

Changes in the Foreign Policy of Iceland after the Financial System Collapse in 2008

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Abstract

The purpose of this thesis is to look for changes in the foreign policy of Iceland after the financial crisis. The point of departure is the ongoing debate about foreign affairs with regards to possible European Union membership and the so called *Icesave* dispute connected to the collapse of the Icelandic financial system. Expenditures for running diplomatic missions abroad have also been under scrutiny in political and public debate.

Within international relations there is a variety of theories on the purpose of running foreign policy or what states are trying to obtain in international relations. Small states are faced with some restrictions but enjoy several benefits as well due to their size. For example, they can not rely on hard power as a method to solve their conflicts as they lack capacity. This makes theoretical approaches focusing on soft power more plausible to explain small state behavior in the international system, for example neo-liberalism and cosmopolitan power. Small states are usually more dependent on alliances and networking than the big states, they need to play strategically and make compromises.

Playing strategically is for example important when determining which locations are key locations to place diplomatic missions. During the ongoing recession three Icelandic diplomatic missions have been closed as a result of tighter budget. Cutbacks have also been made on defense by shutting down Icelandic Defence Agency and on development by closing a few offices belonging to the Icelandic Development Agency in Africa and Latin America. Nevertheless, the need for a strong foreign affairs service seems maybe greater than ever, fighting for Icelandic interests and repairing the renown of the country that was harmed by the bank collapse.

Foreign affairs have become a more important issue area for many other actors than the Ministry for Foreign Affairs (MFA). In the most extensive domestic political debate after the crisis, the *Icesave* dispute with UK and Netherlands, other ministries and ministers have been communicating with the outside world a lot more than usual. The prime minister, minister of finance and minister of trade among others have been active at explaining Icelandic views at the international forum. The president has furthermore become a challenger to the foreign policy decided by the parliament and turned the policy towards the *Icesave* dispute “upside down” by refusing to ratify parliament decisions on the issue. He has also undertaken communications with foreign media on the issue, explaining his decisions and upholding Icelandic interests. On the *Icesave* issue, the debate has largely been on definition of interests, there has not been agreement as to which stand best serves

Icelandic interests. The policy change on the issue leading from the president's decisions has however become what he and the aforementioned actors have had to gather around and defend towards the outside community.

Negotiations with the European Union are currently top of the agenda for the MFA. The leading party in the government is supportive of membership while the coalition partner, Left Green Movement, is opposed to membership. Negotiations will be continued until a contract has been finalized and then membership will be subject to a referendum. Opposition to membership has mainly been founded on beliefs that agriculture and the fisheries will suffer as industry sectors; that they will not flourish under EU legislation. Supporters point out on the other hand that with the current situation Iceland has to adopt most EU legislation chapters through its EEA membership without having the chance to influence them, as they would have through EU membership. The president is a long time opponent to EU membership and given his recent involvement in foreign policy formation, he might have some tricks up his sleeve to frustrate membership supporters.

The Icelandic authorities have been working on strengthening their position in far-away markets as well. Geothermal energy cooperation is ongoing or planned in Russia, China and India. The first new Icelandic consular office after crisis was opened in Mumbai, India recently which comes in addition to the embassy in New Delhi established in 2006. India and Japan were among the first states to officially support the IMF loan program for Iceland after crisis. However, the fellow Nordic countries constitute the strongest support base for Iceland before and after crisis, as indicated by their financial assistance and mutual relationship through the various institutions on Nordic cooperation.

1. Introduction

The *Icelandic Ministry for Foreign Affairs* takes part in international relations in various ways. Its international division takes care of political relations with other states and within global institutions. The Ministry's civilian service works in the interest of Icelandic citizens abroad and addresses their safety and is ready to assist in case of accidents, illness or death. The Directorate of External Trade and Economic Affairs is proposed to enable Icelandic citizens, corporations and consumers to access global markets along with encouraging free trade. All of the above can be said to be in response to international rules and trade agenda, the European integration and global NGOs that directly influence citizens of Iceland and Icelandic corporations. The above are among the official reasons for running a foreign policy in Iceland.¹

What is the *de facto* point of running a foreign policy for a small country like Iceland? Why does it need embassies far away? These are common considerations in public debate in Iceland at present. Collapse of the three privately run banks, whose size had become ten times the size of the economy, was seen by some as a manifesto of globalization's bad influence on Iceland. Their growth was largely driven by activities abroad, such as indebted acquisitions and operating high-interest savings accounts for the public (most notably the Icesave high interest rate accounts online in UK and Netherlands).² Furthermore, many believed the collapse was partly due to imperfect EU legislation³ which in turn strengthened views that Iceland ought to stay outside of the European Union.⁴

The central question of this research is **“How has the foreign policy of Iceland changed as a consequence of the financial crisis that started in 2008?”** and which repercussions (good or bad) can be expected to follow these changes. One apparent change stems from budget cuts where the foreign affairs sector has had its share of cutbacks just like other sectors. In 2009, offices in Pretoria, Rome and Strasbourg were shut down and number of employees in New York, Paris, Vienna, New Delhi and Tokyo was reduced. This raises questions

¹ “Hlutverk,” Ministry for Foreign Affairs (Iceland), <http://www.utanrikisraduneyti.is/raduneytid/hlutverk/> (accessed 19 February 2011).

² Thomas L. Friedman, “The Great Iceland Meltdown,” *New York Times*, 18 October 2008, <http://www.nytimes.com/2008/10/19/opinion/19friedman.html> (accessed 5 March 2011). See also: Jon Danielsson, “Waking up to reality in Iceland,” *BBC News*, 26 January 2009, <http://news.bbc.co.uk/2/hi/europe/7852275.stm> (accessed 5 March 2011).

³ “Iceland warns EU over Icesave row,” *BBC News*, 4 February 2010, <http://news.bbc.co.uk/2/hi/europe/8497738.stm> (accessed 6 March 2011).

⁴ Eiríkur Bergmann, “Sense of Sovereignty,” *Stjórnsmál og stjórnarsýsla – veftímarit* 5, no. 2 (2009): 220-221, http://www.bifrost.is/Files/Skra_0038886.pdf (accessed 6 March, 2011).

about prioritizing, which factors decide that an office in Rome is closed rather than one in, say Ottawa?

Traditionally, the focal point of Icelandic foreign relations has been towards the other Nordic countries as they cooperate in numerous ways through multilateral agreements, institutions such as the Nordic Council and the Nordic Council of Ministers etc.

2. Methods

The main method for the following research will be secondary analysis of data collected by other researchers and from the news media. The data is both quantitative (e.g. from official statistics bureaus) and qualitative. An advantage of this method is that it saves time and expenses, so there is more time to analyze the data. Lack of familiarity with data can be a problem with this method, but there are pros and cons of every method in the social sciences.⁵

In order to research the purpose of running embassies abroad by the Icelandic state, I intend to use other methods as well. First I will derive theories from the existing literature on International Relations. Secondly I will use qualitative methods by interviewing a representative of the Icelandic Ministry for Foreign Affairs. His answers along with claims in public debate against running embassies will be the basis to critically observe existing theories and vice versa. Alan Bryman would presumably refer to this method as qualitative cross-sectional research design because it as such entails “Qualitative interviews or focus groups at a single point in time.”⁶ To begin with, my intention was to interview four or five ambassadors abroad, for that purpose I sent an e-mail to ten Icelandic embassies around the world. None of them replied but an employee of the Ministry in Iceland told me that some of them had contacted the Ministry head office regarding my request. Since some of the questions I intended to ask required personal opinion rather than being strictly limited to information as other questions, ambassadors did not want to participate.

The result was that I only interviewed the aforementioned civil servant by phone and beforehand he had seen the standard questions as he requested. Although this caused changes in the original plan, it is something that can be expected in *elite interviewing*⁷ as defined by Dexter (2006), where the respondent is treated as an expert on the topic. The aforementioned respondent from the Ministry claimed that as civil servants “usually they do not reveal their views on their own fields of work, but on the other hand they are able to explain current government policy”. He mentioned as an example that as bureaucrats working on behalf of the government, they would be careful when it comes to criticism towards their senior officers and the

⁵ Alan Bryman, *Social Research Methods* (New York: Oxford University Press, 2008): 295-300.

⁶ Alan Bryman, *Social Research Methods* (New York: Oxford University Press, 2008): 62.

⁷ Elite interviewee is **any** respondent who is given special, nonstandardized treatment, meaning that he is given the chance to define what is relevant, defining the situation and structuring the account of the situation. See: Lewis Anthony Dexter, *Elite and Specialized Interviewing* (Colchester, UK: ECPR Press, 2006): 19.

government in general.⁸ We then agreed that he could see the questions before the interview and thus gather information from the right places before answering the interview questions. The main implication of this method change is that instead of presenting views of several civil servants and analyzing them in the traditional way for opinion research, the interview will instead be used in the same way as the written references, mainly as a source of information. This I can conclude now that I have completed the interview and seen the answers, knowing that the respondent avoided stating any opinions and rather forwarded information he had gathered.

The interview guide used will be *semi-structured*, series of questions will be decided upon beforehand and but their order can be changed and more importantly questions can be added whenever the interviewer sees a reason to do so, for example to inquire further about a significant response.⁹ The interview will be conducted through telephone (Skype, to be precise) since that is the most convenient way to reach geographically dispersed respondents.¹⁰

In qualitative research, sampling is commonly not random as Burnham et al. (2004) point out and add that it is frequently seen as inappropriate. Rather, they suggest selecting cases with apparent relevance to the research question.¹¹ The reason for selecting this for the research that follows is that there is a stronger emphasis on gathering information, as opposed to public opinion polls where views are in focus. As this research will focus on changes in foreign policy as a result of the financial crisis in 2008, a logical source of information is civil servants since they are working in the affected surroundings.

As with other research methods, this one has its limitations. One is that inevitably the researcher interprets the information gathered and such interpretation varies between individuals. The exact accurate meaning of what was meant or said lies with each respondent and not with the researcher.¹² In addition, more than half of my written references for this research are in Icelandic and inevitably some details will be lost in translation.

The written references used are first of all, published materials from the Ministry for Foreign Affairs. Secondly, information was derived from the news media and whenever possible I used news published in English language, since that enables non-Icelandic speaking readers to look up the cited works if something is unclear.

⁸ Phone conversation with an employee of the Icelandic Ministry for Foreign Affairs, 18 March 2011.

⁹ Alan Bryman (2008): 196.

¹⁰ Alan Bryman (2008): 198.

¹¹ Peter Burnham et al., *Research Methods in Politics* (New York: Palgrave Macmillan, 2004): 157.

¹² Fiona Devine, "Qualitative Methods" in *Theory and Methods in Political Science*, ed. David Marsh and Gerry Stoker (New York: Palgrave Macmillan, 2002): 202 – 203.

Thirdly, academic literature is cited but it should be made clear right from the start that the available literature on Icelandic foreign policy is very limited. Two Icelandic scholars have published by far the largest number of articles and books on the subject, both of them mainly with regards to European integration. Baldur Thorhallsson, professor of Political Science at the University of Iceland, has also focused on small states in Europe in his research. Eiríkur Bergmann is a professor in political science at Bifrost University in Iceland and Director of its Centre for European Studies. He has written several books and articles on Iceland's foreign relations, mainly in a European context. Valur Ingimundarson is another scholar from the University of Iceland; an Associate Professor of History who has focused on security and defense with regards to Iceland-US relations and the NATO membership.

Data has been derived from the official Statistics bureaus in Scandinavia as mentioned in the beginning, where numerical data on foreign affairs has been compared between the Nordic states. *BBC News, the Guardian, Bloomberg* and other foreign media were used as applicable and should be able to reduce possible bias, especially in terms of writing about diplomatic rows between Iceland and the UK. *RÚV* (The Icelandic National Broadcasting Service) is most referred to of the Icelandic media, as I expect it to be more trustworthy than the majority of Icelandic media due to public service broadcasting regulations. Bias has increased within the Icelandic media after the crisis as some of the main actors of the collapse are competing for media power and write their own versions of history.

3. Theory

To set the framework for the following analysis there is a reason to clear out the basic ideas behind the subjects. Foreign policy is a main subject so theoretical ideas will be presented. First, some ideas on the objectives of foreign policy among states will be presented. These include traditional theories from international relations like neo-realism, neo-liberalism and social constructivism. These traditional theories are somewhat outdated in International Relations today though. Thus cosmopolitan power as presented by Gallarotti (2010) is taken into consideration as well. It should be made clear here that because of smallness; Iceland could never become a main global player in exercising hard power or engaging in arms race. Therefore realism in the traditional sense seems very irrelevant to explain Icelandic foreign policy.

3.1 Foreign policy and its objectives

Foreign policy in general can be seen as a state's decisions on how best to pursue its interests towards other states or the "international community" as a whole. These interests are pursued through a variety of subfields, such as economy, security and soft-power. Theoretical approaches differ in their stances as to which subfield is seen as most important; are states more interested in pursuing their own security or economic interests? Realists hold the position that states want to maximize power because of the security dilemma, while constructivists are more concerned with identity and identity creation among states. According to them a state's behavior is determined by socialization, interaction and learning among states.¹³

Sovereign states should not hesitate to throw out their resources to a joint pool and even surrender part of their sovereignty, if they believe in *neo-liberalism*. They should not do this without any reason though, an incentive would have to be there, such as integrated community to promote economic growth or respond to regional troubles. The European Union is an ideal example of this kind of institution; it started as a regional community promoting cooperation within coal and steel manufacturing. The experience from two world wars had sparked more liberal ideas of integration and community building as opposed to realist hard power strategies. Keohane and Nye added to the neo-liberalist school in the 1970s to include increased interdependence in global affairs. First, linkages had increased between states and non-state actors; secondly,

¹³ Derrick Frazier and Robert Stewart-ingersoll, "Regional powers and security: A framework to understanding order within regional security complexes," *European Journal of International Relations* 16, no.4 (2010): 740.

multiple channels of interaction among actors across national boundaries were recognized and thirdly, military force had declined as an instrument of statecraft.¹⁴

Neo-liberals assume that states are key actors in international relations but give weight to other actors as well. States are rational and look to maximize their interests in every issue-area. By cooperating they try to maximize absolute gains, they see value in cooperative behavior but are not so concerned with gains or advantages by other states cooperating. Cooperation is impossible without compromises, but states are likely to join international institutions if they see them as mutually beneficial and if they provide better opportunities for securing national interests. These are general benchmarks in spheres where states have mutual interests, such as in open trade. Other fields are not as well suited for mutual benefits, military and national security are an example, for in these someone's gain is perceived as someone's else's loss (zero-sum game).¹⁵

Cosmopolitan power recognizes that hard power alone is insufficient to explain the behavior of states in the international system. More importantly, it argues that changes in the international system have increased the relative importance of soft power. Gallarotti suggests that strategies combining hard and soft power are most likely to achieve the results wanted.¹⁶ Furthermore, he makes account of important differences between hard and soft power. Hard power is used to force nations to do what they otherwise would not do, while soft power aims at getting them to do voluntarily what the other nation wants them to do.¹⁷ Economic power is yet another category, which some have seen as subcategory under soft power but Gallarotti argues, is better suited under hard power because it can be used for bribery, ergo: making nations do what they otherwise would not do. On the contrary, foreign aid and investments are mentioned as reasons why economic power might be classified as subcategory under soft power. A state might hope for goodwill in some form in return for foreign aid for example.¹⁸

The rise of soft power relative to hard power can be traced to rise of the welfare state and democracy. Economic welfare maximization has become a target for governments because that helps them getting reelected for their posts. Foreign policy is affected by this trend, not only domestic policy and cooperation are

¹⁴ Steven L. Lamy, "Contemporary Mainstream Approaches: Neo-Realism and Neo-Liberalism," in *Globalization of World Politics: An Introduction to International Relations*, ed. J. Baylis and S. Smith, (New York: Oxford University Press, 2006), 213. See also: Robert Keohane and Josep Nye, "Power and Interdependence in the Information Age," *Foreign Affairs* 77, no. 5 (1998): 81-94.

¹⁵ Lamy 2006, "Contemporary Mainstream Approaches: Neo-Realism and Neo-Liberalism", 213-214.

¹⁶ Giulio M Gallarotti, *Cosmopolitan Power in International Relations* (New York: Cambridge University Press, 2010), 16.

¹⁷ Ibid. 23.

¹⁸ Ibid. 35.

used as means to reach prosperity and stability. On the contrary hard power policies risk compromising these goals. In addition, the rise of international organizations and regimes since World War II ended has seen nations participating in networks. These networks have grown with more members, which in turn has strengthened the norms and laws they represent. Unilateral actions disregarding these networks have subsequently become costlier, as a whole organized network is in the way instead of single nations here and there.¹⁹ With the ongoing War on Terror, relevance of soft power in foreign policy is higher than ever “if vicious circles of violence are to be avoided.”²⁰ A relevant example here stems from the recent US capture and killing of Osama Bin Laden, which provoked immediate ideas and announcements on revenge. Already now, avenge killings have started and there is more terrorism on the way if threats are to be taken seriously.²¹

Global information space, a concept used by Chong (2007), describes changes from the early 1990s where states have had to accept competition from various directions. Non-state actors have appeared on stage and exercise soft power in several forms: the internet, global capitalism and so on. New issues have emerged as part of transnational complications, migration, environmental degradation, energy shortages and arms proliferation to name a few. The non-state actors, such as Greenpeace or Amnesty International offer solutions that they claim are missing from the state actors’ side. What NGOs benefit from are small and flexible bureaucracies and shorter routing channels, not so common in state bureaucracies. NGOs can identify and respond to grass-roots needs but they lack accountability as they are not directly accountable to an electorate.²² NGOs represent one of many challengers to foreign affairs services, which consequently need to adapt and reassess their role. Globalization of various fields means that other ministries have also become challengers to some extent, prime ministers and their offices are for example increasingly involved in international and foreign policy matters.²³

¹⁹ Ibid. 41-42.

²⁰ Alan Chong, *Foreign Policy in Global Information Space* (New York: Palgrave Macmillan, 2007), 194.

²¹ “Pakistan: Troops end attack on Karachi naval air base,” *BBC News*, 23 May 2011, <http://www.bbc.co.uk/news/world-south-asia-13495127> (accessed 26 May 2011). See also: Tim Lister, “Eulogies and fury: Jihadists eager to avenge bin Laden’s death,” *CNN*, 12 May 2011, <http://edition.cnn.com/2011/WORLD/asiapcf/05/11/bin.laden.revenge/index.html> (accessed 26 May 2011).

²² Chong 2007, *Foreign Policy in Global Information Space*, 72-73.

²³ Stephan de Spiegeleire and Pertti Joenniemi, “The theory-policy nexus in the sphere of foreign and security policies,” in *The Academia and Foreign Policy Making: Bridging the Gap* (DIIS Working Paper 2011: 05), http://www.diis.dk/graphics/Publications/WP2011/WP_2011-05_Pertti_Joenniemi_The%20Academia%20and%20Foreign%20Pol_web.pdf (accessed 25 May 2011).

Social constructivism explores the networks of states or institutional structures and connection between state identities and interests vs. normative changes. To put it another way, it underscores how norms and identities can unveil and explain the behavior of states in international relations. Institutions are fluid because they change with the activities of states and other agents. ‘Institutions’ encompass more for constructivists than only actual organizations; they are in fact referring to a stable set or structure of identities and interests. Constructivists focus on institutions at the fundamental core of international society, e.g. international law, diplomacy and sovereignty. Human rights and sovereignty are examples of concepts that are founded on a human agreement, unlike spiders or waterfalls which exist regardless of human agreements.²⁴

The definition of power is broader for social constructivists than for e.g. neo-realists, not only meaning the ability to get another actor to do what he otherwise would not do but also as the creation of identities and interests which limit their ability to manage their fate. Identity is always formed in relationship with others; it cannot exist in a vacuum. Identities can thus and do change through interactions with others. According to constructivists, identities shape interests meaning that we know what we want if we know who we are. Normative structures refer to collectively held ideas, such as rules and beliefs (for example sovereignty or human rights) that construct categories of meaning and define standards of appropriate conduct. Actors with a given identity are expected to behave according to their norms, the norms are followed because of costs and benefits of doing so and as they relate to a sense of self.²⁵

3.2 Small states in international relations

International Relations is primarily focused on “great powers”, clear examples are U.S. and its hegemony and the BRIC countries and their economic and political rise in modern times. But small states have increased in numbers and so has their impact on the international system, if we are to believe Christos Kassimeris who also mentions a definition of small member states by the European Union as the ones with population below 40 million. Population is the indicator when votes are distributed within the EU; larger population corresponds to more votes within its bodies, meaning more influence on decision-making.²⁶ The definition of a small state is debated though, since there are scholars who complicate things by bringing in concepts like “micro states” and “middle powers”. Gstöhl and Neumann suggest that micro states should be classified as those who:

²⁴ Martin Griffiths and Terry O. Callaghan, *International Relations: The Key Concepts* (New York: Routledge, 2008), 51-52. See also: Michael Barnett, “Social constructivism,” in *The Globalization of World Politics*, ed. J. Baylis and S. Smith (New York: Oxford University Press, 2006), 258 – 263.

²⁵ Barnett 2006, “Social constructivism,” 264-267.

²⁶ Christos Kassimeris, “Foreign Policy of Small Powers,” *International Politics* 46, no. 1 (2009): 88.

1. claim to maintain effective sovereignty on a territory but whose claims are questioned by other states
2. cannot uphold a *minimum* (as defined by larger states) required presence in the global society of states as a consequence of limited resources. This presence would e.g. be in the form of membership in international organizations and running embassies in key capitals.²⁷

They mention Costa Rica in the interwar era as an example, when it discontinued its membership of the League of Nations concluding that they could not afford it, and thus it went from being a small state into being a micro state. Their argument is then that it is not absence from international society per se that makes a given state micro state, but if the solemn or main reason for its absence is lack of resources, this given state falls into the micro state category.²⁸ Thorhallsson and Wivel provide a somewhat easy way out from this jungle of categories by mentioning the simplest way of defining small states; they are the ones who are not great powers.

Differentiating small EU member states from big ones can be done across various categories; population size, influence on the integration process and corresponding institutions and how these states view their own role and power in the union. Furthermore, states can be weak in one sphere, while strong in another – small states are commonly weak in terms of security policy to name an example, implications for an institution like NATO would be enormous if the U.S. decided to withdraw from the organization, while Estonia's departure would presumably not affect NATO significantly. Thus, small states prioritize between policy areas within international cooperation apparatuses like EU, being proactive in fields of strong interest to them while reactive in spheres of limited interest. To explain the difference, small states pursue their own interests in the areas concerned but keep quiet (or comply with) on other issues where they do not have direct interests. The large states, on the other hand, systematically try to prevent decisions that are favorable to other states but do not concern their interests directly. An example of this is that the large states want to downsize the Common Agricultural Policy and the Regional Policy, neither of which the large states benefit from themselves.²⁹

²⁷ I.B. Neumann and S. Gstöhl, "Introduction" in *Small States in International Relations*, ed. Ingebritsen et al. (Seattle: University of Washington Press, 2004), 6-7.

²⁸ I.B. Neumann and S. Gstöhl, "Introduction" in *Small States in International Relations*, ed. Ingebritsen et al. (Seattle: University of Washington Press, 2004), 7.

²⁹ Baldur Thorhallsson and Anders Wivel, "Small States in the European Union: What do We Know and What Would We Like to Know?," *Cambridge Review of International Affairs* 19, no.4 (2006): 653 – 654 and 659.

Certain procedures within the EU may sound appealing to small states. One is the rotating presidency, another is the voting power (where e.g. qualified majority voting misrepresents size of population) and a third is over-representation in the European Parliament.³⁰

Why should small states join alliances? Reiter (2001) suggests that they do it to be safe from big states. European countries see membership of NATO as a platform to lower their own military expenditure. But he subsequently raises the question whether small states can pursue their security interests within an alliance and what their influence is in alliances. His own answer to that question is that small states now have influence within these alliances, but again it should be underlined that he is referring to security interests in general and specifically NATO. Implications of that are minor however, since larger entities have taken over in modernity and European interests are on the agenda rather than specific national interests in this regard. The small state cannot do anything on its own but in company of others there are possibilities for it.³¹

Small states have increased opportunities today as compared to the past to expand their sphere of influence, through collaboration such as the EU, where they join forces with other states in a mission to pursue common interests. Additionally, international organizations can influence a state's foreign policy, for example if one state finds that its interests differ from the majority within such an organization. Although a common reason why they join such organization must be to exert their influence, in instances they will be pressured by their allies when they fail to comply (their interests differ from the majority's interests).³²

³⁰ Kassimeris 2009, "Foreign Policy of Small Powers," 96.

³¹ Erich Reiter, "Introductory Comments on the Objective of the Small States and Alliances Workshop," in *Small States and Alliances*, ed. Erich Reiter and Heinz Gartner (Heidelberg: Physica-Verlag, 2001), 12 – 13.

³² Kassimeris 2009, "Foreign Policy of Small Powers," 91 and 95.

4. Analysis

In the following subchapters the current situation as well as historical developments in foreign policy of Iceland will be explained and discussed. The theoretical framework presented above will then be weighed against developments in Icelandic foreign policy before and after the crisis as applicable. To begin with a background or overview of Icelandic foreign affairs historically and currently is presented in addition to a brief comparison with the other Nordic foreign affairs services. After that, an account is made of budget cuts after the crisis which should give a sense of priorities within Icelandic Foreign policy. In chapter 4.3 allies of Iceland in the global community before and after the crisis are introduced with and “enemies” are also given mention. These so called enemies are hopefully only temporary, because Iceland will want to keep their recent record of 1st place in Global Peace Index as the world’s most peaceful country.³³ Chapter 4.4 is devoted to the diplomatic missions and projects abroad, which constitute the most expensive field within the foreign policy. Chapter 4.5 makes a short account of defense and national security, an issue area heavily affected by recent cutbacks. Among the current high priorities of the Ministry for Foreign Affairs is following up on the application for membership of the European Union, as will be discussed in chapter 4.6. Last but not least is a chapter on the president which has shaped the foreign policy after the crisis, by acting against the policy agreed by the parliament, *Althingi*.

4.1 Background

As the world has become ever more interconnected, Iceland has followed suit. The size of the country has the implications that it will never be a major actor such as US or China, but finding the right partners is all the more important in order to pursue national interests. Iceland has been an independent state for a relatively short time and key points in its foreign relations since then are identified on the Ministry for Foreign Affairs (MFA) website. Although Iceland became a sovereign state in 1918, Denmark still pursued its foreign policy on behalf of the government of Iceland until 1940, when Iceland fully took control of its own foreign affairs and the MFA was established.³⁴

The first embassy was opened during this era, in the year 1920 and maybe unsurprisingly in Denmark. Twenty years later, when Iceland had fully overtaken its foreign affairs embassies were opened in London and

³³ Simon Rogers, “Global peace index 2011: the full list,” *The Guardian*, 25 May 2011, <http://www.guardian.co.uk/news/datablog/2011/may/25/global-peace-index-2011> (accessed 28 May 2011).

³⁴ “Sögulegt yfirlit um utanríkisþjónustuna,” Ministry for Foreign Affairs (Iceland), <http://www.utanrikisraduneyti.is/raduneytid/sogulegt-yfirlit/> (accessed on 29 March 2011)

Stockholm, followed by openings in Washington in 1941 and in Moscow in 1944. The government signed a treaty with the U.S. in 1941 on securing the defense of Iceland militarily, recognizing its sovereignty, providing food security during World War II (making sure necessities would be available) and securing international voyage. Between 1948 and 1953 Iceland was one of the recipients of Marshall Aid from the United States.³⁵

As the above indicates, ties have been strong with Denmark and the U.S. from the very beginning of official foreign relations of Iceland. The U.S. naval air station that was part of a long lasting agreement between the two states was closed by the U.S. government in 2006 with their unilateral decision. It symbolized declining geopolitical and strategic significance of Iceland, which had been at its peak during the Cold War.³⁶ Although this was seen by some as a knock to the diplomatic relations, ties with the U.S. are still strong; there is still a defense agreement in effect with the U.S. although the army left. Secondly, U.S. has been among the biggest trading partners for many years.³⁷

The link with Denmark appears in many areas; Danish is taught as part of compulsory education in the Icelandic education system and starts in 7th grade of primary school (when pupils are 13 years old) and finishes after second year of secondary school.³⁸ The largest share of Icelandic students, who go for higher education abroad select Denmark, in 2006 for example 48% of Icelandic university students abroad were in Denmark while U.S. hosted the second most (13,2%).³⁹ Ties with the other Nordic countries have also been strong through the years. Their co-operation builds first and foremost on common values and intertwined histories. Formal co-operation began with the establishment of the Nordic Council in 1952, while the Nordic Council of Ministers was established in 1971. The former encompasses co-operation between the parliaments of the countries,

³⁵ "Sögulegt yfirlit um utanríkisþjónustuna," Ministry for Foreign Affairs, <http://www.utanrikisraduneyti.is/raduneytid/sogulegt-yfirlit/> (accessed 29 March 2011)

³⁶ Valur Ingimundarson, "Iceland's Post-American Security Policy, Russian Geopolitics and the Arctic Question," *Rusi Journal* 154, no. 4 (2009): 74.

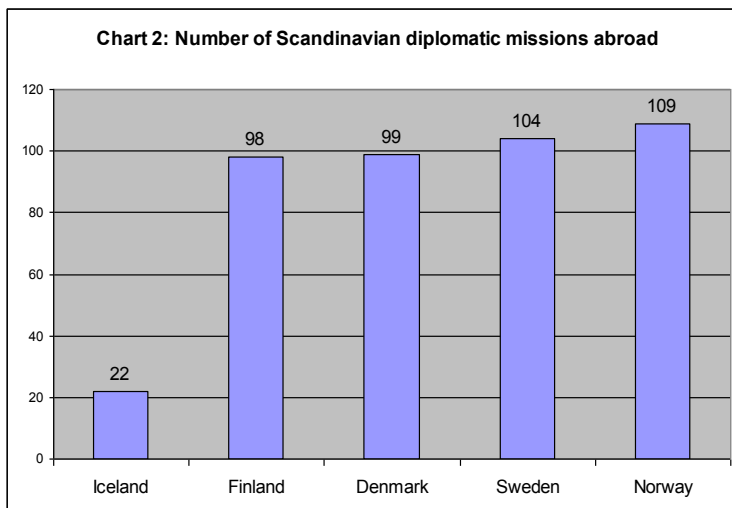
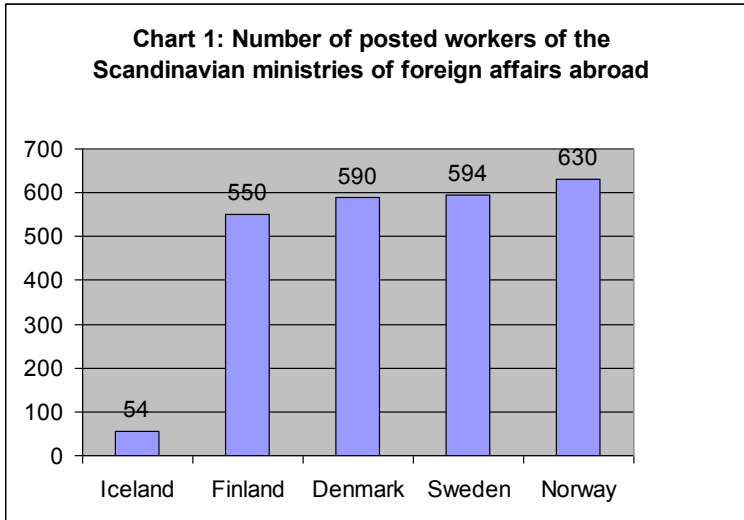
³⁷ "Hagtiðindi (Statistical Series)," Statistics Iceland, 1 (2010), <https://hagstofa.is/lisalib/getfile.aspx?ItemID=10859> (accessed 4 April 2011).

³⁸ "Aðalnámskrá grunnskóla: Erlend tungumál," Ministry of Education, Science and Culture, 2007, <http://brunnur.stjr.is/mrn/utgafuskra/utgafa.nsf/SearchResult.xsp?documentId=F5949715D52DECA1002576F00058DC5B&action=openDocument> (accessed on 5 April 2011). See also: "Aðalnámskrá framhaldsskóla: erlend tungumál 1999," Ministry of Education, Science and Culture, 1999, <http://brunnur.stjr.is/mrn/utgafuskra/utgafa.nsf/SearchResult.xsp?documentId=96EA121AF8F7775D002576F00058D4CB&action=openDocument> (accessed 5 April 2011).

³⁹ "Skólasókn í framhaldsskólum og háskólum haustið 2006," Statistics Iceland, 1 June 2007, <http://www.hagstofa.is/?PageID=95&NewsID=2461> (accessed 5 April 2011). It should be noted that these figures only include students that received loans from the Icelandic Student Loan Fund. Statistics from other countries have shown that the number of Icelandic students abroad is higher and these figures underestimate the number most significantly in the Nordic countries.

while the latter is a forum for the Nordic governments. Other areas of collaboration include the Nordvision (TV association) and for example research, the environment, welfare and culture.⁴⁰

The Icelandic foreign-affairs service is small in comparison with other Scandinavian states. The following charts come from a response by the Minister for Foreign Affairs to an inquiry made by another MP in the parliament, *Althingi*⁴¹:



⁴⁰ "Nordic Co-operation," Norden, <http://www.norden.org/en/about-nordic-co-operation/nordic-co-operation> (accessed 5 April 2011).

⁴¹ Össur Skarphéðinsson, Minister of Foreign Affairs reply to an inquiry by MP Björn Valur Gíslason, 6 December 2010, <http://www.althingi.is/alttext/139/s/0374.html> (accessed 13 May 2011).

As evident, Iceland has by far the fewest diplomatic missions and employees abroad of the Scandinavian states. Iceland also has by far the smallest population, of only 318,452.⁴² Taking account of population, there is one diplomatic mission for every 14,475 people living in Iceland. Finland has a population of 5,375,276⁴³ meaning that there is one diplomatic mission for every 54,849 residents in Finland. In Denmark there are 56,168 residents for every embassy, 90,534 in Sweden⁴⁴ and 45,140 in Norway.⁴⁵ By using this comparison method, Iceland has relatively many embassies abroad. However, on the yearly state budget 2010, appropriations to foreign affairs account for a lower share of the total spending than in the other Nordic countries as will be shown in next chapter.

4.2 Budget cuts

In public discourse on cutbacks following the crisis, a common position is to compare expenditures on health care to expenditures on foreign affairs. *T24*, described as “a platform for opinions and ideas of right wing people”, refers to plans in state budget to cut down spending on health care in the countryside (meaning outside the capital area) by 2.9 billion Icelandic krona (ISK). Expenditure on foreign affairs is brought up in the same context: “At the same time we are going to maintain a foreign affairs service that will cost around ISK 11 billion. Thereof embassies and standing committees will cost ISK 2,675 million.” The author goes on to suggest closing the embassies in India, Japan, Canada, Sweden, Finland, France, Austria and Britain and thereby save ISK 766 million or 26% of the planned cutbacks for health care in the countryside.⁴⁶

All of the ministries under the Icelandic state have had to accept budgetary cuts as a result of the economic crisis. The MFA has had its share of these, with 26% in 2009, 16.6% in 2010 and 10.2% in 2011. The Ministry’s employee also pointed out that budget appropriations to foreign affairs (incl. appropriations to development and in aggregate the ministry plus embassies) in Iceland are the lowest in Scandinavia, 2.12 % of the total state

⁴² “Mannfjöldi 1. janúar 2011,” Statistics Iceland, 8 February 2011, <http://hagstofa.is/Pages/95?NewsID=5650> (accessed 13 May 2011).

⁴³ “Population by age group, end-2010,” Statistics Finland, 22 March 2011, http://www.stat.fi/tup/suoluk/suoluk_vaesto_en.html (accessed 13 May 2011).

⁴⁴ “Sweden’s Population by sex and age on 31/12/2010,” Statistics Sweden, 18 February 2011, http://www.scb.se/Pages/TableAndChart____264373.aspx (accessed 13 May 2011).

⁴⁵ “More men than women for first time,” Statistics Norway, 11 March 2011, http://www.ssb.no/folkemengde_en/ (accessed 13 May 2011).

⁴⁶ “Heilbrigðisþjónusta og sendiráð,” *T24*, 16 October 2010, <http://www.t24.is/?gluggi=grein&tegund=pistill&id=4753> (accessed 12 May 2011).

budget. Sweden and Norway have 3.63% and 3.88% respectively, while Finland has 2.37 % and Denmark 2.34%.⁴⁷

A few diplomatic missions have been closed since the bank collapse and the number of employees has been decreased elsewhere abroad, consequently workload on the remaining staff of the Ministry has increased. The interviewee said that Iceland has few embassies (understandably as a small nation) and that it was vital to have them in key locations and that they are in operable condition, "...if you make too radical cutbacks in an embassy...it will not be able to meet its obligations and that raises the question if it couldn't just as well be closed." he explained.⁴⁸ The embassies closed were in Pretoria, Rome and Strasbourg and the number of employees was reduced in New Delhi, Paris, New York, Vienna and Tokyo. In addition, cutbacks for the Icelandic International Development Agency (subsidiary organ under the Ministry) meant that their offices in Sri Lanka, Nicaragua and Namibia were closed. Cooperation with the two former turned out to be short lived, as it only began with Sri Lanka in 2005 and 2006 with Nicaragua. Namibian cooperation was a different story, stretching back to 1990 (when Namibia got sovereignty) it evolved around fisheries, marine research and fishing management in the beginning. During the last few years there had mainly been social projects, such as supporting periphery groups of the society, including deaf and an indigenous people known as Himba.⁴⁹

Travelling costs have been reduced and so have salaries in the Ministry. Since 2006 the number of posted workers abroad has been reduced by 19%.⁵⁰ Currently, the diplomatic missions are running on minimum workforce according to the Minister of Foreign Affairs, especially considering that they have taken over assignments from shut down offices. Rationalization has also been achieved by increasing use of teleconferencing equipment and by assigning employees abroad to attend meetings in place of specialists located in Iceland. These employees already have a lot to do and there are limits to the extent which they can replace specialists at meetings.⁵¹ Immense reduction of representatives of various ministries of the Icelandic government in Brussels means that chances of influencing EEA decisions according to Icelandic interests have gone down. Current non-presence of many ministries means that they do not get first hand information or act

⁴⁷ Interview with an employee of the Icelandic Ministry of Foreign Affairs, 20 March 2011.

⁴⁸ Ibid.

⁴⁹ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2010, p. 73, <http://www.althingi.is/altext/138/s/pdf/1070.pdf> (accessed 13 May 2011). See also: "Namibia," Icelandic Development Agency, <http://www.iceida.is/samstarfslond-og-verkefni/namibia> (accessed 15 May 2011).

⁵⁰ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2011, p. 94, <http://www.althingi.is/altext/139/s/pdf/1416.pdf> (accessed 17 May 2011).

⁵¹ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2010, p. 94, <http://www.althingi.is/altext/138/s/pdf/1070.pdf> (accessed 13 May 2011).

right away when changes are made.⁵² In the 2011 budget for the MFA, it can be seen that the embassies account for more than one fourth (28 %) of the total allotted to the policy area while the most costly part of the budget is participation in global institutions (30 %).⁵³

Established under the Ministry for Foreign Affairs on the 1st of June 2008, The Icelandic Defence Agency was abolished on January 1, 2011. The agency worked with defense related projects; running the Icelandic air defense system and the Icelandic Radar Agency, that the Icelandic government overtook from the United States in 2007. The estimated amount of staff needed for this institution at its establishment was up to fifty, but after it was closed most of the staff was offered placements at other institutions overtaking the day-to-day operation, such as the National Commissioner of the Icelandic Police and the Icelandic Coast Guard.⁵⁴

4.3 Allies before and after crisis

This chapter is directed towards defining the main allies of Iceland through the years and which changes occurred with the crisis. Not all bilateral relationships will be made account of as that would be too extensive for this paper, the idea is to give a brief historical view of the bilateral relationships mentioned. Canada is among the strong allies, rooting back to migration of thousands of Icelanders to Canada between 1874 and 1914. Currently Canada has the largest population of people of Icelandic descent living outside of Iceland, around 89,000 (2008). Bilateral free trade agreement is in effect between Canada and Iceland through EFTA since 2007.⁵⁵ Changes were not apparent in the relationship between Iceland and Canada after the crisis so this brief introduction will have to do, although a whole thesis and more than that could be written on relations between these countries.

The strongest allies of Iceland through the years have been the neighboring Nordic countries and the U.S. This is due to historical and cultural ties in the case of Scandinavia, while the ties with the U.S. can be said to stem primarily from the army base that was part of their Cold War strategy. Iceland benefited from this strategy for

⁵² Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2011, p. 77, <http://www.althingi.is/alttext/139/s/pdf/1416.pdf> (accessed 17 May 2011).

⁵³ *Ibid.* 96.

⁵⁴ "Stofnun Varnarmálastofnunar," Ministry for Foreign Affairs, 1 June 2008, <http://www.utanrikisraduneyti.is/frettir/nr/4315> (accessed 1 May 2011). See also: The Icelandic Defence Agency's website, <http://www.vmsi.is> (accessed 1 May 2011); and "Varnarmálastofnun lögð niður," *RÚV*, 30 March 2010, <http://www.ruv.is/frett/varnarmalastofnun-logd-nidur> (accessed 1 May 2011).

⁵⁵ Sarah Barmak, "A picture and a thousand words," *The Star*, 13 April 2008, <http://www.thestar.com/News/Ideas/article/413961> (accessed 26 May 2011). See also: "Canada signs first free trade deal since 2001," *CBC News*, 7 June 2007, <http://www.cbc.ca/news/canada/story/2007/06/07/freetradedeal.html> (accessed 26 May 2011).

decades, but the U.S. government withdrew their defense force from Iceland as priorities in U.S. defense affairs had shifted to other regions of the world, such as Afghanistan and Iraq. Security relationship with the U.S. was not over though, but weakened since in-country presence was history. In order to fill in the security gap, the Icelandic government sealed agreements with the UK, Denmark and Norway, fellow members of NATO on air policing. An air policing mission by Britain scheduled for December 2008 was canceled though, as an early evidence of a diplomatic row between Iceland and Britain emerged. Icelandic NATO representatives protested against Britain's decision to use anti-terrorist legislation as a weapon to freeze assets and take over an Icelandic bank in London. The British government explained its action by referring to national security and necessity of stability in the UK financial system. Bottom line, what had been decided to respond to defense needs, was canceled because of an unrelated economic issue of a privately run bank, spillover between fields in relations between the two states.⁵⁶ Social constructivism seems like the theory best able to explain this scenario, Britain had obtained a negative identity seen from an Icelandic viewpoint through interaction during the bank collapse. The anti-terrorist legislation used by UK to freeze Icelandic assets in particular provoked anger both amongst politicians and large shares of the public. Based on that, the government was hardly in a position to accept air policing from the UK at the time as it would risk having the electorate up against them, although the issue was unrelated to the crisis. This could also be seen as a use of soft power, Iceland trying to use diplomatic peaceful ways to express mistrust towards British authorities. It is hard to see that this decision by the Icelandic government had any effects on the Icesave dispute; the British authorities would hardly have seen air policing in Iceland as such a large matter of interest.

The Faroe Islands are the only Nordic state that is smaller than Iceland, with a population of 48,589 in March 2011.⁵⁷ However, they were the first state to offer a helping hand when crisis hit Iceland by presenting a loan of DKK 300 million already at the end of October 2008, with repayments to start five years later and interest rates on level with what the Faroese state government pays on their own loans.⁵⁸ Both being nations of fisheries the states renew their bilateral agreement on fishing every year, permitting fishing of selected species of fish within each others jurisdiction. The Faroe Islands have for a long time been an important market for Icelandic

⁵⁶ Ingimundarson 2009, "Iceland's Post-American Security Policy, Russian Geopolitics and the Arctic Question," 74-76.

⁵⁷ "Fólkatalið vaks við 40 fólku í februar," Statistics Faroe Islands, 1 March 2011, http://www.hagstova.fo/portal/page/portal/HAGSTOVAN/Hagstova_Foroya/news_repos/%CDB%FAgvar%201.%20mar.%202011 (accessed 11 May 2011).

⁵⁸ "Færeyingar bjóða Íslendingum aðstoð sína," Prime Minister's Office (Iceland), 29 October 2008, <http://www.forsaetisraduneyti.is/frettir/nr/3122> (accessed 11 May 2011). See also: "Undirritun viljayfirlýsingar um lán frá færeysku landsstjórninni," Ministry of Finance (Iceland), 18 November 2008, <http://www.fjarmalaraduneyti.is/frettatilkynningar/2008/11/18/nr/11529> (accessed 11 May 2011).

lamb as well.⁵⁹ Iceland's Arctic policy aims at securing its interests with regards to climate change, environment, natural resources and navigation amongst other things. Part of this policy is to strengthen cooperation with the Faroe Islands and Greenland regarding trade, energy, use of resources and tourism.⁶⁰

Four bigger Nordic countries jointly provided an additional loan of Euro 1.8 million. These were Norway, Sweden, Denmark and Finland and the loan supposed to increase the currency reserves and to support the plan by Iceland and IMF on establishing stability and improvements in the Icelandic economy.⁶¹

The current minister of foreign affairs, Ossur Skarphedinsson, wrote an article in the newspaper *Frettabladid* at the end of April 2011, where he describes Iceland's relations with India and begins by stating that "India is among those states that traditionally have served us well." He then mentions their support during the Cod Wars (in the 1970s and earlier) between Iceland and Britain, when Iceland expanded its fisheries jurisdiction. When the Icelandic government undertook a recovery program monitored by the International Monetary Fund (IMF), India supported the initiative and so did Japan within the board of the fund.⁶²

Iceland opened an embassy in the capital of India in 2006 and India opened an embassy in Reykjavik, Iceland a year later.⁶³ Relations have increased in recent years and Iceland's increased interest in India is evident, it was the first Nordic state to publicly announce support for India's bid for a permanent seat at the UN Security Council and "has been generally supportive of India's cause at the UN fora".⁶⁴ During the recent official visit of the Icelandic Minister of Foreign Affairs to India, he opened a new Icelandic consular office in Mumbai, founded on ideas about increased trade collaboration between the states in e.g. geothermal energy and fisheries.⁶⁵ This is the first new consular office established after the crisis in 2008.

⁵⁹ "Ísland og Færeyjar," Iceland.org, <http://www.iceland.org/fo/islenska/adalraedisskrifstofan/island-og-faereyjar/> (accessed 11 May 2011).

⁶⁰ "A Parliamentary Resolution on Iceland's Arctic Policy," approved by Althingi 28 March 2011, <http://www.mfa.is/media/nordurlandaskrifstofa/A-Parliamentary-Resolution-on-ICE-Arctic-Policy-approved-by-Althingi.pdf> (accessed 12 May 2011).

⁶¹ "321 milljarðs króna lán," *RÚV*, 1 July 2009, <http://www.ruv.is/frett/321-milljards-krona-lan> (accessed 11 May 2011).

⁶² Össur Skarphéðinsson, "Indversk-íslenska skapalónið" *Fréttablaðið*, April 26 2011. See also: John S. Dryzek and Susan Hunter, "Environmental Mediation for International Problems," *International Studies Quarterly* 31, no.1 (1987): 88; and Interview with an employee of the Icelandic Ministry for Foreign Affairs, 20 March 2011.

⁶³ "Opnaði nýtt sendiráð á Indlandi," *Visir.is*, 26 February 2006, <http://visir.is/opnadi-nytt-sendirad-a-indlandi/article/200660226037> (accessed 4 May 2011). See also: "Indverskt sendiráð," *Morgunblaðið*, 11 August 2007.

⁶⁴ "India-Iceland Relations," Ministry of External Affairs (India), February 2011, <http://meaindia.nic.in/meaxpsite/foreignrelation/iceland.pdf> (accessed 4 May 2011).

⁶⁵ "Utánríkisráðherra opnar ræðisskrifstofu í Mumbai og fundar með ráðamönnum í Maharastra," Ministry for Foreign Affairs, 1 May 2011, <http://www.utanrikisraduneyti.is/frettir/nr/6265> (accessed 4 May 2011).

Japan is another faraway state to be considered an ally by the Icelandic authorities. They were the first state to announce their support to the IMF recovery program which Iceland sought and declared that they would contribute to that financially.⁶⁶ Diplomatic relations with Japan stretch back to 1956 but an embassy was opened there in 2001. Cultural relations between the countries are highlighted by the MFA. These relations have grown rapidly in recent years, as apparent by language teaching: Japanese at the University of Iceland and Icelandic at Waseda University in Tokyo. Both programs have been well attended. Bilateral agreements in other fields have also been made between universities in the two states. Icelandic musicians *Sigur Ros* and *Bjork* are among names that have held big concerts in Japan.⁶⁷ Just as with India, cooperation within geothermal energy is on the agenda and has in fact been ongoing for some time.⁶⁸

Poland has been linked to Iceland for many years through the influx of immigrants from Poland moving to Iceland for job opportunities. At the beginning of this year (2011), Polish immigrants in Iceland were 9463, which made them by far the largest immigrant group in the country, or 36.8% of all immigrants.⁶⁹ A year after the bank collapse, in October 2009 a contract was signed between the two states for Poland to lend Iceland USD 200 million, which was an addition to the loan of USD 2.1 billion lent by the IMF.⁷⁰

The main allies after the financial crisis have been mentioned above. Diplomatically, enemies have also appeared in what has been a long and winding diplomatic dispute about who should be held responsible for the collapse of Icelandic banks in Britain and the Netherlands respectively, more specifically who should pay back vast sums of money lost by British and Dutch savings accounts holders in Icelandic bank *Landsbanki*. The British and Dutch governments have held the view that Icelandic taxpayers should pay back the sums, while the Icelandic government under pressure from an angry public has attempted to decrease responsibility for this debt rooted in privately run banks. The resistance from Iceland caused the UK and the Netherlands to block Iceland's attempts to get financial assistance from the International Monetary Fund (IMF). A settlement on repayments approved by the parliament, *Althingi*, stranded when the President refused to ratify it and sent it

⁶⁶ Interview with an employee of the Icelandic Ministry of Foreign Affairs, 20 March 2011.

⁶⁷ "Cultural Relations," Iceland.org, <http://www.iceland.org/jp/english/the-embassy/cultural-relations/> (accessed 20 May 2011).

⁶⁸ "Japan-Iceland Geothermal Forum November 16 2010," Ministry for Foreign Affairs, <http://www.mfa.is/speeches-and-articles/nr/6020> (accessed 20 May 2011).

⁶⁹ "Innflytjendur 1.janúar 2011," Statistics Iceland, 15 March 2011, <http://www.hagstofa.is/Pages/95?NewsID=5679> (accessed 9 May 2011).

⁷⁰ "Sameiginleg fréttatilkynning frá fjármálaráðuneyti Póllands og fjármálaráðuneyti Íslands," Ministry of Finance, 4 October 2009, <http://www.fjarmalaraduneyti.is/frettir/frettatilkynningar/frettatilkynningar/nr/12560> (accessed 9 May 2011).

to a national referendum where it was strongly turned down by the public with 93 % of the votes cast. Again the Icelandic government had to send out its representatives in an attempt to settle a new agreement on repayments with representatives of the UK and the Netherlands. After months of negotiations, a new settlement was reached that was a far better result for Iceland in terms of lower interest rates and a far longer repayment period on the Euro 4 billion at stake. Althingi ratified the new agreement, but as earlier the president decided not to ratify and thus forwarded it to a referendum, where it was rejected just as the previous agreement, this time 58 % voted “no”. Icelandic Finance minister Steingrímur Sigfússon ruled out a third attempt to settle the issue through negotiations and both the UK Treasury minister Danny Alexander and Dutch Finance minister Jan Kees de Jager concluded that this second referendum result meant that the issue would presumably end up in international court. These views were not surprising given that the issue was unresolved in spite of around two years of precious time used (or wasted) on negotiating a settlement.⁷¹

Some have feared that Britain and Holland are likely to veto Icelandic membership of the EU because of this reluctance of the small state to comply with their demands. In addition, the dispute has raised doubts about the membership application and MPs from all parties in parliament except the Social Democratic Alliance formally suggested withdrawal of the application in June 2010, nonetheless this motion did not gain majority support in the parliament and was turned down. Figures of doubt amongst the public had also risen sharply according to Gallup opinion polls in July 2010, 60 % were opposed to membership and only 26 % in favor. Two years earlier 50 % of respondents had been supportive of membership and 32 % opposed. The remaining shares in these two polls did not state an opinion.⁷²

On 19 May 2011, the Resolution Committee and the Winding-Up board of the old Landsbanki (labeled “old” to differentiate the privately run bank before crisis from the “new” Landsbanki, owned by the state after the takeover in 2008) held a creditors meeting, where they declared that based on a fixed Icelandic krona (ISK) exchange rate as of 22 April 2009 recoveries were estimated to amount to ISK 1300 billion, or 99 % of the book value of priority claims (the Icesave deposits and wholesale deposits) as of the same date. If recoveries are

⁷¹ Baldur Thorhallsson and Christian Rebhan, “Iceland’s Economic Crash and Integration Takeoff: An End to European Union Scepticism?,” *Scandinavian Political Studies* 34, no. 1 (2011): 58. See also: “UK ‘disappointment’ as Iceland rejects repayment deal,” *BBC News*, 10 April 2011, <http://www.bbc.co.uk/news/world-europe-13022524> (accessed 8 May 2011).

⁷² Baldur Thorhallsson and Christian Rebhan, “Iceland’s Economic Crash and Integration Takeoff: An End to European Union Scepticism?,” *Scandinavian Political Studies* 34, no. 1 (2011): 58 – 59. See also: Opinion polls conducted by *Capacent Gallup* in July 2010, <http://capacent.is/Frettir-og-frodleikur/Thjodarpulsinn/Thjodarpulsinn/2010/07/06/Vidhorf-til-Evropusambandsadildar-Islands/> and in August 2008, <http://www.si.is/media/alhjudlegt-samstarf/2008-08-ESB-almenningur.pdf> (accessed 8 May 2011).

based on ISK exchange rate on 31 March 2011 (quarterly reference date), the estimated recovery is 1,245 billion meaning around 94 % of the book value priority claims.⁷³

Another dispute with the UK is absolutely unrelated to *Icesave* but happens to occur at the same time, but evolves around fish like the Cod wars in the 1970s. This one is about mackerel and started when the Icelandic government raised its mackerel quota from 2,000 tons to 130,000 tons in 2010, since mackerel has in recent years been swimming in Icelandic territory a lot more than it used to. The mackerel does this as a response to global warming, when its usual natural habitat gets too warm it moves up north to find ideal conditions.⁷⁴ UK Fisheries Minister Richard Benyon stated in August 2010: “The UK Government is taking the actions of Iceland and the Faroes very seriously. They are behaving irresponsibly and are undermining the sustainability of the stock on which our fishermen depend, which is in no one’s interests.” The Icelandic Fisheries minister on the other hand claimed: “I think we’re taking from the stock what we deserve, according to estimates on the mackerel stock surrounding Iceland.”⁷⁵ The 2010 mackerel quota was in addition three times more than EU considered reasonable. Some have suggested this could put a string in Iceland’s EU membership negotiations, like Struan Stevenson, the senior vice-president on the European Parliament’s fisheries committee, who said⁷⁶:

“Here is a nation coming to the table to become a member of EU. Yet, what have they given us? A volcanic ash cloud; financial problems with their referendum and refusing to pay debts they owe Britain; and how they are acting in this extraordinarily aggressive fashion over fish stocks. What they are doing is effectively illegal, unreported, unregulated fishing.”

⁷³ “Creditors meeting,” Landsbanki Íslands hf, Resolution Committee – Winding-up Board, 19 May 2011, <http://www.lbi.is/Home/News/News-Item/2011/05/19/Creditors-meeting/> (accessed 19 May 2011).

⁷⁴ Martin Hickman, “Now Britain and Iceland go to war over the mackerel,” *The Independent*, 11 August 2010, <http://www.independent.co.uk/news/world/europe/now-britain-and-iceland-go-to-war-over-the-mackerel-2049099.html> (accessed 12 May 2011).

⁷⁵ Andrew McFarlane, “Why is Britain brace for a mackerel war?,” *BBC News Magazine*, 24 August 2010, <http://www.bbc.co.uk/news/magazine-11062674> (accessed 12 May 2011). See also: Omar R. Valdimarsson, “Iceland Says it ‘Deserves’ to Catch More Mackerel as U.K. Dispute Deepens,” *Bloomberg*, 31 August 2011, <http://www.bloomberg.com/news/2010-08-31/iceland-says-it-deserves-to-catch-more-mackerel-as-u-k-dispute-deepens.html> (accessed 12 May 2011); and “Mackerel quota dispute: statement from Fisheries Minister Richard Benyon,” Department for Environment Food and Rural Affairs, 26 August 2010, <http://www.defra.gov.uk/news/2010/08/26/mackerel/> (accessed 12 May 2011).

⁷⁶ Martin Hickman, “Now Britain and Iceland go to war over the mackerel,” *The Independent*, 11 August 2010, <http://www.independent.co.uk/news/world/europe/now-britain-and-iceland-go-to-war-over-the-mackerel-2049099.html> (accessed 12 May 2011). See also: Caroline Davies, “Britain prepares for mackerel war with Iceland and Faroe Islands,” *The Guardian*, 22 August 2010, <http://www.guardian.co.uk/environment/2010/aug/22/britain-iceland-faroe-islands-mackerel-war> (accessed 12 May 2011).

This comment suggests that Iceland controls its volcanoes and their products, the *Eyjafjallajökull* eruption last year was in fact the biggest shut down of air space since World War II.⁷⁷ No doubt that if Iceland could control their volcanoes and especially for which countries the ash would cause troubles, this could become a very effective hard power tool, more harmful than any known chemical weapons or trade sanctions used in today's international relations. Volcano experts have predicted an era of volcanic activity will be ongoing for several years at least, with the *Grimsvotn* eruption prevailing this spring and already causing some flight delays and cancellations outside of Iceland, these predictions seem to be justified.⁷⁸

4.4 Diplomatic missions and operations abroad

The diplomatic missions have after the crisis had informational meetings with authorities in their host states to explain happenings in the Icesave issue. A special ambassador was sent to Haag, Holland, on a mission to improve relations with the Dutch authorities and provide information on Icelandic views on the issue.⁷⁹ The diplomatic missions have sought to improve relations with the media in the applicable states, on a short notice they can react if information is lacking or if incorrect statements are made. In the UK and the Netherlands public relations firms have been on guard towards media coverage for the Icelandic government, with special regards to the Icesave issue. Defense was also upheld against some claims made in media coverage about the *Eyjafjallajökull* volcanic eruption in spring 2010, to limit the harm made to Icelandic tourism industry.⁸⁰

The above stem directly from the financial crisis, except for the volcanic eruption although some people jokingly related the issues by labeling it as revenge against unreasonable British and Dutch authorities' behavior. Others, such as Stevenson referred to in chapter 4.3, sounded more serious about such notions. The embassies also work on other fields regardless of the crisis, such as culture promotion. Increasingly in the past few years, they have been working as extensions of culture promotion offices run in Iceland, for art, music,

⁷⁷ "Iceland's Eyjafjallajökull volcano reduces activity," *BBC News*, 24 May 2010, <http://www.bbc.co.uk/news/10144911> (accessed 21 May 2011).

⁷⁸ Andrew Hooper, "Why the Icelandic volcano eruption could herald more disruption," *The Sunday Times*, 18 April 2010, <http://www.timesonline.co.uk/tol/news/environment/article7101084.ece> (accessed 21 May 2011). See also: Kate Ravilious, "Get ready for decades of Icelandic fireworks," *New Scientist*, 16 April 2010, <http://www.newscientist.com/article/dn18786-get-ready-for-decades-of-icelandic-fireworks.html?full=true&print=true> (accessed 21 May 2011).

⁷⁹ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2010, <http://www.althingi.is/altext/138/s/pdf/1070.pdf> (accessed 13 May 2011).

⁸⁰ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2011, p. 91, <http://www.althingi.is/altext/139/s/pdf/1416.pdf> (accessed 17 May 2011).

literature etc. Some cultural activities take place within the embassies and other activities are arranged by them, film festivals, literature fairs and more.⁸¹

Serving Icelanders abroad is among the main tasks of the foreign affairs service and their scope has increased as the number of Icelanders living abroad has increased. The diplomatic missions assist in cases of emergency, e.g. illness or accidents, assistance in case of criminal matters and imprisonment. Actions are planned when needed in danger areas, for example after natural disasters.⁸² During the collapse, the diplomatic missions were called upon a lot by companies that were facing obstacles because of the uncertainty surrounding Iceland; they had to pay for goods in cash and lost business primarily because of the same uncertainty. The embassies assisted these companies the best they could and promulgated correct information. Secondly, individuals called upon the embassies in some countries; especially in the early aftermath of collapse when people were facing difficulties with withdrawals from ATM's or had run short on money. At that time, the embassies were permitted by the ministry to lend money to Icelanders, against a certain deposit. The errands thus changed in the early aftermath, but today they are similar to what they were before crisis: business service, cultural cooperation and political issues.⁸³

Asked whether there had been changes in the extent and nature of errands to the Icelandic diplomatic missions abroad following the financial crisis of 2008, the respondent said that interest in Icelandic matters had increased and staff at the diplomatic missions got numerous questions from ministries of foreign affairs and ministries of finance in countries such as Germany, France, USA and Sweden.⁸⁴

Íslandsstofa (e. Promote Iceland) is an initiative that was started in 2010 on basis of the Trade Council of Iceland, but extending its mission to cover a wider field than this predecessor. *Íslandsstofa* is dedicated to attracting more tourists to Iceland; framing the image and promotion of Iceland abroad with the collaboration of public and private actors, exporters, tourism workers and knowledge industry. As before, diplomatic missions promote the interests of the Icelandic economy and with the creation of *Íslandsstofa* they will do so in cooperation with them. The diplomatic missions hold knowledge of local customs and etiquette which they can

⁸¹ Interview with an employee of the Icelandic Ministry of Foreign Affairs, 20 March 2011. See also: "Arts & Culture," Ministry for Foreign Affairs, <http://www.mfa.is/tasks/arts-culture/> (accessed 21 May 2011).

⁸² Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2010, <http://www.althingi.is/alttext/138/s/pdf/1070.pdf> (accessed 13 May 2011).

⁸³ Interview with an employee of the Icelandic Ministry of Foreign Affairs, 20 March 2011. See also: "Aðstoð við Íslendinga erlendis vegna sérstakra aðstæðna á fjármálamarkaði," Ministry for Foreign Affairs, <http://www.utanrikisraduneyti.is/frettir/nr/4531> (accessed 16 April 2011).

⁸⁴ Interview with an employee of the Icelandic Ministry of Foreign Affairs, 20 March 2011.

offer Icelandic companies. Seven of the diplomatic missions have trade- and tourism agents, those are in UK, Denmark, Japan, China, Russia, Germany and India. These agents do market research, e.g. estimating competitiveness of products and services in these markets. They search for trading partners, assist with contacting and arranging meetings with foreign authorities. Small and medium sized companies especially make use of this service, helping them grow. The trade agents also work the other way around, meaning that they respond to inquiries from foreigners considering investments in Iceland.⁸⁵ With regards to tourism, January this year was a record month in number of tourists visiting Iceland and ticket bookings give a reason to believe that the year record will be broken as well with 600,000 tourists visiting the country from abroad this year. Previous all time high for one year was 500,000, indicating that the *Promote Iceland* campaign has been successful so far. Volcanic eruptions have probably also increased interest in Iceland, being covered by all major global news agencies.⁸⁶

In 2009 the Ministry for Foreign Affairs in teamwork with Ministry of Finance and Ministry of Economic Affairs worked on informing partner states and organizations about happenings in the economic agenda partnership between Iceland and the IMF. The Minister for Foreign Affairs met with around 70 other Ministers for Foreign Affairs and spoke to foreign media. In a similar vein, the Minister of Economic Affairs together with embassies in the US, Sweden and Finland arranged meetings in these countries on the current situation and prospects for the Icelandic economy. Secondly, the foreign affairs service spread information about Iceland's position towards the Icesave issue by speaking directly with foreign authorities, thus opting for more positive reactions than would be expected from leaving explanations solely to the varyingly reliable mass media. The president of Iceland refused to ratify the so-called Icesave law in January 2010 sending the law to a national referendum, the Government Offices reacted by coordinating a team to handle media communications before the referendum and the Ministry for Foreign Affairs arranged a media centre in downtown Reykjavik where foreign journalists could meet up with government officials, organizations and individuals for interviews.⁸⁷

Energy has been high on the agenda for the foreign affairs service in recent times, especially geothermal energy. Cooperative projects have been among the main subject matters of diplomatic missions in China, USA,

⁸⁵ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2010, p.87, <http://www.althingi.is/alttext/138/s/pdf/1070.pdf> (accessed 15 May 2011).

⁸⁶ "Stefnir í metfjölda ferðamanna," *Viðskiptablaðið*, 13 April 2011, <http://www.vb.is/frett/62722/> (accessed 26 May 2011). See also: "Metfjöldi ferðamanna í janúar," *RÚV*, 4 February 2011, <http://www.ruv.is/frett/metfjoldi-ferdamanna-i-januar> (accessed 26 May 2011).

⁸⁷ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2010, p.90, <http://www.althingi.is/alttext/138/s/pdf/1070.pdf> (accessed 15 May 2011).

India, Russia and Japan. In the past few years agreements have been sealed with some of the largest global players, such as the US, India and China about geothermal energy, as increasing attention has been paid to the use of this energy source as an option to battle climate change. Some EU states have declared their interest in cooperation with Iceland on geothermal energy, partly in response to directive 2009/28 that requires 20% of all energy used to be derived from renewable resources in 2020. Icelandic engineering firms have been working in Hungary and Croatia on geothermal projects, e.g. designing distribution of heat in the Hungarian city Szentlőrinc. In the recent visit to India by the Minister for Foreign Affairs, geothermal energy cooperation was among the main points of discussion. Projects in Russia are also planned, on using geothermal energy for domestic heating, fish farming and electricity creation.⁸⁸

4.5 Defense and national security

Iceland has never had an army and wants to be seen as a peaceful small state, supportive of human rights, peaceful solutions to disputes and disarmament. The state contributes to mutual security by supporting development, restoration (e.g. after natural disasters) and charity.⁸⁹ As mentioned earlier the recently established Defence Agency was closed as a result of strapped economy after crisis. There is no ministry of defense under the Icelandic government; defense and security are handled by the Ministry for Foreign Affairs. The Coast Guard is to a large extent responsible for securing non-military security, such as sovereignty protection, domestic and high seas fisheries patrol, search and rescue and explosive ordnance disposal.⁹⁰

As before, the defense and national security policy is rooted in the NATO membership and the defense treaty with the United States. Permanent defense facilities and labor in the country are now history and the government has been forced to look for substitutes for the US permanent presence. Agreements were made with six neighbor states based on a wider definition of security than before. Ongoing are negotiations on a broader collaboration within Scandinavia on security and defense.⁹¹ What is meant by a wider definition of security than before is that new risks have been given increased attention in the global system. Financial system exposure is one, health threats and epidemics, environment threats and natural disasters, terrorism,

⁸⁸ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2011, p. 44-45, <http://www.althingi.is/altext/139/s/pdf/1416.pdf> (accessed 17 May 2011).

⁸⁹ *Ibid.* 47.

⁹⁰ David Rudd, "Northern Europe's Arctic Defence Agenda," *Journal of Military and Strategic Studies* 12, no. 3 (2010): 56.

⁹¹ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2010, p. 41, <http://www.althingi.is/altext/138/s/pdf/1070.pdf> (accessed 13 May 2011).

WMD, organized crime, human trafficking, internet security, integration of foreigners to Icelandic society, telecommunications security and more.⁹²

When the US army left in 2006 there was another government in office in Iceland, one that was more influenced by neo-realism than the current government and did their best to convince US authorities to make their army stay, for example by officially announcing support for the US invasion of Iraq. The Left Green Movement was opposed to the military presence here and is opposed to Icelandic membership of NATO. Their bigger coalition partner, the Social Democratic Alliance, supports NATO membership and thus Iceland has not ended its membership of the institution. As mentioned in the introduction to chapter 4, Iceland was recently named the world's most peaceful country by the *Institute for Economics & Peace*. Indicators used to measure level of peace include levels of military expenditure, relations with neighbor states and level of respect for human rights. Levels of democracy and transparency, education and national wellbeing are also taken into consideration from the index. Iceland has claimed the top spot of this index before, but lost it in 2009 and 2010 due to massive public demonstrations after the financial system collapse. Closing the Icelandic Defence Agency due to financial cutbacks should also have helped Iceland reclaiming top spot of this index.⁹³

4.6 Application for European Union membership

Iceland handed in its application to join the European Union on 17 July 2009 and the European Council decided to open negotiations with the state on 17 June 2010.⁹⁴ Although decided and presented after the financial crisis began, this decision was not directly a result of that. It had all the more to do with the fact that for the first time, *Samfylkingin* (e. The Social Democratic Alliance), the only Icelandic political party officially supportive of membership had become the leading party in a coalition government. Having the upper hand in the coalition government, the party was able to push through a membership application, although its coalition partner officially stood against membership.⁹⁵ The general skepticism towards EU in Icelandic politics has been founded on a belief that with membership comes more trouble than benefits, particularly with regards to the fisheries and agriculture.

⁹² Ibid. 52.

⁹³ Simon Rogers, "Global peace index 2011: the full list," *The Guardian*, 25 May 2011, <http://www.guardian.co.uk/news/datablog/2011/may/25/global-peace-index-2011> (accessed 26 May 2011).

⁹⁴ "The Application Process," Ministry for Foreign Affairs, Iceland's application for membership of the EU, <http://europe.mfa.is/sidemenu/explaining-the-application-process/> and "Accession talks," <http://europe.mfa.is/phase-2---negotiation-process/> (accessed 8 May, 2011).

⁹⁵ "Vonar að ríkisstjórnin starfi áfram," *RÚV*, 13 July 2009, <http://www.ruv.is/frett/vonar-ad-rikisstjornin-starfi-af-ram> (accessed 8 May 2011).

The leader of the other and smaller coalition party, the Left Green Movement, finance minister Sigfusson told *Wall Street Journal* in an interview recently some of the reasons why he is opposed to membership. Besides the big issues, fishing and agriculture he mentioned the currency as an obstacle referring to the economic problems of EU countries Greece and Portugal and their requests for bailout. The existence and use of Icelandic krona had secured that Icelandic goods became cheaper abroad through its devaluation.⁹⁶

In the past, links to EU have been through membership of European Economic Area (EEA) since 1994 giving access to the European single market. Through this membership, the country already has to apply 22 of 35 chapters in the EU legislation in its own legislation. Other current links are most notably membership of EFTA, since 1970, Schengen (since 2001), OECD (since 1948), OSCE and the Council of Europe.⁹⁷ Eiríkur Bergmann refers to participation in these organizations as the European pillar, which is the most important of the three pillars of Icelandic foreign policy as he describes, fairly enough since Iceland does not participate in many international institutions outside of Europe.⁹⁸

The second pillar (also second in terms of importance) of Icelandic foreign policy according to the same definition is the Atlantic pillar, standing on the NATO membership and defense agreement with the US. Unlike the European pillar resting on economic affairs, this pillar is focused on strategic security. However, the value of this pillar for the foreign policy decreased when the US army base closed in 2006 and in turn the European pillar got more important since the Icelandic government turned to European neighbors in search for replacement.⁹⁹ See chapter 4.5 for further discussion on defense and national security. The third pillar, according to Eiríkur, covers foreign relations with the rest of the world through for example UN and WTO.

Turning again to the possible membership of the European Union, Jóhanna Jónsdóttir (2009) describes the situation as it is at present with the membership of EEA, in which Iceland adopts a lot of EU legislation without having any say on it. The Icelandic authorities have hitherto made contacts with the organizations and member states of the EU in order to pursue their interests, but that is not a very efficient method to gain influence. If

⁹⁶ Charles Duxbury, "Iceland 'Better off Without EU'," *The Wall Street Journal*, 5 May 2011, <http://online.wsj.com/article/SB10001424052748703859304576304611381496144.html?KEYWORDS=sigfusson> (accessed 28 May 2011).

⁹⁷ "Iceland's home is in Europe," Ministry for Foreign Affairs, Iceland's application for membership of the EU, <http://europe.mfa.is/sidemenu/iceland-in-europe/> (accessed 8 May 2011).

⁹⁸ Eiríkur Bergmann, "Iceland and the EEA, 1994 – 2011," a report for *Europautredningen*, March 2011, <http://www.europautredningen.no/wp-content/uploads/2011/04/Rap7-island.pdf> (accessed 11 May 2011).

⁹⁹ Eiríkur Bergmann, "Iceland and the EEA, 1994 – 2011," a report for *Europautredningen*, March 2011, <http://www.europautredningen.no/wp-content/uploads/2011/04/Rap7-island.pdf> (accessed 11 May 2011).

Iceland was a member of the EU, it would reserve seats in the Council of Ministers and the European Parliament. It would nevertheless be the smallest member state with its population of 320 thousand, currently Luxembourg and Malta are the smallest members of EU with 510 thousand and 412 thousand respectively. The smallness means that it would hold a very limited number of seats within these institutions. Qualified majority vote is dominant within the Council, where each state is allotted votes based on population size. Under the current regulations Iceland would as a small state get maximum three votes of the 345 in total, 255 votes are needed to reach agreements in the council, so it would have very remote chances of influencing through votes. Networking with other states would thus be as important as before. On the other hand, votes are not cast on every topic within the Council and consensus is seen as important and in spite of very limited influence through votes it would have the chance to speak up.¹⁰⁰ One thing that makes Iceland different from other applicant states is its membership of EEA and Schengen and on basis of these Icelandic regulations are already close or fully corresponding to the EU regulations on 22 of the 33 chapters for negotiations.¹⁰¹

In the European Parliament, Iceland would have six seats out of the 750 total. Hence, the voting power would be limited, but therein is a tradition for political parties working towards issue orientations rather than on basis of states. In other words, MPs usually vote on basis of their party rather than their state, except for when there are vital national interests at stake.¹⁰² Turning to effects of EU membership for the foreign policy of Iceland, one thing is that as members Iceland would become participants in the Common Trade Policy. The European Commission has concluded that Iceland has to drop all of its current free trade agreements with third states and revise other contracts to make the in accordance with the EU regulation. Additionally, Iceland will have to take up each and every EU contract on global trade and regulations in the field. However, the current free trade contracts made by Iceland are in most instances with the same states as the EU contracts and allow similar access for Icelandic exports to enter foreign markets.¹⁰³ As negotiations with China on bilateral free trade agreement have not been successful yet, despite negotiations having been ongoing for five years or

¹⁰⁰ Jóhanna Jónsdóttir, "Áhrif aðildar að Evrópusambandinu á fullveldi Íslands," *Stjórnsmál og stjórnsýsla veftímarit* 5, no. 1 (2009): 80 – 81, <http://www.stjornmalogstjornsysla.is/images/stories/fg2009v/jj.pdf> (accessed 11 May 2011).

¹⁰¹ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2011, p. 34, <http://www.althingi.is/altext/139/s/pdf/1416.pdf> (accessed 17 May 2011).

¹⁰² Jónsdóttir 2009, "Áhrif aðildar að Evrópusambandinu á fullveldi Íslands," 80 – 81. See also: "Q&A: The Lisbon Treaty," *BBC News*, <http://news.bbc.co.uk/2/hi/europe/6901353.stm> (accessed 11 May 2011).

¹⁰³ Össur Skarphéðinsson, *Report on foreign and global affairs*, May 2011, p. 25, <http://www.althingi.is/altext/139/s/pdf/1416.pdf> (accessed 17 May 2011).

more, it could be fair to assume that Iceland will not necessarily reach such agreement with China before the EU does.¹⁰⁴

One man who would however most certainly be more interested in reaching a free trade agreement with China rather than joining the EU is President Ólafur Ragnar Grímsson. His influence on foreign affairs of Iceland has increased after the crisis as explained in the following chapter.

4.7 The President effect

In the previous chapters, emphasis has been on the main actor in shaping Icelandic foreign policy, the Ministry for Foreign Affairs on behalf of the government and parliament. Another actor of Icelandic foreign relations, who cannot be disregarded in the light of events after the crisis, is the directly elected president. On two occasions since the crisis started in 2008 he has hindered the parliament's decisions from taking effect as described below.

As already mentioned earlier in this paper, the president of Iceland refused to ratify a law that had been agreed by a parliament majority in spring 2011, the so called Icesave legislation that identified terms and conditions of how the debt of the old Landsbanki in Britain and Holland should be paid back. It identified how many years the Icelandic state ought to have to pay back the British and Dutch governments and at which interest rate. These governments had already paid the 400,000 Icesave depositors in their respective countries and spent long time on negotiating terms with the Icelandic government. The president of Iceland announced on 20 February 2011 that since there was no conciliation within the Icelandic public on the issue according to opinion polls, it should be decided by a national referendum. He also mentioned wide support in the parliament (close to half of the MPs) for a referendum on the issue and that more than 40,000 voters (1/5 of the total having voting rights) had signed a petition asking for a referendum.¹⁰⁵

This was in fact the second time that the president triggered a referendum on an Icesave deal, because approximately a year earlier a contract on repayments was on the table, a deal which was a lot worse than the later version for the cash strapped Icelandic economy. In the following referendum of spring 2010 the electorate made a very clear statement of disagreement with the parliament's result, 93% said 'no' to the

¹⁰⁴ Össur Skarphéðinsson, "Ísland, Evrópusambandið, norðurslóðir og Kína," *Fréttablaðið*, 28 May 2011.

¹⁰⁵ Ólafur Ragnar Grímsson, Announcement by the president of Iceland, 20 February 2011, http://forseti.is/media/PDF/2011_02_20_icesave3_isl.pdf (accessed 22 May 2011). See also: "Iceland president calls referendum on new Icesave deal," *BBC News*, 20 February 2011, <http://www.bbc.co.uk/news/world-europe-12519355> (accessed 22 May 2011).

deal.¹⁰⁶ Some suggested that this was such a major blow to the government that it ought to resign, but the government did not listen to the critics and continued in office. In fact there was already a contract with better terms ready when the referendum took place. Some analysts suggested that the president had with his decision benefited those wanting to break free from the IMF economic recovery program and opposing EU membership, because both institutions would have wanted the deal to go through. The referendum this year (2011) on an improved repayment deal did not give as clear message as the previous one but was quite clear anyway, almost 60% said 'no' this time.¹⁰⁷

The president spoke extensively to foreign media, defending his decision and also defending the Icelandic public's rejection in the referendums.¹⁰⁸ The government was in a strange situation then, having to defend results that they were opposed to, to the outside world although PM's Johanna Sigurdardóttir's first reaction to the second referendum outcome was stating that: "The worst option was chosen."¹⁰⁹ After that, the PM and other government officials have done their best to defend Icelandic interests and explain the situation, for example Sigurdardóttir by stating that "the Icelandic people will not accept a requirement to cover costs related to deposit insurance guarantees, unless the legal obligation for doing so is clear and unequivocal" and adding that opinion and interpretation of the European directive concerned was debated. She also underscored that the UK and the Netherlands would receive payments from the Landsbanki estate, which would possibly even cover the whole loss.¹¹⁰ Finance minister Sigfusson concluded that the outcome had "changed nothing" regarding repayments to British and Dutch depositors and added that they would most likely start later this year. The president had in fact claimed the same as the two government leaders, as soon as the result of the second referendum was clear. There he also announced that: "The leaders of other states and international institutions will have to respect this expression of the national will. Solutions to disputes

¹⁰⁶ "Lokatölur komnar úr öllum kjördæmum," *RÚV*, 7 March 2010, <http://www.ruv.is/frett/lokatolur-komnar-ur-ollum-kjordaemum> (accessed 26 May 2011).

¹⁰⁷ "UK and Netherlands to sue Iceland over lost deposits," *BBC News*, 10 April 2011, <http://www.bbc.co.uk/news/business-13029210> (accessed 26 May 2011). See also: Andrew Ward, "Grimsson defends referendum," *Financial Times*, 6 January 2010, http://www.ft.com/cms/s/0/f9581b1c-faff-11de-94d8-00144feab49a,dwp_uuid=4da69efc-1b8f-11dd-9e58-0000779fd2ac.html#axzz1NUWlw3IM (accessed 26 May 2011).

¹⁰⁸ Eyk Henning, "Riding out the Icesave Storm," *Wall Street Journal*, 11 January 2011, <http://online.wsj.com/article/SB10001424052748703959104576081991312764126.html> (accessed 26 May 2011). See also: "UK 'will get Iceland money back'," *BBC News*, 12 April 2011, <http://www.bbc.co.uk/news/world-europe-13047176> (accessed 26 May 2011).

¹⁰⁹ "UK and Netherlands to sue Iceland over lost deposits," *BBC News*, 10 April 2011, <http://www.bbc.co.uk/news/business-13029210> (accessed 26 May 2011).

¹¹⁰ Jóhanna Sigurdardóttir, "The Icesave referendum has been oversimplified," *The Guardian*, 13 April 2011, 25 May 2011, <http://www.guardian.co.uk/commentisfree/2011/apr/13/icesave-referendum-uk-payments> (accessed 25 May 2011).

arising from financial crises and failures of banks must take account of the democratic principles which are the foundation of the constitutional structure of the West.”¹¹¹

Some MPs and others expressed the view that the president had become too involved in politics, that he was interfering in matters none of his business.¹¹² He is the first ever Icelandic president to exercise this right based on article 26 of the constitution, which is debated both among academics and the public. The first time he called for a referendum was in 2004 on the so called media law, which was rejected in the following referendum just like the Icesave cases. The media law was strictly a domestic issue unlike the Icesave acts that fall under foreign affairs; suddenly the president has become an active agent of Icelandic foreign policy, challenging the government. The president’s decision in 2004 created havoc within the government, which led its leaders to announce plans to have this option removed from the constitution, so that the president would only act in accordance with government policies as had been the working practice for previous presidents.¹¹³

Before being elected as president in 1996, Grimsson had experience as an MP and finance minister so involvement in politics is nothing new for him. Throughout his political career, the president he has been opposed to EU membership. As president he has always been supportive of Icelandic companies expanding and entering global markets, including the so called “Icelandic Expansion,” a term used for Icelandic banks and several other firms that grew to be manifold size of the state economy. Svanur Kristjánsson (2006) argued that the “Icelandic Expansion” had become the foreign policy of Iceland, largely influenced by president Grimsson. The EEA membership shaped the right conditions for this expansion to flourish and it was officially described as an option replacing possible EU membership. Bilateral free trade agreements were to be the replacement for market access gained through EU membership, for example with China. Negotiations on such agreement with China have been ongoing for several years but nothing has been sealed so far.¹¹⁴ They have stalled on two

¹¹¹ Paul Fontaine, “Finance Minister: “Iceland Will Pay” Icesave Debt,” *The Reykjavik Grapevine*, 11 April 2011, <http://www.grapevine.is/News/ReadArticle/Finance-Minister-Iceland-Will-Pay-Icesave-Debt> (accessed 25 May 2011). See also: “UK ‘will get Iceland money back’,” *BBC News*, 12 April 2011, <http://www.bbc.co.uk/news/world-europe-13047176> (accessed 26 May 2011).

¹¹² Fontaine, “Finance Minister: “Iceland Will Pay” Icesave Debt.”

¹¹³ “Engin fjölmiðlalög,” *Fréttablaðið*, 20 July 2004, <http://visir.is/engin-fjolmidlalog/article/2004407200301> (accessed 27 May 2011).

¹¹⁴ Már Wolfgang Mixa and Þröstur Sigurjonsson, “Áfram á rauðu ljósi – fjármálahrúnið á Íslandi og reynsla Norðurlandanna,” *Tímarit um viðskipti og efnahagsmál* 7, no. 1 (2010), http://www.efnahagsmal.is/wp-content/uploads/2010/12/1_2_Afram-a-raudu-ljosi_final.pdf (accessed 27 May 2011). See also: Svanur Kristjánsson, “Forseti Íslands og utanríkisstefnan,” a lecture given at the National Museum, 25 March 2006, <http://silfuregils.eyjan.is/2011/05/17/forsetaembaettid-utanrikisstefnan-og-utrasin/> (accessed 27 May 2011).

things in particular; Iceland does not want to accept temporary free flow of Chinese labor to Iceland while China does not want to accept fish imports from Iceland without tariffs.¹¹⁵

As leader of a political party called The People's Alliance, Grimsson released a book in collaboration with other party members in 1994, called *The Export Way*. This book described how Icelandic firms could expand and grow in the age of globalization, which steps should be taken for them to be competitive globally. After the presidential election in 1996, an opinion poll conducted by the *Social Science Research Institute* (of the University of Iceland) indicated that the president's ability in communicating with foreigners was a deciding factor for his election, 69% of his voters mentioned that as the most important factor in determining how they cast their vote. During his time in office, communication with foreigners has indeed been a priority of his. This is evident by his numerous dialogues with leaders in politics and business in e.g. Russia, China and India.¹¹⁶ In addition he spoke in favor of the Icelandic banking model, which he has later defended by saying: "It is always the mandate of the President to support the economy of the country and those three banks were the biggest companies." He also referred to job opportunities they had provided for young Icelanders in Iceland and abroad. Part of his promotion talks for the banks and other businesses before the crisis had drawn a nationalistic picture of Icelandic superiority traced to old heritage (of Vikings for example) which led to their "brilliance" in business. He was also criticized for being in company with the businessmen and making use of their private jets for trips abroad, nine times he did that between 2005 and 2008 according to *Frettabladid*.¹¹⁷

¹¹⁵ Össur Skarphéðinsson, "Ísland, Evrópusambandið, norðurslóðir og Kína," *Fréttablaðið*, 28 May 2011.

¹¹⁶ Kristjánsson 2006, "Forseti Íslands og utanríkisstefnan."

¹¹⁷ Christian Wienberg and Omar Valdimarsson, "Iceland President Pre-Crisis Tours Promoting Bank Model," *Bloomberg*, 14 April 2011, <http://www.bloomberg.com/news/2011-04-14/iceland-president-defends-pre-crisis-tours-promoting-bank-model.html>. See also: "Forsetinn í níu ferðir utan áætunarflugs," *Fréttablaðið*, 3 March 2009.

5. Discussion

Features of Icelandic foreign policy have been discussed above to the extent possible within the time frame. Some issues could have been covered more thoroughly, such as Arctic issues which are discussed back and forth these days in Icelandic politics, mostly by the foreign minister who attended a recent meeting of the Arctic Council in Greenland. The arctic issues seem very much in a discussion phase so far, which also makes them hard to discuss in relation to theories. For that to be feasible, concrete decisions by the Arctic Council would have been preferred.

This relates to a disadvantage of the subject in general, because unlike research of the Cold War or U.S. foreign policy under George W. Bush, this subject did not indicate any ending point, changes in the foreign policy of Iceland is something that is ongoing right now and will continue to do so. Lots of new relevant information became available in the last ten days or so before deadline, so they had to be incorporated quickly. The lack of end point makes the topic hard to handle without making predictions. Domestic politics have been prone to non-cooperation after crisis; solidarity has decreased which makes decision-making harder in the parliament. Conflicts on the various fields are very apparent, both within the parliament and in public debate. This is maybe the ideal soil for the president to step in and try to bridge “the gap between parliament and the nation” as he claimed to be doing when he refused to ratify a government draft for the first time in 2004.

Presidential elections are scheduled for next year and as far as I know, many believe that the current president will run for election once more and go for a fifth consecutive term. No other candidates have so far announced that they will run for the post and Grimsson has not either although many take that for granted. **If** Grimsson continues in office and **if** the constitutional right of president to trigger referendum will not be removed from the constitution, he will probably affect foreign policy decisions further. These “ifs” are symbolic for the situation because there are many complications in Icelandic politics at present. After the financial system collapse there were loud demands from the public for a new constitution and currently a Constitutional Committee is reviewing the Constitution and designing proposal for changes.

European Union membership is being negotiated but affected by doubts from several directions, e.g. threats from Britain and Holland and opposition by the coalition party Left Green Movement. Already three members of the Left Green stopped supporting the government so currently the government has to rely on a one-man majority.

6. Conclusion

The mission of this paper was to answer the question **“How has the foreign policy of Iceland changed as a consequence of the financial crisis that started in 2008?”** and which repercussions (good or bad) can be expected to follow these changes. The main findings are as follows.

There is a slight contradiction in the fact that demands for cutbacks in the foreign affairs service are on the high at the same time as the need for strong and effective foreign affairs service are maybe higher than ever after the financial crisis. This is a similar contradiction as appears in opinion polls when the majority of people usually want lower taxes, but also better and more service from public institutions; a win-win combination if it was possible. Cutbacks have been made and priorities of the government and Ministry for Foreign Affairs have become clearer. Pretoria, Rome and Strasbourg are not seen as key locations and thus diplomatic missions there were closed. However, in the case of the two latter mentioned, plans on EU membership have presumably affected the decision. Pooling of interests and joint benefits are among the goals of EU membership and therefore fewer diplomatic missions in member states should be needed. On the other hand, staff will be needed for representation at various EU bodies if Iceland becomes a member.

One visible change in Icelandic foreign policy after the crisis is that more people are actively shaping it and more people are speaking on behalf of Iceland than before the crisis. There are several reasons for this; one is the globalization of many political fields as noted in the theory chapter. For example, the biggest domestic political issue in Iceland since the crisis has been the Icesave dispute, which is an economic issue but not any less a foreign (or global) issue. Several Ministries have covered the various aspects of it and for example the Ministers of Foreign Affairs, of Finance, of Trade and the Prime Minister have all undertaken relations with foreign authorities, media, institutions, and so on to explain Icelandic views. There is a spillover in this issue but also in many others such as migration, environmental degradation or energy shortages. This spillover has only increased after the crisis as evident from above. To relate further to the theoretical discussion on NGOs and that what they “benefit from are small and flexible bureaucracies and shorter routing channels” as noted by Chong (2007) this applies to Icelandic government because the bureaucracy is indeed small (compared to bigger states) and the routing channels short which makes coordination between ministries easier, such as with responding to the Icesave dispute.

Ministries of foreign affairs face increasing competition from various directions; their status is constantly challenged by NGOs, multinational corporations and the aforementioned spillover to other ministries. The Icelandic MFA is also challenged from a rather unexpected direction, the president, who has effectively managed to turnaround the policy towards the diplomatic row with UK and Holland. Consequently, the Ministry and other representatives of the electorate have had to adapt their messages to that of the president when speaking to other international actors and foreign media. As covered earlier the president is a long time opponent of joining the European Union, while the current government is in favor of membership, only just, subject to the coalition's leading party's will. Nevertheless, negotiations with the EU are ongoing and will be continued until a contract is on the table, subject to a referendum. Opinion polls on membership are somewhat confusing, opposition to membership has usually been stronger than the support, but generally the majority has been supportive of membership negotiations. This indicates curiosity to see what can be negotiated and how favorable a contract the Icelandic negotiators are able to reach.

EU membership supporters can not rely on anything it seems, there are various doubts surrounding the application, not only from the other coalition government party. The government is currently only relying on a one man majority in the parliament as three MPs have abandoned their support since it was formed in 2009, so the government is "living on the edge" right now. There have been threats from some British and Dutch leaders of standing in the way of Icelandic membership, so nothing can be taken for granted. In this regard, the recent opening of a new consular office in Mumbai, India is interesting, not only because it is the first new office opened abroad after the crisis. Also, because it appears as a way of not putting all the eggs in the same basket, EU membership cannot be taken for granted; other pillars of Icelandic foreign policy need to be strengthened as well. This would be in line with the president's preferences and the government will be extra cautious now that he has turned around their policies twice in one year.

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