

# **The Political Economy of National Borders**

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**Workshop on**

***Country Size and Border Effects in a Globalised World***

**SIRE and the School of Economics**

**at the University of Edinburgh**

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# Motivation

- The formation and breakup of sovereign states has been at the center of history for thousands of years
- In recent decades, a dramatic increase in the number of independent states and the spreading of demand for autonomy and independence have renewed interest in the redrawing of national borders.
- In 1945 there were 74 independent countries (of which 51 were UN members)
- Today the United Nations has 193 members (latest addition: South Sudan in 2011). The smallest member, Tuvalu, has less than 11,000 inhabitants.

## **For centuries, number and size of nations debated by philosophers and political thinkers**

- Aristotle: “experience has shown that it is difficult, if not impossible, for a populous state to be run by good laws”
- Montesquieu: “in a large republic, the common good is sacrificed to a thousand considerations and is subordinated to exceptions; it is vulnerable to whims and accidents. In a small republic, the public good is more strongly felt, better known, and closer to each citizen.”
- David Hume: “Nothing is more favourable to the rise of politeness and learning than a number of neighboring and independent states, connected together by commerce and policy.”

# More recently, size of nations and endogenous borders addressed by political economists

- Traditionally, economists have studied the economic *implications* of national borders (international economics), but have taken borders themselves as given (exogenous).
- A more recent economic literature has focused on the *endogenous* formation and breakup of national states and political unions.
- The literature on endogenous national borders studies the interactions of economic and non-economic (political, ethnic, cultural) variables in the formation and breakup of national states, using the theoretical and empirical tools of economic analysis
- It is part of a broader trend towards studying the deeper historical and cultural determinants of economic and political outcomes and institutions

# Goals of this talk

- Review some key concepts and results on the political economy of national borders
- Discuss a few open research questions
- Sketch the implications of the analysis for Scotland

# Main References

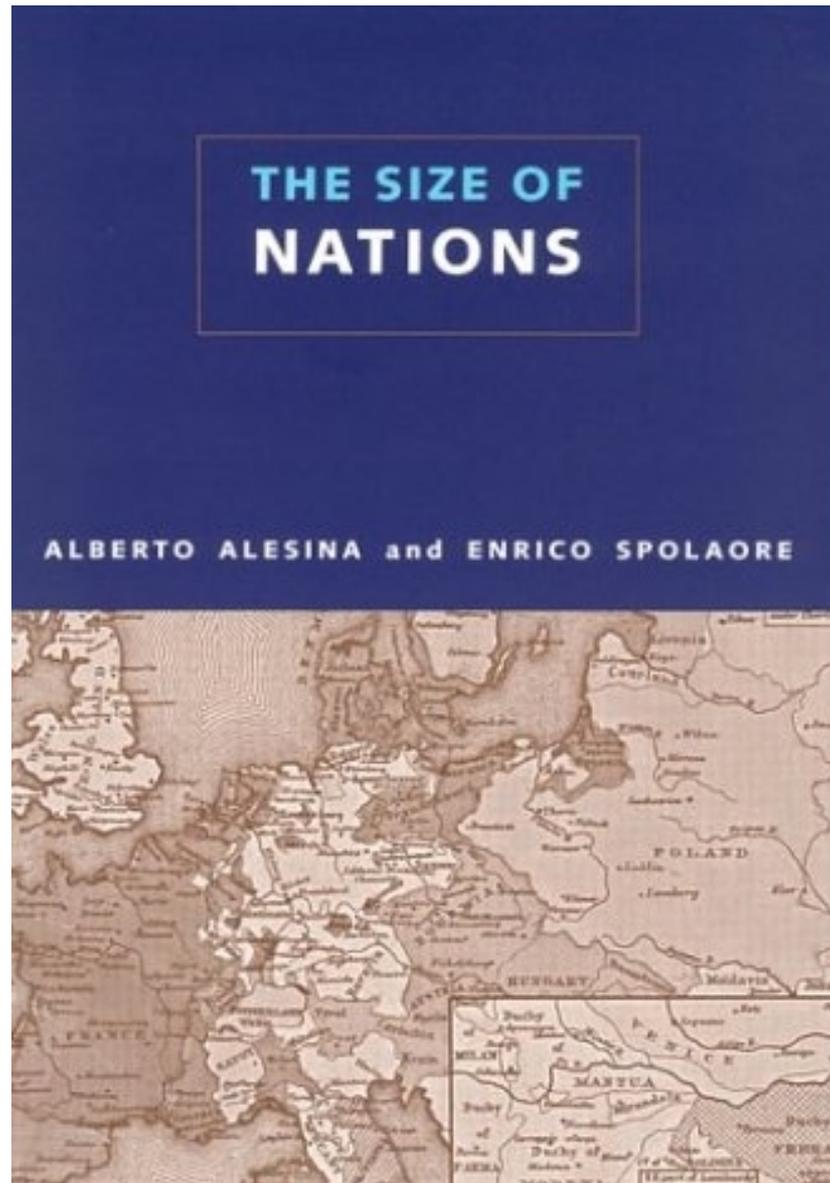
## “The Economics of Political Borders”

prepared for the *Handbook on the Economics of Public International Law*, edited by Eugene Kontorovich, Edward Edgar Publishing (Research Handbooks in Law and Economics series), forthcoming

## “What is European Integration Really About? A Political Guide for Economists”

published in the *Journal of Economic Perspectives*,  
Summer 2013

# commercial break





# Rest of this talk

- The Key Trade-off:
  - Economies of scale vs. heterogeneity costs
- Costs (and benefits) of heterogeneity
- Heterogeneity and conflict within vs. across borders
- The political economy of heterogeneous populations
- The other side of the trade-off: economies of scale
  - defense and security
  - economic integration and political (dis)integration
- Implications for Scotland: in 1707 and in 2014

## A Key Trade-off:

### Economies of Scale vs. Heterogeneity Costs

- **Benefits from a larger size:**
  - economies of scale and scope in the provision of **public goods** (legal system, defense and security)
  - **extent of (domestic) market**, when there are *barriers to international trade*
- but those benefits must be traded against the **costs of heterogeneity**: *different preferences for public goods and policies* in larger, more diverse populations

# Costs and Benefits of Heterogeneity

- Key Distinction: **Public Goods** vs. **Rival Goods**
  - Heterogeneous preferences and traits **negatively** affect the provision of **public goods** - which are **non-rival** in consumption and must be shared by all within a jurisdiction whether one likes them or not
  - In contrast, diversity across individuals and groups comes with **benefits** when considering interactions about **rival** goods

# Important Implications for the Relation between Heterogeneity and Conflict

- **Conflict over public goods** is higher among individuals and groups which are **more different** from each other (higher heterogeneity associated with more conflict)
- **Conflict over rival goods** is higher among individuals and groups that are **more similar** to each other

# Empirical Evidence

## 1) Conflict within borders associated with more heterogeneity

- ***More heterogeneous societies*** more likely to engage in **civil and ethnic conflict** (intrastate conflict), which tends to be over control of **public goods** (government)
  - Montalvo and Reynal-Queirol (2005) and Esteban, Joan, Mayoral and Ray (2012): *ethnolinguistic polarization and ethnic conflict*
  - Desmet, Ortuño-Ortín and Wacziarg (2012): *linguistic cleavages and civil conflict*
  - Arbatli, Ashraf and Galor (2013): *genetic diversity and civil conflict*

# Empirical Evidence

## 2) Conflict across borders is higher among more similar societies

- **International conflict** more likely among states with populations that are *more closely related* (at a smaller *genetic, linguistic, and religious distance*), even after controlling for numerous measures of geographic distance and other factors that affect conflict, including trade and democracy (Spolaore and Wacziarg, “War and Relatedness,” 2012)
- Interpretation: interstate conflict mostly over **rival and excludable goods** (such as **territory** and resources), and hence more likely among states with populations that share more similar preferences, and inherit such preferences with variation from their ancestors.

# Conflict and Endogenous Borders: the contrasting effects of heterogeneity on civil vs. international conflict reinforce each other

- The fact that **more diversity** is associated with **more conflict within borders** is congruent with the fact that **more similar populations** will fight **more** with each other **across borders** to conquer each other's territory, and viceversa.
- Example: consider two types of preferences for public goods: **A** and **B**

# Case 1



- **Low diversity** between each state and the disputed territory – hence, **low probability of within-border conflict** between each state and the people in the disputed territory ex post, when the state is in control of that territory
- Therefore, states 1 and 2 (similar to each other and to the disputed territory) face **high incentives** to go to war *with each other* over territory ex ante.

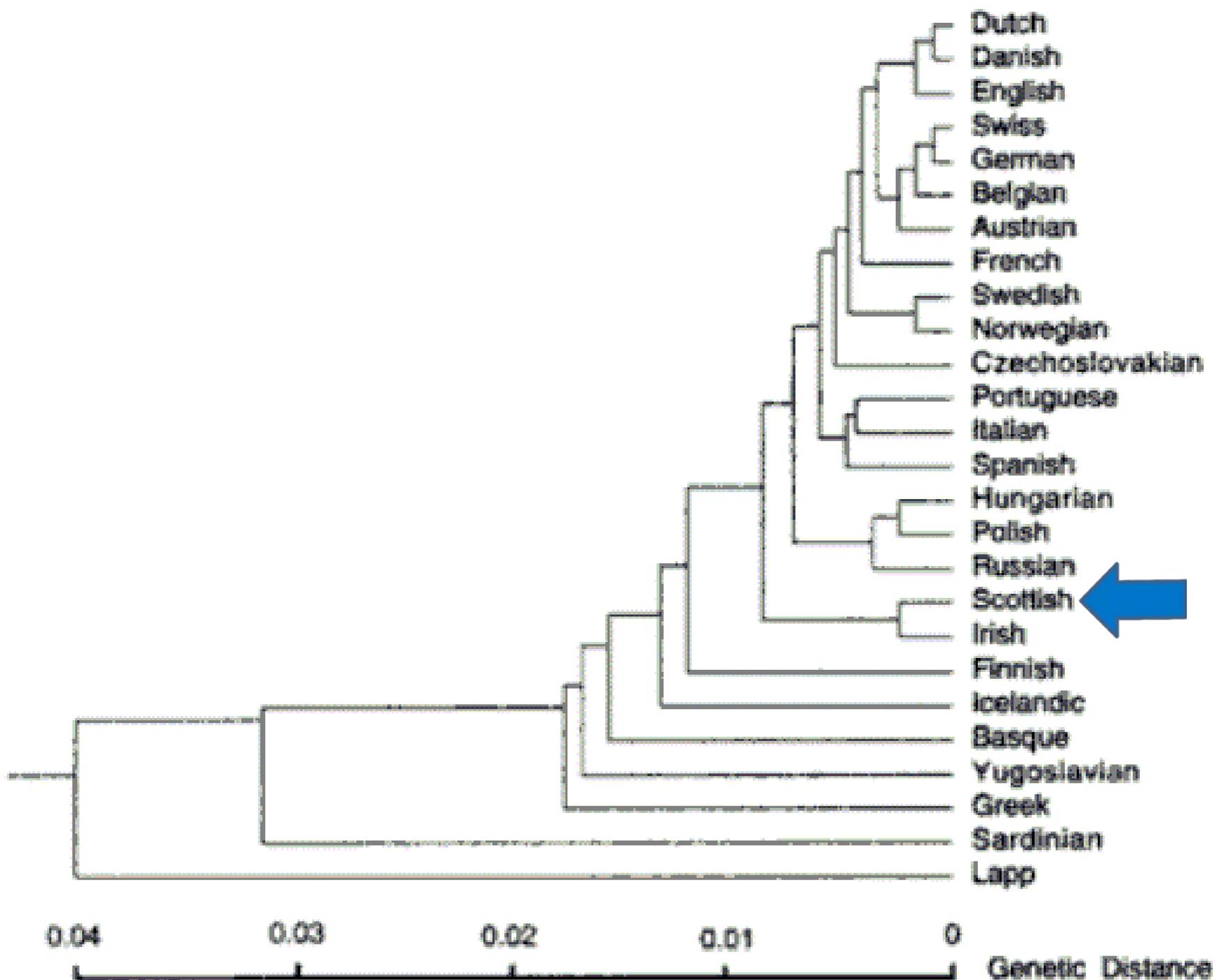
## Case 2



- Low (high) diversity between State 1 (2) and disputed territory – hence, low (high) probability of within-border conflict between State 1 (2) and people in territory if State 1 (2) conquers territory
- States 1 and 2, which are different from each other, face low incentives to go to war with each other over territory – State 1 can take/control territory with much less opposition from State 2.

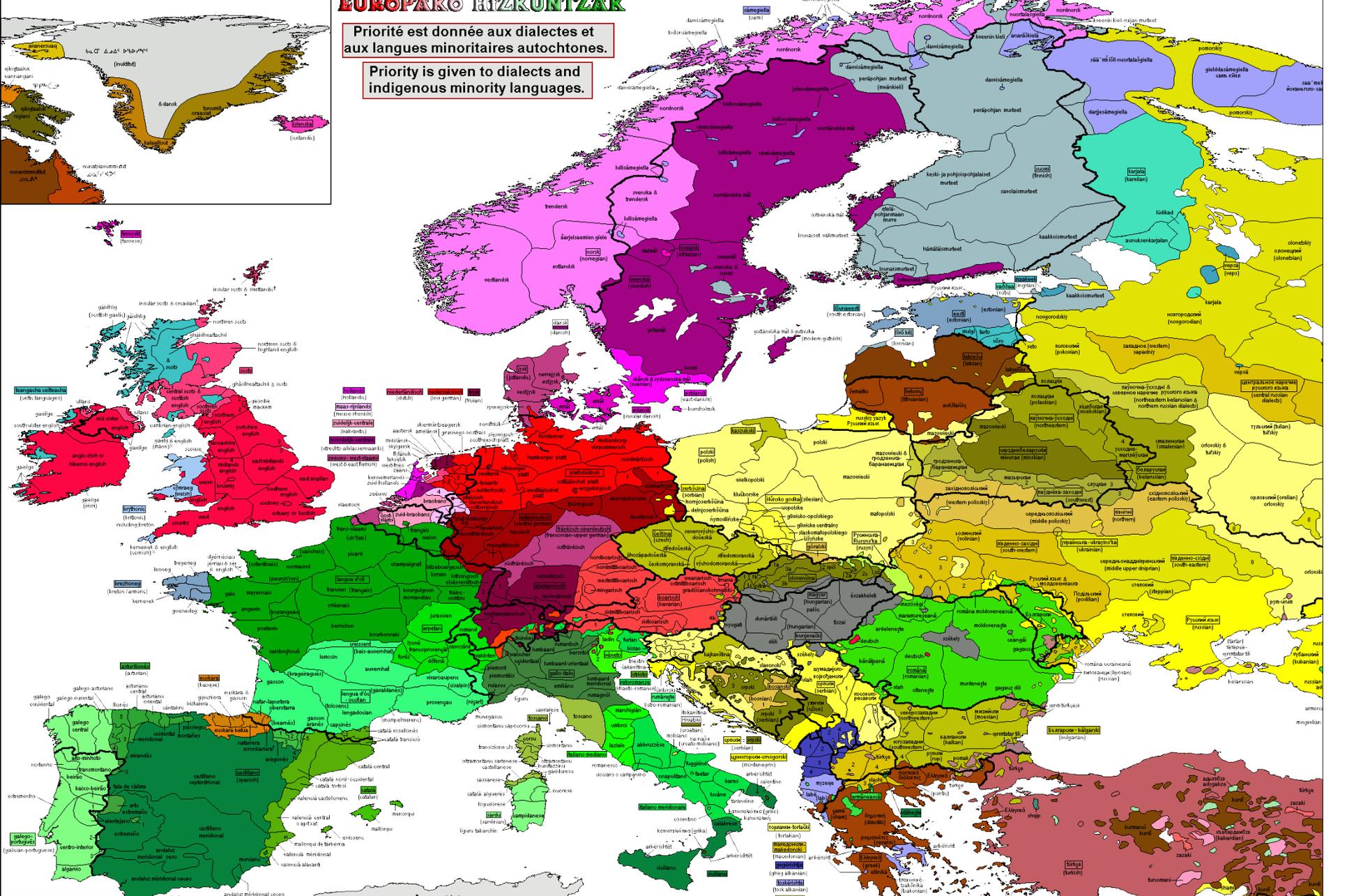
# Research Questions I

- How to measure heterogeneity/distance within and across populations?
  - Ethnolinguistic factionalization and polarization - useful measures, but definitions of groups and their salience may be endogenous
  - Phylogenetic trees based on history of populations, capturing the transmission of inherited traits - e.g., based on genetic distance (using neutral genetic variation) or ancestral cultural distances – such as linguistic distance

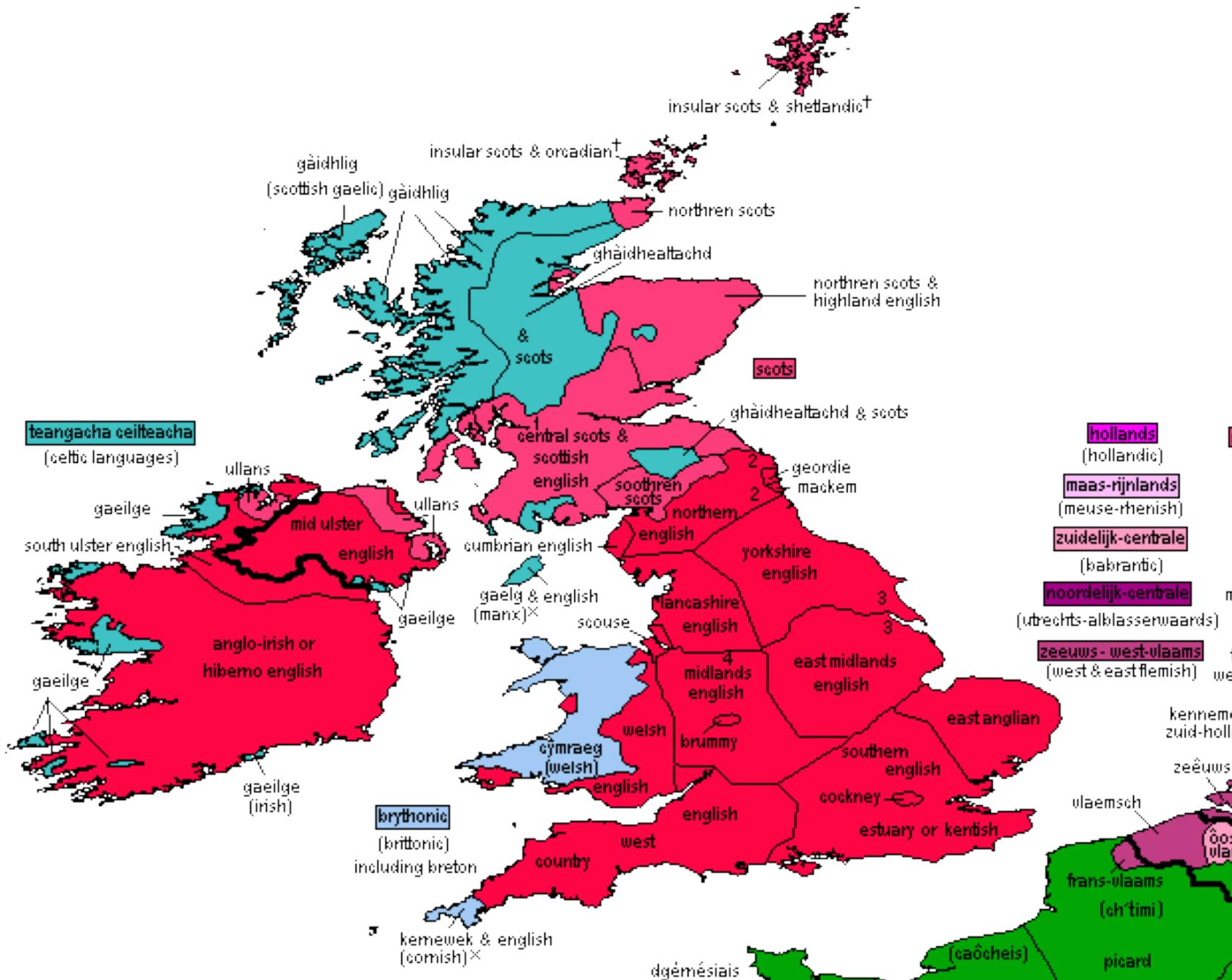


# EUROPAKO HIZKUNTZAK

Priorité est donnée aux dialectes et aux langues minoritaires autochtones.  
 Priority is given to dialects and indigenous minority languages.



INDO-EUROPEAN				ALBANIAN		GREEK	BASQUE	MALTESE	ESKIMO-ALEUT	URALIC	TURKIC	
<b>ITALIC</b> [Color swatches for Italic languages]				<b>GERMANIC</b> [Color swatches for Germanic languages]		<b>CELTIC</b> [Color swatches for Celtic languages]	<b>SLAVIC</b> [Color swatches for Slavic languages]	<b>BALTIC</b> [Color swatches for Baltic languages]	<b>EUSKARA</b> [Color swatch for Basque]	[Color swatches for Maltese and Eskimo-Aleut languages]	[Color swatches for Uralic languages]	[Color swatches for Turkic languages]



**teangacha ceilteacha**  
(celtic languages)

**brythonic**  
(brittonic)  
including breton

**zeeuws - west-vlaams**  
(west & east flemish)

**noordelijk-centrale**  
(utrechts-alklassenwaards)

**maas-rijlands**  
(meuse-rhenish)

**hollands**  
(hollandic)

gaelige  
south ulster english

gaelige

gaelige

anglo-irish or  
hiberno english

gaelige  
(irish)

kernowek & english  
(comish)×

dgemésiais

(saócheis)

frans-vlaams  
(ch'timi)

vlaemsch

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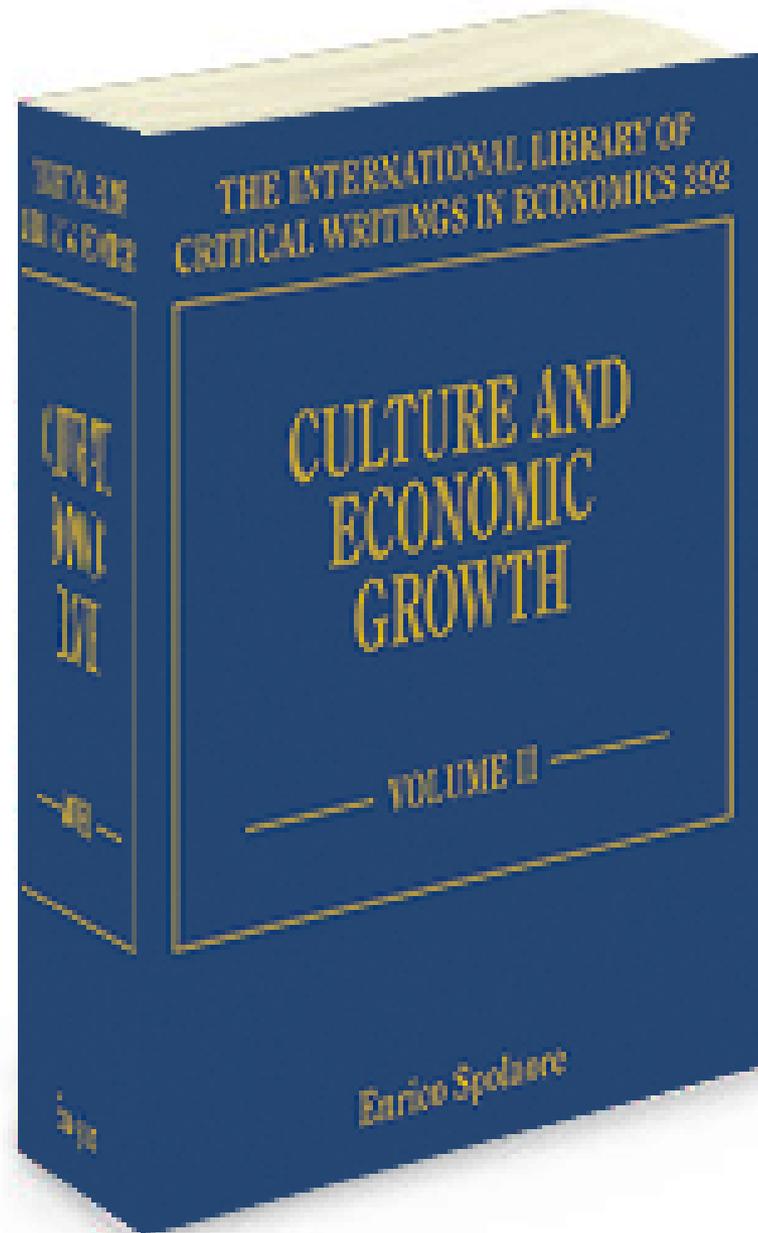
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# Research Questions II

- How do deeper historical and cultural variables affect ***current preferences*** over public goods, policies, and institutions?
- How does heterogeneity of culture and preferences respond ***endogenously*** to ***changes*** in institutions and policies?
- These questions are part of a large and growing literature on culture and economics

# another commercial break



# The Political Economy of Heterogeneous Populations and National Borders

- In general, in political economy what matters is not just aggregate costs and benefits, but their distribution – heterogeneity costs are no exception
- Heterogeneity of preferences has a stronger effect on the number and size of nations when voters *directly* decide national policies and borders (effects of **democratization**)
- Voters “far from the central government” in preferences/culture/identity bear the largest share of heterogeneity costs and, if allowed to vote, will break up an inefficiently large country (Alesina and Spolaore, ch. 3)
- Voters may even break up an efficient country in the absence of optimal *tax and transfers schemes*, which can be unfeasible and/or politically non credible (Alesina and Spolaore, ch. 4).

# Leviathans and Borders

- Rent-maximizing governments (Leviathans) who can ignore heterogeneous preferences of some or most of their subjects – and let “peripheral populations” bear most of the heterogeneity costs - tend to form larger, more centralized states.
- Leviathans concerned about centripetal effects of heterogeneity costs may have an incentive to reduce heterogeneity with policies of cultural and linguistic homogenization, “nation-building,” etc. (Alesina and Spolaore, 2003, chapter 5 – Alesina and Reich, 2013).

# The other side of the trade-off:

## Benefits of scale

- Provision of public goods with large economies of scale - in particular: **defense and security**
- Extent of the **domestic market**

*These benefits depend on the **international economic and political environment**:*

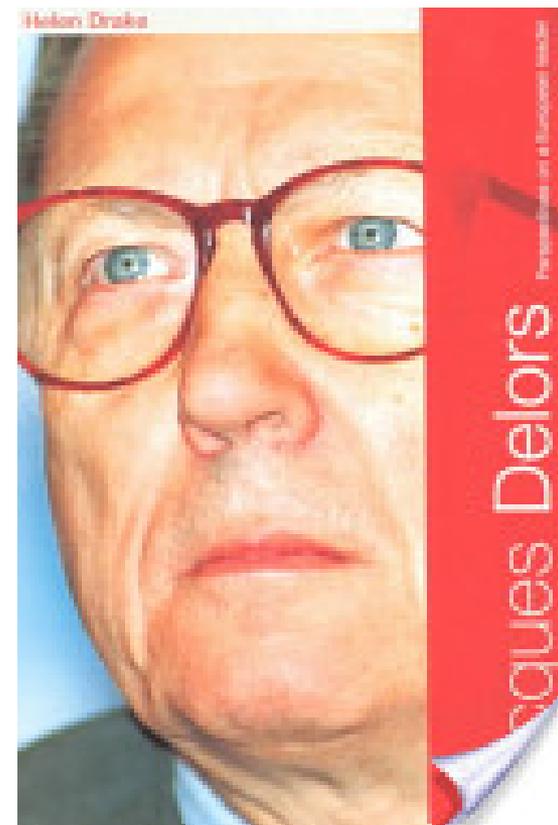
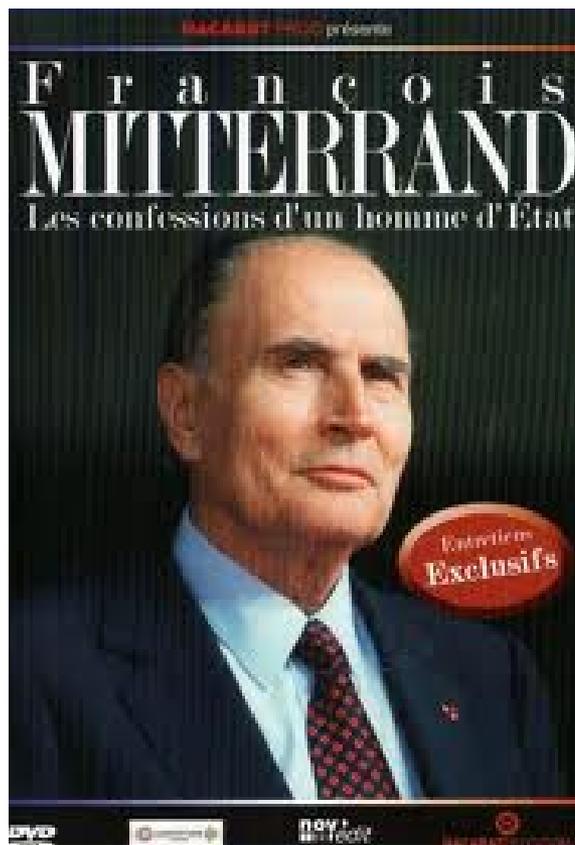
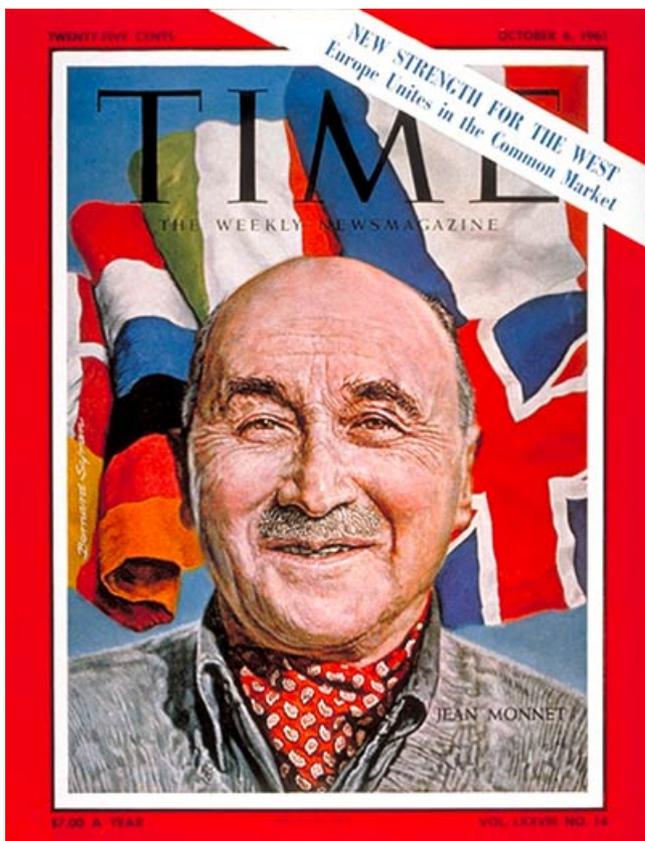
-) They are **higher** in a world of **higher trade barriers, higher international conflict, and weak military alliances**

-) They are **lower** in a world of **lower trade barriers (high economic integration), peaceful international relations, and strong military alliances**

# Economic Integration and Political Integration substitutes or complements?

- The “functionalist” theory of integration is that economic integration across independent countries should lead to political integration among them (for a discussion: Spolaore, 2013)
- However, the example of the German customs union (*Zollverein*) often mentioned in this respect is misleading, because the main force behind commercial integration was political integration pushed by Prussia’s military power (Gilpin, 2001).
- International cooperation among independent countries and political integration (formation of a political union) can be viewed as ***substitute*** ways to lower barriers to trade.
- If two regions can already agree to reduce their trade barriers with each other while remaining independent, they are going to obtain ***smaller*** additional gains from trade if they also form a political union with a unified domestic market.

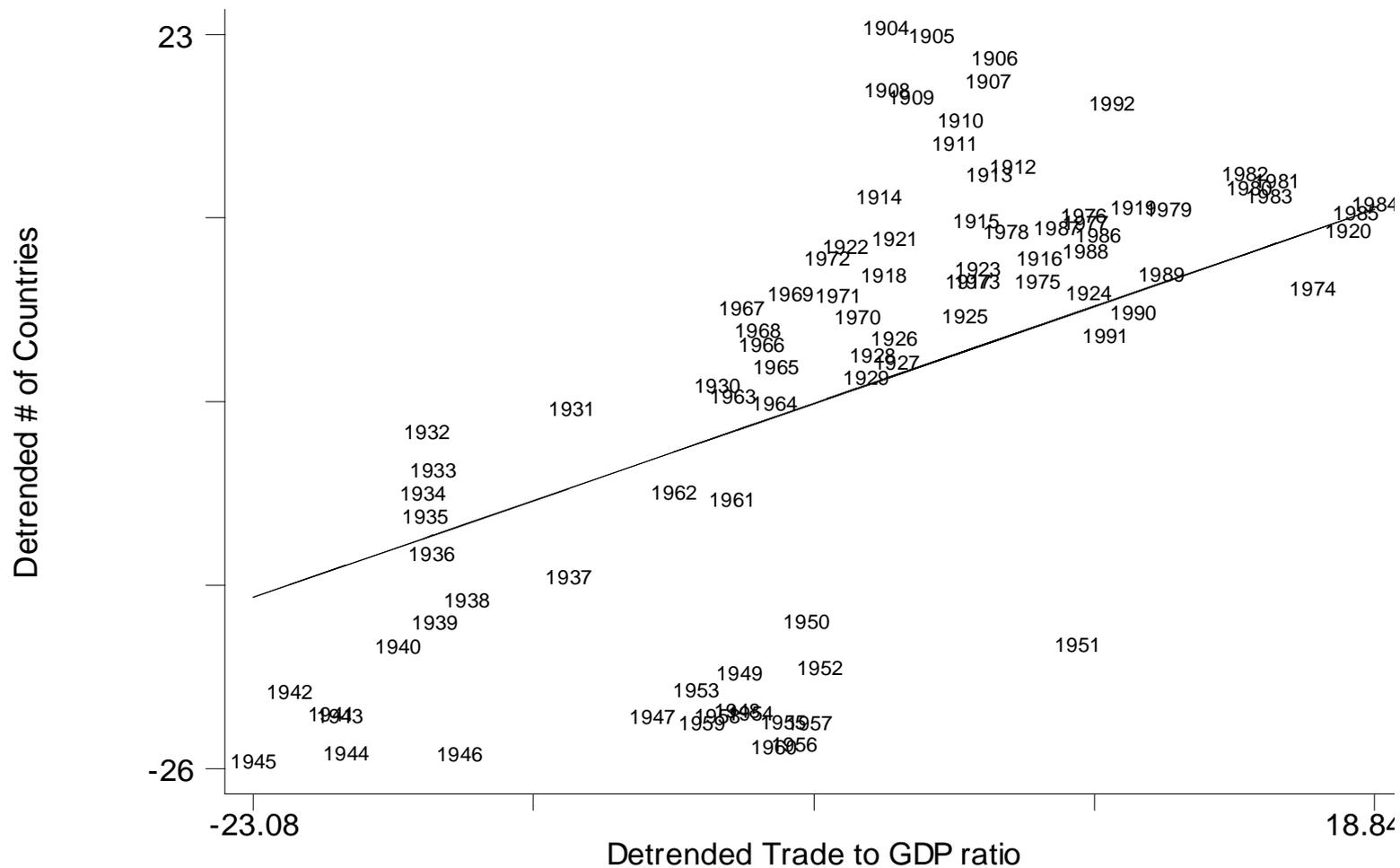
# Summary of paper on Europe: I blame the French (just kidding/je plaisante)



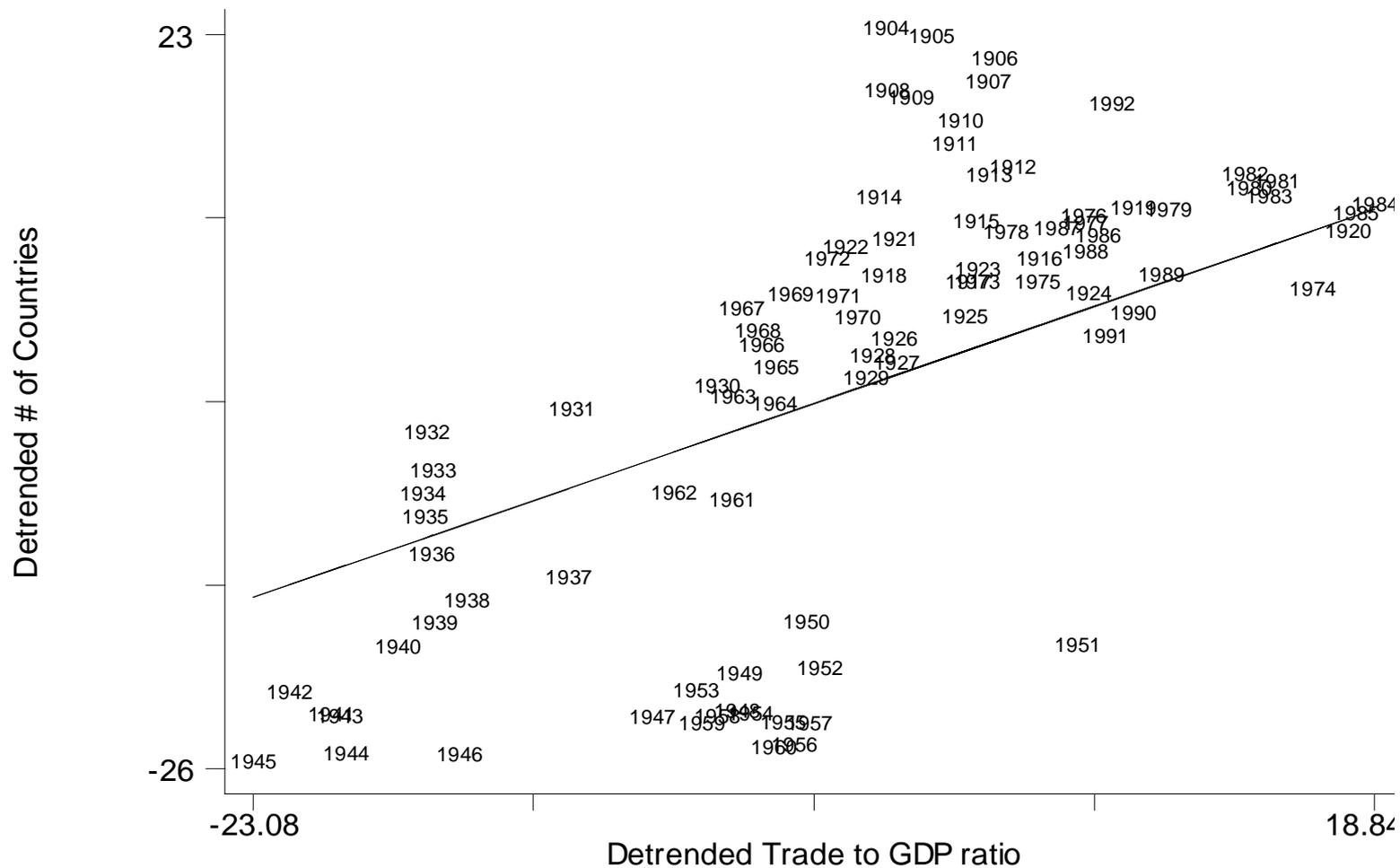
## **Economic integration and political disintegration are mutually reinforcing**

- As international economic integration increases, the economic costs of being small are reduced, and hence political disintegration becomes less expensive
- In a world of smaller countries, international openness is more important
- Economic integration and political disintegration go hand in hand (Alesina and Spolaore, 1997, 2003; Alesina, Spolaore and Wacziarg, 2000, 2005; Spolaore and Wacziarg, 2006)

**Figure 4. Scatterplot of the Detrended Number of Countries Plotted Against the Detrended Trade to GDP ratio (With Sub-Saharan Africa - 1903–1992)**



**Figure 4. Scatterplot of the Detrended Number of Countries Plotted Against the Detrended Trade to GDP ratio (With Sub-Saharan Africa - 1903–1992)**



# Research Questions III

- How much does international economic integration reduce the scale economies associated with larger domestic markets?
- How does the relation depend on the endogenous adjustment of policies to new size and heterogeneity?
- Role of international institutions and cooperation at the regional (e.g. European) vs global level

## Research Questions IV: Relation between International Economic Integration and Conflict

- *Multilateral openness* does *not* reduce the risk of war between pairs of countries.
- However, ***bilateral trade***, by increasing the opportunity cost of conflicts between two partners, ***reduces the probability of conflict*** between that pair of countries (Martin, Mayer, and Thoenig 2008), even when controlling for historical, linguistic, and cultural similarities between populations (Spolaore and Wacziarg 2013).
- Country pairs with a high frequency of past wars are more likely to sign regional trade agreements. This can be explained as a consequence of the complementarity between economic and political gains from trade (Martin, Mayer, and Thoenig, 2010) .

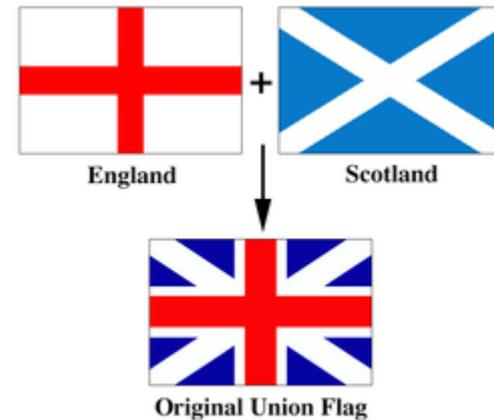
# In sum

- National borders determined by trade-off between heterogeneity costs and benefits of scale in different political and economic environments – both domestically and internationally
- **A larger size** is an equilibrium when borders are determined by **non-democratic** Leviathans, there are high **barriers to trade**, and high levels of **international conflict**
- **A smaller size** can become a new political-economy equilibrium when *heterogeneity costs* have a larger political impact (e.g., **democratization**) and/or become more salient for political and cultural reasons, and *benefits of scale* decrease because of more ***peaceful international relations*** and/or higher ***international integration and economic cooperation among independent countries.***

# Implications for Scotland?

- Two case studies:

**1707** England + Scotland =  
**Great Britain**



**2014** "Should Scotland be an independent country?"

# The Act of Union in 1707 took place in a world of high and increasing trade barriers

- A key motivation for Scotland was *access to trade with England and her colonies in a world of **high and increasing barriers to trade*** (T. Devine's *The Scottish Nation 1700-2007*)
- Barriers to trade between Scotland and its traditional markets in continental Europe were high and increasing
- Barriers to trade between Scotland and England's domestic market and her overseas colonies were also high and at a high risk of increasing in the absence of a union
- Scotland's ability to form its own overseas colonies was low and decreasing after the failure to found a Scottish colony in Central America (Darien fiasco 1695-1700).
- "Article IV of the treaty, which allowed for 'Freedom and Intercourse of Trade and Navigation,' attracted the single largest majority with only 19 votes against." (T. Devine's *The Scottish Nation 1700-2007*, p.13)

# The Act of Union in 1707 took place in a world of high international conflict and non-democratic Leviathans

- Key motivation for England was **defense and security**: need to ensure full control over Scotland during Spanish war of succession (which had resumed in 1702)
- Decisions taken by elites (in England and in the Scottish parliament)
- Vast popular opposition to Act of Union: anti-union demonstrations were common in Edinburgh and Glasgow, and the Articles of Union were ritually burnt in Dumfries.

*“From the unionist perspective, Clerk of Penicuik lamented the yawning gap which he perceived between the parliament and the people on the issue. He estimated that `not even one per cent approved of what [the parliament] was doing.’” T. Devine, *The Scottish Nation*, p. 9*

- Significant transfers and side payments were provided from the English government to members of the Scottish parliament (feasible and credible because taking place across relatively small elites).

# In 2014 the situation regarding benefits of scale is reversed

- **Low barriers** to trade and factor mobility with rest of UK after a breakup
- Very **low trade barriers** with continental Europe and relatively low barriers with rest of the world (including former colonies of England) - Situation unlikely to change in case of breakup.
- If anything, an independent Scotland's **international openness likely to increase** in the long run: Scotland's smaller size and political and cultural attitudes towards European integration likely to be associated with ***stronger incentives to integrate***.
- **Low benefits** from union in terms of **defense and security**, both from Scotland's and England's perspective, given the current geopolitical situation.

# Economic Costs and Benefits from Independence

- In sum, because of the significant reduction in benefits of scale for nation states in Western Europe for economic and political reasons, the ***economic costs of independence*** are likely to be low, specially in the long run, after all transitional costs and adjustments have occurred.
- In principle, there may be some economic benefits – for example, because of different policies towards international economic openness and cooperation in a smaller, more open Scotland. However, those ***economic benefits*** are also likely to be ***relatively small***, because Scotland is already quite open.

# At the end, the answer will depend on Scottish voters' assessment of relative **heterogeneity costs**

- The largest benefits (or costs) from independence would most likely be *political and cultural*, and crucially depend on the extent that independence would reduce expected ***heterogeneity costs from the Scots' perspective***.
- Key variable from this perspective: ***perceived distance*** between Scots and UK voters in terms of ***political preferences for the fundamental traits of the sovereign state*** (the **ultimate public good**).

Thank you

Thenk ye

Tapadh leibh