

a negative relationship between government consumption (as a proxy for government size) and population (as a proxy for country size), most of the countries should lie on or near the diagonal. As can be easily seen, 83 countries (69% of all countries) are situated in the squares of the diagonal and in the vicinity of it (directly below or above the diagonal).⁴⁵ The simple correlation coefficient between the two variables displayed is -0.345 and significant at the 0.1% level.⁴⁶ Nineteen countries exhibiting low government consumption and few inhabitants (southwest of the diagonal) do not show any obvious pattern.

Conversely, there may be an apparent rationale for those 18 countries northeast of the diagonal, which display relatively high government consumption expenditure. Ten of those 18 are members of the OECD; namely Sweden, Australia, Canada, Poland, the U.K., Spain, Italy, France, Germany and the U.S.A. Moreover, 86% of the OECD members can be found on the diagonal or northeast of it. This suggests that OECD members have significantly higher relative levels of government consumption expenditure and therefore larger governments than other countries of similar size. A non-parametric test reveals that government consumption is indeed higher in OECD countries than in the rest (Mann-Whitney-U-Test; two-sided; $p = 0.003$). The distributions are also significantly different from each other (Kolmogorov-Smirnov-Test; two-sided; $p = 0.011$). We will control for this difference in the regressions by means of a dummy for OECD membership.

It has to be mentioned that we do not intend to address the relationship between trade openness and country size here in greater detail.⁴⁷ Clearly, countries which are more open to trade can more easily «afford» to be small (or to split up) than countries with little trade and bad relations with adjacent countries. The explanation for this is straightforward. The more open a country is, the more it can exploit economies of scale effects and effects due to specialization in the production of private goods. It simply follows the rule of comparative advantage and produces whatever it can sell on world markets.⁴⁸

⁴⁵ Countries outside of this area are printed in capital letters.

⁴⁶ Because of the right-skewedness of the distribution of «population», its logarithm is used.

⁴⁷ See, for instance, Rodrik (1996).

⁴⁸ See Section 3.2.4 for a short discussion on openness.