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Under the weight of public debt: How independent are the ECB and the Fed?

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Summary

The independence of the Fed and the ECB is coming under increasing pressure due to rising public debt. Furthermore, particularly in Europe, the ECB has assumed responsibility for the continued existence of the euro, for financial stability and for climate protection. By expanding their balance sheets and taking on a growing range of responsibilities, both central banks have blurred the lines between monetary and fiscal policy, a development not reflected in academic indicators of central bank independence. The reorientation of the Fed sought by US Treasury Secretary Scott Bessent and Fed Chairman Kevin Warsh could reverse this trend. However, high levels of public debt make a lasting return to a more independent and stability-oriented monetary policy difficult.

Zusammenfassung

Die Unabhängigkeit von Fed und EZB steht wegen steigender Staatsverschuldung zunehmend unter Druck. Zudem hat insbesondere in Europa die EZB die Verantwortung für den Fortbestand des Euro, für die Finanzstabilität sowie für den Klimaschutz übernommen. Beide Zentralbanken haben durch die Ausweitung der Bilanz und wachsende Aufgabenbereiche die Grenzen zwischen Geld- und Fiskalpolitik verwischt, was sich in wissenschaftlichen Indikatoren für Zentralbankunabhängigkeit nicht widerspiegelt hat. Die vom US-Finanzminister Scott Bessent und dem Fed-Vorsitzenden Kevin Warsh angestrebte Neuausrichtung der Fed könnte diese Entwicklung umkehren. Hohe Staatsschulden erschweren jedoch eine dauerhafte Rückkehr zu einer stärker unabhängigen und stabilitätsorientierten Geldpolitik.



1. Central bank independence under pressure

Few politicians have been as outspoken about their preferred course of interest rate policy as openly as US President Donald Trump. In September 2026, he wrote on Truth Social: “LOWER THE INTEREST RATES FOR THE UNITED STATES OF AMERICA, AND FAST!”¹. Trump is still trying to force Lisa Cook out of the Fed’s Board of Governors over alleged misrepresentations in mortgage applications. He has repeatedly insulted former Chair Jerome Powell and initiated criminal investigations against him – which Powell has described as political intimidation.²

ECB President Christine Lagarde has come to Jerome Powell’s defence in this dispute. She has emphasised that, whenever there has been political interference, the result has been lower economic growth and higher inflation. At the same time, there are discussions about Lagarde stepping down early for strategic reasons from the ECB in order to limit the Rassemblement National’s influence on European monetary policy should it win the French election. The Rassemblement National’s presidential candidate, Marine Le Pen, wants to persuade the ECB to drive down yields on the heavily indebted country’s government bonds. Meanwhile, the new Fed Chair, Kevin Warsh – appointed by Trump – is talking about a new Treasury-Fed Accord designed to strengthen the Fed’s independence once again (Broughel 2026; Schnabl 2026).

These developments highlight the tension between formal or legally enshrined central bank independence and political influence. The institutional insulation of monetary policy from political influence is based on the recognition that politically motivated interventions can lead to a more expansionary monetary policy and, consequently, to higher inflation, weaker growth and undesirable distributional effects in the long term.³ For this reason, there have been repeated calls to bind central banks to clearly defined policy rules in order to make them more resistant to political pressure (e.g. Friedman, 1968; Taylor, 1993). Since the 1990s, central bank independence has increasingly established itself as an institutional model worldwide.

On the other hand, however, it seems obvious that there has been – and continues to be more than ever – political pressure on central banks, both behind the scenes and even in the open. How independent are the Fed and the ECB, the institutions entrusted with safeguarding two of the world’s leading currencies? How independent are the two central banks, given that their monetary policy responsibilities,

¹ Capital letters in the original text.

² See the statement by Federal Reserve Chair Jerome H. Powell dated 11 January 2026.

³ This was driven both by economic research into the link between central bank independence and price stability (Alesina and Summers, 1993; Cukierman et al., 1992) and by numerous institutional reforms designed to provide central banks with stronger legal safeguards against political influence (Garriga, 2016; Romelli, 2022).



instruments and interdependencies with fiscal policy have increased significantly – even if their legal safeguards suggest a high degree of formal independence?

2. The independence of the Fed and the ECB

In many cases, a central bank's independence is enshrined in law. This is because democratic governments seek a short-term boost to economic activity through interest rate cuts, as these take effect immediately, whilst inflation only follows with a time lag (Kydland and Prescott, 1977; Barro and Gordon, 1983). Independent central banks are intended to resist this political pressure and pursue a credible monetary policy, geared towards long-term price stability. A high degree of credibility helps to anchor inflation expectations and reduce inflation risk premiums on long-term interest rates. Academic research has shown that a higher degree of central bank independence is associated with lower inflation (Cukierman et al., 1992; Alesina and Summers, 1993; Crowe and Meade, 2008; Garriga, 2016).⁴

At the same time, because monetary policy decisions are removed from direct political control, independence also entails a special duty of accountability. The central bank must justify its decisions to the elected representatives of the people. The greater a central bank's decision-making discretion, the more important transparency, reporting obligations, and transparent and independently reviewable procedures become (Goodhart and Lastra, 2018). Accountability requires central banks to explain their decisions and submit to scrutiny, but it must not give political authorities the power to direct individual monetary policy decisions (Binder, 2021). Accountability becomes more important when central bank decisions have distributional, financial stability or fiscal side effects (Goodhart and Lastra, 2018).⁵

The academic literature distinguishes between legal (*de jure*) and *de facto* central bank independence (Cukierman et al., 1992; Crowe and Meade, 2008). *De jure* independence refers to the institutional safeguards enshrined in law, such as appointment procedures, guarantees of tenure, monetary policy decision-making powers and restrictions on government influence. *De facto* independence, on the other hand, describes the extent to which a central bank can actually make its monetary policy decisions free from political pressure. These two dimensions do not necessarily coincide: Even where there is extensive legal independence, informal influence and political expectations can affect a central bank's decisions.

⁴ More recent studies see the advantage of independent central banks in the anchoring of low inflation expectations. For example, Levin et al. (2004) and Leveuge et al. (2018) show that more independent – and thus more credible – central banks are associated with better-anchored expectations and lower inflation persistence. Dincer and Eichengreen (2014) argue that independence and transparency enhance the effectiveness of monetary policy by improving the impact of monetary policy signals on private-sector expectations.

⁵ For a discussion of the ECB's level of accountability, see De Haan and Eijffinger (2000).



Conversely, established institutional norms can safeguard actual independence even where statutory safeguards are weaker (Cukierman, 1992; Drechsel, 2024).

Whilst legal independence can be measured relatively well on the basis of institutional characteristics, actual independence is difficult to assess. Accordingly, established indicators, including the CBIE Index developed by Romelli (2022, 2024), focus on *de jure* independence. To measure *de facto* independence, factors such as the turnover of central bank governors, expert surveys and documented cases of political influence are taken into account (Cukierman et al., 1992; Drechsel, 2024). However, these approaches can only capture certain aspects of *de facto* independence.

2.1. De jure independence of the Fed

The legal independence of the US Federal Reserve (Fed) is underpinned by several institutional safeguards. These include protecting its leadership from short-term political influence (personal independence), the distribution of monetary policy decision-making powers amongst several bodies (organisational independence), the right to set its own budget (financial independence) and the statutory definition of its mandate. These provisions are designed to ensure that the Fed can make its monetary policy decisions independently of the government's short-term interests.

The members of the Board of Governors of the US Federal Reserve are appointed by the President and must be confirmed by the Senate following a hearing and majority approval by *the Senate Banking Committee*. The members of the seven-person Board of Governors serve a non-renewable term of 14 years, which is staggered so that one term expires every two years. A single administration cannot therefore rapidly reshape the entire Board of Governors. The Chair of the Fed is appointed from among the governors for a four-year term. A change at the helm of the Fed does not therefore necessarily lead to an immediate shift in monetary policy, as all members of the Board of Governors remain in office and are not bound by government directives.

In addition to this structural safeguard, the decentralised decision-making structure contributes to the Fed's independence. Monetary policy decisions are taken by the *Federal Open Market Committee* (FOMC), which comprises members of *the Board of Governors* and the presidents of the 12 regional Federal Reserve Banks.⁶ The distribution of decision-making power amongst several actors makes it more difficult for political influence to be exerted. The presidents of the regional Federal Reserve Banks bring perspectives from different regions of the US economy to monetary policy decisions (Bobrov et al. 2025). The president of the Federal Reserve Bank of

⁶ These are appointed by the Board of Directors of the respective regional Fed and must be confirmed by the Fed's Board of Governors. The term of office is five years. The terms of office of all twelve presidents generally end simultaneously in years ending in 1 or 6; they may subsequently be reappointed for a further five years. Of the regional Feds, five always have voting rights: the President of the Federal Reserve Bank of New York always has a vote, and four others do so on a rotational basis.



New York represents the highly significant perspective of New York, the world's leading financial centre. Monetary policy decisions are stabilised by the involvement of the regional central banks, as this pools a wide range of information and reduces the influence of individual interests (Blinder 2004, Bordo and Istrefi 2023). At the same time, controversial discussions on inflation, employment and financial stability can help ensure that decisions are based more on economic analysis than on individual or political interests (Gehring 2015).

A further dimension of legal independence concerns the Fed's monetary policy mandate and decision-making powers. Whilst the objectives are laid down by law by Congress, the Fed has independent discretion in choosing the instruments to achieve them. Originally, the *Federal Reserve Act* of 1913 did not contain an explicit monetary policy mandate. In 1977, Congress added Section 2A – which remains authoritative to this day – through the *Federal Reserve Reform Act*. This obliges the *Board of Governors* and the FOMC to manage monetary and credit aggregates in line with the economy's long-term production potential, “so as to promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates”. The mandate thus establishes the objectives that guide the Fed's independent monetary policy decisions.

The Fed specifies these statutory objectives as part of its monetary policy strategy. Since January 2012, the official operationalisation of the price stability objective has been that an annual rate of change in the *Personal Consumption Expenditures* (PCE) index of 2 per cent is, in the long run, most consistent with the statutory mandate of price stability.⁷ Maximum employment is assessed on the basis of various labour market indicators, including the unemployment rate and the number of job vacancies. Moderate long-term interest rates are regarded as a natural consequence of price stability and are therefore not pursued as an objective in their own right.

The Fed therefore has some leeway in interpreting and implementing its mandate, but cannot alter the statutory objectives on its own. As the mandate is enshrined in ordinary federal law, it can be amended by Congress through the regular legislative process. This represents an important limitation on the Fed's legal independence, particularly when compared with the ECB, whose mandate is enshrined in European primary law. The Fed can determine the budget required to achieve its objectives itself (financial independence).

⁷ The reviews of the monetary policy framework in 2020 and 2025 also reaffirmed this objective. However, the strategy for achieving it was changed: whilst the framework introduced in 2020 envisaged inflation of slightly above 2 per cent at times following periods of persistently low inflation, with the 2025 reform the Fed returned to flexible inflation targeting and emphasises the anchoring of long-term inflation expectations at 2 per cent.



2.2. De jure independence of the ECB

The legal independence of the European Central Bank (ECB) is ensured, as with the Fed, by personnel and organisational safeguards. These are more firmly enshrined in law, as their institutional foundations are laid down directly in European primary law. The Governing Council, as the supreme decision-making body of the European Central Bank, comprises the six members of the ECB's Executive Board and the governors of the national central banks of the euro area Member States.

The members of the Executive Board are appointed by the European Council for a non-renewable term of eight years (Article 283 TFEU, Article 11.2 of the Statute of the ESCB). In practice, all four major euro area countries – Germany, France, Italy and Spain – are represented on the six-member Executive Board. The governors of the national central banks are appointed in accordance with national law, although the Statute of the ESCB stipulates a minimum term of office of five years (Article 14.2 of the Statute of the ESCB). Reappointment is possible. In this way, the ECB combines long-term personnel continuity with the institutional involvement of the Member States in monetary policy decisions.⁸

The decentralised decision-making structure reflects the supranational character of the ECB. Whilst the six members of the Executive Board have permanent voting rights, a rotation system has been in place for the governors of the national central banks since 2015, limiting the total number of voting rights to 21. The five countries with the greatest economic strength and the largest financial sectors⁹ share four voting rights, whilst the remaining 16 central bank governors hold eleven voting rights. The involvement of the national central banks serves not only to incorporate different economic perspectives, but also to ensure the institutional integration of the Member States into a common monetary policy. However, the members of the Governing Council are bound by the interests of the euro area as a whole and may not take instructions from their national governments.

The legal safeguards underpinning the monetary policy mandate are particularly robust. In accordance with Article 127(1) of the TFEU and Article 2 of the Statute of the ESCB, price stability is the primary objective of the European System of Central Banks. Only insofar as this is possible without compromising the objective of price stability does the ESCB support the general economic policies in the European Union, in order to contribute to the objectives of the Union set out in Article 3 TFEU. This hierarchy of objectives distinguishes the ECB from the Fed, which has a dual mandate.¹⁰ Furthermore, the ECB's mandate is enshrined in European primary law

⁸ Under the voting arrangements, each national central bank governor has one vote when entitled to vote, while the six Executive Board members hold permanent voting rights.

⁹ Germany, France, Italy, the Netherlands and Spain.

¹⁰ However, Fed Chairman Kevin Warsh has recently hinted at a hierarchy of objectives, according to which price stability is a prerequisite for high employment (Warsh, 2026).



and can therefore, in principle, only be amended by a treaty change with the consent of all Member States. The legal hurdle for political reorientation of the mandate is thus significantly higher than for the Fed.¹¹

In addition to these institutional safeguards, primary European law contains two explicit restrictions on political influence. Article 130 TFEU prohibits both the ECB and the national central banks from seeking or accepting instructions from EU institutions or the governments of Member States. In addition, Article 123 TFEU prohibits the monetisation of public debt, in particular the granting of credit to Member States' public authorities and the direct purchase of their debt instruments by the Eurosystem. This is intended to prevent monetary policy from being subordinated to the financing needs of public budgets. However, the prohibition does not, in principle, preclude the purchase of government bonds on the secondary market.

2.3. Measuring the independence of the Fed and the ECB

To date, the measurement of central bank independence has focused predominantly on its legal (*de jure*) dimension. As early as 1978, Bade and Parkin, and later Grilli et al. (1991), developed indicators that assess the degree of a central bank's independence on the basis of legal and institutional characteristics. These include, in particular, the appointment and term of office of central bank leadership, monetary policy decision-making powers, the statutory definition of objectives, and restrictions on the monetary financing of the government. Subsequent approaches expanded and refined these criteria (Cukierman et al., 1992; Jácome and Vázquez, 2008; Romelli, 2022, 2024). The indices derived from these criteria enable international comparisons and the analysis of institutional changes over time.

Fig. 1 compares the legal independence of the Fed and the ECB using available indicators for the year 2023. In addition to Romelli's overall CBIE index, its sub-categories are also shown. There are three alternative indices based on Grilli et al. (1991), Cukierman et al. (1992) and Jácome and Vázquez (2008). The values are standardised on a scale from 0 (no independence) to 1 (maximum independence). Both central banks exhibit a high degree of legal independence, with the ECB achieving higher scores in most categories. This reflects, in particular, the stronger legal safeguards for its mandate and the stricter restrictions on political influence. The comparison also illustrates that the assessment of independence depends on the institutional characteristics taken into account and their weighting.

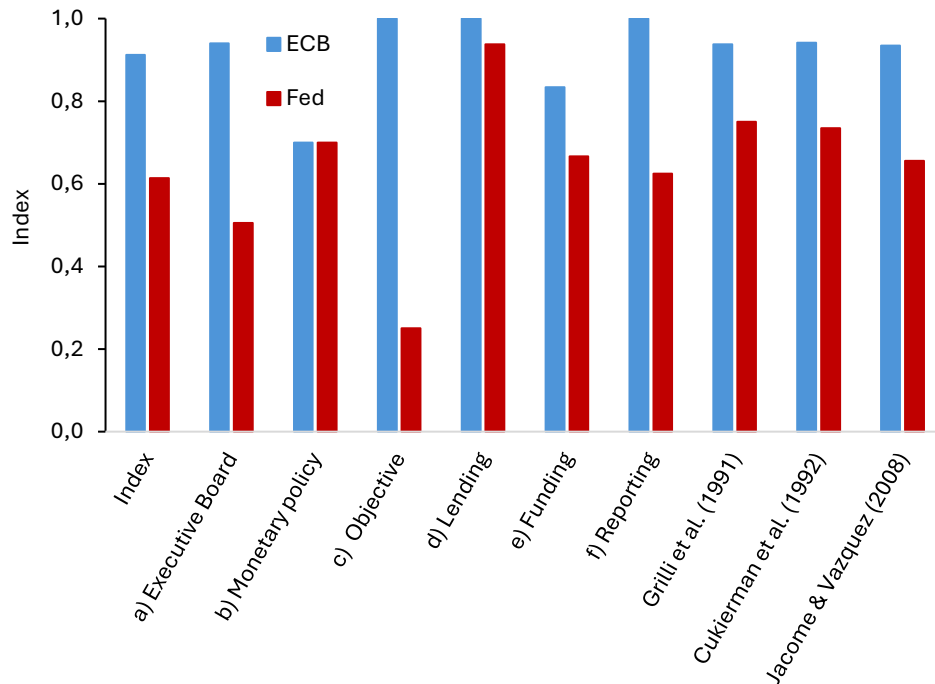
Over time, the academic indicators show that the legal independence of both central banks has remained largely unchanged (Fig. 2). The rise in the Fed index in 1977 reflects the statutory clarification of its mandate through the *Federal Reserve Reform Act*. For the ECB, the index shows a slight decline in connection with the

¹¹ The operationalisation of the mandate has been repeatedly modified over time (Schnabl and Sepp 2021).



transfer of additional tasks in the area of banking supervision in 2014, as this expansion of its remit may create conflicts of interest between monetary policy and banking supervision.

Fig. 1: Measures of the independence of the Fed and the ECB (2023)



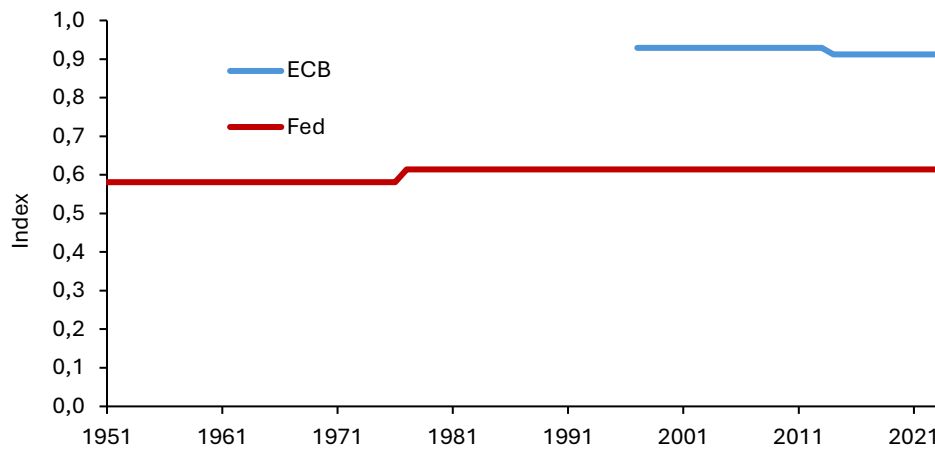
Source: Author's own illustration based on the cbidata.org database. The 'Index' and sub-indicators a) to f) are based on Romelli (2022) and Romelli (2024).

The indicators shown in Figures 1 and 2 capture legal independence exclusively. This also applies to the index by Cukierman et al. (1992) presented there. However, the authors emphasised early on that legal independence does not necessarily correspond to a central bank's actual decision-making autonomy. They therefore supplemented their statutory index with alternative measures of *de facto* independence, in particular the turnover of central bank governors and survey-based assessments of their actual decision-making autonomy. Cukierman and Webb (1995) developed an indicator of political vulnerability that examines changes at the top of the central bank in connection with changes of government.

These approaches provide evidence of political influence, but capture only individual aspects of *de facto* independence and are only comparable to a limited extent between different central banks and over time. More recent studies therefore also draw on historical documents and direct contacts between governments and central bank representatives to identify political influence (Drechsel, 2024; see Chapter 4). A comprehensive indicator of *de facto* independence that is comparable over longer periods has not yet been established.



Fig. 2: Development of de jure independence of the Fed and the ECB



Source: Romelli (2022) and Romelli (2024). 0 = no independence. 1 = maximum independence.

As a result, conventional measures of central bank independence fail to capture an essential dimension: the extent to which central banks can exercise their decision-making autonomy in practice. A high degree of legal independence does not necessarily guarantee that monetary policy decisions are taken free from political influence. Conversely, informal norms and institutional traditions can strengthen actual independence even where statutory safeguards are weaker. For the Fed and the ECB in particular, this therefore raises the question of the extent to which their far-reaching legal safeguards are accompanied by genuine autonomy in monetary policy decision-making.

An analysis of monetary policy practice, in particular the evolution of objectives and instruments, can provide insights into this. The growing interdependence between monetary policy, financial markets and public finances can also shed light on potential political and economic dependencies. Against this background, the following chapter examines the evolution of the Fed's and the ECB's monetary policies and the associated potential implications for their actual independence.

3. The evolution of monetary policy at the ECB and the Fed

The reflections of Hayek (1976), who points to various interests that can put pressure on central banks, provide a theoretical starting point for analysing political influence on monetary policy institutions. From this, three possible channels of influence can be derived.

Firstly, governments' fiscal interests can undermine monetary policy independence. Highly indebted states, in particular, benefit from low interest rates, which limit their borrowing costs, and from inflation, which reduces the real value of nominal public debt. This can create political incentives to push for an expansionary



monetary policy. In many countries, central banks have not been, or are not, independent, but are subject to the instructions of the Treasury.¹²

Secondly, the interests of the financial sector can influence central banks' decisions. Under certain conditions, banks and other financial market participants benefit from favourable refinancing opportunities, additional liquidity and stabilising interventions by central banks during financial crises. This can give rise to expectations of central banks that restrict their scope for monetary policy action, particularly during crises. Revolving-door relationships between private financial institutions and central banks can develop when influential figures from private financial institutions move into senior positions at central banks. Mario Draghi initially worked at the Italian Ministry of Finance, Goldman Sachs and the Banca d'Italia before becoming President of the European Central Bank.

Thirdly, central banks' institutional incentives to expand their remit can contribute to an expansion of sphere of influence. According to Niskanen's (1971) bureaucracy theory, public institutions have incentives to expand their responsibilities, resources and scope for decision-making, as this is associated with higher pay and greater prestige for their leadership. Applied to central banks, this could, for example, involve taking on additional responsibilities in banking supervision or even in areas unrelated to financial markets – such as climate policy. The financial autonomy may facilitate such expansion, as they can allocate the necessary financial resources to themselves. Such an expansion of their mandate can create political interdependencies and conflicts of interest.

These three mechanisms provide an analytical framework for understanding the evolution of the Fed's and the ECB's monetary policy. Particularly since the global financial crisis of 2008/2009, both the Fed and the ECB have significantly expanded their monetary policy instruments and considerably broadened their remit. The following section examines how this development has unfolded and to what extent it may have given rise to dependencies. A distinction must be made between monetary policy measures taken to fulfil the statutory mandate and possible restrictions on actual decision-making autonomy.

3.1 The Fed's evolution from the Greenspan Put through QE to balance sheet expansion

Under Fed Chairman Alan Greenspan (1987–2006), a monetary policy strategy – known as *the Jackson Hole Consensus* – took hold, which attached increasing importance to the stabilisation of the financial markets. Greenspan argued that the Fed could hardly reliably identify speculative exuberance in the financial markets and that interest rate rises to curb potential price bubbles could cause significant

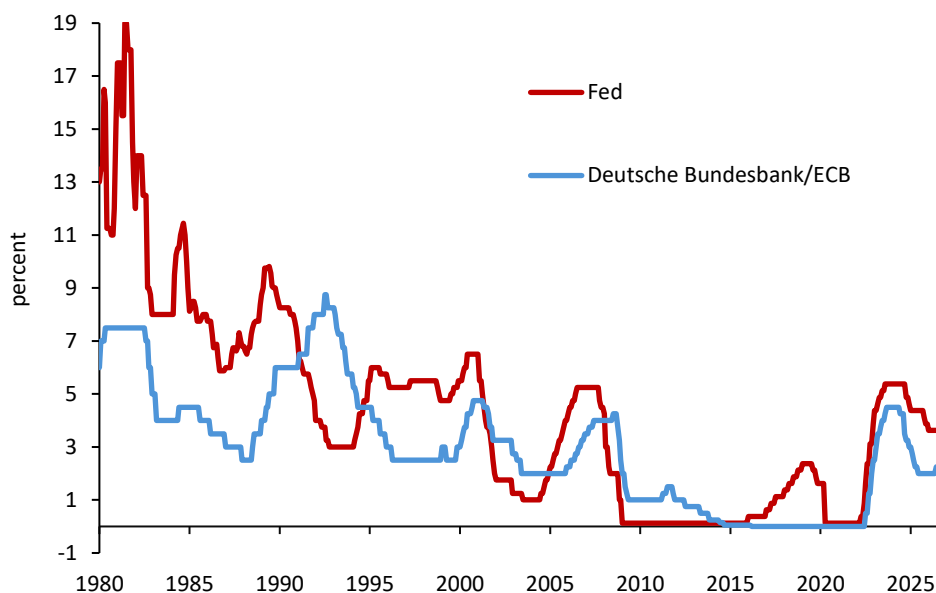
¹² This was also the case, for example, in many of today's eurozone countries prior to the start of the euro adoption process, specifically France, Italy and Spain (De Grauwe 2022).



costs to the real economy. If, on the other hand, a bubble were to burst, the Fed should cut interest rates sharply to prevent an economic crash. The Fed followed this pattern – which later became known as the ‘Greenspan Put’ – during the 1987 stock market crash, the 1998 LTCM crisis and the bursting of the dot-com bubble in 2000. This gave rise to an implicit safety net against financial market losses, a practice also adopted by Greenspan’s successors. As a result, the federal funds rate gradually fell to zero (Fig. 3).

During the global financial crisis of 2008–2009, the Fed, under Ben Bernanke, significantly expanded its interventions. It purchased mortgage-backed securities and government bonds on a large scale to stabilise the financial markets. The various programmes of so-called quantitative easing (QE) caused the Fed’s balance sheet total to grow to nearly nine trillion dollars by 2022 (Fig. 4). At the same time, yields on long-term US government bonds fell to historic lows, reaching around 0.65 per cent at times during the coronavirus crisis (Fig. 5). As US Treasuries are an important benchmark for price discovery on international capital markets, the Fed’s quantitative easing measures constituted a major intervention in both national and international financial markets.

Fig. 3: Key interest rates



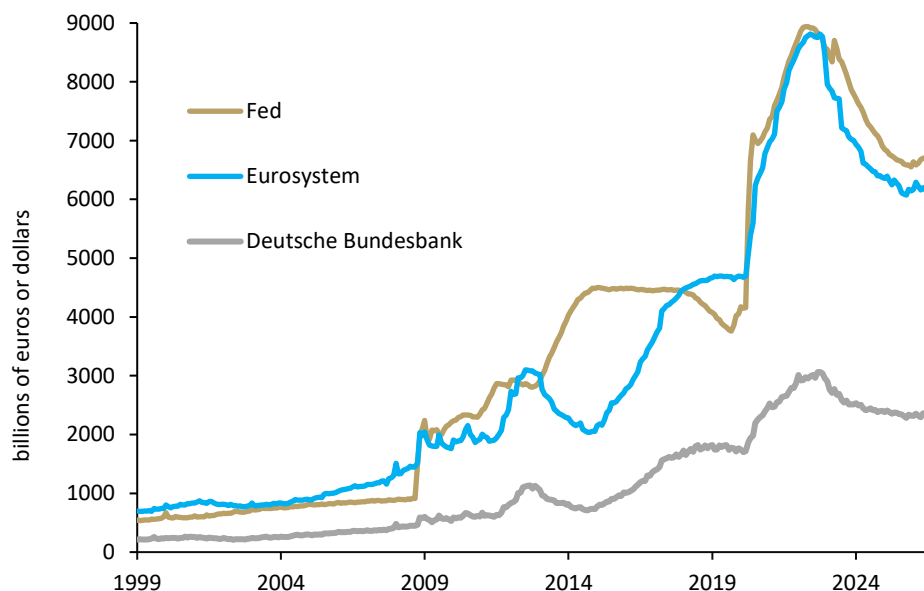
Source: Fed, Deutsche Bundesbank, ECB.

The causes of the long-term decline in interest rates are a matter of debate in the economic literature. Research papers from within the central banking community have emphasised structural factors in particular. Laubach and Williams (2003) and Holston, Laubach and Williams (2017) – papers produced within the Federal



Reserve System – attributed the decline in natural real interest rates, amongst other things, to lower long-term growth potential and changes in saving and investment behaviour.¹³ Bernanke (2005) pointed to a global *saving* glut, which he argued had pushed down US interest rates via international capital flows. These explanations imply that central banks did not themselves significantly cause the long-term decline in interest rates, but rather adjusted their key interest rates to an equilibrium interest rate level that had fallen due to structural factors. These explanations imply that central banks largely accommodated a decline in equilibrium interest rates driven by structural factors, rather than actively causing the decline themselves. As a result, they also tend to diminish the responsibility attributed to central banks for the economic consequences of prolonged low interest rates.¹⁴

Fig. 4: Balance sheet total



Source: Fed, Deutsche Bundesbank, ECB.

In contrast, Gehringer and Mayer (2019), in an empirical study covering the US, the euro area, Japan and the United Kingdom, point to a substantial influence of monetary policy on long-term interest rates. Their findings contradict the notion that central banks merely react to a ‘natural’ interest rate determined independently of

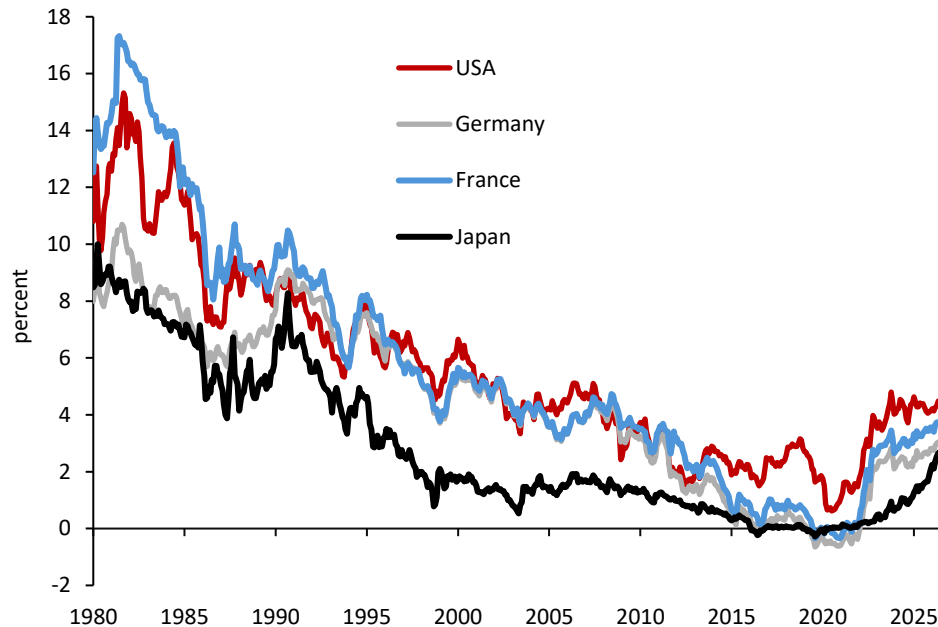
¹³ John Williams was President of the Federal Reserve Bank of San Francisco from 2011 to 2018 and has been President of the Federal Reserve Bank of New York since 2018.

¹⁴ Summers (2014) cited secular stagnation—which reduces demand for capital—as the reason for falling interest rates. Gordon (2017) argued that all viable investment projects had already been undertaken and that growth would therefore remain persistently low and sluggish. On the influence of central banks on academic research, see also Bugdalle (2026).



their own policy.¹⁵ Mayer and Schnabl (2021) demonstrated that there is no measurable correlation between demographics and household savings.

Fig. 5: Yields on 10-year government bonds



Source: OECD, Cabinet Office Japan.

3.2 The ECB's evolution from a focus on stability to an expansion of its remit

The ECB was established with the introduction of the euro, modelled on the stability-oriented approach of the Deutsche Bundesbank. Although its mandate, enshrined in European primary law, has remained largely unchanged, it has significantly altered its monetary policy strategy and instruments over time (Schnabl and Sepp, 2021). Among other things, during the revision of the monetary policy framework in 2003, the reference value for money supply growth (M3) was effectively abandoned and the upper limit for the inflation rate was reinterpreted as a point target.

The uniform, increasingly expansionary monetary policy, characterised by strong money supply growth, was accompanied by significant economic imbalances within the euro area. In some southern Member States in particular, low real interest rates between 2003 and 2007 fuelled strong credit expansion, rising property prices and an increase in government spending. When the financial crisis of 2008–2009

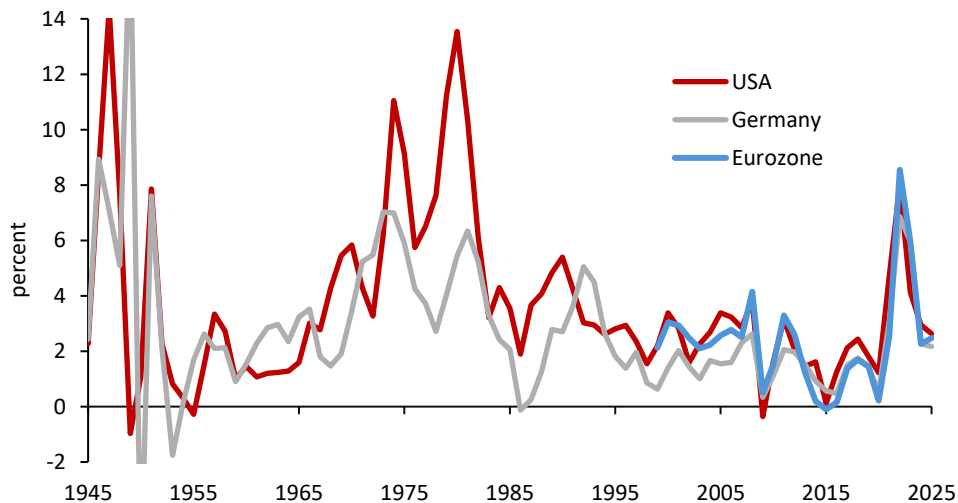
¹⁵ In addition, the method of measuring inflation was changed after the Boskin Commission (1996), commissioned by the US Senate, found that the Consumer Price Index in the US was overestimating the cost of living by around 1.1 percentage points per year. For more on the change in the measurement of inflation, see Schnabl and Sepp (2021).



evolved into the European sovereign debt crisis, the ECB found itself increasingly faced with the task of stabilising not only the price level but also the functioning of the financial markets, the integrity of the euro area and the financing conditions of individual Member States.

A decisive turning point was the announcement of the *Outright Monetary Transactions* (OMT) programme in 2012, which followed ECB President Mario Draghi's pledge to do whatever it takes to preserve the euro. Under certain conditions, the programme allowed for the potentially unlimited purchase of government bonds from individual Member States on the secondary market. Although it was never activated, its mere announcement contributed significantly to reducing the risk premiums on government bonds of highly indebted eurozone countries. From 2015 onwards, extensive government bond purchases followed under the *Asset Purchase Programme* (APP), which were justified by persistently low inflation (see Fig. 6). During the coronavirus crisis, the ECB once again significantly expanded its securities purchases through the *Pandemic Emergency Purchase Programme* (PEPP). The purchases could be distributed more flexibly amongst Member States in order to counteract a fragmentation of financing conditions.

Fig. 6: Consumer price inflation



Source: BIS, Eurostat. Note: To improve international comparability, the Consumer Price Index (CPI) is used for the US instead of the Personal Consumption Expenditures (PCE) price index preferred by the Fed. Both indices show a very similar trend over time.

As a result, the Eurosystem's balance sheet total rose sharply (Fig. 4). Since 2022, the so-called Transmission Protection Instrument has, under certain conditions that leave room for political interpretation, permitted targeted purchases of government bonds from individual euro area countries. The crises thus provided the justification for a transformation of the ECB's monetary policy towards extensive purchases of government bonds. The compatibility with the prohibition on monetary



financing of governments enshrined in the European treaties – particularly in Germany – was legally contentious. Over time, the ECB's toolkit within the framework of unconventional monetary policy became increasingly tailored to developments in individual member states (Pfeifer and Schnabl, 2026).¹⁶

This development raises a fundamental question regarding the distinction between monetary and fiscal policy. The ECB generally justified its interventions on the grounds of ensuring monetary policy transmission and fulfilling its price stability mandate. At the same time, the measures provided significant relief to public finances, particularly in highly indebted Member States. This led to increasing interdependence between monetary policy and fiscal conditions in the euro area, even though the European treaties provide for an independent monetary policy and prohibit the direct monetary financing of government.

3.3. De facto independence of the Fed and the ECB

The analysis shows that, despite their legal independence remaining largely unchanged, the monetary policy practices of the Fed and the ECB have changed considerably. Expansionary monetary policy has not only influenced financing conditions but has also broadened the economic scope for action available to governments and financial market participants. This may have given rise to, or reinforced, interests that run counter to monetary tightening. The three mechanisms outlined at the outset provide a framework for examining the potential implications for de facto independence.

Given the growing interdependence between monetary and fiscal policy, low interest rates and large-scale government bond purchases reduce the financing costs of public budgets and allow for higher levels of public debt without a corresponding rise in current interest expenditure. This creates a significant incentive for highly indebted countries to favour a permanently expansionary monetary policy. This is because rising interest rates undermine the sustainability of public finances and can trigger political pressure on central banks to scale back planned interest rate rises. In the euro area, the announcement of the OMT programme in 2012 and the ECB's subsequent government bond purchases already contributed significantly to reducing the financing costs of highly indebted Member States. The ECB justified these measures on the grounds of ensuring monetary policy transmission, presumably also because providing long-term relief for government budgets does not form part of its monetary policy mandate.

To the extent that concerns about government borrowing costs shape monetary policy decisions, they create a potential conflict with the principle of monetary policy independence and its commitment to price stability. The ECB's interventions

¹⁶ This marked a departure from the principle that there should be a single, common monetary policy for all member states – *'one size fits all'*.



may therefore be interpreted as indications of a growing risk of fiscal dominance, whereby fiscal considerations increasingly constrain the central bank's monetary policy autonomy (Braun, 2018; Jones and Matthijs, 2019). For instance, the Governor of the National Bank of Belgium, Pierre Wunsch, has argued with regard to the European Central Bank that it is unable to act without taking into account the fiscal implications of its monetary policy decisions (Barwick, 2023).

In the US, the Fed's expansionary monetary policy has come under increasing criticism from this perspective. The current US Treasury Secretary, Scott Bessent (2025), has argued that the Fed has blurred the line between monetary and fiscal policy through its extensive government bond purchases. The new Fed Chair, Kevin Warsh (2026), described the extensive government bond purchases as '*fiscal policy in disguise*'. The criticism is directed in particular against the Fed's role as a major creditor to the US government and the associated support for favourable government borrowing conditions.

As for the second mechanism – the financial markets' growing dependence on monetary policy support – the 'Greenspan Put' had established the expectation that the Fed would intervene to stabilise the markets in the event of significant price falls. Subsequent quantitative easing programmes reinforced this expectation by lowering long-term interest rates and risk premiums and boosting demand for financial assets. Sharply rising share and property prices fuelled high profits for financial market players. The new Fed Chair, Kevin Warsh, has accordingly criticised the Fed's long-standing monetary policy as a redistribution from Main Street to Wall Street (Schnabl, 2026).

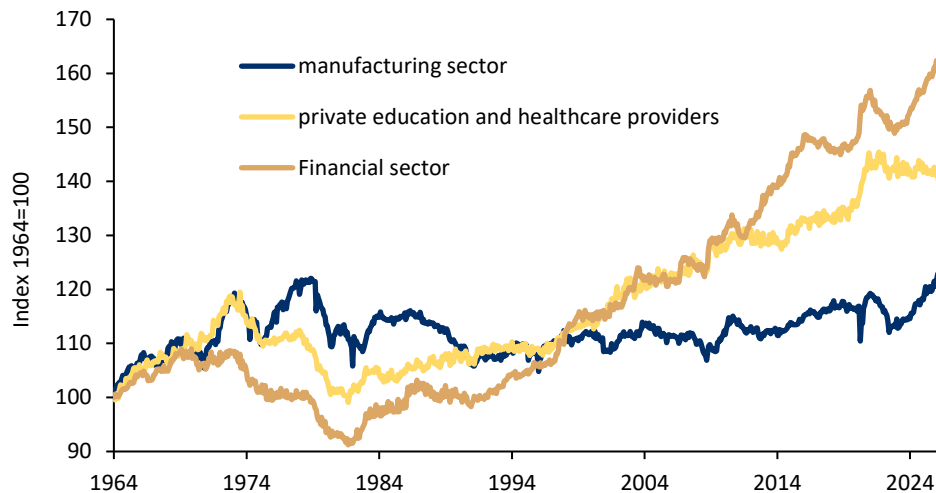
The distributional effects of the expansionary monetary policy were not confined to the asset markets. Low interest rates also expanded the scope for fiscal spending, thereby benefiting sectors of the economy that profited significantly from the expansion of government expenditure. In the US, this applies in particular to the education and healthcare sectors, where government funding, public insurance schemes and regulatory decisions play a key role. Rising government expenditure in these sectors can increase demand for labour and support positive wage growth.

Against this backdrop, the divergent sectoral trends in real wages in the US are revealing (Fig. 7). Whilst employees in the education, healthcare and financial sectors recorded real wage growth over a long period – particularly during the prolonged phase of predominantly expansionary monetary policy – wage growth in the manufacturing sector was significantly weaker. This pattern is consistent with the hypothesis that expansionary monetary policy disproportionately benefited sectors



closely linked to government spending and financial markets, both through rising asset prices and by expanding the fiscal room for manoeuvre.¹⁷

Fig. 7: Sectoral real wage trends in the US



Source: Bureau of Labor Statistics.

The current US Treasury Secretary, Scott Bessent (2025), has criticised the bureaucratic expansion at the Fed. He argues that, through the sharp expansion of its balance sheet, the Fed has extended its remit beyond the statutory dual mandate of price stability and maximum employment to encompass an ever-expanding range of economic, financial and social policy objectives (*mission creep*). Similarly, the ECB has expanded its mandate. In the course of the euro crisis, it assumed responsibility for the cohesion of the euro area and took over the supervision of the major banks.

In essence, the ECB effectively moved away from the principle of market neutrality (Cœuré, 2015). This principle states that, when intervening in financial markets, a central bank should avoid systematically distorting relative prices or favouring certain sectors, issuers or countries.¹⁸ ECB Executive Board member Isabel Schnabel (2021) argued in favour of replacing the existing principle of market neutrality with the principle of climate-oriented market efficiency.

In July 2021, the ECB announced the integration of climate change into its monetary policy framework. The focus was on bond purchases and the requirements for the provision of collateral in refinancing operations with the ECB. This was followed in July 2022 by the decision to target corporate bond purchases under the CSPP and the PEPP towards issuers with a better climate track record – as measured by

¹⁷ In addition to monetary policy, sectoral wage trends can also be influenced by other factors, such as differences in productivity, changes in the employment structure and international competitive conditions.

¹⁸ By purchasing substantial quantities of government and corporate bonds, the ECB directly influenced their yields, reduced risk premiums and altered the allocation of capital between countries and sectors.



emissions, transition targets and the quality of disclosure – and to introduce climate-related disclosure requirements for private-sector assets (ECB 2021; ECB 2022). In July 2025, the ECB incorporated a climate factor into the valuation of assets used in the central bank’s refinancing operations (ECB 2025). Critics, however, see this as a move towards industrial policy objectives, as the central bank’s decisions influence relative financing costs and thus alter the allocation of capital between companies and sectors (Gehring 2022).

Furthermore, ECB President Christine Lagarde (2020) announced in 2020 that, in an increasingly digitalised economy, the strength and autonomy of European payment systems must be safeguarded. Since then, the ECB has pushed for the introduction of a digital euro, arguing that Europe must break the dominance of American payment systems in Europe. To this end, the ECB has initiated a legislative process in Brussels. The digital euro has taken on political dimensions because the ECB is thereby assuming a more active role in European payments and intervening in a payment system that has hitherto been organised predominantly by the private sector. This raises questions regarding competition with private payment service providers, the protection of personal payment data and the democratic oversight of a state-provided digital payment infrastructure.

The ECB’s reorientation of monetary policy – which has taken place even without formal changes to its mandate – can be understood as a far-reaching politicisation of the central bank. This increases the political sensitivity of its decisions and creates additional channels for controversy and criticism that could undermine its credibility.

4. A turning point for central bank independence?

If price stability is subordinated to the government’s financing needs or other objectives, inflation rises and growth falls (Weise 2012; Ahmed et al. 2021). Sections of the population closer to the state – e.g. civil servants – benefit at the expense of other sections of the population, who suffer from rising prices. If the financial sector is stabilised through low interest rates, it benefits at the expense of other sectors of the economy. If inflationary pressure and the associated public discontent become too great, this can lead to a political upheaval, as is currently being observed in Argentina.¹⁹ There have been repeated instances in the past of monetary policy realignments despite an unchanged institutional framework.

¹⁹ There, the Peronists have for a long time financed high levels of government spending with the help of the central bank, with social groups close to the Peronists in particular benefiting from this excessive government spending. The entire population had to bear the burden through high inflation. During his election campaign, the new president, Javier Milei, had promised to put an end to large-scale redistribution. Through drastic spending cuts and the resulting reduction in the budget deficit, he has achieved a significant decline in inflation (see Kleinheyer and Schnabl 2025).



4.1. Historical precedents for a monetary policy reversal in the United States

The 1950s and 1960s were a period of high monetary stability in the Western world, as the dollar was pegged to gold and other currencies were pegged to the dollar. The Fed regained its independence in 1951 and kept the dollar stable. In the second half of the 1960s, however, the Vietnam War increased the US's financing burdens. President Lyndon B. Johnson exerted increasing pressure on the Chairman of the Federal Reserve, William McChesney Martin, to help finance the Vietnam War and the government's 'Great Society' programme through the purchase of government bonds.²⁰ Archival records show that, due to political pressure, members of the Federal Reserve's Open Market Committee delayed necessary monetary tightening measures (Weise 2012).

Even when inflationary pressures were evident, central bankers weighed monetary policy objectives against the anticipated political costs. In 1969, President Richard Nixon appointed his close confidant Arthur Burns as Chairman of the Federal Reserve, and put pressure on him to cut interest rates – particularly as the 1972 re-election campaign approached.²¹ Burns is reported to have told a journalist that a Fed Chairman ultimately had to do what the President demanded, as otherwise the central bank would lose its independence (French, 2010). When inflation subsequently rose sharply in the 1970s, Burns attributed this to one-off factors such as rising oil prices due to geopolitical tensions or rising food prices caused by droughts (Roach 2021).²²

However, the sharp expansion of the money supply led to a combination of inflation, low growth and rising unemployment (stagflation). Furthermore, the dollar came under pressure as the international reserve currency: by the end of the 1970s, the US could only finance itself adequately abroad by issuing bonds denominated in German marks and Swiss francs. This subsequently led to a new shift in monetary policy. In the late 1970s, Paul Volcker succeeded William Miller as Chair of the Fed; Miller, who had succeeded Arthur Burns, had served for only 17 months and was regarded as too 'dovish' (Medley 2013). President Jimmy Carter appointed Miller as Secretary of the Treasury, thus clearing the way for Volcker. He was regarded as someone who was prepared to fight inflation consistently, even in the face of

²⁰ Johnson is said to have summoned Martin to his ranch in Texas to criticise him sharply over interest rate rises (Fessenden 2016).

²¹ Audio recordings and diaries illustrate the intensity of this pressure, with discussions on monetary policy being closely linked to electoral considerations (Drechsel 2024).

²² The expansionary monetary policy of the 1970s was justified in academic circles on the grounds that inflation could reduce unemployment (Samuelson and Solow 1960). From this, for example, the German Chancellor Helmut Schmidt derived the view that he would rather have five per cent inflation than five per cent unemployment.

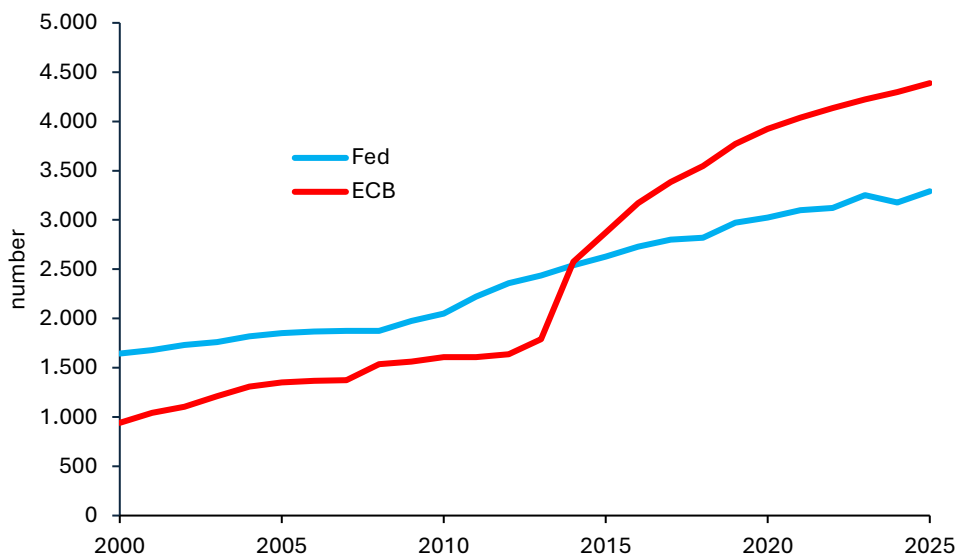


political resistance.²³ Volcker raised key interest rates sharply (Fig. 3), which, following a brief recession, ultimately led to the period of low inflation in the 1980s.

4.2. The Bessent–Warsh critique

Criticism of the expansionary monetary policy of recent decades has found its way into a potential shift in the Fed's policy direction through US Treasury Secretary Scott Bessent and the new Fed Chair Kevin Warsh. Bessent (2025) accuses the Fed of having expanded its remit far beyond its original monetary policy mandate since the 2008 global financial crisis. He includes among these the management of asset prices, extensive government bond purchases, a growing role in banking supervision and regulation, and the consideration of additional economic policy objectives (see above). As an expression of this institutional expansion, Bessent points to the sharp rise in the Fed's workforce and budget (Fig. 8 and Fig. 9). As the Fed is predominantly self-financed from its own income and its day-to-day expenditure is not subject to Congress's regular budgetary approval process, he sees this as a problem for democratic accountability. The Fed expanded its balance sheet from around 900 billion dollars before the financial crisis to, at times, nearly nine trillion dollars (see Fig. 4), without congressional approval.

Fig. 8: Number of staff positions at the Fed and the ECB



Source: Fed and ECB annual reports. From 2018 onwards, annual averages rather than figures as at the reporting date.

However, Bessent's criticism is directed not only at the scale of central bank activities, but also at their economic consequences. He argues that the Fed has systematically overestimated its own ability to steer the economy and, on the basis of

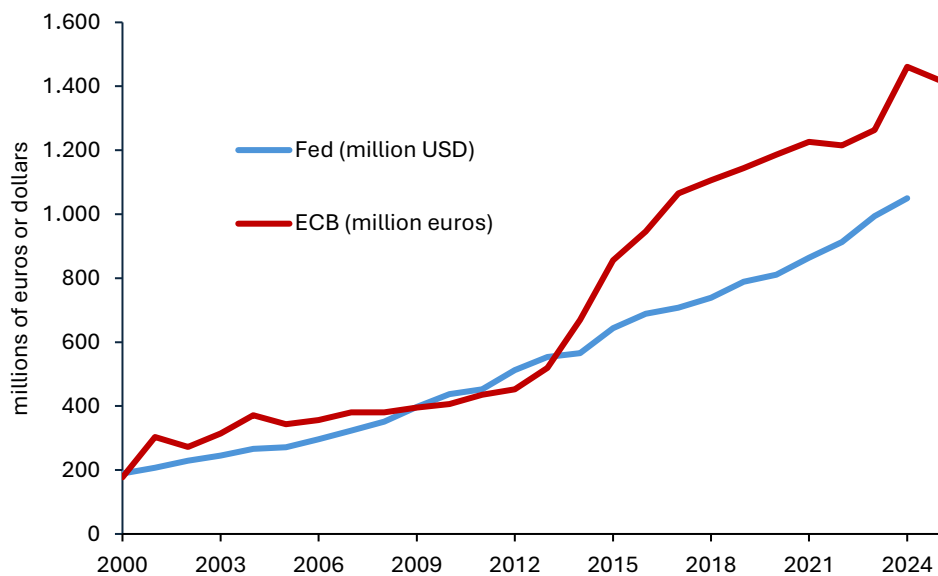
²³ At a conference of the American Bankers Association in San Francisco, Volcker responded to pressure from the Treasury Secretary to cut interest rates by stating that, despite unusual communication from the Treasury, the Fed had no plans to lower interest rates (Todd 2012).



flawed models, misjudged the impact of its policies on inflation and growth. In Bessent's assessment, the Fed's policies have redistributed resources in favour of financial markets. Its purchases of mortgage-backed securities have influenced the allocation of credit, while its large-scale purchases of government bonds have blurred the boundary between monetary and fiscal policy.

Bessent's criticism thus addresses the three mechanisms previously discussed that may limit the actual independence of central banks: fiscal interests, the growing importance of financial market stabilisation, and the institutional expansion of the Fed's remit. As these developments have undermined the Fed's independence and credibility, the Fed should return to its original, narrow and clearly measurable mandate. A similar debate, however, does not yet exist in the euro area. Following the recent rise in yields on French government bonds, a debate has begun in France regarding the ECB's role in relation to yields on French government bonds. In the broader context, the question is currently being raised as to whether the ECB will once again safeguard the cohesion of the euro in the event of a potential new euro crisis.

Figure 9: Development of the Fed's and the ECB's budgets



Source: Annual reports of the ECB and the Fed.

4.3. Warsh's reform agenda

Building on the critique put forward by Bessent (2025), Warsh (2026) presented a reform agenda in his speech at Jackson Hole, aimed at a more rule-based and restrained approach to monetary policy guided by its statutory mandate. The starting point is his critique of the assumptions on which the expansionary monetary policy of recent decades was based. In particular, he considers the notions of a permanent global savings glut (Bernanke, 2005) and permanent secular stagnation (Summers, 2015; Gordon, 2017) to be outdated in light of new technological developments.



Artificial intelligence, he argues, opens up considerable potential for productivity gains whilst simultaneously creating a high demand for capital. Monetary policy must take these changes into account, rather than assuming a structural oversupply of savings and weak investment opportunities.

A key component of the reform agenda concerns the Fed's communication and decision-making. Warsh is particularly critical of the practice of *forward guidance*, whereby central banks communicate their expected future interest rate policy to the financial markets. Committing too firmly to future decisions would restrict monetary policy flexibility and impair the information function of the financial markets. If market participants base their expectations predominantly on the Fed's announcements, and the Fed in turn uses these market expectations to assess the economic situation, this can result in mutually reinforcing misjudgements. Warsh therefore advocates a more restrained approach to communication, leaving market participants more scope for independent assessments.

Furthermore, Warsh sets out six guiding principles for future monetary policy. Firstly, decisions should be based on data that is as up-to-date, relevant and reliable as possible, with greater weight given to longer-term trends than to individual data points. Secondly, the Fed must assess the relationship between aggregate demand and supply, whilst remaining mindful of the considerable uncertainty surrounding potential output. Thirdly, Warsh reaffirms the inflation target of two per cent, measured by the Personal Consumption Expenditures (PCE) price index, as a binding monetary policy target. Fourthly, he sees no fundamental conflict of objectives between price stability and maximum employment in the medium term, as high inflation itself undermines employment and economic prosperity.

The other two principles relate directly to the monetary policy toolkit. Fifthly, short-term interest rates should once again form the central instrument of monetary policy, whilst unconventional measures should remain confined to exceptional crisis situations. Sixthly, Warsh again attaches greater importance to the money supply. In this context, both the monetary base created by the central bank and the money created by commercial banks should be taken into account.²⁴ Although, according to Warsh, financial innovations alter the relationships between the money supply, velocity of circulation and economic activity, this does not justify neglecting monetary developments when assessing future inflation risks.

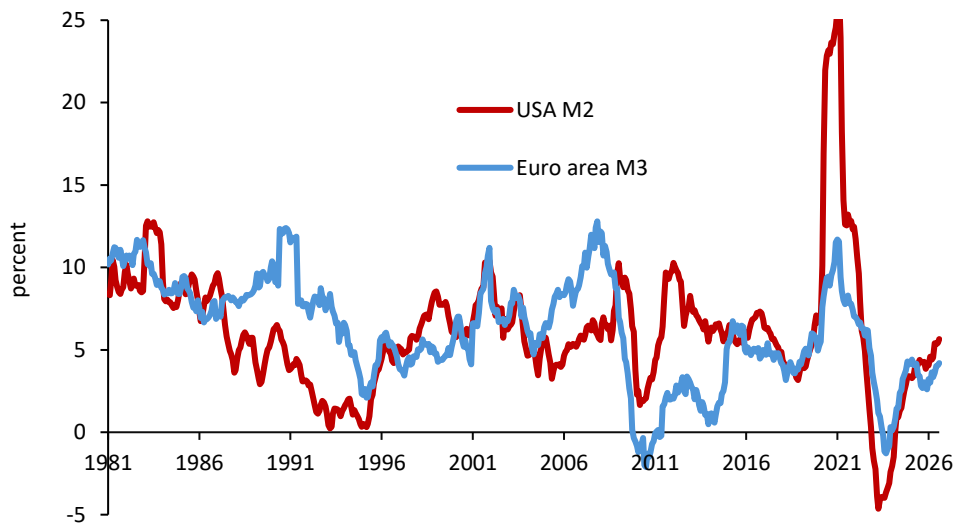
The significance of this final principle is illustrated by the trend in monetary aggregates in the US and the euro area (Fig. 10). In particular, the sharp rise in money supply growth in 2020 was not regarded by either the Fed or the ECB as a sufficient warning sign of the subsequent sharp rise in inflation. From Warsh's (2026) perspective, this argues in favour of giving greater consideration to monetary

²⁴ See also Warsh (2022). This is consistent with Friedman's (1963) view that inflation is always and everywhere a monetary phenomenon.



aggregates and conducting a more critical review of the monetary policy models used to date. Warsh aims to stabilise the dollar by reducing the Fed's balance sheet, which, in his view, is linked to depoliticising the Fed (Schnabl 2026).

Fig. 10: Money supply growth



Source: Annual reports of the ECB and the Fed.

5. Outlook: When government debt dictates monetary policy

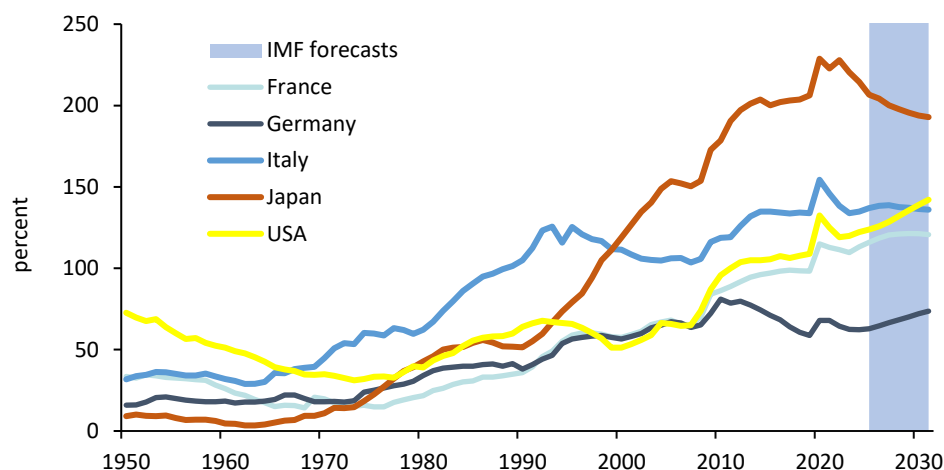
Whilst central banks may be institutionally independent, the appointment of senior central bankers by politicians provides a gateway for political influence. The Deutsche Bundesbank, which had long enjoyed a high degree of independence, is likely to have been the exception rather than the rule since the abandonment of the gold standard in the early 1970s. A review of the development of the US Federal Reserve's independence shows that, within a largely unchanged institutional framework of the Federal Reserve System, monetary policies could be shaped in very different ways. In this light, central bank independence risks becoming little more than a fig leaf rather than a reliable safeguard of lasting monetary stability.

This is likely also to be the case for the European Central Bank, which started out with a high degree of independence (monetary dominance) and has, over time, moved closer to the practice of monetary financing of government expenditure in the euro area (fiscal dominance). This has gone hand in hand with an increasing erosion of debt control mechanisms within the EU (Bugdalle 2025). Central banks can use this growing fiscal dominance to expand their sphere of influence. For the European Central Bank, the expansion of its remit and the associated increase in its budget are particularly striking (see Fig. 8 and Fig. 9). However, a look at the US in the late 1970s also shows that a shift towards a more stability-oriented monetary policy can be politically desired and consistently brought about.



This raises the question of whether the US is currently at a similar juncture to that of the late 1970s. One parallel is that the dollar's status as the world's reserve currency is under threat today as well (Gehring 2026). Major holders of dollar reserves, such as China and Russia, have significantly reduced their holdings of US Treasuries, and the dollar's share of global currency reserves has declined in favour of gold. If the US does not wish to jeopardise the dollar's status as the world's reserve currency, stabilising the dollar in line with the strategy advocated by Scott Bessent and Kevin Warsh is in the US's political interest. However, this is countered by President Donald Trump's attacks on the Fed and potential resistance within the Fed itself, possibly from the President of the Federal Reserve Bank of New York, John Williams (2026), who is likely to represent continuity with the Fed's pre-Warsh monetary policy approach.

Figure 11: Public debt as a percentage of gross domestic product



Source: IMF.

Ultimately, however, the struggle between governments and central banks may be decided less by political intentions than by economic realities. Historically, pressure on central banks to finance government spending has been particularly high when public debt was high. In the US, public debt as a proportion of gross domestic product currently stands at 123 per cent, a level similar to that seen after the Second World War (Fig. 11). Further interest rate rises by the Fed would increase the US government's interest burden even further, even though interest expenditure is already higher than military expenditure. A sustained restrictive monetary policy by the Fed would necessitate a significant cut in government spending, which Donald Trump has so far failed to achieve despite initially ambitious austerity targets – and shows no sign of making further efforts in this direction.

In a Europe reluctant to reform, the desire for monetary financing of government debt is likely to be even greater in some large eurozone countries such as France. Amid growing concerns about a sovereign debt crisis in France and, consequently,



a new euro crisis, Finance Minister Roland Lescure and the promising presidential candidate Marine Le Pen have already publicly considered whether the ECB could reduce yields on French government bonds. By announcing the so-called Transmission Protection Instrument, the ECB has positioned itself to rescue the euro once again – a task that is, in fact, a fiscal one. A shift away from the ECB's increasing politicisation therefore seems unlikely.



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