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Introducing the New Federal Reserve Chair – Jerome Powell

Jerome (Jay) Powell has been nominated to replace Janet Yellen as Chair of the Federal Reserve. Powell, currently serving on the Board of Governors, will be charged with the ongoing "normalization" of interest rates and the reduction of the size of the Fed's balance sheet - making the determination on the optimal level of interest rates and balance sheet reduction to meet the Fed's dual mandate of job growth and low inflation.

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Last Thursday President Trump nominated Federal Reserve Governor Jerome (Jay) Powell to be the next Chair of the Federal Reserve replacing Janet Yellen when her term ends in February (she can remain on the Board of Governor's until 2022 when her term ends but she is expected to resign from the Board when her term as Chair ends). Below are our observations about Mr. Powell's nomination.

- Mr. Powell has been on the Board of Governors for five years. Although he is a Republican, he was appointed as part of a "package deal" along with Democrat Jeremy Stein by President Obama so that the Republican Senate would approve both in order to fill two open seats.

- Breaking a trend of having PhD Economist to head the Fed (the last three have been going back to the late 1980's) he is a lawyer by training. He worked for several years in Private Equity at the Carlyle Group and served in the George H. W. Bush administration as the Under Secretary of the Treasury for Domestic Finance. He also worked as an investment banker at Dillon Read.

- Market participants believe he will carry on most of the policies of Janet Yellen with some minor tweaks. He did not register any votes against the majority (though that does not mean that he did not oppose policy as FOMC voters opposed to the policy statement have voted with the majority in order to show unity with the Chair) but it is thought that he was a skeptical of the extent that continued quantitative easing in 2012 was aiding economic growth (QEIII). Additionally, while agreeing with the need for bank regulation in the Dodd-Frank bill, he has expressed concern about the efficiency of the execution of the act.

- According to the Bloomberg Intelligence Fed Spectrometer (rated on a scale of -2 -to- +2 with negative numbers an indication that the voter is a dove and positive numbers an indication that the voter is a hawk), Powell is rated at "0" neutral (neither a hawk or dove) in his views on monetary policy.

- While the outgoing Chair Yellen is considered "dovish" rated at "-1" (favoring the economic growth mandate over the inflation containment mandate by the Fed through lower interest rate targets and asset purchases), there are no indications that Mr. Powell will change the interest rate increase and balance sheet reduction plans of the Fed once he is the new Chair.

- We continue to expect that the Fed will raise interest rates at its next meeting in December by 25 basis points (bps) to the 1.25%-1.50% level, continue the hikes in 2018 with at least two 25 bps increases, and will continue the process of reducing the $4.5 trillion asset holdings on the Fed's balance sheet (most likely down to $2.5 trillion). Mr. Powell has said that the reduction of the balance sheet should be as exciting as watching paint dry.

- While we believe that he was an excellent selection by the President, what could make us wrong?

    - Mr. Powell has been "guarded" in his comments whenever speaking publically keeping his thoughts "close to the vest", especially relative to other FOMC members. While we think we know his views on FOMC interest rate policy and economic stimulus, we do not know his views with any degree of certainty.

    - He is not a trained economist (we realize there are those who believe this is an asset and not a liability – for more on that topic read the book "Fed Up" by former Fed official Danielle DiMartino Booth). While we realize that he has several years' experience as a Board of Governor member under both Chair's Yellen and Ben Bernanke, there is the looming question on what actions would he take during a financial and/or economic crisis similar to what Bernanke faced late last decade (having been a student of the Great Depression, he along with Secretary of the Treasury Henry Paulson took emergency corrective action to save the financial system). Hopefully, he will not be faced with a similar situation.

    - There are some that are worried (doves) that President Trump could still name Dr. John Taylor at Stanford as the next Vice Chair of the Fed which they view as Yellen for Taylor trade that could turn the FOMC much more hawkish. So far, there has been no indication that he will be nominated and possibly would not accept a nomination since he was seen as one of the three finalist for the position (Yellen was the other).

Additional Changes at the Board of Governors and at the regional Federal Reserve Banks

- There are three Board of Governor spots open at the Fed's Board (three if Dr. Yellen resigns from the Board).

    - The Vice Chair position is vacant since the retirement of Stanley Fischer in October. As mentioned above, John Taylor's is a possibility for the spot.

    - When Randal Quarles was nominated to the Vice Chair for Supervision, Carnegie Mellon University Economics Professor Marvin Goodfriend (formerly a long-time senior vice president and policy advisor to the Richmond Federal Reserve bank) was mentioned as a possible nominee to the Board, but so far nothing has been announced.

    - The spot held for a community bank member has gone unfilled for a few years as President Obama's nominee was never brought before the Senate for a vote and President Trump has yet to send a nominee to the Senate.

- At the regional Federal Reserve Banks there are two current searches for new Presidents being conducted.

    - The Richmond Fed's board is searching for a replacement for Jeff Lacker who resigned in April after admitting that he was the source of a leak of secret market-sensitive information to a consulting firm. Mark Mullinix is serving as the bank's acting President.

- New York Fed President William Dudley just announced that he will retire mid-year 2018 (he wants to give the NY Fed enough time to have a successor in place well before the mandatory end of his term in January 2019). The NY Fed's board has begun the process of finding a successor to Mr. Dudley.
    - This position is important in that the NY Fed President is a permanent FOMC voter while the other regional Fed Presidents rotate for voting purposes.

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