What's Hot: Riding high interest rates with Treasury FRNs and AT1 CoCo bonds

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Wichtige Erkenntnisse

- In a context of high and rising interest rates as well as a flat yield curve, Treasury Floating Rate Notes prove to be a useful instrument given their low duration and low volatility
- Rising yields in AT1 CoCo bonds prove to be macro rather than credit related, making those bonds attractive as the underlying European banks continue to display strong fundamentals

MARKETING COMMUNICATION – Please refer to the prospectus and KID of the relevant fund before making any final investment decisions.

In 2002, the iPhone did not exist, the Euro had just entered circulation and Bitcoin was still years from being introduced. The world was recovering from the dot-com bubble and the recession that followed, with the Fed cutting interest rates to historic lows to support the economy.

A few years later, in an overheating economy, rate-hiking cycles led the US Treasury 10-year yield to over 5%, peaking just before the Global Financial Crisis. It was then driven to an all-time low below 1% during the COVID pandemic after over a decade of Quantitative Easing and zero-rate policies put in place by central banks to revitalize the economy.

After the pandemic, higher persistent inflation led the Fed on another rate-hiking cycle that sent the 10-year Treasury yield almost back to its 2007 levels, before easing a little in the years that followed.

Today, a different picture lies before us: geopolitical tensions causing ever-so-high oil prices, rising inflation fears, and most importantly a high fiscal deficit in the US have propelled the US Treasury 10-year yield back to its 2002 levels, pointing at roughly 5.3%1 on the 30th of September.

But this dynamic is not confined to the US – it affects all developed markets across the globe. The U.K. 10-year Gilt rose above 5.4%1 in September, reaching its highest level since 2007 – the German 10-year

Bund yield reached 3.6%1, a level last reached in 2009 – the Japanese government 10-year yield reached 3.1%1, levels last seen in 1996.

A lot of different instruments are available to investors who want to invest in bonds - as markets are shifting into higher rates environments all around the globe, it is important to consider how different bond instruments may behave in the current environment.

For investors investing in USD, we focus first on US Treasury Floating Rate Notes and elaborate on why they make sense in the current environment.

The case for US Treasury Floating Rate Notes

A key metric investors look at when investing in bonds is **duration**.

Duration measures the sensitivity of a bond's price to a change in interest rates. The longer the duration, the more the bond price will move when interest rates change.

When rates are declining, long duration bonds will see their price advance - when rates are rising, on the other hand, low duration bonds will be more immune to price drops.

Investors, in the current setting, are not being rewarded to take on duration risk – the **yield curve is not very steep** (see Figure 1): investors are not paid a significantly higher yield for locking their money for longer.

In the current environment, with rates being high and with a sentiment of them staying higher for longer, **Treasury Floating Rate Notes** are a very well positioned instrument mainly because, by design, their duration is very low.

What are Treasury FRNs?

The US Treasury started issuing Floating Rate Notes in 2014, as part of a new class of issuance – the latest since the introduction of TIPS back in 1997.

A Floating Rate Note is a rather simple instrument: it is a coupon-paying bond with a finite maturity, whose **coupon is not fixed, but variable**. The coupon rate is the sum of two parts: a benchmark rate, and a spread rate.

In the case of the US Treasury, the coupon is updated every week based on the 13-week T-Bill auction, which sets the highest accepted discount rate for this instrument: this is the **benchmark rate**. During the first auction of a new FRN issuance, a **spread rate** will be agreed upon and fixed for the remainder of the bond's life. This rate is based on the highest accepted discount margin during this auction.

Interest is accrued daily, and **coupons are paid out quarterly**.

This is essentially why FRNs, by design, have a very low duration: since the coupon rate is reset every week, an FRN will have a very low sensitivity to a movement in rates because whatever happens to interest rates will be reflected in the bond's coupon at the next weekly update.

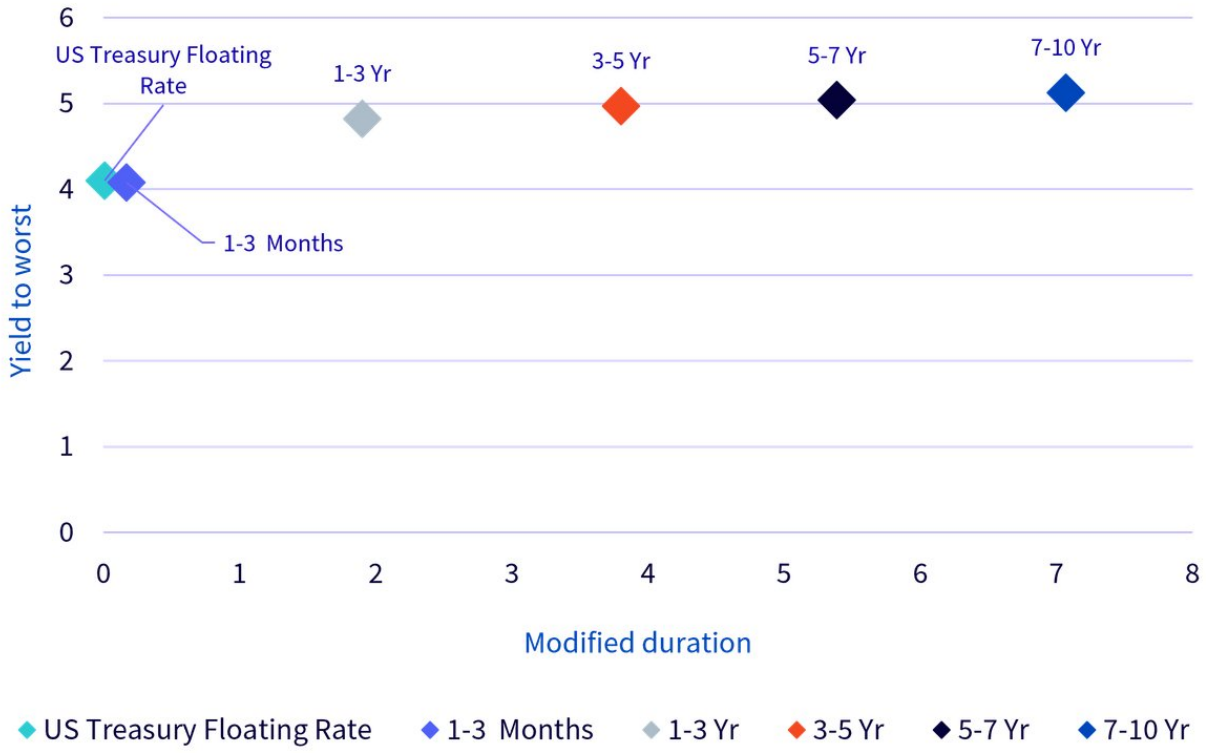
US Treasury FRNs compared to other Treasury instruments

Treasury FRNs differ from the other instruments used by the US Treasury. They make quarterly interest payments and their coupons adjust with the weekly auction of the 3-month T-bill rate.

FRNs	TIPS	T-Bills	T-Notes
Coupons			
+ Effectively reset weekly + Paid quarterly	+ Semi-annual coupon + Fixed rate of the adjusted principal	+ No coupon	+ Fixed semi-annual coupon
Principal			
+ Repaid at maturity	+ Adjusts to CPI	+ Repaid at maturity	+ Repaid at maturity
Maturity			
+ 2 years	+ 5, 10 and 30 years	+ Up to 1 year	+ 2, 3, 5, 7 and 10 years
Duration			
= time to next reset = 7 days	? maturity	= maturity	< maturity

Figure 1 shows that US FRNs exhibit the lowest duration amongst all US Treasury instruments while offering yields comparable with certain other Treasury maturities shown in Figure 1.

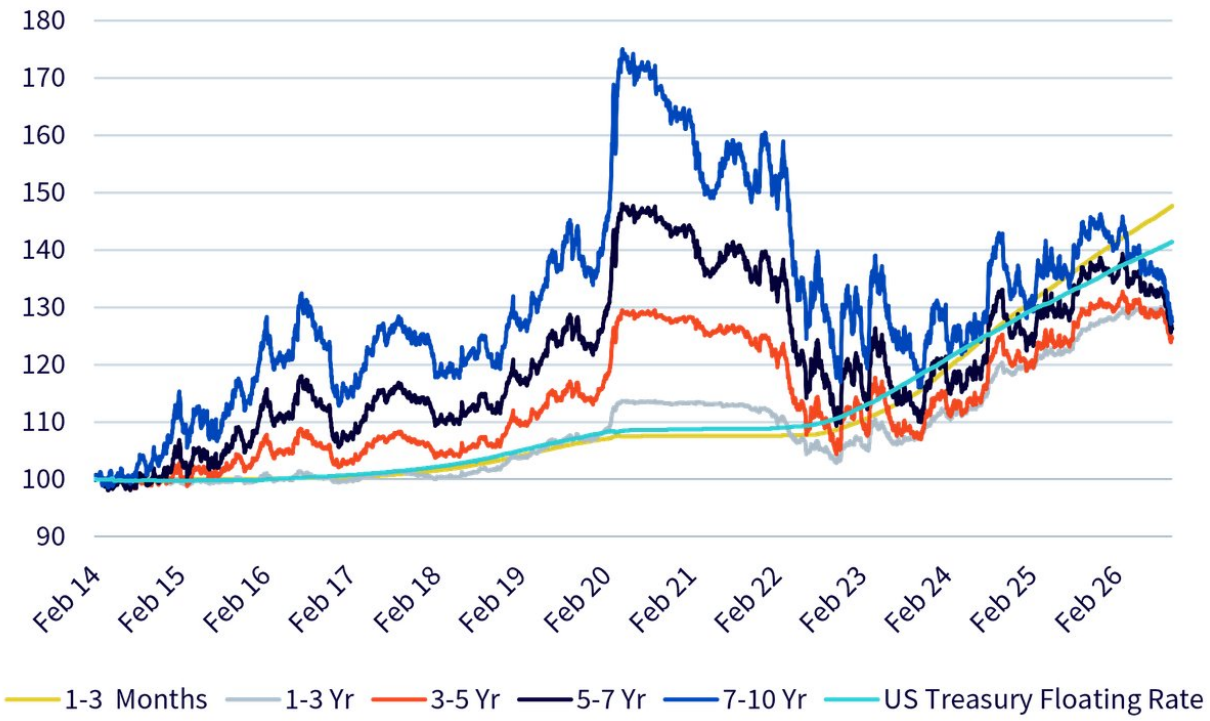
Figure 1: YTW vs modified duration for diferent U.S. Treasury insturments



Source: WisdomTree, Bloomberg, data as of 30.09.2026 (latest available data).YTW = yield-to-worst. Modified duration = percentage change in a bond price for a 1% parallel move in the yield curve.

Given their lower duration, they also exhibit much lower volatility compared to longer maturity US Treasury bonds, as can be seen on Figure 2: their historically lower price volatility may provide diversification relative to longer-duration Treasury exposure.

Figure 2: Total return evolution of different treasury strategies



Source: WisdomTree, Bloomberg, data as of 30.09.2026 (latest available data). **Historical performance is not an indication of future performance and any investment may go down in value.**

WisdomTree provide access to US Treasury FRNs via the **WisdomTree USD Floating Rate Treasury Bond ETF**, whose aim is to track the Bloomberg Barclays U.S. Treasury Floating Rate Bond Index, which tracks all the issuances of FRN by the US Treasury.

Investors should note that floating-rate Treasury exposure remains subject to interest-rate, market and currency risks. While FRNs generally have lower duration than fixed-rate Treasury bonds, their income can fall if short-term interest rates decline. The value of an investment may also fall, and investors whose base currency is not US dollars are exposed to movements in exchange rates.

The case for AT1 CoCo bonds

European banks continue to report strong profitability and capital metrics, with Q2 2026 results generally remaining resilient. Q2 2026 results confirmed it. Meanwhile, bond yields have surged across the board: **sovereigns, investment-grade corporates**, and, sharply, **AT1 CoCo bonds**, issued primarily by banks.

AT1 CoCo (Additional Tier 1 Contingent Convertibles) bonds are instruments issued by banks as part of their Additional Tier 1 capital buffer. They don’t have a fixed maturity and are callable by the issuer at pre-determined dates. Their survival is contingent on the good health of the bank: if the bank’s capital ratio falls under a threshold, CoCo bonds can either be written down or converted into equity, depending on the terms.

Morningstar DBRS called Q2 2026 "another quarter of solid results" for the European banking sector, with **aggregate net profit up 18% year-on-year**. The story holds up from every angle: resilient net interest margins, higher fee income, robust capital markets activity, asset quality that stayed low-risk despite geopolitical tensions, stable-to-improving credit indicators, and contained cost of risk. Several banks, **Deutsche Bank, Barclays, Société Générale** among them, also announced additional share buybacks, supported by their reported capital positions.

For roughly five months now, with a sharp acceleration in August and September, bond yields have risen hard. Here's the key insight: **The yield increase appears to have been driven primarily by broader interest-rate movements rather than a material widening in AT1 credit spreads.** The crucial detail: AT1 credit spreads remain near historic lows. AT1 credit spreads have remained relatively tight, indicating limited spread widening despite the increase in overall yields. **Higher yields are coming from the risk-free rate component, not from a repricing of bank credit risk.**

An ETF like the **WisdomTree AT1 CoCo Bond** (tracking the iBoxx Contingent Convertible Liquid Developed Europe AT1 index) is currently yielding a 7.01% Yield-To-Worst in USD, as of 28/09/20262.

That compares very favourably with investment-grade corporates (offering markedly lower yields today3) and even with much of generalist high yield, while starting from a higher average issuer quality since European banks are typically stronger credits than the average industrial high-yield name.

AT1 CoCo bonds are subordinated instruments and involve additional risks compared with conventional corporate bonds, including the potential for coupon cancellation, conversion into equity or principal write-down under certain circumstances. Their value may fall as well as rise and investors may lose part or all of their investment.

1Bloomberg. Data as of 30/09/2026

2 WisdomTree

3 Markit iBoxx EUR Liquid Investment Grade Index, as of 29/09/2026 (Bloomberg)

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WisdomTree USD Floating Rate Treasury Bond UCITS ETF

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