

# The Economics of Independence

A Question of Size

# Small Countries: Heroes....

- Huge success stories: Ireland's Celtic Tiger, Iceland, Baltic States

# Small Countries: Heroes....to Zeros?

- Huge success stories: Ireland's Celtic Tiger, Iceland, Baltic States
- Banking collapse in Iceland
- Fiscal crisis in Greece and Baltic States
- In Ireland.....both

# Mighty minnow?

## World Competitiveness Index, 2010

Country	Ranking
<b>Switzerland</b>	<b>1</b>
<b>Sweden</b>	<b>2</b>
<b>Singapore</b>	<b>3</b>
United States	4
Germany	5
Japan	6
Finland	7
Netherlands	8
Denmark	9
Canada	10

# Mighty minnow? Or Little PIG?

**World Competitiveness  
Index, 2010**

**Moody's Misery Index, 2010**

Country	Ranking
<b>Switzerland</b>	<b>1</b>
<b>Sweden</b>	<b>2</b>
<b>Singapore</b>	<b>3</b>
United States	4
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Japan	6
<b>Finland</b>	<b>7</b>
Netherlands	8
<b>Denmark</b>	<b>9</b>
Canada	10

Country	Ranking
Spain (10% debt, 20% unemployment)	1.
<b>Latvia (8.5%, 19.9%)</b>	<b>2</b>
<b>Lithuania (9.2%, 17.6%)</b>	<b>3</b>
<b>Ireland (12.5%, 14%)</b>	<b>4</b>
<b>Greece (12.2%, 10.2%)</b>	<b>5</b>
UK (12.9%, 8.7%)	6
<b>Iceland (10.7%, 10.6%)</b>	<b>7</b>
United States (10.3%, 10.4)	8
<b>Jamaica (9.1%, 11.3%)</b>	<b>9</b>
France (8.3%, 10.2%)	10

# New Consensus: Big Is Best

*“In turbulent times it’s better to be on the bigger boat”* – Paul Volcker, former Federal Reserve Chair

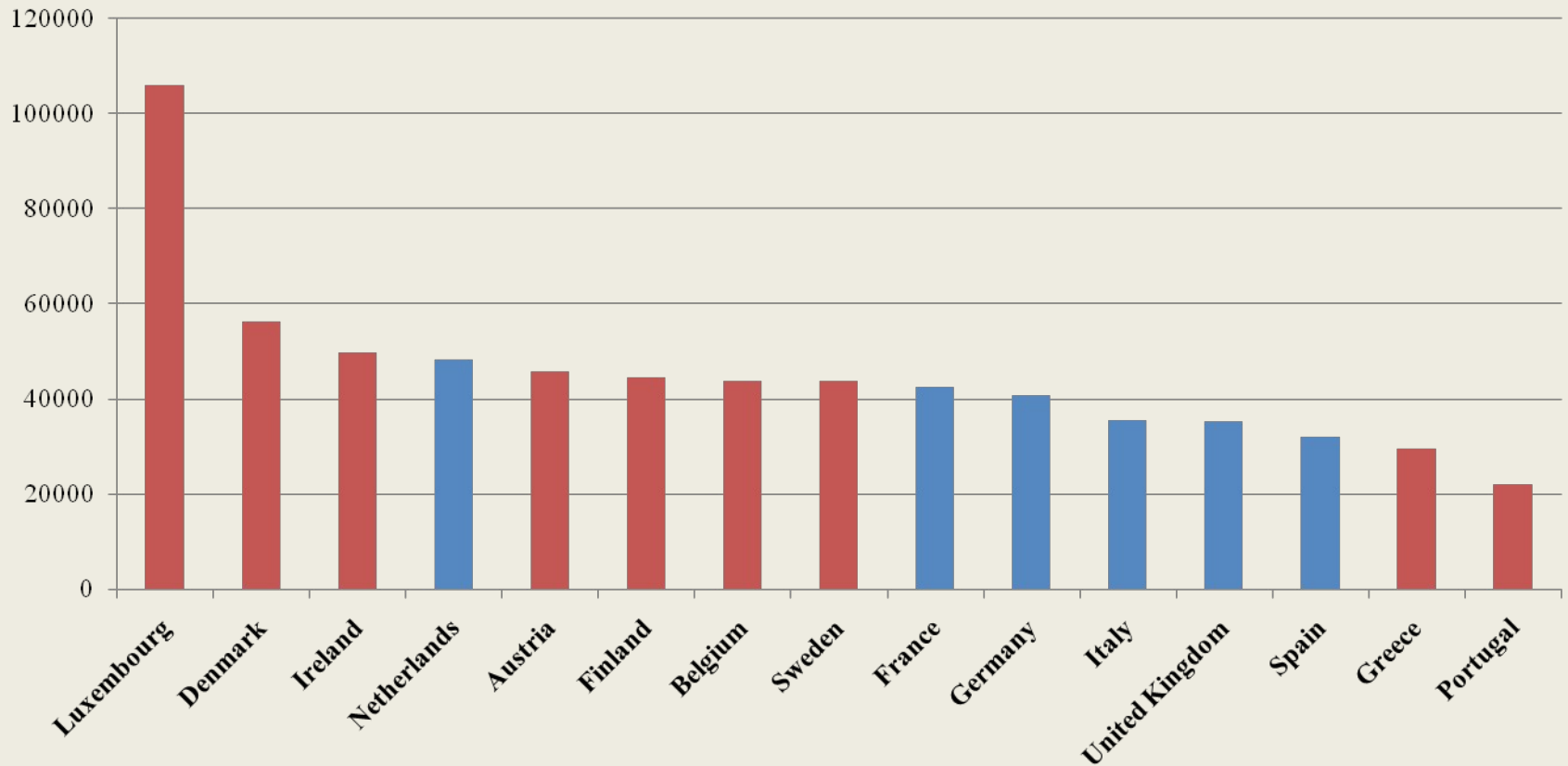
*“NOKIA should have relocated to California a decade ago”* *Bloomberg Business Week*, editorial, 20<sup>th</sup> to 26<sup>th</sup> September 2010

It is tragedy of the eurozone that it is run as a collective of small countries.” Walter Munchau, *Financial Times*, June 2010

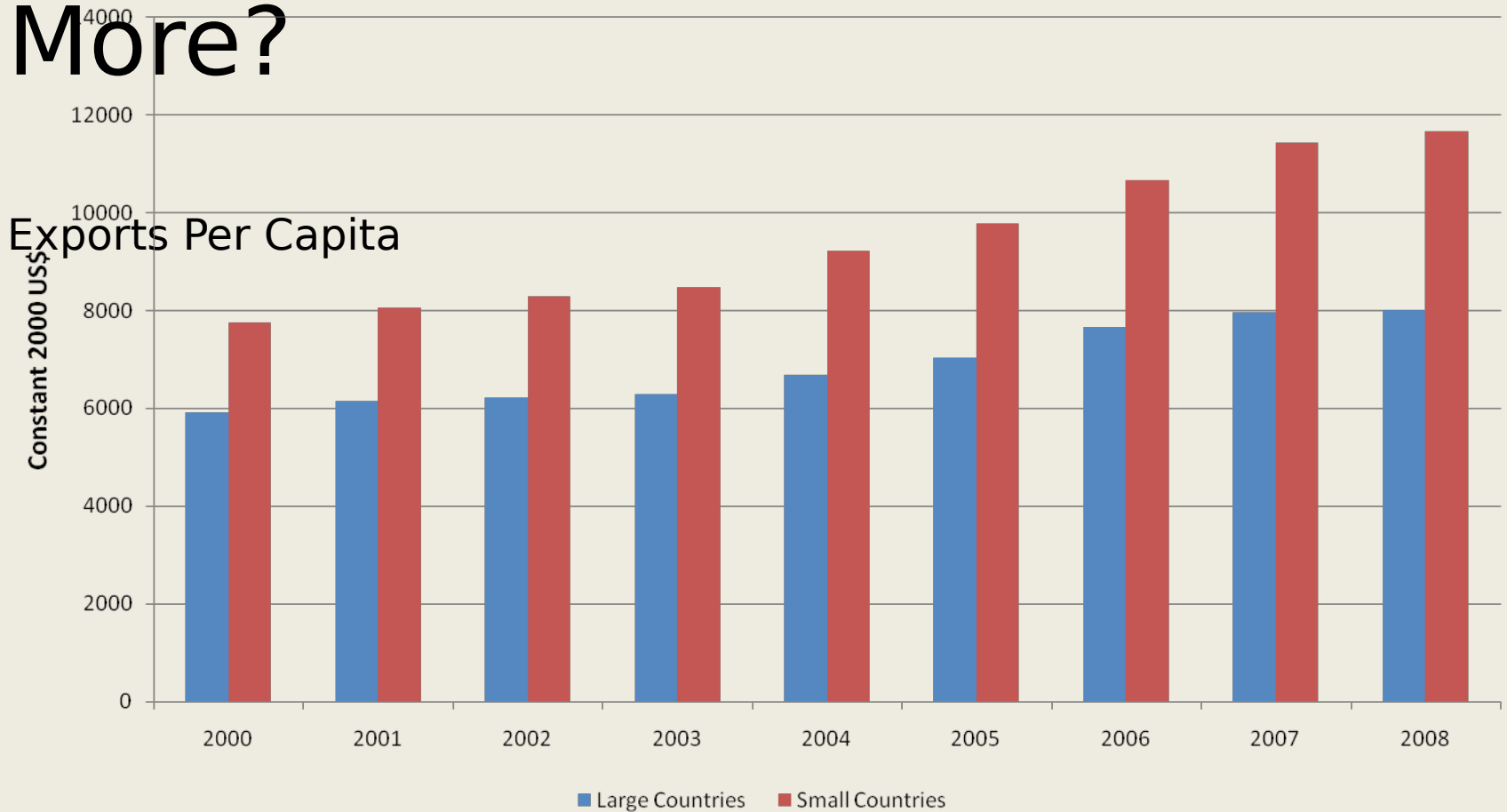
...without getting into any real specifics...a large country is very likely to be stronger than a small country”. Dominique Strauss-Kahn, Interview, *Newsweek*, November 8 2010

# Small is Richer

GDP per capita (2009 US dollars)

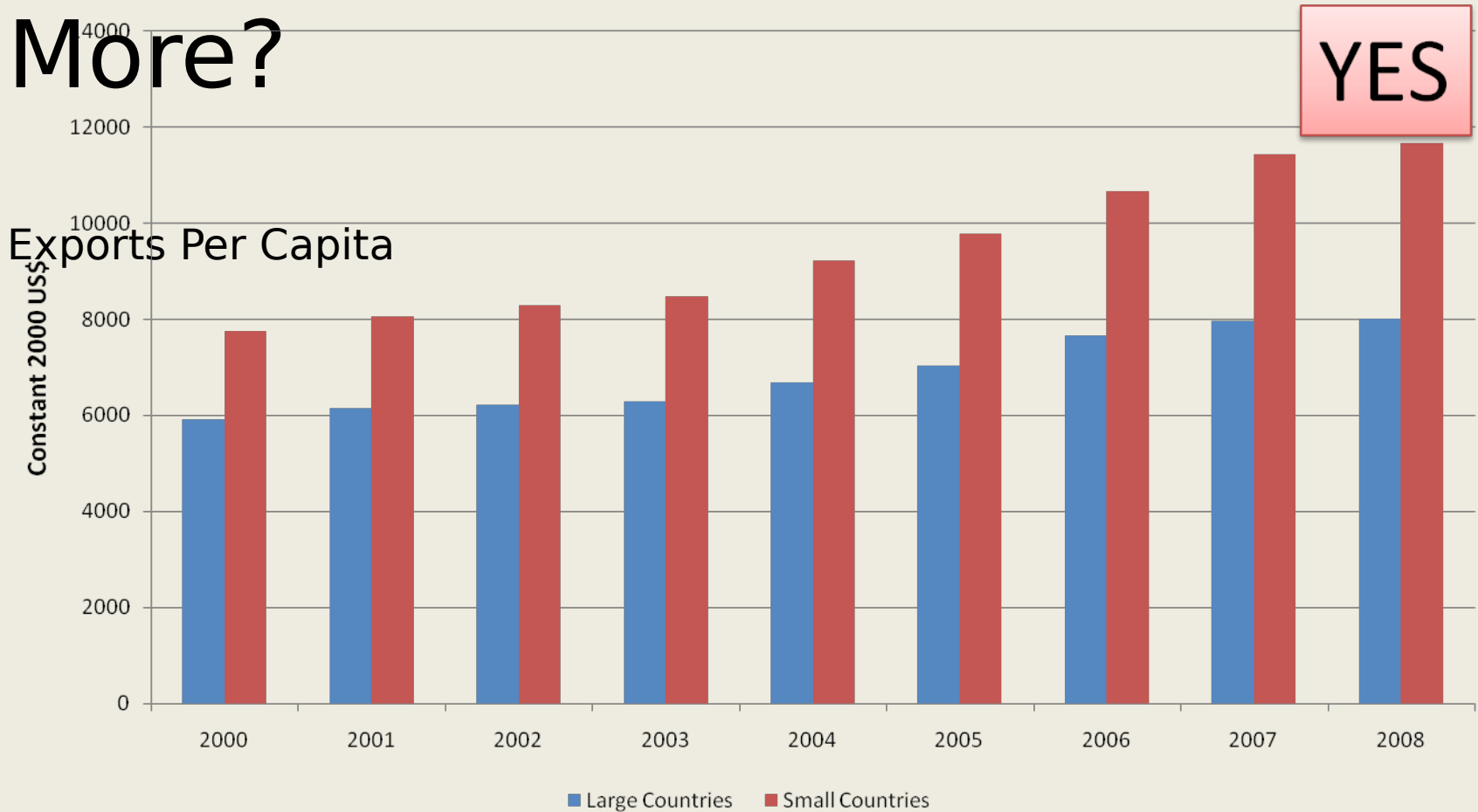


# Have Small Countries Gained More?

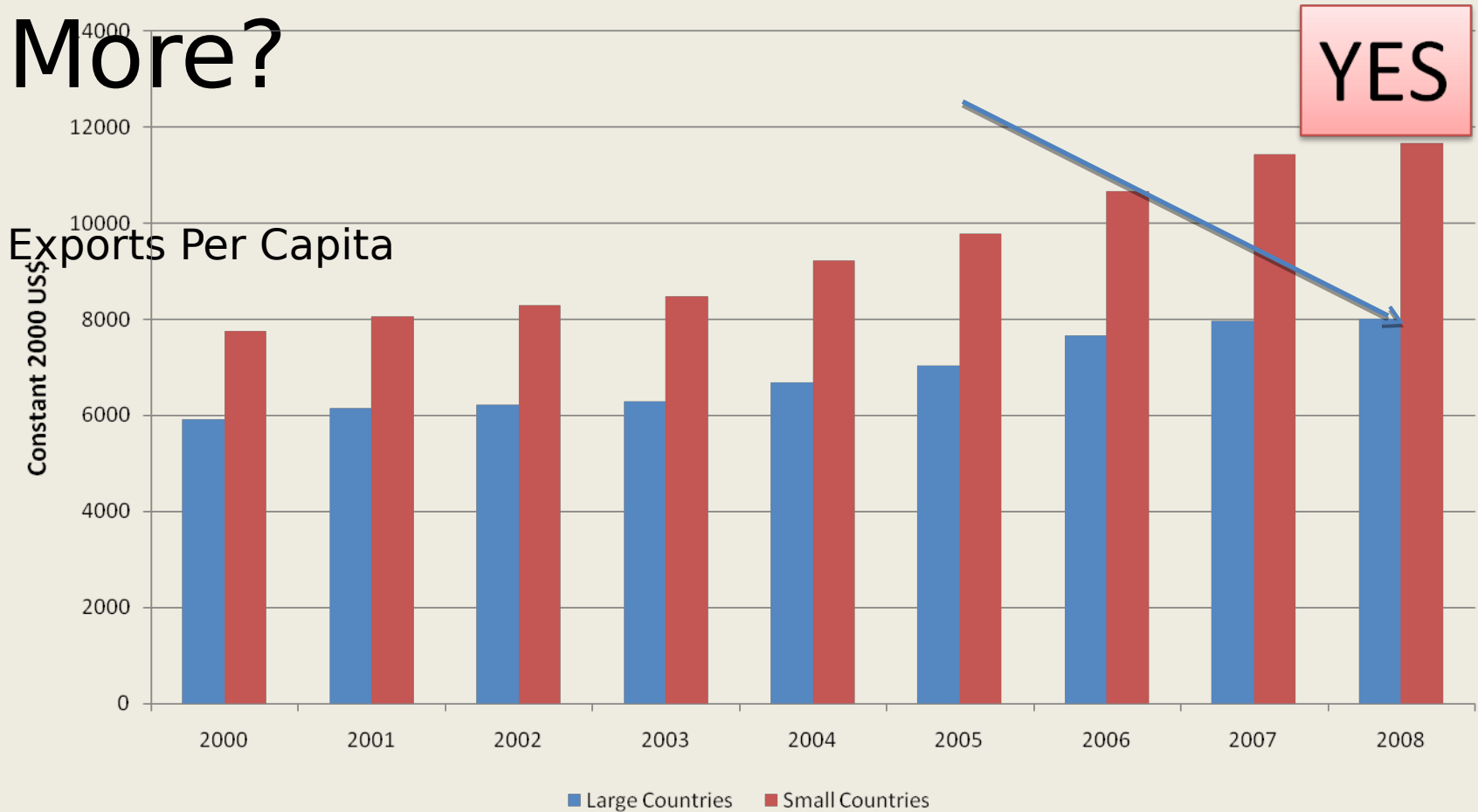




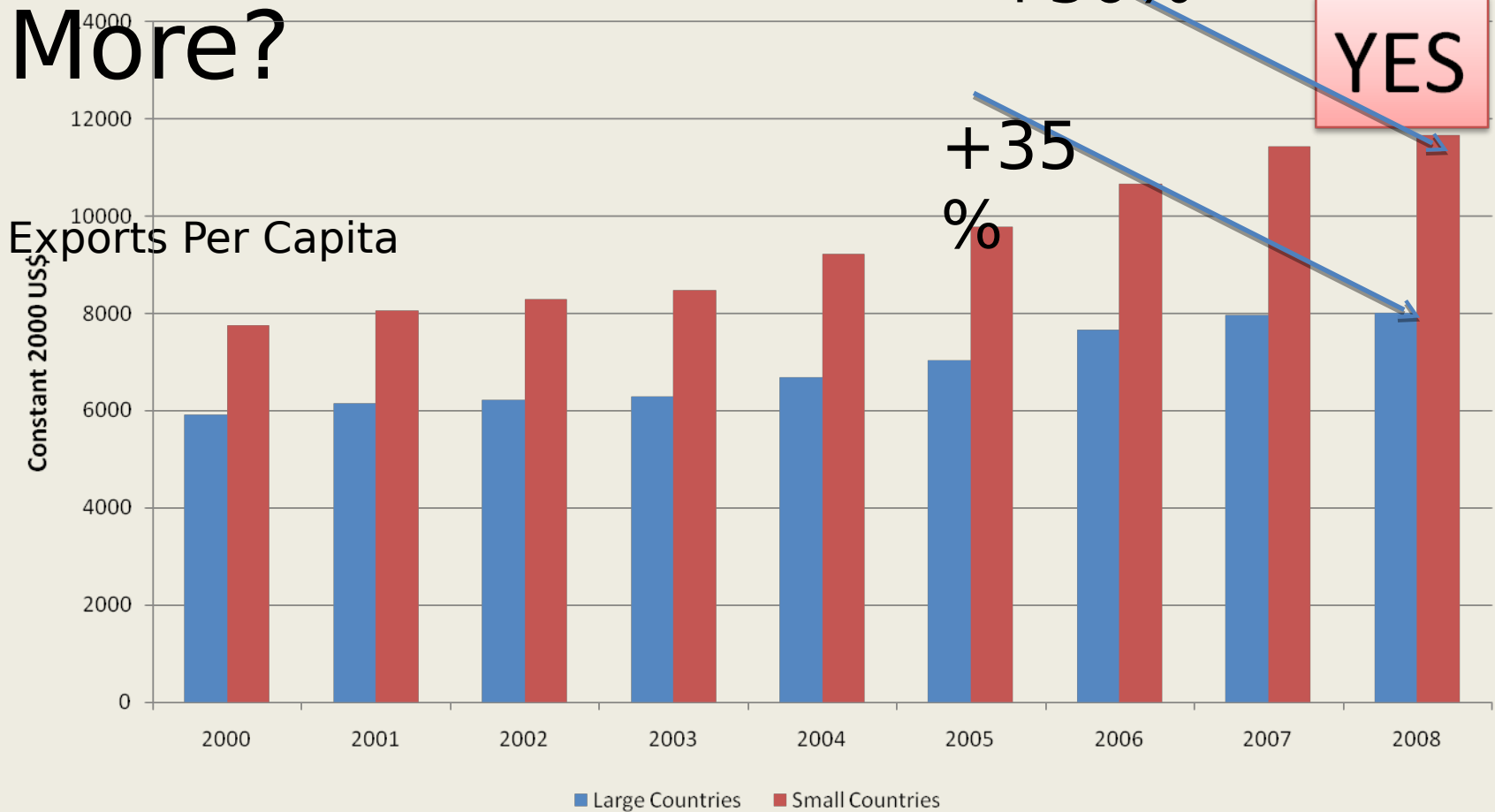
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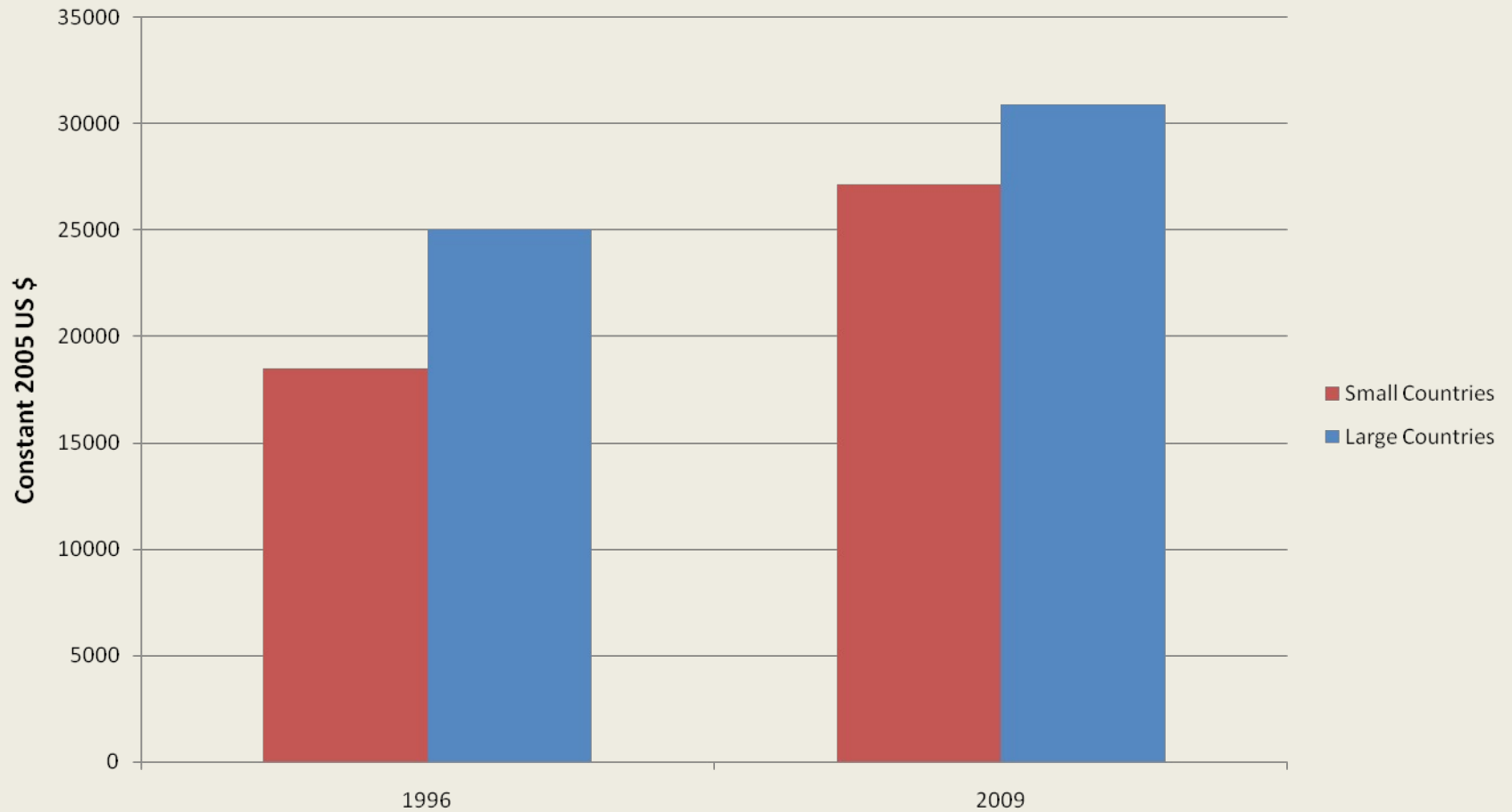
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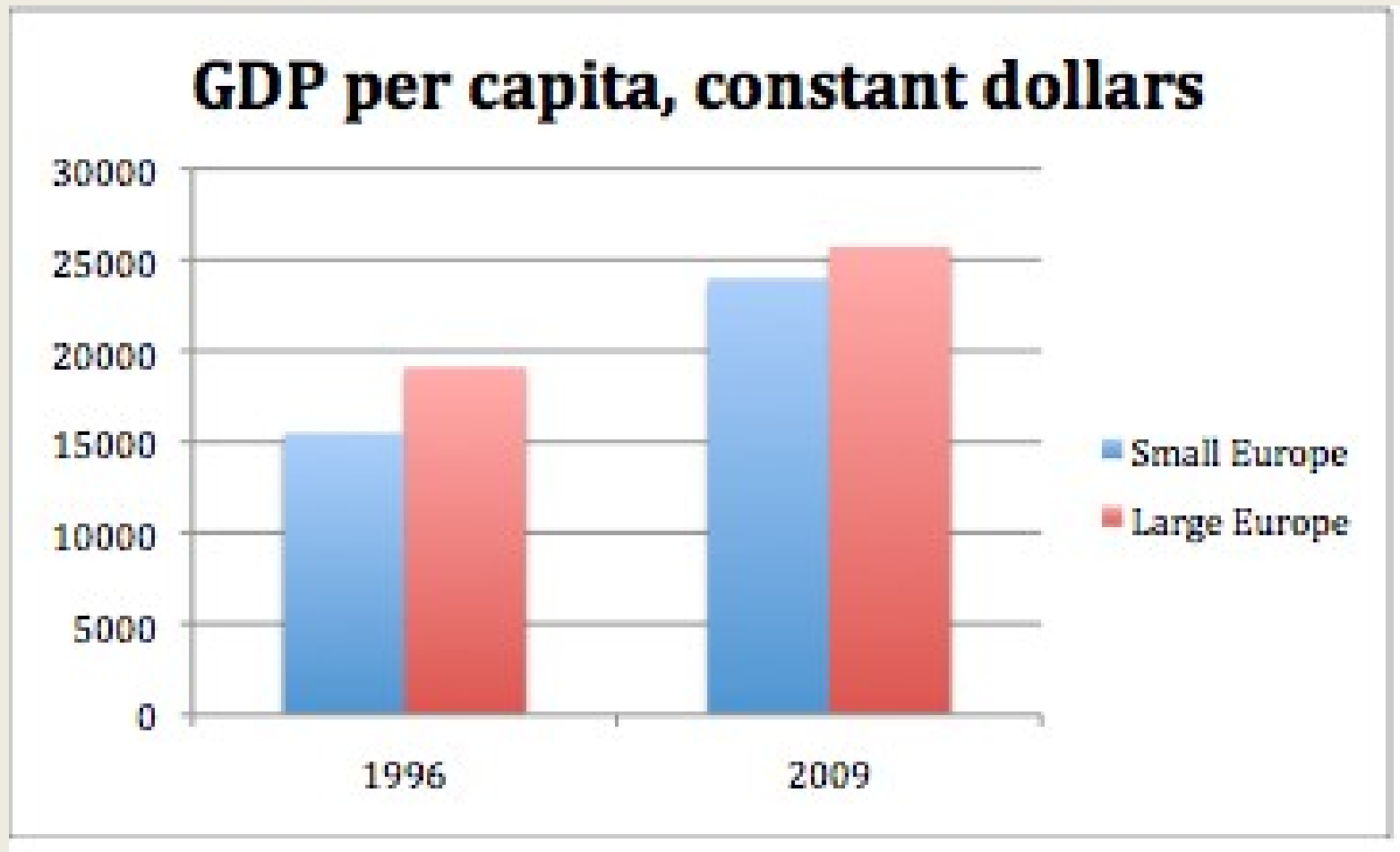
# Have Small Countries Gained More?



# Trade bonus → Growth bonus

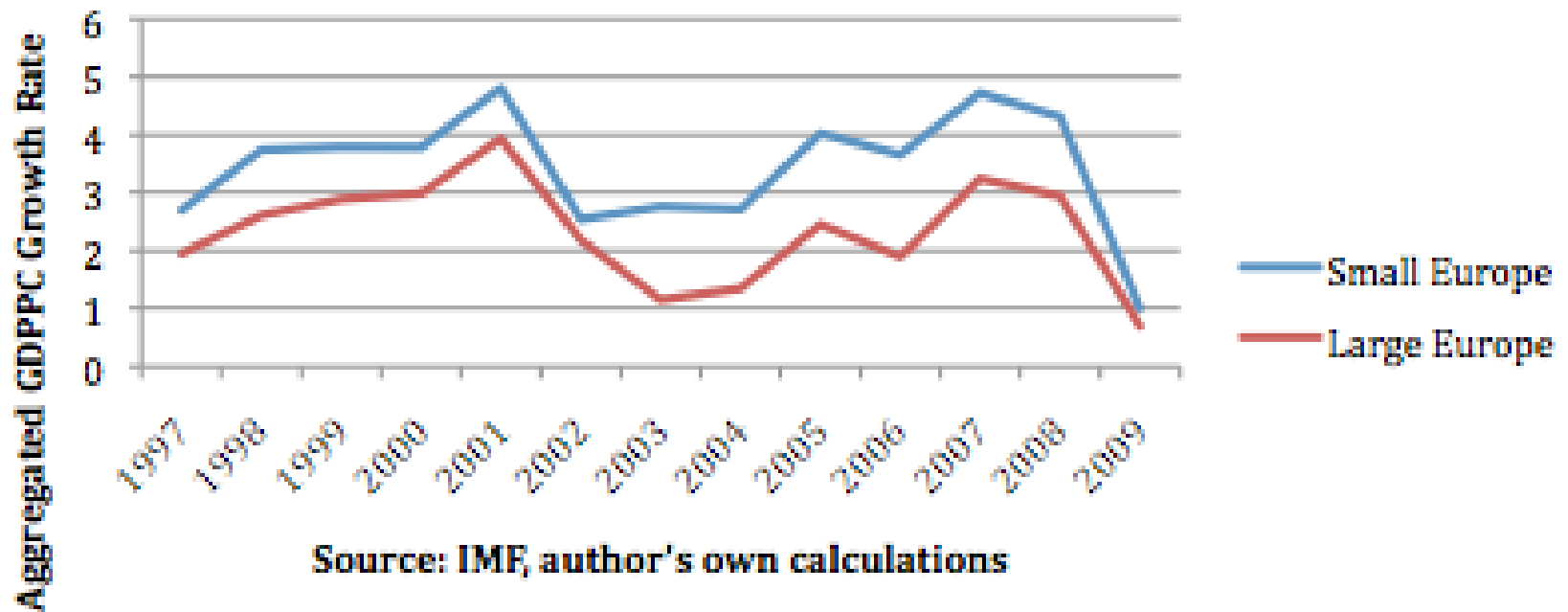


# Small Countries grow faster

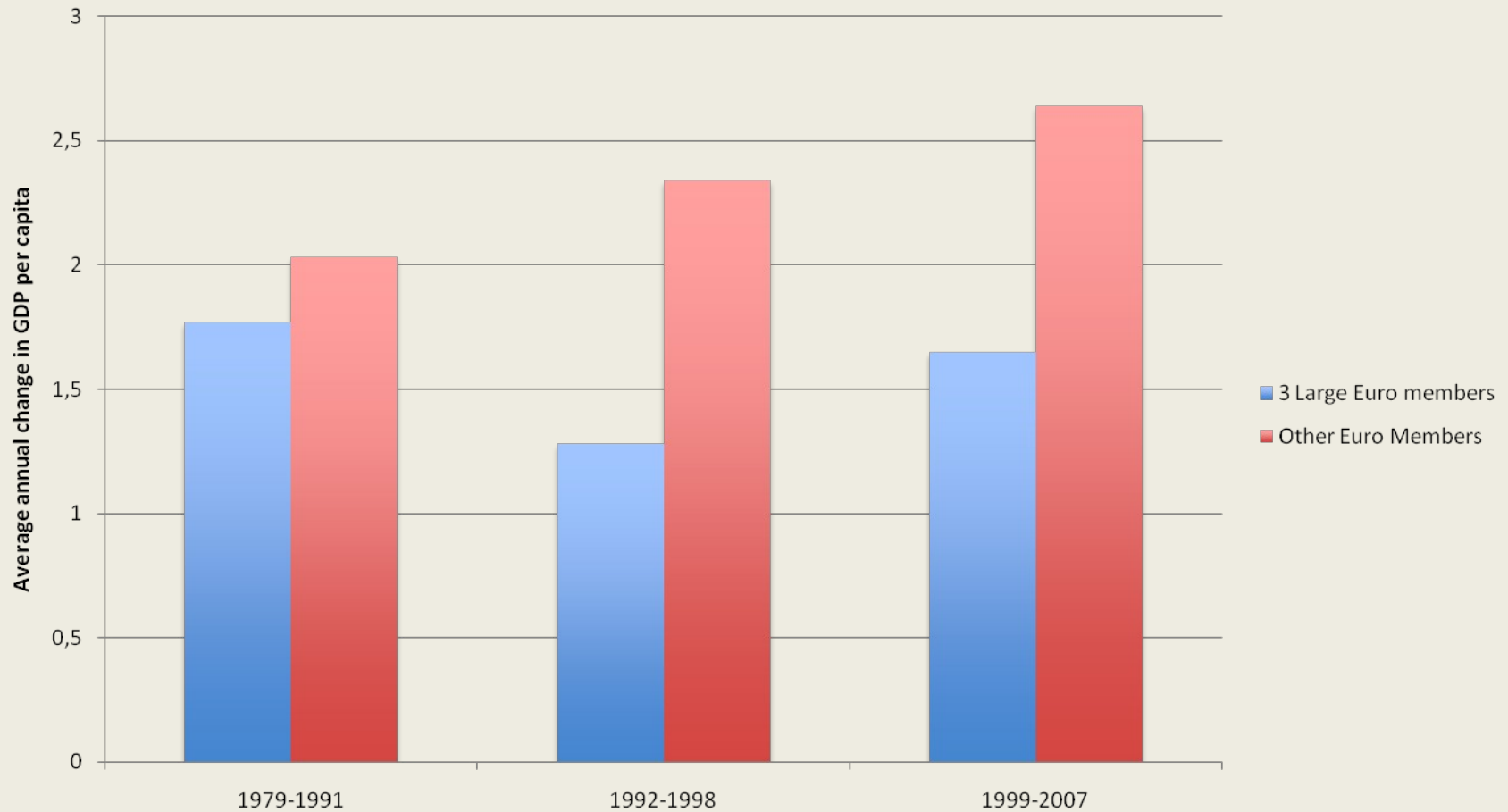


.....consistently

## GDP per capita growth by country size group



# .....and historically



Source: Fitoussi and Laurent,  
2010

It has been argued that as time goes by, the desirability of having smaller nations increases. And the economists who say so are not (I repeat NOT) some crazy Catalan nationalists.....

**XAVIER SALA-I-MARTIN**



Vive La France!

If all nations were small, and none were large, humanity would be freer and happier

**ALEXIS DE TOCQUEVILLE**

Vive La France!!

I love small nations. I love small numbers. The world will be saved the few

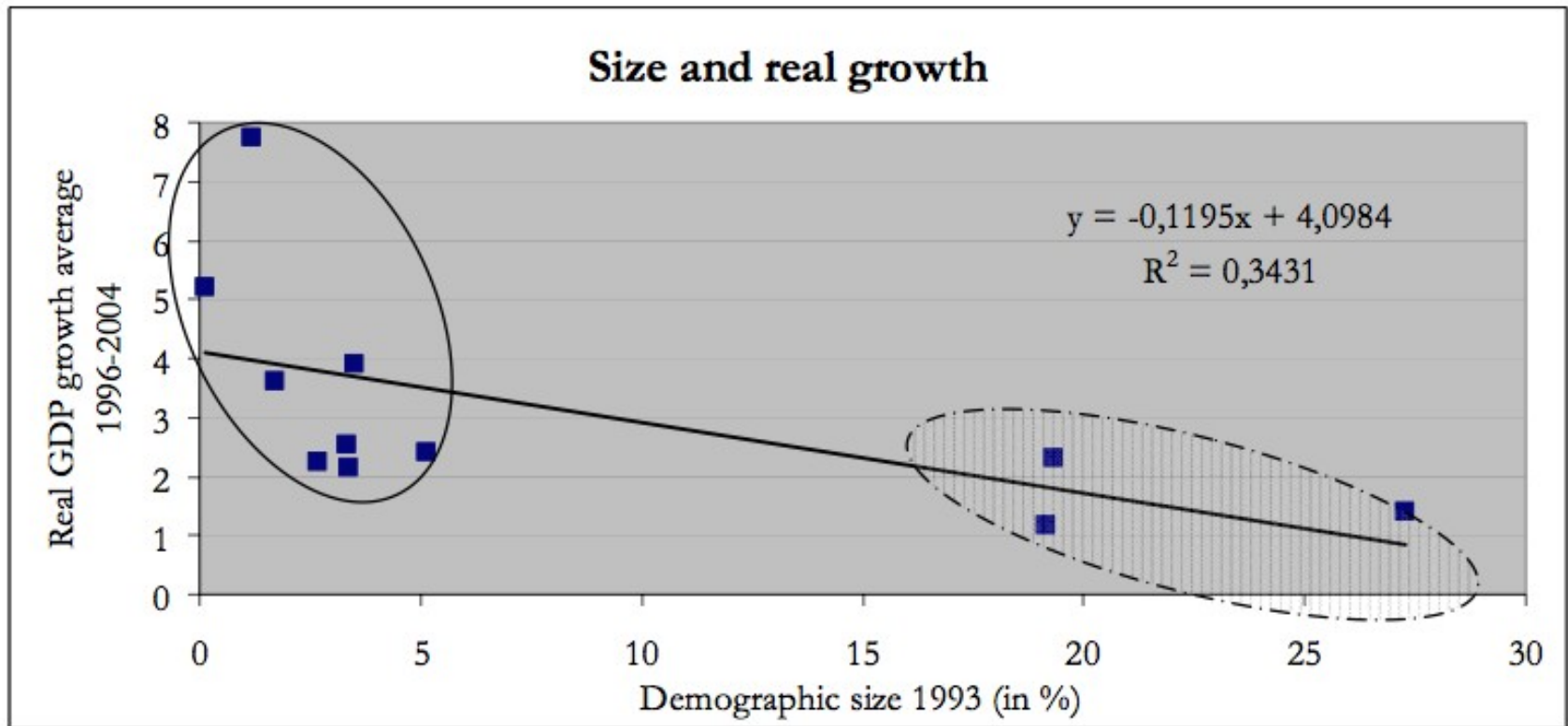
**ANDRÉGIDE**

# Vive La France!!

In quantitative terms we have found evidence of a systematic divergence between small states and large states that amounts to over 2.3% in real growth

**LAURENT ET LE CACHEUX  
(2006)**

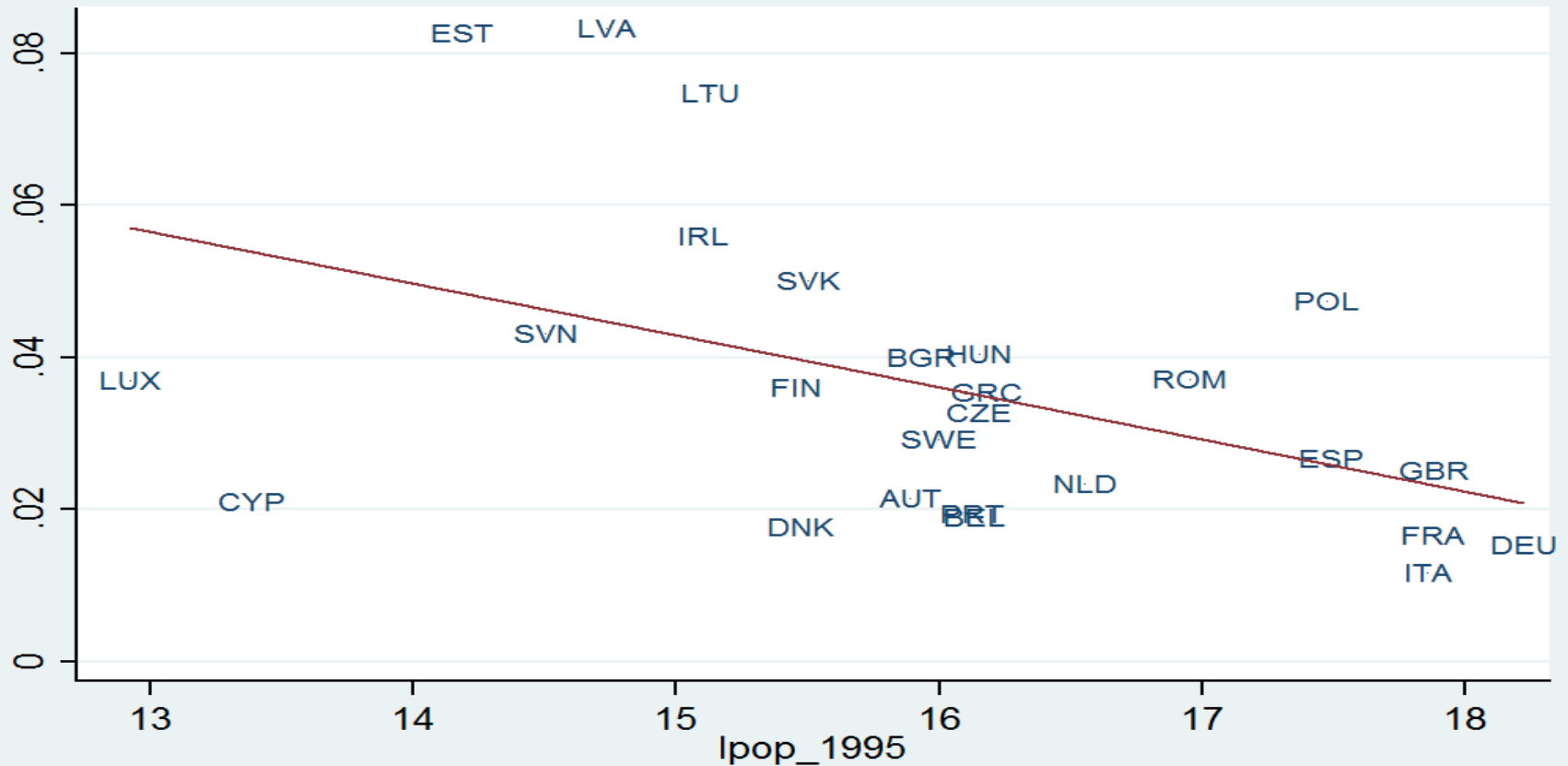
# The Size Nexus a la Sciences-Po



Difference between “small eight” and “big three” = 2.3

Coefficient significant at 5 %.

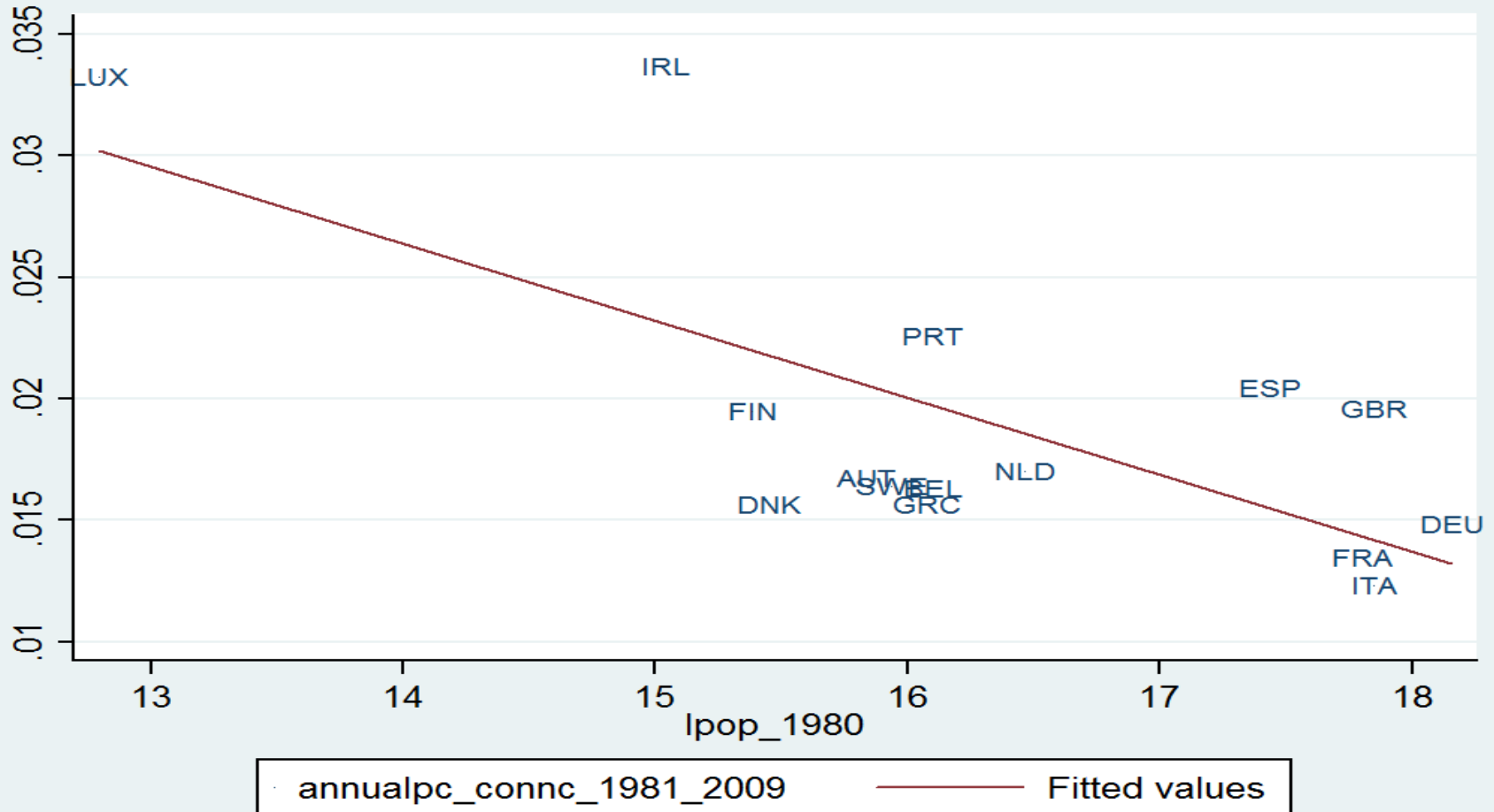
# How important is size to growth?



annualpc\_connc\_1996\_2007

Fitted values

# How important is size to growth?



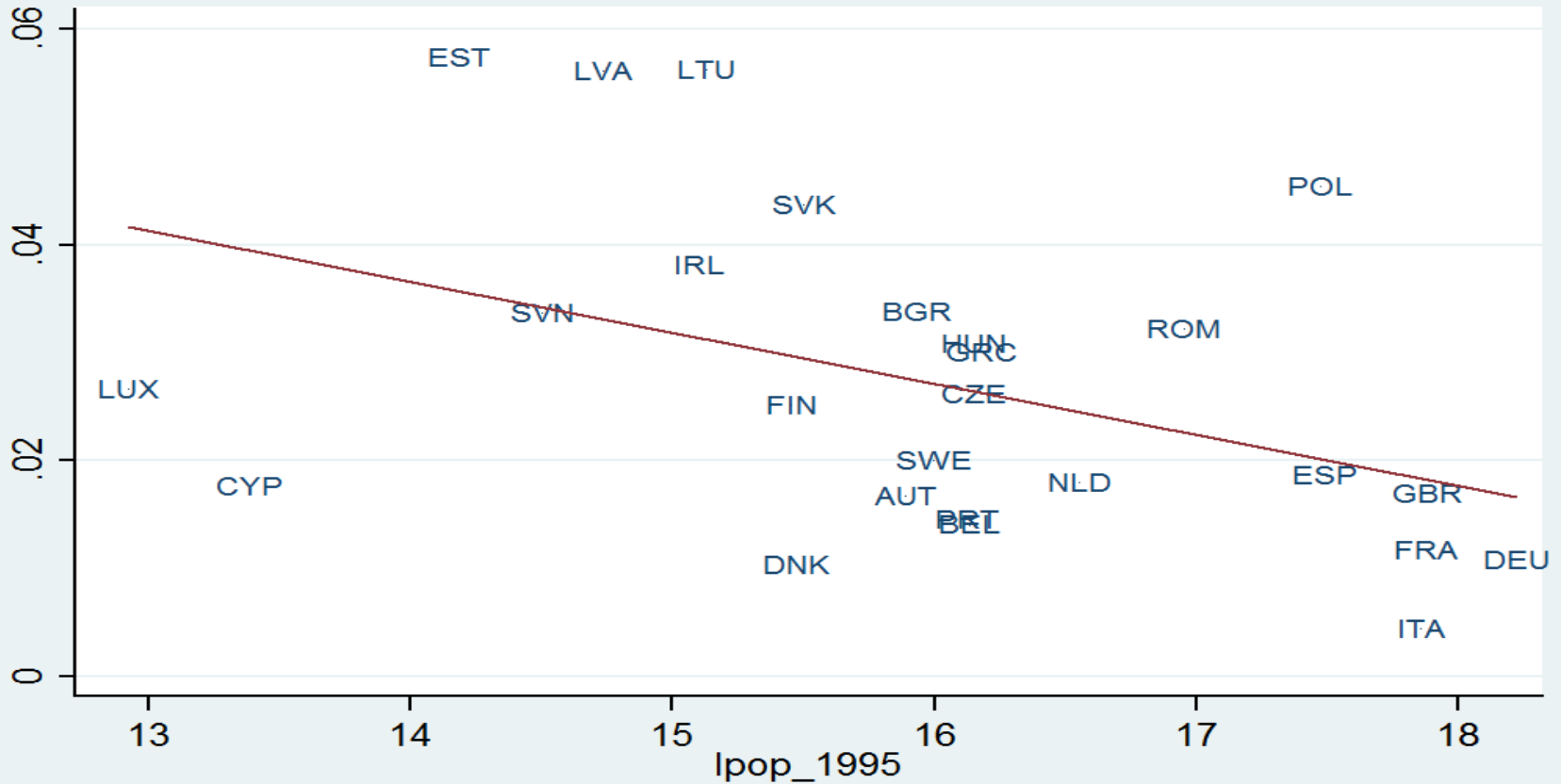
# What we can say...

- Contrary to prevailing of theory and opinion
- Small countries do well in the good times
- ...and no worse in the bad

# Small Countries Lead the World



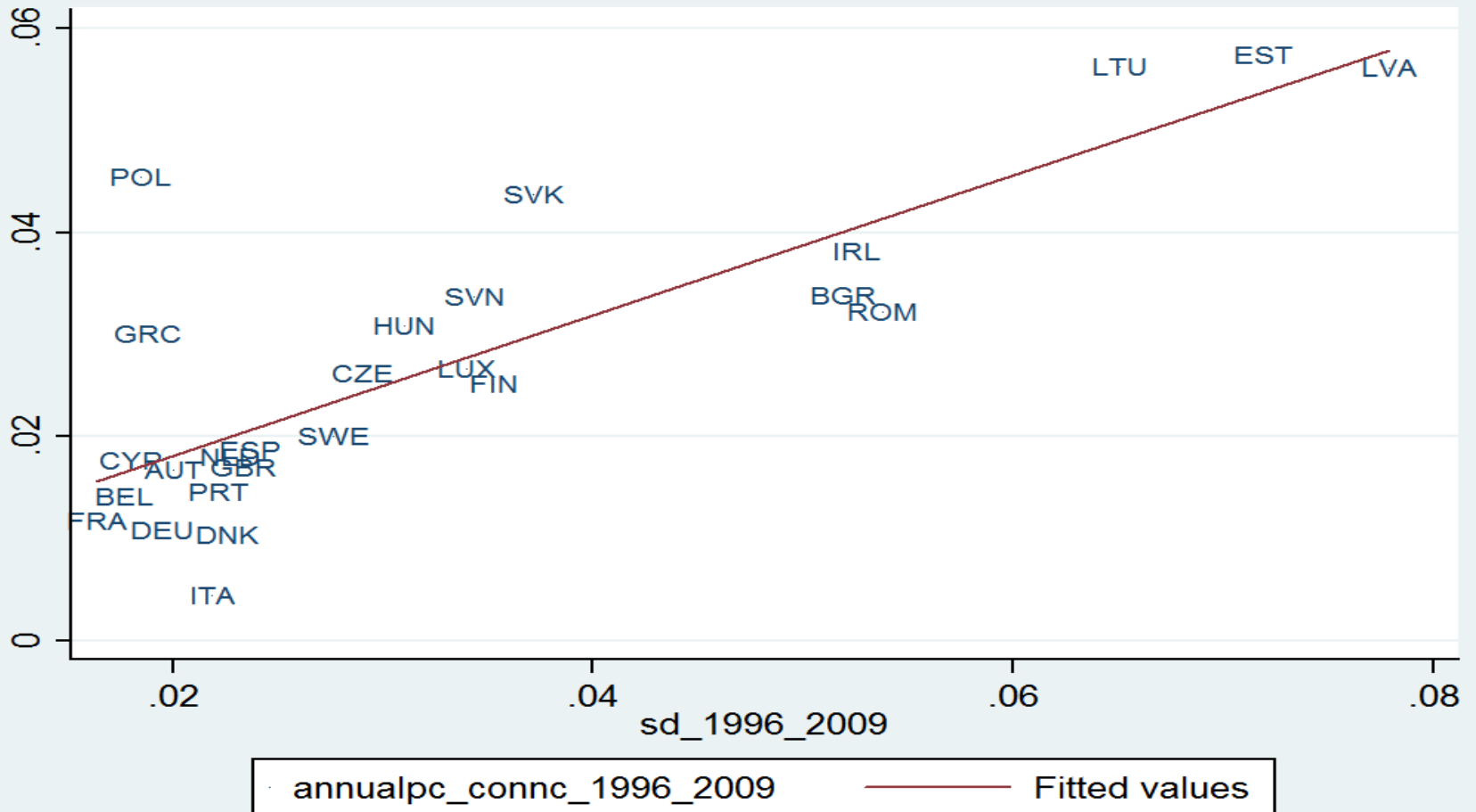
# Small more volatile



annualpc\_connc\_1996\_2009

— Fitted values

# But volatile grow faster



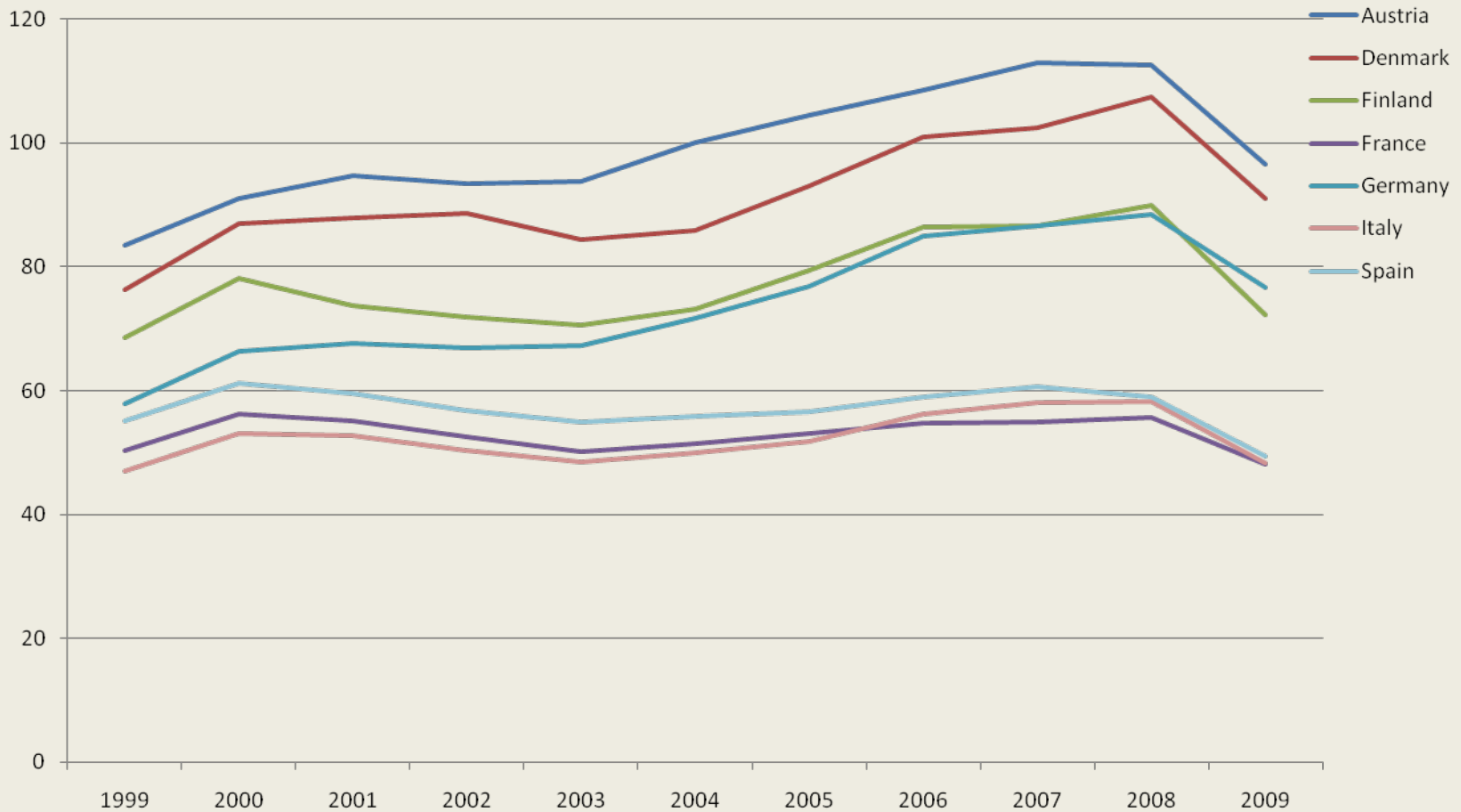
# The Big Advantages of the Small

- Openness to Trade

# Small Nation Stars

Country	Company	Sector	Global 500 ranking
Austria	OMV	Oil and Gas	333
Austria	Erste Group Bank	Banking	466
Austria	Strabag	Construction	486
Belgium	Dexia Group	Banking	49
Belgium	Anheuser-Busch	Brewing	196
Belgium	Delhaize Group	Food retailing	291
Belgium	KBC	Banking and Insurance	361
Belgium	Cie Nationale à Portefeuille	Investment company	482
Denmark	A.P. Møller-Mærsk	Shipping/logistics	147
Denmark	Danske Bank Group	Banking	235
Finland	Nokia	Telecommunications	120
Luxembourg	Arcelor Mittal	Steel	99
Sweden	Volvo	Automotive	278
Sweden	L.M. Ericsson	Telecommunications	301
Sweden	Vattenfall	Energy	303
Sweden	Nordea Bank	Banking	409
Sweden	Skanska	Construction	476

# Strategic lessons: Klein-Staat Deutschland?



Source: OECD, Laurent  
and Le Cacheut, 2010

# The Big Advantages of the Small

- Openness to Trade
- Policy innovation

# Laboratories of Innovation

Country	Policy Innovation
New Zealand	Inflation targeting (1990)
Chile	Private pensions (1990s)
Singapore	Congestion charging (1975)
Sweden	Keynesian demand management (1930s)
Estonia	Flat taxes (1994)
Costa Rica	Abolition of the military (1948)

# The Big Advantages of the Small

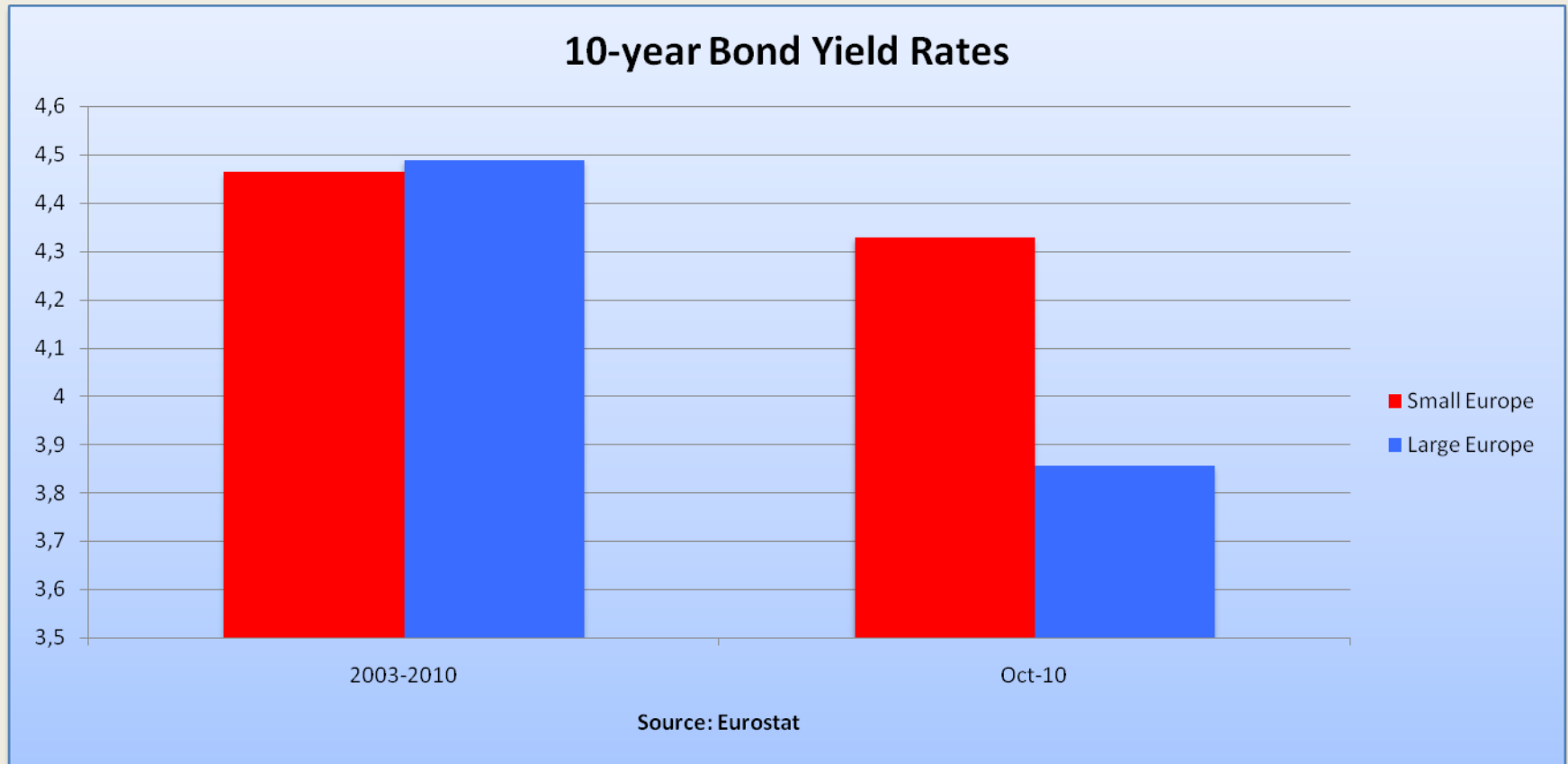
- Openness to Trade
- Policy innovation
- Social Cohesion



# Small country success still searching for a Big Theory

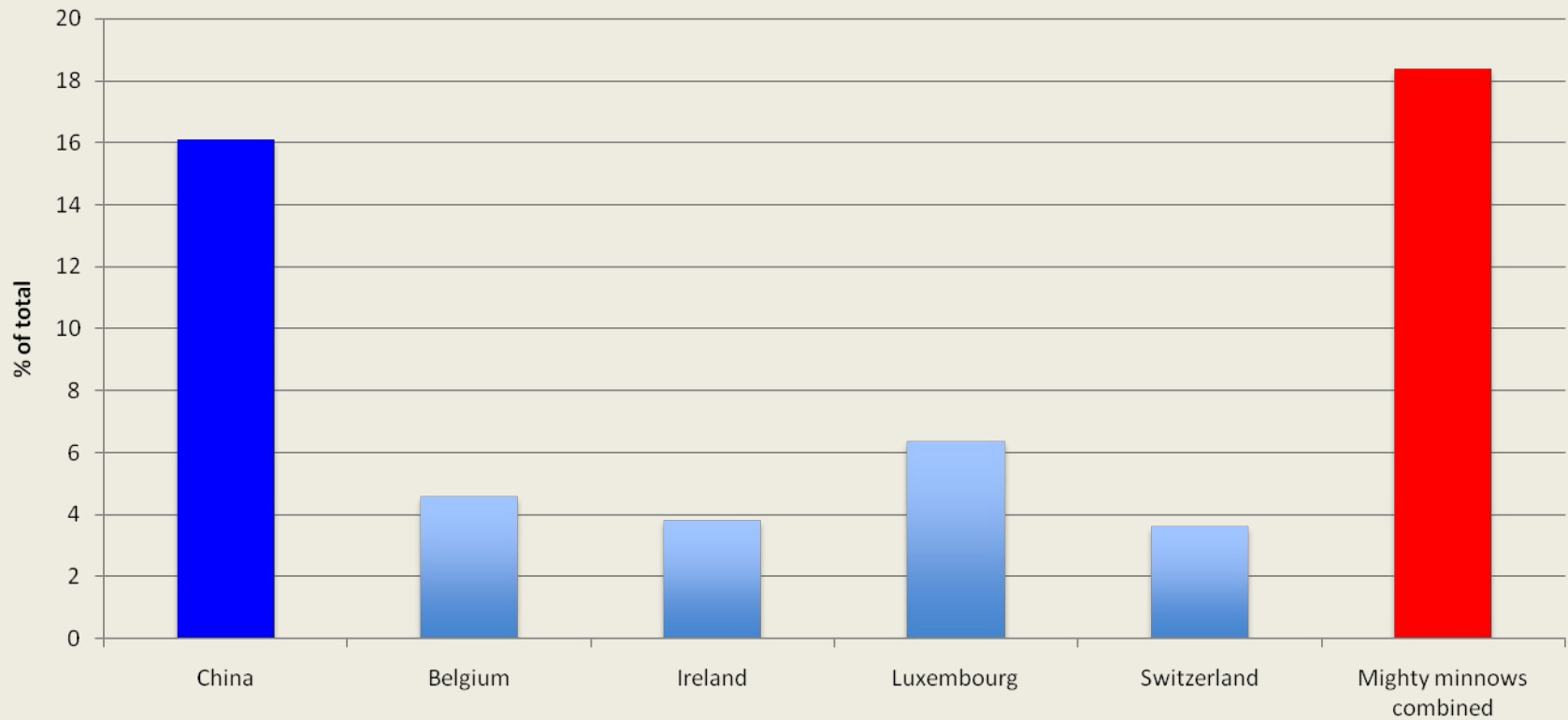
- Kuznets (1960): small nations more cohesive and therefore more adept at responding to technological change
- Katzenstein (1985): small nations better at designing industrial policy
- Alesina and Spolaore, *The Size of Nations* (2005): size matters less in a world of open trade. Diseconomies of scale can flow from heterogeneity.
- Mancur Olson (1965): *The Logic of Collective Action*

# The Costs of Small Size



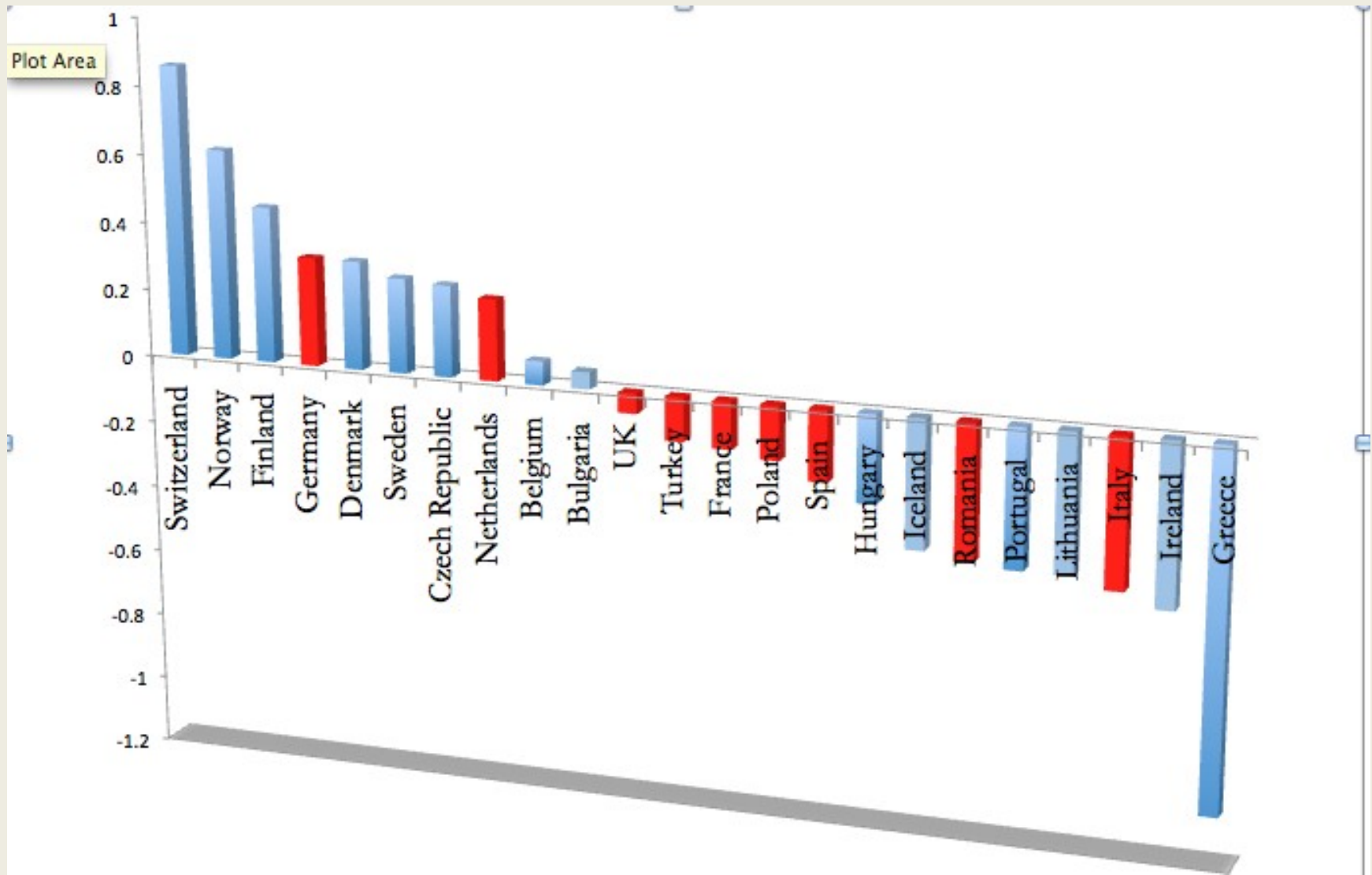
# The mighty minnows

% US LT and ST Debt



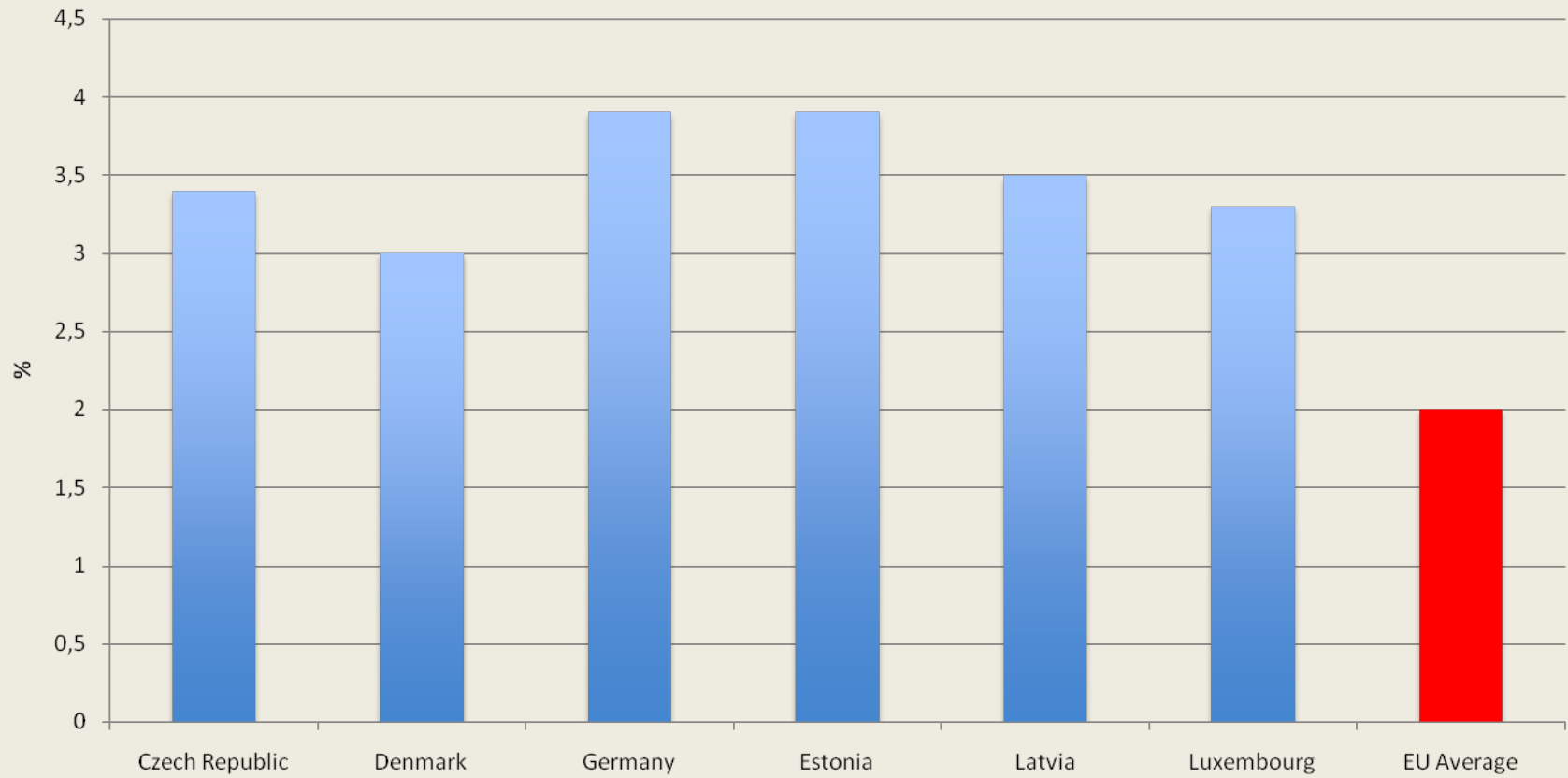
Source: US Treasury Statistics, June 30, 2009

# Fiscal Vulnerability Index

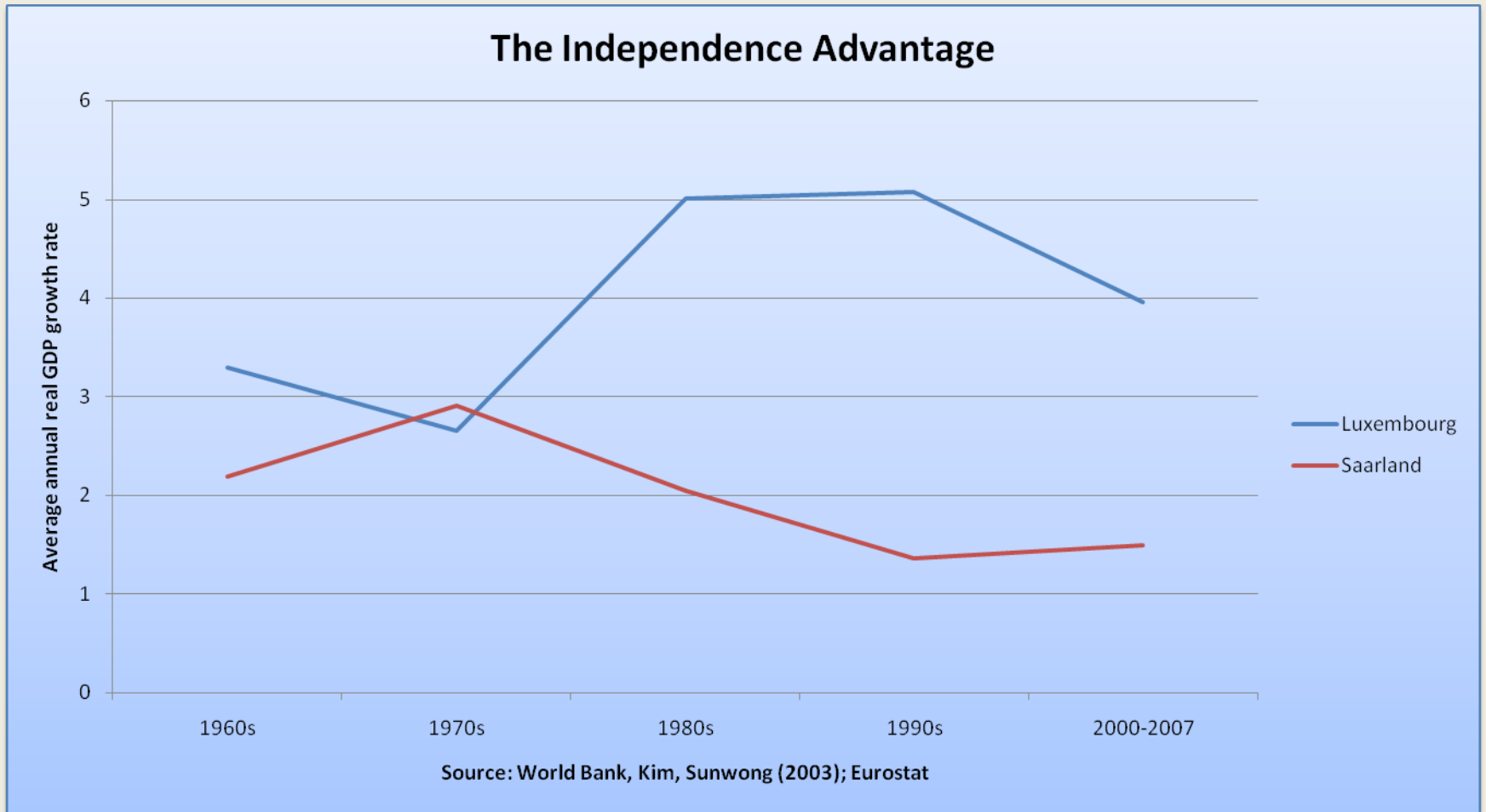


# Bouncing Back

First Three Quarters GDP Growth, 2010

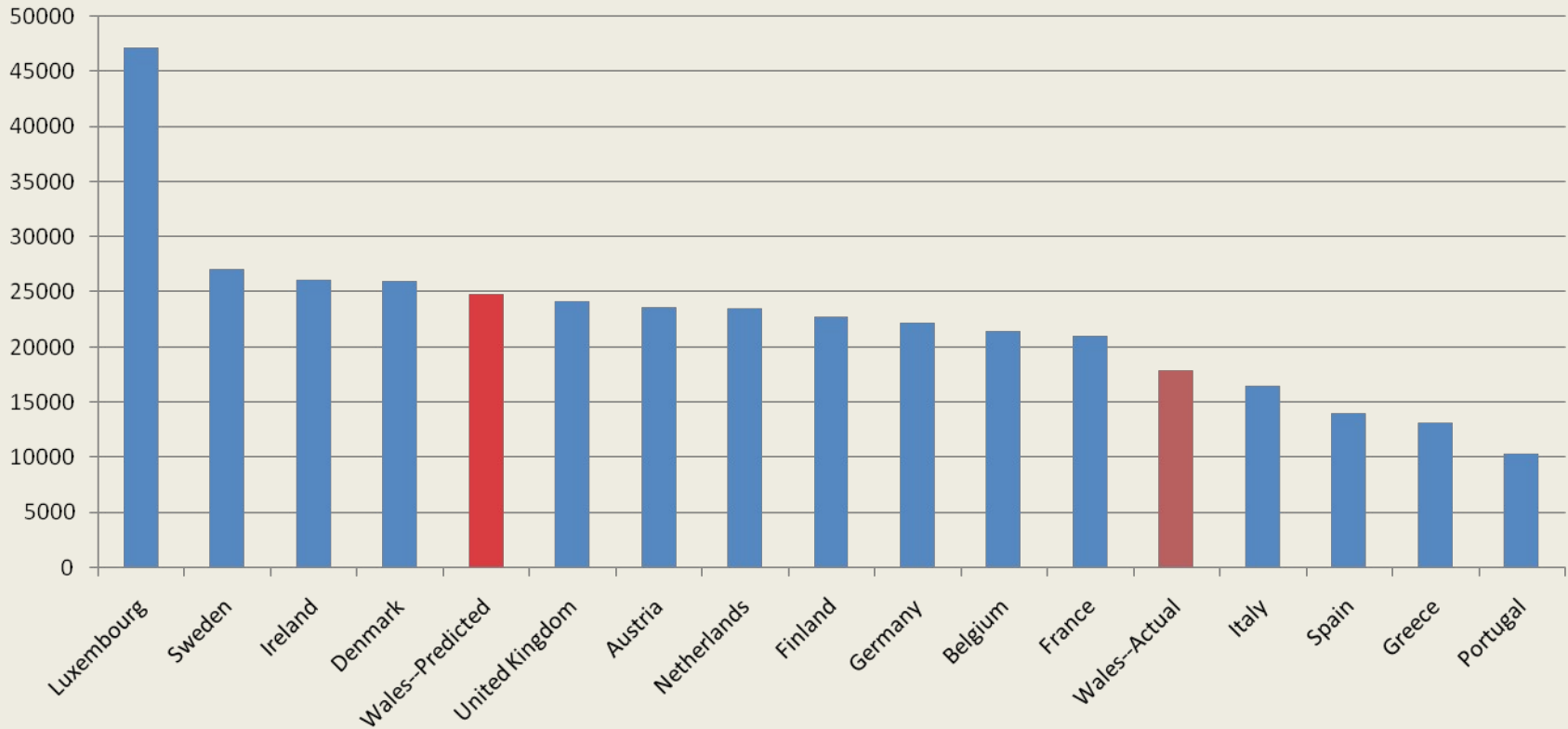


# Saar v. Lux

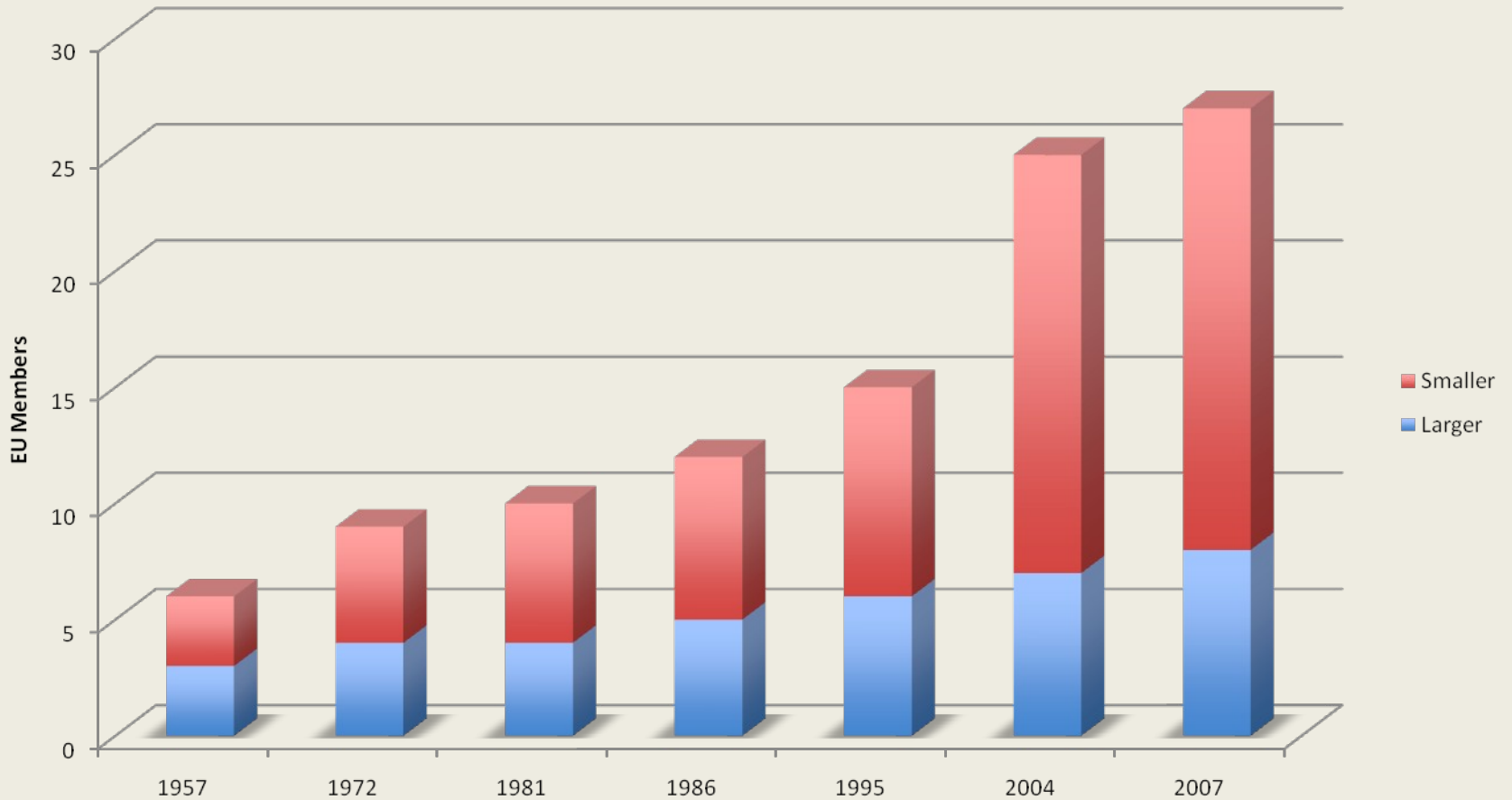


# Wales: the Independence Dividend

2009 GVA per capita (2000 US\$) of EU-15 and Wales (Actual and Predicted from Model)



# Europe: the flotilla





# Euzkadi compared

