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Nabiullina Will Be Superior Central Bank Head

By Martin Gilman

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Last week's announcement by President Vladimir Putin that he was appointing Elvira Nabiullina as the new head of the Central Bank surprised many observers. In fact, the appointment, subject to confirmation by the State Duma, makes sense and is consistent with precedent in post-Soviet Russia. It may come to be seen as more than just a sound choice for the post.

Russian and foreign observers have given mixed reviews over the past week to Putin's choice, but Nabiullina's superb technocratic skills, sharp intellect and serious approach to public policy issues make her an excellent candidate to lead the Central Bank.

Let's start with the precedents. Over the past 20 years, two heads of the Central Bank were insiders: Viktor Gerashchenko and Tatyana Paramonova. Neither one had a sterling reputation in running the bank, although they both deserve more credit than is commonly assumed, given the difficult circumstances in which they operated. The other two Central

Bank heads, Sergei Dubinin and Sergei Ignatyev, came from the Finance Ministry. Dubinin, appointed in 1995, was sacrificed as a consequence of the 1998 default, but was largely responsible for transforming the bank into the most professionally managed public institution in the country.

Ignatyev, who took over from Gerashchenko in 2002, continued this process. Before his surprising transformation into a central banker, he had been an academic and a first deputy finance minister. His areas of expertise included neither monetary economics nor banking. The same could be said for Alexei Ulyukayev, the current first deputy chairman of the Central Bank, who was, above all, a fiscal expert, first at the Gaidar Institute and then at the Finance Ministry. Both were credited with doing a reasonable job of managing Russian monetary policy through a challenging period and are considered to be respected central bankers. What's more, both will remain at the Central Bank if Nabiullina is confirmed.

Above all, Nabiullina is a highly qualified technocrat. She is valued for her broad experience, competence under fire and hard work. Less than a year ago, she was still the economic development minister. Her period in the Kremlin was all too brief to be much of a respite. It seems that Putin chose her because he wanted all of those qualities plus a keen sense of pragmatism.

Since Nabiullina is smart and will appreciate what is at stake, she will adapt well to her new job. There is no reason to believe that the political process would try to interfere directly in monetary issues. After all, Putin respects competent, career technocrats like Ignatyev and former Finance Minister Alexei Kudrin. Nabiullina will also benefit from her highly professional staff who will advise her on the intricacies of credit channels and banking regulation. Since monetary policy is only a part of a country's macroeconomic framework, she will be in a good position to coordinate a consistent set of policies with her colleagues in the government.

One of the sounder arguments for choosing a pragmatic technocrat is that presumably she will not come with an a priori theory of monetary economics or banking. The same could not be said for some of the other candidates considered for the job whether from banking or politics. Russia certainly does not need someone running its Central Bank as an economic experiment.

There is another reason why Nabiullina is a good choice. Like Ignatyev and Ulyukayev, Nabiullina was in a top policy position at the time of the August 1998 default, serving as the deputy minister of economy and effectively heading the government's commission on economic reform. She resigned when Yevgeny Primakov became prime minister in September 1998. As a policy veteran of that tumultuous era, she knows first-hand what price is incurred for financial instability. Whatever the prevailing view about economic growth, Nabiullina understands that confidence in a country's money is critical to the maintenance of economic health. She also appreciates from her time as the head of the Center for Strategic Reform in the early 2000s that future growth depends upon productive investment by a dynamic private sector.

Perhaps greater than any local political pressure to loosen the monetary reins, the real problem may come from an unlikely quarter: the Group of Seven central bankers have thrown away the rulebook and are printing money in a desperate attempt to revive their economies. So what happens when she meets her foreign counterparts at the monthly meetings in Basel or at the International Monetary Fund?

Actually, central banks in countries like Russia should have modest ambitions. Sure, in the extreme, a central bank could implement a policy that destroys its currency and economic credibility. Even now, one can see examples of this from Argentina to Venezuela to Zimbabwe.

Otherwise, having a sound technocrat in charge and a professional staff seem to be the right approach. It is essential to appreciate just how little maneuvering room any head of the Russian central bank actually has in practice. This also applies to other central banks of major emerging market countries with supposedly more flexible exchange rates and stronger inflation-targeting credentials such Poland, Turkey, Hungary, Mexico, Brazil, India and South Africa.

These countries all seem to understand that since they don't have the privilege of printing a reserve currency; they have to keep monetary policy relatively tight. Yet they want to avoid a sharp real appreciation of their exchange rates. In fact, the Central Bank followed the same nominal flexibility as these other so-called floaters before the crisis from 2005 — and exactly the same flexibility afterward. Like Russia, they also were running a "quasi-peg" for the past 10 years with similar results. They tried to prevent a rapid appreciation of their currencies, despite the supposedly large differences in inflation-fighting credibility among the central bank governors involved.

So why did Russia have a much greater inflation problem? Because the Central Bank printed a lot more money than the others. But Ignatyev really had little choice. All of the seven other countries had current account deficits, so they were just sterilizing capital inflows. Russia had a much bigger problem: It was running a current account surplus equivalent to 10 percent of gross domestic product so the monetization created by that positive foreign balance was much greater. Since 2010, what has really facilitated Ignatyev's life and helped to bring inflation down has been a decline in the current account surplus combined with capital outflows. Any other reasonable Central Bank head would have done the same.

To see how Nabiullina will perform, it would be useful to know the future path of oil prices and Russia's balance of payments rather than her predilection for monetary or real sector economics.

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