Green Keynesians?

Recessions are bad for the environment, but what policies should environmentalists recommend to prevent a global economic slow down?

Nick Mabey, E3G, 2007

Stagnant or Sustainable?

As the post-war situation in Iraq dominates headlines, a major diplomatic initiative led by the US to prevent global recession has been little reported. The US Treasury Secretary has been travelling the world urging countries to adopt expansionary economic policies which will raise world GDP growth, particularly in the Euro-zone and Japan where growth rates are stagnating.

Environmentalists have always disliked GDP as an indicator, for many good reasons, but what should an "environmental" response to the threat of global recession look like?

At the moment there is no coherent response, and this fuels suspicion among the general public – skilfully exploited by anti-environment politicians in all countries – that environmentalists are against prosperity and would like nothing more than to see the world economy stagnate. Indeed, many strains of environmental thought seem to echo these themes in their search for a "steady state" economy.

However, this is neither a practical nor ethical position for environmentalists to take. The economy, like an ecosystem, exists in a dynamic equilibrium and requires constant activity to remain stable. A recession disrupts this system, harming the poorest who have fewest resources to ride out the bad times. The environmental vision has always been to decouple the economy from increasing pressures on the natural environment, and to direct it towards fulfilling both basic human needs and a wide range of aspirations beyond simple consumption. This will require a dynamic, innovative and (eco-)efficient economy; not a stagnant and failing one.

However, after years of expanding global investment and globalisation of production, world supply capacity now well outstrips demand, resulting in falling prices and a real risk of prolonged global recession or even outright depression. The USA can no longer play the role of consumer of last resort as it is running its largest ever trade deficit. The resulting devaluation of the dollar has begun to reduce US imports and export deflationary pressures to the rest of the world. This threatens a re-occurrence of the twenty year "long recession" which followed the global technological and investment revolution in the 1870s.

The recent years of economic slow down have already damaged developing countries. Despite the growth in high-tech exports from parts of Asia in the last decade, over 70% of exports from Africa and the Middle East, and over 60% from Latin America (excluding Mexico) are primary products. Weak global demand has resulted in fluctuating and depressed global prices for these goods, encouraging countries to exploit their resources more intensely to regain revenues and reducing investment in environmental improvement. On the other side, lower OECD growth has hardly been seen to lower rich countries' environmental footprint, as this is not simply correlated with gross economic consumption [3]. For example, fear of recession is likely to reduce household investment in expensive but environmentally beneficial items, such as energy efficient products or home improvements.

During the last global recession in 1992-3, most measures of national measures of sustainability, for example the World Bank's Genuine Savings indicator – which includes environmental costs, – fell substantially. Even countries operating dynamic and seemingly sustainable economies took much of the next decade to recover their pre-recession levels of sustainability.

Green Shoots
A green response to the current global economic crisis has to be able to deal with immediate – but hopefully temporary - macroeconomic imbalances; while also laying the foundation for future sustainability.

An alternative approach is vital, as the stimulus packages currently being promoted by economic authorities involve boosting consumer spending by further reducing interest rates and personal taxation levels. This will result in further unsustainable consumption, rising debt levels and increasing inequality. Increased personal consumption in the North caused through interest rate reductions will be concentrated in well-off groups – particularly homeowners – and is also unlikely to help those developing countries which depend on exports of primary commodities.

In contrast, a green stimulus package would focus on generating public goods and providing greater certainty in future incomes. This would require countries to raise social investment levels through measures such as increased education, health and environmental expenditure. All of these are labour intensive areas which put money directly into lower income households. Social insurance schemes would be strengthened to provide households with significant income cover over the deepest part of the recession, thus minimising their exposure to risk and subsequent shifts in consumption.

Environmental and resource taxes should rise to help balance this expenditure, combined with classic Keynesian public borrowing. Additional measures would shift economic incentives to encourage innovation and investment in less resource intensive private and public investment. These longer-term incentives are key to helping offset the decline in private R&D typically seen in recessions, thus laying a basis for future sustainable growth.

A green economic stimulus package would aim to strengthen public investment, maintain private consumption – particularly at lower income levels - and maintain levels of long-term public and private innovation, particularly in resource efficiency. This suite of objectives goes well beyond the simple "green tax reform" proposals currently being put forward. A package of measures such as this should see both indicators of GDP and Genuine Progress increase in both the short and long term.

More Action; Fewer Indicators
Such a package will not be simple to design in practice. All options will have some potentially negative consequences; for example, on car-dependent rural communities or some developing country exporters. The balance of consumption shifts at different income levels will need to be carefully balanced, and any perverse impacts on low income groups (e.g. pensioners) balanced with targeted expenditure or policy packages.

Any credible green economic package will need to be based on significant research and modelling and accept the inevitable trade-offs which will occur. However, currently none of this research base exists. Most environmental economics dealing with macro-economic issues is focused on highlighting problems through case studies of the negative impacts of

past economic programmes [6], or by developing alternative indicators to GDP; such as the Genuine Progress Indicator or Environmental Footprint.

But highlighting the problem is only the first step. All economists agree that the problem is to raise growth, create jobs, maintain economic stability, and even preserve the environment. They disagree over how to achieve these objectives and what balance of objectives is feasible - and to some extents desirable. The disputes between Keynesians, Monetarists and Supply-Siders revolve as much about the means to an end as the end itself.

GDP itself emerged as just one indicator based on a body of Keynesian theory aimed at eliminating long-run unemployment. It was never, and never has been, the ultimate abstract measure of ultimate economic truth used by macroeconomists to design policy.

Environmental considerations will find no similar place inside macroeconomic policy making unless they can be translated into robust and theoretically coherent economic policy packages, which also make sense in political and social terms. Only then will there be a sustainable alternative to short-sighted calls for growth at all costs.

E3G

2007