Thinking Clearly about Markets and Mandates

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MARKETS VS. MANDATES
PROMOTING ENVIRONMENTAL QUALITY AND ECONOMIC PROSPERITY
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Scarcity means Tradeoffs
Environmental Tradeoffs
If MB > MC, do it!

Value

MB

MC

Emissions/Extraction

Blackboard Economics
Markets vs. Mandates

Resource owners respond to changing values.
Gains from trade result in cooperation, not conflict.

Politics & administrators assign environmental goals.
Command-and-control dictates how to achieve them.

Moving Picture
Why do Markets Fail?

• The divergence in costs occurs “owing to the technical difficulty of enforcing compensation for incidental disservices.”

• The divergence in benefits occurs “because incidental services are performed to third parties from whom it is technically difficult to exact payment.”
“... on occasion, governmental administrative regulation (could) lead to an improvement in economic efficiency. This would seem particularly likely when, as is normally the case with the smoke nuisance, a large number of people is involved and when therefore the costs of handling the problem through the market ... may be high.

Ronald Coase, The Problem of Social Cost, p. 18
Incidental Services and Disservices Mandates
Mandates: Necessary and Successful?

Emissions of Sulphur Dioxide in U.S. and Canada, in Gg annual emissions

U.S. Deer Population (in millions)
Too Successful?
Coase expressed concern about what he called “Blackboard Economics,” saying “the governmental administrative machine is not itself costless. It can, in fact, be extremely costly.”

“It is not sufficient to contrast imperfect adjustments of unfettered private enterprise with the best adjustment that economists in their studies can imagine. We cannot expect that any public authority will attain, or will even wholeheartedly seek, that ideal.”
Mandates can Backfire, have Unwanted Effects

- Plastic Bag Bans → use of plastic
- Fracking Bans → local air quality
- Endangered Species Act → habitat destruction
- Clean Air Act → power plant vintage
- Blood Mineral Embargo → violence
- Enviro Regulations on Hydropower → pollution from coal
“Policies need to be analyzed in terms of the incentives they create, rather than the hopes that inspire them.”

Thomas Sowell
Alternative to “Mandate, Regulate, Litigate”

“Market forces could prove to be the environment’s best friend – if only greens could learn to love them”

April 2005
Finding the ways that work “by using a non-confrontational, collaborative approach.”

“We examine every environmental problem through an economic lens.”
Markets at Work

Crowdsourcing for Migratory Birds

TNC: “There's not a lot of opportunity to ...forecast when the birds will arrive and rent the habitat instead.”

Fishing Rights in the Great Barrier Reef

WWF: “It was a practical way to remove the threat of gill nets from a section of the reef... incredibly important for threatened species.”
Can markets help with the Mother of Them All?

CLIMATE CHANGE!

- Climate change is about risks to people and property.
- Owners of at-risk property adapt.
  - Land, Water, Finance
- Markets also incentivize mitigation.
Conclusion: Markets or Mandates?

• Markets provide the incentive to accommodate environmental change.
  • Conservation & Mitigation
  • Adaptation

• Government accommodates markets by lowering transaction costs and removing barriers to trade.
  • Encourages environmental & energy entrepreneurship.

• Mandates may be a necessary substitute for markets.
  • BUT they can lead to political manipulation.

• If mandates create tradeable rights, they facilitate markets.
  • Cap-and-Trade