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More political intrigue around the Federal Reserve

What's moving markets

- In a public statement on January 11, Federal Reserve (Fed) Chairman Jerome Powell announced that he had been subpoenaed by the Department of Justice in an investigation of Fed headquarters renovations during 2025.¹
- The announcement comes only two weeks before the U.S. Supreme Court is scheduled to hear arguments on the Trump administration's case to dismiss Fed Governor Lisa Cook, over alleged mortgage fraud.²
- Investors were surprised by the Sunday evening statement, and U.S. financial futures markets retreated by a fraction of a percent in the S&P 500 Index, the 10-year U.S. Treasury, and the U.S. dollar exchange rate against major global currencies. Gold prices rose 1.8% in the overnight hours.

Our perspective

- Gold's rise, coupled with the negative financial market reaction, seem to us a reflexive reaction to a new chapter in the Trump administration's attempts to influence monetary policy to cut interest rates more aggressively than what the Fed delivered in 2025.
- Such a threat is concerning, but the administration's chances of controlling Fed policy seem low:
- First, the 2026 U.S. economy seems set to outpace its post-World War II average. Aggressive interest rate cuts might overheat the economy and raise inflation. We believe any Fed Board of Governors will want to prioritize above all else the preservation of its reputation for inflation control.
- Second, to control the Federal Open Market Committee, the administration would have to secure a majority of the 12 voting members of seven governors and five regional Reserve Bank presidents. The current Board just reaffirmed the existing set of Bank presidents, and President Trump may have a maximum of three governor seats to fill. Even if he were to control these three, the legal steps involved could take years to complete.
- Finally, signs of bipartisan Senate Banking Committee opposition to such a replacement plan is already public.³

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1. Howard Schneider and Ann Saphir, "Trump team ramps up attack on Fed's Powell with criminal indictment threat", Reuters, January 12, 2026.

2. Ibid.

3. William Ma, "DOJ probe on Powell draws swift backlash from Congress as key senator says he won't confirm anyone for the Fed until case is resolved", *Fortune*, January 11, 2026.

Implications for investors

- Today's news of legal maneuvering accompanies other concerns, including President Trump's proposal to limit bank interest rates on credit cards to 10% and the intensifying demonstrations in Iran.
- Now is a good time to recall that our 2026 Outlook theme, "Trendlines over headlines" remains firmly intact. Just as in 2025, the new year is continuing the rush of headlines that we believe do not change the trajectory of positive trends that are already in place and look durable through the balance of the year.

What to do now

The trends we see driving returns this year are measured (not aggressive) Fed rate cuts, deregulation, continued corporate technology spending, and significant corporate and individual tax refunds. The first two should combine to lower business costs, while the latter two raise revenue through increased borrowing. We expect these trends to raise U.S. corporate earnings broadly across equity markets. Globally we see a procyclical upswing underway. Strong, positive signals from shipping and transportation activity, copper outperforming gold, and the S&P 500 Index Consumer Discretionary sector outperforming the more defensive Consumer Staples sector so far this year.

We would still overweight U.S. large- and mid-cap equities relative to strategic allocations and take international equity allocations to neutral on pullbacks. We also reiterate our favorable ratings on S&P 500 Index sectors Industrials, Financials and Utilities. The Utilities sector seems particularly oversold and attractive for new cash. Realistically, we believe a procyclical bent should dominate, but we do not expect a straight line higher in equities. There is still room for investors to ask questions during earnings seasons, while headlines remain a risk for whiplash. We'll still look to take profits when valuations get extended and to rebalance into sectors that look attractive fundamentally and in valuation.

We also like our fixed income guidance to stay underweight in short- and long-term fixed income. Investors in short-term Certificate of Deposits (CDs) and money market funds should consider that this past June the U.S. Centers for Medicare & Medicaid Services projected average annual health care inflation at 2.5% between 2026 and 2033. Ultra-short rates may only just cover that inflation but may not stretch to cover inflation in other necessities. In the long maturities, some yield volatility is likely and the duration risk remains material, so we favor new money into investment-grade maturities of 3-7 years, where yields are close to 10-year yields, but with much less duration risk.

On commodities, we still favor precious and industrial metals. Gold could be a useful hedge, if long yields spike higher. An allocation of 2%-3% to precious metals could be appropriate for clients of any risk tolerance and investment objective.

Volatility due to policy and corporate earnings uncertainties may continue in coming weeks, which is why we expect our guidance to remain nimble and to treat market pullbacks as opportunities to rebalance funds toward emerging favorites. The goal of rebalancing is to reduce exposure where prices have become the most extended and to recycle the proceeds into potentially better values. In this way, rebalancing seeks to reduce near-term risk and to look for new potential opportunities as we expect the S&P 500 Index to continue trending toward our 2026 year-end target range of 7400-7600, but not in a straight line. The process of rebalancing may be easier to do when one focuses more on the fundamental trendlines than on headlines.

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