



UNIVERSITY OF ICELAND

In Defence of Small States: Reflections after the 2008 Icelandic Bank Collapse

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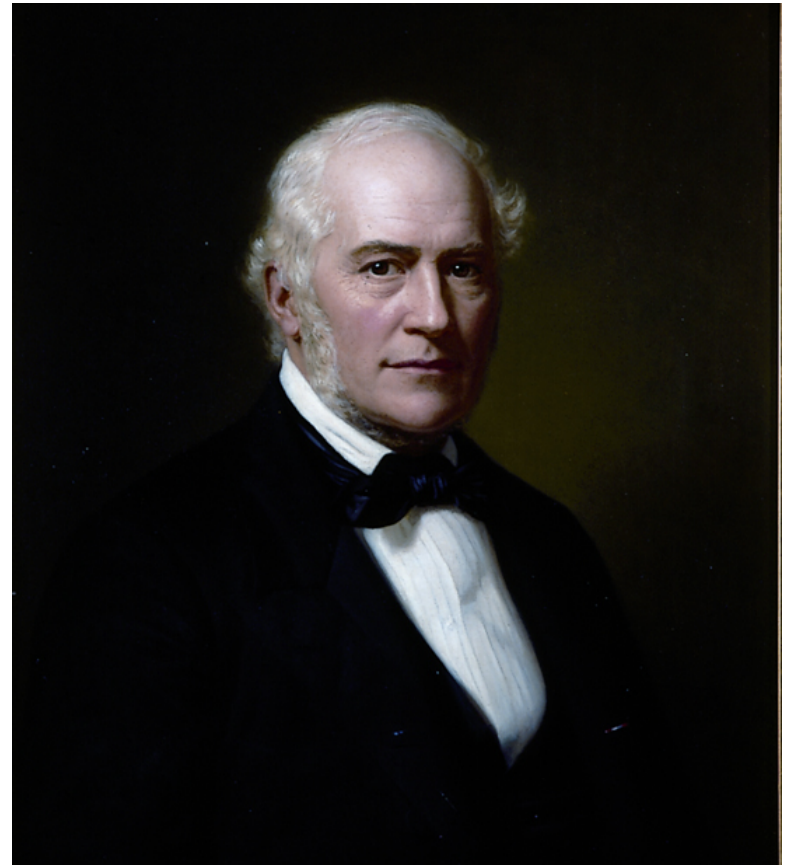
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The Sibert-Thorhallsson Thesis

- 2008 bank collapse showed Iceland was too small
- She has to join the EU to get “shelter”
- Small economies more volatile
- Economies of scale in providing public goods
- Small countries more vulnerable to disasters
- Lack of professionalism in small states
- Political favouritism in small states

Was Jon Sigurdsson Wrong in 1848?

1. Icelanders have from outset been independent, sovereign
2. A distinct nation with her own language and culture
3. They know better than foreign bureaucrats what is right for them
4. Iceland should trade with all, not only with one



Proliferation of Small States

- No! History shows that Jon Sigurdsson was not wrong
- 76 independent states in 1946; 195 in 2016
- Main causes:
 1. Disintegration of empires (Russia, Habsburg and Ottoman dominions, British Empire)
 2. Nationalism (Secessions of Norway 1905, Iceland 1918, Slovakia 1993, etc.)
 3. Triumph of democracy, less resistance to secession
 4. Most important: increased economic integration making smallness less costly

More Economic Integration Makes Less Political Integration Possible



Small States Wealthier

- Maintain open economies, enjoy benefits of free trade
- Alesina: Of 10 richest countries, only 4 with populations over 1 million: US, Switzerland, Norway, Singapore
- Large countries not rich: China, India, Indonesia and Brazil (only exception US)
- Becker: Less systemic exploitation; monopoly not subsidised; homogeneous populations

Small States Volatile and Vulnerable?

- Volatile? True, but not very relevant because:
 1. Found ways to cope with volatility, flexibility and consensus politics (Katzenstein)
 2. Large states volatile, Great Depression in the US and Germany, Nazism
- Vulnerable? True, but not the whole story:
 1. homogeneity means more solidarity
 2. Self-insurance can stretch over time no less than space

Economies or Diseconomies of Scale?

Outlays to produce public goods as a proportion of GDP in 2006 (OECD)

Country	Public Services	Defence	Public Order	Total
Sweden	7.7	1.7	1.3	10.7
Denmark	6.0	1.6	1.0	8.6
Iceland	4.8	0.1	1.4	6.3
The UK	4.9	4.9	2.6	10.0
The US	4.8	4.8	2.1	11.2

Less Costly to be Small

- Costs of statehood, e.g. foreign service, negligible fraction of GDP
- The more cohesive, or homogeneous a state, the less the cost of maintaining public order and reach consensus
- Small states not aggressive like large ones (less militarism)
- Complexity also has its costs (e.g. multi-layered and non-transparent bureaucracy)

Less Professionalism?

- Smaller talent pool, yes. But professionalism depends more on civic culture than size of population (Brazil, India, China, Indonesia all corrupt countries, with little professionalism)
- Civic culture strong in some small countries because of strong collective identity, solidarity, cohesion, trust, transparency
- Little “hard corruption” in small Nordic countries, perhaps some “soft corruption”

Political Patronage: 2008 Study

- Comparative survey of party patronage in 15 European countries
- Iceland one of five with least party patronage (Netherlands, Denmark, the UK, and Norway)
- Little corruption according to Transparency International index
- To be expected: cohesive, transparent, homogeneous, strong civic culture
- Major reforms in 1991–2004 Iceland; opportunities for corruption reduced by transferring decisions from political to private realm

Core of Truth in “Shelter” Theory

- In a wide sense, implausible; in a narrow sense, trivial
- Wrong to speak of cultural shelter: aim is fruitful, cultural exchanges
- Wrong to speak of economic shelter: aim is trade to mutual benefit
- But small states lack military power and therefore need allies or protectors
- Therefore, the Atlantic Alliance essential to small states in Europe
- Blessing in disguise that in financial crisis Iceland was left out in the cold

