

“The Environment . . . Putting Our Money Where Our Mouths Are”

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“Put your money where your mouth is.” What a crass saying . . . I like it, though. It challenges those who *say* they value something to divulge what they actually will sacrifice to get it. That’s much more revealing about someone’s true feelings. We need more of this in the management of environmental resources . . . both being asked to pay for environmental goods and being given the opportunity to do so.

This is the way it works for most goods in our economy. You purchase whatever amount of tomatoes, shoes, roofing material, tennis balls, etc. that you wish. By doing so, your money talks – you reveal that you value the good more than the value of the cash sacrificed. This simultaneously gives incentives for you to buy only goods you value more than the price (and refrain from buying those you do not) and for suppliers to provide it to the marketplace if the price covers the cost of making it. This system works pretty well in getting vast quantities of a wide variety of goods produced and into the hands of consumers. It also responds well to changes in consumer desires. Witness the dramatic rise in the production of such goods as DVDs, low-fat beef, high-def TVs, radial tires, and regional air travel that came along to match the surge in demand for these products.

Yet we seem to have a difficult time addressing the surge in “demand” for environmental goods. By most accounts, it appears that we value environmental goods greatly and increasingly so, and with good reason. Naturally, clean air and water are essential to life itself – but it goes beyond this. We value scenic mountains, wildlife, wide open spaces, a peaceful walk in the woods, the beauty of the surf crashing against the rocks, and so on . . . all very magnificent and uplifting. And our increased material wealth heightens the desire for such environmental goods. In economist’s lingo, this is an increase in demand.

How is this increase in demand met? In great contrast to what happens with other goods, we seem to be trying to improve the availability of environmental goods by incessantly hounding one another: “You drive too big a car!,” “You throw away too much stuff!,” “Your toilet uses too much water!” I suppose that the intent is to improve the availability of clean air and water, but what a messy way to do it. We appear to be constantly looking over one another’s shoulder and announcing the contemptible nature of other’s consumption while proclaiming the righteousness of our own. Talk about leading to uncivilized social discourse. And, I might add, it’s antithetical to a basic principle of a free society that we have broad choice in our personal behavior.

So why the big mess with environmental goods and not with other goods? Basically, we are missing a good pricing system for the former. Nobody bothers me about my tomato consumption because the price I pay for them covers the cost of using the resources that produce them. I have the correct incentive not to “overuse” tomatoes

and suppliers have an incentive to produce them as long as the price covers their cost. These incentives are absent for many environmental goods because I am not able (nor required) to pay for the resources I use. Air, open water, access to range land and other environmental goods are priced at zero, thus there is little incentive for individuals to conserve on their use or, where feasible, for others to produce them. As a result, we do not effectively meet the latent demand for these types of goods and overuse is a persistent problem, e.g., air and water pollution, overfishing, and rangeland and forest overuse.

While it's easy to identify the lack of a pricing system as the problem, implementing a good one may not be easy. A big reason is that property rights are hard to establish for some environmental goods. We have clear property rights to many resources and goods, meaning that those who wish to use them have to buy it at a price agreeable to the owner. Thus, with some sensible property and contract law and a dose of competition, we've got a nice pricing system going. But, as just noted, getting the first step of defining property rights is difficult for certain environmental goods.

It's not always impossible, though. In fact, some of the most dramatic cases of natural resource overuse have been solved with the implementation of property rights. The African nation of Namibia had long experienced diminishing populations of wild animals, poaching, and overuse of public lands. In the mid-1990s the government there began allowing groups and communities to obtain ownership over large tracks of rangeland the wildlife residing there. A thriving ecotourism industry has emerged, resulting in large increases of previously declining populations of animals such as elephants and rhinos. (Another important benefit has been creation of wealth for many poor Africans. See http://www.enterprise-africa.org/repository/docLib/20070318_Namibia_CBNRM.pdf.)

Establishing property rights over resources such as air and open water is not so straightforward, though. However, it's still possible to emulate important aspects of a pricing system. The Environmental Protection Agency's emissions trading system for sulphur dioxide (SO₂) does so. Electric utilities are awarded the "rights" so emit a certain amount of SO₂. Any amounts not used can be sold and if more emissions are sought, they must be purchased. In effect, use of the air must be purchased. Potentially, this idea can be used for other pollutants. A system like this – sometimes called cap and trade – has been proposed for greenhouse gases. Naturally, it's important to set the cap amount correctly and for greenhouse gases, this has been especially troublesome. Unfortunately, good analysis of the issue is being buried under a morass of politics and hype. Nevertheless, the principle of establishing a market and having individuals pay for the resources used is a good one.

Such a "market" gives me incentives not to overuse resources and implicitly assures others that the price I pay compensates for the cost of its use. No more need to worry about how much water I use any more than how many shoes I buy. So let's put our money where our environmental mouths are. Let's be willing to pay for environmental goods and once we do, stop carping about everyone else's purchases. (A version of the above article appeared in *Business Lexington*, June 15, 2007.)