

Joseph Wayne Smith is a visiting scholar in the department of philosophy, the Flinders University of South Australia. Evonne Moore is an environmental policy consultant with Moore and Gunnell in Adelaide, South Australia.

Economic Rationalism and Sustainable Development

A Book Review by Evonne Moore and Joseph Wayne Smith

GREEN MARKETS: THE ECONOMICS OF SUSTAINABLE DEVELOPMENT

By Theodore Panayotou
San Francisco: Institute for
Contemporary Studies, 1993
169 pp., cloth \$29.95, paper \$14.95

Theodore Panayotou's *Green Markets* is concerned with presenting an economic analysis of environmental degradation and an outline of the reforms necessary for the achievement of sustainable development. Panayotou maintains that there are underlying causes of environmental degradation common to countries in different geographical localities, as varied as the rain forests of South America and the stagnating lands of sub-Saharan Africa. The cause of environmental damage is not economic growth, which by itself "neither causes nor remedies environmental degradation" (p.1) but rather, "bad" economics arising from flawed government policies and disturbed markets that inappropriately price natural resources.

Panayotou is an "economic rationalist" in the sense in which that term is used in Australia: that market mechanisms produce the most efficient allocation of scarce resources relative to alternative mechanisms of allocation. The economic rationalist believes in the virtual infallibility of the invisible hand of the market, and is hostile to government intervention to regulate markets or to central economic planning.

This view, which we may call "naive economic rationalism," is open to a number of criticisms. Market mechanisms do not mechanically generate fair or just outcomes: an economy may be economically efficient, even though the distribution of incomes is highly inequitable. Market economies cannot guarantee stability and full employment: indeed market capitalism goes through roller-coaster rides of booms and slumps. Finally there is the question of *externalities*. The market mechanism often does not adequately take into account the cost and benefits of environmental resources such as clean air and water, and these resources are often degraded.

Panayotou is not a naive economic rationalist. He does believe that markets are normally efficient

mechanisms for the allocation of scarce resources, but he also is well aware of the problem of externalities. Panayotou is a sophisticated economic rationalist. He notes that market failure can arise from a number of factors such as:

- ill-defined or non-existent property rights
- unpriced resources and absent or weak markets
- spillover effects or linkages between sectors of the economy operating outside the sphere of market mechanisms
- high transaction costs and market imperfections such as lack of competition, monopolies, oligopolies and segmented markets

and other factors such as uncertainty and risk aversion, and irreversible decisions (p.34). Panayotou presents a detailed account of why these factors dull the efficiency of market mechanisms. This, however, is not taken to constitute an argument against sophisticated economic rationalism: rather it shows that governments must act as economic mechanics to clean the sludge from existing economies so that markets can operate freely and economic growth can occur at greater rates. Sustainable development — "[the] alleviation of poverty, a decline in fertility, the substitution of human capital for natural resources, effective demand for environmental quality, and a responsive supply" (p.14) — cannot occur without economic growth.

Panayotou is dismissive of the limits-to-growth tradition (*limitationism*) in ecological economics:

The alarmist prediction that continued economic growth must lead to ecological disaster or that sustainability will eclipse growth, as well as utopian prescriptions to ban growth and change people's values, derive from a fixation on the physical manifestations and symptoms of environmental degradation: hectares of forests lost, tons of soil eroded, species endangered, tons of pollution generated. The way to attain sustainable growth is to dispense with a preoccupation with the symptoms of environmental degradation and to look for root causes rather than proximate cause (p.142).

To prevent environmental degradation, most resources must be owned and rationally priced so that responsible ecologically sustainable economic activities occur.

Those of us who are "alarmists," who believe that life on earth is being threatened by human economic activity, would be rightly dismissive of Panayotou's key argument. If sustainable development does require endless economic growth, then limitationists would conclude that "sustainable development" is a contradiction in terms. If the full environmental costs of growth are to be paid for, then limitationists would conclude that economic growth is not possible. What, after all, is the economic cost of destroying ourselves? Surely markets require a habitable planet: the value of life is a more basic value than economic value for it is necessary to be alive to have any perception of valuable things at all. Panayotou, unlike most economic rationalists, understands this. He admits that if economic growth occurs by appropriating other people's resources or transferring costs onto others, then the growth economy cannot continue. However, he maintains that increased efficiency and innovations arising from human knowledge and capital will transcend those limits. This argument is not defended at any length in the concluding pages of Panayotou's book and the book falls suddenly flat at the point where one would expect the peak of argument.

Population expansion is mentioned by the author on page 70 only in passing. He would appear to believe in the demographic transition theory, namely that reductions in population growth in the Third World will be the outcome of increased economic growth and rising living standards. Supporters of this theory seldom deduce the logical consequence of this position, namely that even if a rise in living standards will ultimately lead to a reduction in population growth, uncontrolled population growth can also lead to a decrease in living standards and destruction of the environment. Even if the demographic transition theory was correct, it is by no means clear that increased economic growth is a sufficient measure to control global population growth. Population growth may well outstrip any benefits allegedly contributed by an expanded economy.

Australians and Americans are told by the economic rationalist to "become more efficient," "to deregulate," "to introduce more labor market reforms," "to increase levels of foreign investment and immigration" and "to be more internationally competitive." The evidence is clear, at least in the Australian case, that economic rationalism is an economic and social disaster. (See: S. Rees, G. Rodley, and F. Stilwell (eds.), *Beyond the Market: Alternatives to Economic Rationalism*, [Pluto Press, Australia, 1993].) "Economic efficiency," "deregulation" and "labor market reforms" reduce barriers

such as workers' conditions and environmental protection in the names of *profitability* rather than the abstract concept of "efficient" use of scarce resources, and "international competition" flattens American and Australian working conditions until they are comparable to competing nations in the global market. How can Western nations compete with countries such as China, which uses the slave labor of its prisoners to produce goods for the global market? It is arguable that economic rationalism has failed to solve even basic economic problems such as the problem of employment, so *a fortiori* it would seem hardly capable of dealing effectively with the issue of the global environmental crisis. Panayotou considers none of these questions. His book is consequently flawed and cannot therefore be viewed as a major contribution to the ecologically sustainable development debate.■