Comments on Stephen DeCanio's paper entitled "Is Economics the Wrong Language for Addressing Climate Policy"
Rachel Cleetus, November 17, 2006

Reading Stephen Decanio's paper was a pleasure. It set my mind racing about a host of issues that have troubled me since I entered graduate school in economics years ago. Economics, as it is taught today in most American graduate schools, fails to provide students with a perspective on the ***social*** science aspects of the discipline instead focusing exclusively on mathematical models. The study of the history of economics is not required in most graduate programs, leaving many students with the impression that neoclassical economics is "received wisdom", akin to the bible, rather than a strand of thought that has evolved from and coexisted with competing ideas.

Economists actually have a long tradition of weighing in on the social, philosophical and ethical dimensions of public policies. Adam Smith, who has come to be (in)famously associated with the invisible hand theory of free markets, was himself one such. In fact, he first received renown for '*The Theory of Moral Sentiments*', written in 1759, seventeen years before '*The Wealth of Nations*'. The former is a study of human psychology and ethical motivations that goes beyond pure self-interest and recognizes the human ability to have sympathy for the situation of others[1] (albeit a narrow sphere of 'others'). Smith was deeply interested in the causes and remedies for income inequality[2]. In the modern day, Amartya Sen has taken on the mantle of 'moral philosopher' with his keen insights on social choice theory.

So why is it that most of us economists are trained to ignore the normative issues and focus solely on issues of efficiency? Why this timidity in discussions of equity? And does this make us particularly ill-equipped for confronting the many complex issues raised by climate change?

One must point out that equity and efficiency are not necessarily two separate notions, especially with regards to climate change policy. Establishing property rights (a central tenet of neoclassical economics), for example through a system of tradable emissions permits, has *both* efficiency *and* equity implications[3].

DeCanio's paper raises several concerns, the key one being that the utilitarian framework (Least Common Denominator Utilitarianism or LCDU) is thoroughly inadequate when applied to climate change. Among the drawbacks: Kaldor-Hicks (K-H) transfers are

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[1] How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortunes of others, and render their happiness necessary to him, though he derives nothing from it... (*The Theory of Moral Sentiments)*

[2] What improves the circumstances of the greater part can never be regarded as an inconveniency to the whole. No society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable. *(The Wealth of Nations, Book I, Chapter VIII)*

[3] See Chichilnisky G, 2000. "Equity and Efficiency in Global Emissions Markets" in *Environmental Law, the Economy and Sustainable Development*. Cambridge UP.

impossible between generations (and, as Amartya Sen has noted, compensating transfers are rarely seen in the real world, even between members of an existing generation); How are preferences formed and how are they changed? How does one resolve the need for full information? Property rights are not immutable. K-H transfers will not be voluntarily forthcoming in the case of externalities (of which climate change is an example).

One can add to this a long list of other short-comings of mainstream economic analyses including:

- Traditional cost-benefit analyses are inadequate when the paths chosen are widely divergent; they only work well when marginal changes are being evaluated.
- Endless debates can ensue over the choice of appropriate discount rates that factor in intergenerational and cross-national ethical issues
- Smooth utility functions do not capture the realities of climate discontinuities and abrupt changes and lock us into an "incremental" policy world.
- The interconnectedness of ecological systems is not well represented in a discrete goods framework.
- Measuring welfare in terms of GDP changes is fundamentally flawed. GDP is a funny number. For example, GDP goes up during wars. GDP is enhanced by rebuilding efforts after natural disasters. GDP does not include ecosystem services, and some of the biggest impacts of climate change will fall on such 'non-market' goods and services. What GDP really seems to measure is consumption. And we are locked in a framework that equates increasing consumption with increasing welfare. To confront climate change in a meaningful way, we have to move away from this limiting view.
- The institutions that underlie economies play an important role in determining the effectiveness of policies. Universal policy prescriptions should be regarded with due skepticism.

What then is the appropriate role for the economist in the debate over climate change policy? I submit that our role is to be one of several voices, providing a necessary perspective, but never losing sight of the fact that this is a narrow perspective. Our models, no matter how sophisticated, remain a partial view of the world. As DeCanio says, we cannot lay claim to being the ultimate arbiters on public policy issues.

Furthermore, we have an obligation to maintain a high level of professional integrity in our analyses. Climate change is a serious problem; it will require real dollar costs to avert the worst of it. We shouldn't be shy about saying that to policymakers because these costs are miniscule compared to the potentially catastrophic consequences of unchecked global warming.

In closing, DeCanio argues that economists must "engage in a discussion of moral principles". This is indeed an ambitious and intriguing proposal and I am keen to learn more about what he means by this.