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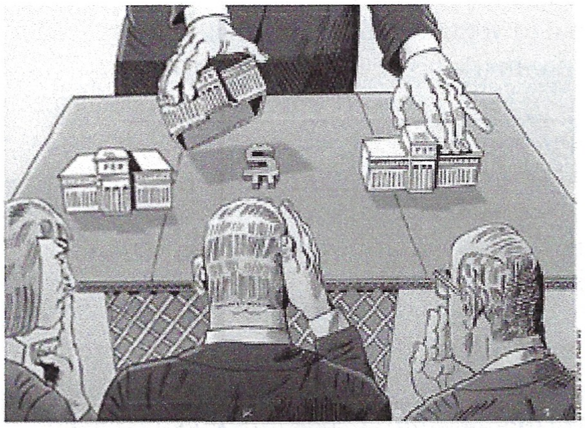
The U.S. built its economic credibility slowly over a long time. Once lost, it won't be easy to regain.



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Trump's Risky Game With the Fed

By Kenneth C. Griffin And Anil K. Kashyap

Note

The U.S. benefits from strong economic fundamentals, yet it faces two challenges: an unsustainable fiscal trajectory and unacceptably high inflation. Elevated long-term interest rates reflect growing market doubts about the stability of inflation and the sustainability of public finances. Without resolution, the government will pay more to finance deficits, young families will struggle to afford homes, and companies will invest less.

Runaway inflation during the Biden administration cost the Democrats in the 2024 elections. Rightfully, President Trump and his administration have made controlling inflation a priority. Lower inflation should naturally produce lower interest rates. But statements and actions that undermine the independence of the Fed risk stoking both higher inflation and higher longterm rates. The president's strategy of publicly criticizing the Fed, suggesting the dismissal of governors,

and pressuring the central bank to adopt a more permissive stance toward inflation carries steep costs. These actions raise inflation expectations, increase market risk premiums, and weaken investor confidence in U.S. institutions.

Mr. Trump's interventions and his dismissal of the head of the Bureau of Labor Statistics have damaged the credibility of official economic data. Together, these developments highlight risks that recall experiences in emerging markets where political influence eroded institutional credibility. While the U.S. benefits from a large stock of credibility accumulated over decades, it isn't limitless. If eroded, markets will demand far higher interest rates for longer-term debt.

History shows the dangers. In the 1970s, the White House pressured the Fed to keep interest rates artificially low. The central bank's reluctance to tighten policy as inflation accelerated contributed to a prolonged surge in prices, regarded as one of the Fed's greatest failures. Research consistently shows that once credibility is compromised, inflation expectations become unanchored, borrowing costs rise, and restoring stability becomes far more difficult.

The U.K.'s recent experience also provides a cautionary tale to the U.S. Political leaders criticized the Bank of England and the Office of National Statistics, questioning their decisions and the accuracy of economic data. Amid elevated inflation and fragile finances, this sparked a crisis of confidence that forced the Bank of England into an emergency intervention to stabilize markets. The consequences remain: The loss of credibility has left the U.K. facing higher borrowing costs, forcing painful fiscal choices involving spending cuts and tax increases.

None of this is to suggest that the Federal Reserve should be insulated from criticism. In recent years, critics and supporters have vigorously debated its response to post-pandemic inflation. The Fed has responded by adjusting its statement on longer-run goals and monetarypolicy strategy—and has learned many painful lessons. Independence isn't a permanent entitlement; it must be earned and maintained through transparency, accountability and performance. But there is a clear process for accountability. Congress has a duty to oversee the Fed, and this oversight must be free of undue interference from the executive branch.

It is in the president's best interest for the Fed to be seen as independent— and to act independently. That independence gives the central bank space to make difficult choices required to curb inflation. In a worst-case scenario, if the Fed visibly bows to political pressure and permits inflation to rise unchecked, tens of millions of retired Americans will see their savings diminished. Senior voters—tired of bearing the brunt of inflation—could cost the administration dearly in the midterms. The president can protect the Fed's independence and further his objectives by nominating qualified candidates in the mold of Govs. Michelle Bowman and Christopher Waller— respected experts who share some of his priorities. The Senate, in turn, should fulfill its constitutional role by ensuring that only well-qualified, independent-minded people are confirmed.

Protecting the Fed's independence is essential, but it is only part of the broader effort needed to strengthen America's economic foundation. To put the nation on a better trajectory, the president should press Congress to reduce government spending and advance reforms that raise long-term growth potential—modernizing permitting, ensuring that taxpayer-supported universities equip students with the skills the future demands, and pursuing immigration policies that attract the world's brightest. Congress must summon the will to halt the surge in the ratio of debt to gross domestic product while structural reforms—targeted deregulation and investment in human capital— reinforce the effort. And an independent Fed must have space to pursue its dual mandate with resolve—restoring inflation to 2% while safeguarding employment.

Credibility in economic policymaking is built slowly, through practice and respect for processes, and can be lost quickly if those processes are disregarded. Preserving credibility is essential because it benefits all Americans by keeping the costs of borrowing money lower, supporting sustainable growth, and maintaining global confidence in U.S. institutions. Once lost, it is costly and time-consuming to rebuild. Protecting it must remain the central priority of U.S. economic policy.

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