

The Warsh Fed

Between market expectations and institutional constraints

- Markets initially expected Kevin Warsh to tilt the Federal Reserve in a more dovish direction, but his first Federal Open Market Committee meeting showed that the committee remains more concerned about persistent inflation than eager to validate expectations of rapid rate cuts.
- Despite the focus on whether a Warsh chairmanship will lower interest rates, the most likely outcome is a more constrained version of the “Warsh Doctrine” than markets initially anticipated.

The Warsh doctrine combines a greater willingness to lower interest rates with a smaller Fed balance sheet, and a shift to what Warsh views as a clearer and more disciplined monetary framework

Introduction

Since Kevin Warsh’s appointment as the 17th chair of the Federal Reserve, investors have tried to define a “Warsh Doctrine.” In its simplest form, the doctrine combines a greater willingness to lower interest rates with a desire to shrink the Fed’s balance sheet, reduce its footprint in financial markets, and restore what Warsh views as a clearer and more disciplined monetary framework.¹

The appeal of this narrative lies in its ability to offer something for almost everyone. The White House sees the prospect of lower rates. Markets see the possibility of easier financial conditions. Fiscal conservatives welcome a smaller central bank. Critics of post-crisis monetary activism see an opportunity to redefine the Fed’s role.

However, his first Federal Open Market Committee (FOMC) meeting as chair on June 17 complicated this narrative. Warsh began his tenure with a unanimous rate hold, a more inflation-conscious forecast, and a review of Fed practices.²

FOMC firewall

While Warsh will undoubtedly influence the debate, he inherits an FOMC that remains more hawkish than markets initially expected

The FOMC determines U.S. monetary policy, not the chair alone. Warsh can shape the agenda, but he inherits a committee more hawkish than markets initially expected. In April, three members dissented in favor of removing language from the FOMC statement suggesting the next move was likely to be a cut rather than a hike, underscoring the difficulty of building consensus around easing.³

This constraint was evident on June 17. The FOMC voted unanimously to hold the federal funds target range at 3.5%-3.75%, reaffirmed its ample-reserves framework, and described economic activity as expanding at a solid pace. The updated projections were also less dovish than the market narrative had implied.⁴

The median participant expected personal consumption expenditures (PCE) inflation to end 2026 at 3.6% and core PCE inflation at 3.3%, unemployment at 4.3%, and the federal funds rate at 3.8%.⁵ Advocates of lower rates must explain why policy should ease despite stronger productivity growth, solid labor market conditions, and inflation still well above target.

Warsh's initial moves were more procedural than dovish. He announced the creation of five task forces —communications, balance-sheet policy, data sources, productivity and jobs, and inflation frameworks—to review the Fed's operating model.⁶ This allows him to reshape the institution's framework over time without forcing the FOMC into a lower-rate stance that many members may resist.

This institutional reality matters because it will be hard to implement the doctrine.

Artificial intelligence (AI) illustrates this change. Warsh has suggested that AI-driven productivity gains could expand supply and justify lower interest rates. The June FOMC statement acknowledged strong productivity growth and capital investment, but the committee did not treat them as grounds for easing policy. Many Fed officials worry that AI's short-term effects may be inflationary rather than disinflationary, given the enormous investment required in data centers, energy infrastructure, semiconductors, and related services.⁷

A similar debate surrounds inflation measurement. Warsh has floated giving greater weight to trimmed-mean inflation measures, which can sometimes look more benign than traditional core inflation indicators.⁸ But changing the inflation framework is easier to discuss than to implement. Fed officials have spent decades refining inflation metrics, and many committee members are unlikely to embrace a methodology if it appears designed to produce a more dovish outcome. If the review appears designed to justify lower rates while inflation projections remain above target, critics may argue that the Fed is changing its dashboard to reach a predetermined outcome.

Institutional reforms

The broader significance of a Warsh chairmanship may lie in his ability to implement institutional reforms.

The task forces are the clearest early sign that Warsh's chairmanship may matter most through institutional reform rather than immediate rate cuts. They map closely onto his critique of the post-2008 Fed: that it became too reliant on forward guidance, too active in financial markets, too expansive in its interpretation of economic data, and too willing to blur the line between monetary policy and broader economic management.

Warsh may find more support from the FOMC for his proposed balance sheet reductions.⁹ Since 2008, quantitative easing, emergency lending facilities, and extensive forward guidance have made the Fed a larger and more active market

Warsh has repeatedly argued that monetary policy should rely more heavily on interest rates and less on balance sheet interventions

participant.¹⁰ Warsh wants monetary policy to rely more on interest rates and less on balance sheet interventions. Many Fed officials may be receptive in principle. From June 2022 to December 2025, the FOMC reduced securities holdings by over \$2.2 trillion.¹¹

The policy debate is less ideological than operational: how far can the Fed shrink its holdings without undermining the ample-reserves framework that supports short-term rate control and money market stability? Past reserve shortages have disrupted money markets, and easier liquidity regulations, combined with a smaller Fed balance sheet, could compound the risks if reserves become scarcer than expected.¹²

Warsh also appears to believe that the Federal Reserve has expanded beyond its original mandate.¹³ His concern is not simply inflation or growth, but the growing tendency of markets to rely on central bank intervention. This philosophy could affect everything from crisis management to market communications.

Investors are also watching the lender-of-last-resort function. A more restrained Fed could set a higher threshold for emergency liquidity facilities, support for non-bank financial institutions, or dollar swap lines with foreign central banks. This is where Warsh's institutional agenda matters most for Europe: not because it guarantees a weaker global safety net, but because it introduces less predictability in how the Fed would respond in the next crisis.

Conclusion

The political context during Warsh's tenure further complicates matters.

Warsh takes office at a moment when President Trump is advocating lower interest rates and when concerns about Fed independence have become increasingly prominent. Yet it would be a mistake to assume that political alignment necessarily translates into policy compliance.

Some observers in Washington argue that much of Warsh's positioning reflects political pragmatism rather than ideological subservience. Regardless of whether this is true, the more relevant question is whether he can preserve institutional credibility while navigating intense political pressure.

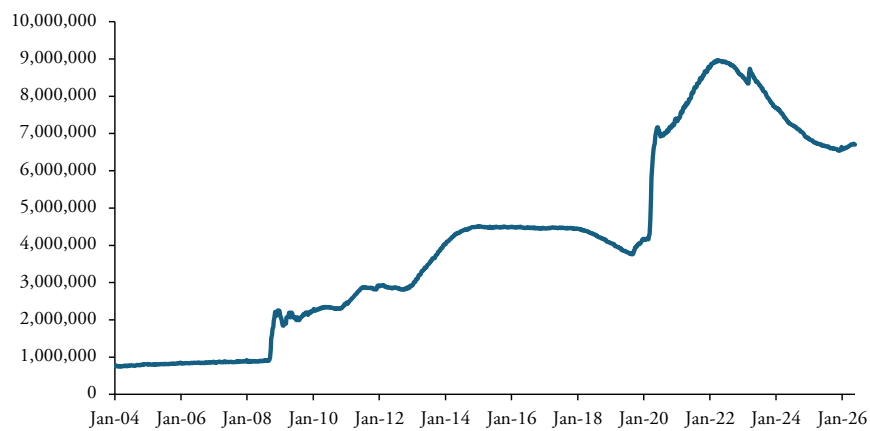
For decades, the Federal Reserve's greatest asset has been its credibility. The challenge for Warsh will be balancing institutional reform while preserving the confidence that allows the Federal Reserve to influence markets in the first place.

The "Warsh Doctrine" is likely to emerge in a more limited form than markets first expected

The most likely outcome is a more constrained "Warsh Doctrine" than markets initially anticipated. A dovish Warsh Fed would weaken the dollar, ease global financing conditions, and give the ECB greater room to lower rates. But the June meeting points to a more complicated outcome: a Fed that may become less interventionist before it becomes meaningfully easier on rates. If the Fed becomes more reluctant to deploy extraordinary liquidity

facilities during periods of market stress, European banks, governments, and firms could face greater funding volatility and a less predictable dollar backstop. For Europe, the Warsh era may mean that changes in the Fed's operational philosophy ultimately matter as much as changes in interest rates.

EXHIBIT 1.0 – TOTAL ASSETS OF THE FEDERAL RESERVE SYSTEM, JANUARY 2004 – MAY 2026
(USD MILLIONS)



Source: Federal Reserve Bank of St. Louis.

Notes

- ¹ <https://www.cfr.org/articles/what-to-expect-from-kevin-warshs-fed-in-the-first-100-days>
- ² <https://www.federalreserve.gov/newsevents/pressreleases/monetary20260617a.htm>
- ³ <https://www.economist.com/finance-and-economics/2026/05/27/kevin-warshs-troublesome-inflation-in-tray>
- ⁴ <https://www.federalreserve.gov/newsevents/pressreleases/monetary20260617a.htm>
- ⁵ <https://www.federalreserve.gov/monetarypolicy/files/fomcprojtabl20260617.pdf>
- ⁶ <https://www.federalreserve.gov/mediacenter/files/FOMCpresconf20260617.pdf>
- ⁷ <https://www.federalreserve.gov/monetarypolicy/fomccalendars.htm>
- ⁸ <https://www.dallasfed.org/research/pce>
- ⁹ <https://www.reuters.com/business/finance/former-fed-officials-say-size-may-not-matter-balance-sheet-2026-05-18/>
- ¹⁰ <https://www.federalreserve.gov/releases/h41/>
- ¹¹ <https://www.federalreserve.gov/monetarypolicy/policy-normalization.htm>
- ¹² <https://www.reuters.com/business/finance/warsh-faces-hearing-framework-smaller-fed-balance-sheet-emerges-2026-04-21/>
- ¹³ <https://www.cfr.org/articles/what-to-expect-from-kevin-warshs-fed-in-the-first-100-days>