

The Warsh Nomination: Market Implications of the Potential New Chair

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The Race for the Eccles Building

In less than four months, Jerome Powell's run as the Chairman of the Federal Reserve will come to an end, marking the end of an era defined by post-pandemic inflation surge and a campaign for "higher for longer" interest rates. As May 2026 approaches, the spotlight has shifted from the Fed's "dot plot" to the White House's list for central bank candidates who will have to balance promoting market stability with pressures to push for aggressive easing of monetary policy. On Friday, January 30th, Mr. Trump announced that he would nominate **Kevin Warsh**, former Fed governor, to be Powell's successor. This decision will do more than fill a seat - it will signal whether the next four years will continue to be defined by institutional credibility or a fundamental "regime change" in how the world's most powerful central bank operates.

This is the perfect opportunity to take a glimpse into the President's top choice, understanding Warsh's qualifications, policy stances, and how his leadership would impact the trajectory of the Federal Reserve.

The Evolution of Kevin Warsh

Warsh's array of experiences spans back to more than two decades, and clearly, out of all Trump's picks for the Fed Chair, he has the most direct experience with the Federal Reserve.

Warsh began his career at Morgan Stanley, where he spent seven years in the M&A department, rising to the level of executive director, where he advised a wide range of companies on capital market transactions and strategic growth. Unlike the typical academic economist, Warsh was more "**market-savvy**", per Ben Bernanke, previous chairman of the Fed, understanding the underlying mechanisms of the financial system and how markets react to policy in real-time.

His transition to the public sector started in 2002, when Warsh joined the National Economic Council (NEC) as a Special Assistant to the President for Economic Policy. During this time, he primarily served as the liaison between the White House and independent financial regulatory agencies, advising capital markets, banking, and securities regulatory policy. At age 35, Warsh was later appointed as the **youngest Governor in the history of the Federal Reserve in 2006**, leading to his term being defined by the 2008 Great Financial Crisis. During the height of the meltdown, Warsh acted as the Fed's middleman to Wall Street, leveraging his Morgan Stanley contacts to help coordinate the rescue of failing financial institutions. He would later resign in 2011, several years before his term ended due to disagreements over the Fed's introduction of an unorthodox tool: **Quantitative Easing (QE) which is an aggressive bond-buying program**.

Ever since leaving the Fed, Warsh has become a prominent critic of the central bank from his position at the Hoover Institute (Stanford University). He has also conducted an independent review for the Bank of England (BoE) in 2014, recommending transparency reforms which were eventually adopted by the UK parliament. Additionally, Warsh pivoted back to his private sector roots, joining the Duquesne Family Office and serves on boards like UPS and Coupang. Recently, Warsh has advocated for "a regime change" at the Fed, arguing that the current Fed model is broken and that AI-driven productivity gains will allow for lower interest rates without triggering inflation. This is a stance that perfectly aligned him with the current administration's goals.

The Market Playbook: What to Expect Under Warsh

Despite it just being a day from the announcement of Kevin Warsh being nominated as the new Fed Chair, markets have already been pricing in their expectations for Warsh's new policy shifts within the central bank. Here is what they are expecting:

- 1. The Steepening of the Yield Curve:** Leaning towards dovish policy, we can expect short-term yields to drift lower as the federal funds rate potentially heads to a range of 3.0 - 3.50% by year-end. Warsh has also clearly expressed his distaste for QE, and has placed emphasis on reducing the Fed's balance sheet through Quantitative Tightening (QT). This puts upward pressure on longer-term yields as lower demand of long-dated bonds force investors to demand a higher "term premium." The problem with this is that longer-term debt such as the 30-year fixed mortgage rate will stay elevated, even as the Fed eases policy. The continuation of QT brings the risk of the Fed entering a "scarce reserves regime" where the Fed isn't flooding banks with cash. This could cause the repo market

to seize up, spike borrowing costs for financial institutions, and tighten credit conditions exactly when the administration wants them loose.

- 2. The AI-Productivity Hunch:** Warsh believes that AI is creating some sort of “supply-side miracle” that can justify cutting rates even if GDP growth remains hot as he argues that AI-driven efficiency prevents the growth from becoming inflationary. I would argue that this theory may be right in the short-term as initial AI adoption may displace workers, creating a temporary cooldown and disinflationary pressure that could justify Warsh’s call to cut interest rates further. However, once this “AI miracle” takes hold, it expands the economy’s production further, leading to a surge in capital expenditures and aggregate spending. If the Fed has already cut rates based on this initial displacement, they risk falling behind the curve as the economy overheats, potentially triggering a second wave of inflation.
- 3. A More Opaque Federal Reserve:** Warsh has been a vocal critic of the Fed’s dot plot and excessive forward guidance, so markets are bracing for higher volatility and increased dependence on available data to make decisions. This risks deanchored expectations as the market has priced in the future based on Fed transparency since 2008. If Warsh decides to taper the Fed’s balance sheet or shifts policy without transparency, he risks causing irrational market reactions. The market tends to price in the “worst-case scenario” for every move (consistent with theory in economics and psychology), leading to higher volatility and a “risk premium” on U.S. assets that could actually slow down the growth Warsh is trying to ignite.

Ultimately, Kevin Warsh still represents the **"best-case"** choice for an administration seeking to overhaul the Federal Reserve. Amidst months of speculation, he stands out as the most qualified candidate, who’s been through the fire of a global financial crisis, which gives the markets a much-needed sense of stability.

However, his proposed "regime change" is a high-stakes experiment. By trading institutional transparency for opaque flexibility and betting the house on an AI-driven productivity miracle, Warsh is attempting to thread a needle that requires perfect timing. If his theory on supply-side growth fails to outrun the inflationary heat of a debt-heavy economy, or if his balance sheet reduction spikes mortgage rates, the result won’t just be a policy error, it will be a fundamental

de-anchoring of the U.S. bond market. For investors, the Warsh chairmanship promises the rate cuts they want, but at the cost of significantly higher volatility.

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