

## Emerging economies in 2026: toward further central bank rate cuts and capital inflows

11/01/2026

Confidential

---

### Summary

*The accommodative monetary policies observed in most emerging countries in 2025 are expected to continue in 2026, although situations vary significantly from one country to another. The median expected decline in key interest rates in 2026 is estimated at around 50 basis points, which is about half the decline observed in 2025. Last year, these monetary easing measures were made possible mainly by disinflationary dynamics, driven by lower global food and oil prices and the depreciation of the dollar.*

*In the first half of 2026, assuming no major external shocks, favourable external financial conditions are expected to continue to encourage capital inflows, following a record year in 2025. As the expected total decline in the Fed's key interest rate (50 bp) in 2026 is similar to the decline in emerging countries, the yield spread will remain significantly in favour of the latter. Moreover, for some countries, the slowdown in inflation could widen the real interest rate differential with the United States. Finally, the expected further decline in the dollar would also contribute to the continuation of this trend.*

*In addition, in the longer term, the structural improvement in the competence of the central banks of some of these countries, by improving the conduct of monetary policy, is also helping to support these capital flows. Greater independence, the adoption of inflation targeting regimes that help anchor expectations, and the use of unconventional monetary policy instruments have strengthened the credibility and effectiveness of central banks, thereby reassuring foreign investors.*

*This increase in competence partly explains why emerging countries taken as a whole are now less exposed than before to unexpected changes in US monetary policy: domestic monetary policy shocks now play a predominant role in determining bond yields, while the influence of US monetary shocks appears weaker and mainly concentrated on risky assets.*

---

## 1. The cycle of monetary easing observed in most emerging countries in 2025 is expected to continue in 2026

1.1. In 2025, central banks in most emerging countries eased their monetary policy, in line with expectations at the beginning of 2025

During 2025, **a large majority of central banks in emerging countries lowered their key interest rates**. Of the 23 emerging countries we analysed<sup>1</sup>, **the median decline in 2025 was -100 basis points (bp)**, compared with "only" -50 bp in 2024 and an increase of +75 bp in 2023.

In fourteen of these twenty-three emerging countries, **central banks behaved roughly as expected at the beginning of last year by the consensus of forecasters** (which had anticipated a median decline of 75 bp). Although these central banks have deviated little from the anticipated trajectory – even if some have eased their monetary policy more than expected – there has been **heterogeneity in the pace and scale of the rate cuts recorded during the year among these countries**.

	Inflation		Key interest rate					Anticipated changes between now and end of 2026 (bp) <sup>3</sup>
	2025 (%)	Target <sup>2</sup> (%)	End of 2025 (in %)	Change in 2025 (bp)	Forecasts as of 01/01/2025 (%)	Deviation from expectations in 2025 (bp)		
<b>Vietnam</b>	3.5	4.5 – 5.0	4.5	0	4.45	5	-14	
<b>Chile</b>	3.4	3.0	4.5	-50	4.45	5	-21	
<b>Malaysia</b>	1.4	n/a	2.75	-25	3.05	-30	-8	
<b>South Korea</b>	2.3	2.0	2.5	-50	2.30	20	-20	
<b>Peru</b>	1.5	2.0	4.25	-75	4.35	-10	-22	
<b>Thailand</b>	-0.5	5.0	1.25	-100	1.95	-70	-20	
<b>South Africa</b>	3.5	3.0	6.75	-100	7.0	-25	-50	
<b>Philippines</b>	1.8	3.0	4.5	-125	5.0	-50	-25	
<b>India</b>	0.7	4.0	5.25	-125	5.75	-50	-11	
<b>Indonesia</b>	2.9	2.5	4.75	-125	5.25	-50	-51	
<b>Poland</b>	2.4	2.5	4	-175	4.80	-80	-46	
<b>Kenya</b>	4.5	5.0	9	-225	9.90	-90	-67	
<b>Russia</b>	6.6	4.0	16	-500	16.90	-90	-392	

Some countries in Latin America (Chile, Peru) and Asia (Malaysia, South Korea, Thailand) saw moderate declines (up to 100 basis points) in their key interest rates during 2025. These moderate declines can be explained by inflation levels and inflation expectations that are close to (Chile<sup>4</sup>, and South Korea)

<sup>1</sup> Note: our sample of emerging countries comprises countries in Latin America, Africa, Eastern Europe and Asia. These 23 emerging countries are those for which forecasts are available on Bloomberg.

<sup>2</sup> Note: targets are either taken from Z. Zhang's database, drawn from the article "Does inflation targeting track record matter for asset prices? Evidence from stock, bond, and foreign exchange markets", or directly from the websites of the central banks.

<sup>3</sup> Note: the forecasts are dated 1 January 2026.

<sup>4</sup> [Chile Interest Rate](#), [Trading Economics](#), 10/2025

or slightly below (Thailand and Peru) **the targets set by central banks, as well as satisfactory growth levels that have been less affected than expected by the new US trade policy.**

Other countries, such as **South Africa (-100 bps in 2025)**, the **Philippines, India and Indonesia (-125 bps each in 2025)**, as well as **Poland (-175 bps)**, experienced **more significant monetary easing in 2025**.

In **South Africa**, this is mainly due to a **favourable inflationary trajectory<sup>5</sup>**, in a context where the central bank has lowered its inflation target (to 3%, with a tolerance margin of plus or minus one percentage point)<sup>6</sup>.

In the **Philippines** and **Indonesia**, the cuts in key interest rates in 2025 are part of a cycle of monetary easing that began in the third quarter of 2024.

The **Philippine central bank, which lowered its key rate again in December 2025**, has reduced it by a **total of 200bp since August 2024**. This cut has **been** made possible by a context of **controlled inflation (1.8%, below the 3% target)**.

**After a 125bp cut since the beginning of the year, the Indonesian central bank decided to keep its interest rate unchanged in October and November 2025, while inflation is expected to remain within the target range in the short term, supported by a stable rupee and measures to support economic growth<sup>7</sup>.**

**In India, the cycle of rate cuts only began at the start of 2025<sup>8</sup>**. Here too, successive cuts, driven by historically low inflation and favourable expectations, **are enabling the central bank to provide further support to the economy<sup>9</sup>**.

The situation is similar in **Poland**: in December 2025, the central bank **decided on its sixth rate cut since May (175 bp in total), with the aim of supporting growth in an environment where inflation remains below target<sup>10</sup>**.

In other countries such as **Kenya and Russia**, where **large rate cuts were anticipated at the beginning of last year, these have now materialised (225 bp and 500 bp respectively in 2025)**.

In **Kenya**, these rate cuts were driven by **inflation below the central bank's target (4.5% vs. 5%) and a desire to support growth through bank lending<sup>11</sup>**. While the growth outlook is stable at around 5%, **the high level of uncertainty surrounding global trade policy, geopolitical tensions and, in particular, the potential impact of future droughts on agriculture pose certain risks<sup>12</sup>**, in a context where the authorities will begin negotiating a new programme with the IMF in early 2026<sup>13</sup>.

**In Russia, after a period of monetary contraction aimed at curbing inflation – which peaked at 10.3% year-on-year in March 2025 – and stabilising the rouble, the central bank began easing its monetary policy in June 2025**. The key interest rate has thus fallen from its wartime high of **21% to 16%** in December 2025. **This rapid decline in rates has been made possible by a faster-than-expected slowdown in inflation**, although it remains above its target (6.6% compared to a target of 4%). However, this rate cut is not expected to be sufficient to enable an immediate recovery in growth: 0.8% growth is projected for 2025 and 1.2% for 2026<sup>14</sup>.

<sup>5</sup> [South Africa Interest Rate](#) , *Trading Economics*, 20/11/2025

<sup>6</sup> [South Africa: Staff Concluding Statement of the 2025 Article IV Mission](#) , *IMF*, 06/12/2025

<sup>7</sup> [Indonesia Interest Rate](#) , *Trading Economics*, 11/2025

<sup>8</sup> [Good days for home loan borrowers: EMIs to drop further after RBI cuts repo rate](#) , *The Economic Times*, 4 December 2025

<sup>9</sup> [Changes to India's repo rate since June 2000](#) , *Reuters*, 05/12/2025

<sup>10</sup> [Poland Eases Monetary Policy with Sixth 2025 Rate Cut](#) , *Trading Economics*, 03/12/2025

<sup>11</sup> [Kenya's central bank cuts key rate again to spur bank lending](#) , *Reuters*, 09/12/2025

<sup>12</sup> [Kenya Cuts Interest Rate to 9% in Record Easing Streak](#) , *The Kenyan Wallstreet*, 15/12/2025

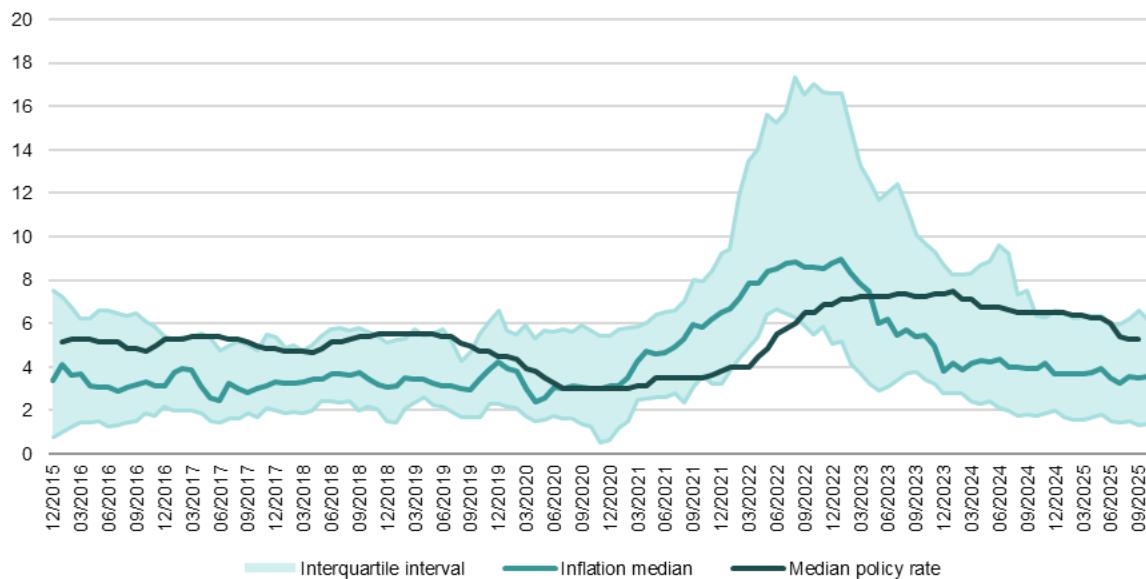
<sup>13</sup> [Kenya expects more IMF programme talks during January staff visit](#) , *Reuters*, 10/12/2025

<sup>14</sup> [Russian central bank expected to cut key rate by 50 bps to 16% at December meeting](#) , *Reuters*, 03/12/2025



Thus, **these monetary easing measures came alongside a disinflationary trend that continued in 2025** (see Figure 1). **This is evidenced by the decline in food prices** – which account for an average of 29% of the CPI basket in the emerging countries studied – **during the first three quarters of 2025**. Food prices fell by 1% in the third quarter of 2025 (quarter-on-quarter) and **were 5% lower than in the previous year**, driven by a sharp decline in cereal prices (rice, wheat, maize) against a backdrop of abundant global supply, as well as other food products (sugar, fruit), which offset the slight increase in the prices of oils and flours<sup>15</sup>.

**Figure 1 – Inflation, median and interquartile range, and median policy rate in our panel of emerging countries<sup>16</sup>**



Source: Statistical offices of the respective countries, LSEG, GSA calculations

This disinflation was also driven by the continued decline in global oil prices and a shift in Chinese exports, causing an influx of low-cost goods<sup>17</sup>.

Indeed, **oil prices** – which account for less than 10% of the CPI basket in emerging market – **fell in 2025** (see Figure 2) due to **persistent trade tensions and an imbalance between strong production growth** (increase in OPEC+ production targets) and **sluggish consumption growth** (slowdown in Chinese demand)<sup>18</sup>.

**Furthermore, external financial conditions remained favourable, with an increase in capital flows** (see section 2) contributing to an appreciation of emerging market currencies against the **US dollar** (see Figure 3)<sup>19</sup>.

**The dollar depreciated due to uncertainty generated by Donald Trump's tariff announcements, doubts about its status as a safe haven, concerns about the debt induced by the "Big Beautiful Bill", and the Fed's rate cuts<sup>20</sup>.**

<sup>15</sup> Commodity Markets Outlook, World Bank, 10/2025

<sup>16</sup> This panel comprises 32 countries. The 23 countries cited in the tables in this study, as well as China, Bangladesh, Qatar, the United Arab Emirates, Saudi Arabia, Egypt, Morocco, Angola and Bulgaria.

<sup>17</sup> Monetary policy: what now?, BNP Paribas, 25/09/2025

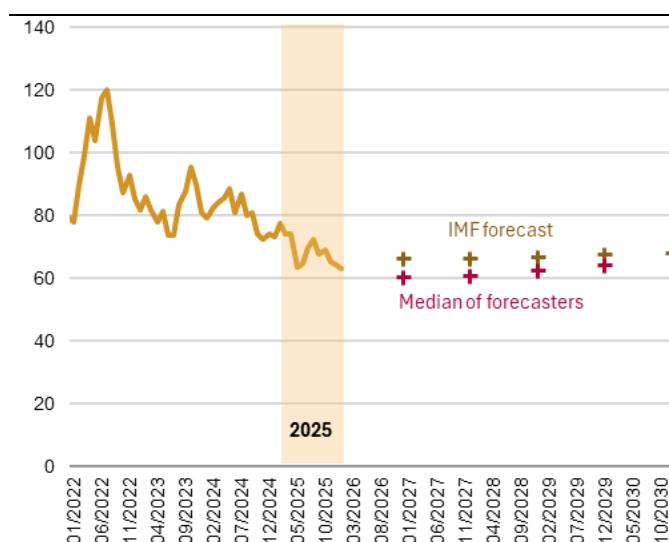
<sup>18</sup> Oil Market Glut: Rising Supply and Slowing Demand Shape 2025 Outlook, World Bank Blogs, 04/11/2025

<sup>19</sup> Monetary Policy: What Now?, BNP Paribas, 25/09/2025

<sup>20</sup> Why the U.S. Dollar Is Depreciating in 2025 and What It Means for You, HUDSON Financial Partners, 21/10/2025

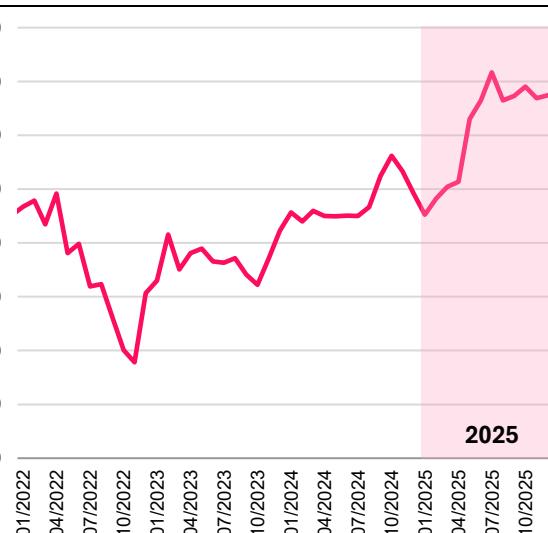
By reducing import costs, **this appreciation of emerging market currencies against the dollar contributed to disinflation and gave central banks more leeway to lower interest rates<sup>21</sup>**. An IMF study shows that, on average, in emerging economies, the transmission of the exchange rate to consumer prices is 22%<sup>22</sup>.

**Figure 2 – Oil prices (Brent, USD/barrel) and forecasts for the coming years**



Source: Energy Information Administration, United States, IMF, Bloomberg

**Figure 3 – Evolution of a basket of 25 emerging market currencies against the dollar<sup>23</sup>**



Source: MSCI

1.2. For some countries, such as Turkey, Argentina and Nigeria, key interest rate cuts were not as sharp as anticipated at the beginning of 2025

In Turkey, Argentina, Nigeria, Colombia and, to a lesser extent, Hungary and Romania, monetary easing in 2025 was significantly less than anticipated.

	Inflation		Key interest rate				
	2025 (%)	Target (%)	End of 2025 (in %)	Change in 2025 (bp)	Forecasts as of 01/01/2025 (in %)	Deviation from expectations in 2025 (bp)	Anticipated changes between now and end of 2026 (bp)
<b>Turkey</b>	30.9	5.0	38	<b>-950</b>	31.1	690	-909
<b>Argentina</b>	31.4	5.0	29	<b>-300</b>	24.3	475	-650
<b>Nigeria</b>	14.5	n/a	27	<b>-50</b>	22.7	435	-700
<b>Colombia</b>	5.3	3.0	9.25	<b>-25</b>	6.8	250	-18
<b>Hungary</b>	3.8	3.0	6.5	<b>0</b>	5.25	125	-78
<b>Romania</b>	9.8	2.5	6.5	<b>0</b>	5.35	115	-106

<sup>21</sup> Monetary policy: what now?, BNP Paribas, 25/09/2025

<sup>22</sup> Non-Linear Exchange Rate Pass-Through in Emerging Markets, IMF, 2016

<sup>23</sup> Note: each currency is weighted equally to its country's weighting in the MSCI Emerging Markets Index.

With regard to Turkey and Argentina, **although the monetary easing measures in 2025 are among the most significant in the emerging markets, at -950 bp and -300 bp respectively in 2025, they are still far from what the markets had anticipated at the beginning of the year**: the latter had forecast an additional decline of **690** basis points in Turkey and **475** basis points in Argentina. In addition to the persistent fragility of their external accounts and therefore their currencies, these differences can be explained by **slower-than-expected disinflation** in 2025, forcing both central banks to moderate their easing, or even to halt it, as evidenced by **the 350 bp rise in the key interest rate in April 2025 in Turkey and the maintenance of the key interest rate at 29% in Argentina since January 2025**. In both countries, inflation at the end of 2025 (30.9% year-on-year in Turkey and 31.4% in Argentina) **remains well above the targets set by the central banks** (5% in both cases), and even above Turkey's year-end target (24%)<sup>24</sup>. At the end of 2025, this persistent inflation can be explained in Turkey by an increase in the cost of services (school fees and school bus fares)<sup>25</sup> and in Argentina by a rise in the price of beef<sup>26</sup>. Furthermore, since May 2025, the Central Bank of Argentina has decided that its interest rates will be determined by supply and demand<sup>27</sup>.

**In Nigeria and Colombia, key interest rates were eased only once in 2025: by 50 basis points in September in Nigeria and by 25 basis points in May in Colombia.** These relatively moderate cuts **contrast with expectations at the beginning of the year**, which predicted easing of **485** basis points in Nigeria and **275** basis points in Colombia in 2025.

In Nigeria, the decision to keep the key interest rate unchanged for most of the year, and then since September after the first cut, **is explained by the desire to consolidate the progress made in terms of disinflation**<sup>28</sup>. Indeed, inflation fell for the eighth consecutive month in November 2025, from 24.2% in March to 14.5%<sup>29</sup>. For 2026, the Central Bank of Nigeria **has set an inflation target of 16.5% (+/- 2%), with the aim of reaching 13% in 2027**, thus formalising its transition to an inflation targeting framework<sup>30</sup>.

In Colombia, **it is also the risks of a resurgence of inflation, which remains above the central bank's target** (5.3% year-on-year in November 2025 for a target of 3.0%), **that have led the central bank to keep its key interest rate unchanged since May 2025**. Inflation **rose again between June and October 2025**, from 4.8% to 5.5%. Furthermore, the government's suspension of the fiscal rule, which imposes institutional constraints to protect public finances, and its increase in the deficit target (from 5.1% to 7.1% in 2025) are also sources of risk<sup>31</sup>.

Finally, in **Romania and Hungary, key interest rates remained unchanged throughout 2025, at 6.5% in both countries, while the markets had expected cuts of 115 bp and 125 bp respectively in 2025**. In both countries, this lack of reduction can be explained by inflation remaining above the target set by the central banks, although in Hungary it is closer to the target (3.8% year-on-year in November 2025 for a target of 3%) than in Romania (9.8% in November for a target of 2.5%). Furthermore, in Hungary, **the central bank also cites currency stability as a reason for keeping rates unchanged**<sup>32</sup>. In Romania, **inflation reached one of its highest levels in two years in November, driven by a series of tax increases and austerity measures implemented to reduce a budget deficit exceeding 9% of GDP**, the highest in the European Union<sup>33</sup>.

<sup>24</sup> [Turkey Interest Rate](#) , *Trading Economics*, 12/2025

<sup>25</sup> [Turkey's central bank cuts key rate by 100 basis points to 39.5 per cent](#) , *Turkish Minute*, 23/10/2025

<sup>26</sup> [Argentina monthly inflation pushed up by higher beef prices in November: Reuters poll](#) , *Reuters*, 10/12/2025

<sup>27</sup> [Argentina's Central Bank announces plan to stop deciding interest rates](#) , *Buenos Aires Herald*, 14/05/2025

<sup>28</sup> [Nigeria's central bank holds key rate, wants inflation to fall further](#) , *Reuters*, 25/11/2025

<sup>29</sup> [Nigeria Interest Rate](#) , *Trading Economics* 25/11/2025

<sup>30</sup> [Nigeria Central Bank Targets 16.5% Inflation in 2026 Under New Framework](#) , *Bloomberg*, 30/12/2025

<sup>31</sup> [Colombia central bank holds rate at 9.25% amid fiscal uncertainty, inflation](#) , *Reuters*, 27/06/2025

<sup>32</sup> [National Bank of Hungary Review: Plenty of reasons to sit tight | articles](#) , *ING Think*, 21/10/2025

<sup>33</sup> [Romania Inflation Rate](#) , *Trading Economics*, 12/11/2025



### 1.3. In Ghana, Mexico and Pakistan, the rate cuts decided by the central banks were greater than expected

**Ghana, Mexico and Pakistan** are the only three emerging countries in our study sample to have experienced more significant monetary easing in 2025 than what had been anticipated at the beginning of the year.

	Inflation		Key interest rate				
	2025 (%)	Target (%)	End of 2025 (in %)	Change in 2025 (bp)	Forecasts as at 01/01/2025 (%)	Deviation from expectations in 2025 (bp)	Anticipated changes between now and end of 2026 (bp)
<b>Mexico</b>	3.8	3.0	7	-300	8.50	-150	-50
<b>Ghana</b>	6.3	8.0	18	-900	19.50	-150	-417
<b>Pakistan</b>	5.6	5.0 – 7.0	10.5	-250	13.35	-285	-170

In Mexico, the key interest rate fell by 300 basis points in 2025, 150 basis points more than anticipated at the start of the year. This sharper fall in rates can be explained by inflation close to its target (3.8% year-on-year in November 2025 for a target of  $3\% \pm 1$  percentage point)<sup>34</sup> as well as the desire to support sluggish economic growth<sup>35</sup> : +0.7% growth is expected in 2025, affected by the slowdown in real wage growth and the decline in remittances from abroad<sup>36</sup>.

Ghana, meanwhile, is the emerging country that experienced the strongest monetary easing in 2025, with a decline of 900 basis points, i.e 150 basis points more than forecasters had anticipated at the beginning of the year. This sharp decline can be explained by faster-than-expected disinflation (from 23.5% in January to 6.3% in November). The strong performance of the external sector, which helped to stabilise the currency, and moderate imported inflation also contributed to this<sup>37</sup>.

Finally, in Pakistan, the key interest rate has fallen by 250 basis points since the beginning of 2025, whereas expectations predicted a rise of 35 basis points at the beginning of the year. This gap between expectations and reality can be explained by inflation remaining within the range set by the central bank. However, despite this controlled inflation, the central bank did not continue its easing policy, keeping its key interest rate unchanged for four consecutive meetings, as the short-term macroeconomic outlook deteriorated slightly following the floods, raising the risk of a rise in inflation<sup>38</sup>. Finally, in December, the Pakistani central bank lowered its key rate by an additional 50 basis points following the IMF's approval of a \$1.2 billion disbursement, which brought foreign exchange reserves to over \$15.8 billion and enabled the government to service its debt, while providing room for manoeuvre to support monetary policy<sup>39</sup>.

### 1.4. Brazil is the only emerging country to have pursued a restrictive monetary policy in 2025

Brazil is the only emerging country among the 23 countries we analysed to have pursued a restrictive monetary policy in 2025. This monetary tightening, which began in September 2024, follows a period of post-pandemic easing. In 2025, the central bank's key interest rate rose by 275 basis points, from 12.25% at

<sup>34</sup> [Mexico Inflation Accelerated Ahead of Banxico Rate Meeting](#), Bloomberg, 09/12/2025

<sup>35</sup> [Monetary Policy Statement](#), Banco de Mexico, 08/08/2025

<sup>36</sup> [Mexico's economy surprises to the upside, but outlook is weak](#), Dallas Fed, 16/10/2025

<sup>37</sup> [Ghana Monetary Policy November 2025](#), Focus Economics, 24/11/2025

<sup>38</sup> [Pakistan central bank holds interest rate at 11% for fourth time in a row](#), Reuters, 27/10/2025

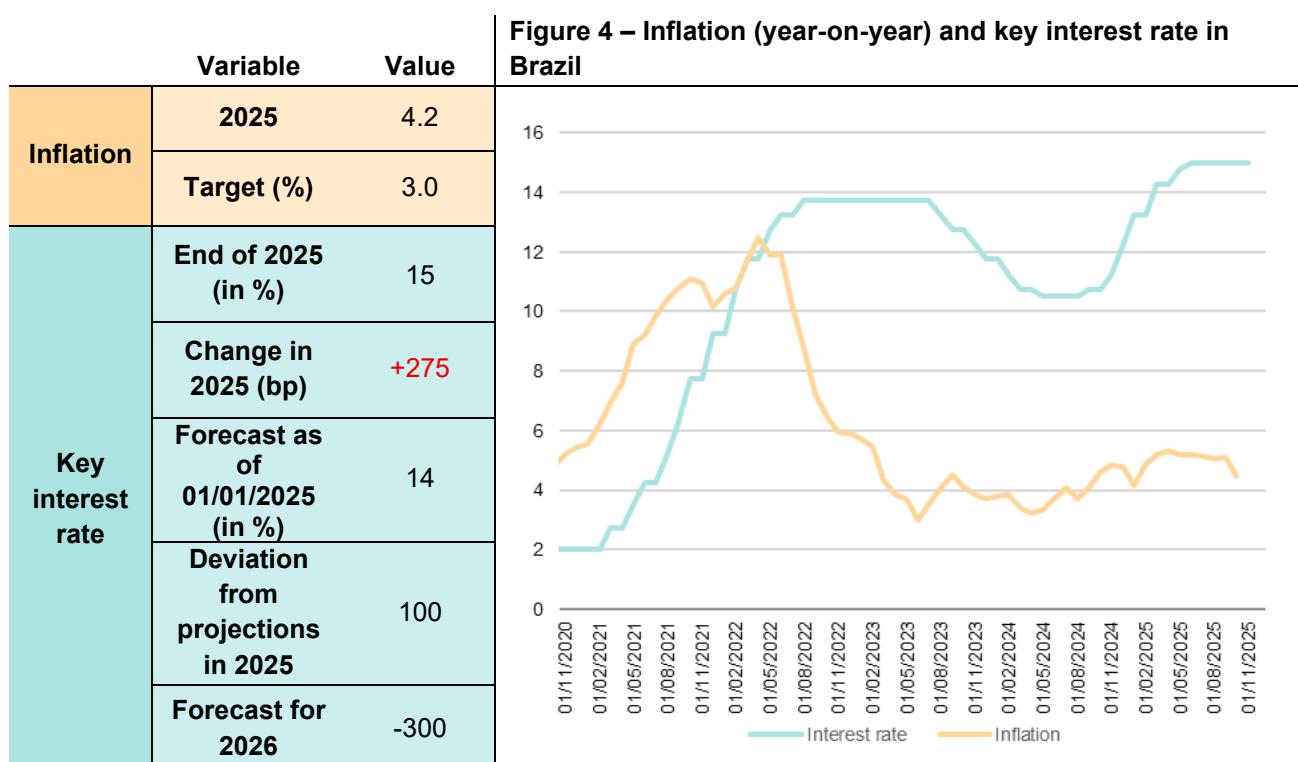
<sup>39</sup> [Pakistan Interest Rate](#), Trading Economics, 15/09/2025



the beginning of January 2025 to 15% in June. These decisions were justified by the need to bring inflation and inflation expectations back to their 3% target<sup>40</sup>. Inflation stood at 4.2% in November, down slightly from the previous month but still above the target set for this year<sup>41</sup>. This is mainly due to the Brazilian currency remaining weak against the dollar, despite the favourable trend in external accounts in recent years. The high budget deficit continues to worry international investors, limiting portfolio inflows.

**However, since July 2025, the Brazilian central bank has chosen to keep its key interest rate unchanged, judging that maintaining the interest rate at its current level over an extended period would be sufficient to ensure that inflation converges towards the 3% target<sup>42</sup>.** Furthermore, according to the IMF, while monetary policy transmission remains effective, **credit growth has been strong in recent years**. The Fund explains this dichotomy by both **cyclical factors** (faster-than-expected growth, low unemployment and rising incomes stimulating demand for credit) and **structural changes** (improved financial inclusion and credit availability)<sup>43</sup>. **Thus, it is also possible that the Brazilian central bank is still adjusting its monetary policy to this new equilibrium.**

Using the 12-month inflation expectations published by the Brazilian central bank<sup>44</sup>, we have constructed three scenarios: **an optimistic scenario**, which uses the minimum inflation rate (scenario 1); **a central scenario**, which uses the median inflation rate (scenario 2); and a **pessimistic scenario**, based on the maximum inflation rate predicted by the survey (scenario 3). We then constructed the **projections for the central bank's key interest rate based on these three scenarios, applying a Taylor rule<sup>45</sup>** (see Figure 5).



Source: *Brazilian Institute of Geography and Statistics and Central Bank of Brazil*

<sup>40</sup> [Brazil central bank holds rates, signals confidence in maintaining stance](#) , *Reuters*, 5 November 2025

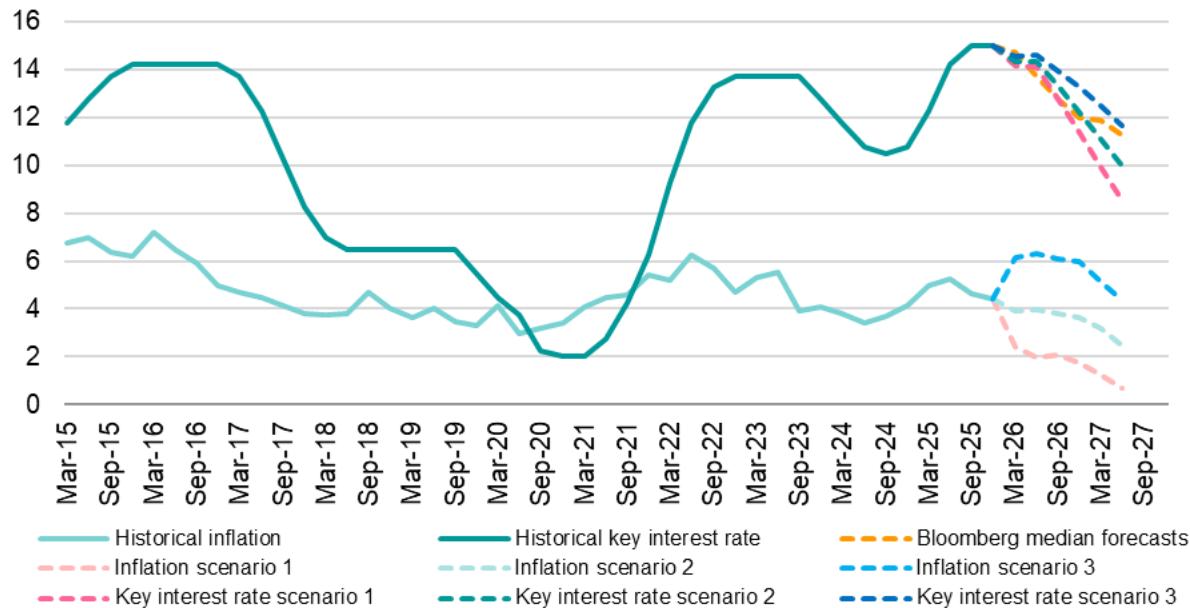
<sup>41</sup> [Explaining Strong Credit Growth in Brazil Despite High Policy Rates](#) , *IMF*, 9 October 2025

<sup>42</sup> [Brazil central bank holds rates, signals confidence in maintaining stance](#) , *Reuters*, 05/11/2025

<sup>43</sup> [Explaining Strong Credit Growth in Brazil Despite High Policy Rates](#) , *IMF*, 09/10/2025

<sup>44</sup> [Market Expectations System](#), *Central Bank of Brazil*

<sup>45</sup> Note: the Taylor rule determines the central bank's interest rate response based on the difference between inflation expectations and the inflation target. We have used the Brazilian central bank's version of this rule.

**Figure 5 – 12-month inflation expectations and Selic rate forecasts according to three inflation expectation scenarios**

Source: Banco do Brasil, Bloomberg, GSA calculations

**In the central scenario, the Selic rate would begin to fall in the first quarter of 2026 and reach 10% in the second quarter of 2027. In the pessimistic scenario, in which inflation expectations rise to 6.3%, the Selic rate also falls from Q1 2026, but only to 11.7%, which is 1.7 percentage points higher than in the central scenario.**

### 1.5. Monetary easing in emerging countries is expected to continue in 2026

**In 2026, forecasters generally expect monetary easing measures to continue.** However, the extent of the reduction in key interest rates would be more limited than that observed in 2025<sup>46</sup>. While the average decline expected in 2026 is 180 basis points – comparable to that observed in 2025 – the median decline anticipated by forecasters is only 51 basis points, or about half the median decline in 2025. In 2023 and 2024, the median changes in key interest rates were -50 bps and +75 bps, respectively.

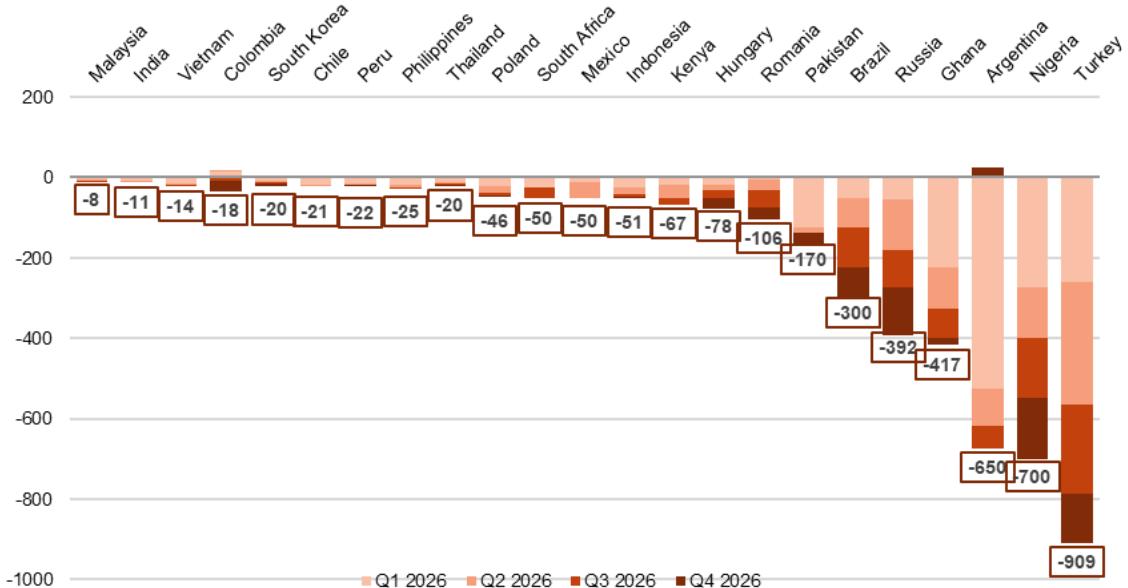
Furthermore, these easing measures are far from uniform across emerging countries. While the market anticipates very sharp declines in key interest rates for countries such as **Turkey** (-909 basis points expected in 2026), **Nigeria** (-700 bp) and **Argentina** (-650 bp), monetary easing is likely to remain very moderate in some countries, such as the **Philippines** (-25 bp) and **Thailand** (-45 bp).

These likely differences in the size of rate cuts can be explained by uneven disinflation rates and staggered easing cycles<sup>47</sup>. For example, countries such as Brazil and Hungary are expected to begin their monetary easing cycles in 2026, while in several Asian countries inflation is already at historically low levels and could even start to rise again, particularly in **India**<sup>48</sup> (4.4% expected at the end of 2026, see Figure 7).

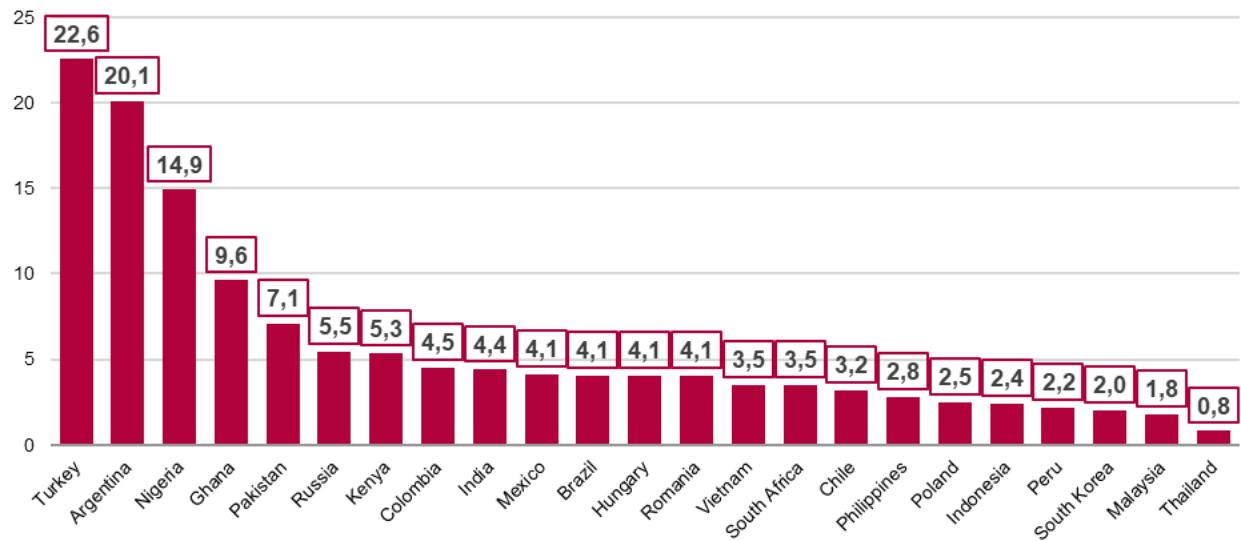
<sup>46</sup> Monetary policy: what now?, BNP Paribas, 25/09/2025

<sup>47</sup> Monetary policy: what next?, BNP Paribas, 25/09/2025

<sup>48</sup> Monetary policy: what next?, BNP Paribas, 25/09/2025

**Figure 6 – Anticipated changes in key interest rates for a selection of emerging countries in 2026**

Source: Bloomberg

**Figure 7 – Inflation expectations for Q4 2026 in selected emerging countries (year-on-year)**

Source: Bloomberg

It is interesting to note that the countries for which rate cuts are most strongly anticipated in 2026 **are also those where inflation is expected to be highest at the end of that year**, notably Turkey, Argentina and Nigeria. This situation can be explained by the fact that inflation is currently very high in these countries and that the levels anticipated for the end of 2026 already correspond to significant declines (-9 percentage points in Turkey and -11.3 percentage points in Argentina). In Nigeria, the anticipated decline in rates despite inflation that is not expected to fall could be explained by a still very high level of monetary tightening at the end of 2025 – with the key rate reaching 27% – so that a gradual easing would not cause inflation to pick up again.

**The trend is unlikely to be uniform: rising political uncertainty, linked in particular to elections in 2026 (April in Peru, May in Colombia and Vietnam, November in the United States), as well as the worsening of certain budgetary vulnerabilities, could increase the volatility of capital flows and multiply episodes of downward pressure on certain emerging market currencies<sup>49</sup>.**

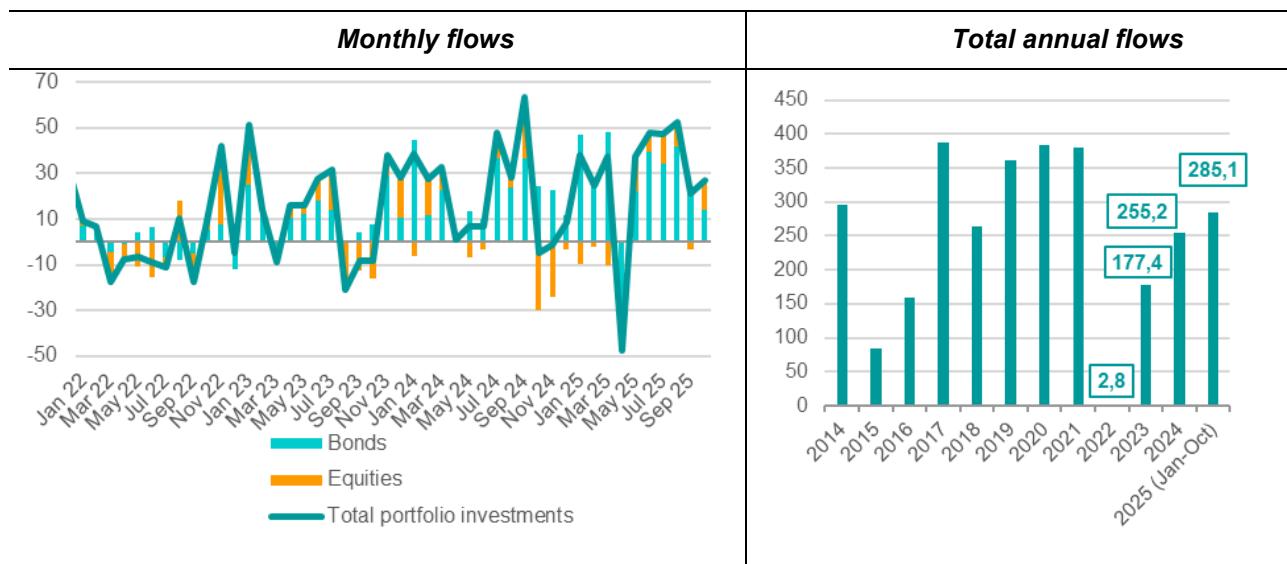
## 2. Interest rate cuts in emerging countries were accompanied by an influx of capital

### 2.1. Record capital inflows in 2025, underpinned by renewed interest in emerging market assets and a weak US dollar

#### 2.1.1 Rising portfolio investment amounts

The year 2025 was marked by a resurgence investment momentum in emerging markets. **Net portfolio investment in particular saw only positive months in 2025, with the exception of April 2025**, according to data from the *Institute of International Finance* (IIF) tracker. Net portfolio investment inflows to the 37 emerging countries covered amounted to US\$285 billion in the first 10 months of the year, compared with US\$255 billion for the whole of 2024. This represents a 15% increase year-on-year over 10 months.

**Figure 8 and 9 – Portfolio investment flows to emerging countries**

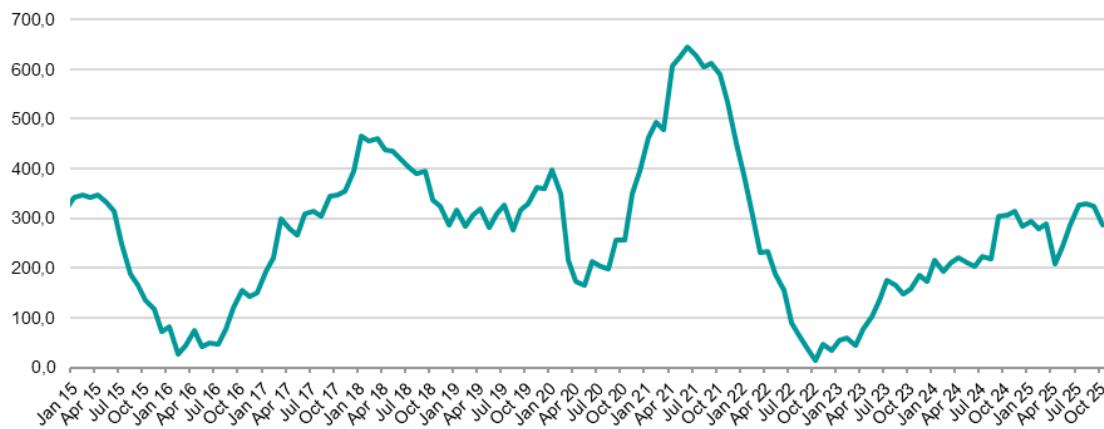


*Note: 37 countries are included: China, India, Indonesia, Korea, Malaysia, Philippines, Thailand, Vietnam, Argentina, Brazil, Chile, Colombia, Mexico, Peru, Costa Rica, Panama, Saudi Arabia, UAE, Qatar, Kuwait, Bahrain, Oman, Czech Republic, Hungary, Poland, Russia, Turkey, Ukraine, Romania, South Africa, Nigeria, Kenya, Ivory Coast, Senegal, Egypt, Morocco, Tunisia.*

Source: IIF

Net investment in emerging countries reached a historic low in 2022 (only +US\$2.8 billion), coinciding with the monetary tightening initiated by the US Federal Reserve (Fed). Since 2022, flows have gradually recovered in 2023, 2024 and 2025 (Figure 9), but remain below the levels seen in 2019 to 2021, when investors, driven by the search for yield in a low-interest rate environment, directed capital massively towards developing countries.

<sup>49</sup> [Monetary policy: what now?](#), BNP Paribas, 25/09/2025

**Figure 10 – Portfolio investment flows to emerging markets (12-month rolling average)**

Source: IIF

### 2.1.2 Local currency assets attractive to certain types of investors due to falling interest rates

The attractiveness of emerging market assets in 2025 is both a cause and, to some extent, a consequence of monetary easing. In these countries, monetary easing has been accompanied by an increase in the value of financial assets.

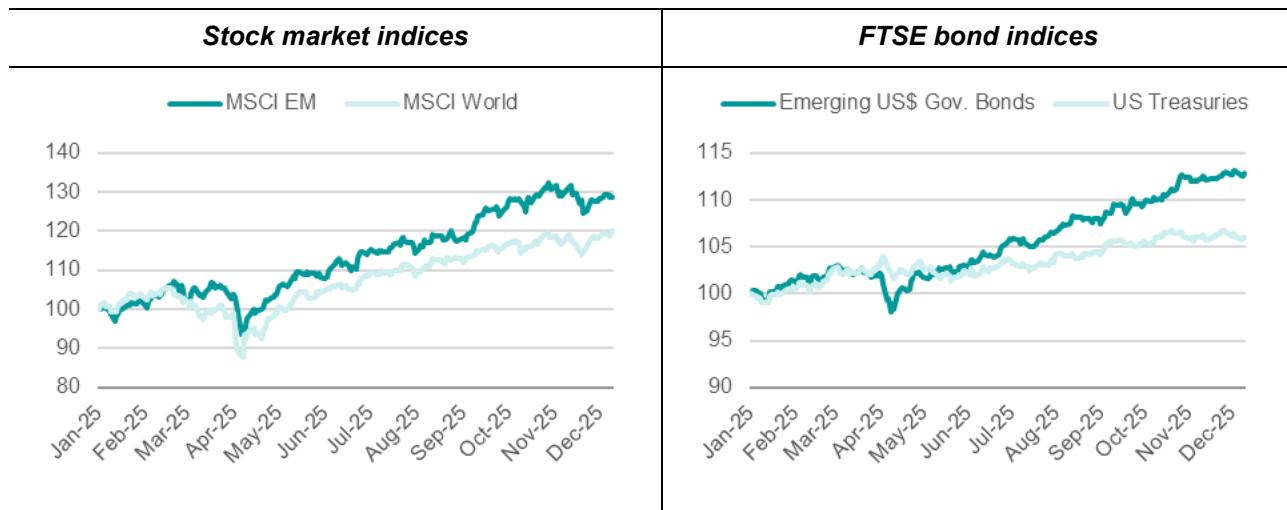
With regard to bonds, **the fall in key interest rates has had an impact on sovereign bond yields, which have fallen, increasing the value of bonds**. This makes these assets attractive to short- to medium-term investors seeking capital gains, such as *mutual funds*. Conversely, for investors focused on carry strategies (holding bonds to maturity), such as pension funds, the attractiveness of local currency bonds increases when the interest rate differential between the United States and emerging countries widens (see below).

For emerging market equities, **the prospect of lower-cost capital due to falling interest rates can boost corporate earnings expectations** and thus the value of equities offering opportunities in local markets.

As a result, financial markets in emerging countries outperformed those in developed countries in 2025. As of 19 December, the MSCI EM, the stock market index reflecting the equity markets of a large number of emerging countries<sup>50</sup>, was up 26% since the 1<sup>st</sup> of January, compared with 18% for the MSCI World, the global index.

With regard to sovereign bond indices, a performance gap in favour of emerging countries can also be observed. Since January, the FTSE index reflecting the performance of emerging market bonds denominated in US dollars has risen by 13%, compared with 6% for US Treasury bonds.

<sup>50</sup> The MSCI EM index covers 1,195 assets across 24 countries. China, Taiwan, India, Korea and Brazil are the most heavily weighted countries.

**Figure 11 and 12 – Stock market and bond index performance, base 100 = January 2025**

Source: LSEG Datastream

### 2.1.3 The depreciation of the dollar also played a key role in the influx of investment

**In 2025, the depreciation of the dollar against most emerging market currencies also played a key role in directing capital towards emerging markets.**

The depreciation of the dollar generally pushes up the valuation of emerging market assets and increases the risk appetite of international investors, who turn more towards these emerging market assets. According to a study by the Bank for International Settlements covering 17 emerging countries with monthly data between 2006 and 2024<sup>51</sup>, fluctuations in the dollar are the dominant factor in investment flows to emerging countries.

**Figure 13 – DXY dollar index**

Source: LSEG Refinitiv

*Note: A decline in the index reflects a decline in the dollar against a basket of global currencies.*

**The effects of the dollar seem to be stronger than those of the VIX volatility index (the most commonly used indicator of global risk appetite) or changes in the interest rate differential with the United States.** A one standard deviation depreciation of the dollar against other advanced economy currencies<sup>52</sup> (equivalent to 9% over the period observed) tends to increase, in the same month, the ratio of local currency bonds and emerging market equities to total assets held by non-residents by 0.29 and 0.16 percentage points, respectively.

<sup>51</sup> The US dollar and capital flows to EMEs, [www.bis.org](http://www.bis.org), 16/09/2024

<sup>52</sup> The authors use the dollar index relative to other advanced economies to avoid endogeneity between exchange rates and investment flows between the United States and emerging markets.

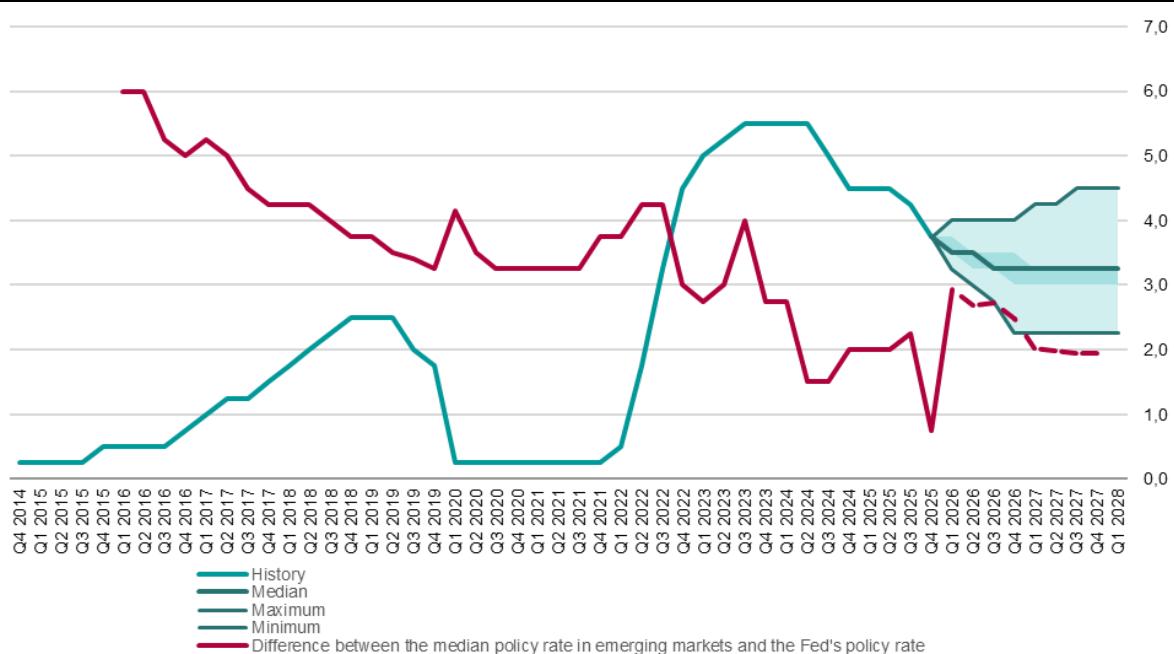
In other words, the simultaneous rise in the value of equities and bonds, and especially the appreciation of emerging market currencies against the dollar, fuelled carry trade investment flows to emerging markets by international investors in 2024. The return on carry trade in 2025 reached its highest level since 2009, according to the Bloomberg *Emerging Market Carry Index*<sup>53</sup>.

## 2.2. A renewed attractiveness that could be confirmed in 2026

### 2.2.1 Real interest rate differentials could widen due to slowing inflation in emerging markets

**In 2026, US Fed rates are expected to be reduced**, in the median scenario of forecasters, twice by 25 bp in 2026 (see Figure 14). This decline means that the interest rate spread with emerging countries will remain unchanged. This trend therefore argues for net investment flows into emerging markets to remain at a fairly high level.

**Figure 14 – Fed decision expectations and spread between the median policy rate in emerging markets and the Fed's policy rate**



Source: Bloomberg

Note: expectations are for the end of 2025

Furthermore, while inflation could remain under pressure in the US in 2026 due to disruptions caused by the application of tariffs, it is slowing or stable in most emerging countries. **As a result, several countries could benefit from an increase in the real interest rate differential with the United States**, such as Argentina, Turkey, Romania, Nigeria, Colombia, and Pakistan, all of which could see this differential widen by several percentage points<sup>54</sup>.

**Moreover, if the dollar remains weak (see below), as expected, exchange rate fluctuations would not offset the widening of real interest rate differentials.** Furthermore, a weak dollar helps to reduce imported inflation and the burden of dollar-denominated debt, which has a positive impact on the credit risk of other countries.

<sup>53</sup> Carry Trade Revival That Electrified EM Spurs 2026 Optimism - Bloomberg, Bloomberg.com, 14/12/2025

<sup>54</sup> Calculations based on interest rate and inflation forecasts aggregated by Bloomberg or, if unavailable, by the IMF.

**It should also be noted that emerging countries' exposure to US shocks is declining.** Indeed, in a study on the impact of US and domestic monetary shocks on financial variables in emerging markets, the IMF shows that domestic shocks have a significantly greater effect on government bond yields than US monetary policy shocks, whose impact is weaker and statistically insignificant. On the other hand, US monetary policy shocks have a more pronounced effect on riskier asset classes, such as stock prices, exchange rates, and credit spreads<sup>55</sup>.

Finally, the IMF also points out that the increased ability of economies to cope with periods of risk aversion, the reduced need to intervene in foreign exchange markets when economic policy frameworks are robust, and evidence of greater autonomy in national monetary policy **indicate a gradual shift toward an international environment that, while remaining heterogeneous across countries, is more akin to the classic Mundell-Fleming trilemma than to the “dilemma” highlighted by Rey (2015)**, in which monetary policy independence can only be preserved at the cost of capital controls<sup>56</sup>.

### 2.2.2 A rebalancing of risk in favour of emerging countries

**In 2025, investors generally perceived an increase in political uncertainty in the United States**, with frequent and unexpected announcements of customs duties, negotiations to replace Fed Chairman Jerome Powell at the end of his term in May 2026 and renewed geopolitical tensions between the United States and other countries around the world (China, Venezuela, South Africa, etc.).

**In Europe, the evolution of risk as perceived by investors has also been generally unfavourable.** The loss of competitiveness of the old continent, particularly in industry, is illustrated by the economic slowdown in Germany (with virtually zero growth expected in 2025, at 0.2%). Political deadlock in France has increased the country's fiscal fragility, causing its sovereign rating to fall by one or two notches to a simple A rating from two of the three main agencies (A+ according to S&P and Fitch, Aa3 according to Moody's<sup>57</sup>). On the eastern fringes of the continent, geopolitical tensions with Russia have increased, and little political progress has been made towards resolving the Russo-Ukrainian conflict.

At the same time, several emerging countries have seen their economic situation normalise after several years of disruption linked initially to the pandemic, inflation and reduced availability of capital in 2022 and 2023. Turkey, for example, has tightened its monetary policy, Nigeria has liberalised its exchange rate and ended costly energy subsidies, Egypt has made progress in its IMF programme, and several countries that have recently undergone sovereign debt restructuring (Ghana, Zambia, Sri Lanka) have seen their sovereign ratings return to an upward trajectory<sup>58</sup>. The end of the 2024 election cycle, in which half of the world's population was called to the polls, has also eased investors' perception of risk.

In this context, risk premiums assigned to emerging countries are falling relative to those of advanced economies. Given the factors underpinning this dynamic, it could continue into 2026, offering emerging countries new opportunities to attract capital.

### 2.2.3 A dollar that remains weak could also drive capital towards emerging countries

For 2026, several banks continue to believe that the dollar remains overvalued and that its weakness could persist into 2026, with the leaving the dollar at or below its current level. ABN Amro estimates that the exchange rate could reach 1.25 EUR/USD by the end of 2026, compared with 1.17 in December 2025<sup>59</sup>.

<sup>55</sup> [Emerging Market Resilience: Good Luck or Good Policies?](#) , IMF, 10/2025

<sup>56</sup> [Emerging Market Resilience: Good Luck or Good Policies?](#) , IMF, 10/2025

<sup>57</sup> As of 6 January 2025

<sup>58</sup> [Reuters, Marvellous emerging markets tipped for another star showing in 2026](#), 19 December 2025

<sup>59</sup> [Dollar weakness will continue in 2026 - ABN AMRO](#) , [www.abnamro.nl](http://www.abnamro.nl), 27 November 2025

In real terms, the consensus among forecasters (median established by Bloomberg) anticipates a prolonged depreciation of the dollar, with the DXY index falling from 98.5 at the beginning of 2026 to 97 in the second half of 2026, close to its 2025 low of 96.6.

Morgan Stanley, for example, believes that further depreciation could mainly occur in the first half of 2026, bringing the DXY dollar index from its current level of 98-100 to 94 in mid-2026, which would be its lowest level since 2021. This trajectory would be explained by a weakening of the US economy (labour market, growth, etc.) and uncertainties about the Fed's governance. The White House's favourite candidate, Kevin Hassett, has indicated his inclination towards extending the cycle of monetary easing<sup>60</sup>. Therefore, if these factors ease in the second half of 2026, the dollar could return to its current level<sup>61</sup>.

This prospect of a weaker dollar could continue to boost the appeal of emerging market assets, particularly those denominated in local currencies, since, conversely, **emerging market currencies could appreciate in 2026, continuing the trend seen in 2025**, as in Mexico and Brazil, which are among the emerging market currencies that appreciated the most in 2025<sup>62</sup> (+16% and +12% between January and December 2025, respectively).

For these countries, however, excessive currency appreciation could have negative effects on the real economy, weaken export competitiveness and hamper economic diversification. Finally, in the event of a sudden and/or massive reversal of this dynamic on the foreign exchange market, there could be a decline in foreign investment, which would be detrimental to emerging countries.

**Box: The structural improvement in the capacities of central banks in emerging countries is enhancing the conduct of monetary policy and contributing to capital inflows**

In emerging economies, **monetary policy management has gradually improved, accompanied by the consolidation of central bank credibility**. Several factors illustrate this increase in central bank expertise.

➤ **Better anchoring of inflation expectations**

Firstly, **since the early 2000s, central banks in emerging economies have introduced inflation targeting rules** (targets or ranges), enabling them to better anchor inflation expectations. For example, out of 33 emerging countries in 2000, only 8 had inflation targeting rules, compared with 32 out of 33 in 2024 (see Figure 15). **The adoption of an inflation targeting regime leads to a significant decline in the transmission between exchange rates and consumer prices** for most emerging countries<sup>63</sup>.

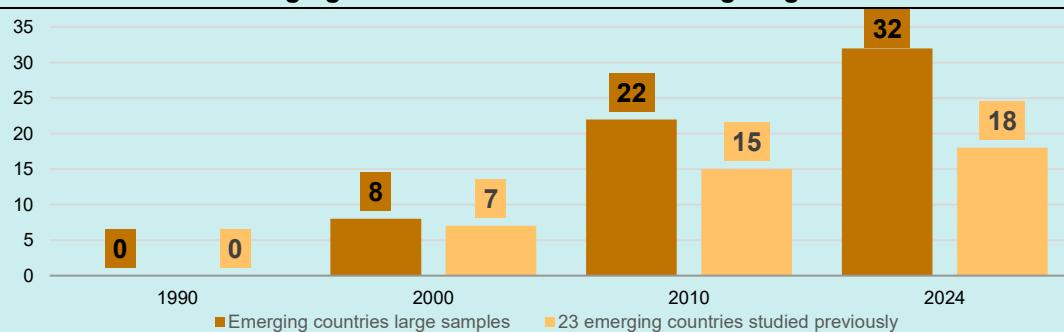
<sup>60</sup> Fed chair front-runner Hassett says 'plenty of room' to cut rates | Reuters, Reuters, 9 December 2025

<sup>61</sup> U.S. Dollar Depreciation Could Deepen Through First Half | Morgan Stanley, Morgan Stanley, 26/11/2025

<sup>62</sup> Wild currency swings put emerging markets in the spotlight | Reuters , Reuters, 15/12/2025

<sup>63</sup> Exchange Rate Pass-through in Emerging Countries: Do the Inflation Environment, Monetary Policy Regime and Institutional Quality Matter? , CEPII, 2016



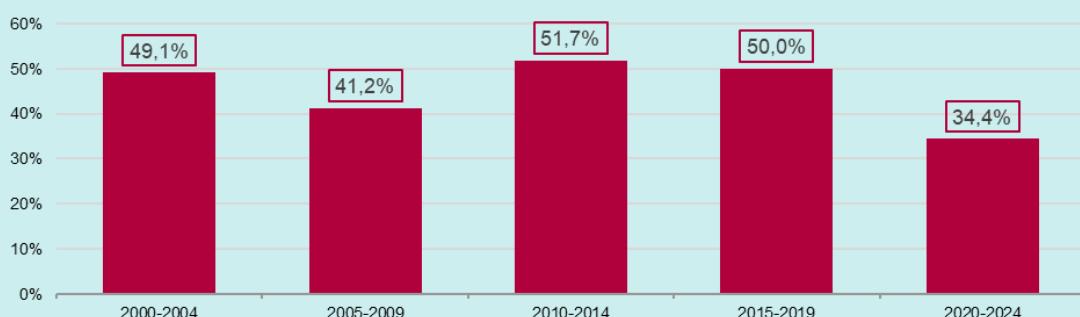
**Figure 15– Number of emerging countries with an inflation targeting rule<sup>64</sup>**

Source: Zhongxia Zhang

Furthermore, an IMF study shows that, since the 2008 economic crisis, **the coefficients associated with inflation in the Taylor rule** – i.e. the central bank's reaction function, which determines decisions to raise or lower interest rates based on inflation expectations, the output gap and the exchange rate – **have declined**. In other words, **central banks now attach less importance to deviations in inflation expectations from the target than before**, probably **due to their increased credibility and more firmly anchored long-term inflation expectations**<sup>65</sup>.

Finally, **the establishment of rigorous frameworks for communicating monetary policy decisions and the rationales behind them reflects this increase in competence among central banks in emerging economies**. For example, many central banks in emerging markets (Thailand, Chile, South Africa and Georgia) have developed sophisticated communication frameworks: regular press conferences, policy statements and monetary policy reports<sup>66</sup>.

Nevertheless, **while the anchoring of inflation expectations has improved, the ability of central banks to keep inflation within the defined target range** (between the lower and upper bounds)<sup>67</sup> **has not really improved** (see Figure 16): on average, between 2000 and 2004, end-of-year inflation was within the target in 49% of cases, compared with an average of 50% between 2015 and 2019 and 34% between 2020 and 2024, a period marked, however, by the Covid-19 crisis and the inflationary consequences of the invasion of Ukraine on food and energy prices.

**Figure 16 – Evolution of central banks' accuracy in meeting their inflation targets**

Source: Zhongxia Zhang

<sup>64</sup> Note: in this graph, the "large sample of emerging countries" group represents a panel of 33 emerging countries. The other sample corresponds to the 23 emerging countries studied in part 1 of this study, with the exception of five countries for which we do not have data. These 18 emerging countries are also part of the "large sample".

<sup>65</sup> [Emerging Market Resilience: Good Luck or Good Policies?](#), IMF, 10/2025

<sup>66</sup> [Emerging Market Resilience: Good Luck or Good Policies?](#), IMF, 10/2025

<sup>67</sup> Note: for the few emerging countries that do not have defined upper or lower bounds, we have set bounds of  $\pm 2$  percentage points around the target.

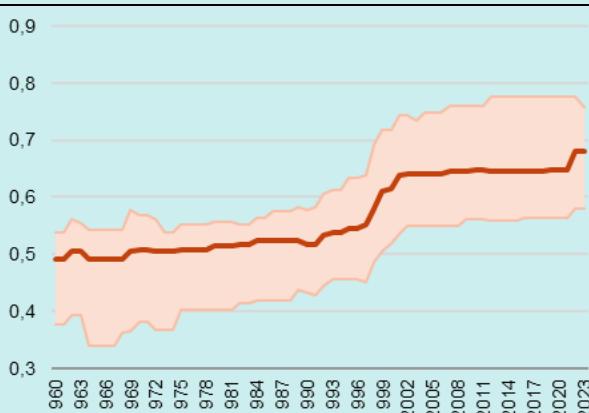
- **Although there is room for improvement, the independence of central banks in emerging countries is strengthening**

**Better monetary policy management by central banks also requires independence from government<sup>68</sup>.**

**In emerging economies, central bank independence has increased in recent decades**, as evidenced by the improvement in the central bank independence index (see Figure 17), whose median value in our sample of emerging economies rose from **0.49 in 1960 to 0.68 in 2023**.

However, **this independence remains imperfect**. An IMF study, which analyses the motivations behind governor transitions – distinguishing between political considerations, transparent rule-based procedures and the prevalence of professional qualifications – **shows that changes motivated by political considerations remain significantly more frequent in emerging markets** (around 50% of transitions) than in advanced economies (only 8% of all changes)<sup>69</sup>.

**Figure 17 – Central bank independence index in selected emerging economies (ranging from 0 to 1)**



Source: Romelli, *The political economy of reforms in central bank design: evidence from a new dataset* (2022)

Furthermore, **inflation expectations are less firmly anchored in countries where politically motivated changes of governor are frequent**.

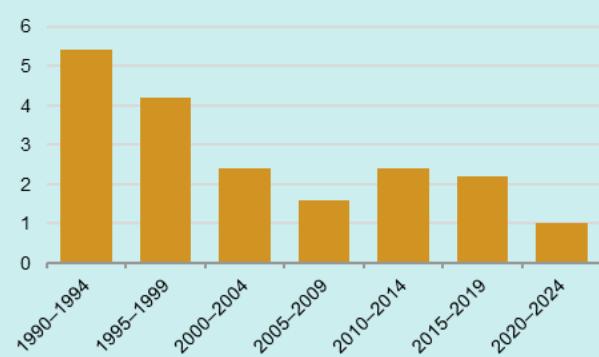
Expectations exceed the target by around 1% when such changes are recurrent, and by more than 2% when they are the norm. Conversely, in countries where the monetary authority is not subject to such transitions, inflation expectations remain close to the target<sup>70</sup>.

**If we focus solely on the 23 emerging countries studied in the first part of this report, we nevertheless see a notable improvement:** the average number of irregular changes in central bank governors has **fallen sharply since the 1990s** (see Figure 18), while the average length of service of governors has risen significantly (see Figure 19).

<sup>68</sup> [Emerging Market Resilience: Good Luck or Good Policies?](#), IMF, 10/2025

<sup>69</sup> [Emerging Market Resilience: Good Luck or Good Policies?](#), IMF, 10/2025

<sup>70</sup> [Emerging Market Resilience: Good Luck or Good Policies?](#), IMF, 10/2025

**Figure 18 – Average number of irregular changes in central bank governors in a selection of emerging economies****Figure 19 – Average tenure of central bank governors in selected emerging economies (years)**

Source: *When is a Central Bank Governor Replaced? Evidence Based on a New Data Set, Journal of Macroeconomics*

- The use of new monetary policy instruments during the pandemic also reflects the growing expertise of central banks in emerging economies

Finally, in recent years, emerging economies have incorporated non-traditional monetary policy instruments – such as interest rate guidance and asset purchase programmes – in order to broaden their range of options. This diversification of instruments also reflects the growing expertise of their central banks.

The first uses of these unconventional monetary policies were triggered by the pandemic, which highlighted the limited leeway of many central banks in emerging economies, constrained by zero interest rate floors or the risk of capital outflows. In this context, some central banks have turned to "forward guidance", i.e. an explicit commitment to follow a monetary policy stance announced in advance. In recent years, India, Israel, Chile, Brazil and Peru have introduced forward guidance mechanisms. Brazil and Peru have favoured an approach conditional on economic performance, while Chile, Israel and India have opted for announcements without a specific time frame. These measures have proven effective<sup>71</sup>.

Similarly, asset purchase strategies – consisting of central banks buying bonds denominated in local currency to ease tensions in financial markets and stabilise bond markets – have achieved their objectives. In some countries, such as Chile, India and Israel, asset purchases have complemented interest rate guidance<sup>72</sup>.

Thus, the ability of central banks in emerging markets to implement forward guidance and asset purchase strategies reflects an improvement in their independence and credibility, resulting in particular from greater transparency in their monetary policy<sup>73</sup>.

<sup>71</sup> [New monetary policy instruments in emerging market economies, Banque de France, 01/07/2024](#)

<sup>72</sup> [New monetary policy instruments in emerging market economies, Banque de France, 01/07/2024](#)

<sup>73</sup> [New monetary policy instruments in emerging market economies, Banque de France, 01/07/2024](#)