

US dollar set for another soft year in 2026

16 December 2025 – Market Economics

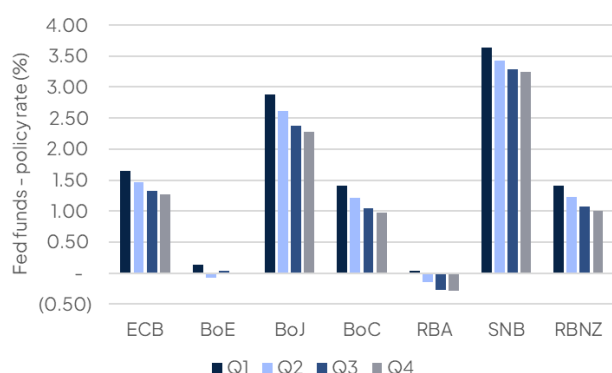
- The US dollar will slide against peers again in 2026 though the moves will be more muted than in 2025.
- Rates differentials will weigh on the US dollar as the Federal Reserve continues with rate cuts while peer central banks keep policy on hold or signal that they are preparing to move rates higher.
- Emerging market currencies held up relatively well in 2025 notwithstanding the threats from tariffs and policy uncertainty.

Another soft year for the US dollar

We expect the US dollar will decline compared with peer currencies in 2026 as policy differentials increasingly move against it. Among major central banks, the Federal Reserve will stand out as still cutting policy while peers will either keep rates on hold or lean towards tighter policy.

On the surface, the US dollar doesn't look like a natural candidate to weaken. Growth in the US economy will be faster than all major peers in 2026, based on consensus projections, and inflation will also be materially higher. But a softening labour market is encouraging more dovish views from the Fed even amid the higher inflation environment. Our expectation is for another 75bps of cuts from the Fed in 2026 compared with no change in policy from the European Central Bank and hikes from the Bank of Japan.

Nominal policy rate differentials



Source: Bloomberg, Emirates NBD Research. Note: consensus projections.

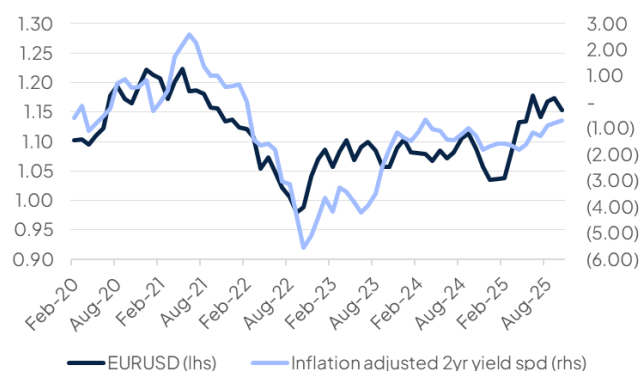
Euro to gain though not at same pace as 2025

We expect that the Euro will extend its 2025 gains against the US dollar in 2026 although the scale of appreciation will be far more muted. Economic activity in the Eurozone remains sluggish—the regional economy expanded by just 1.4% y/y in Q3 2025—but that is a material improvement from the static levels of activity recorded in 2024. PMIs

across the bloc have improved recently with the HCOB services PMI holding around 53 in the final months of 2025.

Inflation in the Eurozone will remain relatively stable in 2026, close to target levels of around 2%. After cutting rates by 100bps in 2025 we do not expect that the ECB will cut rates any more in 2026, keeping the deposit facility at 2%. Several ECB policymakers have even been making a case that upside risks to growth may warrant the bank needing to actually hike rates though we are not expecting that to be an imminent change in direction.

Rates moving in favour of EURUSD



Source: Bloomberg, Emirates NBD Research.

While the Eurozone's economy may not be showing signs of vigour, it does appear to be at least stable. Narrowing rate differentials will favour the Euro in 2026 though the momentum on rates will be more to do with the Fed than the ECB or Eurozone economic dynamics. We expect EURUSD will move from 1.17 at the end of 2025 to 1.21 by the end of 2026, an appreciation of about 3.4% compared with 13% gains in 2025.

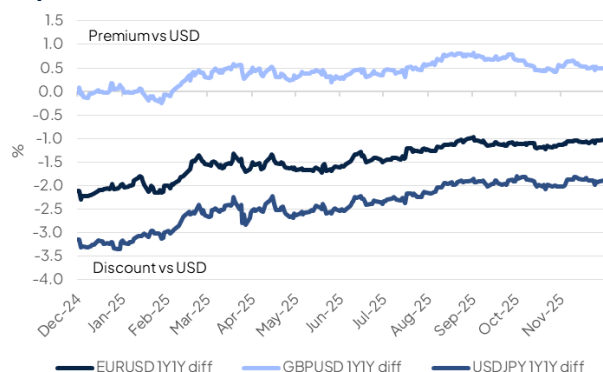
Could 2026 be the standout year for JPY?

The Japanese yen looks the most likely candidate for strengthening in 2026 though near-term political noise means that any gains could be delayed until later in the year. Economic activity will decelerate markedly in 2026 as trade and investment cool. But



in an effort to restore some growth and inflation momentum, Japan's new government under prime minister Sanae Takaichi has approved a large stimulus package worth a total of USD 135bn in direct and indirect support measures.

JPY poised to recover



Source: Bloomberg, Emirates NBD Research.

Despite the sizeable government stimulus, inflation is still expected to be moderate in 2026. The Bank of Japan hiked rates by 25bps at its January 2025 meeting but has since held policy unchanged. Following another 25bps hike expected at the December 2025 meeting, we expect at least one more hike in 2026. While policy rates in Japan will still be low, the hikes will contribute to substantial narrowing of the rate differential between the Bank of Japan and Fed, supporting our view that the yen will be able to strengthen in 2026. Moreover, on most measures of effective exchange rates the Yen remains among the cheapest currencies of G10 peers.

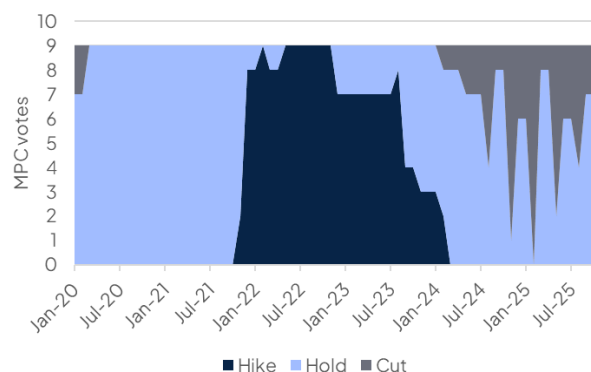
However, geopolitical anxieties over China-Japan relations will threaten the near-term outlook for the yen. That could push more of the appreciation into the second half of the year provided that geopolitical worries fade. We expect USDJPY to end 2025 at around 155 before strengthening to 140 by year-end 2026.

Outlook for sterling is neutral

For the British Pound we are neutral on 2026. Momentum in the economy is faltering and is forecast to moderate in 2026 to be among the slowest growing major economies. At the same time inflation has remained a challenge for the UK economy, rising from 2.5% at the end of 2024 to 3.6% as of October 2025. Rising unemployment in the UK and higher taxes on businesses will likely cool consumption and investment in 2026, helping to turn the inflation outlook lower.

Like the Federal Reserve in the US, the Bank of England is dealing with substantial dissents in forming a majority view. We expect at least two more 25bps cuts from the BoE in 2026 which will help to narrow rates differentials with the US and inflation-adjusted differentials should favour the UK.

Split votes on the rise at Bank of England



Source: Bloomberg, Emirates NBD Research.

We are targeting an end of year GBPUSD at 1.35, only moderately higher than the 1.33-34 where it will end 2025.

Commodity currencies to pull higher while CHF flat

In commodity currencies, central banks look to have brought their rate cuts to an end and 2026 will likely be characterized by extended holds to policy or commentary that prepares markets for rates to move higher in the medium term. For CAD, AUD and NZD we expect relative outperformance to the US dollar.

We see no immediate change in policy for the Swiss National Bank which took rates to 0% in June 2025. Inflation in Switzerland has remained low, holding either side of 0% for much of 2025 with the focus for the economy much more on how Switzerland navigates the impact of US tariffs. The Swiss franc will continue to serve as a haven currency and may strengthen during periods of strain in the market. But on a fundamental basis alone we are neutral on CHF and expect it to end 2026 at around USDCHF 0.81.

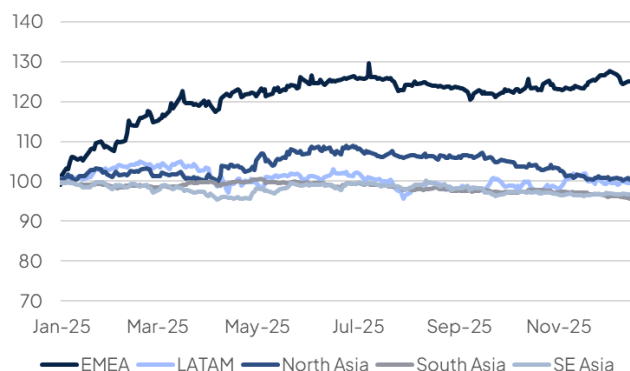
EM FX withstanding challenges

Emerging market FX held up relatively well in 2025 notwithstanding the challenge imposed across many economies by the imposition of US tariffs. Strong appreciations in markets like RUB, ZAR, MXN and BRL helped to keep our overall EM FX index relatively steady while CNY managed gains of a bit less than 4% since the start of the year.



Now that the threat of tariffs and trade disruptions are in the base, or at least part of the 'known unknowns', EM FX will be much more dependent on the specific economic cycles at play in individual economies.

EM FX shows resilience amid tariff challenges



Source: Bloomberg, Emirates NBD Research. Note: Jan 1 2025 = 100; weighted by nominal GDP in USD terms.

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FX Forecasts - Majors

	16-Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
EUR / USD	1.1752	1.18	1.20	1.20	1.21
USD / JPY	154.83	153.00	150.00	145.00	140.00
USD / CHF	0.7963	0.80	0.80	0.81	0.81
GBP / USD	1.3363	1.33	1.34	1.34	1.35
AUD / USD	0.6633	0.67	0.69	0.70	0.70
NZD / USD	0.5776	0.59	0.59	0.60	0.62
USD / CAD	1.3769	1.39	1.38	1.38	1.35
EUR / GBP	0.8794	0.89	0.90	0.90	0.90
EUR / JPY	181.96	180.54	180.00	174.00	169.40
EUR / CHF	0.9358	0.94	0.96	0.97	0.98

FX Forecasts - EM

	16-Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
USD / SAR	3.7522	3.75	3.75	3.75	3.75
USD / AED	3.6728	3.67	3.67	3.67	3.67
USD / KWD	0.3068	0.30	0.30	0.30	0.30
USD / OMR	0.3850	0.39	0.39	0.39	0.39
USD / BHD	0.3770	0.38	0.38	0.38	0.38
USD / QAR	3.6452	3.64	3.64	3.64	3.64
USD / INR	90.9287	90.00	90.50	90.50	90.75
USD / CNY	7.0430	7.05	7.03	7.00	7.00
USD / SGD	1.2911	1.30	1.29	1.29	1.28



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