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The Challenge of Going Green

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In the 25 years since the beginning of the modern environmental movement, the United States has spent more that $1 trillion to address environmental threats caused by commercial activities. During the latter part of this period, the U.S. economy has shifted from approximate trade balance on a long-term basis to chronic trade deficit. The coincidence of these two trends has led many to suspect that environmental regulation is impairing the "competitiveness" of U.S. industry.

The conventional wisdom is that environmental regulations impose significant costs on private industry, slow productivity growth, and thereby hinder the ability of U.S. companies to compete in international markets. This loss of competitiveness is believed to be reflected in declining exports, increasing imports, and a long-term movement of manufacturing capacity from the United States to other countries in the world, particularly in "pollution-intensive" industries.

A more recent, revisionist view asserts that environmental regulations are not only benign in their impact on international competitivenesses but may actually be a net positive force driving private business and the economy as a whole to become more competitive. This argument – articulated most prominently by the Harvard Business School's Michael Porter – has generated a great deal of interest and enthusiasm among some influential policymakers, including Vice President Al Gore.

Now a heated debate has arisen around these two views. Noah Walley and Bradley Whitehead tend to endorse the conventional view of environmental regulations impairing economic competitiveness. In drawing on their extensive experience working with major corporations, they introduce some much-needed reality to the debate, but anecdotal evidence can take us only so far.

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Together with my colleagues Adam Jaffe, Steve Peterson, and Paul Portney, I recently reviewed the statistical evidence from more than 100 academic and government studies that illuminate this ongoing debate. In our report, "Environmental Regulation and International Competitiveness: What Does the Evidence Tell Us?" we concluded that the truth lies somewhere between the two positions.

We found little to document the view that environmental regulation has had a measurable adverse effect on competitiveness. Although its long-run social costs – including productivity slowdown – may be consequential, studies gauging the effects of environmental regulation on net exports, overall trade flows, and plant-location decisions have produced estimates that are small or statistically insignificant.

The picture is bleaker still for the tenet that environmental regulation stimulates innovation and competitiveness. Not a single empirical analysis lends convincing support to this view. Indeed, several studies offer important, if indirect, evidence to the contrary. Natural skepticism regarding this regulatory free lunch should remain unabated.

Rather than advocate either of the two extremes, policymakers should aim to establish environmental priorities and goals that are consistent with the real trade-offs that all regulatory activities inevitably require; that is, policymakers should base environmental goals on the careful balancing of benefits and costs. In so doing, policymakers should seek to reduce the magnitude of those costs by identifying and implementing flexible and cost-effective environmental policy instruments, whether of the conventional type or the newer, market-based breed.