

Prospects

No. 26/029 – 3 February 2026

USA – What would Chair Kevin Warsh mean for the Fed?

- After months of speculation and at times conflicting headlines, President Donald Trump has finally made his choice for the next Fed Chair: Kevin Warsh, a former Fed governor who sat on the Board from 2006-11 and was also in the running the last time Trump selected a Fed Chair.
- Warsh is a more conventional pick than some of the other contenders and seems generally well respected, with most of the early reaction from other Republicans being positive. As such, we think he will eventually be confirmed, though the process could be a bumpy and drawn-out one given complications created by the DoJ investigation of current Chair Jerome Powell.
- Warsh is an interesting choice as he was considered a notable hawk during his previous stint on the Fed, though he has recently pivoted in a dovish direction, and we think he would bring this newfound dovish approach to the role.
- Warsh was also a sceptic of QE during his time on the Fed and has been a consistent advocate of a smaller balance sheet, so he could make a push in that direction. He has also been highly critical of “mission creep”, offering some scathing recent criticisms of the Fed, so he may push for some other types of reforms as well.
- That said, we are not convinced that Warsh will be able to drive a drastic shift in Fed policy, at least on his own, whether on rates or the balance sheet. We maintain the view that the Fed chair is not a dictator that sets policy unilaterally but instead would need to be able convince the rest of the FOMC. Thus, somewhat counterintuitively, we think there is a good argument that the more dovish and aggressive Warsh were to be, the more hawkish and resistant to change the rest of the Fed would be, as this approach would make it less likely that the rest of the Committee found his arguments convincing.
- Warsh’s approach may also have an impact on the decision that Chair Powell eventually makes about whether he will stay on as a Governor after his term as Chair ends. Again, we think a more aggressive, “bull in a China shop” type approach from Warsh would raise the odds that Powell decides to stay.

Who is Kevin Warsh?

Kevin Warsh is a finance industry veteran, having spent a stint at Morgan Stanley before moving to government roles. He worked in the Executive Branch under George W Bush’s administration, including some time at the National Economic Council, before being appointed to the Fed and spending five years on the Board of Governors from 2006-11.

Warsh has also acted as an occasional advisor to President Trump, for example as a member of a business forum Trump assembled in 2016, and was on the short list of contenders for the Fed Chair position when Trump eventually ended up selecting Powell during his first term. He has a similar educational background to Chair Powell in that he has a law degree as opposed to an advanced economics degree.

What are his confirmation prospects?

We think that Warsh will eventually be confirmed by the Senate, though the process could be a bumpy and drawn-out one, for reasons other than Warsh himself. When looking just at Warsh, he is a more conventional pick than some of the other contenders and seems generally well respected, with most of the early reaction from other Republicans being positive.

However, the administration's pressure on the Fed via the recent DoJ investigation into Powell's comments on the Fed's building renovation could complicate the process, as Republican Thom Tillis has announced he will not advance any Fed nominee until the DoJ probe is resolved. Even as Tillis has praised Warsh as "a qualified nominee with a deep understanding of monetary policy", he has not wavered from this view. Earlier this morning, Tillis also suggested that the Lisa Cook case may have to be resolved as well before he drops his stance opposing any new Fed nominees.

Tillis is an important figure on this front as he is a member of the Senate Banking Committee, where Republicans hold a slim 13-11 advantage. Thus, without Tillis's support, the Committee would be deadlocked, throwing a roadblock into the confirmation process. Tillis has also already announced that he will not be running for re-election in 2026, so he is unlikely to be susceptible to any political pressure such as the threat of a primary challenge by a MAGA candidate.

We would highlight that Warsh would be taking over the seat that is currently held by Stephen Miran, thus replacing one Trump pick with another. Miran's term technically ends tomorrow on 31 January, though because of the existence of what is known as a "hold over" provision, he is allowed to continue serving on the Fed until his successor is confirmed.

What would Warsh's stance be on rates?

Interestingly, Warsh was generally considered a notable hawk during his time at the Fed from 2006-11. Even during the depths of the financial crisis, Warsh remained concerned about inflation in his commentary at the time. For example, as late as April 2009 when core PCE had dipped below 1%, Warsh remarked, "I continue to be more worried about upside risks to inflation than downside risks".

More recently, however, he has clearly changed his tune, instead advocating for rate cuts. For example, Warsh recently criticised the Fed for not looking through the one-off change in prices that he believes tariffs will result in, saying that the Fed's hesitance to do so "is actually quite a mark against them".

He has also reiterated the argument advanced by Kevin Hassett and Stephen Miran, among others, that Trump's tax and deregulatory policies will help contribute to a productivity surge (along with AI). With a productivity surge resulting in disinflationary pressures and strong growth, that opens up more room for the Fed to cut, in Warsh's view.

Looking ahead, we think Warsh would bring this newfound dovish approach to the role. Despite his past concerns about inflation, he would likely continue to advocate the productivity story to push for lower rates, though we do not think he would go so far as to advocate aggressively slashing rates by multiple percentage points in a short period of time.

What about for other tools?

Outside of rates, Warsh has devoted a good amount of commentary to the balance sheet, which he believes has become bloated and could become much smaller. This was a key issue for Warsh during his previous time on the FOMC, and his decision to resign in 2011 stemmed at least in part from opposition to QE2. Thus, Warsh is likely to advocate some change to balance sheet policy, likely supporting a reduction in the size of the balance sheet in conjunction with lower rates.

Warsh has also offered some scathing criticism of the Fed's "mission creep". Essentially, Warsh believes that the Fed has strayed too far from its core mission and has taken on a more expansive role than it should have. This includes forays into climate change and inclusion, which Warsh believes should not be a part of the Fed's considerations.

This has escalated into some pretty harsh soundbites, such as the following quote: "I think what we need is regime change at the Fed. And that's not just about the chairman, it's about a whole range of people, it's about changing their mindset and their models, and frankly it's about breaking some heads, because the

way they've been doing business is not working". As such, **Warsh may also try to implement a number of reforms to the institution and how it operates.**

How effective would Warsh be as Chair?

We do think that Warsh is a qualified candidate and that will be seen as less political than some of the other possible choices. His previous time on the Fed will have also helped build up some credibility, even if his abrupt shift towards a stance more in line with that advocated by Trump may raise questions for some.

That said, we are not convinced that Warsh will be able to drive a drastic shift in Fed policy, at least on his own. As we have outlined numerous times in the past, the Fed Chair is not a dictator that sets monetary policy unilaterally but instead would need to be able to make a convincing argument in support of his preferences to get the rest of the Committee to go along.

Somewhat counterintuitively, in fact, we think that the more dovish and aggressive Warsh is, the more hawkish and resistant to change the rest of the Fed may end up being. For example, if Warsh were to come in guns blazing advocating immediately slashing rates by hundreds of basis points, then he would likely lose the rest of the Committee fairly quickly. If he were to come in saying he understood the opposition of others while laying out an economic case to take rates modestly lower, however, he would likely get more buy-in. Thus, how effective Warsh ends up being may depend on the approach he takes.

For now, however, we are not changing our call on the Fed and continue to hold a hawkish base case that sees the Fed keeping rates on hold for the entirety of 2026 before one final cut in 2027. If the data plays out as we expect with growth remaining strong, the labour market stabilising and inflation struggling to return all the way to 2%, we think Warsh would struggle to convince the rest of the Committee to execute a dovish pivot, though we will keep a close eye on Warsh's approach to the job and how receptive others seem to his arguments.

We also maintain our view for now that reserve management purchases will continue past April, albeit at a slower pace than the current USD40bn per month, despite Warsh's views on the balance sheet. Given the disruptions in funding markets that arose late last year, we think it may be a struggle to convince the rest of the Committee to perform an about face and vote to begin shrinking the balance sheet once again.

What will Powell do after May?

Warsh's approach to the role may also have an impact on the decision that Chair Powell eventually makes about whether he will stay on as a Governor after his term as Chair ends. Again, we think a more aggressive, "bull in a China shop" type approach from Warsh would raise the odds that Powell decides to stay. As a reminder, even though his term as Chair ends in May, Powell's term as a Governor lasts until 31 January 2028 and so he is able to stay on the Board until then, if he so chooses.

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