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Iceland and the European Recovery
Program. An historical analysis of how
economic challenges and domestic politics
shaped a unique economic development
program.

Georg Gylfason

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Abstract

The Icelandic membership in the European Recovery Program is often overlooked in the historical literature that focuses on examining the complex legacies of the Marshall Plan. But the Icelandic ERP is quite unique when examined more carefully. The country emerged from the war relatively unscathed and had in effect benefitted enormously during the years of the war. Yet the country received a generous share of ERP assistance. Per capita, Iceland received the more financial support than all the other 16 ERP member countries. At the same time the Icelandic government maintained strict isolationist trade policies and was an awkward member of the OEEC. Iceland would maintain these policies all the way up to 1960. Meanwhile the countries of Western Europe were adopting liberal economic policies, which, which facilitated three decades of growth. This has been touted as one of the primary achievements of the ERP. Which begs the question, why did Iceland receive so much financial support and not adopt the policies stipulated in the ERP conditions?

This dissertation will seek to answer this question. Focusing in on the role of domestic politics and how that factor influenced the design of Iceland's unique ERP program. The analysis will make use of archival evidence, officials documents from the US and Icelandic governments, and articles published in the four main newspapers, which dominated the political discourse in Iceland in the post-war years.

1. Introduction

The European Recovery Program (ERP), more commonly referred to as 'The Marshall Plan', was a large-scale aid program which the United States offered to countries in Europe that had been left devastated at the end of the Second World War. The program went into effect in April 1948. The stated purposes of the Marshall Plan, presented in a now famous speech given by George C. Marshall at Harvard University on June 5th, 1947, was to revive the badly damaged economies in Europe, prevent breakdown in trade due to scarcity of foreign

exchange, and offset massive shortages in food and other vital supplies that seemed to be looming over citizens in Europe. He argued that assisting in the recovery effort of those damaged economies would encourage the demoralised and traumatised people of Europe and prevent political instability that would result from prolonged economic hardship and pessimism towards the future.¹

The program formally came to an end in 1951, when it was replaced by the Mutual Security Act (MSA), however, effectively the program is considered to have continued until 1952 and in some countries stretched into 1953. It is commonly thought that the program was replaced with the MSA by the United States Congress because of the Korean War and the growing opposition from Republicans, who had recently gained numerous seats in Congress after the 1950 congressional election. In total the aid delivered to the 16 recipient countries amounted to approximately 13.3 billion dollars. The program consisted of a combination of loans, grants, and technical assistance. The size and composition of the aid package delivered to each of the recipient nations varied significantly. The scope and type of assistance that each country received was determined by several factors, such as the economic conditions in each country, and the economic plan that they provided the ERP governing body, the Economic Cooperation Administration. The composition of the aid program delivered to each country was also determined by the bilateral negotiations that took place between the US government and the authorities from each of the countries that received aid. Each member country provided the US with a four-year economic plan. Special legations were also sent to each member country, tasked with overseeing the implementation of the program and communicating with the country's government. The deal making process produced an agreement that fit the political and economic preferences of the US and each of the 16 nations.

¹George C. Marshall, "Remarks By The Secretary of State at Harvard University on June 5, 1947" The George C. Marshall Foundation, accessed August 28, 2023, <https://www.marshallfoundation.org/the-marshall-plan/speech/>.

This negotiation process was shaped by many different factors that influenced both decisions of the US government and the government of each aid receiving country. Some countries received disproportionately large financial assistance, whilst other countries received quite meagre sums. Although most of the aid delivered to all sixteen countries came in the form of grants, the ratio of grants versus loans that each country received varied greatly between recipients. For instance, Austria's aid package consisted solely of grants, while Ireland's and Portugal's ERP were mainly loans. A lot of the literature devoted to analysing the Marshall Plan and its historical significance has primarily focused on the larger economies, and therefore the biggest Marshall aid recipients. Less attention has been devoted to examining the ERP in the smaller states, especially those situated in the European periphery.

The case of Iceland falls into the latter category. Its participation in the ERP is often overlooked in the grand narratives, essay collections, or studies dedicated to the Marshall Plan. There are only a handful of articles that touch upon the Icelandic ERP found in peer reviewed journals. Yet, the program presents a curious case that is well worth examining further. Iceland, along with four other countries (Sweden, Portugal, Ireland, and Turkey), managed to avoid the destruction of the war and yet it was included in the ERP. But unlike the other four who received quite modest sums, Iceland received a very generous amount of aid, which mostly consisted of grants. In per capita terms, Iceland received the most aid of all 16 countries, roughly twice as much as the Netherlands, which comes in second on that list.² Unlike most other ERP member countries, Iceland did not comply with many of the conditions set forth by the US government and the ECA.

During the years between 1945 and 1960 most countries in Western Europe were beginning to remove trade barriers, adopt economic policies that promoted balanced macroeconomic management, and embracing international cooperation through newly formed multilateral organisations like the OEEC and the IMF.

² Gunnar Á. Gunnarsson, "Ísland og Marshalláætlunin 1948-1953," *Saga* 34:1 (1996): 96.

Iceland, however, maintained extensive protectionist policies, using a complex system of high tariffs, import quotas, and rationing of imported consumer goods. Iceland was not an active participant in the international institutions, and the government's stance towards these organisations has been characterised as cautious and to some extent ambivalent. Finally, the public policy favoured by the government at the time prioritised growth, through ambitious state-led investment schemes, which often came at the expense of macroeconomic balance. Taking these unique features into account, the ERP in Iceland gives rise to several interesting questions. How did a small, sparsely populated island nation in the North Atlantic manage to secure such large amounts of aid without submitting to the program's conditions?

Over the years several attempts have been made to answer this question, or some variation of it, which have produced a range of theories that draw attention to different factors that shaped various dimensions of the ERP. Some have drawn attention to the unique features in the country's economy, while others have emphasised the country's strategic position and the government's strong bargaining power in its negotiations with the US. One point that is often mentioned in the literature, but rarely examined comprehensively, is the complex role that Icelandic politics play in this story. This point touches upon and connects the different theories posited about Iceland and its unique Marshall Plan.

The goal of this dissertation is to provide a detailed qualitative analysis of the role of domestic politics and how they influenced the design of the reconstruction program in Iceland. The analysis will strive to establish a meaningful understanding of complex dynamics between domestic politics and international cooperation. This appraisal of the Marshall Plan in Iceland also seeks to add new information and perspectives to the growing literature dedicated to analysing the effectiveness of aid programs and their conditionalities. Before delving into the methodology and sources selected to carry out this investigation, a short review of some literature dedicated to the study of the Marshall Plan is appropriate and

useful. The review will work to situate this case study within existing debates about the Marshall Plan, its significance, and how it should be interpreted. The review will also provide examples of approaches and several key concepts, which will guide the dissertation's analysis.

2. Literature Review

For a long time, scholars who examined the ERP were preoccupied with the goal of determining whether it was necessary for the economic revival of Western-Europe.³ Many early investigations, published shortly after the 1950s, concluded that the program played a crucial role in facilitating economic recovery. In many ways this echoed the points championed by the ECA officials and other policymakers involved in designing the program.⁴ This interpretation still holds sway over popular discourse about the Marshall Plan, which is commonly seen as one of the most successful aid programs in history. This can be seen in notions to implement other recovery programs in the same vein as the Marshall Plan, to deal with contemporary crises.

However, in the mid-1980s more critical analyses of the ERP started appearing, questioning the positive judgement about the program. Chief among the sceptics was historian Alan S. Milward. He argued that the program's impact on economic recovery in Europe was much smaller than commonly claimed. While not saying that the ERP was completely redundant, his thesis stated that the Marshall Plan was not big enough to be a vital component in placing Western-Europe on the high economic growth path that lasted until the 1970s. He claimed that the ERP served a more auxiliary role in an impressive economic recovery that was already underway in Europe at the time. The main achievement of the ERP was to provide additional dollars which had rapidly

³ Tony Judt, "Introduction," in *The Marshall Plan: Fifty Years After*, ed. Martin Schain (New York: Palgrave Macmillan, 2001), 1–9.

⁴ For a good overview of earlier interpretations see Lucrezia Reichlin, "The Marshall Plan Reconsidered," in *Europe's Postwar Recovery*, ed. Barry Eichengreen, Studies in Macroeconomic History, (Cambridge: Cambridge University Press, 1995), 39–67.

dissipated, in part because of the speed of the recovery.⁵ He dismissed assertions about the program's significant impact on European economic integration and he was also sceptical about the idea that the Marshall Plan had brought about the widespread adoption of liberal economic policies.⁶ Milward's thesis elicited a strong reaction among many of his peers that objected to his dismissal of most of the major achievements of the Marshall Plan and its historical significance. However, his first claim has endured, that the economic significance of the ERP, in terms of its effect on investment, was not as great as was commonly believed.⁷

Over the years the literature has tended to focus on evaluating the influence that the program had on economic policy making in the recipient countries and its impact on the move towards multilateral cooperation and integration. For example, in an article published in 1991, the economists Barry Eichengreen and J. Bradford De Long argued that while the certain aspects of the Marshall Plan had been overestimated, the ERP still played a crucial role in speeding up the recovery process by altering economic policymaking in Europe. They stressed the importance of the conditions of the ERP, which motivated the recipients to lower trade barriers and adopt balanced macroeconomic management practices, which paved the way for rapid growth. They concluded that the ERP "should be thought of as a large and highly successful structural adjustment program."⁸

Those who examine the ERP through the lens of the Cold War see the program in a more favourable light. For instance, the American historian Michael J. Hogan concluded in his widely read book from 1987, that the ERP was an immensely successful foreign policy initiative. He states that through the program the US managed to establish a strong front, which buttressed the

⁵ Alan S. Milward, *The Reconstruction of Western Europe, 1945-51* (London: Routledge, 1984), 356–366.

⁶ Alan S. Milward, *The Reconstruction of Western Europe, 1945-51*, 377–385.

⁷ Irwin Wall, "The Marshall Plan and French Politics," in *The Marshall Plan: Fifty years After*, ed. Martin Schain, (New York: Palgrave Macmillan, 2001), 168.

⁸ Barry Eichengreen and J. Bradford De Long, "The Marshall Plan: History's Most Successful Structural Adjustment Program", *NBER Working Papers*, no. 3899: 2–5.

communist influence from gaining ground in Western Europe.⁹ In a more recent book published in 2018, the American economist Benn Steil claims that the unique context of the geopolitical struggle, along with the fact that Western-European governments were more natural allies and well aligned to put the aid into effective use, made the Marshall Plan a unique aid program with limited bearing outside of the Cold War context.¹⁰

This seems to be the interpretation in the literature that focuses on aid and conditionality in general. In chapter published in the *Handbook of Development Economics*, the economist Jonathan R. W. Temple, writes that ERP, specifically in terms of structural adjustment, can be considered a success. But, crucially, also stresses that these achievements were possible because the program was rebuilding something that was already there. He adds that, the consensus is that the ERP achievements are impossible to reproduce because of the special circumstances of the Cold War, that heavily influenced the programs.¹¹ His chapter also provides clues about the role of domestic politics has in shaping the effectiveness of aid programs. For instance, factors like political equilibrium in the aid receiving country and the quality of the political leadership do seem to have significant influence over the effectiveness of aid programs.¹²

In an article published in 2001, the historian Kathleen Burke gave a thorough overview of the historiography of the Marshall Plan and demonstrated the areas that have been examined thoroughly and where more research could be done. For instance, Burke argues that a lot of the historiography has been dominated by American-based historians, who primarily use documents found in American archives. She pointed out that authors such as Michael J. Hogan, who relied almost solely on American sources of evidence, risk underestimating the role of

⁹ Michael J. Hogan, *The Marshall Plan: America, Britain, and the Reconstruction of Western Europe, 1947-1952* (Cambridge: Cambridge University Press, 1987), 430–442.

¹⁰ Benn Steil, *The Marshall Plan. Dawn of the Cold War* (Oxford: Oxford University Press, 2018), 339–376.

¹¹ Jonathan R. W. Temple, “Chapter 67 - Aid and Conditionality” *Handbook of Development Economics*, Vol. 5 (Bristol: University of Bristol Department of Economics, 2010), 4417–4423, 4439–4443.

¹² Jonathan R. W. Temple, “Chapter 67 - Aid and Conditionality”, 4454–4458.

the aid recipient governments. She cites numerous studies, which examine countries that are often left out of the more popular narratives, like Milward's and Hogan's famous accounts. Finally, she demonstrates how the case-studies centred on the countries that have been left out of the larger narratives provide meaningful insights into the dimensions, motives, and complex interplay between international relations and domestic politics that lie behind large-scale foreign policy initiatives, like the ERP.¹³

Despite giving a good overview of research done on the smaller countries that took part in the program, Burk does not provide any examples of research done on the Icelandic ERP. That is because next-to-nothing has been written in English about the subject. There is more existing literature in Icelandic and most of the theories that explain the unique features of Iceland's ERP can be found in that section of the literature.

Over the recent 10 to 15 years there has not been a lot of research published about Iceland's ERP. To a large degree, the early appraisals and narratives written by contemporaries of the ERP in Iceland are still core texts in the literature. These articles were written by individuals who were quite involved with the Marshall Program, being either directly responsible for administering it or involved in the political debate surrounding it. As a result, the accounts are often quite biased towards each author's political beliefs and their involvement with the ERP.¹⁴ However most agree that the severity of the economic crisis, which Iceland went through between 1948 and 1951, warranted the inclusion of Iceland in the economic relief program. The difference in opinion lies in what determined the size of the aid, its implementation and to what extent the program affected the economy.

¹³ Kathleen Burk, "The Marshall Plan: Filling in some blanks," *Contemporary European History* 10, no. 2 (2001): 267–275.

¹⁴ See for instance *Frá Kreppu til Viðreisnar: Ættir um hagstjórn á Íslandi á árunum 1930-1960*, ed. Jónas H. Haralz (Reykjavík: Hið Íslenska Bókmenntafélag, 2002). This book contains the most widely read appraisals of economic policy making during 1930-1960, the contributions are written by economists directly involved with public policy at that time.

The most cited article among these accounts is one written by Þórhallur Ásgeirsson, who served as permanent secretary of the Ministry of Commerce during the ERP years. The article was published in 1956, two years after the Icelandic government had declared the Marshall Plan over. The article echoes triumphant speeches given by Icelandic government officials at that time, who declared the program an overall success. However, detailed statistical information provided in the article about the program's size, the composition of the aid delivered, and how it was spent, have made it a valuable primary source, which might explain the longevity of its relevance in the literature.¹⁵

It was not until much later that more critical appraisals of the program began to surface. In those articles and book chapters, scholars compare the stated goals and purposes of the ERP, and its achievements in other countries, to how things unfolded in Iceland. They all observe that the Icelandic ERP presents an unusual case that elicits the numerous puzzling questions mentioned in the introduction.

The Icelandic historian Valur Ingimundarson, who has spent decades studying the relationship between Iceland and the US government during the decades of the Cold War, provides a convincing argument that explains many factors that produced Iceland's unique ERP. He argues that the generosity and lenient attitude of the US towards the Icelandic government and its economic management can be explained by the strategic importance of the island nation, and the US' desire to maintain a military presence in Iceland to fortify the North Atlantic against the Soviet Union aggression. To accomplish this, the US government needed to maintain a friendly relationship with Icelandic authorities and support the parties in government who were favourable towards a US military presence there. Funneling large amounts of economic aid and forgoing certain conditions was the price they paid to secure these strategic interests.¹⁶

¹⁵ Þórhallur Ásgeirsson, "Efnahagsaðstoðin 1948–1953," *Fjármálatíðindi*, 2 (May-June 1956): 61–70.

¹⁶Valur Ingimundarson, "Buttressing the West in the North: The Atlantic Alliance, Economic Warfare, and the Soviet Challenge in Iceland, 1956–1959," *International History Review* 21, no. 1 (1999): 102; see also Þór Whitehead, "Leiðin frá hlutleysi 1945-1949," *Saga* 29:1 (1991): 78–81, 86–100.

In an article written by Guðmundur Jónsson, professor of economic history at the University of Iceland, in which he examines the reticent attitude of the Icelandic government towards European cooperation and integration, he argues that the unique structure of the country's economy made it very difficult to adopt the policies that were being embraced by other members of the OEEC.¹⁷ When Iceland's commercial interests are considered, as well as its reliance on a single export commodity, and the wide-ranging effects the war had on the economy, it is easier to understand and sympathise with the narrow set of choices and pressures faced by policy-makers in Iceland. Guðmundur also stresses the significance of domestic politics, particularly the strong preference for growth and investment over balanced macroeconomic governance, that was shared among politicians across parties in Iceland.¹⁸

Other scholars have made similar observations, for instance, the economist Sigurður Snævarr describes economic policymaking during the fifteen years from the end of the war until 1960, as being characterised by tensions between two opposing schools of thought in economic policymaking. One favoured state driven growth and investment strategies and protectionist policies designed to influence domestic consumption and shield domestic industries. The other, inspired by more recent economic theories, emphasised policies that promoted macroeconomic stability and advocated for trade liberalisation and international cooperation. During the ERP years, the coalition governments which governed at the time vacillated back and forth between these two schools of thought. For instance, soon after taking what had seemed like firm steps towards adopting the newer policies in the spring of 1950, by devaluing the currency by close to 43 per cent and abolishing numerous trade restrictions, the government quickly reverted back to its previous practices after a series of economic shocks. Ten years would pass until the government attempted to adopt these liberal practices, which ushered in a period of growth that lasted until 1973. It has been

¹⁷ Guðmundur Jónsson. "Iceland, "OEEC and the trade liberalisation of the 1950s," *Scandinavian Economic History Review*, 52:2-3 (2004): 62-84.

¹⁸ *Ibid*

argued that one of the reasons for the longevity of these isolationist policies is the complex and volatile political situation of that time.¹⁹

The most recent article by an unaffiliated researcher, that focuses solely on the Marshall Plan, was written by political scientist Gunnar Á. Gunnarsson and published in 1996. In the article the author examines how domestic politics, mainly party-politics and political intrigues, influenced the design of the ERP in Iceland. Gunnarsson uses a lot of archival sources from the Ministry of Foreign Affairs and the Ministry of Commerce. Although he manages to provide an original and interesting thesis to explain several curious features in the design and implementation of the ERP in Iceland, his argument that the negotiations were as sinister or corrupt as he makes them out to be not entirely convincing.²⁰

The Marshall Plan and how it unfolded, not only in Iceland but in many other small or peripheral states, is an under researched subject. Examining cases like Iceland can offer scholars a lot of meaningful information about the complex dynamics that shape how foreign aid is given and received, and how it is used. A project like this involves examining asymmetric power dynamics; both political and economic; geopolitics like Cold War strategy and containment; and the relationship between domestic politics and international relations. All these factors create a unique outcome in the case of Iceland and a detailed analysis of how this transpired will produce compelling results.

3. Methodology and sources

This analysis will make use of archival evidence, both Icelandic and American, that demonstrates the significance of domestic political concerns in influencing the choices of both Icelandic and US policymakers involved with designing and carrying out the ERP in Iceland. These sources will also inform the approach taken when examining the second set of primary sources analysed here.

Newspaper articles provide a useful glimpse into the discourse surrounding

¹⁹ Sigurður Snævarr, *Haglýsing Íslands* (Reykjavík: Heimskringla, 1993), 55–66.

²⁰ Gunnar Á. Gunnarsson “Ísland og Marshalláætlunin 1948-1953,”: 109-119.

certain topics and ideas that were prevalent at the time. In this dissertation the four major newspapers that were published at the time will be examined. They were all widely circulated and read by most Icelanders. Each newspaper publication was owned and operated by one of the four main political parties in Iceland: the rightwing Independence Party (IP), the centrist agrarian Progressive Party, the Social Democratic Party, and the The People's Unity Party – The Socialist Party, commonly referred to as the Socialist Party (SP).

Thus, the newspapers each represent one of the four parties that competed for seats in parliament. Since this dissertation is intended for English speaking readers the Icelandic names of these publications will be abbreviated into acronyms or appropriate translations. *Alþýðublaðið* (hereafter referred to as *ABL*), was a widely read and distributed paper which had close connections with the Social Democratic Party. *Tíminn* (hereafter referred to by its English translation, *The Times*) was a daily newspaper founded in 1917 and throughout the 20th century it was edited by members of the Progressive Party. *Morgunblaðið* (hereafter referred to by the acronym *MBL*) is a daily morning newspaper first published in 1913 that is still operating today.²¹ Since its founding it has always retained a close connection with the dominant right-wing party, the Independence Party. *Pjóðviljinn* (which roughly translates as the *Nations Will*, will be referred to as NW) was a daily newspaper that began its publication in 1936 and ceased operating in 1992. It was founded and edited by one of the founders of the Icelandic Communist party (originally formed by more radical members of the Social Democratic party in 1922), which in 1938 splintered into a new party: the so-called Popular unity Party or the Socialist Party.

4. Statistical overview of the Icelandic ERP

In the 1955 article -by Þórhallur Ásgeirsson, who then served as permanent secretary of the Icelandic Ministry of Commerce, Ásgeirsson provides a useful

²¹ All of these newspapers are accessible on the digital library Timarit.is.

overview of the ERP in Iceland. The ministry was largely responsible for administering the transactions involved with the importation of American goods, which was the main component of the aid program. The payments for these imports, paid in the local currency, were deposited into a so-called Counterpart Fund. The accumulated balance of this fund would later be used to finance large infrastructure and industrial projects, during the final years of the reconstruction program. As such the article is a valuable primary source, providing accurate and complete figures relating to the size and nature of the aid program in Iceland. Ásgeirsson begins with providing figures that measure the financial aid that Iceland received, broken down into three categories: grants, loans, and conditional grants. The amount of aid is shown in table 1 and is provided in US dollars and Icelandic krona (based on the exchange rate at the time of the article’s publication in the spring of 1955).²²

Figure 1. Economic Aid received 1948–1953.

| Type of Aid | Dollars | ISK |
|--------------------|-------------------|--------------------|
| Grants | 29.850.000 | 486.257.00 |
| Loans | 5.300.000 | 86.337.000 |
| Conditional Grants | 3.500.000 | 57.015.000 |
| Total | 38.650.000 | 629.609.000 |

(*Source*: Þórhallur Ásgeirsson, “Efnahagsaðstoðin 1948-1953”: 61)

As can be seen from table 1, the program primarily consisted of grants, first issued in dollars and later in European currencies, after the founding of the European Payments Union in 1950. These grants took the form of purchasing authorisations which the recipient country used to import American goods, and later European products, in exchange for payment in the recipient country’s currency. This measure was designed to prevent shortages of vital supplies, which were an imminent threat to many European nations at the time, that had exhausted their foreign currency reserves and had a balance of payment deficits.

²² Þórhallur Ásgeirsson, “Efnahagsaðstoðin 1948-1953”: 61-70.

Initially the imports mainly consisted of essential goods like foodstuffs, animal feed, and fuel; products that Iceland could not provide on its own.

Figure 2. US Contribution (in millions of dollars)

| US Fiscal Year | Grants | | Loans | Conditiona l Grants | Total |
|----------------|-------------|--------------|------------|------------------------|--------------|
| | Direct | EPU | | | |
| 1948/49 | 2.5 | – | 2.3 | 3.5 | 8.3 |
| 1949/50 | 5.0 | – | 2.0 | – | 7.0 |
| 1950/51 | 5.4 | 7.0 | – | – | 12.4 |
| 1951/52 | 0.6 | 3.9 | 1.0 | – | 5.5 |
| 1952/53 | 1.2 | 4.25 | – | – | 5.45 |
| Total | 14.7 | 15.15 | 5.3 | 3.5 | 38.65 |

(Source: Þórhallur Ásgeirsson, “Efnahagsaðstoðin 1948-1953”: 61)

Figure 2 illustrates the change in Icelandic government policy with regards to the ERP. Initially the plan was to join the program for the purposes of promoting Icelandic exports, and not apply for grants. The government did, however, take loans to invest in the renewal of the fish trawler fleet and machinery for fishmeal processing plants. The Conditional grants, reported in the breakdown, came in the form of a deal struck between Iceland and the US 1948, where the US facilitated trade in frozen fish between Iceland and Germany, which was dealing with serious currency issues at the time. The US paid for the shipment in dollars and delivered the stock to Germany in exchange for their inconvertible currency.

However, as the economic situation deteriorated Iceland applied for grants, near the end of 1948. The grants increasingly began to cover purchases of machinery, machine parts, and other materials, used to modernise the agricultural sector and fishing industry. In the spring of 1950, the ECA agreed to assist in the construction of two hydroelectric plants and later that same year to assist with the construction of a fertiliser plant. After that most of the dollar grants went into those three projects. Out of the 29.8 million dollars of grants, close to 7.85 million dollars was used to import building material and machinery that would be used in the construction of the projects.

The three big investment projects also received direct financial support from the ECA by authorising the government to withdraw roughly 117 million ISK from the counterpart fund, which it could then lend to the three projects. The ECA also provided direct financial loans to the projects, in total close to 75 percent of the initial capital needed for the three projects came from the US aid program. In 1953 counterpart fund, along with the bonds in hydroelectric stations and the fertiliser plant, was transferred into the custody of the newly established Iceland Bank of Development.²³

To an outside observer, these figures might not seem particularly high, when compared to the billions of dollars that went to the major economies in Western Europe. However, during these years, close to 25 percent of Iceland's imports were financed with ERP and EPU currency. From 1950 to 1953, ERP assistance accounted for close to 20-25 percent of gross domestic investment. At its height, in 1950-1951, ERP share of gross domestic investment was close to 46 percent.²⁴ In comparison, in Germany, which had been devastated in the war, the ERP reached up to 25 percent of domestic investments at the program's height.²⁵

5. Analysis of evidence from Icelandic and American archives

Upon examining the archival evidence from US National Archives and the Icelandic Ministry of Commerce, it quickly emerges how prominently domestic political concerns featured in the design and implementation of the ERP. There are numerous examples in the vast array of reports, correspondence, memorandums, and minutes that have been preserved in each document collection. There are, in fact, so many examples that presenting and discussing them at length would go beyond the scope of this dissertation. To stay within the dissertation's restrictions, the analysis will be limited to a handful of documents.

²³ Sigurður Snævarr, *Haglýsing Íslands*, 400, 483.

²⁴ Þórhallur Ásgeirsson "Efnahagsaðstoðin 1948-1953", *Fjármálatíðindi*, 2 (maí-júní 1956): 70;

²⁵ Charles Maier, "Introduction", *The Marshall Plan and Germany: West German development within the framework of the European Recovery Program*, ed. Charles Maier (New York: Berg, 1991), 7.; see also Valur Ingimundarson, *Í Eldlínu Kaldastríðsins* (Reykjavík: 1996), 158.

Each document examined here has been carefully selected by taking into consideration their significance and the extent to which they demonstrate the dynamics being analysed. First, the archival evidence that can be found in Icelandic records will be examined.

5.1 Records from the Icelandic Ministry of Commerce

After going through numerous official documents that can be found in the somewhat disorganised bundle of the Marshall Plan, which contains an assortment of different types of records from the Ministry of Commerce kept in the National Archives of Iceland several key pieces of evidence can be found and will be discussed further here. These documents reveal the governments preferences and priorities towards the ERP, and the role that domestic politics plays in informing their choices.

We begin with a correspondence letter, between the Icelandic ambassador in Washington, Thor Thors, and the Minister of Foreign Affairs, Bjarni Benediktsson, dated December 4, 1948. In it, Thor writes that he agrees with the minister that the optimal route for securing the government's interests, with regards to the ERP, is to bypass the OEEC and instead communicate directly with State department and ECA staff members in Washington. It is quite curious to see the government adopt this strategy so early on in the process, especially since the initial reasons for Iceland's participation was to get a seat at the table in OEEC. The change in government's stance towards OEEC has been explained by early disappointments and frustrations with the early OEEC conferences and meetings held in Paris several months before.²⁶ We can see this attitude towards the OEEC all throughout this period. For instance, in a memorandum of conversation between the ambassador, Thor Thors, and the ECAs Director of European Program Division, dated December 29, 1950, the ambassador stresses the government's preference for negotiating with the US government directly. When asked why they do not want to submit their

²⁶ ÞÍ. Viðskiptaráðuneytið (e. Ministry of Commerce), Marshallaðstoðin 1948-1952 (1994 B/234), Letter from Thor Thors to Bjarni Benediktsson (December 4, 1948).

proposals to OEEC, Thor responds quite bluntly, stating that the Icelandic government has not had good experience with dealings with the OEEC. Describing the consultation process as too slow and rigid. On top of that he adds that the negotiation process is quite antagonistic, which has produced unsatisfying results for the government.²⁷

It certainly seems to be the case that Icelanders were met with a more accommodating audience in Washington, that was sensitive to the circumstances and needs of the government. Especially when it came to matters such as domestic political concerns. There are numerous examples to be found which show Icelandic officials making references to the delicate political situation as a reason for requests to either get higher amounts of aid or to accelerate the delivery of the already approved loans or grants. Early on the political concerns that were referenced, concerned the pressing need to prevent further decreases in the standard of living and fears that it would lead to strengthening of the Socialist party. Later when the three big investment projects had been approved by parliament, we can see that one of the main arguments for getting the US to help sponsor these projects is that they will strengthen the government's popular approval, which they argue is necessary to carry out the measures towards stabilising the economy.²⁸

These arguments seem to have persuaded the US officials. On the few occasions where the ECA responds negatively to these governments' requests, or voices scepticism towards their ambitious investment plans, the Icelandic officials react quite strongly. For example, in late 1948 and early 1949, when the Icelandic government had changed its stance towards applying for economic aid, the ambassador in Washington visited several department heads of the ECA in Washington to ask them for rapid delivery of grants. Sensing the hesitation

²⁷ ÞÍ. Viðskiptaráðuneytið (e. Ministry of Commerce), Marshallaðstoðin 1948-1952 (1994 B/234), Memorandum from the Legation of Iceland Washington 6 D.C. (Thor Thors), (December 29, 1950).

²⁸ ÞÍ. Viðskiptaráðuneytið, Marshallaðstoðin 1948-1952 (1994 B/234), Memorandum (August 15, 1952).

among the ECA officials, Thor gives them an ultimatum, either the US agrees to provide Iceland with the requested dollar grants, or Iceland would leave the ERP.²⁹ These documents clearly demonstrate that the Icelandic officials were keenly aware of their strong dealmaking position towards the US government. In correspondence between Thor Thors and Þórhallur Ásgeirsson, dated June 11, 1951, we can see the Icelandic negotiating strategy laid out, in clear terms. The primary objective is to acquire as much assistance from the US as possible, and get it without going through time consuming procedures and scrutiny.³⁰ The next section will provide a clearer picture of US priorities towards Iceland and how that informed their lenient stance towards the country.

5.2 US policies towards Iceland and its reconstruction program

Almost a year before the Icelandic government signed the agreement to join the ERP, State Department officials began examining the economic and political situation in Iceland and opportunities for the US to influence certain outcomes that would secure their interests with the small island nation. By then they anticipated that the government would soon be compelled to seek outside assistance and began drawing up plans on how the US could provide such assistance. One factor that motivated the preparation of those plans was based on their fears that a rapid decline in living standards, that seemed to be imminent, might lead to increased support for the Socialist Party at the expense of the three-party coalition. They feared that should the Socialists re-enter government it would spell the end of US military presence in Iceland, and possibly align the country with the Soviet bloc through bilateral trade treaties. The report recommends that the aid program take these considerations into account and be designed and implemented in a way that would strengthen the current government, work towards isolating the Socialist Party, and prevent

²⁹ ÞÍ. Viðskiptaráðuneytið, Marshallaðstoðin 1948-1952 (1994 B/234), Memorandum of conversation between Thor Thors and ECA officials about grant allotments (January 14, 1949).

³⁰ ÞÍ. Viðskiptaráðuneytið, Marshallaðstoðin 1948-1952 (1994 B/234, Letter from Ambassador Thor Thors to Þórhallur Ásgeirsson (June 11, 1951).

them from gaining ground.³¹ As will be seen in other documents, this was a primary concern that influenced the -decision making of US government officials throughout the Marshall Plan years.

Two years later, when the Icelandic government had decided to issue a request for ERP grant allotments, which it had initially intended to forgo, the ECA sent the economist E. Harrison Clark to the country to assess the situation and provide recommendations on strategy moving forward. Along with examining the economic situation and the aid requirements needed to confront economic hardships, Clark also analysed the political situation and to what extent it should have factored in the decision-making process of the Marshall planners in Washington. His report on the political situation was quite striking; he reported that the coalition government, held together by a series of compromises, was on the verge of breaking apart and unable to carry out adequate measures to ensure economic stability. He went on to describe “a rather appalling lack of knowledge of economic causes and consequences” among the politicians and government officials, that prevented them from dealing with the rampant inflation.³² On top of that he mentioned that the Socialist Party had just succeeded in forcing through wage increases, which further upset the government’s deflationary measures. He reported that the cabinet would fall in October and a general election would commence. He added that all the political parties had started campaigning and the political discourse was primarily focused on domestic political issues. He believed the unrest had diverted attention away from the ECA and the Marshall Plan. He also shared his concerns about Communist activities in the country, which he believed were growing in strength.³³

³¹ National Archives [NA] (Maryland), Record Group [RG] 341 Air Force – Plans Project Decimal File, PD 400.329 Iceland (11 July 47) (US Aid To), Box 837: Report, “Study of Possible Extension of US Aid to Iceland,” 11. June 1947.

³² NA, RG 469, Records of the US Foreign Assistance Agencies, 1948–61, Mission to Iceland, Office of the Director, Subject Files, 1948–53, Correspondence-Finance: Report, “Report on Iceland” (Harrison Clark), no date (1949).

³³ *Ibid.*

Considering all these different factors, he concluded by recommending that the ECA treat Iceland rather differently than other countries in Europe. He argued that the ECA should refrain for now from pressuring the government to make rapid changes to their fiscal and monetary policies. He stated that “there has to be a fair amount of carrots and a rather thickly velveted stick.”³⁴ The report is a remarkable piece of evidence that clearly shows how sensitive the Marshall Planners were towards the political situation in Iceland, and the significant degree to which it factored in their policies towards the government. Clark’s recommendations, to acquiesce to the political objectives and needs of the pro-Western parties in government, would turn out to be a dominant and enduring factor that influenced the decisions of the ECA throughout the duration of the ERP. The report revealed other factors, also identified in recent studies, for instance old-fashioned economic theories that had a hold over many policymakers and their reluctance to adopt liberal economic ideas that were spreading across other OEEC countries at the time.³⁵

Almost a year after the 1949 elections and the establishment of a two-party coalition government formed by the Progressive Party and the Independence Party, the American ambassador in Iceland met with the Minister of Foreign Affairs to discuss the new government’s economic plans and their aid requirements. In a memorandum that describes the conversation that took place in late October 1950, it is reported that the main topics of the discussion were the three big investment projects that the government had placed on the agenda, with plans to begin construction as soon as possible. At the time the Icelandic government had begun to petition the ECA to assist with financing the investment projects. The memo brings attention to the fact that the foreign minister had begun to involve himself in the negotiations with the US government, which was interpreted as a sign of the high importance that the Icelandic government placed on these projects. It is also recounted that these projects and the pressure from the government to secure finance for them are

³⁴ Ibid.

³⁵ Ibid.

clearly motivated by a political deal struck between the two governing parties. Reporting that it is a “more or less understood agreement between the Conservative and Progressive parties that if the priority construction of the electric power plants, so desired by the Conservative elements, were approved, then the second most important program, namely the construction of the fertiliser plant, would be approved by the Government.”³⁶

The Icelandic government succeeded in their efforts to secure aid and assistance for these grand projects, despite concerns voiced by the ECA officials about high costs and limited economic benefits the projects would generate in the short term. They were particularly sceptical of the economic rationale behind prioritising the construction of the fertiliser plant.³⁷ They warned the Icelandic government of the inflationary effects of these costly projects and tried to convince them to scale down their size and put in place additional deflationary measures to offset the effects of these investments. But to a large degree, the government got what they wanted from the ECA and gave little in return, in relation to following ECA policy recommendations.³⁸

When the ECA was replaced by the MSA in October 1951, the future of the program being carried out in Iceland, and the investment projects that were underway, were thrown into uncertainty. The tightening of the budget and the change in policy, which the MSA was charged with carrying out, came at delicate time for the two-party coalition government which had at the time begun the construction of one of the hydroelectric plants and had plans to begin construction of the second power plant and the fertiliser plant in the following year. To secure these projects, which both parties had championed among their constituents, the government began lobbying the MSA to continue providing the

³⁶ NA, RG 59, Central Decimal File, Box 3503: Memorandum (Edward B. Lawson) 19. October 1950.

³⁷ NA, RG 469, Records of the US Foreign Assistance Agencies, 1948–61, Mission to Iceland, Office of the Director, Subject Files, 1948–53, Telegrams relating to the Recovery Program, 1949–50, Box 1: American Embassy (Paris) to ECA, September 26, 1949.

³⁸ NA, RG 469, Records of the US Foreign Assistance Agencies, 1948–61, Mission to Iceland, Office of the Director, Subject Files, 1948–53, Box 11: “Comments on the Proposed Allotment for Assistance to Iceland,” no date (February 1951).

financial aid necessary to finish these projects. A memorandum of a meeting between an MSA representative and Benjamín Eiríksson, one of the government's main economic advisors, captures the essence of the negotiations between the government and the MSA which took place late in the year 1951 and extended well into 1952. In the meeting Eiríksson states the government's bid for increased assistance, permission access, and for counterpart funds to be dispensed more liberally. In response to this request the MSA official asks Eiríksson what the government is prepared to do in return, to which Eiríksson replies that he cannot give any assurances about putting in place any deflationary or liberalising measures on behalf of the government. The reasons for this, he adds, are the same as those observed in previous documents: the government is facing external pressures and a precarious political situation, with elections on the horizon. He also adds that the government's inability to comply with MSA policy recommendations can be explained by the "tendencies" of the present coalition leadership.³⁹ In his book, Valur Ingimundarson, observes that the MSA, much like its predecessor organisation, eventually relented in the negotiations and decided to continue assisting the government with the three big investment projects.⁴⁰ However, as informative as this archival evidence is, it lacks any nuanced descriptions of the domestic political concerns that are brought up so often in the evidence that we have examined.

6. Analysis of the political discourse gathered from the four newspapers

The discourse surrounding the Marshall Plan, as presented in the four main political newspapers of the time (ABL, The times, MBL and NW), provides useful material that allows for an examination of the politics which seem to have influenced choices of Icelandic and American authorities, and the design of the ERP in Iceland. By examining articles and opinion pieces published over the years that the program spanned, an observation can be made of the differences

³⁹ NA. RG 469, Records of the US Foreign Assistance Agencies, 1948–61 . Mission to Iceland. Office of the Director. Subject Files, 1948-53, Correspondence-Finance, Box 4: Memorandum of a Conversation between R. G. Birnberg and Benjamín Eiríksson, September 18, 1952.

⁴⁰ See Valur Ingimundarson, *Í eldlínu kalda stríðsins*, 242–247.

and similarities between the parties in how they interpreted the ERP to fit their policies and political agendas. By examining these sources, it is possible to flesh out key themes in the political discourse surrounding the Marshall Plan. To fit the scope of this dissertation the analysis will be narrowed to examining the discourse surrounding selected key themes. During the late 1940s up to the 1960s, the four parties wielded considerable leverage over various key interest groups, public and private organisations that influenced the livelihoods of ordinary citizens in Iceland. During this time, they also maintained a strong hold over the political discourse through their respective broadsheet newspapers. Each paper would present to their readers a carefully crafted narrative, designed to shape public opinion towards issues, like the ERP, in a way that aligned with the policies of each party at the time.⁴¹

Following is an examination of the debate between the supporters of the ERP and its opponents. This debate, and the political struggle that it echoes, reflects mounting tensions between the opposing political ideologies championed by the US and the Soviet Union. Within each country, the Cold War intensified the political disputes and conflicts between political parties that supported the opposing political ideologies. As demonstrated in the archival sources, preventing the Socialist Party from seizing control was a big factor that influenced the decisions of both American and Icelandic agents involved with crafting the ERP. We then turn towards examining a debate about macroeconomic and monetary policy issues, between the three, pro-Marshall Plan parties, that began mounting in 1949. This debate was motivated by a more complex web of traditional political quarrels between the parties, which represented different sections of society which supported contrasting policies, depending on their specific needs and interests. As the economic situation worsened, these differences became more pronounced, and eventually led to the breakup of the broad coalition that had been maintained since 1947. The final section of this chapter will examine the discourse surrounding the Marshall Plan after the crisis of government came to an end, with the formation of a two-party government, composed of the IP and

⁴¹ Gunnar Á. Gunnarsson, “Ísland og Marshalláætlunin”, 114–119.

PP. Here the focus will be on the role of ERP in the new, more narrow, political equilibrium that was established with the coalition government.

6.1 Cold War discourse, nationalism, and the ERP

The breakdown of the coalition government, which was made up of the IP, the SDP and the SP, in late 1946 is often regarded as the event that ushered the Cold War into Icelandic politics. The 1940s and 1950s are characterised by the considerable difficulty that the parties had overcoming their differences to form an effective government. The coalition, often referred to as the ‘Innovation Government’, was an ambitious and radical political experiment that has garnered a lot of attention from Icelandic scholars since its formation in 1944. It was the first time the Socialist party had entered into government, but they were responsible for its untimely end. In late winter 1946 the SP left the coalition after an agreement was signed with US government, which provided the US army a 6-year extension to operate a military base near the village of Keflavík.⁴²

Soon after the breakup of the Innovation Government, the SDP, IP and PP came out in support of Western alignment. These parties formed a coalition government and collectively worked towards isolating the Socialist Party. Shortly after Iceland was offered to join the ERP, all three partnering parties came out in favour of Iceland’s membership of the ERP and each party’s paper communicated a similar message. Emphasis was placed on the merits of international cooperation and the commercial opportunities that the membership offered Icelandic exports. The papers all asserted that Iceland’s participation did not entail any disadvantageous binding constraints or restrictions.⁴³ Crucially, the government’s stance at that time was to not apply for any aid, except for occasional loans and assistance to facilitate export transactions to other ERP

⁴² Helgi Skúli Kjartansson, *Ísland á 20.öld*, (Reykjavík: Sögufélag, 2002), 237; Jens B. Baldursson, *Nýsköpunarstjórnin: aðdragandi og upphaf* (Reykjavík: Rót, 1979), 5- 6.

⁴³ Bjarni Benediktsson “Þátttaka í Marshalláætluninni Íslendingum brýn nauðsyn”, *Morgunblaðið*, April 9, 1948, 1, 3, 12; Gylfi Þ. Gíslanón, “Marshalláætlunin er mikið hagsmunamál fyrir Íslendinga” *Alþýðublaðið*, April 27, 1948, 5; *Tíminn*, July 6, 1948, 1.

member states that lacked convertible currency at the time. At this point in time the government interpreted its role in the ERP to be that of a commercial partner that could lend a helping hand to the reconstruction efforts, particularly by providing fish products to the devastated countries in Europe.⁴⁴

The ERP was met with fierce opposition from members and supporters of communist parties, which operated in many European countries at the time. They saw the Marshall Plan as an attempt to consolidate American political and economic dominance over Europe and interpreted it as a direct assault on socialist ideologies in each of the participating countries. According to them, the ERP was a thinly veiled conspiracy designed to subvert the will of the labouring classes and undo all the achievements of the organised labour movement over the years. The end goal, they argued, was to eliminate socialist ideology from the political spectrum. They also made the case for another hidden objective behind the ERP: to bring about changes in the European economies which would open them up to exploitation by American free-market capitalists. These concerns were also voiced by the Icelandic Socialist Party, numerous lengthy speeches in Parliament and scathing articles published in their paper *NW*.⁴⁵ In many ways the criticisms voiced by the Socialist Party in Iceland echoed the arguments levied by other leftist-, socialist parties in Europe.⁴⁶

The Socialists would also make use of nationalist arguments and invoke ideas about sovereignty, neutrality and freedom from foreign influence. These ideas were quite potent at the time, with Iceland having recently gained complete independence in 1944. For instance, one criticism that the *NW* frequently brought up was a condition in the ERP agreement, which stipulated that recipient countries must permit American private businesses to operate in their countries. In their articles, they warn that this condition will grant powerful American companies the opportunity to dominate private business in Iceland,

⁴⁴ *Alþingistíðindi* 1947 D, 120.

⁴⁵ *Alþingistíðindi*, 1948, B, 1972.; *Þjóðviljinn*, March 23, 1948, 3; *Þjóðviljinn*, April 7, 1948, 1, 8; *Þjóðviljinn*, January 14, 1949, 5.

⁴⁶ Benn Steil, *The Marshall Plan*, 179–195.

drawing comparisons to the infamous Danish monopoly trade of centuries past. By signing the agreement, Iceland was effectively replacing one foreign ruler, for another.⁴⁷

The pro-Western parties in Iceland, and their papers would turn the Socialist argument, about surrendering to foreign influence, around, and accuse the party of taking orders from the Soviet Unions and conspiring to overthrow the democratic government to instil an autocratic socialist regime that would serve another foreign master. The other publications responded to the alarming claims that the NW made about the conditions of the ERP agreement. Dismissing them as flagrant attempts to mislead the public about the ERP by deliberately misrepresenting or exaggerating certain stipulations of the agreement and their effects on the economy. They often warned their readers that communists everywhere in Europe were working desperately towards sabotaging the reconstruction program to prolong the economic hardship, which the three parties argued the Socialists would use to gain power. Upon examining the response articles in the three pro-Western papers, it is striking to see how coordinated they are in their messaging about the merits of the ERP.⁴⁸

However, when the economic situation began deteriorating at a rapid pace in the summer of 1948, the government changed its initial stance towards the ERP and began applying for a share of the grant allotments. This prompted a fierce response from the SP, which accused the government of misleading the public. By applying for grants, or 'bribes' as NW called them, the government was committing itself to a series of unfavourable conditions. In the NW reporters regularly reminded their readers of the assertions that the foreign minister, Bjarni Benediktsson, made in 1947, that the government would avoid seeking direct grants.⁴⁹ In response to this, MBL published a speech that Benediktsson held in Parliament in May 1948, where he admitted that the circumstances had

⁴⁷ *Þjóðviljinn*, April 24, 1948, 4.

⁴⁸ *Alþýðublaðið*, April 10, 1948, 4; *Týminn*, July 8, 1948, 5; *Morgunblaðið*, October 10, 1948, 8.

⁴⁹ *Þjóðviljinn*, September 29, 1948, 5.; *Þjóðviljinn*, March 15, 1949, 8.

forced him to reconsider his stance. He adds that his party, unlike the SP, has the strength of character to change their mind on issues, when confronted with circumstances that threaten material well-being of the country's citizens.⁵⁰ After the government's application for grant allotments was granted by the ECA, pro-ERP papers started arguing that the Marshall grants were simply too good of an offer to pass up, especially considering the circumstances.⁵¹

As the economic situation continued to deteriorate, with inflation skyrocketing, into the year 1949, one of the criticisms that the NW levied against the pro-ERP parties would become more troublesome as the months passed and elections drew closer. This criticism concerned the government's deflationary measures, and to what extent the ERP would force the government to adopt new measures that were more in line with the policies that the program favoured. NW articles warned that soon the government would be pressured by the ECA to devalue the currency. An act that will be most painfully felt by the labouring classes.⁵² This issue specifically turned out to be a hot button issue in the months leading up to the election in the autumn of 1949. Although the previous analysis of official documents indicates that the government was at no time pressured into devaluing the currency, the issue did end up fracturing the three-party coalition which resulted in a prolonged period of government crisis. But it seems that disagreement on this matter was motivated by internal pressures, within the parties which supported the measures (IP, PP) and the ones that rejected it (SPD).

6.2 Government crisis, political dealmaking and changes in policy

The economic situation continued to deteriorate, and the slump would last well into 1950. However, 1949 would turn out to be the most consequential year for the story of the ERP in Iceland. During that year the economy teetered on the verge of collapse and general elections were scheduled to take place in October.

⁵⁰ *Morgunblaðið*, May 18, 1949, 4.

⁵¹ *Morgunblaðið*, April 3, 1949, 5; *Tíminn*, May 18, 1949, 4–5; *Alþýðublaðið*, August April 3, 1949, 1.

⁵² *Þjóðviljinn*, September 17, 1948, 4; *Þjóðviljinn*, March 30, 1949, 6–7.

Currency devaluation seemed to its supporters to be the only adequate solution to break the cycle of inflation and wage increases and make the country's exports competitive again. Furthermore, many felt that the growing complexity of state bureaucracy that carried out the government's strict import and investment controls, along with the subsidies being transferred to the failing fishing industry, was becoming quite unpopular. Many began voicing the opinion that these policies had run aground.⁵³

In 1949, as the months passed, the idea started gaining serious traction among members of the PP and the IP who began advocating for the change in policy.⁵⁴ Devaluation was rejected by the SP, which ever since the signing of the ERP agreement had alleged that it would be forced upon the country by the ECA.⁵⁵ The major trade unions in the country were also opposed to the measure.⁵⁶ Finally, SDP could lend its support to measure to come out against currency devaluation. In the articles published in the ABL the party attacks their partners in government, accusing them of undermining the economic policies that the three parties had settled upon in 1947. They also warn their readers that devaluation would provoke a fierce reaction from the trade unions.⁵⁷ However, at the same time, the SDP could not ally itself with the SP. Thus, they were forced to tread a delicate line, between the two opposing sides of the debate.⁵⁸ This ambiguous stance would turn out to be politically costly. After the election the SDP lost two seats and was down to mere seven members of parliament out of 52 seats.

The clear winner of the election was the PP, which managed to secure four additional seats in parliament. With a clear majority, a two-party coalition government by the PP and the IP would have seemed a straightforward match.

⁵³ Sigurður Snævarr, *Haglýsing Íslands*, 57–59; Jónas H. Haralz, “Hvað sögðu ráðgjafarnir”, *Frá Kreppu til Viðreisnar*, 273–275.

⁵⁴ *Morgunblaðið*, May 7, 1949, 16; *Tíminn*, January 5, 1949.

⁵⁵ *Þjóðviljinn*, February 13, 1949, 4; *Þjóðviljinn*, July 26, 1949, 4.

⁵⁶ *Alþýðublaðið*, February 16, 1949, 4; See also Valur Ingimundarson, *Í eldlínu kalda stríðsins*, 166–177, he provides a detailed analysis of how the Trade Unions interacted with the ERP.

⁵⁷ *Alþýðublaðið*, September 7, 1949, 4.

⁵⁸ *Alþýðublaðið*, September 21, 1949; 4; *Alþýðublaðið*, October 6, 1949: 5.

The two parties agreed on devaluation issues, and they had a long history of working together in government. But that was not the case and the negotiation process proved long and difficult. Neither party seemed willing to make the necessary compromises to set up an effective government. The two parties finally managed to reach an agreement in early March 1950. In the meantime, a minority government led by the IP administered the country's affairs, during the months of government crisis. It has been argued that the difficulties in reaching a settlement were to a large degree due to the personal animosities between the party leaders: Ólafur Thors (IP leader) and Hermann Jónsson (PP leader).⁵⁹

Soon after the government was formed the currency was devalued by 42.6 percent, and significant steps were taken to lift trade restrictions. Other measures were introduced to promote a balanced budget. These policies represented a sharp break with previous policies that had been pursued for almost two decades. However, the government could not go as far as they wanted on these issues, and the effects of the measures turned out to be quite limited. Eventually the government would also later revert back to former policies and reinstitute some trade restrictions. There are a number of reasons for this, several economic factors like external inflation, problems finding markets for fish exports and have observed. But there is which factor that influenced this reversal, which was the change in equilibrium between the four major political parties.⁶⁰

Despite having a large majority in parliament, when the SDP left the partnership, it effectively severed the ties between government and trade unions. Together, the SDP, the trade unions, and SP, although not allied with the SDP in any sense, restricted the government's capacity to push through many of their economic reforms. The only part of the IP-PP government that could be introduced without significant objections were its investment schemes plans to begin construction of the hydroelectric plants and the fertiliser plant. Even the

⁵⁹ Helgi Skúli Kjartansson, *Ísland á 20.öld*, 237

⁶⁰ Bjarni Bragi Jónsson, "Hafta- og styrkjakerfi á Íslandi", *Frá Kreppu til Viðreisnar*, 192–209.

Socialist NW, despite criticising the select issues pertaining to the projects, is generally favourable towards the idea of having these public works built. Which reveals the penchant for large investment projects shared among politicians across parties in Iceland.⁶¹ These projects did in many ways undermine liberal policy reforms that the government had tried to instil.⁶² When their attempts to change economic management failed, all the attention went towards three big projects. This can be seen in the discourse presented in the IP papers, *MBL*, and the PP newspaper, *the Times*, especially between the years 1951 up to 1953.⁶³

In the archival evidence examined and in more recent analyses of this period in Iceland's political history, it has been argued that the deal struck between the two parties, about which investment projects should be prioritised, provided the foundation on which the coalition rested. The IP got the hydroelectric plants and in return the PP got the fertiliser plant and increased funding for other projects that benefitted its constituents in the countryside. The latter project was the most controversial part of Iceland's project of the three. Upon examining the articles published in the PP paper, *The Times*, getting this plant built is a top priority for the party. In *The Times* campaign messaging, there was a noticeable sense of frustration towards the SDP and in particular the IP, and their influence over policies on industrial investment and allocation of aid. The writers of those articles and opinion pieces felt that too much of the government's spending had gone towards strengthening the fisheries, while citizens in the countryside and agricultural industry had been ignored.⁶⁴ In these articles they make promises that the party, if it secures enough support, would strive towards correcting this imbalance. The fertiliser plant becomes a centre piece in their election campaign rhetoric.⁶⁵ Examining this discourse seems to support the claims made by American officials about the fertiliser plant being politically motivated.

⁶¹ *Þjóðviljinn*, October 16, 1953, 3.

⁶² *Morgunblaðið*, March 5, 1953, 7; *Alþýðublaðið*, June 28, 1951, 5.

⁶³ *Tíminn*, June 12, 1951, 5; *Morgunblaðið*, May 1, 1952, 8.

⁶⁴ *Tíminn*, October 8, 1950, 5

⁶⁵ *Tíminn*, June 1, 1950, 4.

After 1951 and all the way up to 1953 we can see that the debate around the ERP began to settle down and become less prominent in the public discourse. In the few articles that discuss the ERP, the focus is almost entirely placed on the big three projects and their significance for the Icelandic economy. This sentiment is perfectly captured in a radio address, given by Björn Ólafsson (IP party member) then the Minister of Commerce, May 15, 1953. In his speech he announces that the recovery program has come to an end, after the government had notified the US authorities that Iceland would not be needing more financial assistance. The reason for this decision is that the US has supplied the country with enough capital to finish the construction of the three big projects, and that the country's exports and balance of payment situation have begun to improve. In the short account, where the minister goes over the achievements of the ERP in Iceland, most of the time is spent discussing how the program has benefited the country's industry and the lasting infrastructure that has been built with the program's assistance. Only a couple of sentences are spent discussing the progress made towards liberalising the economy, remarking that more effort will be put into that in the future.⁶⁶ These policy changes would have to wait for additional seven years, when a coalition government composed of the IP and SDP formed a strong alliance in 1960, that was able to bring about the changes that IP-PP government had tried to put in place in 1950.⁶⁷

Conclusion

It has been said by many scholars who have studied the issue, that the European Reconstruction Program was too small to have any lasting effect on the economic development that took place in the decades after the war. If it were to have significantly influenced the growth trajectory of the economies in question the size of the aid package would have needed to be much larger than it was. This does not hold true in the case of Iceland, where the size of the aid program was massive in proportion to the size of the Icelandic economy. The analysis of the

⁶⁶ *Morgunblaðið*, June 17, 1953, 1–2.

⁶⁷ Sigurður Snævarr, *Haglýsing Íslands*, 64–70.

archival evidence demonstrates that the Icelandic government was able to secure great quantities of aid in their negotiations with the US authorities. Cold War strategic priorities and the unique economic circumstances in Iceland played an influential role in determining the distinct ERP that was put in place in Iceland. But, domestic political concerns were also a critical factor. The US officials were quite concerned about the political stability in the country, the weak alliances that lay at the foundation of the government coalitions. They were particularly worried about the possibility of the SP gaining support in the economic and political turmoil that they judged was imminent if left unchecked. Icelandic government officials seem to have been keenly aware of this apprehension among US officials and to some extent used it to their advantage when negotiating with the ECA and other US government department heads. However, the political situation was not only a bargaining chip in the hands of the Icelandic government. Their scramble towards securing finance for the big investment projects, after the ECA had been replaced by the MSA, demonstrates that getting these projects built was of great political importance to them.

When we turn towards the conditions of the ERP, which are considered, by scholars like Barry Eichengreen to be the most important part of the program, that had a significant lasting impact on the ERP member countries. Again, the case of Iceland reveals a completely different story. There the opposite happened, ERP did not induce the government to abandon their isolationist policies and emphasis on investment and growth projects. In the documents examined there is even evidence of the ECA recommending that the government should move slowly towards full liberalisation. It also seems that the failed attempt to liberalise the economy in 1950 was motivated by domestic political factors, like the public sentiment towards the strict economic policies that the three-party government coalition pursued, and the fierce competition between the four parties in the months before the election 1949. The failure of these attempts to change the economic structure of the country, can also be in part explained by the stalemate that characterised the political environment all throughout the 1950s. The only economic policies that politicians from the three parties could

unite were the ambitious investment projects, which had been the preferred solution to economic difficulties that the economy faced at the end of the war. This preference would end up absorbing a large portion of the ERP. They became a visible reminder of the program's achievements and its lasting legacy.

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