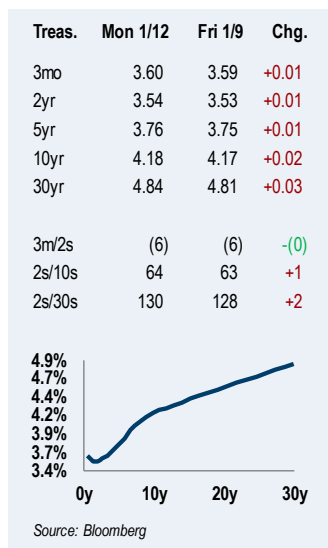




January 12, 2026

RATCHETING UP THE ATTACKS

- The Trump Administration ratcheted up attempts to force the Federal Reserve (Fed) to lower interest rates by opening a DOJ investigation into Federal Reserve Chair Jerome Powell.
- Decades of empirical research across countries show that an independent central bank is a critical part of containing inflation for the long run.
- Attacks on Fed independence make it less likely that the Fed will cut rates, but a successful “political capture” means cuts to short-term interest rates, higher longer-term rates, and potentially significant declines in risk assets.



On January 11, news reports indicated that the U.S. Department of Justice was seeking indictments against Fed Chair Jay Powell related to the renovation of Federal Reserve buildings in Washington. As New York judge Sol Wachtler commented, “A grand jury could indict a ham sandwich.” There is widespread recognition in the financial community that the investigation is aimed at removing Jay Powell so that the Trump Administration may replace him with a more compliant Fed Chair. In response to the news reports, Jay Powell released a [brief video statement](#) criticizing the DOJ investigation and casting it as a debate on “whether the Fed will be able to continue to set interest rates based on evidence...or by political pressure or intimidation.”

Jay Powell’s term as Fed Chair expires in May, though if he chooses, he could remain on until 2028 as a member of the Federal Reserve Board. Any indictment—even a ham sandwich one—against a sitting Fed Chair threatens the independence of the central bank to set interest rates and will have negative effects on the economy and financial markets. Central bank independence seems like an academic topic, but it is one of the underpinnings of stability in growth and inflation over the last four decades.

As one of its primary charges, the Federal Reserve sets overnight interest rates to manage the tradeoff between full employment and inflation. Inflation is a long-term economic force that outlasts any single political cycle. When the Fed (or any central bank) is free to raise interest rates to fight inflation without significant interference, economic and financial markets deem runaway inflation less likely.

In contrast, when there is significant political interference in central bank policymaking, markets lose confidence in the central bank to fight inflation, and inflation naturally rises. Three recent, though extreme, examples include:

- Azerbaijani President Aliyev replacing a long-standing central bank head with a family business connection in 2013, helping inflation rise to 17% by 2016.
- Turkish President Erdogan installing his son-in-law to oversee Türkiye’s central bank in 2018, contributing to a rise in inflation to 20%+ and eventually even higher.
- The Sri Lankan treasury department borrowed directly from the central bank to fund a budget deficit post-COVID, causing inflation to surge to 70%.

When policymakers can’t credibly commit to fighting inflation and instead kowtow to politicians’ demands to stimulate the economy, the economy tends to end up with higher inflation without lasting gains in employment. Beyond these examples,

empirical studies¹ have repeatedly found that more independent central banks are associated with lower and less variable inflation.

As one can intuit from the above list, threats to central bank independence are unheard of among G10 nations; it is more of a problem in developing economies. Here in the U.S., the Federal Reserve is more likely subject to a softer threat to independence that we've dubbed "political capture." Indeed, we cited Fed political capture as the biggest risk to fixed-income markets in our [2026 outlook](#). Unlike in developing economies, there is a long history of institutional credibility with the Fed that will not be erased with a single attack. But a series of efforts to capture the central bank will almost certainly have a series of effects:

1. Force today's central bankers to fight back by cutting interest rates *less* than they otherwise might;
2. Pressure inflation higher and create difficulty fighting inflation if it rises organically;
3. If the capture is successful, push lower overnight interest rates than would otherwise be the case;
4. Force higher long-term interest rates than would otherwise be the case (ironically, foiling the Trump Administration's apparent goals);
5. Widen risk premia on all asset classes.

This last point, wider risk premia, is arguably the most significant immediate problem from Fed political capture. Risk premia represent the additional returns investors require for taking on a risky investment. While inflation upside would take some time to emerge, markets can, of course, respond very quickly. When risk premia widen, investors demand higher compensation and, to get to those higher future returns, prices of all investments have to fall today. That includes things like long-term bonds that are obviously tied to interest rates, as well as stocks and even real estate that are less-directly tied.

The immediate situation is a developing one, and we suspect attempts to charge Jay Powell criminally will be unsuccessful, but the direction of increasing attacks on the Federal Reserve is clear.

¹ [Bade & Parkin \(1985, 2007\)](#), [Chiquiar & Ibarra-Ramírez \(2019\)](#), [Alesina \(1998\)](#) to name several prominent papers all finding similar conclusions.

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