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National representation in supranational institutions: The case of the European Central Bank

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ABSTRACT

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Supranational institutions face an important trade-off when hiring personnel. On the one hand, hiring decisions are based, as in most organizations, on a candidate's professional qualifications. On the other hand, supranational institutions often aim for broad national representation. Reviewing evidence from the European Central Bank, we show that nationality is indeed relevant for both hiring and decision-making. Specifically, we find a disproportionately narrow spread of national representation in the top management of the ECB. Further, there is evidence for the existence of national networks between adjacent management layers. Finally, monetary policy decisions seem to be linked to national representation in the core business areas of the ECB. Examining a sample of 27 European countries over the period from 1999 to 2008, we estimate Taylor rules for alternative sets of euro area aggregates derived from different weighting schemes of national macroeconomic data. Our results indicate that weights based on national representation in the mid-level management of the ECB's core business areas best describe the central bank's interest-rate setting behavior. *Journal of Comparative Economics* **42** (1) (2014) 19–33. WU Vienna, Department of Economics, Althanstrasse 39-45, 1090 Vienna, Austria; Darmstadt University of Technology, Department of Law and Economics, Marktplatz 15, 64283 Darmstadt, Germany; Austrian Institute of Economic Research (WIFO), Arsenal, Objekt 20, 1030 Vienna, Austria; ETH Zurich, KOF Swiss Economic Institute, Weinbergstrasse 35, 8092 Zurich, Switzerland; CESifo, Poschingerstrasse 5, 81679 Munich, Germany.

1. Introduction

In central banking, the geographical background of decision-makers and staff is often an issue of considerable relevance. Some central banks require that its staff members have the nationality of the home country. The central bank of the Philip-

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pines, for instance, requires that applicants for employment must be Filipino citizens.[1] Other central banks have established monetary policy decision-making bodies in which, by law, (some) seats are explicitly allocated by region. In Pakistan, for instance, the central bank's central board of directors comprises one director from each of the provinces.[2]

Having no firm basis in theory, the focus on geographical representation has, in practice, both benefits and costs. Governments and central banks that implement such rules generally aim to improve decision-making and credibility, two important conditions for the success of monetary policy. Specifically, it is argued that regional representatives bring with them specific knowledge of local conditions, thereby allowing to collect and process a broader range of information. Also, regional representatives are able to communicate decisions to a wider public.[3] At the same time, however, when the geographical background of an individual is taken explicitly into consideration, other potential criteria, most notably a candidate's professional qualifications, automatically become relatively less important for appointment and promotion.

In this paper, we examine empirically issues related to the geographical representation of personnel in central banks. Analyzing the composition of the management team at the European Central Bank (ECB), we ask whether regional features matter for employment. We also search for evidence of networks among staff members along regional lines. Finally, we examine whether the regional composition of central bank staff has a measurable impact on policy-making.

The focus on the ECB has, for our purposes, a number of useful features. First, the ECB is a multinational institution, such that nationality is a reasonable approach to differentiate geographical background.[4] Also, nationality is a personal characteristic that is easily observed, both internally and externally. Second, the ECB is a young institution. Having been officially established in 1998, it had to build up its staff quickly from virtually zero so that there are hardly persistence effects in recruiting. Third, the ECB is an institution of great policy relevance. The ECB is not only the largest European Union financial body, it also has financial and organizational autonomy.[5] Given the ECB's genuine powers, governments of euro area member states should have a strong incentive for national representation in this institution.[6] Fourth, in contrast to other policy areas in the European Union, monetary policy directly affects economic conditions in all euro area member countries, thereby providing another strong incentive for national representation.

In our analysis, we focus particularly on national representation at the management level of the ECB, a choice that is motivated by a large organizational literature. For instance, Pfeffer (1985, p. 68) argues that "[o]rganizations are full of people. It often seems only natural and appropriate to analyze and manage organizations using individuals as the units of analysis." Thereby, we go substantially beyond previous work with a focus on national representation in the ECB's decision-making body, the Governing Council.[7] Instead of examining de jure representation of countries as defined in political documents, we analyze de facto presence of nationals in the institution. Specifically, we estimate panel data models for staff shares of the 27 member states of the European Union (EU) in the top management of the ECB over the period from 1999 through 2010.

Previewing our results, we find that a nation's share of ECB managers is reasonably explained by country-level determinants of job applications (such as a country's distance from the ECB headquarter) rather than broad geographical representation. This finding seems to indicate that hiring decisions are generally made on the basis of a candidate's professional qualifications. Still, national background also seems to matter for recruitment. There is evidence that strong national representation at a particular management level is typically associated with similarly strong national presence at the subordinate management layer. Finally, based on Taylor rule estimates to describe the ECB's interest-rate setting behavior, we find that monetary policy decisions are most closely linked to national representation in the core business areas of the ECB.

The remainder of the paper is organized as follows. Section 2 reviews the relevant literature. Section 3 provides some institutional background on the European Central Bank, followed by a description of the data in Section 4. The heart of the paper is Section 5 which presents our empirical model and the estimation results. Section 6 briefly summarizes our findings.

[1] See http://www.bsp.gov.ph/about/recruitment.asp. Citizenship is a requirement that is occasionally even included in the central bank law, typically for influential positions such as board members or shareholders. For instance, for members of the Monetary Committee, Article 16 of the Bank of Israel law stipulates that "[a] member from amongst the public shall be qualified for appointment if he is a resident of Israel" (see http://www.bankisrael.gov.il/deptdata/pikuah/bank_hakika/eng/new_law_2010_eng.pdf). The South African Reserve Bank Act requires, in Article 4, that "[n]o person shall be appointed or elected as or remain a director if he or she is not resident in the Republic" (see http://www.reservebank.co.za/internet/Publication.nsf/LADV/7DC59462E47AFDD-F42256ED60038AE5C/$File/S+A+Reserve+Bank+Act.pdf). The State Bank of Pakistan Act notes that "no person shall be registered as a shareholder [...] who is not a citizen of Pakistan" (see http://www.sbp.org.pk/about/act/SBP-Act.pdf).

[2] See http://www.sbp.org.pk/about/act/SBP-Act.pdf. In similar fashion, the central board of directors of the Reserve Bank of India comprises one director from each of the four local boards (see http://rbidocs.rbi.org.in/rdocs/Publications/PDFs/RBIA1934170510.pdf). Central banks that aim for broad regional representation in their supervisory bodies include Danmarks Nationalbank and the Swiss National Bank.

[3] See, for instance, Goodfriend (1999) for a more detailed discussion. Gerlach-Kristen (2006) examines the performance of alternative decision-making procedures.

[4] Egeberg (1996) follows a similar approach; see also Michelmann (1978).

[5] The European Investment Bank and the European Investment Fund are other financial bodies of the European Union (see http://europa.eu/institutions/financial/index_en.htm).

[6] Scheller (2004, p. 44) notes: "As an organization created by the EC Treaty, the ECB enjoys genuine powers. [...] This feature distinguishes the ECB from the various decentralized agencies of the Community, which possess their own legal personality but have competences delegated to them by the Community institutions."

[7] Examples include, among others, Heinemann and Huefner (2004) and Belke and von Schnurbein (2012).