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Free Enterprise: Taking the highway, not the high road

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This week's extraordinary display of car executives backing up - figuratively and literally - President Barack Obama during the announcement of new, tougher fuel-efficiency standards was worthy of a cameo appearance on the World Series of Poker.

One commentator even questioned the effect that "truth serum" would have on the executives' statements.

The White House listed several policy objectives. They included thwarting a hodgepodge of competing new state rules. California had led a coalition of 14 states in such efforts but agreed to scale back those ambitions in order to support the new federal rules.

Regarding efficiency, having a more streamlined regulatory approach is likely more optimal.

However, among political economists, the United States is famous for its "laboratory of the states" in which competition among states tends to select the most promising policy proposals. In that sense, federal preemption is not necessarily always best.

Obama also mentioned in his announcement the national security implications of the nation's reliance on oil as well as the resulting high levels of carbon emissions. The new CAFE (corporate average fuel economy) standards are intended to limit both.

As this column had pointed out two years ago, making CAFE regulations more stringent will also lead to various unintended (and costly) side effects.

These include additional miles driven because of lower cost per mile and also more miles driven in older cars because of the expected higher costs for the newer, more fuel-efficient cars.

Furthermore, given that a backdoor to fulfilling the new guidelines includes the manufacturing of smaller cars, there are various estimates of a possibly higher highway death toll, which is traditionally measured in fatalities per 100,000 miles driven.

The irony, of course, is that another (unpopular) policy instrument would be available to achieve the stated goals while avoiding some of the most costly side effects of higher CAFE standards.

A 2004 brief by the non-partisan Congressional Budget Office (available at tinyurl.com/opmtaa [1]) cited strong evidence that an increase in the gasoline tax would be preferable - using efficiency and cost-benefit criteria - to an increase in fuel economy standards.

A just-published study by two University of Michigan economists supports this argument with respect to reductions in carbon emissions. Exploiting the above-mentioned variation in state gasoline taxes over the past decades, the two authors find evidence "... that a 10 cent per gallon increase in the gasoline tax would reduce carbon emissions from vehicles in the United States by about 1.5%."

The paper (available at tinyurl.com/psdozc [2]) contextualizes this by stating that "... total U.S. carbon dioxide emissions increased by 1.1% annually between 1990 and 2007."

To be clear, pointing out such evidence has nothing to do with favoring or opposing new taxes in general. It is simply an application of good principles of public finance and public policy. Namely, faced with two or more policy alternatives proposed to achieve a policy goal, the objective of the economic analysis is to identify the most economically efficient option.

Of course, political feasibility is never far removed from the considerations of politicians maximizing reelection chances.

It is only a sign of the times that the de facto ownership of major car companies by the government permits Congress and the executive to relegate economics secondary to political considerations.

Conveniently, one does not have to make the hard calls when one holds all the poker cards.

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