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## Political instability and non-market valuation: Evidence from Croatia



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### ABSTRACT

We examine the effect of political instability on willingness to pay estimates (WTP) from nonmarket valuation, using data from a choice experiment implemented in Zagreb, Croatia to value groundwater quality and quantity. To evaluate the sensitivity of preferences for environmental quality to instability, we use the timing of a period of public protest that occurred in the city during the data collection and compare preferences before and during the protest. We find some evidence that WTP is lower in the period of political instability, but the result is sensitive to the specification used.

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## 1. Introduction

This paper investigates the influence of political instability on preferences for environmental quality through non-market valuation. We use a choice experiment conducted in Zagreb, Croatia in 2011, to value a groundwater aquifer conservation plan. To assess the effect of political instability on preferences for environmental quality, we use the variation introduced by a series of anti-government

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protests that began in the country during data collection. We use the timing of the protests, which is exogenous to the implementation of the survey, to discriminate between respondents interviewed before and after the protest and compare their WTP. The results suggest that political instability may influence WTP in the short run. We find some evidence that instability does not affect preferences for environmental quality but influences respondents' WTP into a government managed fund. We also find that after the protest the idiosyncratic error component is smaller, suggesting that the population's view of the good has become more homogeneous. We attribute these changes to the post-protest decrease in government credibility (Oh and Hong, 2012). The results suggest that even a brief period of instability can have important effects on environmental preferences. Nevertheless, results are sensitive to the specification used, and in particular to the inclusion of an alternative specific constant for the status quo alternative.

The paper contributes to the literature in a number of ways. To our knowledge this is the first study attempting to quantify the impact of political instability on preferences for environmental quality. Contrary to much of the empirical literature on political instability that concentrates on countries with long history of social unrest and inefficient or non-functioning institutions, we use a case study from a democratic state that has been mostly peaceful and stable for the past years, and show that even brief periods of instability can have substantial influence on stated behavior in the short run. The results are relevant for many countries that experience brief instability but do not slip into prolonged and violent political confrontation. Finally, the period we study is short, reducing the influence of confounding factors on preferences for environmental quality.

Political instability is used in research to describe a diverse range of phenomena. Events associated with political instability can generally be divided into two categories. First, political instability includes episodes of social unrest such as politically motivated violence and riots. Second, instability can suggest sudden government changes and electoral surprises that are outcomes of agents' interaction in the political system. In this paper we use the term to imply a period of politically motivated unrest that introduces uncertainty regarding the government's ability to implement policies and remain in power (Carmigani, 2003). Lacking data after the end of the unstable period, we can only speculate about the long term influence of instability.

The rest of the paper is structured as follows: Section 2 discusses the relevant literature while Section 3 presents the models and hypotheses. Section 4 presents the case study and describes the survey, while Section 5 reports the results. Section 6 concludes.

## 2. Literature review

An increasing body of research looks at the influence of political instability on observed individual and household behavior. Political instability is among others related to decreased welfare (Dupas and Robinson, 2010), increased risk taking (Dupas and Robinson, 2012), increased propensity to engage in violence (Miguel et al., 2011) and decreasing human capital accumulation (Shemyakina, 2011). Many studies focus on the impact of instability on health outcomes (Bundervoet et al., 2009; Akresh et al., 2011, 2012). Most of those studies focus on countries with a long history of instability, often manifested by civil war. In contrast, the present paper extends research by examining the influence of a brief episode of instability in an otherwise peaceful country.

The long run influence of political instability on environmental performance and resource use is ambiguous. Fredriksson and Svensson (2003) show that the stringency of environmental regulation can decrease with increasing political instability, depending on the level of corruption. Furthermore, firm investment in abatement technology increases with government corruptibility but the effect is smaller when political instability is higher (Fredriksson and Wollscheid, 2008). Skoulikidis (2009) attributes part of the deterioration of the state of Balkan rivers to political instability during the 1990s. Stable democratic institutions (Farzin and Bond, 2006) and the quality of governance (Bhattarai and Hammig, 2004) are also important for environmental quality. Buitenzorgy and Mol (2011) find that countries transitioning to democracy have lower deforestation rates compared to established democracies and non-democracies, while Papyrakis (2013) finds a negative association between environmental performance and social and ethnic fragmentation that often motivates political instability

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