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Warsh as Fed Chair: Something for Everyone

Kevin Warsh's nomination signals a potential shift that could meaningfully influence markets and policy direction.

Insight from sub-adviser Wellington Management

Juhi Dhawan, PhD
Macro Strategist

Key Points

- Kevin Warsh's appointment may reinforce confidence that economic data—not political pressure—may guide rate decisions.
- His push for a renewed Treasury/Federal Reserve (Fed) accord could reshape the balance-sheet playbook.
- A shift toward deregulation and structural reform may redefine the Fed's architecture, potentially influencing financial conditions and equity valuations.

President Donald Trump has announced Kevin Warsh as the next Federal Reserve (Fed) chair, subject to Senate confirmation. As I've discussed before, "personnel is policy," and the Fed chair is an incredibly important voice not only in the direction of monetary policy but also in the way the central bank carries out its supervisory and regulatory responsibilities.

With that said, here are my five key takeaways on Warsh:

1. On interest rates — The choice of Warsh, who has advocated "hard money" policies over the course of his career, should allay concerns to some degree that managing inflation may take a back seat to political priorities. Markets may be more willing to believe that economic data will dictate how monetary policy is conducted, which could stabilize the dollar from a debasement-risk perspective.

2. On the balance sheet — Warsh has been consistently vocal about a new Treasury/Fed accord. This suggests room for more creative maneuvering to change the composition and size of the Fed balance sheet, so that the Treasury and Fed row together—for instance, in terms of Treasury issuance and Fed purchases, or policies around mortgage-backed securities as another example. Term premia[1] were up a touch, as of this writing, as markets tried to factor in this lean from the nominee. The specific actions Warsh might take and the time frame are up in the air, but I would emphasize that with his experience in the markets and at the Fed during the Global Financial Crisis, he may be more willing than most to experiment with Treasury Secretary Scott Bessent on how to think about deficits, bond yields, housing affordability, and other thorny issues.

3. On deregulation and supervision — I would view Warsh as supportive of the new Fed directive toward deregulation and expect him to be an active ally to Fed Board member Michelle Bowman in her efforts on that front. Since he left the Fed, Warsh has been one of the most consistent critics of what he sees as its "mission creep." This leaves room for banking supervision to perhaps move back to the FDIC, as one example—an idea Bessent has advocated. Something not discussed as much is whether we could see a tiering of interest the Fed pays on excess reserves that banks hold—money that's paid out to primarily large and sometimes foreign banks, rather than being remitted to the Treasury. This would align with the balance sheet point above and would be a big deal for markets in terms of tightening financial conditions and potentially weighing on US equity market multiples. The offset to these effects would be presumably lower short-term interest rates; but again, whether and when that will occur is not clear.

4. On Fed architecture — As a critic of the Fed, Warsh may also be likely to scrutinize the model-based approach of the Fed staff, the central bank's personnel, or its research agenda. There could be a material change in how the Fed approaches market data as opposed to economic data. I could also

[1] Term premia is the compensation investors require for bearing the risk of longer maturities, which are more sensitive to changes in interest rates.

imagine a nod of support to the idea of a comprehensive audit of the Fed proposed by many of its critics.

5. On markets/crises and politics — Warsh is a pragmatist and politically astute. He would also bring strong communication skills and valuable market experience to the role from his time at the Fed. Warsh will need these qualities given the complex issues surrounding the US deficit/debt and the need to walk a fine line between an activist president, a more strident Congress, and vigilant markets. He has shown he can pivot and shift views, which may be especially important if bond yields come under pressure given the large US fiscal deficit. Expect the unexpected from Warsh, including a willingness to do what is necessary even if it isn't "ideal."

Final thoughts

Warsh may take a step forward in reducing the power of the Fed from its current broad mandate. He may also be instrumental in changing the Fed's architecture and working more closely with the Treasury in managing the Fed balance sheet.

The level of control the Trump administration has over interest rates, as well as over broader regulatory and supervisory decisions, will depend on the ultimate makeup of the Fed Board, including whether Jerome Powell chooses to keep his seat. It will take some time before these decisions are made and before they matter to the markets, but over the medium term, I would expect them to prove consequential for the conduct of monetary and broader policies.

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For guidance on how shifts at the Fed may influence your finances, talk to your financial professional.