The Fed’s going to power on with Powell

A continuation theme should be the dominant outcome from the Biden decision to stick with Chair Jerome Powell. But there will be a more influential Brainard influence to be taken into account. And while we can't ignore this, the overall policy thrust leaves us as we were. The Fed will still taper, and likely hike in 2022

Jerome Powell will lead the US Federal Reserve for a second term

More of the same, but with a heightened Brainard influence in any case

President Biden has ignored calls from progressives in his party to replace Jerome Powell as Fed Chair and has instead nominated him for a second term. This was the generally expected outcome given the successful role Powell played in steering the economy through the pandemic and the consequent broad bipartisan for his re-nomination.

This must have been an important consideration given the President’s frustration in getting legislation passed due to wafer-thin majorities in the House and Senate. Biden would not have wanted another battle of attrition that diverts him from achieving his policy agenda since this Fed role requires Congressional approval.

This will upset the progressive wing of the Democrat party

This will upset the progressive wing of the Democrat party, particularly Senator Elizabeth Warren, who addressing Powell directly in September called him “a dangerous man to head up the Fed”. The criticism centres on Powell’s willingness to back Vice Chair Randal Quarles' decision to reverse some of the restrictive rules and regulations imposed on the banking sector in the wake of the global financial crisis. He had also faced criticisms from some quarters due to a perception of not doing enough to address climate risk within the Fed’s framework.

The decision to reappoint Powell was made easier by Quarles stepping down from the Fed Board of Governors ahead of schedule after his position of Fed Vice Chair for banking supervision ended in October. It allows Lael Brainard, who the progressives had favoured for Fed chair, to step into that vice-chair role and roll back some of the changes introduced by Quarles without the awkwardness of him sitting across the table.

Moreover, with two vacancies on the Fed Board of Governors now that Quarles is departing, Biden has the opportunity to shape the Fed further to ensure that monetary policy is truly focused on achieving the “broad-based and inclusive” goals as set out in the updated Fed’s 2020 policy framework.

Any material market impact is subjacent to this particular announcement

This decision also removes uncertainty with Powell’s current term ending in February. Had there been any delay in appointing a new Chair due to a lack of political support this could have caused significant financial market nervousness, particularly if we are right and the economy is soaring, inflation is above 6% and the Fed is still stimulating the economy with QE.

There is a theme of continuity for markets that should result in minimal material impact

In consequence there is a theme of continuity for markets that should result in minimal material impact. It does not change the likely trajectory of policy. The Fed will still taper, and will likely hike in 2022 (we think at least twice in 2H), and the rates market will remains in a state of anticipation for tighter policy and a higher rates environment generally.

Risk assets also not be overly impacted by this outcome. Some degree of risk-on would be an understandable outcome on more of the same ahead. Any risk-off seen would be more an excuse to go in that direction, rather than a material outcome that can be linked to the continuation of Powell at the helm of the Federal Reserve.

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