Daily: The Treasury’s rare intervention buys time, not a solution

UBS CIO · 2026-08-20 · English original

From the studio

Podcast: Signal over Noise with Ulrike Hoffmann-Burchardi, on Apple or Spotify (6 mins)Video: Market Playbook | James Cheo on fixed income (5 mins)Video: The AI Show | China tech earnings update and what's next (3 mins)

Thought of the day

The US Treasury surprised markets this week by doubling the size of its buyback operations for longer-dated Treasuries, targeting the 10-30-year segment of the market. The move came after the 30-year Treasury yield climbed to 5.34%, its highest level since 2007, amid growing concerns over persistent fiscal deficits, rising government borrowing needs, and weaker demand for long-duration government debt.

While the increase in buybacks is modest relative to the USD 32 trillion Treasury market, it still prompted a notable reaction: 30-year Treasury yields fell nearly 10 basis points, the US dollar weakened against every major G10 currency (DXY -0.8%), gold prices rallied more than 4%, and equities moved higher. Adding to the surprise, the announcement came just two weeks after Treasury officials outlined a buyback schedule that gave no indication of the move, and was timed ahead of a closely watched 20-year auction and during the typically quiet late-summer trading period.

The Treasury's actions may have helped cap the surge in yields this week, but we think investors should avoid overinterpreting the longer-term implications:

The Fed path still depends on inflation, not intervention. While the Treasury announcement overshadowed the July Fed minutes, the minutes reinforced that inflation remains policymakers' primary concern. Several officials favored a rate increase, while many believed further tightening could be necessary if inflation does not continue to improve. At the same time, most participants expected inflation pressures to moderate over the remainder of the year. Importantly, the minutes predated the softer inflation and labor-market data released this month. In our view, the latest data remain consistent with the Fed staying on hold this year, albeit with a data-dependent stance.

History shows bond-market interventions have limits. Japan and the UK offer useful lessons. Both countries have used bond purchases, buybacks, or issuance adjustments to influence long-end yields. While such measures can reduce volatility and provide temporary relief, they have not permanently lowered borrowing costs when fiscal, inflation, or supply dynamics remained unfavorable. We believe the same principle applies in the US. The Treasury's buybacks may discourage aggressive curve-steepening trades and reduce near-term market stress, but they do not address the forces supporting higher term premia, including persistent deficits, elevated capital demand, and a shift in Treasury ownership toward more price-sensitive private investors. In addition, the temporary nature of the program (which runs from 9 September through 4 November) reinforces the view that this is a tactical measure rather than a permanent solution.

While unusual, this is not quantitative easing. Unlike QE via the Fed, the Treasury cannot create money to fund asset purchases. Any buybacks must be financed elsewhere, most likely through increased bill issuance or adjustments to other parts of its funding program. In effect, the operation reshapes the maturity profile of debt held by investors rather than reducing the amount of debt markets must absorb. It neither removes the government's financing needs nor resolves concerns about Treasury supply.

So we take the Treasury's intervention as further evidence that policymakers are increasingly focused on maintaining stability at the long end of the curve and are uncomfortable with the pace of the recent rise in yields. Its action may help cap near-term yield volatility and reduce the risk of disorderly market moves, but it does not fundamentally alter the outlook for rates. Our base case remains that the Fed is unlikely to raise rates this year if inflation continues to moderate, although policymakers have retained the option to tighten should price pressures prove more persistent than expected.

For investors, we continue to favor quality fixed income in short- and medium-term maturities. We believe yields in these segments remain attractive, and income opportunities are compelling and do not require a strong view on long-term interest rates. At the same time, we see little reason to position aggressively for higher long-end yields.

We also remain constructive on equities. A potential near-term cap in bond yields and lower rate volatility would further support market sentiment, particularly in rate-sensitive sectors like tech and AI. However, we believe the more important drivers of equity performance remain robust earnings growth, resilient economic activity, and continued AI infrastructure investment. Periods of volatility like this can be used to diversify investors' equity exposure, balancing technology leadership with cyclical and broadening earnings opportunities.

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