The Moscow Times
30 YEARS
INDEPENDENT NEWS FROM RUSSIA

# U.S. Must Lead Effort to Treat Energy Myopia

By Michael Spence

April 03, 2012




I have been surprised by the recent coverage in the U.S. media of gasoline prices and politics. Political pundits agree that presidential approval ratings are highly correlated with gas prices. When prices go up, a president's poll ratings go down. But in view of the United States' long history of neglect of energy security and resilience, the notion that the administration of U.S. President Barack Obama is responsible for rising gas prices makes little sense.

Four decades have passed since the oil-price shocks of the 1970s. We learned a lot from that experience. The short-run impact — as always occurs when oil prices rise quickly — was to reduce growth by reducing consumption of other goods because oil consumption does not adjust as quickly as that of other goods and services.

But given time, people can and do respond by lowering their consumption of oil. They buy more fuel-efficient cars and appliances, insulate their homes and sometimes even use public transportation. The longer-run impact is thus different and much less negative. The more

energy-efficient one is, the lower one's vulnerability to price volatility.

On the supply side, there is a similar difference between short-term and longer-run effects. In the short term, supply may be able to respond to the extent that there is reserve capacity (there isn't much now). But the much larger, longer-run effect comes from increased oil exploration and extraction, owing to the incentive of higher prices.

All of this takes time, but, as it occurs, it mitigates the negative impact. The demand and supply curves shift in response to higher prices (or to anticipation of higher prices).

In terms of policy, there was a promising effort in the late 1970s. Fuel-efficiency standards for automobiles were legislated, and car producers implemented them. In a more fragmented fashion, states established incentives for energy efficiency in residential and commercial buildings.

But then oil and gas prices entered a multidecade period of decline. Policies targeting energy efficiency and security largely lapsed. Two generations came to think of declining oil prices as normal, which accounts for the current sense of entitlement, the outrage at rising prices and the search for villains: politicians, oil-producing countries and oil companies are all targets of scorn in public-opinion surveys.

A substantial failure of education about nonrenewable natural resources lies in the background of current public sentiment. And now, having underinvested in energy efficiency and security when the costs of doing so were lower, the United States is poorly positioned to face the prospect of rising real prices. Energy policy has been "pro-cyclical" — the opposite of saving for a rainy day. Given the upward pressure on prices implied by rising emerging market demand and the global economy's rapid increase in size, that day has arrived.

Countercyclicality is a useful mindset for individuals and governments. Recent history, particularly the excessive accumulation of private and public debt, suggests that we have not acquired it. Energy policy — or its absence — seems another clear example. Rather than anticipating and preparing for change, the United States has waited for change to be forced upon it.

Energy-policy myopia has not been confined to the United States. Developing countries, for example, have operated for many years with fossil-fuel subsidies, which have come to be widely recognized as a bad way for governments to spend their limited resources. Now these policies have to be reversed, which implies similar political challenges and costs.

Western Europe and Japan, both of which are almost entirely dependent on external supplies of oil and gas, have done somewhat better. For security and environmental reasons, their energy efficiency increased via a combination of taxes, higher consumer prices and public education.

The Obama administration is now working to initiate a sensible long-term approach to energy, with new fuel-efficiency standards for motor vehicles, investments in technology, energy-efficiency programs for dwellings and environmentally sound exploration for additional resources. Doing this in the midst of an arduous post-crisis deleveraging process, a stubbornly slow recovery, the process of building a new, more sustainable growth

pattern, is harder — politically and economically — than it might otherwise have been, had the United States started earlier.

Still, better late than never. Obama is correctly attempting to explain that effective energy policy, by its very nature, requires long-term goals and steady progress toward achieving them.

One frequently hears the assertion that democracies' electoral cycles are poorly suited to implementing long-term, forward-looking policies. The countervailing force is leadership that explains the benefits and costs of different options, and unites people around common goals and sensible approaches. The Obama administration's effort to put long-term growth and security above political advantage thus deserves admiration and respect.

If criticism of democratic governance on the grounds of its "inevitable short time horizon" were correct, it would be hard to explain how India — a populous, complex and still-poor democracy — could sustain long-term investments and policies required to support rapid growth and development. There, too, vision, leadership and consensus-building have played a critical role.

The good news for U.S. energy security is that in 2011, the country became a new net exporter of petroleum products. The price of fossil fuels, however, is likely to continue to trend upward.

Declining dependence on external sources, properly pursued, is an important development. But it is not a substitute for higher energy efficiency, which is essential to making the switch to a new and resilient path for economic growth and employment. A side benefit would be to unlock a huge international agenda for energy, the environment and sustainability, where U.S. leadership is required.

This effort requires persistence and a long official attention span, which in turn presupposes bipartisan support. Is that possible in the United States today?

The U.S. political system's persistently low approval ratings stem in part from the fact that it seems to reward obstructionism rather than constructive bipartisan action. At some point, voters will react against a system that amplifies differences and suppresses shared goals, and policy formation will revert to its more effective pragmatic mode. The question is when.

Michael Spence, a Nobel laureate in economics, is professor of economics at New York University's Stern School of Business, distinguished visiting fellow at the Council on Foreign Relations and senior fellow at the Hoover Institution. His latest book is "The Next Convergence — The Future of Economic Growth in a Multispeed World." © Project Syndicate

*The views expressed in opinion pieces do not necessarily reflect the position of The Moscow Times.*

Original url:
https://www.themoscowtimes.com/2012/04/03/us-must-lead-effort-to-treat-energy-myopia-a13796