

# MARKET SIGHT LINES



## The Nomination of Kevin Warsh: His Leadership and Approach May Smooth Out How We Experience Risk

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The nomination and potential appointment of Kevin Warsh as Federal Reserve Chair may signal a fundamental shift in the central bank's operational approach, moving away from an era of seeking to dampen market fluctuations through high-frequency guidance toward a framework anchored in institutional discipline defined by both transparency and accountability. While markets have grown accustomed to a Fed that actively attempts to steer investor expectations, a Warsh-led committee could prioritize raw transparency and genuine price discovery. This transition suggests a return to a more limited, orthodox role for the central bank – one that emphasizes long-term inflation credibility and reduces the Fed's footprint within financial markets.

### THE TAKEAWAY: A SHIFT FROM POWELL TO WARSH MEANS CHANGE

Kevin Warsh may aim to move the Fed away from constant market signaling, instead emphasizing a predictable framework that prioritizes long-term stability over short-term market calm. In summary:

- Warsh's experience spans markets and crisis-era Fed decision-making, with a focus on inflation credibility, financial stability, and market functioning under stress.
- Despite a hawkish reputation, his history reflects more consensus-building than dissent, implying early change may focus on process and persuasion, not abrupt surprises.
- A clear window into Warsh's views is his 2014 review of the Bank of England, in which he signaled a preference for transparency, accountability, and private sessions of open debate.
- In a 2020 interview with the Yale Program on Financial Stability, Warsh reinforced his preference for real-time market signals over stale data, and cleaner boundaries in a crisis.
- Warsh has more recently expressed discomfort with the Fed's oversized balance sheet and high-frequency forward guidance, preferring the Fed to communicate more simply.
- Should Warsh apply these principles, investors may have to parse real-time market data to understand Fed policy implications, which may, in turn, result in increased market volatility day to day, including interest rates, bonds, currencies, and stocks.

## IN-DEPTH: KEVIN WARSH AS FED CHAIR WILL INFLUENCE HOW INVESTORS INTERPRET CURRENT/FUTURE MONETARY POLICY AND DAY-TO-DAY MARKET VOLATILITY

Kevin Warsh may steer the Fed away from constant “data-dependent” market signaling toward a stable policy anchor emphasizing individual accountability and a smaller institutional footprint. Going deeper:

- Warsh’s experience spans markets and crisis-era Fed influence, with a focus on inflation, financial stability, and market functioning:
  - Warsh served as a Fed Governor from February 2006 to March 2011, spanning the global financial crisis.
  - During his term he focused on real-time, market-functioning signals more than lagged traditional data.
- Despite a hawkish reputation, he has focused more on consensus-building than dissent, signaling early changes may focus on process and persuasion rather than abrupt change or surprises:
  - Warsh maintained a 100% consensus voting record during his Fed tenure, with no formal dissents.
  - We expect him to focus on communication/process changes over an immediate “rates regime” shift.
- Warsh’s 2014 review of the Bank of England provides a window into his preferences for transparency, accountability, and private sessions of open debate:
  - He favors immediate disclosure of individual votes after meetings to reflect the true balance of debate.
  - He also warned that over-recording/transcribing meetings can chill deliberation, reducing decision quality.
  - These principles may create a shift from “managed predictability” to “discipline through transparency.”
- Warsh’s 2020 interview with the Yale Program on Financial Stability reinforced key preferences:
  - He critiqued reliance on “stale” data sets from the Bureau of Labor Statistics and Bureau of Economic Analysis, especially in crisis conditions.
  - He prefers interpreting capital market flows and asset prices, not just broad macro data.
  - He highlighted the need to clarify lines of authority between the Fed and the U.S. Treasury in determining who is responsible for financing crisis actions, preferring a more limited Fed role.
- He is uncomfortable with a large balance sheet and frequent forward guidance, preferring simple communication:
  - He considers forward guidance “monetary junk food” that may mask market discovery, leading to muted near-term volatility but the prospect of a buildup to bouts of much higher volatility.
  - He is expected to focus on shrinking what he has called a “bloated balance sheet” and question the “abundant reserves” regime, likely a shift away from using the balance sheet as a policy tool.
- Should Warsh apply these principles, investors may focus on real-time market data to parse policy implications:
  - Notably, realized volatility has been approximately three times higher during Jerome Powell’s press conferences than those of his predecessors.
  - Volatility spikes around policy uncertainty are likely to be episodic rather than persistent, suggesting we may see increased market volatility day to day, including interest rates, bonds, currencies, and stocks, even as growth and earnings remain intact.
  - These moves may increase the term and risk premiums embedded in asset prices, particularly in rates and FX, with the potential to amplify volatility across asset classes even absent major policy shifts.

## CONCLUSION

For investors, the transition to Kevin Warsh as Fed Chair may signal higher day-to-day volatility but a reduction in catastrophic tail-risk. By moving away from the practice of providing the market with a constant roadmap of future policy moves, a Warsh Fed would prefer market participants to seek to price risk based on economic data rather than central bank promises. While this may trigger more focused price-discovery shocks as the market adjusts to the lack of a “safety net,” the ultimate goal is a more resilient financial system where the Fed acts as a disciplined guardian of the currency’s value rather than the primary driver of asset prices.

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