

Reviews

The Size of Nations, by Alberto Alesina and Enrico Spolaore (MIT Press, Cambridge, Massachusetts, and London, England, 2003), pp. 261.

Since World War II the number of independent countries has almost tripled. Is this tendency going to continue, and lead to a world of an increasing number of minuscule states? Or will the process of economic and political integration draw a world map with fewer borders and larger countries? Thinking about these issues requires a deep understanding of the forces behind the creation and destruction of national borders. The determinants of the size and number of nations are the central themes addressed in *The Size of Nations*.

The authors define a nation-state as the successful monopolist of the legitimate use of force within a given territory. In this context, they argue that the sizes of national states are due to trade-offs between the benefits of size and the costs associated with heterogeneous preferences. The benefits are derived from economies of scale in the provision of public goods and policies, larger domestic markets, interregional insurance and redistribution. The costs stem from differences in cultural, religious, linguistic or economic factors that may lead to different individual choices over those same public goods and policies. The possibility of a world organised in several overlapping jurisdictions, each of them providing one public good with different geographical domains, is satisfactorily ruled out on the basis of the economies of scope and transaction costs associated with the provision of public goods by this maze of independent jurisdictions.

Alesina and Spolaore present a stylised model that captures the key elements of this basic trade-off. Fixed costs in the production of public goods capture the benefits of size while distance in their one-dimensional world captures the costs of heterogeneity. This tractable model provides an optimal framework to shed light on how the trade-off is resolved in different institutional environments. Differences in political regime, the degree of integration in foreign markets or the level of violence in the resolution of international conflicts provide the sources of exogenous variation required to generate meaningful predictions.

Their benchmark is the ‘optimal’ number of countries determined as the solution that maximises welfare given the suggested trade-off. Moving from this benevolent central planner to a voting equilibrium introduces the tensions created by the uneven distribution of the net benefits of size, recognising the incentives that border regions have to break away and redraw borders. As a result, in the absence of transfers, the equilibrium configuration under democratic rule involves smaller jurisdictions than the optimal size. Along these lines, monetary transfers, like the special tax status enjoyed by the Basque Provinces, or political transfers, like the increasing participation of Catalonian nationalistic parties in the design of national policies, are means used by the Spanish state to minimise the uneven distribution of the benefits of size across the state, attenuating the urge for segregation.

The authors argue that borders in a world of Leviathans, in which leaders rule against the will of a majority of the citizens, tend to vanish. Rent-maximising dictators prefer large empires to small countries, in order to extract larger total rents. Ignoring the will of their citizens and therefore the costs of heterogeneity tilts the trade-off drawing a world map with fewer and larger countries. Nonetheless, the delicate balance between expansion and increasing heterogeneity of population is what decides the fate of empires. The most important implication of this analysis is that democratisation should be accompanied by an increase in the number of countries. In this context the dismembering of the former Soviet Union is an example that quickly comes to mind.

The degree of economic integration with the rest of the world is another important factor shaping the trade-off between the benefits of size and the costs of heterogeneity. As the world becomes more integrated, one of the benefits of large countries, the size of their market, vanishes and as a result the trade-off between size and heterogeneity shifts in favour of the latter. We should observe the process of economic integration matched with political segmentation and an increase in the number of countries. Global challenges, some of them closely related to economic integration, like the destabilising effects of speculative capital

flows and others coming from different sources, like climate change or international terrorism, are an important counterbalance that at this stage is left out of the analysis.

Finally, they argue that a more violent world requires larger countries that provide better protection to their citizens. Even in a peaceful environment, under imperfect enforcement of international law, a country's bargaining power depends on its military capability. Along these lines decreases in the probability of international conflict will be an additional force reducing the advantages of size and therefore leading to an increase in the number of countries.

In the last chapters, besides providing a mass of quantitative evidence, the authors review the last millennium of world history through the lenses of their model, from the formation of the city-states of the European Renaissance, minuscule states that exploited their outward orientation to complement the domestic market, to the decomposition of the Soviet Union, a vast and heterogeneous empire that did not survive the process of democratisation and opening initiated by Mikhail Gorbachev. They also discuss the rise of the absolutist monarchies in the 16th century in an increasingly expansionist world where economies of scale in wars and public administration outweighed the costs of heterogeneity for those highly non-democratic governments. The birth of the modern nation-state under the influence of the liberal philosophy and the first signs of the industrial revolution, with the former leading to a transformation of the existing absolutist regimes and the latter promoting the economic integration that gave birth to Italy and Germany. And finally, the period of decolonisation that followed the Second World War, with an important increase in the degree of democratisation and an explosion in international trade giving rise to a dramatic increase in the number of independent countries.

As the authors acknowledge the book is 'only' a first attempt to explore a new field. The result is an outstanding example of the use of formal models to dissect a complex reality and provides new and valuable insights on the forces that shape the configuration of national borders. I recommend this book highly, not only to public economists, but also to any scholar interested in economics, political science, sociology or social geography.

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Simplicity, Inference and Modelling: Keeping It Sophisticatedly Simple, by Arnold Zellner, Hugo A. Keuzenkamp and Michael McAleer, (eds) (Cambridge University Press, Cambridge, 2001), pp. ix + 302.

I can't recall it ever being said explicitly, and I have tried very hard to do so, but one of the lessons that I took from my education in econometric modelling was that models should be parsimonious. It is also one of those tenets of modelling that I want my students to take away with them. Most would agree that larger datasets provide scope for larger, richer, more complicated models, although that need not be at odds with Occam's razor of no unnecessary complication. The advent of computer-intensive approaches, such as bootstrapping and non-parametric methods, has changed much statistical practice from 'learning a lot from a little' to 'learning a little from a lot'. Whereas techniques were directed to extracting the maximum amount of information from small datasets, often by the introduction of substantial amounts of non-sample information, it is becoming increasingly common to work with techniques that are perhaps less efficient but compensate by requiring large datasets. It is reasonable, therefore, to question the role of parsimony when large datasets are being used for modelling. This brings us to the subject of this review, which is a collection of thought-provoking papers from the multidisciplinary *Conference on Simplicity and Scientific Inference*, which was organized and held at Tilburg University in January 1997. A simple summary of the book is probably best provided by the editors themselves (on both the inside sleeve of the dust jacket and on the first page of the book):

A problem with Occam's razor is that nearly everybody seems to accept it, but few are able to define its exact meaning and to make it operational in a non-arbitrary way. Using a multidisciplinary perspective, with contributions from philosophers, mathematicians, econometricians and economists, this monograph examines simplicity by asking six questions. What is meant by simplicity? How is simplicity measured? Is there an optimum trade-off between simplicity and goodness-of-fit? What is the relationship between simplicity and empirical modelling? What is the relationship between simplicity and prediction? What is the connection between simplicity and convenience?