

Let's Stop with the Rate Hike Talk Already

Published May 8, 2024

Kevin Flanagan

Head of Investment and Fixed Income Strategy

Key Takeaways

- The UST market reacted positively to the results of the May FOMC meeting, the Powell presser and the April jobs report due to the context of the re-introduced rate hike narrative being downplayed by Powell.
- The UST 2-Year yield hit a pre-May FOMC meeting peak of 5.04%, the highest reading since November, and the UST 10-Year yield rose to 4.74% on an intra-day basis, to reach its most elevated level since October, indicating a potential reversal of the UST rally of Q4.
- The bottom line is that “higher for longer” remains a dominant theme for the U.S. bond market.

Coming into this year, it's safe to say that all the attention within the money and bond markets was on Federal Reserve rate cuts. It wasn't a question of “if,” but “when” and by “how much.” Well, we all know now how that narrative has turned out thus far. In fact, just within the last few weeks the whole rate cut discussion was turned completely around, as—believe it or not—the Treasury (UST) arena was actually contemplating the exact opposite...could the Fed give us a renewed rate hike.

So, how did we go from point A (rate cuts) to essentially point Z (a rate hike)? Certainly, the economic data released in April was a starting point, specifically on the inflation side of the equation. CPI and PPI both came in hotter than expected, basically halting the disinflation trend that had been prevalent in 2023. In addition, labor market data revealed new momentum in job growth, and consumer spending, as measured by retail sales, was also solid.

However, the final piece of the puzzle seems to have been a comment from N.Y. Fed President Williams, considered to be one of the Fed's three official spokespersons. While he said that a rate hike “is not my baseline,” he did say it is possible if the data warrants such a move.

Needless to say, the UST market did not greet this headline favorably. Indeed, the UST 2-Year yield hit a pre-May FOMC meeting peak of 5.04%, the highest reading since November. Meanwhile, the UST 10-Year yield rose to 4.74% on an intra-day basis, to reach its most elevated level since October. In other words, the incredible UST rally during Q4 was getting closer to being reversed entirely.

Why is this so important? Because it explains why the UST market reacted in such a positive fashion to the [results of the May FOMC meeting](#), the Powell presser and then the April jobs report that followed a couple

days later. Without this context, the May Fed-day probably would have been viewed as being neutral with a case for perhaps a hawkish spin on the Powell presser.

Instead, the money and markets focused on Powell's downplaying the chance of a renewed rate hike. If the whole rate hike narrative hadn't been re-introduced, the focus probably would have been on the Fed chair's statement that gaining confidence to cut rates will take longer than originally thought. Additionally, although the employment data did not meet consensus forecasts, it still revealed a relatively solid labor market setting.

Conclusion

The bottom line is that ["higher for longer" remains a dominant theme for the U.S. bond market](#). Against this backdrop, we believe investors should consider turning to the WisdomTree suite of Treasury Funds as a toolkit to position their fixed income portfolios for both the current and prospective rate outlooks:

- [The WisdomTree Floating Rate Treasury Fund \(USFR\)](#)
- As well as our two new Treasury laddered Funds:
 - [The WisdomTree 1-3 Year Laddered Treasury Fund \(USSH\)](#)
 - [The WisdomTree 7-10 Year Laddered Treasury Fund \(USIN\)](#)
- [The WisdomTree 1-3 Year Laddered Treasury Fund \(USSH\)](#)
- [The WisdomTree 7-10 Year Laddered Treasury Fund \(USIN\)](#)

Important Risks Related to this Article

There are risks associated with investing, including the possible loss of principal. Please read the Funds' prospectus for specific details regarding the Funds' risk profiles.

USFR: Securities with floating rates can be less sensitive to interest rate changes than securities with fixed interest rates, but may decline in value. Fixed income securities will normally decline in value as interest rates rise. The value of an investment in the Fund may change quickly and without warning in response to issuer or counterparty defaults and changes in the credit ratings of the Fund's portfolio investments. Due to the investment strategy of this Fund it may make higher capital gain distributions than other ETFs.

USSH & USIN: Because the Funds are new, they have no performance history. U.S. Treasury obligations may provide relatively lower returns than those of other securities. Changes to the financial condition or credit rating of the U.S. government may cause the value to decline. Fixed income securities are subject to interest rate, credit, inflation and reinvestment risks. Generally, as interest rates rise, the value of fixed income securities falls.