

WSJ Print Edition



Trump's tensions with Fed Chair Jerome Powell include criticism of cost overruns in the central bank's renovations. A2
MICHAEL M. SANTIAGO/ GETTY IMAGES



Fed chief Powell has resisted pressure from the president. TOM WILLIAMS/ CQ ROLL CALL/ ZUMA PRESS

Independent Fed Anchors Global System

BY DAVID UBERTI AND JUSTIN LAHART

President Trump's threat to attempt to fire Federal Reserve Chair Jerome Powell has raised a pressing but potentially unanswerable question: What would the global economy and financial markets look like without an independent U.S. central bank?

Shielded from White House interference, the independent Fed has increasingly served as an anchor for U.S. and global markets, stepping in to steady the ship during the 2008-09 financial crisis, the Covid pandemic and other shocks of recent years. Economists credit the central bank's ability to help keep things stable in large part to its power to make moves it deems necessary, regardless of politics.

Now, former Fed officials and investors warn that a central bank more beholden to the White House could lose its ability to act quickly and credibly in the face of financial threats. On Tuesday, Trump suggested in a White House

Note

1

meeting with Republican lawmakers that he could soon try to oust Powell, escalating months' worth of criticism that the central bank has kept interest rates too high for too long.

The president later said it was highly unlikely that he would fire Powell.

Trump's pressure campaign against Powell has recently centered on the \$2.5 billion renovation of the central bank's headquarters in Washington, with the White House criticizing cost overruns and marble construction.

"Politicians almost always think interest rates should be lower than they are," said Alan Blinder, a Princeton University economist and former Fed vice chair. "This is the major reason we need an independent central bank."

The possibility that the firewall could crumble holds the potential to reverberate across markets at an unpredictable moment for the economy. The U.S. is still shaking off years of inflation above the Fed's longstanding 2% target, with recent data showing that price pressures from Trump's trade wars are beginning to mount. Central bankers and investors the world over are waiting on the Fed's next move.

Economists fear that an unprecedented shakeup at the center of it all could add to the uncertainty—and undermine the Fed's credibility when the next crisis explodes. That could matter not just for the U.S. economy, but other countries' economies, too. When markets around the world have spiraled lower in the past, such as during the 1998 Russian debt crisis, the Fed has stepped in to shore them up.

The Fed's ability to do so relies in part on its capacity to keep credit flowing when markets are freezing up, according to Harvard University economist Jeremy Stein. That requires that thousands of Fed employees are able to quickly step into the breach. He worries that threats to the Fed's independence will over time erode the talent and depth of experience of the Fed staff.

"That—and of course the quality of leadership—can potentially make a huge difference in a crisis," said Stein, a governor at the central bank from 2012 to 2014.

The Fed has frequently participated in international financial rescues, such as of Mexico in 1982 and again in 1995, often to prevent a chain reaction of panic from destabilizing the global financial system. It maintains "swap" lines under which it lends dollars to foreign central banks who then lend the dollars to their own banks when they are under stress. The Fed worked with global central banks and finance ministers in the financial crisis to stop big financial firms from failing.

The Fed typically worked with the administration of the day on these rescues. It's unclear if a Fed more directly controlled by Trump would participate as readily in such efforts, or attach different conditions related to Trump's other priorities.

The tension flaring now during a period of relative calm revolves around the core of Trump's agenda—tariffs—and the extent to which they could spur knock-on inflation in earnest.

Trump's pressure campaign for rate cuts has played out in public in recent months, with the president at times mocking Powell as "Mr. Too Late." After federal data Tuesday suggested inflation accelerated modestly in June—in part due to tariff impacts—Trump said the central bank should slash its roughly 4.3% federal-funds rate by 3 percentage points.

"You say that to any economist, and they don't know whether to laugh or cry," said Blinder, who served at the central bank from 1994 to 1996.

Low interest rates encourage businesses and consumers to borrow and invest more, which can boost economic growth. They also risk pushing inflation substantially higher.

Low rates can also inflate financial markets. Investors, unable to generate strong returns in safe assets, such as short-term Treasury notes, will move into progressively higher-risk assets, where returns are higher, but so is the danger of steep losses.

While low rates can fuel an asset bubble, they can also make it more difficult for the Fed to right the economy after a bubble bursts, notes Robert Barbera, director of the Center for Financial Economics at Johns Hopkins University. That is because with rates already low, the central bank would have less scope for cutting them further. "The room to deliver largesse will greatly shrink if you're in the largesse- provision business all of the time," he said.

The Fed sets a short-term lending rate called the federal funds rate. Trump has argued that the Fed should lower rates because it could help reduce interest payments on the U.S. government's massive pile of debt.

But the short-term borrowing costs controlled by the Fed don't necessarily dictate rates for longer-term loans, like mortgages, offered by commercial banks. Those rates reflect where investors believe the Fed will be setting rates well into the future. They could go substantially higher if they think today's Fed is being pressured into causing tomorrow's inflation problem.

"If you're forcing the central bank to cut short-term interest rates, and it's pretty clear to markets that's the case, then it may well be that long-term interest rates go up in the opposite direction, and in a big way," said Raghuram Rajan, an economist at the University of Chicago Booth School of Business who was governor of the Reserve Bank of India from 2013 to 2016.

This dynamic played out Wednesday immediately after reports of Trump's threat, with investors selling off longdated Treasuries. The U.S. dollar and stock market weakened, while the price of gold—seen as a safe haven in times of financial stress—rallied.

Investors fear that volatility could be a preview of markets' reaction if Trump ends up following through on his threat to fire Powell. Goldman Sachs Chief Executive David Solomon said Wednesday that Fed independence is "something we should fight to preserve."

"I think central bank independence, not just here in the United States but around the world, has served us incredibly well," he told CNBC. Other bank CEOs echoed the sentiment.

Some Fed skeptics question how independent the central bank actually is anyway, since it works alongside the White House in times of crisis. Others question that independence because it may constrain a president's agenda to increase spending, cut taxes or impose tariffs.

Copyright (c)2025 Dow Jones & Company, Inc. All Rights Reserved. 7/18/2025
Powered by TECNAVIA

The following is a digital replica of content from the print newspaper and is intended for the personal use of our members. For commercial reproduction or distribution of Dow Jones printed content, contact: Dow Jones Reprints & Licensing at (800) 843-0008 or visit djreprints.com.
