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Market View
Policymakers look to reassert control of bond markets

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At a glance

Both the new US Treasury and the Fed leadership arrived promising to intervene less in markets.

Long-term US borrowing costs reached their highest since 2007, before the Treasury stepped in.

Jackson Hole sounded firmer on inflation, but the Fed has committed to no particular path.

In January, US Secretary of the Treasury, Scott Bessent, was asked directly whether the Treasury was intervening in currency markets to support the Japanese yen. His answer was "absolutely not", followed by a reminder that the US has a strong dollar policy and that the job of government is to get the fundamentals right.[1] Before taking office he had also criticised his predecessor for seemingly skewing government borrowing towards short-dated debt, arguing that it artificially held down long-term borrowing costs.[2]

Chair Kevin Warsh arrived at the Federal Reserve (Fed) in May with a similar instinct. He removed the practice of signalling in advance where interest rates were heading, and has said he considers it healthy for bond markets to move on economic data rather than on what the central bank tells them.[3]

Six weeks on from the July meeting, both institutions have intervened more actively than at any point in years. The Treasury has bought yen and moved to hold down long-term bond yields; the Fed has spent the summer being read, and occasionally misread, by a bond market looking for direction. Below, we consider what has occurred, how markets responded and what it means for investors in government bonds.

A Treasury that said it would not intervene

On 28 July the yen fell to its weakest level against the dollar in 40 years. Within days the US joined Japan in a coordinated currency intervention, its first alongside Tokyo in more than a decade, with the New York Fed selling euros to buy yen on the Treasury's behalf.[4] Bessent said afterwards that the authorities would not hesitate to intervene again. On Thursday, the Yen appreciated to its strongest level since February. Firming rate hike expectations by the Bank of Japan, who are priced in to hike rates by 0.25% in two weeks' time, paired with mounting speculation of further intervention led to a 2% appreciation of the yen.

The Treasury also asked the Fed to make it easier for foreign central banks to borrow dollars using their US government bonds rather than having to sell them outright.[5] The purpose was clear: Japan is the largest foreign holder of US government debt and large-scale selling would have pushed US borrowing costs higher still. In late August the Treasury took further action, announcing it would at least double the size of its operations to buy back its own outstanding debt, to $4 billion, from 9 September.[6] The dollar weakened following the announcement.

The Fed muddled the message in July

The backdrop to all of this was a difficult July. The Fed held interest rates for a fifth consecutive meeting, with three regional presidents dissenting in favour of an immediate increase.[7] Warsh was emphatic on inflation, telling reporters there was no soft target and no implicit one, only a target of 2%.

Bond markets were unconvinced. Yields on 30-year US government bonds rose to 5.21%, their highest since 2007, while yields on two-year bonds fell.[7] This combination shows investors were questioning the Fed's inflation credibility and therefore demanded higher yields to lend longer raising concerns for the Treasury. The subsequently announced Treasury buyback programme is intended to not only improve market liquidity and ease some of the upward pressure on longer-dated yields.

Jackson Hole sounded firmer, but promised nothing

Warsh used his Jackson Hole address on 28 August, marking his hundredth day in office, to set out his approach going forward. He acknowledged that summer inflation readings had been better than expected but said they did not suggest underlying trends had meaningfully improved, and indicated the Fed may still have work to do.[8] He declined to offer any guidance on the path of rates, telling the audience he was committed to a discipline rather than to a decision, and that markets should not look primarily to the Fed for their next trade.

The reaction inverted July's position. Yields on two-year bonds rose sharply, as investors moved to price a possible increase in September, while 30-year yields barely moved.[9] This illustrates that long-term borrowing costs rise when investors doubt the Fed's resolve on inflation, and stabilise when they are reassured of it.

The impact was not limited to the US, government bond yields across the world rose on the back of this firmer message on inflation. Gilts, Japanese Government bonds and German bunds all rose to highest levels in over a decade, rising to 5.23%, 3.03% and 3.38% respectively for ten-year maturities before settling lower towards the end of the week.

What this means for portfolios

On balance, we believe intervention of this kind can smooth market conditions but is unlikely to change where long-term yields settle. Buying back debt and supporting the yen both address symptoms. The level of long-term borrowing costs will continue to be set by the outlook for inflation and by how much the government needs to borrow, neither of which has changed. These measures may not change the bigger picture but they could help reduce the sharp, disorderly moves that have unsettled bond markets over the past two months.

For government bond investors, this argues for expecting continued volatility in longer-dated debt rather than a steady fall in yields. Yields at current levels do offer a return well above what has been available for most of the past two decades, and for investors able to hold to maturity, this provides a genuine opportunity. We would be more cautious about the very longest maturities, where the outcome depends most heavily on inflation over a horizon no one can forecast with confidence.

The Fed's September meeting is now the more important event. Warsh has been clear that he will be led by the data rather than by prior commitments, which means each inflation and employment release carries more weight than it did under his predecessor. Investors should expect a less predictable path, and position accordingly.

Sources

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2 Bloomberg, February 2025 — replace with a firmer primary citation before publication

3 Fed meeting recap, CNBC, 29 July 2026

4 Yen intervention: US, Japan confirm intervention, CNBC, 3 August 2026

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7 Fed holds interest rates steady after cliffhanger meeting, CNN Business, 29 July 2026

8 Keynote remarks by Chairman Warsh at the 2026 Jackson Hole Economic Policy Symposium, Federal Reserve Board, 28 August 2026

9 2-year Treasury yield jumps as Warsh says Fed may 'have work to do', CNBC, 28 August 2026

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Jeremy is our Deputy Chief Investment Officer. He sits on the Investment Committee and chairs the Fixed Income Committee. His coverage encompasses both rate and credit products and works closely with the funds team.