

## New Leadership, New Direction

The results of Kevin Warsh’s first official set of meetings on monetary policy as the Chairman of the Federal Reserve were like a breath of fresh air.

It wasn’t so much what he said, as what the Fed did not say, in particular in the official statement at the conclusion of the meetings, which was extremely short and to the point compared to the statements issued in recent decades under the leadership of Ben Bernanke, Janet Yellen, and Jerome Powell. Warsh’s philosophy on Fed communication seems to more closely resemble that of former long-time Chairman Alan Greenspan, who unfortunately passed away earlier today. Not Greenspan’s elegant and winding prose, but Greenspan’s unwillingness to hint strongly about what the Fed would do next.

Warsh doesn’t like the intense form of “forward guidance” that’s evolved at the Fed, where it treats the markets and the economy like some sort of young child that is always on the verge of a tantrum and needs to be placated, as if every shift must be communicated well ahead of time, and the Fed needs to ask for permission (“Please clean-up your room later today, is that OK?”) Instead, Warsh wants the Fed to make it clear it will pursue its definition of price stability, which we believe is the 2% inflation goal, and that’s that.

Warsh says he wants the financial markets to think about what’s going on in the economy, not how the Fed will react to what’s going on in the economy, which ought to be a secondary issue if the Fed is focused on price stability. Signaling his commitment to a new strategy, Warsh was the one “missing dot” from the dot plot that came out of the last week’s meeting, withholding his projection of the path of short-term interest rates in the years ahead, while all other Fed decisionmakers continued to participate.

We are also pleased that Warsh is having the Fed take a much closer look at the size of its balance sheet and the shift from the “scarce reserve” system the central bank used for

many decades to a system of “ample reserves.” Don’t expect an imminent shift back to a scarce reserves system, but at least the Fed has now taken a first step in that direction.

Although Warsh was on the Fed as a regular member back during the Global Financial Crisis and supported the original version of Quantitative Easing at the time, he opposed later rounds of QE and has had some second thoughts about the policy tool. Hopefully he will recognize that it was not QE that saved the economy in 2008-09 or during COVID.

One way to tell how serious Warsh will be about changes and reforms at the Fed is to watch things other than monetary policy. The Fed has become too large an institution. It’s not just about its enormous balance sheet, it’s also about personnel. The Federal Reserve system employs about 25,000 workers. Yes, that includes bank regulators, check clearers, night watchmen, currency distribution systems, and researchers. But are all those researchers really focused on issues related to banking or monetary policy?

The Chicago Fed, in particular, seems gung-ho for a role in community development, including on issues of housing affordability. But every dollar that’s spent on this project, and others similar, is a dollar that instead would have gone to the US Treasury, reducing the need for future tax revenue. Ultimately, these are taxpayer funds being used to do what Fed officials want, without an appropriation by Congress.

One big problem is that former Chairman Jerome Powell is still a regular member of the Fed’s Board of Governors and we think he is unlikely to leave until at least late this year. While many say he’s sticking around due to potential legal issues involving cost overruns at the Fed, it might also be to see the outcome of the mid-term elections this Fall, because those elections may determine who Trump can appoint as a successor. If so, this is a purely political decision, which is exactly what Powell in the past has said he’s against.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
6-24 / 7:30 am	Q1 Current Account Balance	-\$208.8 Bil	<b>-\$177.5 Bil</b>		-\$190.7 Bil
9:00 am	New Home Sales – May	0.640 Mil	<b>NA</b>		0.622 Mil
6-25 / 7:30 am	Initial Claims – Jun 20	225K	<b>225K</b>		226K
7:30 am	Personal Income – May	+0.4%	<b>+0.4%</b>		0.0%
7:30 am	Personal Spending – May	+0.6%	<b>+0.5%</b>		+0.5%
7:30 am	Durable Goods – May	-4.9%	<b>-4.0%</b>		+8.0%
7:30 am	Durable Goods (Ex-Trans) – May	+0.5%	<b>+0.3%</b>		+1.1%
7:30 am	Q1 GDP Final Report	+1.6%	<b>+1.6%</b>		+1.6%
7:30 am	Q1 GDP Chain Price Index	+3.5%	<b>+3.5%</b>		+3.5%