Economic and Market Commentary
Trump vs. the Fed: Reshaping Independence and Leadership of the Federal Reserve

September 2, 2025

President Trump has made it clear that he wants lower interest rates and believes that the current Fed has been unwilling to move quickly enough. Trump currently has three appointed members of the 12-member voting committee and will be able to appoint a new chair in 2026, along with an additional member in 2027. It is likely that the new composition of the Fed will be more willing to lower rates, even at the expense of higher inflation.
The media has been reporting that there have been a couple of dissenters on interest rate decisions. Historically, dissenting votes are common within the Fed and have been higher during periods of heightened inflation. And while unusual, this is not the first time that a president has tried to influence the Fed.

Here are some likely consequences of heavier influence by the administration and areas of risk and opportunity for investment portfolios:

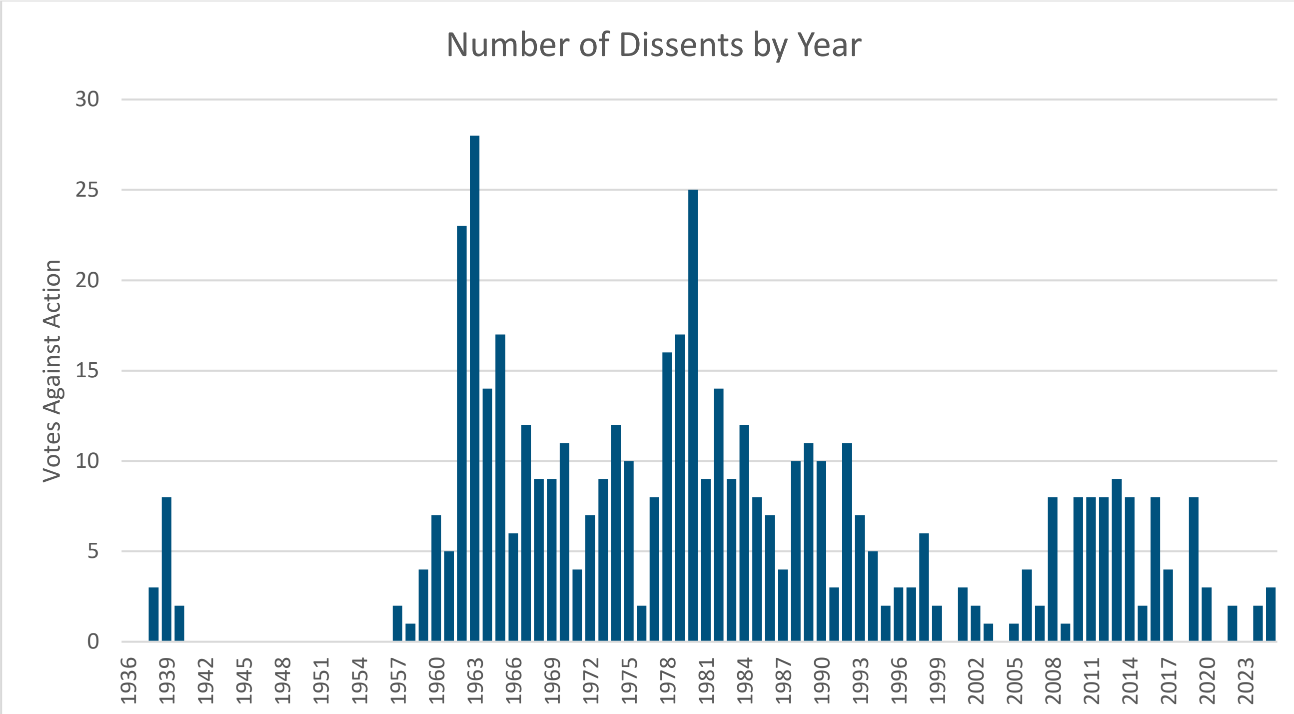
The Federal Reserve and the Federal Open Market Committee (FOMC)

The Federal Reserve was created under the Federal Reserve Act of 1913 following a series of financial panics. Its purpose was to maximize employment, stabilize prices, and moderate long-term interest rates. The FOMC is comprised of seven board of governors (which are appointed by the President of the U.S.) and five of the 12 Federal Reserve Bank presidents, who rotate every year. Fed governors are appointed and confirmed based on 14-year terms that are staggered, so that each U.S. president will likely be able to nominate one to two per term. Currently, three members (including Federal Chairman Powell) were appointed by President Trump with a fourth vacancy set to be filled in September.

The Federal Reserve Bank presidents are elected after serving concurrent five-year terms by their public directors with approval by the board of governors in years that end with one and six. These directors are members of the business community and not representatives of Federal Reserve Bank members in their districts. Federal Reserve Bank presidents tend to have a background in academia/government or Wall Street/consulting.

History and Perspective

There has been a lot of attention on the composition of the FOMC and how members vote. It is assumed that the number of dissenting votes is unusually high and that they are political. The reality is that the number of dissents in the past couple of years is not unusual. In fact, we have seen much higher levels that tend to coincide with periods of increasing inflation or financial crises.



Source: St. Louis Fed

In the 1930's and 1940's, President Roosevelt had significant influence over the Fed to help coordinate with the Treasury during the Great Depression and World War II. The 1950's and 1960's were periods of stability with little political influence. In the early 1970's, President Nixon was able to influence Fed Chairman Burns (1970 to 1978) to lower rates prior to the 1972 election. This provided a short-term economic boom, which was eclipsed by stagflation in the late 70's. Fed Chairman Volcker (1979 to 1987) had political backing to fight inflation even at the expense of short-term pain.

Is the current environment similar to previous periods, or is something structurally changing?

Likely Outcome and Consequences

With a Republican Congress and a couple of forthcoming Fed Governor vacancies to fill, we expect to see a Fed that is more dovish and motivated to get interest rates down quicker than the current or previous members. While the high likelihood of a Fed cut for September was already in the works, it is our belief we will begin to see action in 2026 with a new chairman and one new governor. That would put four of the governors, including the chairman, in a position to influence the rest of the voting members. The wild card will be the voting bank presidents, who will be up for reappointment in February of 2026.

The reasoning behind the pressure to fire and replace Fed Governor Lisa Cook centers on the fact that the Board of Governors must approve the Fed Bank Presidents. With Chairman Powell's term not over until May, President Trump would not have a majority of the governors as appointments to potentially require the reappointment of Fed Bank presidents to commit to lowering rates.

With all this being said, the Board of Governors has never denied the seating of a Federal Reserve Bank president. The next reappointment of a Federal Reserve Bank president will not be until 2031.

While we expect to get a more doveish Fed, we see less likelihood it will be an overwhelming majority of FOMC voters. The frequency of interest rate decision dissents is just picking up, in our opinion.

Market Reactions

If the Fed's independence is seen as at risk, a steepened yield curve seems likely to us. If we get significant interest rate cuts while inflation stays elevated, we anticipate yields on the 10-year and beyond staying near current levels or higher.

The primary reason for a steepening yield curve is the potential for term premium to increase (the spread required to hold longer maturities) due to political uncertainty and the risk of inflation becoming less of a focus. Historically, we have seen term premium increase significantly (in the mid-to-late 1970's as well as right after the last two financial crises). More recently, we have seen inflation expectations pick up with the announcement to remove Governor Cook.

The 10-year yield has managed to stay in a range recently, even with all the potential changes to the Fed. One reason is that the Secretary of Treasury has adopted the policy of issuing mostly short-term bills rather than longer maturity bonds. This has created some degree of scarcity as we have not seen the supply of bonds outstrip demand.

If we were to dive into comments and policy positions by members of the current administration, we would see that the playbook is to get short-term rates down first, then attempt to get longer-term rates down by limiting supply or possibly Yield Curve Control. Yield Curve Control was last used after World War II to artificially keep rates low to manage servicing of the debt. We must also take into consideration the administration wanting a weaker dollar.

What Does the Future Hold

In the short term, we expect to see interest rate cuts by the Fed that will be supportive of assets. We have begun to see a broadening out of equity markets with U.S. small cap stocks recently outperforming large cap stocks along with the continued rally in commodities, mining stocks, and cryptocurrency. Small cap stocks are more sensitive to short-term rates and commodities move with expectations of future inflation and dollar weakness.

While markets have begun to price in a less independent Fed, they still have a long way to go in pricing it in fully. It is possible that some members of the FOMC may vote similarly in line to that of some Supreme Court justice nominations. Candidates tend to stick to political lines during confirmation hearings, but when part of a decision-making committee can be more independent in how they vote. As we get into mid-2026, we will have a better view of how Fed policy is likely to change and how significant those changes will be.