



# Icelandic Liberalism and Its Critics: A Rejoinder to Stefan Olafsson

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In 2017, I published a paper on Icelandic liberalism in this journal. It was in two parts, the first one describing Iceland’s liberal heritage of the 19th and 20th centuries (Gissurarson 2017a), while the second one was on the extensive liberal reforms of 1991–2004 and their critics, and the 2008 Icelandic bank collapse and anti-liberal narratives about it (Gissurarson 2017b). The journal invited Professor Stefan Olafsson to respond, as he had been mentioned in my paper as a leading critic of the liberal reforms and a proponent of (what seems to me to be) an anti-liberal narrative on the bank collapse. His lengthy composition (Olafsson 2017) stands in need of some corrections and comments.<sup>2</sup>

## The 2003 election campaign

In his response to my paper, Professor Olafsson makes some implausible or inaccurate claims. He says, for instance, that he, unlike me, has “never been active in any political-party advocacy” (Olafsson 2017, 400). This is not correct. Olafsson was active in, and on the Board of, the Social Democratic Alliance (Bandalag jafnadarmanna) which was founded before the 1983 parliamentary election and merged with the Social Democratic Party in 1986 (Althydubladid 1983). He was

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2. I shall not be discussing Olafsson’s personal attacks on me.

also an Alternate Member of the Board of the Socialist Debating Club (Malfundafelag felagshyggjufolks) which was founded in 1985 (Thjodviljinn 1985), operating for a few years with the aim of uniting Icelandic left-wing parties against the centre-right Independence Party. Olafsson's services to socialism were deservedly recognised in 2007, when he became, with Professor Thorvaldur Gylfason, the first recipient of the "Socialist Award" given by the Youth Wing of the Social Democrats (Morgunbladid 2007).<sup>3</sup> It is true however that in Iceland Olafsson has taken a position less as an advocate of any one political party than as a critic in general of what he calls "neo-liberalism" or "libertarianism" but what I call simply "liberalism."<sup>4</sup>

It was as a critic of neoliberalism that Olafsson played a prominent role in the parliamentary election campaigns of 2003 and 2007 as I briefly mentioned in my second paper (Gissurarson 2017b, 374–375). In 2003, he was the director of a research institute at the University of Iceland. This institute was to a large extent funded by the City of Reykjavik, then controlled by a coalition of left-wing parties under the leadership of Social Democrat Ingibjorg S. Gisladdottir, the mayor. A month before the election, the institute published a report purporting to show that poverty was much more extensive in Iceland than previously thought, with 7–10 percent of the population below the poverty line (Njals 2003). Gisladdottir, now a parliamentary candidate, devoted a major speech to the report, also quoting Olafsson's studies of poverty in Iceland (Gisladdottir 2003). When the report was criticised, analytically and empirically, Olafsson wrote a newspaper article defending it (Olafsson 2003), asserting that his own earlier studies suggested the same general conclusion as the report's author: that poverty was more widespread in Iceland than in the other Nordic countries, those countries long having served as a standard for the Icelanders.

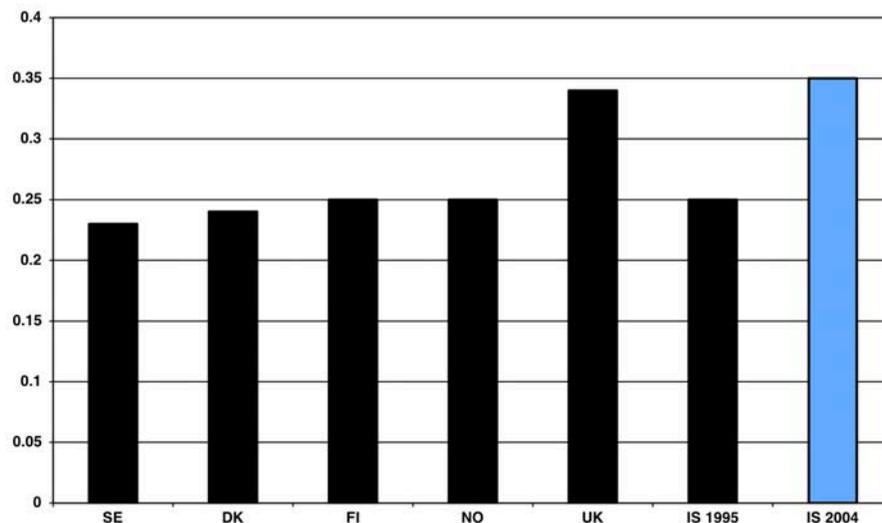
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3. The name of the award was "felagshyggjuverdlaun." While *felagshyggja* is a traditional translation of the English word *socialism*, in all fairness it should be pointed out that it may have a wider meaning, signifying general left-wing sympathies rather than a call for central economic planning. The word apparently was constructed by Jon Duason and intended to be the direct equivalent of 'socialism' (Duason 1917). The main ideologue of the Social Democrats, Economics Professor Gylfi Gislason, used 'felagshyggja' as a translation of 'socialism' (Gislason 1977).

4. Needless to say, 'liberalism' has taken on a different meaning in the United States than in Europe or Latin America. A European or Latin American liberal stands squarely in the tradition of Adam Smith and John Locke, whereas in the United States the name is mostly used as a general term about people of the left, for example economist John Kenneth Galbraith. It is also true that some intellectuals such as John Stuart Mill and John Maynard Keynes occupy a somewhat ambivalent position, being liberal in some ways, but rejecting or at least not accepting fully economic liberalism. It should be recalled, though, that Mill for example was wary of the concentration of power in the hands of government (Mill 1977/1859, 306) and that he thought that socialism might spontaneously and gradually replace capitalism because workers' cooperatives might become more efficient than privately owned companies (Mill 1967/1879). If Olafsson wants to call himself a liberal, I can only say that imitation is the sincerest form of flattery.

Olafsson is therefore not technically wrong when he says that his own data on poverty in Iceland were derived from an earlier period (Olafsson 2017, 419). But the 2003 report on poverty, written as a master's thesis under his supervision and published by his institute a month before the parliamentary election, certainly was used as ammunition for the left-wing parties running against the then coalition government of the Independence Party and the Progressives. Olafsson has himself disclosed that after the election some prominent professors at the University of Iceland requested a meeting with the University's rector, expressing concern over the role played by Olafsson's institute in the election campaign.<sup>5</sup> Two years later, in 2005, the institute was dissolved.

**Figure 1.** Olafsson's Gini coefficients for 1995 and 2004



*Source:* Olafsson 2006b.

As I pointed out in my paper (2017b, 374–375), in early 2007 a comprehensive survey of poverty, social exclusion and income distribution in Europe showed that in the very year, 2003, in which the debate had raged about poverty in Iceland, a smaller proportion of Icelanders, 5.4 percent, were below the poverty line than in any other country in Europe except Sweden. This certainly was a significantly

5. Olafsson mentioned this in at least two interviews, one on the short-lived television station NFS in September 2006 (Magnusson 2006) and the other on internet magazine *Pressan* in February 2010 (Gissurarson 2010). Unfortunately, neither interview is available online. In the latter interview Olafsson accused me of having orchestrated the visit of those professors to the rector. No, distinguished university professors are not at my command.

lower figure than the 7–10 percent in the much touted report published in 2003 by Olafsson’s institute. In the European survey, poverty was defined as having income below half of median income (Eurostat 2007; Statice 2007)—it was therefore relative, rather than absolute, poverty. In his response to me, Olafsson emphasises that his own data stemmed from 1985–1997. But if the findings of the European survey are accepted, then apparently only two possibilities exist: (1) If Olafsson’s earlier data were correct, revealing more poverty in Iceland than in the other Nordic countries, then in the period from 1998 to 2003 poverty had been rapidly reduced to a lower level than in three out of the four other Nordic countries. If this was the case, then the heated discussion in the 2003 election campaign on poverty in Iceland, instigated by Olafsson, was somewhat misguided. (2) Olafsson’s earlier data were not correct, and even in those earlier years poverty was no more extensive in Iceland than in the other Nordic countries. Neither possibility would seem to enhance Olafsson’s reputation as an expert on poverty in Iceland.

## The 2007 election campaign

For many Icelanders, Professor Olafsson’s findings on poverty were counterintuitive. Rightly or wrongly, there was, and is, a common perception among them that in their country poverty is less of a problem than almost anywhere else. It was therefore perhaps not surprising that as the years passed Olafsson was to change his emphasis, targeting income distribution rather than poverty. In the autumn of 2006, less than eight months before the 2007 parliamentary election, Olafsson publicly claimed that in the period from 1995 to 2004 income distribution in Iceland had become much more unequal than in the other Nordic countries.<sup>6</sup> In support of his claim, he quoted data from various sources, where the most recent ones were said to be from Eurostat, the EU Bureau of Statistics. In a newspaper article, Olafsson published a graph purporting to show income distribution as measured by the Gini coefficient. In 2004, it was supposed to be 0.35 for Iceland, in terms of individual disposable income. The most relevant parts of the graph are reproduced here in Figure 1. Olafsson added that the new Eurostat

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6. Olafsson, in his public pronouncements before the 2007 parliamentary election and in his response to me in this journal, uses data from 1995 onwards, not from 1991 when the liberal reforms I discussed (in Gissurarson 2017b) started under David Oddsson as Prime Minister. A possible explanation is that in 1991–1995 the Social Democrats were in a coalition with the Independence Party and Olafsson, being close to them, did not want to criticise them. But in fact, the period from 1995 to 2004 is an appropriate frame of reference, for two reasons that are quite distinct from such a political consideration: In 1995, the economy had recovered from a previous recession, and after 2004 the bubble economy created by extensive debt accumulation abroad started.

data corresponded well with data quoted by Professor Thorvaldur Gylfason on income distribution in Iceland (Olafsson 2006b).

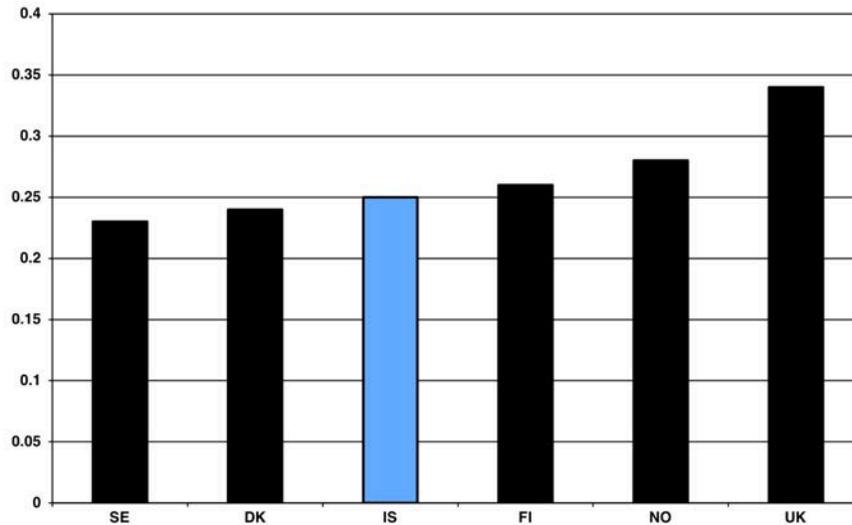
As I pointed out at the time (Gissurarson 2007a; b) and later (2017b, 375), there was a problem with those data: Whereas Eurostat had calculated Gini coefficients for other countries excluding capital gains from stocks, it had mistakenly included them in the Gini coefficient calculated for Iceland. The comparison between Iceland and other countries was therefore invalid. This mistake was almost immediately corrected by Eurostat and the data removed from its website. Undaunted however, Olafsson gave a newspaper interview in late October 2006, no longer quoting any data from Eurostat but vaguely mentioning other sources, such as the OECD and the World Bank, asserting that in Iceland inequality had increased more rapidly than in the US under Reagan, in the UK under Thatcher and, probably, in Chile under Pinochet (Olafsson 2006c).

In early 2007, Eurostat published its aforementioned survey of poverty, social exclusion and income distribution in European countries, using data from 2003–2004 (Eurostat 2007; Stalice 2007, 11–12). The 2004 Gini coefficient in terms of individual disposable income calculated for Iceland turned out to be 0.25, and not 0.35, as Olafsson had claimed earlier, quoting Eurostat as his source. In Figure 2, Gini coefficients for selected countries are reproduced. Soon thereafter, Olafsson published a newspaper article (Olafsson 2007) in which he did not directly withdraw his earlier assertions, but mentioned the Eurostat survey and expressed surprise that the exclusion of capital gains from stocks could make such a difference that the Gini coefficient for Iceland would go down from 0.35 to 0.25.<sup>7</sup>

The original error—on which Olafsson based his statements in the autumn of 2006—was made by Eurostat, not by Olafsson. But he took it up, asserting that it corresponded well with recent data from other sources, and after the error was corrected, he just dropped his reference to Eurostat and repeated that income inequality had increased more rapidly in Iceland than in most other countries, as a result of deliberate policies pursued since 1995 by the coalition government of the Independence Party and the Progressives (Olafsson 2007). What is really important is that after the initial error had been corrected, the data confirmed the intuition of many Icelanders that there was less poverty in Iceland than in almost any other country of the world, and that in the period from 1995 to 2004 income distribution, as traditionally measured, had not become less equal in Iceland than the other Nordic countries, broadly speaking.

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7. It is indeed surprising. I asked a person from Statistics Iceland about it, and he replied that the sample from tax returns which was used to calculate data about income distribution in Iceland had included individuals who had gained immense amounts of money from selling stocks.

**Figure 2.** Eurostat's Gini coefficients for 2004

*Source:* Eurostat 2007; Statice (2007, 11–12).

In the ensuing discussion I repeatedly made the point that for a liberal in the classical sense, income distribution is not necessarily a problem, unlike poverty: The gap between, say, the richest 10 percent of the population and the poorest (or the least rich) 10 percent did not matter as much as the set of opportunities for all income groups to increase their income and improve their living standards by their own initiative, ingenuity and hard work. In the year 2004, our main point of reference in the discussion, there was practically no unemployment in Iceland; the set of opportunities facing the Icelanders was probably as adequate as could be found in any other country in the world. Also, as a result of Iceland being a homogeneous, relatively tolerant society with no dialects or other great barriers between classes, races or regions, social exclusion was less serious than in most other countries, while social mobility was high (Gissurarson 2007a; b; 2009).

One does not need to agree on everything with American philosopher John Rawls (1971) to see that his approach is important: How fares the worst-off group in society? There is little doubt that in 2004 the living standards of that group, say the 10 percent of the population with the lowest income, would have been better in Iceland than in most or even almost all other countries, given her prosperity, low level of relative poverty—and thus an even lower level of absolute poverty—and less social exclusion than in most other countries.

## Taxation and inequality

A part of Professor Olafsson's critique of the 1991–2004 liberal reforms was that increased income inequality was the result of deliberate policies, especially on taxation, pursued by the coalition government of the Independence Party and the Progressives, in power from 1995. He asserted that while pretending to cut taxes, the government had in fact increased the tax burden. The government also had, Olafsson maintained, shifted the tax burden from the rich to the poor and from corporations to families by not raising the tax-free income allowance in line with increases in wages or prices. Indeed, Olafsson made the sarcastic remark that David Oddsson, Prime Minister from 1991 to 2004, should be regarded as a "Taxation King" (Olafsson 2006a).

The assertions are misleading or plainly wrong in many respects. First, from the vantage point of 2006–2007 there did not seem to be any significant or unusual increase in income inequality, as traditionally measured, in the period from 1995 to 2004: The Gini coefficient was 0.25 in 1995 according to Olafsson's own estimate (Olafsson 2006b), and it was again 0.25 in 2004 (Eurostat 2007; Statice 2007). The increase in this kind of inequality seems to have taken place mostly in the period from 2004 to 2007 and it was, as Olafsson states, non-negligible. Its cause was, as Olafsson recognises, the bubble economy based on enormous debt accumulation by the banks. Later, apparently, Gini coefficients have been calculated backwards for 1995 and the following years, and they have turned out to be lower than Olafsson had estimated in his newspaper articles of 2006–2007 (Olafsson 2017, 416, Figure 3).<sup>8</sup> But in my paper I was giving a historical account of the debate on inequality before the 2007 parliamentary election. By introducing such more recent data, Olafsson is by no means correcting what I said in early 2007: He is correcting himself, rejecting his own earlier estimate, albeit without explicitly mentioning it.

Second, the tax burden imposed by central government did not become heavier in any meaningful sense in the period from 1995 to 2004: Total tax revenue of central government amounted to 31.1 percent of Gross Domestic Production, GDP, in 1995 and to 31.9 percent in 2004 (Statice 2018). The increase only became non-negligible by including tax revenue by municipalities, the most important of

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8. The Gini coefficients Olafsson quotes since 2003 are derived from Icelandic Statistics and Eurostat and easily available online. However, I have not been able to find the source for the Gini coefficients that Olafsson provides for the years prior to 2003 (Olafsson 2017, 416, Figure 3). He refers to the Icelandic Tax Authority (Ríkisskattstjóri), but no historical data on Gini coefficients are to be found on the website of the Authority and when I contacted members of the staff they did not know of any such calculations made and published by the Authority.

which was the City of Reykjavik, controlled by a coalition of left-wing parties since 1994: Total tax revenue at both levels, the municipalities and central government, increased from 39.6 percent in 1995 to 42.6 percent in 2004 (*ibid.*).<sup>9</sup> However, this was not a great increase. Be that as it may, it seems somewhat unfair to accuse the 1995–2004 Oddsson governments of an increase in the tax revenue of Icelandic municipalities and to make sarcastic remarks about Oddsson being a “Taxation King.”

Third, Olafsson’s assertion is an example of how unintended outcomes are interpreted as the results of deliberate policies. The grain of truth in it is that despite extensive tax cuts, the total tax revenue of central government as a proportion of GDP did not go down: it slightly increased, ever so little. But as Olafsson himself acknowledges, in Iceland the years from 1991 to 1995 were marked by economic difficulties, whereas the period from 1995 to 2004 saw rapid economic growth. In a tax system with tax-free income allowances there is an inbuilt tendency for the level of taxation to move in the opposite direction to the business cycle. During a downturn, a higher proportion of total income ends up below the tax-free allowance limit, so the level of taxation, as a proportion of Gross Domestic Production, GDP, goes down. The reverse happens during an upswing. Then incomes of most economic agents rise, so a higher proportion of total income ends up above the tax-free allowance limit and the level of taxation as a proportion of GDP consequently goes up, other things being equal. This is precisely what happened in 1995–2004, offsetting various tax cuts. The tax burden was not intentionally made heavier; rather, a higher proportion of income became liable to taxation. Again, even if corporations did not enjoy any tax-free allowances like individuals, during the upswing a higher proportion of them registered net profit and thus paid income tax.

Olafsson actually makes this very point when he criticises my emphasis on the fact that in Iceland, total revenue from corporate taxes, as a proportion of GDP, increased in 1990–2003 despite a significant reduction in the corporate tax rate, from 50 percent to 18 percent (Olafsson 2017, 415). Of course the economic upswing played a role, but such upswings do not simply happen on their own: the ground has to be prepared for them. In Iceland, the economic upswing of 1995–2004 was encouraged by corporate tax cuts, the elimination of public subsidies to loss-making companies, the facilitation of free trade, and price stability. As I pointed out in my paper, in 1990–2004 the internationally recognised index of

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9. It is not clear wherefrom Olafsson derived the figures on tax revenue that he presented in 2006 (Olafsson 2006a). According to him, total tax revenue, of central and local government combined, increased from 33.4 percent of GDP in 1995 to 41.1 percent in 2004, or by 7.7 percentage points. While tax revenue figures on the OECD and World Bank websites are different from those found on the Statistics Iceland website, none of them corresponds with the figures presented by Olafsson in 2006.

economic freedom increased for Iceland from 6.6 to 7.9. In 2004, Iceland had the 9th freest economy in the world and the freest economy in the Nordic countries (Gissurarson 2017b, 370–371; Gwartney and Lawson 2006, 20).

Olafsson does not reject the uncontested, and remarkable, fact that in Iceland, total revenue from corporate taxes, as a proportion of GDP, increased in 1990–2003 despite a significant reduction in the corporate tax rate, but he calls the explanation that the tax base had grown considerably “Arthur Laffer’s voodoo economics.” He also insinuates that I stopped in the year 2003 “because the semblance of a relationship is much weaker or nonexistent after that. Reservations are clearly in order regarding this supposed victory of Laffer’s voodoo economics in Iceland” (Olafsson 2017, 415). But there was a simple reason why I chose 2003 as the end point: It was that the credit bubble began in 2004. Indeed, I stressed this in my paper, remarking that this was “before the credit bubble preceding the 2008 bank collapse” (Gissurarson 2017b, 369).

Fourth, Olafsson deals cavalierly with another response of mine (Gissurarson 2017b, 377) to his 2006 critique. He had asserted that the government had intentionally increased the tax burden of low-income people by not raising the tax-free allowance in line with increases in prices or wages (Olafsson 2006a). I had pointed out (Gissurarson 2009, 60) that in this context it should not be ignored that payments into occupational and private pension funds had been exempted from taxation. Indeed, this change more or less made up for the relative fall in the tax-free allowance. But now Olafsson (2017, 413) invokes the fact that contributions to occupational pensions funds were never left out in figures on the tax burden. But that is not to my point. His original accusation, made in a series of newspaper articles before the 2007 parliamentary election (e.g., Olafsson 2006a), was that because the government had not raised the tax-free allowance in line with increases in prices or wages, it had intentionally increased the real tax burden. I drew attention to the fact that this was wrong because of the tax exemption of pension fund payments. That was all. I also commented that I personally did not see any special need to link the tax-free allowance to the price level. It is in my opinion not healthy that a sizeable segment of the population does not pay any income tax. The income-tax-free allowance is much higher in Iceland than in most other countries. It would be even more misguided to link that allowance to the real wage level: It would mean that irrespective of the development of wages, groups which could well afford to pay income tax because their wages had risen, would be permanently exempted from it (Gissurarson 2007a; b; 2009). In my opinion it is bad policy to engineer a sizeable segment of the population with no skin in the income-tax game.

## Inequality not necessarily injustice

In the debate on income inequality, I repeatedly drew attention to the fact that liberals in the classical sense do not necessarily worry about it, whereas they regard poverty as a social evil (Gissurarson 2007a; b; 2009). I stressed that the calculation of Gini coefficients is only one of many ways to try to illuminate the economic situation of different groups in society, and by no means a perfect one (cf. Arnason 2014). Consider the 2008 bank collapse. Professor Olafsson rightly remarks that income distribution then became much more equal: the Gini coefficient for Iceland went down (Olafsson 2017, 417). Those who personally lost the most financially by the collapse were high-income groups. But is such a development really desirable? Would the rest be better off if the best-off group would either lose most of its income or choose to pay taxes in other countries?

In the debate, I also analysed Olafsson's rhetoric. He consistently employed the ancient Icelandic word *ojofnudur* about inequality in income distribution. But this ancient word is better translated as injustice, aggression or violence: In the Icelandic sagas, taking place in the 10th and 11th centuries, an *ojafnadarmadur* was someone trying to set himself above the law. The meaning of the much rarer antonym *jofnudur* would then be equality before the law (not of outcomes), or equity (in the original jurisprudential sense), or fairness and impartiality towards all concerned. Usually, 'ojafnadarmadur' in the Icelandic sagas is translated into English as 'troublemaker,' but also as 'unjust man.'<sup>10</sup> By employing the ancient word 'ojofnudur' about inequality in income distribution instead of using the more accurate expression 'ojofn tekjudreifing,' Olafsson implied that there is something unjust about inequality in income distribution. I then went on to argue that the liberal reforms of 1991–2004 actually may have led to an increase in 'jofnudur' or equality before the law, or equity, because discretionary power to hand out goods had been greatly reduced, with opening up markets, removing barriers to competition, privatising, and cutting taxes (Gissurarson 2007a; b; 2009; 2012).

Olafsson however chooses to misconstrue this argument as if I had claimed that income inequality, as traditionally measured, had not increased in 1991–2004 (Olafsson 2017, 417). It may have increased, and I would be perfectly willing to concede this, on the basis of recent data, although according to Olafsson's own

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10. The former translation is found, for example, in *The Saga of the People of Vatnsdal*, Ch. 16; *The Saga of the People of Vopnafjord*, Ch. 12; and *The Saga of the People of Eyri*, Ch. 8 and 57. The latter translation is found in *The Saga of the People of Eyri*, Ch. 12 and 30. In *The Saga of the People of Eyri*, Ch. 25, 'ojofnudur' is translated as injustice and coupled with arrogance (V. Hreinsson, ed., 1997).

estimate of the 1995 Gini coefficient for Iceland, presented before the 2007 parliamentary election, it had indeed not increased: His Gini coefficient for 1995 was 0.25, and Eurostat's coefficient for 2004 was also 0.25. But again, I, like other liberals in the classical sense, would not regard an increase in income inequality as a burning cause for concern, unless it had been brought about by greater coercion and corruption and not by greater individual choice. Assume that at a certain point in time there is in Iceland what Olafsson would consider a just income distribution,  $D_1$ . Then Milton Friedman visits and gives a lecture, charging 50 dollars a ticket. Five hundred people gladly pay the admission fee. The new income distribution,  $D_2$ , has now become more unequal, Friedman being richer by \$25,000 and five hundred Icelanders being poorer, each by \$50. Where is the injustice in the move from  $D_1$  to  $D_2$ ? (Nozick 1974).

## **The Icelandic welfare state: Nordic or Anglo-Saxon?**

Professor Olafsson's main contention about the 1991–2004 liberal reforms was that Iceland was being wilfully transformed from a Nordic welfare state to an Anglo-Saxon one, with more poverty and more inequality than in the Nordic countries and with less generous provisions for the needy (Olafsson 2006b). It is true that the Icelandic welfare state differs in some aspects from the Scandinavian model: Welfare benefits are not regarded as general rights, but rather as provisions solely for the needy; the Icelanders are a young nation compared to the Scandinavians; and the norm in Iceland is not to retire as soon as one can, but rather at 70 years and sometimes even later.

This explains the paradox that outlays per capita on welfare benefits have tended to be lower on average in Iceland than in the Scandinavian countries, while provisions for the needy have been as generous or even more so. In my paper, and in other writings, I took the example of child benefits in 2006 (Gissurarson 2017b, 376). In Sweden, all parents enjoyed the same child benefits regardless of their income, but in Iceland the benefits were means-tested so that single parents in low-income groups received higher payments than in Sweden whereas parents in high-income groups did not receive any child benefits at all. Olafsson cannot but accept this uncontested fact, but he qualifies it by asserting that in Iceland a reduction in the benefits started at a lower income level than he considers appropriate (2017, 423). This may be true, but it is not a refutation of my point that even if outlays per capita on welfare benefits have on average been lower in Iceland than in the other Nordic countries, provisions for the neediest part of the population have been as

generous or even more so. Partly, of course, the lower average outlays are explained by the fact that the Icelanders are on average younger than their Scandinavian cousins. For these two independent reasons, it is seriously misleading to use as an argument against the Icelandic welfare state the fact that it spends less on average on welfare provisions than the Scandinavian countries.

## Pensioners in Iceland

In my paper (2017b, 363–364), I emphasised that the Icelandic pension system is one of the strongest in the world. Olafsson ascribes to me the view that David Oddsson “had a large role in reforming the occupational pension funds during his premiership” (Olafsson 2017, 404). Olafsson misconstrues my words. What I wrote was this: “While 1991 was certainly a turning point in Icelandic politics, in many ways the Oddsson governments up to 2004 *continued and reinforced reforms that had already been initiated*. This applied not only in the fisheries, but also to the pension funds which were now however greatly strengthened” (Gissurarson 2017b, 363, italics added). In some fields, as I stressed in the paper, the great achievement of the Oddsson governments was not so much to initiate reforms as to keep them going on an even keel.

Olafsson tries to play down the impact of the 1997–1998 pension reforms. But surely the introduction of private, heritable pension schemes was an important improvement, and, since the occupational pension fund for public employees controls about one-fifth of the total assets of the pension system, it was a great step towards the sustainability of the whole system when this fund was strengthened by replacing, wherever possible, defined-benefit with defined-contribution. I did not say that the system had become sustainable, as Olafsson asserts (2017, 404), but that the aim of the reforms was “to make the system sustainable in the long run” (Gissurarson 2017b, 363). Unsurprisingly, after 2004 the reforms had to continue in order to reach that aim.

Olafsson tries to correct me on a detail: that at the time when the occupational pension funds were established in 1969, a pensioner with no other source of income than the basic pension would receive roughly what amounted to the minimum wage. This was not so, he says: at that time, his or her basic pension was significantly lower than the minimum wage (Olafsson 2017, 405). But nowhere did I say that I was referring to the late 1960s. It was obvious from my paper that I was referring to the situation in the 1990s and the early 2000s when this was true. Incidentally, I based my short description of the Icelandic pension system on a paper by an expert at the Icelandic Ministry of Finance (Jonasdottir 2007).

Olafsson refers to a controversy he had with the Icelandic Ministry of Fi-

nance shortly before the 2007 parliamentary election. Having been proved wrong on inequality by the 2007 Eurostat survey, Olafsson fiercely criticised the Ministry for alleged deceptions about the living standards of pensioners (Arnason, Olafsson, and Olafsson 2007).<sup>11</sup> The Ministry had quoted figures from the Nordic Statistics Commission showing that the average payment of statutory retirement pensions in 2004 was higher in Iceland than in the other four Nordic countries (Nososco 2006, 142, Table 7.8). Against this, Olafsson quoted another figure from the same source, retirement pension per pensioner, showing that it was lower than in three of the four other Nordic countries (Nososco 2006, 178, Table 7.23). But there was an obvious explanation for the divergence between the two figures. The former figure was calculated by finding the sum of basic and occupational pensions and dividing it by the number of recipients of basic pensions, which in 2004 amounted to 26,000 individuals. The latter figure was calculated, on the other hand, by dividing total expenditure on pensions by the number of people that had reached retirement age, which in 2004 amounted to 31,000 individuals. In other words, of the 31,000 Icelanders of retirement age in 2004, 5,000 did not take pension, mostly because they had continued working full-time after becoming 67 years old.

This explains the paradox that in 2004, at the same time as total expenditure on pensions was relatively lower in Iceland than in the other Nordic countries, individual pension income was at least as high, if not higher, as the Nordic Statistics Commission recognised: “The low expenditure in Iceland is due to the high employment rate among the elderly compared with the other Nordic countries” (Nososco 2006, 171). It was disingenuous of Olafsson to quote total expenditure on pensions in Iceland as a significant argument for the inadequacy of the Icelandic welfare state. What most people would find more relevant would be the real income of those Icelanders dependent on pensions. Certainly, in 2004, the elderly in Iceland did not face worse prospects than the elderly in the other Nordic countries. Indeed, the aforementioned Eurostat survey showed that in 2004 poverty among the elderly was nowhere at a lower level than in Iceland except in Luxembourg (Eurostat 2007; Statice 2007).

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11. Olafsson’s comment on this is however not very clear. “Another spin from Gissurarson is about what he claims is a vindication of my conclusion that some Icelandic pensioners have in the past faced worse living conditions than comparable groups in the other Nordic welfare states” (Olafsson 2017, 421). He must have meant to say ‘refutation’ and not ‘vindication’. I cannot make sense, either, of the following criticism he makes on the same page of data provided by the Nordic Statistical Commission: “These are assessed figures with weak assumptions about compositional proportions of basic and occupational pension expenditures and not direct measures of pensioner incomes at all, as Gissurarson however claims.”

## Lessons of history

Professor Olafsson's treatment of historical facts is casual, even careless. He seems to deny, for example, that Jon Sigurdsson, the leader of Iceland's struggle for independence, was an economic liberal, stating that his "concern was mainly to relieve Icelanders of the Danish trading monopoly and to propound that Icelanders should be given the freedom to take care of their own business" (Olafsson 2017, 401). While none of this is wrong in itself, a study of Sigurdsson's writings shows that he was indeed an economic liberal, or a libertarian in Olafsson's preferred terminology. This conclusion is supported by the many direct quotations from Sigurdsson's works provided in my paper. Moreover, this is not only my personal opinion, but the consensus of scholars who have studied Sigurdsson's ideas, such as Economics Professor Olafur Bjornsson (1947) and History Professor Gudmundur Halfdanarson (1997). In a paper in English, Halfdanarson aptly characterises Sigurdsson as a "liberal nationalist" (1999, 111). This is not unsurprising: Sigurdsson was a typical 19th century liberal, and a nationalist and a utilitarian to boot.

Also, Olafsson seems to deny my suggestion that one reason for the high inflation rate in Iceland until the early 1990s was a relatively weak state confronting quite militant labour unions: "The Icelandic state was not weak during the period 1960–1990, as Gissurarson claims" (Olafsson 2017, 406). Olafsson is of course entitled to his opinion, but elsewhere he has written: "In a way the very high inflation rates of the 1960–1990 period can be seen as a sign of the inability of the governments and the institutional structure of the society to handle great fluctuations in the basic economy and social struggles that arose from these fluctuations" (Olafsson 2011, 12).

Again, Olafsson seems to think that he is somehow refuting my suggestion by observing that it was in 1990 that the National Pact between employers and the labour unions, on moderate wage increases in return for government measures to bring down inflation, was made. "The National Pact was indeed implemented one year before Oddsson came to power and he had nothing to do with it. Still Gissurarson allows himself to count the taming of the inflation as an integral part of Oddsson's reform program" (Olafsson 2017, 407). But my claim was not that Oddsson and his political associates made the National Pact, but rather that they fulfilled it. It was the fiscal and monetary restraint shown after 1991 which kept inflation down. In my paper I also pointed out that the comprehensive indexation of financial obligations introduced in 1979 had removed a major incentive for excessive credit creation or money printing, the real cause of inflation (Gissurarson 2017b, 365). In the long run, institutions and incentive structures are more impor-

tant than political personalities, while it is also true that fortune favours the brave, as the Romans observed.

## The nature of the Icelandic left

In his response to my paper, Professor Olafsson seems to deny that the Icelandic labour unions were long dominated by radical leftists, receiving advice and financial support from Moscow. “There may possibly have been some interventions from Moscow during the interwar period (that is contested, though), but not at all from the 1960s onwards” (Olafsson 2017, 406). First, it is not contested by any scholar of whom I know that the Icelandic communist movement received both advice and financial support from Moscow in the interwar period. This was uncovered in documents found in Moscow after the collapse of the Soviet Union, mostly in the Comintern files. The evidence is presented in my book on the Icelandic Communist movement (Gissurarson 2011) and in History Professor Thor Whitehead’s book on the same subject (Whitehead 2010) as well as in earlier works by speakers of Russian who had studied the Moscow documents (Hannibalsson 1999; J. Olafsson 1999). Second, the documents showed that the Socialist Party—founded in 1938 when the communists merged with a left-wing faction of the Social Democrats, while retaining full control over the new party—also received substantial financial support, as well as advice, from Moscow. This is even admitted by Kjartan Olafsson, Executive Director of the Socialist Party in 1962–1968, although he claims personally to have been unaware of the donations from Moscow (K. Olafsson 2006). I have tried to calculate how much this support would now be worth, concluding that it would have amounted in total to at least \$3.5 million from 1940 to 1972 (Gissurarson 2015), a sum that should be considered in relation to a population that reached 200,000 as late as 1968.

An important difference between Iceland and the three Scandinavian countries was that in 1942 the Socialists (as the communists now called themselves) replaced the Social Democrats as the dominant force in the labour movement. Militant members of the Socialist Party, some trained in Moscow, controlled some of the most important labour unions, for example the Reykjavik Workers’ Union.<sup>12</sup> While most donations from Moscow were secret and only exposed after the collapse of the Soviet Union, some Soviet support was public. One instance con-

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12. Diehard Stalinist Eggert Thorbjarnarson, Executive Director of the Socialist Party in 1943–1957, had been trained in Moscow and worked for almost three years, 1934–1937, in the Comintern headquarters. In the 1940s, he was instrumental in bringing important labour unions under the control of the radical socialists, or communists (Gissurarson 2011).

trary to what Stefan Olafsson asserts is that in 1961 the Reykjavik Workers' Union, fighting a long and bitter strike, accepted £5,000 from the "Union of Soviet Construction Workers" which was of course a cover for the Kremlin masters (Morgunbladid 1961). In 1968, the Socialist Party was dissolved and replaced by a more broadly-based party, the People's Alliance, which cut all formal ties to the Soviet Union after the invasion of Czechoslovakia. But a few individuals active in the People's Alliance and some Icelandic labour unions maintained contact with the Communist Bloc much longer (Gissurarson 2011).

## **The common financial framework of the EEA**

Olafsson repeatedly has tried to blame the bank collapse on the liberalisation of the Icelandic economy by the Oddsson governments of 1991–2004 (Olafsson 2017, 409–410). But as I pointed out in my paper (Gissurarson 2017b, 384) this is implausible for several reasons. One is that in 2007, the year before the collapse, Iceland had the 24th-freest economy in the world which means that 23 economies were freer (Gwartney and Lawson 2009, 10). If economic freedom was the problem, then why did the banking sectors in those 23 economies not collapse? Another reason is that the enormous debt accumulation of the banks occurred in 2004–2008, after the liberal reforms had taken place and after Oddsson had left politics to become one of the three governors of the Central Bank of Iceland (CBI). A third, and crucial, reason is that Iceland, as a member state of EEA, the European Economic Area, had introduced the same legal and regulatory framework for the banking sector as other member states—the EU countries, Norway, and Liechtenstein.

Olafsson (2017, 409) says that on Oddsson's "watch the country was drowned in foreign debt." It should be emphasised that this was debt accumulated by the commercial banks, fully private since 2003, and that it takes two parties to create such debt: the creditor and the debtor. The reason the Icelandic banks could accumulate debt was that they found many institutions and individuals abroad willing to lend to them, not least because of the good reputation Iceland has acquired during Oddsson's tenure as Prime Minister in 1991–2004. Again, the CBI did not have the authority or the information to stop the debt accumulation. It was the Icelandic Financial Supervisory Authority (IFSA) which regulated the banks and could request information about them. The CBI, on the other hand, could only warn the bank managers and leading politicians against the debt accumulation. Publicly, the CBI governors had to be cautious, but nevertheless Governor Oddsson remarked in a speech in November 2007:

For a while, cheap capital was readily available, and some were bold enough to grab the opportunity. But the flip side of expansion, and the side that cannot be ignored, is that Iceland is becoming uncomfortably beleaguered by foreign debt. At a time when the Icelandic government has rapidly reduced its debt and the Central Bank's foreign and domestic assets have increased dramatically, other foreign commitments have increased so much that the first two pale into insignificance in comparison. All can still go well, but we are surely at the outer limits of what we can sustain for the long term. (Oddsson 2007)

In his perceptive and balanced report on the bank collapse written at the initiative of the International Monetary Fund, Kaarlo Jännäri, former Director of the Finnish Financial Supervisory Authority, pointed out that in Iceland, as in the other Nordic countries, there was a strong legal tradition of strict authority: "Iceland, like the other Nordic countries, is a nation where the actions of the authorities must be based on law. Discretionary powers are strictly limited. In retrospect, it is easy to assert that the Icelandic banks' expansion abroad should have been restricted, but in the European Single Market framework and with the European Passport, this was simply not something that could be readily accomplished within the existing legal environment" (Jännäri 2009, 16).

The bank collapse certainly was monumental, in Icelandic terms, yet still Olafsson tends to exaggerate it. He says that the Icelandic banks "accumulated foreign debts amounting to between 8 and 9 times the Icelandic GDP" and that taken together the banks "made up the third-largest bankruptcy in world history" (Olafsson 2017, 408). Apparently, Olafsson mistakes the total debt of the banking sector for being their total foreign debt, while he casually throws out an inaccurate figure for the total debt without referring to any source. In fact, the total assets (or liabilities) of the Icelandic banks amounted to 7.4 times GDP in 2007, whereas figures from 2008 do not reflect the economic reality adequately: they fluctuated as GDP grew very little and the currency plummeted (Benediktsdottir et al. 2011, 191). It is also somewhat disingenuous to add together three different private companies in order to create "the third-largest bankruptcy in world history."

## **Were the CBI governors negligent?**

In his response to my paper, Professor Olafsson (2017, 409) writes: "The independent investigative committee that thoroughly studied the collapse of the banks concluded that the three governors of the Central Bank and the governors of the Financial Surveillance Authority had seriously neglected their duties." There is a minor lapse here because there was only one IFSA Director, not many "governors." A more important inaccuracy is that Olafsson writes as if the Special

Investigation Commission (SIC) on the bank collapse had concluded that the three governors of the CBI had “seriously” neglected their duties. This is not what the SIC Report says. It says there that the governors “showed negligence” in certain matters (Hreinsson et al. 2010, ch. 21 pp. 155, 159–160).<sup>13</sup> This is not the only time Olafsson has misquoted the conclusions of the SIC Report. In a book chapter on the Icelandic bank collapse he wrote about the CBI and IFSA: “In fact, the governors of these institutions (including David Oddsson, the most influential neoliberal politician) were found guilty of gross negligence by the Committee. The same applied to the government ministers who had duties in the relevant areas” (Olafsson 2016). There is a difference between “serious” or “gross” negligence on the one hand and negligence without any such amplifying adjectives on the other hand.

It has to be noted in what it was, precisely, that the SIC found the CBI governors negligent. First, it was when the governors rejected a request by Landsbanki in August 2008 for a credit facilitation to enable the bank to meet certain liquidity demands by the UK Financial Services Authority (FSA). As the governors pointed out, they rejected the request because the operation would have been very risky: Landsbanki wanted it to be secret which probably would have been illegal, while such a facilitation would probably have been tantamount to a loan of last resort on which certain rules applied. The SIC did not criticise the CBI’s decision to reject Landsbanki’s request, as the SIC acknowledged that the operation would have been very risky. The SIC however argued that the CBI governors, before they made their final decision, should have investigated Landsbanki’s financial position at the time and the grounds on which the FSA based its demands. The CBI governors responded that it was self-evident that they had to reject Landsbanki’s request so that more paperwork was not necessary, especially since there were more urgent matters with which to deal in the midst of the credit crunch. They added that they had not had authority to investigate Landsbanki’s financial position, the IFSA being the only government agency with such authority (Oddsson 2010; Gudnason 2010; Fridriksson 2010).

Second, the SIC found the CBI governors to have shown negligence when they rejected a request by Glitnir in September 2008 for a loan of €500 million so that the bank could meet certain upcoming obligations. Instead, the CBI advised the government to inject capital amounting to €500 million into Glitnir. Again, the SIC did not take issue with the CBI’s decision to reject Glitnir’s request, noting that there was no guarantee that the bank would be rescued by such a loan. The SIC however argued that the CBI governors, before they made their final decision,

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13. There is a misprint in the latter part of the conclusion on the CBI governors, “showed negligent” instead of “showed negligence.”

should have investigated Glitnir's financial position at the time. The CBI governors responded that the issue had to be resolved over a weekend, from the point in time when Glitnir's request was first made Thursday 26 September to the point in time markets opened in the morning of Monday 29 September and that there had therefore not been any opportunity for extensive consultations or investigations, adding that they had not had legal authority to investigate Glitnir's financial position (Oddsson 2010; Gudnason 2010; Fridriksson 2010).

Both admonitions were essentially not about the important decisions which the CBI governors had made, rejecting the requests by Landsbanki in August of a credit facilitation and by Glitnir in September of an emergency loan. These decisions were deemed by the SIC to be prudent and reasonable in themselves. The criticisms were about the lack of paperwork concerning them. These admonitions by the SIC seem however extraordinary when decision-making in other countries during the financial crisis is analysed. For example, U.S. Secretary of the Treasury Hank Paulson was making many and much larger decisions about the life and death of financial firms in a matter of a few hours, even minutes, over the phone, without any paperwork, simply because in the desperate situation in which he found himself decisions had to be made quickly (Paulson 2010). It took the Federal Reserve Bank of New York only a few hours to decide on extending \$30 billion in credit facilities to Bear Stearns, so that it could be taken over by JP Morgan Chase, which initially had offered \$2 a share for it and then suddenly, to reduce controversy, raised its offer to \$10 a share (Geithner 2014, 155–158). On the same weekend as the decision was made about Glitnir, the British government was dealing with Bradford & Bingley; Chancellor Alistair Darling gave himself forty-eight hours to resolve the matter (Darling 2011, 134). When the U.S. investment banks Goldman Sachs and Morgan Stanley decided to transform themselves into commercial banks in order to obtain assistance from the Federal Reserve Board, they did so overnight: The requirement of a 30-day waiting period for such applications was simply waived (Bernanke 2015, 311).

Reading the admonitions by the SIC, one cannot but recall the well-known witticism that a memorandum is written not to inform the reader but to protect the writer. Moreover, it should be pointed out that the negligence which the SIC found, was according to the 2008 Act on the SIC, passed after the collapse, in other words according to a rule applied retroactively to events before the collapse.

## **Warnings and proposals by the CBI governors**

Professor Olafsson (2017, 409) tries to play down the fact that David Oddsson and his two colleagues at the CBI several times warned leading government

ministers as well as the bank managers against the rapid and indeed enormous debt accumulation of the banks and their main customers. While there is no written record of many of these warnings, some are well-documented. The first time Governor Oddsson seems to have mentioned a possible collapse of the bank system was in a meeting with the leaders of the then coalition government, Geir H. Haarde of the Independence Party and Halldor Asgrimsson of the Progressives, in November 2005, shortly after he had been appointed to the CBI (Gunnarsson 2009, 72). Again, Oddsson warned three government ministers, Prime Minister Haarde, Finance Minister Arni M. Mathiesen and Education Minister Thorgerdur K. Gunnarsdottir, against the vulnerability of the banks in late 2007 (Oddsson 2017; Haarde 2017). In 2008, at many meetings Oddsson uttered warnings: on 13 January (Hreinsson et al. 2010, ch. 19 pp. 102–103), on 7 February (*ibid.*, ch. 19 p. 120), on 1 April (ch. 18 p. 11, ch. 21 p. 57), on 16 April (ch. 19 pp. 163–164), on 7 May (ch. 18 p. 12), on 8 July (ch. 21 p. 73) and on 30 September 2008 (ch. 20 pp. 68–78).<sup>14</sup>

The SIC noted that Oddsson's warnings were particularly forceful at the meeting 7 February 2008, attended by his two CBI colleagues and the leaders of the then coalition government, Haarde of the Independence Party and Ingibjorg Gisladdottir of the Social Democrats, and by Finance Minister Mathiesen, as well as by high officials. Indeed, the SIC found that Haarde showed negligence by not resolutely reacting to these warnings (Hreinsson et al. 2010, ch. 21, pp. 129, 132, 147). A case against Haarde before a specially convened Impeachment Court was mostly based on this conclusion by the SIC. However, the Court acquitted Haarde of most charges, finding him guilty only of violating a formal constitutional stipulation that important matters should be put on the agenda of cabinet meetings (*Althingi v. Haarde* 2012). At Haarde's trial, one witness after another testified that there was very little, if anything, that he as Prime Minister could have done in 2008 to avert the collapse. The basic problem was that already in 2005—the year Oddsson became a CBI governor—the banks had grown too big for the CBI and the Icelandic Treasury to be able to rescue them in the case of a severe liquidity crisis.

It should be pointed out, nevertheless, that it was Governor Oddsson who personally stopped the planned acquisition by Kaupthing of a Dutch bank, announced in the autumn of 2007: This would have expanded significantly the already over-extended Icelandic banking sector (Hreinsson et al. 2010, ch. 19 pp. 102, 110–111).<sup>15</sup> Moreover, at confidential meetings the CBI governors suggested sev-

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14. Four chapters of the SIC Report (Hreinsson et al. 2010) are available in English, Chapters 2, 17, 18 and 21. In citations of those chapters page numbers of the English version are given.

15. Formally, it was the IFSA which withheld permission for the acquisition. But it was at the initiative of

eral measures that the banks could take to reduce their size relative to the Icelandic economy: for Kaupthing to move its headquarters to another country, such as Denmark or the UK (*ibid.*, ch. 19 pp. 198, 122, 124, 256–257); for Landsbanki to transfer deposits in its branches abroad to subsidiaries abroad which would have meant that they were insured by the host country's deposit insurance schemes (ch. 18 pp. 17–18, 20, ch. 19 pp. 124, 209); and for Glitnir to sell its Norwegian bank which was regarded as financially sound (ch. 19 pp. 256–257). But the bankers envisaged great difficulties in implementing such measures, not least because of the credit crunch. As Jännäri points out in his aforementioned report, “many of the covenants in the Icelandic banks’ funding arrangements would have been breached had the banks retrenched rapidly. Breach of covenants would have led to early redemption demands for an important part of the banks’ funding; thus the banks were faced with a kind of Catch-22 situation” (Jännäri 2009, 16). Whereas Oddsson’s many warnings were taken seriously by Prime Minister Haarde and Finance Minister Mathiesen, they were received with scepticism by the Social Democrats, their leader Gísladóttir dismissing his warning 7 February 2008 as “one man’s venting” (Hreinsson et al. 2010, ch. 21 p. 97). Indeed, Gísladóttir as late as early September 2008 urged the banks to continue collecting deposits abroad (Gísladóttir 2008).

It is therefore unfair of Olafsson to assert that Governor Oddsson and his CBI colleagues “did nothing” (Olafsson 2017, 410). Moreover, Oddsson was the first person in authority to recognise the imminent collapse of the banks, as his request to attend a cabinet meeting Tuesday 30 September 2008 showed: On that occasion, he said that the banks were about to fall and that what was needed was to ring-fence Iceland, divide up the bank assets and liabilities into a domestic and a foreign part, with government stepping in to save the domestic one (Hreinsson et al. 2010, ch. 20 p. 70). The details of such a ring-fencing were prepared by a Special Liquidity Crisis Task Force at the CBI over the next few days, with the help of a Bank of England expert that Oddsson asked for from Governor Mervyn King. But the proposed ring-fencing met with great resistance from the Social Democrats in the government. Finally, the CBI governors, in a last-ditch effort, sent a private jet for three experts from JP Morgan who in the wee hours of Monday 6 November managed to convince the Social Democrats of the inevitability of ring-fencing (*ibid.*, ch. 20 pp. 102–103). Subsequently, in the evening of the same day Parliament passed an Emergency Act which gave priority to the claims of depositors over those of other creditors on the estates of the banks—all three of which fell in the course of the next three days. By the Emergency Act, the Icelandic Treasury

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Oddsson who told the IFSA Chairman of the Board (Jon Sigurdsson) that he would take all responsibility for the decision (Oddsson 2017).

avoided a government guarantee of deposits which in the circumstances might have entailed enormous difficulties. The Emergency Act is now widely regarded as having been a prudent and sensible measure. Thus, not only were Oddsson and his CBI colleagues among the persons of authority who were uttering warnings about the impending collapse and suggesting ways of reducing the over-extending banking sector: they also led the crucial first steps towards reconstruction, against resistance from the Social Democrats.

## **The Icelandic blame game**

I believe that the three SIC members strove to be fair. But they were not operating in a vacuum. The Icelandic nation, unused to adversity, was in a shock over the bank collapse, and there was strong demand for finding someone to blame and thus to make the collapse intelligible to laymen. Perhaps the SIC had the unconscious agenda of trying to disperse blame widely among the previous powers to be, not exempting anyone. Oddsson, of course, had occupied a prominent position before the collapse, both as Prime Minister and CBI governor, and his confidential warnings and proposals in the latter office were not generally known. The media machine of business tycoon Jon Asgeir Johannesson also turned on him after the collapse, casting him as the chief culprit. It is however noteworthy that the SIC, with a generous budget, unrestricted access to documents, many full-time experts at its disposal, and powers to require every person of authority to testify, having dug hard for a year and a half could only find two instances (again, in connection with a credit facilitation to Landsbanki in August 2008 and an emergency loan to Glitnir in September 2008) of what it presented as negligence of the CBI governors, both instances essentially being about lack of paperwork supporting important decisions.

Olafsson (2017, 410) alleges that I only blame “one of the business moguls for everything that went wrong during the height of the bubble years.” There is no basis for this allegation. Of course Jon Asgeir Johannesson, to whom he refers, was not alone in his recklessness. He just went further than the others. As I observed, he “was not only Iceland’s greatest business mogul and her only real media magnate,” but also “with his group, by far the biggest debtor of the Icelandic banks” (Gissurarson 2017, 380). In its Report, the SIC expressed the opinion that the concentrated risk of the Icelandic banks had been dangerously high for some time before their collapse. The SIC went on: “The clearest example is Baugur Group and affiliated companies [controlled by Johannesson]. In all three banks, as well as in Straumur-Burdaras, Baugur Group had become too large a risk exposure” (Hreinsson et al. 2010, ch. 21 p. 15). Perhaps Olafsson should direct his ire at the

SIC rather than at me.

Olafsson (2017, 402) also says that I claimed he and another critic of the 1991–2004 liberal reforms, Professor Thorvaldur Gylfason, were “some special envoys of one of the prominent businessmen of the bubble economy years, Jon Asgeir Johannesson.” This is not what I wrote. I said that both “professors had connections to Johannesson: Gylfason was a columnist for Johannesson’s newspaper *Frettabladid*, and Olafsson’s wife was and is the anchorwoman of the evening news on Johannesson’s television station.” Few people would not recognise the difference between asserting that two individuals *were special envoys* of a media mogul and noting that they *had connections* to him. Moreover, Olafsson correctly points out that for a while I wrote regular columns for the same newspaper as Gylfason, *Frettabladid*. But after I repeatedly had criticised the owner, Johannesson (e.g., Gissurarson 2005; 2008), the contract with me was cancelled. However, unlike me, Gylfason strongly supported Johannesson, arguing against a law proposal intended to reduce media concentration (Gylfason 2004a; b). Such a law would have greatly limited Johannesson’s domination of the media market. Gylfason also alleged that a police investigation of Johannesson’s activities was politically motivated (Gylfason 2005), even if it eventually led to Johannesson’s conviction for bookkeeping irregularities, and later for tax fraud.

## What caused the bank collapse?

The general conclusion of the Special Investigation Commission (SIC) into the bank collapse was that “Explanations for the collapse of the banks Glitnir, Kaupthing Bank and Landsbanki are first and foremost to be found in the rapid growth of their balance sheet, and hence their size at the collapse” (Hreinsson et al. 2010, ch. 21 p. 1). But the relative size of the banks is not a sufficient explanation. It is like explaining broken glass by its breakability. Something had to happen to the banks, and there is little doubt what this something was, as I pointed out in my paper: (1) Hedge funds targeted the Icelandic banks in a relentless effort to bring them down. (2) European central banks refused to help the CBI to provide liquidity to the banks, even if Iceland was, through her membership in the EEA, supposed to be a full participant in the European internal market. (3) The U.S. Federal Reserve Board refused to extend the same help in the form of dollar swap deals to the CBI as it gave to the three Scandinavian central banks. (4) The British Labour government closed down the two British banks owned by Icelanders, at the same time as it offered a £500 billion rescue package to all other British banks; the close-down of Kaupthing’s subsidiary KSF brought about the fall of the parent company, for a few days the only survivor of the crisis. (5) The British Labour

government invoked the 2001 Anti-Terrorism Act against not only Landsbanki but also, however briefly, the CBI and the IFSA. On the Treasury's website, Landsbanki was listed alongside the Taliban, Al-Qaida, and the governments of Iran and North Korea. This extraordinary and brutal measure made rescue attempts virtually impossible (Gissurarson 2017b; c).

Professor Olafsson writes however as if the banks deserved their fate. "The three largest banks as well as most saving banks were of course seriously sick and then went into bankruptcy" (Olafsson 2017, 410). It is true that the Icelandic banks behaved recklessly, and in some cases illegally, although such cases were mostly about desperate last-minute attempts to keep them going. But as Finance Professors Asgeir Jonsson and Hersir Sigurgeirsson—quoted with apparent respect by Olafsson elsewhere (2017, 210)—point out in a well-researched book, there is no reason to believe that the assets of the Icelandic banks were on average worse, or better, than those of banks in other countries (Jonsson and Sigurgeirsson 2016, 18). Danske Bank in Denmark, UBS in Switzerland, and RBS in Scotland would all have collapsed if they had not been rescued, crucially by the U.S. Federal Reserve Board. The use of the Anti-Terrorism Act against Icelandic authorities and companies is also ironic considering that many rescued banks have since been exposed for money laundering and other violations of the law (Gissurarson 2017c). In my paper, I offer several explanations that I am not going to repeat here of the fact that the Icelandic banks were not rescued alongside banks in other countries (see Gissurarson 2017b, 384–389). Certainly one explanation may be, as Olafsson holds, that central bankers and other authorities abroad sincerely believed that the Icelandic banks had worse assets than other banks. But Olafsson is surely wrong that this would be the only explanation for their leaving Iceland out in the cold. In particular, the crucial decisions by the U.S. Federal Reserve Board and the British Labour government on the Icelandic banks cannot be explained solely by such a belief.

In his discussion of the Icelandic banks, Olafsson (2017, 408) repeats his earlier assertion that the 2002 privatisation of a large share in Landsbanki was an example of "favouritism and cronyism," and chooses to ignore the crucial fact which I pointed out in my paper about the three main buyers: that they were in no way connected to the Independence Party leadership at the time. The only one of them who previously had been active in the Independence Party had, in fact, managed the campaign of David Oddsson's main rival in the Party primaries before the 1982 municipal election. Another one was apolitical, at least according to himself, and the third one was a member of the Progressive Party (Bjorgolfsson 2014, 100). Olafsson also ignores another relevant fact, that in response to criticisms of the privatisation of Landsbanki, two reports were commissioned from the National Audit Office which found no significant flaw in the process (National

Audit Office 2002; 2003). The reason the offer by the eventual buyers of Landsbanki was accepted was simply that most thought it was overall the most advantageous one, especially since they would be bringing into the Icelandic economy money that they had made abroad. In my opinion, it would not have made a difference if Landsbanki had been sold to others.

## Concluding remarks

Several of Professor Olafsson's contentions expressed during and after the time of the 1991–2004 liberal reforms in Iceland turned out to be wrong: The liberal reforms did not bring about a fundamental change in the Icelandic welfare state; they did not increase relative poverty; if income inequality increased, then it did not do so at a faster rate than in the other Nordic countries; and welfare provisions were no less generous for the needy than in the other Nordic countries. The dispute over how to interpret the 1991–2004 liberal reforms in Iceland has become bitter and invidious—and perhaps amusing to observers of our tiny country. I maintain that these reforms were very successful, producing a healthy, vibrant economy, without in any way reducing welfare provisions or lowering the safety net. The ultimate argument for their success is indeed how quickly the Icelandic economy recovered after the 2008 bank collapse.

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