The Year of Fed Irrelevance Is Almost Complete: The Treasury is the New Sheriff in Town

By Vineer Bhansali| August 27th, 2026

As part of the annual outlook earlier this year, I postulated that 2026 might be a year where Central Banks become largely irrelevant (here). This was followed by the view that monetary policy driven "monetary quantitative easing (MQE)" would be replaced by "Fiscal Quantitative Easing (FQE)" (here) as the Fed's powers are "cancelled" and replaced by other powers on the way to monetary-fiscal convergence. Based on this I recommended keeping bond durations short, look for a steeper yield curve, hold some precious metals, and if holding a lot of equities, hedging the downside and replacing the upside with options while optionality is cheap.

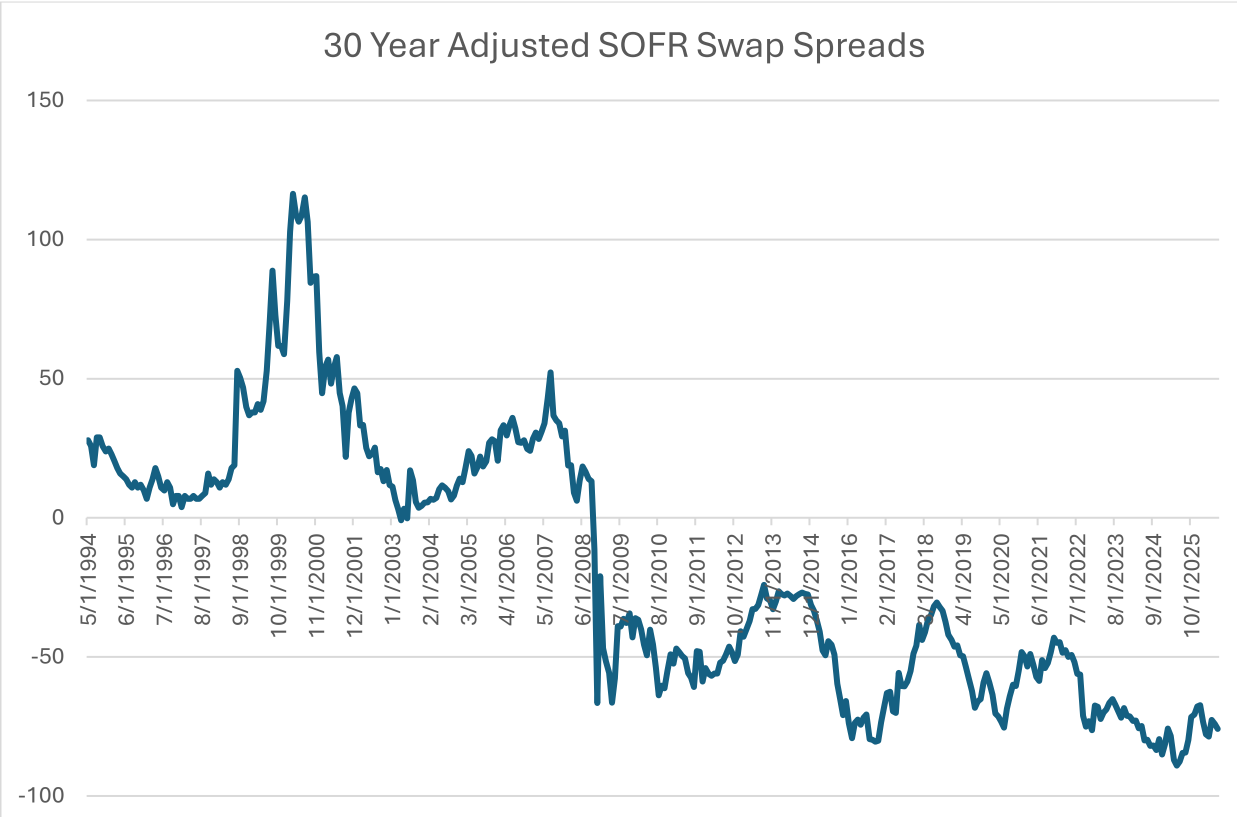
So far, so good. What's next?

To recap, the new Fed chair has basically announced that he will let the market do the talking and not force the market to dance to its tunes by either intervening or managing expectations. In response to this, yield curves have steepened and gold has caught a bid on its way to a much higher place. Stocks have rallied and the price of protection in equities has collapsed further. Almost on script, a few days ago the Treasury (fiscal) announced a surprise buyback of long-end bonds to support liquidity in the bond market. People are calling this a "Bessent Put". Most participants see this for what it is – an attempt at what we have called Fiscal Quantitative Easing, which is probably a more technical term for "operation twist" where the Treasury re-jiggers the shape of the yield curve. Note that to engineer this the Treasury has to borrow cash to buy these longer bonds back. It can either borrow short —e.g. in the T-Bill market — or borrow long — e.g. by issuing more notes and bonds. It is doing both. So, when the Treasury borrows money with one hand to buy with the other hand, it is basically just moving the chairs around. Net-net, it is just engineering a temporary reduction in the risk premium, which, by any metric, is "easing" of long-term financial conditions. No wonder that the equity market has since started a new leg up and gold and other stores of value have also seen a new bid.

Also, in doing so, it has usurped some of the powers of the Fed, making the Fed even more irrelevant, since if it issues more T-Bills to finance the purchase of the bonds, T-Bill yields will go up, and the Fed will have to either (1) raise rates to match the higher T-Bill yield, or (2) buy those T-Bills to keep rates where they are. If the Fed does not raise rates, then it is forced into quantitative easing by the actions of the Treasury. Circle complete, Fed becomes a subject to Treasury actions; i.e. Fed irrelevance. All eyes are on Fed Chair Kevin Warsh who speaks tomorrow at Jackson Hole to see if he acquiesces to this setup, or perhaps fights back to claim some independence. My guess, and not a very good one, is that he will lean toward the former, since his implicit mandate is now different. Rather than micro-managing policy, the Fed will become more of a keeper of guidelines or boundary conditions, and try to manage its own dissents, making unanimous policy making impossible. Instead of "whacking-the-mole" in a tactical sense, the Fed will gently hand that duty over to the Treasury, while working on developing a new set of long-term strategies and guidelines using the now infamous "task-forces".

Will this work? And what, one may wonder, is the path forward? If we assume that there is a limit to the buyback operation we just spoke about, then either long-term yields are allowed to resume their upward trend until something breaks, or the Fed has to tighten to convince the markets that it is serious about fighting inflation. In the setup I painted, the Fed does not tighten, and the market will attempt to tighten policy for it. The Treasury will attempt to rein this in by "pushing on a string"; i.e. by trying to buy the bonds that everyone is selling (or shorting). Common sense tells us that this is a hard job since buying back a small amount of bonds with borrowed money is not likely to work in the long run. This leaves only a few solutions, one of which is to declare a maximum cap on yields (this happened in 1942, which also forced the Fed to buy unlimited amounts of T-Bills, see here), or force governmental and quasi-governmental agencies to buy bonds at a ceiling yield (this is exactly what happened in Japan the last two decades or so), or hope for a market crash that results in recession and fall in yields (a very bad choice). Either way, technically the financial repression "works" to keep long-term yields low. But it also leads to side effects that we should now address to imagine our best strategy in such a world.

First, low long-term yields in Treasuries do not necessarily mean that public investors will follow suit. Since the Treasury market today is a very small portion of the bond market, the suppression of low long-term Treasuries will do very little for the market clearing mechanism for interest rate duration. The benchmark for long-term duration is the interest rate swap market. Due to the inherent leverage provided by swaps (one can obtain duration for liability hedging without committing the full principal), swaps have been trading at a lower yield than Treasuries. In a world where duration has to be rebalanced somewhere, repression in the Treasury markets results in swap spreads heading back toward positive territory. Today, at almost -67 basis points, these spreads are providing investors with an opportunity to position for a duration readjustment at very attractive levels.



30 Year SOFR Swap Spreads

Data prior to 2020 uses LIBOR swaps with the ISDA fixed spread adjustment of -26.16 bps between LIBOR and SOFR Swaps

Source: Bloomberg, LongTail Alpha

Second, low long-term yields on Treasuries, all else being equal, are stimulative and inflationary. There is nothing magical about this. Inflation is a tax on purchasing power, but is a necessary evil if one is not willing to control it in the short run by more aggressive action. Investors can look in two places: the first one, of course, are real assets that are also liquid. The best such asset is, of course, gold. I have written extensively about this. The second asset that has become attractive again are long-term TIPs. TIPs in the 30-year sector are trading at right around 3% “real yield”, and with inflation running at around 3.5%, this results in a yield of about 6.5%. Not bad. I am sure you can wait and get an even better entry point, but since I have almost never caught the turning point in markets, this yield is already in the zone where, for the first time in many years, I am willing to go out on a limb and suggest they are a reasonable addition to a portfolio. This is even more compelling when we realize that for most large investors, their objective is to make inflation (CPI) plus 3% to 4%. Well, we are almost there! If one has a long-term liability that is CPI + 4, today we are entering a zone where we can insulate this risk and reduce long term liability risk to zero! Yes, TIPs are not very liquid, and yes TIPs did very badly in the 2008 financial crisis when everything got sold. But for long-term owners of assets, these issues create investment opportunity. The best time to buy unloved assets is when no one loves them. A strategy such as PIMCO's (my old employer) commodity real-return, which doubles up on commodities and TIPs, might be even better for those who can stomach the volatility and leverage (caveat emptor – it got crushed in the GFC due to mass-scale liquidation).

Finally, the fact that the Fed has mostly become irrelevant and the Treasury is the new sheriff in town has a very simple consequence for volatility. Since policy will become more and more tactical and short-termist (this is because political cycles are compressed into elections), we should expect frequent pivots and new innovations to keep a lid on markets totally taking over control of economics. This means that it is going to be very hard to forecast what happens next in the short run. Frequent crashes and melt-ups are likely to become the norm across asset classes. In short, "bi-modality" and "regime shifts". Volatility is on sale across markets, and should be owned as an asset that does well when stuff (frequently) hits the fan.

I started this year with the speculation that the Fed will become largely irrelevant in this "Year of the Fire Horse". True to its name, this year is showing a convergence towards this end point much faster than I imagined. It's only August, the year ain't over yet. But as the story evolves to its natural settlement point, this is a great time for investors to position for what follows in the aftermath.

Important Disclosures

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