

that law-making can be viewed as a public good with a consumption obligation, since nobody can be excluded from its consequences and all citizens have to obey the law. The «producers» of laws normally have a territorial monopoly on passing and enforcing laws or similar legal regulations.

5.2 Sources of welfare in VSC

It goes without saying that there are a lot of factors, which play a role in influencing a country's welfare. One might conjecture that a country's endowment in terms of natural resources, its climate and its disaster proneness, the growth and demographical composition of its population, its important institutions, its geographic location, its laws, its religious and ethnic background, its ethnic and linguistic fractionalization, its knowledge base, its political system, and its relationship to adjacent countries, to name but a few, may affect growth and welfare or the living standard of a country. It is, furthermore, obvious that there are a lot of interrelations between the determining factors of welfare. Since we are looking at the welfare issue through the lens of VSC, we are especially interested in the effect of size on welfare, although it seems to be obvious that

so many diverse factors affect the economic well-being of different countries that it is extremely difficult to isolate the factor of size to ascertain its impact upon the dynamic course and prospects of an economy (Vakil, 1960, p. 135).

It has been made clear in the previous section that economic theory deduces an «inferiority» result for VSC, which would imply a negative relationship between country size and welfare, meaning that smaller countries should have lower levels of welfare in general. This section is designed to test for that hypothesis by means of a multiple regression analysis. Note that given the clear theoretical prediction, everything apart from a relatively stable negative relationship between country size and welfare would be a surprise, whereas the stylized facts in the previous section would lead us to conjecture that size and welfare are not interrelated.