**Leading the Future of the Public Sector: The Third Transatlantic Dialogue**
**University of Delaware, Newark, Delaware, USA**

**May 31–June 2, 2007**

**Workshop 5: Leadership and the New Public Management**

# Leading Central Banking in Europe

Martin Marcussen

*Address for correspondence:*
Martin Marcussen
Associate professor
Department of Political Science
Copenhagen University
Øster Farimagsgade 5
PBox 2099
DK-1014 Copenhagen
Denmark

mm@ifs.ku.dk
+45 35.32.34.99

**ABSTRACT**

Central bank reform takes place everywhere and it seems that the reforms are pointing in the same direction towards more transparency, outcome performance and committee decision-making. However, in Europe the reforms differ in terms of time, timing and tempo. By investigating leadership strategies in the Swedish Riksbank, the Danmarks Nationalbank, The Banca d'Italia and the European Central Bank these differences come out clearly. To understand them factors at the micro, meso and macro-level will have to be brought in.

**From Buddies to Managers**

It is not long ago that central bankers cultivated an image of mysticism by actively invoking the sacred aura of their institution. When newly employed personnel entered the US Federal Reserve Building, they were expected to abide to the confidential fraternity of that institution. They were "taking the veil" – an expression that describes nuns entering a convent (Greider, 1987: 54). In Germany, the same. The Bundesbank was reputed for its very effective socialization mechanisms ensuring that newcomers rapidly integrated into the procedures and cultures of the institution. Bundesbank insiders referred to this phenomenon as "the Becket effect" drawing "on the saga of Henry II's chancellor, Thomas à Becket, who opposed the King after he was made Archbishop of Canterbury – and was murdered for his pains" (Marsh, 1992: 22). This helps to explain the development of a very strong sense of community within the Bundesbank.

The Federal Reserve's decision-making process has been described as the modern equivalent of mysterious sanctification. The FED "enfolded itself in the same protective trappings that adorned the temple – secrecy, mystique, an awesome authority that was neither visible nor legible to mere mortals. Like the temple, the Fed did not answer to the people, it spoke for them. Its decrees were cast in a mysterious language people could not understand, but its voice, they knew, was powerful and important" (Greider, 1987: 240). In a similar vein, and borrowing a concept from William Ouchi (1980), Bundesbank governors are best described by their "curious clannishness" (Marsh, 1992: 22). Accordingly, it has been common to take the "mythology of central banking" as a point of departure for theory building within the field of central bank studies (Chant and Acheson, 1973; Acheson and Chant, 1973). In line with Selznick (1948), a central bank sort of bureau will be concerned with enjoying a long life and with achieving prestige within the social hierarchy of government bureaus. This can best be done by avoiding conflict with stakeholders and by consolidating autonomy by a strategy of mythology-building. Milton Friedman once observed that central bankers had two principal objectives: 'avoiding accountability on the one hand and achieving public prestige on the other' (Friedman cited by Fisher, 1990: 1181, fn. 5).

The issue is probably best summarized by Karl Brunner:

> "Central banking [has been] traditionally surrounded by a peculiar and protective political mystique. Criticism of Central Banks, if it occurred at all in the political arena, [has been] muted and infrequent … The mystique thrives on a pervasive impression that central Banking is an esoteric art. Access to this art and its proper execution is confined to the initiated elite. The esoteric nature of the art is moreover revealed by an inherent impossibility to articulate its insights in explicit and intelligible words and sentences" (Brunner, cited in Goodfriend, 1986: 64).

The 1990s, however, have seen sweeping reforms in the world of central banking. Like many other parts of the public administration, central banking has been exposed to sigma-type values and reforms associated with that type of thinking, such as transparency, communication, evidence-based decision-making, autonomization and de-politicization, outcome performance etc. For instance, today, central bankers are busy emphasizing their *transparency and communicative* skills. According to the European Central bank (ECB) "in democratic societies, central bank independence needs to be balanced with accountability to the public and its elected representatives" (ECB, 2004: 66). Sure, accountability has a somewhat different meaning in the world of central banking than for the rest of the public administration (Forder, 2002: 64). To central bankers, accountability refers to an obligation to properly explain and justify decisions. To all others, accountability is also normally associated with a possibility to dismiss the accountable (Gregory, 2003: 559). This is clearly not possible with regard to the ECB Executive Board.

It is also a common theme to refer to *evidence-based decision-making in committees* (Blinder, 2006). A decade ago, final responsibility for decisions made in central banks was placed on the shoulders of a single governor. Today, most central banks are organized around collective decision-making in committees that are typically constituted by a variety of societal actors and supported by a research department. The establishment of the European Central Bank, for instance, replaced twelve central banks which mostly used to be run by individual governors. By involving a broad section of societal actors in the formulation of monetary policies the signal here is that central banking apparently has become pluralized and that decisions are being made on the basis of scientific analysis, in contrast to intuition. Evidence so far does not seem to support the hypothesis that committee decision-making is more effective than single governor decision-making.

A third trend in central banking concerns a general shift towards *outcome performance* taking the form of inflation targeting. General rules are being established thereby reducing the extent to which discretion can be exercised in monetary policy-making. Inflation targets are typically formulated by the treasury of the country in question as a result of which most central banks cannot be said to be goal independent. However, central banks have, over the course of the 1990s more often than not, been reformed so as to enhance their instrument independence. Again, so far there is no evidence to the fact that inflation targeters are more effective in maintaining inflation stable than those central banks that are not bound by a precise formulation of their objective. In addition, there is not much evidence confirming that inflation targeters are in fact pursuing the stated targets.

In general, therefore, it seems as if central bankers today are constructing new images of themselves in the broader public. From cultivating an image based on lambda-types values, today central bankers promote a picture based on sigma-type values (Hood, 1991). From possessing clan-like characteristics, modern central bankers present themselves as being more in the business of managing organizations in free market competition (Ouchi, 1980) (Table 1).

*Table 1:* From Buddies to Managers

| | Central Banking as Business | Central Banking as Bureaucracy | Central Banking as Buddying |
|---|---|---|---|
| Criteria for success | Resource effectiveness and price stability | Regularity and predictability. Trust, and societal stability | Security and welfare of in-group members |
| Indicators of failure | Resource waste and missed targets | Arbitrariness and lacking societal legitimacy | External supervision and intervention |
| Recruitment | Ability to deliver is decisive for hiring decisions | Formal merit is decisive for hiring decisions | Integrity, loyalty and personal contacts are decisive factors |
| Employment conditions | Time-limited contracts | Unlimited if formal rules are complied with | Unlimited if group norms are complied with |
| Decision-making | Evidence-based committee work | Rule-based standard operating procedures | Intuition – typically a one man's show |
| Style of interaction | Goal-oriented | Formal | Personal |
| Relation to environment | Frequent with stakeholders and customers | Routinized contacts with stakeholders | As little as possible |

Clearly, central bankers cannot be reasonable compared to private businesses. There is not much competition among central banks. Rarely do central banks go bankrupt and, basically, they do not have to perform well to prosper and grow. In addition, whereas private businesses mostly have to redirect their policies so that they conform to markets, central banks are more often than not in a position to influence the economy. They can simply redirect markets so that they conform with central bank objectives. However, despite these obvious differences between private businesses and autonomous, national agencies such as a central bank, management philosophies from the private sector have gained ground in the world of central banking. *The purpose of this paper is to investigate how central bank leadership has responded to the "modern" central bank discourse*. In which ways, if any, has managers undertaken institutional reforms, and if central bank managers are exposed to the same global reform discourse how can we then explain that different institutional reforms have been undertaken in the Danmarks Nationalbank, the Swedish Riksbank, the Banca d'Italia and the European Central Bank?

**Leadership Challenges in Four Central Banks**

A common characteristic for the typically quite substantial reforms undertaken in central banking over recent years are that they expose central bank governors to three types of leadership challenges: concern with the *perception* of central bankers held by stakeholders and the broader population, concern with the extent to which outcome *performance* is maximized, and concern with streamlining and adapting existing working *procedures* to new functions.

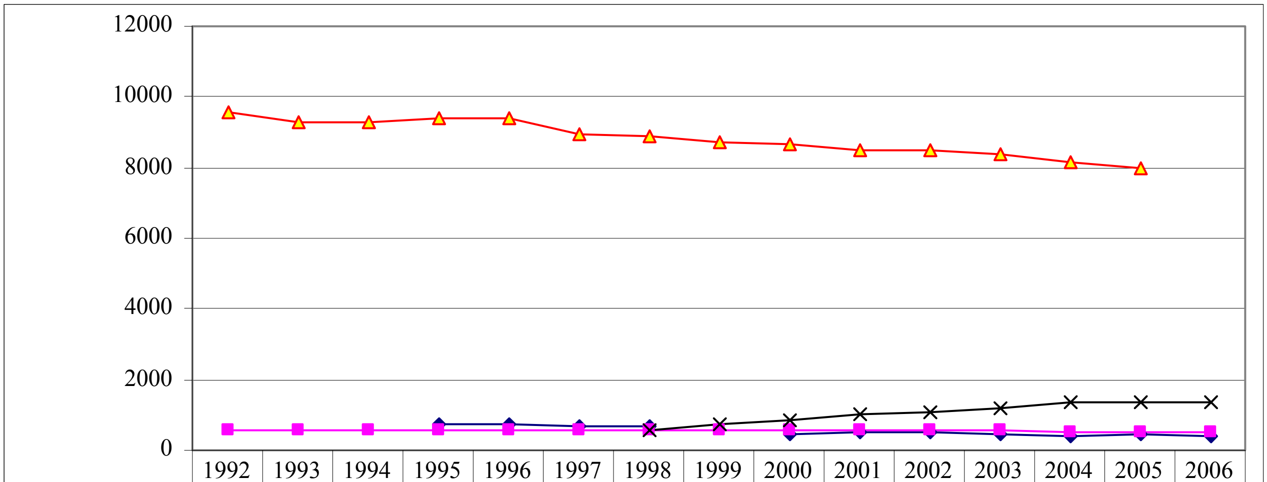
As regards perception, it has been particularly challenging for central bank managers to turn an organizational culture and practice based on deep-rooted introversion into one based on communication, openness, and talk. Among the world-wide trends in public management, the ones farthest away from the self-identification of central bankers concerns accountability and broad legitimacy. The balance that has to be found is one between legal autonomy from political supervision, on one hand, and an obligation to be answerable to broader public needs and to the requirements of the stakeholders, on the other. Most typically central bankers frame the issue in terms of a particular type of transparency (Blomgren and Sahlin-Andersson, 2007), i.e. one which perceives transparency as a means to enhance outcome effectiveness of central banking.

On the internal lines central banks have, clearly in accordance with sigma-type values, been institutionalizing a series of governance principles such as a formulation of a clear strategy and mission statement, the introduction of rules that preempt conflicts of interests at the level of the board of the bank, the establishment and strengthening of an independent audit function, establishment of unambiguous lines of responsibility throughout the organization, and official adherence to corporate principles in the business sectors of the central bank, e.g. in the areas of procurement, buildings and human resource policies, including rules on ethics and codes of conduct (Koch, 2007: 5). Much of this has come from the IMF in the form of a Code of Good Practices on Transparency in Monetary and Fiscal Policies (IMF, 2000).

When it comes to performance, "an almost lexicographic priority is typically assigned to the price stability objective" (Frisell *et al*., 2006: 6). Accordingly, it is in relation to price stability that the success or failure of independent central banks are measured. This dimension is, at first glance, not new to central bank managers, since some dimension of stability has always been the primary objective of the art of central banking. Indeed, some would argue that the inner core of a central bank culture can be characterized as a stability dogma. In earlier periods, gold was synonym to stability, then anchor currencies such as the British Pound, the US Dollar or the German Mark, symbolized stability. The issue is, however, that stability today is being politically defined as being a certain range of accepted price inflation. Thus, central bankers, in pursuing their most central objective, typically need the full backing of their political counterparts. As we will see, in the case of the ECB such a backing cannot be taken for granted.

With regard to procedures, European monetary integration has changed the rules of the game. This clearly is a major challenge to central bank management. Depending on the extent to which a certain European central bank is integrated with the Euro-area, different rules apply. Some central banks belong to the Euro-insiders and others to the Euro-outsiders. If anything, the creation of a European System of Central Banks has enhanced the process towards creating a differential process of integration (Umbach and Wessels, 2007). Clearly, Euro-insiders have formally transferred the competence to conduct monetary policy to the European Central Bank. But also, Euro-outsiders, such as Danmarks Nationalbank, which is pursuing a stable currency policy in relation to the Euro, is *de facto* not utilizing its monetary competences. In addition, most central banks have lost competences over financial supervision (Arnone *et al*., 2007). Only one of the central banks investigated in this paper, the Banca d'Italia, possesses the formal authority to undertake supervision of the financial sectors. Yet, in principle all four central banks have responsibility for the stability of the payment systems of their constituencies. Giving away competences and central functions such as these must necessarily have large consequences for the internal structuring of work within central banks. A most immediate consequence of this reduction of central bank competences among the national central bank in the Euro-area is that a considerable number of bank personnel has been dismissed (Figure 1). Mostly in the regional branches but also in the central offices.

*Figure 1:* Development in staff numbers (FTEs)




| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Sweden | | | | 754 | 709 | 664 | 669 | | 460 | 488 | 501 | 450 | 420 | 429 | 404 |
| Denmark | 593 | 578 | 589 | 592 | 586 | 579 | 566 | 556 | 552 | 563 | 559 | 544 | 536 | 516 | 515 |
| Italy | 9542 | 9295 | 9307 | 9396 | 9400 | 8956 | 8914 | 8730 | 8663 | 8515 | 8481 | 8351 | 8132 | 7957 | |
| ECB | | | | | | | 550 | 720 | 830 | 1032 | 1094 | 1170 | 1362 | 1369 | 1343 |

Source: Annual Reports

In the following, I will shortly study how four central banks have managed these challenges in terms of institutional reforms. It makes sense to distinguish between different types of central banks according to the ways in which they traditionally have been positioned in the world of central banking (decision-takers or decision-makers) and according to how they seem to have reacted to present challenges as regards institutional modernization (first-movers or late-comers). These dimensions make it possible to distinguish between four types of leadership strategies: The Swedish efforts of overhauling the internal structures and procedures, the Danish attempts at compensating for Euro-outsiderness by diversifying external relations, the ECB's success in establishing itself as a veritable powerhouse and global monetary authority, and the Italian pains at maintaining a position of authority inside and outside Italy (Table 2).

*Table 2*: Four answers to the leadership challenge in modern central banking

| | Exposure to Challenges | |
|---|---|---|
| | Decision-takers | Decision-makers |
| First Movers | *Sweden:* Internal modernization | *ECB:* Establishing and Consolidating Authority |
| Late Comers | *Denmark:* External Network Diversification | *Italy:* Rescuing what's left of Authority |

***Internal Modernization in Sweden***

We know that Denmark and Sweden have a troubled relationship with the European Union. We also know that public debate in these two countries about the European Union oscillates between almost complete silence about day-to-day activities in the EU, on one hand, and very intensive campaigns preceding EU-referendum campaigns, on the other. In Denmark, the issue of introducing the Euro and thereby becoming fully integrated into the Euro-area has been up for public referendums on three occasions. In 1992, the Euro was rejected, in 1993, a so-called opt-out from the Euro-area was adopted, and in 2000 the Euro was rejected once again. In Sweden, the Euro was rejected once in 2003 (Table 3). Across party lines, there are no serious attempts in these two countries at present to re-engage in a debate about the possibilities of introducing the Euro as a national currency. The position as semi-permanent Euro-outsiders seem to have been consolidated by the perception that it is actually possible to find a way to success and stability outside the Euro-area, and the realization that membership of the Euro-system, rather than constituting a reform catalyst in various countries have worked as a reform barrier (Duval and Elmeskov, 2006).

*Table 3:* Referenda in Denmark and Sweden on EMU

| **Denmark** | Yes | No | Turnout | Result |
|---|---|---|---|---|
| 1992, 2 June: Referendum about the Maastricht Treaty with a protocol in which the Danish government promises to organize another referendum before adoption of the Euro | 49,3 | 50,7 | 83,1 | Rejected |
| 1993, 18 May: Referendum about the Maastricht Treaty with a declaration stating that the Danish government has obtained an opt-out from the third stage of EMU | 56,7 | 43,3 | 86,5 | Accepted |
| 2000, 28 September: Referendum about abolishing the opt-out and introducing the Euro | 46,9 | 53,1 | 87,5 | Rejected |
| **Sweden** | | | | |
| 2003, 14 September: Referendum about introducing the Euro | 42 | 55,9 | 82,6 | Rejected |

Although extremely important, the peaks and bottoms of public debate is only one face of the European Union in Sweden and Denmark. The other face of the twin-faced EU is the professional and pro-active diplomatic European activities that take place continuously – but which are typically hidden from the attention of the broader public. Underneath the surface, Danish and Swedish civil servants are finding their ways inside and outside the EU labyrinth, creating networks of contact and adapting their institutions to the reality of European integration (Jacobsson *et al*., 2004). This is also the case with central bank institutions in these two countries. Historically, internal cooperation within the framework of formal or informal exchange rate regimes is the norm rather than the exception (Table 4). Seen in that perspective, the current Euro-outsiderness of the Danish and Swedish central banks is somehow an abnormally.

*Table 4:* The Danish and Swedish Central Banks in Successive Cooperative Currency Arrangements

| Cooperative Currency Arrangements | **Sweden** | **Denmark** | **Italy** |
|---|---|---|---|
| EMU | | | 01.01.1999 - present |
| ERMII | | 01.01.1999 – present | |
| ERM | 17.05.1991 – 19.11.1992 | 01.01.1979 – 01.01.1999 | 11.1996 - 12.1998<br>03.1979 - 08.1992 |
| Snake Cooperation | 03.1972 – 29.08.1977 | 19.02.1972 – 01.01.1979 | 09.1971 – 01.1973 |
| Smithsonian Agreement | 19.12.1971 – 19.03.1973 | 19.12.1971 – 19.03.1973 | |
| Bretton Woods | 31.08.1951 – 23.08.1971 | 12.12.1946 – 23.08.1971 | 04.1946 – 08.1971 |
| Interwar Gold Standard | 01.04.1924 – 27.09.1931 | 01.01.1927 – 29.09.1931 | 12.1927 – 11.1934 |
| Classical Gold Standard | 27.05.1873 – 02.08.1914 | 01.01.1875 – 06.08.1914 | 04.1883 – 01.1894 |

*Source: Jonung (2000), Mikkelsen (1993), Olsen and Hoffmeyer (1968), Svendsen and Hansen (1968), Sveriges Riksbank (1999: 4), Garofalo (2005).*

However, the ways in which these two countries' central banks have compensated for their Euro-outsiderness have differed to a considerable extent. Formally, the position of the Swedish central bank within the Swedish public apparatus as well as the adopted monetary and financial policies which characterize Sweden as a Euro-outsider have gone through a long series of policy and constitutional reforms over the past two decades. In comparison, Danmarks Nationalbank and the Banca d'Italia do not come anything near the waves of reforms undertaken in Sweden (Table 5).

*Table 5:* Constitutional Reforms in the Riksbank, Nationalbanken and the Banca d'Italia

| | **Sweden** | **Denmark** | **Italy** |
|---|---|---|---|
| 1981 | | | Divorce between Banca d'Itaia and the Treasury: The Central Bank is no longer legally obliged to finance government deficits |
| 1982 | The government announces a 16 percent devaluation within the framework of the ERM | The government declares its support for a fixed exchange rate regime. | |
| 1987 | | A so-called "sound policy"/"stability-oriented" macro-economic policy strategy is being pursued, implying sound money (low inflation) and sound finances (balanced budgets) | |
| 1988 | A new Riksbank Act:<br>• The chairman of the Governing Board is no longer appointed by the government, but by the other seven members of the Board.<br>• The Governor's term in office is made longer (five years) than that of the rest of the Board and the parliament (three years, at the time).<br>• There is no indication of the objective for monetary policy-making | | |
| 1991 | The government declares that low inflation is an overriding goal for stabilization policy. | | |
| 1992 | *November*: After repeated speculative attacks against the Swedish currency the Riksbank abandons the pegged exchange rate policy. | | *February*: The Banca d'Italia acquires the exclusive right to set interest rates |
| 1993 | *January*: The Riksbank declares an explicit inflation target.<br>*February*: A parliamentary committee presents a proposal for a new Riksbank Act, including a price stability objective for monetary policy and increased central bank independence. The proposal does not achieve enough political support and is not formally presented to the parliament.<br>*October*: The first inflation report is published. | | *November*: The Treasury's account at the Banca D'Italia is closed down. |
| 1995 | *January*: Sweden becomes a member of the European Union.<br>*November*: The first Inflation Report is published. | | |

| | | | |
|---|---|---|---|
| 1997 | The Riksbank starts to publish its inflation forecasts and Financial Stability Reports. | | |
| 1997 | A new proposal for a price stability objective and increased central bank independence is presented, this time under broad political consensus. | | |
| 1999 | An amended Riksbank Act comes into effect. | | January 1999: The Banca d'Italia becomes a full member of the Euro-system |
| 2005 | | | Fazio scandal triggers reform: time-limited tenure of governor; transparency and collective decision-making. |

*Source: Heikensten and Vredin (2002: 9), Hoffmeyer (1993), Quaglia (2005a, 2005b, 2007).*

Internally, these changes have also implied considerable structural and procedural reforms in Sweden, whereas in Denmark, reforms have been informal. Thus, over the preceding ten years the organization and culture of the Riksbank have been completely overhauled. From 1997 onwards, competences were gradually transferred from the top level management to the individual departments. The number of departments has been reduced from sixteen to eleven in 2000 and then again from eleven to seven in 2004. The regional offices were closed down and a considerable number of employees in these offices as well as in the Riksbank building have been dismissed. For instance, in 2003 the Board of the Riksbank decided that the number of employees (FTEs) would be reduced by 10 per cent over a three year period. Regular attitude surveys among bank staff have been carried out since 1997. The most recent survey concludes that the employees on those unites that have been cut down in recent years "tend to have more negative impressions" of the Riksbank and its Governor (Sveriges Riksbank, 2007: 52). Towards the end 1990s, the Riksbank used to be one of the most attractive workplaces in Sweden for newly graduated economists. This is no longer so. The Riksbank has simply dropped out of Universum Communication's ranking of the top-15 most popular workplaces (www.universumeurope.com).

All managers of the Riksbank have been going through intensive management training with particular focus on communication and output performance. The official corporate culture declared in 2002 is based on openness, competence, cooperation, overall view (whole of government), initiative and respect. The Executive Board adopted a so-called strategic plan in 2005 with strategic targets emphasizing quality, efficiency and confidence, and in 2006 this plan was turned into a "new vision" for the Riksbank. By constantly comparing itself to other central banks as well as other public authorities and private corporations, and by constructing an organization prepared for change, the "new vision" will be transformed to reality. Over the years, the Riksbank has, by example and choice, taken a lead in the discussion among central banks about central bank efficiency. The point of departure is that central banks are not, like private corporations, exposed to market competition as a result of which other efficiency enhancing mechanisms will have to be installed in central bank organizations. Completely in line with sigma type values the recommendation is to reduce the number of tasks entrusted to central bankers (focusing on the efficiency of the payment system and maintaining price stability), spelling out precisely when an outcome has been achieved (by introducing Inflation Targeting, for instance) and by improving the transparency of the organization thereby allowing for internal and external evaluations of the bank (Blix *et al*., 2003). In short, the Riksbank seems to have closely followed the mainstream advices about central bank modernization (Mendzela, 2002, 2003, 2006).

***External Network Diversification in Denmark***

In Denmark, the situation is very different. Over the last decade, no major internal reforms have taken place in the Danmarks Nationalbank. In 1998 a so-called "information office" and a web-site was installed underlining a felt need to respond regularly and systematically to inquiries. The following years a number of regular publications were streamlined, both in terms of form and content, thereby appealing to a larger readership. The number of employees has, overall, remained relatively constant. However, the composition of employees has changed radically. Slowly but steadily, an increasing number of university-educated economists are painting the picture, replacing employees from other lower-educated branches. The bank has a quite low turn-over rate and the average seniority seems to be very high (13-15 years on average; 21-22 years among leaders). The number of employees with more than 25 years of seniority amounts to 20 per cent of the workforce. A survey conducted among the employees concluded that employment satisfaction is high. Danmarks Nationalbank has for many years figured among the 15 most popular workplaces for newly graduated economists (www.universumeurope.com). From 2000, a personal directive was adopted emphasizing the importance of employee satisfaction and personal development. Increasingly emphasis is being put on education and skill-upgrading of employees in the Danmarks Nationalbank. Over the last decade, the budget consecrated to learning arrangements has doubled manifold. Interestingly, Danmarks Nationalbank actively encourages its younger economists to take a stage in one of the many international financial institutions around. On average 15-20 persons are permanently on leave from Danmarks Nationalbank, spending time in an international organization.

From 2000, the bank explicitly states it basic values. One central element is to safeguard traditions while attempting to engage in renewal. Another central value is to provide services to the public. Transparency becomes central in that regard. The level of transparency institutionalized in the Danish central bank does not, however, measure up with the Swedish Riksbank. The Danish governor does not have an obligation to explain his policies in parliament, and no minutes are being released from decision-making forums.

In terms of organizational structure, the number of departments has, if anything, remained relatively constant over the years (16-17 departments). Literally nobody has been dismissed over the last decade as a result of streamlining the organization. In contrast to other central banks in the same period, no resources have been invested in a distinct research department. A certain tendency towards decentralization has taken place in recent years. Decisions about promotion, for instance, are now being made in the various departments rather than in the executive board.

In the Danish central bank, the non-reforms that have taken place are explained by the fact that the bank undertook the major part of its reforms earlier than the world trend (Pedersen, 2006: 10). For instance, the last regional branch was closed already in 1989. In addition, the costs of running the bank are, in international comparison, quite low. This is taken to be an indication of the continuous streamlining which is taking place in a gradual manner, rather through large-scale reforms. In addition, it is more labor intensive to run a system of inflation targeting such as the Swedish Riksbank, than to tie ones currency to the Euro. Finally, the salaries of the employees in the Danish central bank are, although clearly higher than in manufactory, among the lowest in Europe (Table 6). Reforms or not, the Danish central bank governor has for years topped the rankings of the most trusted and most powerful decision-makers among Danish elites (Berlingske Nyhedsmagasin, various years).

*Table 6*: Staff Costs in Four Central Banks

| 2004 | (1) Annual salary in industry in Dkr | (2) Staff costs per employee per year in Dkr. | (2)/(1) | Relative price level | Staff costs per employee per year in Dkr., PPP corrected | Index of PPP-corrected staff costs |
|---|---|---|---|---|---|---|
| Danmarks Nationalbank | 309.000 | 529.000 | 1,7 | 100 | 529.000 | 100 |
| Swedish Riksbank | 277.000 | 536.000 | 1,9 | 89 | 602.000 | 114 |
| Banca d'Italia | 199.000 | 564.000 | 2,8 | 75 | 752.000 | 142 |
| European Central Bank | … | 923.000 | … | 79 | 1.168.000 | 221 |

Source: Pedersen (2006: 12)

Which compensation strategies have been applied in the two Scandinavian central banks in question? Clearly, tremendous internal and constitutional reforms have been undertaken in Sweden. The ongoing reform programs implemented over the last ten years have fundamentally altered the central bank on almost all dimensions. Such policy and constitutional reforms have been absent in the Danish case. If anything, considerable informal changes have taken place. Gradually, the composition of employees has been altered. Today, the Danish central bank is a knowledge organization just as any other central bank. A quite substantial amount of the budget is being applied on education and HR-development. In addition, increased emphasis has been put on establishing a more differentiated relationship to other actors on the scene for international capital. For instance, young employees are being encouraged to take up positions in international financial organizations, and the traveling activity has, on a general note, increased dramatically. This is done deliberately so as to cultivate contacts and consolidate lines of information. Information that the Danish central bank does not automatically get through membership of the ECB or BIS decision making centers. In Sweden, no further change has taken place with regard to external networking. The Riksbank, in contrast to Danmarks Nationalbank, has traditionally been very well integrated into international financial circles.

***Rescuing what's Left of Authority in Italy***

In the Italian political landscape, the Banca d'Italia has for almost three decades constituted a pillar of stability and reliability. The country ranks a lowly 45$^{th}$ on Transparency International's 2006 Corruption Perception Index (CPI) which is just below Malaysia, South Korea and Botswana and down five points from the previous year. Seen in that perspective the Banca d'Italia is perceived to be an island of trustworthiness and public opinion surveys reveal that the Bank is one of the most trusted institutions in Italy (Quaglia, 2007: 6). Among economic students, the Banca d'Italia appears to be a very attractive workplace (www.universumeurope.com). This may also have something to do with the fact that the bank's staff have consistently been among the best paid civil servants in Italy (Table 6). On a larger scale, the Italian central bank governor is one of the best paid central bankers in the world (Table 7). The Banca d'Italia is furthermore one of the largest central banks in Europe in terms of employees (Figure 1). Even if regional offices have been cut off and the head office has been marginally slimmed, these reforms do not amount to a major overhaul of the organization. In fact, membership of the Euro-area has not in itself triggered any internal reforms of the Banca d'Italia.

*Table 7:* Central Bank Governors' Salaries, 2003 (US$)

| | | |
|---|---|---|
| Antonio Fazio | Banca d'Italia | $700.000* |
| Wim Duisenberg | European Central Bank | $417.000 |
| Lars Heikensten | Sveriges Riksbank | $241.000* |
| Bodil Nyboe Andersen | Danmarks Nationalbank | $253.000 |

*membership of the Board of the Bank for International Settlements adds another $90.000 to the salary

Source: www.centralbanknews.com, 18th August 2003; annual reports.

Externally, the Banca d'Italia has for many years maintained a reputation for research excellence. The Bank clearly obtains prestige by its active research profile and in European and global rankings the Banca d'Italia is located among the very best. The Banca d'Italia has established a veritable power house of research with a research department which in size equals the one of the Bank of England (St-Amant *et al.*, 2005). Thus, the ECB, the Banca d'Italia and the Bank of England are the only European central banks among the top ten central banks in terms of publishing in top-quality academic journals. In addition, the Banca d'Italia has also traditionally had a reputation for being a very efficient financial supervisor. Except from the bankruptcy in 1981 of the Banco Ambrosiano there have not been any major financial scandals in Italy during the 1980s and 1990s. Since 2000, however, the situation has changed radically.

The internal governance reforms undertaken in 2005 appear to be a very rare exception to the general rule that the Banca d'Italia has been very immune from global management fashions. The fact that Antonio Fazio violated EU rules on the free movement of capital by attempting to stop the foreign banks ABN Amro and BBVA from acquiring control of private Italian banks has seriously damaged the credibility of the Bank. It took long and sustained pressure from EU member states, the European Commission, financial markets and even in the form of strikes among the Bank staff to convince Fazio to resign in December 2005, leaving the seat to Mario Draghi, a professor in economics with extended professional experience from private and public offices. The Italian parliament used the occasion to approve legislation under which future governors would be appointed for only six years, renewable only once. Until then, the governor used to be chosen from among the deputy governors and appointed for life (Table 8). The parliament also introduced some principles of transparency requiring the Bank to publish reports more frequently, to write justifications for decisions made and minutes for meetings of the Executive Board. Finally, some elements of collectivity were introduced with the 2005 reform. Until then, Mr. Fazio had been a centralizer solely representing the bank externally as well as internally. But now the decisions are to be made collectively by the five members of the Executive Board, i.e. the governor, the director general and the three deputy directors-general (Quaglia, 2007). In terms of appointment, the procedure has been opened up, allowing for more governmental influence. At present, all members of the executive board are being appointed by the Italian President acting on a proposal from the prime minister. This should allow for more outsiders to enter the decision-making forums of the bank.

*Table 8:* Average tenure in four European central banks

| **Denmark** (employment to the age of 70) | **Italy** (6 year terms) | **Sweden** (5 year terms) | **ECB** (EMI) (8 year terms) |
|---|---|---|---|
| Bramsnæs (1936-49)<br>Nielsen (1950-1964)<br>Hoffmeyer (1965-95)<br>Nyboe-And. (1995-05)<br>Bernstein (2006- ) | Einaudi (1945-48)<br>Menichella (1948-60)<br>Carli (1975-1979)<br>Ciampi (1979-1993)<br>Fazio (1993-2005)<br>Draghi (2005- ) | Rooth (1929-1948)<br>Böök (1948-1951)<br>Lemne (1951-1955)<br>Åsbrink (1955-1973)<br>Wickman (1973-1976)<br>Nordlander (1976-79)<br>Wohlin (1979-1982)<br>Dennis (1982-1993)<br>Bäckström (1994-02)<br>Heikensten (2002-05)<br>Ingves (2006-) | Lamfalussy (1993-96)<br>Duisenberg (1996-03)<br>Trichet (2003-) |
| Average tenure:<br>17,25 years | Average tenure:<br>12 years | Average tenure:<br>7,6 years | Average tenure:<br>5 years |

***Establishing and Consolidating Authority at the ECB***

If both the Danmarks Nationalbank (1818), the Swedish Riksbank (1668) and the Banca d'Italia (1893) are old central banks with long institutional memories, the European Monetary Institute (EMI), the predecessor to ECB, was established at the beginning of the so-called second stage of the Economic and Monetary Union in Europe on January 1, 1994. With the start of the third and final stage of EMU on January 1, 1999 the ECB was established in the picture of the German Bundesbank as the most independent central bank on the globe with a legal mandate to pursue price stability as its primary objective. Clearly, a European Central Bank that is taking over exclusive competences of monetary policy from 12 EU-member states with established traditions in an everything but optimal currency area is a daunting task requiring planning and analysis down to the smallest detail and demanding professional leadership. The question that everybody asked at the time of the transition to the third stage of EMU was whether the ECB would possess the same kind of credibility as the Bundesbank. To obtain that credibility a high level of legal autonomy from political supervision was supplemented with a transparency policy and the establishment of a veritable powerhouse of research in Frankfurt. The best economic researchers from Europe and abroad were employed to boost the scientific authority of the organization. The ECB Governor went out of the way to underline that the ECB intended to over-comply with the treaties establishing the ECB. For instance, according to the treaties the ECB is only required to publish annual reports and to present them to parliament. In addition to this, the ECB engaged in active interaction with the media, with researchers, with European and national elected politicians etc. Despite of that, a recurrent theme in the debates between the Economic and Monetary Affairs Committee of the European Parliament and the ECB President has been the need for more transparent action. Indeed, in contrast to the central banks of Sweden, Denmark and Italy, the ECB has from the very beginning had a much more troubled relationship with Parliament.

Already during the first year of the life of European Economic and Monetary Union the first of a series of external events challenged the governance structures of the ECB. In 1999, the EU-Commission under Commission President Jacques Santer was forced to resign as a result of internal mismanagement, fraud and nepotism. This had repercussions in all corners of the EU system, also in the ECB where the concept of Corporate Governance became central. Internal as well as external audit mechanisms were established in the ECB and systematic cooperation with the EU office for fighting corruption (OLUF) was initiated. In addition, accountability and legitimacy became integral concepts in the management vocabulary of the Bank. Over the next couple of years, staff rules and codes of conduct were adopted, and systematic education of managers was initiated. Equal opportunity and ethics advisers were employed and more systematic relations to employer organizations in the form of a social dialogue as well as with the European ombudsman were established.

The next challenge that had repercussions for internal management was the preparation for the introduction of the Euro on January 1, 2002. During 2001, the entire apparatus was working frenetically to inform citizens about this event, to educate bankers, civil servants and technicians, to solve technical and logistical problems and to convince the financial markets that everything was in control. Having succeeded the replacement of a large number of national currencies with the Euro with convincing professionalism, the next challenge was already waiting for the ECB managers in 2003. During that year, ten Central and Eastern European countries were making their last preparations for membership of the European Union. For their part, ECB managers formulated a set of new decision-making rules which was, at first, rejected by the European Parliament, but then later adopted by the Heads of State and Government. Then started a major education effort involving technical assistance so as to assure that the new members had the right institutional infrastructure for membership, i.e. independent central banks and sound financial institutions. The ECB formulated an Accession Master Plan spelling out an economic dialogue with the new members, and listing a large series of workshops, training, conferences and the establishments of an appropriate IT-infrastructure.

In 2003, after consultation with the ECB employees, the first mission statement of the ECB was formulated. The result of a staff survey showed that ECB personnel identified themselves with values such as “high level of integrity”, “competence”, “efficiency” and “transparency”. In 2005 “Trust”, “accountability” and “decentralization” were added to the list. Also in 2003, the executive Board set up a program office to monitor an organizational change program called “ECB in motion”. The ECB’s looked at itself as a constantly changing and adapting organization. In the same vein, it introduced “diversity management” with a view to cultivating differences among the multinational staff-members exploiting their individual talents and capabilities.

With these challenges the ECB was gradually expanding in terms of budget and personnel. The number of departments was growing and rapidly the Euro-Tower in Frankfurt became too small as a result of which new premises are being constructed. Overall, the ECB has, despite of all the challenges to its internal governance and the politicized environment been exceptionally successful in delivering results. The Euro is strong compared to the dollar and inflation in Europe remains close to 2 per cent. In addition, EuroBarometer surveys conclude that the ECB is considered to be one of the most trustworthy Institutions of the European Union.

Clearly, the ECB together with the Swedish Riksbank, in contrast to the Banca d'Italia and the Danmarks Nationalbank, almost fully adopt the latest management principles and values as described in the introduction to this paper. Both banks are in a process of almost constant change, establishing multiple channels of communication with the environment, increasingly focusing on single and measurable objectives, making decisions in collective forums and streamlining organizational structures and processes to cope with new challenges. The leadership strategies adopted in Danmarks Nationalbank are more characterized by silent information seeking and pragmatic, informal adaptation to challenges when they occur. This is clearly in line with the traditional Danish model of institutional change. Over the last two decades, this has, in the case of Denmark, proved to be a success. Danish institutional competitiveness seems to be high in all sorts of international rankings. In Italy, the situation is different. From having been the only source of stability in a very politicized atmosphere, the Banca d'Italia has lost credibility on the international financial scene. This it is trying to regain through formal reforms. It remains to be seen whether the colossal Banca d'Italia reacts to these reforms in appropriate ways or whether it will be forced into reform tracks similar to other banks of the same size, such as the Bank of England. This will bring the Banca d'Italia into the mainstream reform trend and away from the mythical pictures of central banking as being a paradise for buddies.

**Conclusion: Same but Different**

Over the last two decades, the four central banks that have been studied in this paper have all developed in the same direction. Central banking is not (anymore) as closed and distant as usually claimed. Increasingly central banks are communicating with the world. Norms such as transparency, accountability, communication, and committee decision-making go together with norms such as autonomy, science, governance by rules and evidence-based reflection. However, it comes out clearly that the reform tempo, time and timing of the four central banks investigated in the paper differ to a considerable degree. Two questions emerge. Firstly, how can we understand the differences? And, secondly, do these reforms imply that we are moving towards a "better place" than the one we came from?

To answer the first question it may be useful to adopt a broad reform perspective usually referred to as a transformative perspective (Christensen and Lægreid, 2001, 2007). Accordingly, we will need to merge explanatory factors from the macro, meso and micro level to grasp the complexity of institutional reform. At the macro-level, it makes sense to focus on external challenges to central bank governance structures. The meso-level highlights organizational routines and cultures, and the micro-level pinpoints reform entrepreneurs. In the case of Sweden, for instance, the currency crises of Autumn 1992 and the up-coming membership negotiations regarding membership of the European Union turned out to be decisive triggers for a reconsideration of the institutional structure of monetary policy-making. From scratch, Swedish central bank leaders rapidly started to put together a format for an entirely new central bank borrowing from global first movers such as the Bank of Canada and the Reserve Bank of New Zealand, and learning from successful management reforms elsewhere in the Swedish public administration. The resulting model turned out not to be different from, but rather very similar to other semi or fully autonomous agencies in Sweden.

In Denmark, in contrast to Sweden, there have been no major external shocks that could trigger central bank reform. On the contrary, over the last two decades, the Danish economy has gone through one of the longest periods of constant growth and low inflation. The Danish success model works and it seems to be the case that the Bank in its own informal and gradual ways are keeping costs down on a level which largely compares to the rest of the public administration.

This is very much in contrast to the situation in Italy. For decades, no basic internal reforms of the governance structure of the Banca d'Italia have taken place. Being the third largest central bank in Europe, and clearly the most expensive in running costs, the central bank has not felt a pressure for change because it constituted the only island of stability on an unruly political arena. However, it took micro-level scandals to change the situation. When Fazio, who had established procedures and structures which guaranteed that he had full control over and information monopoly in the gigantic organization, turned out to be the weak link thereby undermining trust in the entire organization, the route was laid out for reforms. Much is still to be done, however, before the Banca d'Italia can measure up with Sweden or the ECB in terms of modernization.

The ECB seems to be a special case among the four central banks. It is newly established, it is supranational and the change dynamics are built into the organization at the meso-level. It is planning for governance change resulting from the introduction of the Euro in 2002 and enlargement with new members in 2004. External factors also play a role, though. The legitimacy crisis and the administrative deficit of the EU-Commission spilled-over into the ECB that reacted by emphasizing transparency, communication and accountability to an even higher extent.

It is easy to come to an agreement about the inappropriateness of lambda type values in modern governance systems. Seen in that perspective it seems to be a democratic improvement that a closed, self-sufficient public administration is opened up for external scrutiny. However, the new place towards which we are moving may have its own problems. Employees in central banking, for instance, seem to have lost confidence in their managers. Ongoing reforms, downsizing and reorganizations have apparently led to staff mistrust and lowering staff morale. Half of the central bank staff surveyed across the EU said employment conditions are worsening, 39 per cent reported a drop in job satisfaction and 43 per cent said they no longer share the values of the organization for which they work (Storey, 2002a; 2002b). In other words, in solving one problem – lacking transparency, introversion and low effectiveness – another management problem seems to pop up.

This may not be the only problem to worry about. Autonomous, single-purpose organizations such as independent central banks chasing the low inflation objective may in general be unsuited to the whole-of-government framework now identified as the fashion that replaces New Public Management (Christensen and Lægreid, 2006). When central banks make decisions it has consequences elsewhere in the polity and if central bankers stubbornly pursue their narrow objectives neglecting demands and needs elsewhere in the societal apparatus, then the whole business of central banking may be running into a legitimacy crisis. An early warning of that is the ongoing rhetorical battle that unfolds in the European Parliament when debating with the ECB president. MEPs are insisting on a whole-of-government approach to the running of monetary policies in Europe, and the ECB president is even stronger emphasizing its constitutional duty to bring inflation down in Europe. Even the most independent central banks in history, the Bundesbank and the American Federal Reserve System, could not in the longer term afford to ignore political signals for policy changes.

## References


Acheson, Keith and John F. Chant (1973), "Bureaucratic Theory and the Choice of Central Bank Goals", *Journal of Money, Credit, and Banking*, 5(2): 637-655.

Arnone, Marco, Salim M. Darbar, and Alessandro Gambini (2007), "Banking Supervision: Quality and Governance", *IMF Working Paper*, WP/07/82, Washington: International Monetary Fund.

Blinder, Alan (2006), "Monetary Policy by Committee: Why and How"? *DNB Working Paper*, no. 92, February, Amsterdam: De Nederlandsche Bank.

Blix, Mårten, Sonja Daltug and Lars Heikensten (2003), "On Central bank Efficiency", *Economic Review of the Riksbank*, no. 3, pp. 81-93.

Blomgren, Maria and Kerstin Sahlin-Andersson (2007), "Quests for Transparency: Signs of a New Institutional Era in the Health Care Field", in Tom Christensen and Per Lægreid, eds. *Transcending New Public Management. The Transformation of Public Sector Reforms* Ashgate, pp. 155 -178.

Chant, John F. and Keith Acheson (1973), "Mythology and Central Banking", *Kyklos*, 26(2): 362-379.

Christensen, Tom and Per Lægreid, eds. (2006), *Autonomy and Regulation: Coping with Agencies in the Modern State*, Cheltenham: Edward Elgar.

Christensen, Tom and Per Lægreid (2007), "Introduction – Theoretical Approach and Research Questions", in Tom Christensen and Per Lægreid, eds. *Transcending New Public Management. The Transformation of Public Sector Reforms*, Aldershot: Ashgate, pp. 1-16.

Christensen, Tom and Per Lægreid, eds. (2001), *New Public Management. The Transformation of Ideas and Practice*, Aldershot: Ashgate.

Duval, Robert and Jørgen Elmeskov (2006) "The Effects of EMU on Structural Reforms in Labour and Product Markets", *Economics Department Working Paper*, no. 438. Paris: OECD.

ECB (2004), *The Monetary Policy of the ECB*, Frankfurt: European Central Bank.

Fischer, Stanley (1990), "Rules versus Discretion in Monetary Policy", in Benjamin M. Friedman and Frank H. Hahn (eds.), *Handbook of Monetary Economics*, vol. 2, North Holland, Amsterdam, pp. 1169–1178.

Forder, James (2002), "Interests and 'Independence': The European Central Bank and the Theory of Bureaucracy", *International Review of Applied Economics*, 16(1): 51-69.

Frisell, Lars, Kasper Roszbach and Giancarlo Spagnolo (2006), "Governing the Governors: A Clinical Study of Central Banks", paper presented at the workshop "The Governance of Central Banks", August 31st – September 1, Stockholm: Riksbanken.

Garofalo, Paolo (2005), "Exchange Rate Regimes and Economic Performance: The Italian Experience", *Working paper*, no. 10, Rome: Banca d'Italia.

Goodfriend, Marvin (1986), "Monetary Mystique: Secrecy and Central Banking", *Journal of Monetary Economics*, (17), pp. 63–92.

Gregory, Robert (2003); "Accountability in Modern Government", in B. Guy Peters and Jon Pierre, eds. *Handbook of Public Administration*, London: Sage, pp. 557-568.

Greider, William (1987), *Secrets of the Temple. How the Federal Reserve Runs the Country*, New York: Simon and Schuster.

Heikensten, Lars and Anders Vredin (2002), “The Art of Inflation Targeting”, *Sveriges Riksbank Economic Review*, no. 4, Sveriges Riksbank, Stockholm, pp. 5–34.
Hoffmeyer, Erik (1993), *Pengepolitiske problemstillinger 1965-1990*, Copenhagen: Danish Central Bank.
Hood, Christopher (1991), “A Public Management for All Seasons”? *Public Administration*, 69(1): 3-19.
IMF (2000), “Supporting Document to the Code of Good Practices on Transparency in Monetary and Financial Policies, Part 1: Introduction” (July), www.imf.org/external/np/mae/mft/sup/part1.htm
Jacobsson, Bengt, Per Lægreid and Ove K. Pedersen (2004), *Europanization and Transnational States. Comparing Nordic Central Governments*, London: Routledge.
Jonung, Lars (2000), “Från guldmyntfot till inflationsmål – svensk stabiliseringspolitik under det 20:e seklet”, *Ekonomisk Debatt*, 28(1): 17-32.
Koch, Elmar B. (2007), “Challenges for Governance at Central Banks”, paper presented at the conference “Non-state Actors as Standard-setters: The Erosion of the Public-Private Divide”, February 8-9, Basel, Switzerland.
Marsh, David (1992), *The Bundesbank. The Bank that Rules Europe*, London: Heineman.
Mendzela, John (2002), “Leadership and Management in Central Banking”, *Central Banking*, 13(2): 40-46.
Mendzela, John (2003), “Leadership and Management of Central Banks”, *Central Banking*, 13(3): 59-66.
Mendzela, John (2006), “How to Manage the 21$^{st}$-Century Central Bank”? *Central banking*, 16(4). 31-39.
Mikkelsen, Richard (1993), *Dansk pengehistorie 1960-1990*, Copenhagen: Danmarks National Bank.
Olsen, Erling and Erik Hoffmeyer (1968), *Dansk pengehistorie 1914-1960*, Copenhagen: Danmarks Nationalbank.
Ouchi, William G. (1980), “Markets, Bureaucracies and Clans”, *Administrative Science Quarterly*, 25(1), 129-141.
Pedersen, Erik Haller (2006), “Danmarks Nationalbank’s Operating Costs and Number of Employees in International Comparison”, *Working Papers*, no. 35. Copenhagen: Danmarks Nationalbank.
Quaglia, Lucia (2005a), “Civil Servants, Economic Ideas, and Economic Policies: Lessons from Italy”, *Governance*, 18(4): 545-566.
Quaglia, Lucia (2005b), “An Integrative Approach to the Politics of Central Bank Independence: Lessons from Britain, Germany and Italy”, *West European Politics*, 28(3): 549-568.
Quaglia, Lucia (2007), “The Banca d’Italia: Between Europeanisation and Globalisation”, paper presented at the workshop: “Changing Modes of Central Bank Governance: Internationalization and Europeanization” at the University of Cardiff, 19-20 April.
Selznick, Philip (1948), “Foundations of the Theory of Organization”, *American Sociological Review*, 13(1): 25-35.
St-Amant, Pierre, Greg Tkacz, Annie Guérard-Langlois and Louis Morel (2005), “Quantity, Quality, and Relevance: Central Bank Research, 1990-2003”, *Working Paper*, 2005-37, Ottawa: Bank of Canada.

Storey, John (2002a), “The European System of Central Banks as an Organizational innovation: Implications for Work Practices and Employment Relations”, *Working Paper Series*, no. 1, Open University Business School Research: Human Resource Research Unit.

Storey, John (2002b), “Comparative Practice in Employee Representation and Consultation: A Study in European Central Banking”, *Working Paper Series*, no. 1, Open University Business School Research: Human Resource Research Unit.

Svendsen, Knud Erik and Svend Aage Hansen (1968), *Dansk pengehistorie 1700-1914*, København: Danmarks Nationalbank.

Sveriges Riksbank (1999), *Annual Report 1998*, Stockholm: Sveriges Riksbank.

Sveriges Riksbank (2007), *Annual Report 2006*, Stockholm: Sveriges Riksbank.

Umbach, Gaby and Wolfgang Wessels (2007), “The European System of Central Banks: Implications for ‘Insiders’ and ‘Outsiders’”, paper presented at the workshop: “Changing Modes of Central Bank Governance: Internationalization and Europeanization” at the University of Cardiff, 19-20 April.

8.576