

6. A new view on very small countries

This study is designed to provide a better understanding of the public sector organization and its inherent problems in VSC. It dwells upon public expenditure as well as upon institutional choice for the provision of public goods. Based on theoretical predictions and existing empirical analyses of single VSC, we aim at a thorough overview of the constitutive characteristics and peculiarities which are relevant and/or existent in most or all VSC. Furthermore, we study the important impact of public policy on economics in the special context of VSC.

It has been mentioned in the course of the study that economists have not shown a lot of interest in the peculiarities of VSC and their public sectors, although we were able to demonstrate here that VSC are a meaningful unit for economic research. What is even more serious is that many existing theories on VSC and the economic consequences of being small are inconclusive or counter-intuitive. Empirical work on very small countries mainly suffers from data problems, in the sense that a lot of VSC do not provide all necessary data or that data are hard to compare across countries. The situation has been improving gradually, thereby creating more and more possibilities for empirical assessments of VSC problems and peculiarities.

In this study, we nevertheless mainly follow an empirical approach. Although our analysis was also limited by data problems, we arrived at empirical findings that are important for VSC and that challenge the conventional economic wisdom. Before going into the details of the implications of this study on public economic theory and on economic policy of VSC, we briefly summarize the main results:

- We detect a statistically significant size effect, in the sense that smaller countries have larger public sectors. Thus, small countries have to bear a cost disadvantage which may theoretically be traced back