

‘Warsh’ and Dry

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Key Takeaways

- Treasury markets have rapidly repriced toward a higher-for-longer Fed outlook, with the 10-year Treasury yield climbing to 4.60% and fed funds futures now fully pricing in a rate hike by March 2027 after previously expecting multiple cuts.
- As inflation pressures, stronger labor data and geopolitical risks fuel the “inflation trade,” investors may want to reduce duration exposure and prepare for additional volatility across fixed income markets.
- Treasury Floating Rate Notes, accessed through strategies like the WisdomTree Floating Rate Treasury Fund (USFR), can provide a defensive barbell allocation by helping investors hedge against rising rates while maintaining exposure to U.S. government debt.

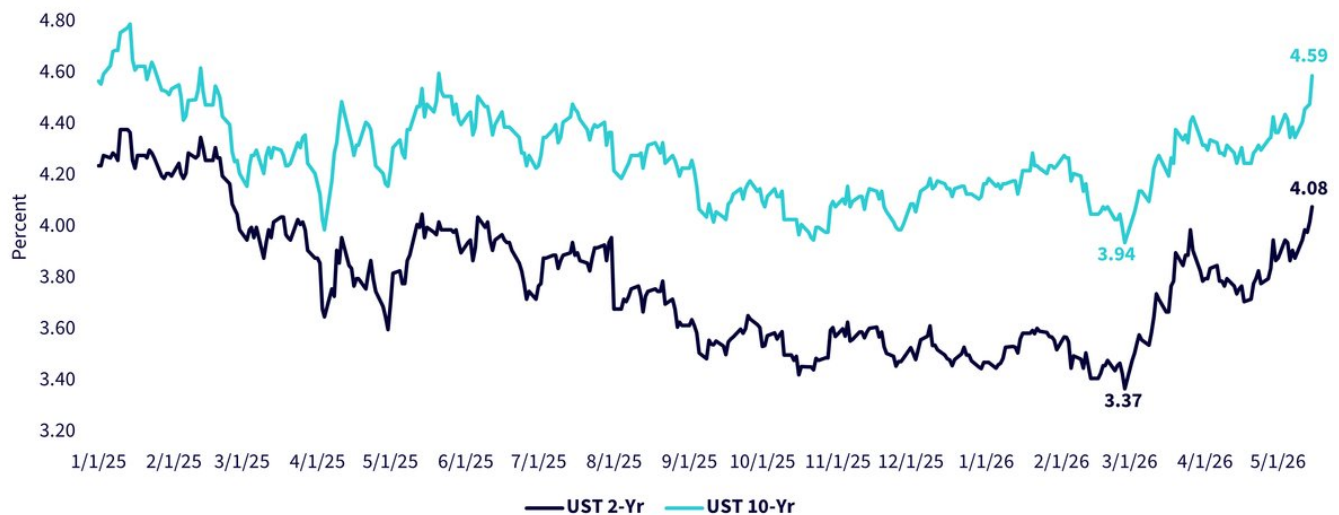
How many headlines can a bond investor handle at one time? Let's see, at the present time, the money and bond markets have been juggling ongoing Middle East headlines, a return of inflation (both headline & core), better than expected jobs reports, new Treasury coupon auctions, etc., etc.

Or better yet, how would you like to become the new Fed Chair right about now? That's the situation new Fed Chairman Kevin Warsh finds himself in. Indeed, Warsh now enters the Eccles Building (Fed Headquarters) as the new leader, while also having a former Fed Chair, a.k.a. Jay Powell still sitting on the Federal Open Market Committee (FOMC) as an automatic voting member due to his retained stance as a Fed Governor.

In terms of upcoming monetary policy, as we have written in a series of Warsh-related blogs this year, the new Chairman will follow the data, and at this point in time, that data is pointing to a Fed that appears to be done cutting rates, and is on hold for the rest of 2026.

I still don't think the Fed is close to a rate hike, but for the upcoming June FOMC meeting, a shift in the language of the policy statement from an easing bias to one of a 'balanced' outlook seems to be the most likely scenario. However, the fed funds futures market has now fully priced in a rate hike for March 2027, a remarkable shift from its pre-war status of discounting almost three rate *cuts* for the same timeframe.

Figure 1: U.S. Treasury Yields



Source: St. Louis Fed, as of 5/15/26.

The Inflation Trade

The U.S. Treasury (UST) market has also shifted into a different mindset. Indeed, the ‘inflation trade’ has taken hold, whereby yield levels across the fixed coupon maturity spectrum have risen in a rather visible fashion since the end of February (see graph). Here’s some highlights:

- The UST 10-year yield has increased by about 65 basis points (bps) during this timeframe.
- As of this writing, the yield had jumped to 4.60%, the highest reading since early 2025.
- Technical analysis, such as one-year Fibonacci retracement levels, are being tested, with a break-through putting 4.80% potentially in play.
- The UST 2-year yield has surged over 70bp from its pre-war low.
- It has pierced the 4% threshold and is also at its highest reading since early 2025.
- At its current level of 4.08%, the two-year has now also priced in a Fed rate hike.

Solution

So, how can a bond investor combat the ‘inflation trade’? Answer: the time-tested barbell strategy. The cornerstone of this approach are UST Floating Rate Notes (FRNs). Treasury FRNs not only mitigate the duration and volatility risks of fixed coupon maturities, they also serve as a very useful hedge when the money and bond markets are pricing in the potential for Fed rate hikes. The [WisdomTree Floating Rate Treasury Fund \(USFR\)](#) allows investors to access this important asset class and can serve as a cornerstone of the barbell strategy.

Important Risks Related to this Article

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