

Fed Independence: Safe for Now, but Under Long-Term Threat

January 2026 may go down in history as the month when the Federal Reserve (Fed) successfully defended its short-run independence. But despite winning significant battles, the long-term war could still be lost because President Trump – and possibly his successors – will have time on their side. The first notable event was the Trump Administration launching what Federal Reserve Chair Jerome Powell characterized as a “dishonest attempt at revenge” – a criminal investigation into purported financial improprieties. This extraordinary attack on the central bank’s leader represents an unprecedented escalation in presidential interference with monetary policy. Yet paradoxically, this overreach strengthened rather than weakened the Fed’s independence by mobilizing a chorus of support – from members of Congress to business leaders to the markets more broadly. The success of this defense was evidenced by the fact that financial markets barely flinched. The dollar edged lower, stocks dipped modestly and bond yields rose slightly – reactions that suggested investors viewed the episode more as political theater than genuine threat. This muted response reflects confidence in the institutional safeguards protecting the Fed, at least for now.

The second notable event was the Supreme Court hearing on President Trump’s attempt to fire Federal Reserve Governor Lisa Cook over purported allegations of mortgage fraud. Lower courts had already ruled that Cook could stay in place, at least for now, and the Supreme Court justices signaled that they agreed – as evidenced by prediction markets now assigning just a 3% probability to Cook being removed before the end of February. It is unlikely that Trump will be able to influence interest rates – let alone slash them to the 1% he has called for – for the next year and possibly even for the rest of his term. Unfortunately, while the short-run protections seem stronger than ever, there is very little that would prevent a sustained and concerted effort to remake the Federal Reserve into something very different than it has been for at least the past half century.

Several factors explain why Trump’s frontal assault backfired. First, Powell’s uncharacteristically direct response proved effective – a chair known for careful calibration broke from his usual reserve, amplifying his credibility across the political spectrum. Second, the Senate moved quickly to defend institutional independence. The bipartisan pushback raised the bar considerably for Trump’s nominee Kevin Warsh when Powell’s term as chair expires in May 2026. Third, the structure of monetary policymaking itself provides protection. Interest rates are set by the twelve-member Federal Open Market Committee (FOMC) through majority vote, not presidential decree. Removing Powell would not give Trump control over rate decisions. Recent dissents demonstrate FOMC members increasingly vote their convictions rather than defer to the chair.

The episode makes Powell more likely to remain at the Fed beyond May 2026. While his chair term expires then, his appointment as governor does not end until January 2028, allowing him to continue defending institutional independence as a voting member. And behind all of this are financial markets and business leaders that have reacted strongly when there have been credible threats to the Fed’s independence, but have recovered as those threats have receded. The current controversy invites comparison with the European Central Bank (ECB), which enjoys greater formal independence than the Fed. The ECB president serves a single eight-year non-renewable term, eliminating any incentive to curry favor with political leaders for reappointment. The Fed chair serves a renewable four-year term, creating at least theoretical pressure to accommodate presidential preferences. More fundamentally, the ECB’s legal framework provides clearer protection against political interference. The Maastricht Treaty explicitly prohibits EU institutions and

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Jason Furman, Harvard University, Cambridge, MA, USA.

member state governments from seeking to influence ECB decision-makers. While the Federal Reserve Act protects governors from removal without cause, the definition of “cause” is legally ambiguous – a vulnerability Trump has sought to exploit. Moreover, the fact that the ECB has to deal with 21 different governments dilutes the power of any one of them; in contrast, the Fed is ultimately beholden to the much more powerful U.S. Government.

International comparisons underscore how much ground the U.S. has lost. Academic rankings of central bank independence now place the Federal Reserve in the bottom half globally, a remarkable decline from its position near the top in 1980. The world median for central bank independence has risen steadily, particularly over the past two decades, while the Fed’s formal protections have remained largely static since the 1951 Treasury–Fed Accord. So far, this divergence in the degree of protection from interference has not manifested itself in different policy, economic or financial trajectories. But it could over time. The American central bank was designed to resist short-term political pressure but may prove defenseless against sustained efforts to undermine its autonomy over multiple presidential terms. The mathematics are straightforward. One seat on the seven-member Board of Governors becomes vacant every two years and more if governors choose to leave before their terms are over, a practice that may become less common now that more could be at stake. Over eight years, a determined Trump and his successor could remake the Board’s majority. Once a new group controls the Board in Washington, it could leverage authority over regional Federal Reserve Banks to ensure like-minded regional presidents. New regional presidents require the approval of a majority of the Board in Washington, something it could deploy more aggressively to steer those jobs towards its preferred candidates. Even more aggressively, a majority of the Washington-based Board can dismiss regional presidents for “cause”; it is possible that the legal seriousness of the “cause” required to fire regional presidents, none of whom are confirmed by the Senate, could be considerably weaker than to fire a Senate-confirmed governor like Cook.

Within six to eight years, a committed president could fundamentally transform the institution. The scenario becomes especially concerning if Trump’s approach represents not an aberration but a new normal. If a future Democratic president faces a Fed stacked with Republican partisans, the temptation to respond in kind could prove irresistible. The result would be an institution that swings between administrations, staffed by political operatives rather than technocrats, commanding far less public legitimacy. Even more extreme would be if Trump were replaced by a Republican with a similar mindset who thought the White House, not the Fed, should call the shots on interest rates. These institutional risks carry direct economic consequences. Decades of research demonstrate that central bank independence delivers tangible benefits: lower and more stable inflation, less severe business cycles and no adverse effects on employment or growth.

The Federal Reserve has survived Trump’s aggressive assault with its independence largely intact. But this outcome reflects neither the inevitability of institutional preservation nor the impossibility of future threats. Rather, it demonstrates that independence must be vigilantly defended by courts that maintain high bars for removing Fed officials, senators who insist on independent-minded nominees, which hopefully Warsh will prove to be, and Fed governors who vote their convictions regardless of presidential preferences. The calm market response to the Powell investigation should not breed complacency. Markets reacted calmly because they observed these defenses rapidly mobilizing – senators objecting, former officials speaking out and the system holding. Should those defenses weaken, the market response would likely be less sanguine.

Central bank independence is not a permanent achievement but an ongoing political equilibrium. The U.S. established robust norms of Fed independence over many decades, but norms can erode quickly once breached. Whether Powell’s successful resistance is the high-water mark of independence or merely the opening skirmish in a longer campaign to subordinate monetary policy will depend on the vigilance of America’s political institutions and the wisdom of its voters in the years ahead. For now, the Fed is safe. But “for now” is doing considerable work in that sentence.