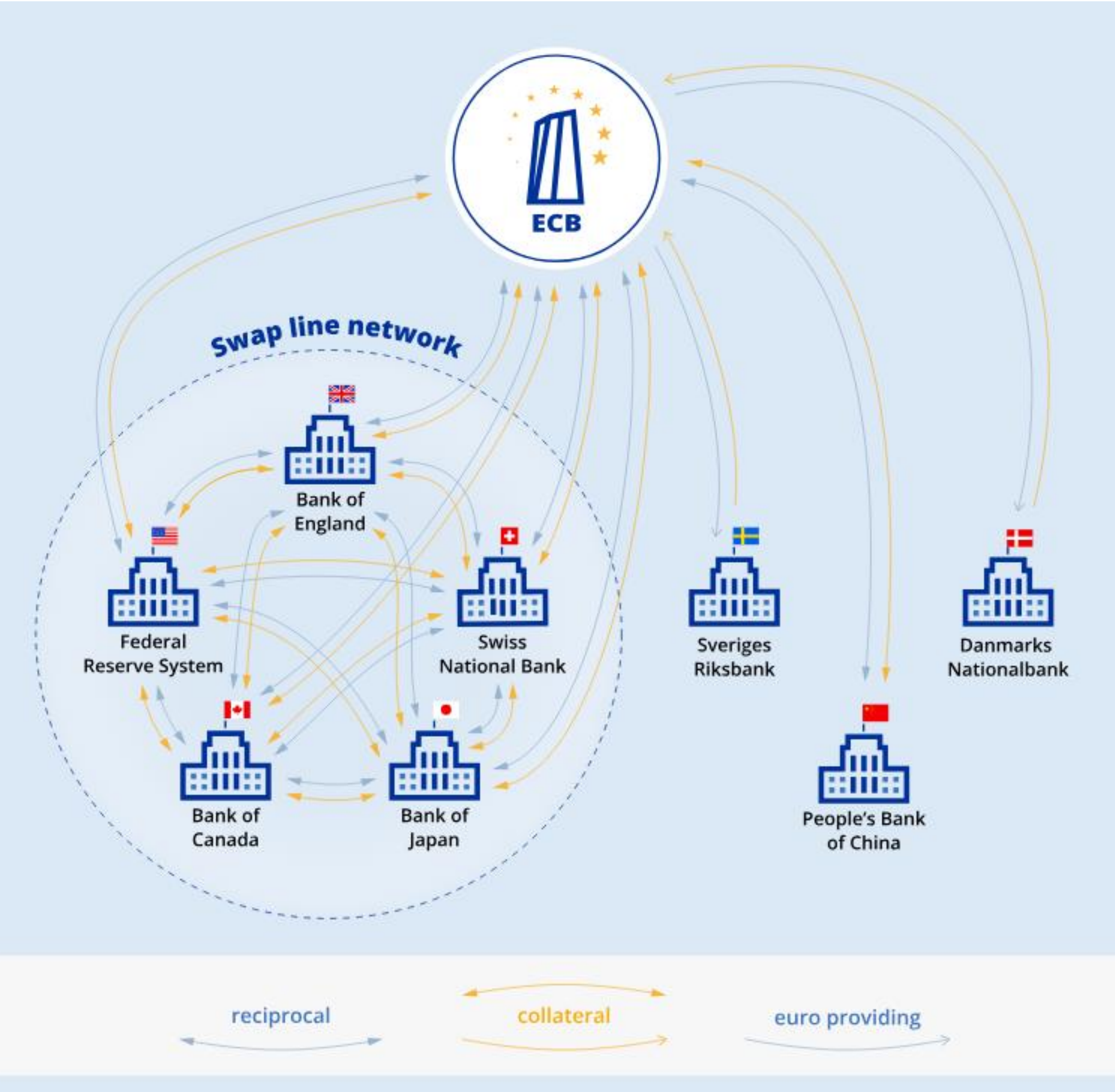
Aggregated Balance Sheet of UAE Banks - Liabilities & Capital (AED billion)



Source for the charts: CBUAE; Bloomberg; FAB

Appendix:

[ECB](#) says swap and repo lines are well-established instruments in central banks' toolkits



Source: ECB

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