

Political Pressure on Central Bank Independence and Corporate Borrowing CostsAuthor: Elsy Ghanem¹*Affiliation:*

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Abstract:

This study asks a simple question with real consequences for corporate finance: does political pressure directed at a central bank's independence, rather than ordinary monetary tightening, show up in the price of corporate debt? Between 2025 and 2026 the Federal Reserve faced an unusually sustained campaign of public pressure from the Trump administration, including repeated demands to cut interest rates to 1% or below, the removal of Governor Lisa Cook, a Department of Justice inquiry connected to the Fed chair's testimony, and the installation of a new chair, Kevin Warsh, who nonetheless voted to raise rates in September 2026 against the White House's wishes. Using publicly reported investment-grade (IG) and high-yield (HY) corporate bond option-adjusted spreads together with Treasury yield data, this paper compares four windows: the 2024 baseline, the April 2025 tariff-driven repricing shock, the third-quarter 2025 compression that followed a routine rate cut, and the independence-specific stress episodes tied to the Cook removal, the DOJ inquiry, and the September 2026 hike. The evidence indicates that markets distinguish between conventional policy moves, which corporate spreads absorbed and then compressed again, and independence-specific political interference, which coincided with a separate widening in long-end Treasury yields even as short-term policy expectations pointed toward cuts. The paper concludes that attacks on central bank independence carry an identifiable borrowing-cost premium distinct from ordinary rate-cycle risk, with implications for corporate treasurers, credit analysts, and the broader debate on the limits of political control over monetary policy.

Keywords:

Central Bank Independence, Corporate Borrowing Costs, Monetary Policy, Political Risk, Corporate Credit Spreads, Federal Reserve, Option-Adjusted Spreads

Introduction:

Nobody really questioned Fed independence until recently. You just assumed the central bank did its job — dual mandate, data-driven, above the political fray — and moved on. That stopped being true in 2025. Trump wanted rates at 1% or lower, and when Powell wouldn't budge fast enough, things escalated quickly: a DOJ inquiry tied to Powell's own testimony, then the removal of Governor Lisa Cook in August 2025, something that hadn't happened before in the Fed's history. Even after Kevin Warsh — Trump's own pick — took over as chair in May 2026, he still voted for a rate hike in September, which tells you something. Trump called the board "hostile" and "political" afterward and kept demanding 1% anyway.

This sequence of events offers an unusual natural laboratory for corporate finance. If bond markets are efficient and forward-looking, they should price political risk to central bank independence separately from ordinary shifts in the policy rate, because the two carry different implications: a rate cut lowers the risk-free benchmark uniformly, while a credible threat to Fed independence raises the probability of future policy mistakes, inflation surprises, and a weaker anchor for long-run rate expectations — all of which corporate borrowers, not just the government, must price into their cost of capital.

The core research question this paper addresses is: did the 2025–2026 political pressure campaign against the Federal Reserve measurably raise corporate borrowing costs, independent of the ordinary rate-cutting cycle that was occurring at the same time? To answer this, the study pursues four objectives: (1) establish a pre-pressure baseline for investment-grade and high-yield corporate spreads; (2) compare that baseline to spread behavior during a clearly identifiable non-independence shock (the April 2025 tariff announcement) to establish what an ordinary macro shock looks like in this market; (3) compare both to spread and yield behavior during the independence-specific episodes (the Cook removal, the DOJ inquiry, and the September 2026 hike); and (4) assess whether long-end Treasury yields, which are more sensitive to inflation-credibility risk than to the current policy rate, moved differently during independence-related episodes than during routine cuts.

Literature Review:

The idea that central bank independence matters isn't new — Kydland and Prescott (1977) laid out the basic problem decades ago: if politicians can lean on monetary policy, they'll always be tempted to juice the economy short-term even if it costs more in inflation later, and markets know this going in. Barro and Gordon (1983) built on that. What I found more useful, honestly, was the empirical side — Cukierman (1992) and later Alesina and Summers (1993) actually went and checked: countries with more independent central banks really do get lower, steadier inflation, without paying for it in lost output. That's the whole argument for keeping the Fed insulated in the first place.

A separate strand of literature examines how markets price policy uncertainty more broadly. Baker, Bloom, and Davis (2016) constructed the widely used Economic Policy Uncertainty index and showed that spikes in policy uncertainty are associated with reduced investment and higher risk premia across asset classes, including corporate credit. Applied to corporate bonds

specifically, the European Central Bank's 2025 review of U.S. spread behavior documented that investment-grade spreads sat at historic lows through 2024 before widening sharply following the announcement of new U.S. tariffs in early 2025, illustrating how quickly a credible macro-policy shock can reprice credit risk even without any change in the fundamentals of individual issuers (Domenech Palacios & Jaňčoková, 2025).

Another important element affecting corporate borrowing costs is the recent AI revolution, Blockchain technology has increased firm performance (Khalife et al., 2024), enhanced the banking sector sustainability, especially in vulnerable environments (Athari et al., 2023), and revolutionized audit practices (Sawaya et al., 2026), thus increasing financial transparency (Saber & Sassine, 2022), technology also allowed the ability to analyze investor sentiments (Khalife et al., 2025), which significantly affected economic growth (Athari et al., 2026) and market efficiency. Some studies argue that the impact of central banks was reduced due to the creation of decentralized assets such as cryptocurrencies (Beainy & Kamel, 2026) and the increase of use of equity financing (Rizk & Sassine, 2023) instead of debt financing. Furthermore, the dependance of the financial system on the US Dollar, renders the actions of other central banks less relevant (Kamel et al., 2025).

What the existing literature has not yet addressed directly is whether the market distinguishes between two categories of policy shock that are often bundled together in casual commentary: an ordinary, even aggressive, change in the policy rate, and a credible threat to the institutional independence of the central bank itself. Sell-side commentary from mid-to-late 2025 hints at such a distinction — several fixed-income outlooks noted that long-end Treasury yields were challenging the 5 percent level specifically because of "nervousness related to the Fed's independence," even as short-end yields moved lower on rate-cut expectations (ABN AMRO Private Banking, 2025). This paper builds directly on that observation, treating it as a testable proposition rather than an aside, and asks whether it also shows up in corporate credit spreads and not just in the Treasury curve.

Methodology:

This paper uses a comparative case-study design built on publicly available, third-party-reported market data rather than a proprietary bond-level dataset, consistent with the scope of a classroom research project. Two families of variables are tracked: (1) corporate credit variables — ICE BofA option-adjusted spreads (OAS) for U.S. investment-grade and high-yield corporate bonds, as reported by the Federal Reserve Economic Data (FRED) database and summarized in the European Central Bank's 2025 Economic Bulletin box on U.S. corporate spread resilience, together with quarterly commentary from asset managers (Columbia Threadneedle, Franklin Templeton); and (2) Treasury-curve variables — the 5-year, 10-year, and 30-year U.S. Treasury

yields, tracked through the same sell-side commentary and contemporaneous financial press coverage of FOMC decisions.

Four comparison windows were defined based on identifiable, dated events rather than arbitrary calendar cuts: (i) the 2024 baseline, representing conditions before the political pressure campaign intensified; (ii) April 2025, capturing the market's reaction to the administration's tariff announcements — a genuine macro shock but not, on its face, an attack on Fed independence; (iii) the third quarter of 2025, after the Fed's first rate cut of the cycle, to observe how spreads behaved once markets had absorbed a routine, telegraphed policy easing; and (iv) the period from Governor Cook's removal in August 2025 through the September 2026 rate hike, encompassing the DOJ inquiry, Chair Warsh's installation, and the hike itself — the cluster of events most directly tied to institutional independence rather than to the rate level per se.

This design has clear limitations, which are treated as a feature of the methodology rather than concealed: the spread figures for windows (iii) and (iv) are reported qualitatively in the underlying commentary (as "multi-decade lows" or spreads "widening" and yields "challenging" a round-number threshold) rather than as the precise weekly OAS series a full econometric event study would require, and no attempt is made here to control statistically for simultaneous macro surprises such as labor-market data or inflation prints that occurred in the same windows. The paper therefore presents itself as a structured comparative case study that establishes a plausible pattern worth testing formally, not as a causal econometric estimate.

Results:

Table 1 summarizes the four comparison windows against the indicators described above.

Window / Event	IG OAS (bps)	HY OAS (bps)	10Y Treasury	Long-end signal
2024 baseline (pre-pressure)	83 - 112	264 - 393	~4.0 - 4.3%	Multi-decade tights
April 2025 tariff repricing shock	120	461	~4.3%	Sharp risk repricing
Q3 2025 (post rate cut, pre-Cook firing)	Multi-decade lows*	Multi-decade lows*	5Y at 3.74%	Spread compression resumes
Aug – Dec 2025 (Cook firing, DOJ probe)	n/a (qualitative widening)	n/a (qualitative widening)	30Y approaching 5%	Independence-risk premium
Sept 2026 (hike despite pressure)	n/a	n/a	10Y at 4.79% (Sept 1)	Highest 10Y since Jan 2025

**Franklin Templeton's Q3 2025 commentary described investment-grade spreads as reaching their tightest levels in roughly 25 years by the end of the quarter, following the Fed's first 2025 rate cut; exact basis-point figures for that specific week were not separately disclosed in the source and are therefore reported qualitatively.*

Two patterns stand out. First, the April 2025 shock and the Q3 2025 rate cut produced opposite effects on corporate spreads despite both being significant, widely anticipated monetary and trade-policy events: the tariff shock widened IG spreads from a 2024 baseline of 83–112 basis points to 120 basis points and pushed high-yield spreads from a 264–393 basis point range to 461 basis points, while the subsequent rate cut — an equally consequential policy action — was followed by spreads compressing back to multi-decade lows within roughly five months. This suggests that ordinary policy actions, even large ones, are absorbed by corporate credit markets once their direction and magnitude become predictable.

Second, and central to this paper's research question, the cluster of independence-specific events behaved differently from either of the ordinary-policy windows. Sell-side commentary from September 2025 describes the 30-year Treasury yield "challenging the 5% yield level" specifically because of nervousness tied to Fed independence, even while the market broadly expected further rate cuts — a combination that would be difficult to explain if investors were pricing only the near-term policy rate. By September 2026, with Warsh at the helm and having just delivered a rate hike opposed by the President, the 10-year Treasury yield reached 4.79 percent, its highest level since January 2025, coinciding with the period of maximum public conflict between the White House and the Fed. Unlike the April 2025 tariff shock, this widening occurred without a comparable single macro catalyst, consistent with the interpretation that markets were pricing a standalone independence-risk premium.

Discussion and Conclusion:

What this basically confirms is something Kydland and Prescott were arguing back in 1977: markets don't just price in where rates are headed, they price in whether the institution setting those rates can still be trusted to do its job. The April 2025 tariff shock rattled spreads and then they came right back down once the Fed cut and everyone understood the plan. The Cook firing and the DOJ probe didn't work that way — there wasn't a clean "shock, then resolution" pattern. Long yields just stayed elevated through it. That's the difference between a market pricing a policy and a market pricing doubt about the whole institution.

For corporate treasurers and credit analysts, the practical implication is that headline Fed rate decisions may be a less reliable signal for the cost of long-term debt issuance than the state of the institution's perceived independence. A firm planning a long-dated bond issuance during a period of acute Fed-independence stress, such as the Cook removal or the DOJ inquiry, may face a higher effective borrowing cost than the prevailing policy rate alone would suggest, purely because of the independence-risk premium embedded in long Treasury yields. For governance and public-policy purposes, the results add an empirical dimension, however preliminary, to a long-standing theoretical argument for shielding monetary policy from short-term political control: the cost of eroding that independence appears to be paid, in part, by ordinary corporate borrowers rather than by the government alone.

This study has clear limitations that also chart the path for future research. Beside not mentioning sustainability which is one of the most important topics in the modern literature (Kaspard et al., 2026), it relies on qualitatively reported spread and yield data, rather than a continuous daily series, limits the precision of the comparison and rules out formal statistical significance testing. A natural extension would construct a proper event-study regression using daily ICE BofA OAS data around exact event dates (the Cook removal announcement, the DOJ inquiry disclosure, the Warsh confirmation vote, and the September 2026 FOMC decision), controlling for contemporaneous macro surprises such as CPI and payrolls releases. A further extension could compare the U.S. experience to other documented episodes of central bank independence pressure, such as Turkey's repeated leadership changes at the Central Bank of the Republic of Turkey, to test whether the borrowing-cost premium identified here generalizes beyond the U.S. institutional context.

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