Funding the Future

Trump and the Fed: an MMT perspective

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As is clear from multiple media reports, the dispute between the Trump administration and the US Federal Reserve (which is the US equivalent of the Bank of England, and is the US central bank) has escalated sharply, with its chair, Jerome Powell, now being threatened with criminal indictment in what he describes as political dispute over who controls US interest rate policy.

The headlines have prompted predictable responses. Commentators are suggesting that markets will revolt if Trump ends Fed control, that inflation will surge, that central bank independence is sacred, and that this is how democracies slide into chaos. That is all so very neoliberal, if I might say so.

From an MMT perspective, the most important question is not whether Trump is right or wrong about the level of interest rates. The more important issue is what this row reveals about money, power, and the modern state. If Trump really does go for the Fed and insists that interest rates be cut heavily, as he says is his desire, the economic consequences will matter, but the political and constitutional consequences may matter more.

There are four points that matter to me.

Firstly, the dispute exposes a truth that is rarely discussed, which is that interest rates are a policy choice. The narratives being repeated are that markets set interest rates and that the central bank's job is merely to respond to this external discipline. This is the story of the bond vigilante. That story is convenient to those promoting the power of markets, but it is not accurate. The short-term interest rate at the heart of any monetary system is an administered price. It is set by the central bank, not discovered by a market.

The reality is that the Fed, like any central bank, sets the overnight rate it wants and supplies whatever quantity of reserves is required to ensure the payments system clears at that rate. This is how central banking works. If Trump chose to force rate cuts, it would not demonstrate any new truth about economics. It demonstrates something mundane: the Fed can always set the rate where it wishes, and it always could.

That, in turn, helps explain why so-called central bank independence has become so ideologically loaded. Independence is often described as the removal of politics from money. It is nothing of the sort. It is the relocation of politics into a space where democratic contest is discouraged. The decision about who controls the supply and price of money is always political. The question is simply who is allowed to make that decision, and in whose interest.

Second, rate cuts are not automatically progressive. In fact, in a financialised economy, they tend to inflate wealth. There is a widespread belief that lower interest rates are, by definition, good for the economy. Sometimes they are. But that does depend on what economy one has in mind, and who within that economy holds power.

In a financialised society like the one we live in, interest rate cuts quickly boost asset valuations. Share prices tend to rise. Property prices can rise, especially where supply is constrained. Debt leverage for businesses, and most especially speculators, becomes easier and cheaper. Portfolios gain value. The earliest and largest beneficiaries are often those who already own assets or who can borrow against them at favourable terms. That is not a moral judgement: it is simply the distributional arithmetic of the system we have. That this might be Trump's real motive for cutting interest rates cannot be ignored: he might understand what others are missing.

So, from an MMT perspective, it is never enough to ask whether rates should be cut. We must ask why this is the goal. A rate cut that accompanies a serious strategy to expand capacity through public investment, housing provision, decarbonisation, full employment policy, and stronger public services could have very different consequences from one that accompanies a renewed round of deregulation, tax cuts for the wealthy, hostility to labour, and the encouragement of speculative behaviour. Not all rate cuts are equal, in other words.

In this context, it is very hard to imagine Trump seeking heavy rate cuts as part of a coherent strategy for productive capacity or care. It seems far more likely that he sees them as a route to a market boom that flatters his politics, rewards his constituency, and creates the appearance of success. If so, the likely result is not inclusive prosperity, but another round of wealth inflation and another deepening of inequality.

Third, inflation risk does not arise solely from too much money, as most commentators say is the case at present. Instead, it comes at least as much from economic fragility, weak institutions, and who in the economy holds price-setting power. What this means is that the argument that if politicians subdue central banks and cut rates, inflation will inevitably follow is not necessarily true, as the media often implies, and MMT, I think, rejects this simplistic story.

Inflation is not a monetary plumbing problem. Nor is it the direct product of some imagined quantity of money sloshing around an economy. Inflation arises when nominal spending outstrips real capacity, or when the supply side is disrupted, or when those with market power can raise prices because conditions allow them to do so. Inflation is, then, most often a political economy phenomenon, rooted in fragility, scarcity, conflict, and rent extraction.

In that light, the danger with Trump is not merely that rate cuts might happen at the wrong moment. The danger is that the wider programme surrounding those cuts may itself be structurally inflationary. If you combine trade disruption, tariffs, weakened regulation, politicisation of administration, hostility to planning, and tolerance of monopoly power, you create an economy that is less resilient. Shocks pass through into prices more readily. Firms with market power exploit the resulting instability. Households without bargaining power very obviously suffer the most.

If inflation returns under such conditions, it will not be because the experts were overruled. It will be because an already fragile economy was made more fragile still, by choice.

All of this leads to what seems to me to be the decisive fourth point. Money is not a commodity. It is a legal and constitutional structure. It is issued by the state. It is enforced through taxation. It is the foundation of any state's payment systems. And it is, in the end, a public monopoly.

That is why the question posed by Trump’s assault on the Fed cannot be reduced to the right interest rate. The real issue is what happens when the currency issuer’s authority is subordinated to personal command. There is a difference between democratic accountability and factional capture. There is a difference between using monetary power for public purposes and using it to reward allies and punish opponents. There is a difference between imperfect institutional legitimacy and the domination of institutions by one man’s will. This is the real struggle that is being fought out right now.

MMT insists that the power of the currency issuer should be used openly and transparently to pursue public purposes such as full employment, stable prices, real investment, and the provision of essential services. Trump does not appear to share any of those views. He appears to want to make the currency issuer obedient to him alone, and once obedience replaces legitimacy, the harm can last long after the individual who demanded it has left office, because the precedent remains. This is where the crisis in what Trump is doing comes from: it is all about the collapse of governance over a currency as essential to world well-being as the US dollar is.

So what might happen if Trump wins his battle with the Fed and insists on heavy rate cuts?

The orthodox answer is that inflation expectations might rise, the bond market might sell off, delivering a perverse increase in real interest rates, and confidence might weaken. It cannot be denied, those things could happen.

But the more important MMT answer is that this episode reveals the nature of money as a public monopoly, and then threatens to place that monopoly at the service of private power rather than public purpose. It risks turning monetary policy into a lever for wealth inflation rather than capacity-building. And it increases fragility, which is one of the major sources of modern inflation. That, in turn, points to something much deeper than a technical dispute that is going on here. Trump is pursuing a power struggle for control of the state’s monetary authority for private gain, and that is why the dispute matters. The issue is not about interest rates. The issue is who is trying to cut them, why, and for whose benefit.