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Nationality and the ECB's Executive Board

Laura Moretti
Center for Financial Studies

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by Laura Moretti

The European Central Bank's (ECB) Governing Council (GC) consists of the Governors of the national central banks (NCBs) of the 17 euro area countries and the six members of the Executive Board (EB). The latter consists of the President, the Vice-President and four other members, who are all appointed by the European Council for a non-renewable term of eight years.

While nationality should not count in the EB, recent appointments of members to the EB show that it remains important. There is an implicit agreement that France, Germany and Italy should be represented on the EB at all times. For example, when President Trichet's term expired and Mario Draghi was appointed as his successor in 2011, France was left without a seat in the EB, but Italy with two. Lorenzo Bini-Smaghi, another Italian member of the Board, subsequently resigned almost a year and an half before the end of his eight-year mandate after what appeared to be outside pressure.

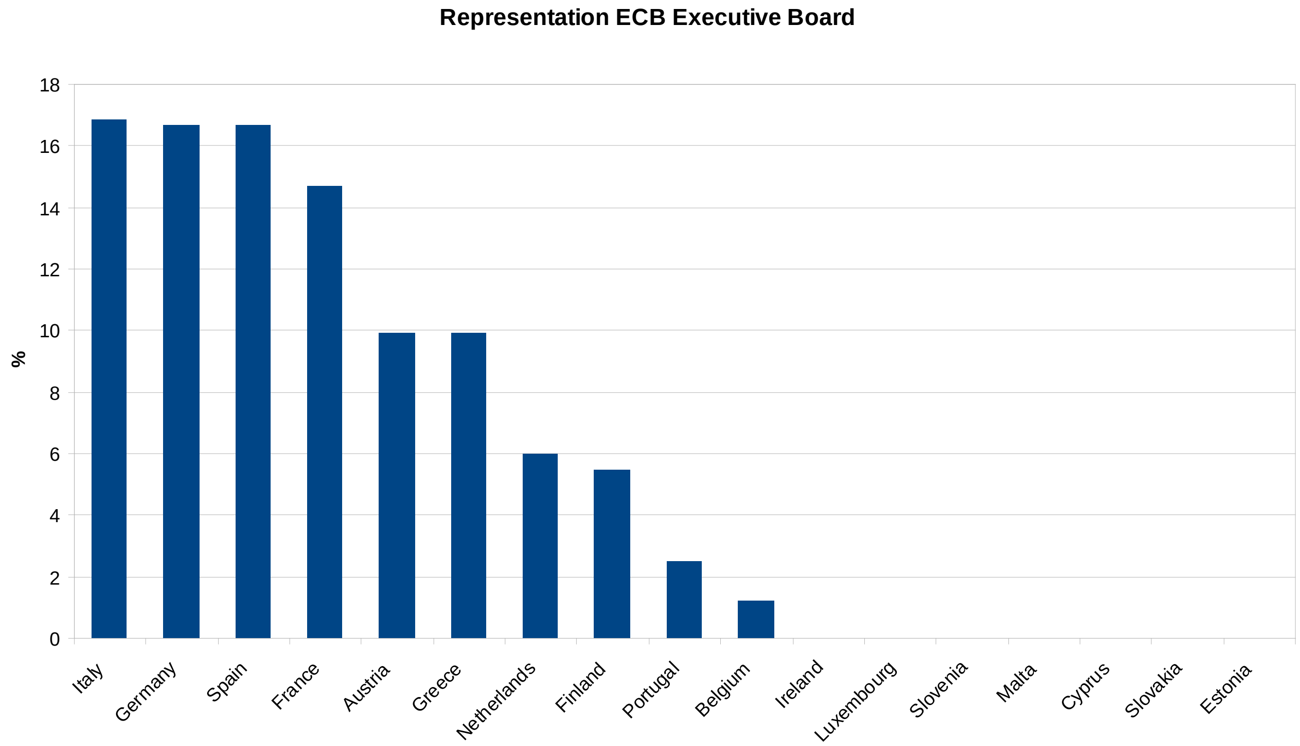
Previously, this implicit agreement also involved Spain. However, when José Manuel González-Páramo’s term ended in May 2012, the Spanish government hoped to maintain a seat in the EB and proposed Antonio Sáinz de Vicuña, head of the ECB’s legal directorate. In the end, Yves Mersch of the Central Bank of Luxembourg was appointed, but only at the Eurogroup meeting in July 2012 after extended discussions.[1]

To understand the role played by the protection of national influence in the appointment of EB members, I analyze the allocation of seats in the EB since the launch of the euro. From January 1999[2] till May 2012, 16 appointments to the EB have been made. Since not all of them were of the same length, I compute the percentage of the total man-months available in the EB in order to study the importance of nationality. Note that the number of seats on the EB is limited to six. Between January 1999 and May 2012 there were 161 months and therefore 161*6 = 966 total man-months of EB membership. Since Germany had one member of the EB at all times, Germany had 161/966 = 16.6% of these man-months. Figure 1 reports the distribution of percentage of man-month for each country.

[1] The appointment still needs the formal approval of the European Council after consulting the European Parliament and the ECB’s GC.

[2] The appointments for the GC started on June 1st 1998.

Figure 1



Next, I contrast these measures of EB membership with the NCBs' subscription shares of the ECB's capital. They are computed using a key that reflects the respective country's share in the total population and gross domestic product of the EU[3]. These two determinants have equal weighting. The ECB adjusts the shares every five years and whenever a new country joins the EU. The adjustment is made on the basis of data provided by the European Commission.[4]

The capital key is a natural benchmark for the country's expected influence within the ECB. However, while all NCBs of the EU countries contribute to the ECB's capital, not all EU members belong to the EMU. In fact, currently the 17 eurozone NCBs' contribution amounts to 69.97% of the ECB's capital. Hence, I compute the percentage of the capital key weighted for the effective months of representation in the GC and only for the euro zone members, see Figure 2.[5] For example, Deutsche Bundesbank, after the last capital increase (29 December 2010), subscribes to 18.94% of the ECB's capital, but, when considering only the capital represented in the GC, the share rises to 27.06%. Moreover, to take into account the fact that countries have been represented in the GC for different periods, I compute a weighted average of the actual percentage representation in the GC. Hence, Deutsche Bundesbank subscribed, on average, 29.29% of the ECB's capital.

[3] Since the start of Stage Three of Economic and Monetary Union on 1 January 1999 the capital key has changed four times: a five-yearly update was made on 1 January 2004 and again on 1 January 2009; additional changes were made on 1 May 2004 (when the Czech Republic, Estonia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Slovenia and Slovakia joined the EU) and on 1 January 2007 (when Bulgaria and Romania joined the EU).

[4] For more information see www.ecb.int/ecb/orga/capital/html/index.en.html.

[5] As a simplification I refer to the single countries represented in the GC even though the subscribers of the ECB's capital are the NCBs.

Figure 2

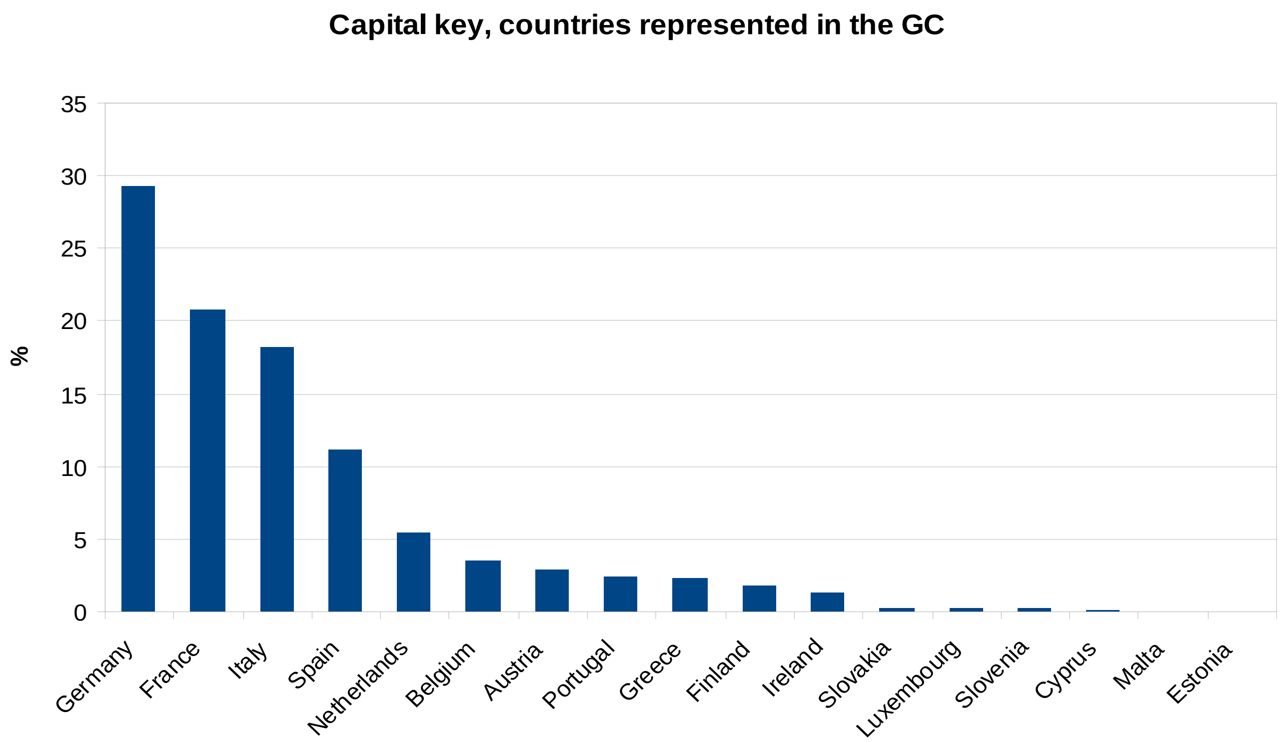


Figure 3 compares the actual man-month representation in the EB by country with the expected using the capital key. For example, since Deutsche Bundesbank represented, on average, 29.29% of the ECB's capital in the GC and there were 966 man-months available in the EB in the period in consideration, Germany would have been expected to be represented in the EB for 282.95 man-months (i.e. 29.29%*966) or an extra 121.95 man-months. Figure 4 highlights the difference between the actual and the expected man months of representation in the EB.

Figure 4 shows that Germany had 122 man-months of membership in the EB less than one would have expected on the basis of the capital key. In brief, Germany could have been expected to hold a second seat in the EB for more than ten years.[6]

[6] A formal test of the hypothesis that the EB distribution is drawn from the same distribution as the capital key rejects that hypothesis.

Figure 3

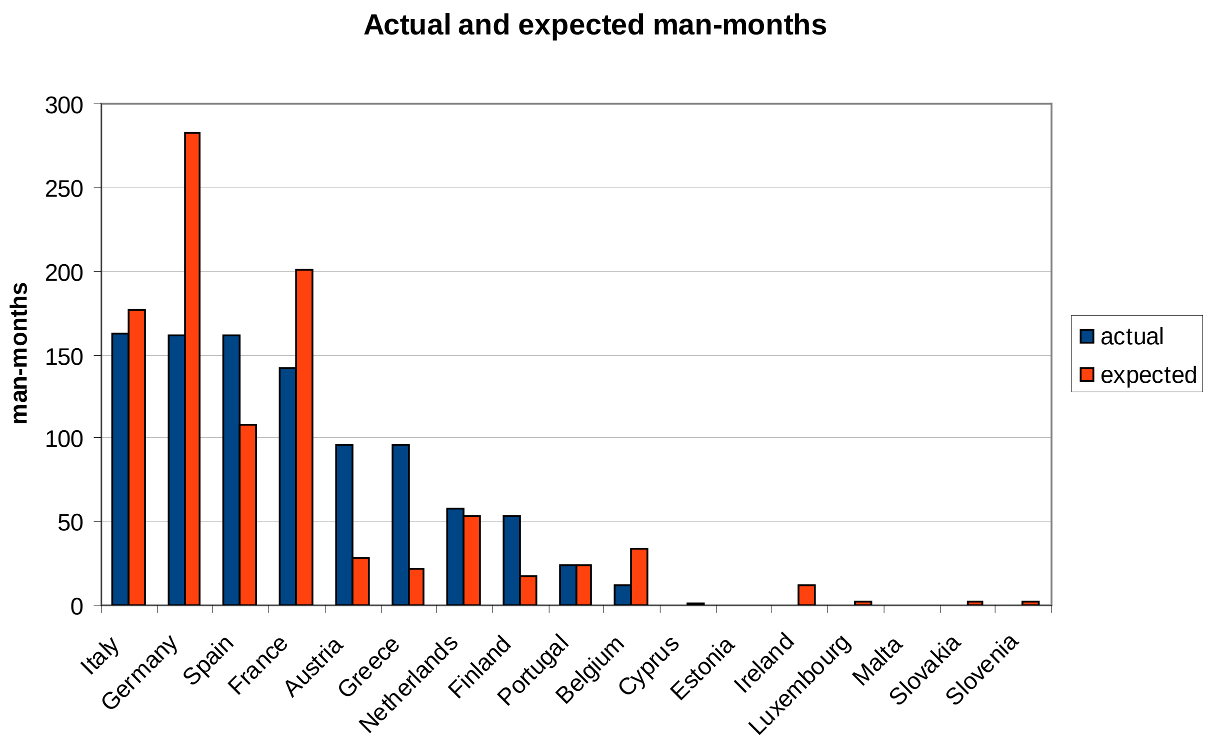
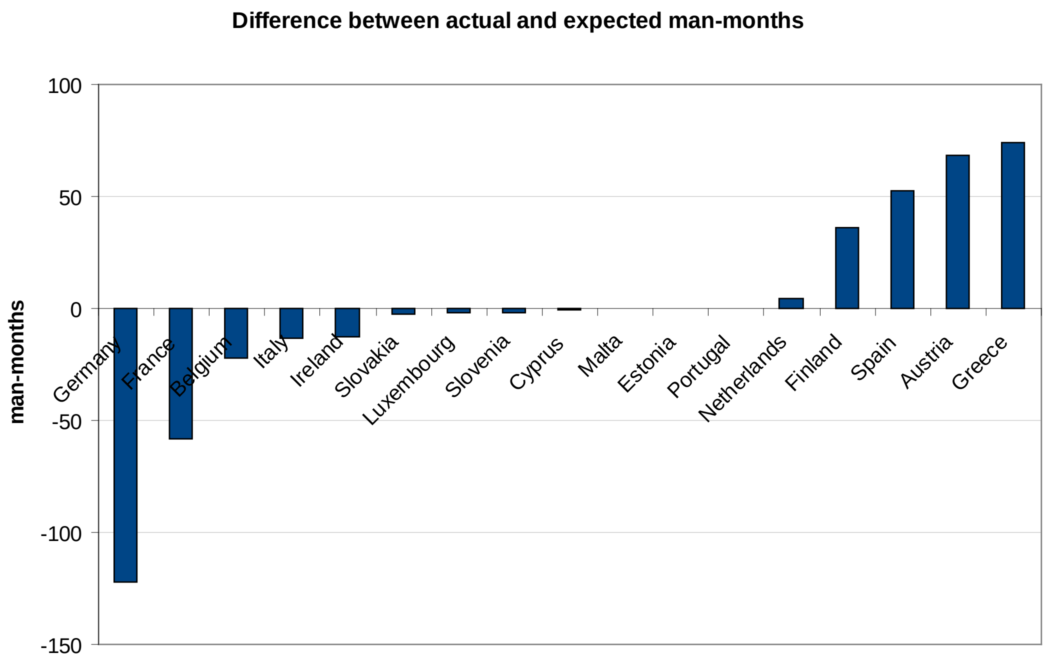


Figure 4



Overall, the Figure shows that the larger countries, in particular France and Germany, have been underrepresented while Austria, Finland and Greece have been overrepresented. This overrepresentation of the smaller countries arises as a consequence of the relative short ECB history and of the "lumpiness" of appointments (each comprises 96 man-months, except the initial ones) and it is likely to go away over time. By contrast, the under-representation of larger countries seems to be systematic.

There is a growing sentiment in Germany that this imbalance represents a problem. Bundesbank President Jens Weidmann in a recent interview pointed out the conflict between the Bundesbank's shares of voting rights in the GC and its actual influence saying that it is "the largest and most important central bank in the Eurosystem" and has "a greater say than many other central banks".[7]

The under-representation of some countries might be more of a problem when taking unconventional monetary policy decision than interest rate setting decisions. In fact, it is commonly argued that since the ECB's objective is to set interest rates to achieve price stability in the euro area, the nationality of the decision makers is irrelevant. The collegial decisions-making procedure with no revelation of the voting record or, apparently, without an explicit voting is aimed at ensuring that monetary policy is set in the best interest of the euro area as a whole.

However, tensions have arisen during the financial crisis when deciding unconventional monetary policy interventions. Decisions on how to improve the flow of credit in the economy by accepting a broader range of collateral and engaging in outright purchases in government bonds and other claims involve the assumption of risk by the ECB. While the risk arising from these operations is often assumed entirely by the national central banks that engage in them and haircuts on collateral have been increased to offset it, there is little doubt that the ECB's own balance sheet has become riskier. Since any losses on it would be shared according to the capital key, the under-representation of the larger countries on the GC that would have to shoulder a greater share of the risk could lead to excessive risk taking.

There are two ways to deal with the German under-representation. One is to give Germany a second EB appointment; a second is to use weighted voting. However, that would force the GC to start voting on all matters, which it has so far sought to avoid, presumably in order to minimize public perceptions of disagreements between members.

The exceptional circumstances in which the ECB has been operating in the past years are testing not only the currency union itself, but also its institutional design. While the Governing Council of the ECB was designed to mainly set interest rates optimally for the union as a whole, the recent crisis has expanded the tools of the ECB to include unconventional monetary policy actions that potentially increase the risk exposure of its balance sheet. Since each country would contribute to the losses according to its capital key, a different voting mechanism that takes into account the single country's contribution to the ECB's capital could be advisable.

[7] For the complete interview see: http://www.bundesbank.de/Redaktion/DE/Interviews/2012_07_27_weidmann_bundesbankmagazin.html