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Measuring the Economic Value of Sustainable River Basin Management: The Full-Preference Rank Method

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February 2015

Online at <https://mpra.ub.uni-muenchen.de/122255/>
MPRA Paper No. 122255, posted 02 Oct 2024 06:48 UTC

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Abstract

This study exploits the data from a full-preference ranking Choice Experiment (CE) designed to investigate how respondents evaluate a set of proposed improvements in the Asopos water catchment in Greece. These improvements are following the prescriptions of the European Union Water Framework Directive (2000). We first estimate a rank-ordered logistic regression based on the full set of choices by respondents to calculate the willingness to pay (WTP) of respondents for each one of the three attributes considered in the CE (that is, environmental conditions, impact on the local economy and changes in the potential uses of water). The model is initially estimated for the full sample and then re-estimated twice for two sub-samples: the one includes only the residents of Athens and the other includes only the residents of Asopos. Afterwards, we examine the effect of various demographic and socio-economic factors (such as income, gender, age, employment and education) on the estimates of our model in an attempt to reveal any differences among respondents with different characteristics. Thus, our analysis simultaneously provides a robustness check on previous findings in the literature and additional information about how various demographic and socio-economic characteristics affect the evaluation of the selected attributes.

Keywords: Choice experiment, Full-preference ranking, Logistic regression, Asopos River Basin, Environmental degradation, Water quality and quantity; Random utility maximization; Logit probabilities; Water Framework Directive; Residency-specific use and non-use valuation, Willingness to pay (WTP).

JEL Classification: Q25, Q51, Q53.

1. Introduction

Asopos is a 57km long river in Greece that runs across Viotia and Attiki. The catchment of the river covers an area of 724 km² and hosts numerous rare habitats and bird species, many of which are protected by EU legislation. The local area is also visited by many tourists who organize various recreational activities. It is worth mentioning that more than one third of the total residences in Asopos river basin (RB) serve as a second residence for their owners.

Unfortunately, this area of unique natural beauty, which supports a rich ecosystem that creates the perfect environment for the wildlife, is nowadays environmentally degraded due to unregulated human activities. A major source of environmental degradation is related to the industrial activities that take place in the areas nearby the Asopos River. Pollution became a hazard for the health of the local residents and visitors, while farmers started to worry about the effect of contamination on their agricultural production. Protests by the local population raised public awareness and put pressure on the government and the local authorities to take action and investigate the severity of the problem. This also attracted the interest of researchers.

Dimaras *et al.* (2010) and Papadiochou *et al.* (2011) apply a Contingent Valuation Method to obtain willingness to pay (WTP) estimates for improvements in the groundwater resources of the Asopos area. The former study focuses on local residents, while the latter uses a sample of households in Athens. The analysis of Dimaras *et al.* (2010) concludes that households in the Asopos area are willing to pay €400 per year to an independent management organization, while the relative estimated WTP for households in Athens by Papadiochou *et al.* (2011) is €45 per year. Laoudi *et al.* (2011) is another study that analyzes the economic damage of groundwater degradation in the Asopos area. The study examines the cost of developing alternative methods for the provision of drinking water to local communities. On the other hand, Louzidou (2009) investigates the cost of constructing a Central Wastewater Processing Unit for the industrial and domestic waste of the Avlona region in Attiki. Finally, Koundouri *et al.* (2012) estimate the WTP for a number of improvements in the Asopos RB for residents in Athens and the Asopos area. In general, their analysis does not reveal any significant differences between the WTP estimates of the two populations.

Our study is based on the results of a full-preference ranking Choice Experiment (CE) designed to investigate how respondents evaluate a bundle of proposed improvements in the Asopos water catchment. The CE focuses on three attributes: environmental conditions, impact on the local economy and changes in potential water uses. Our goal is twofold: First, we estimate the willingness to pay of respondents for each one of the three attributes considered in the CE by means of a rank-ordered logistic regression. Second, we investigate the effect of numerous demographic and socio-economic factors on the estimates of our model. In this way, we reveal how each one of the factors under scrutiny affects the evaluation of the selected attributes. Our analysis uses the full set of choices by respondents in an attempt to take advantage of all information available in dataset.

To anticipate our key results, our estimates for the WTP are qualitatively similar to those of Koundouri *et al.* (2012). However, our WTP estimates are substantially higher revealing a stronger willingness by respondents to finance environmental revitalization and conservation activities in the Asopos RB. When it comes to the sensitivity of the estimated coefficients on various demographic and socio-economic characteristics, we find strong evidence that suggest that some socio-economic factors (e.g. income and especially gender, age and education) affect

most of our estimates and especially the cost coefficient. Unemployment is also highlighted as a crucial factor that generates statistically different estimates. Moreover, respondents who are employed in tourism and people who frequently visit the Asopos area seem to have a different attitude towards the proposed improvements in the area compared to all other respondents. Finally, the place of living (Athens or Asopos) affects only how people evaluate the improvements in the environmental conditions.

Our analysis reveals useful information about how various demographic and socio-economic characteristics affect the willingness to pay of respondents for each one of the proposed improvements in the Asopos river basin. Our findings can assist policymakers to perform a cost-effectiveness and cost-benefit analysis for the determination of the optimal set of activities needed for the environmental upgradation of the area. Our analysis can also help in the development of the proper socio-economic instruments to select an efficient pricing system for the implementation of various environmental improvements in the region.

The layout of this paper is as follows: Section 2 describes the dataset and the methodology, while Section 3 reports the empirical findings and the policy implications of our analysis. Finally, Section 4 concludes.

2. Data and methodology

The initial dataset consists of the results of a full-preference ranking choice experiment that took place from September to October 2011 by trained interviewers. Quota sampling was followed according to 2001 Census data and the final sample included 150 respondents from Asopos RB and 150 respondents from Athens.

The design of the survey followed the standard five steps for a Choice Experiment: selection of desired attributes, definition of levels, choice of the experimental design, construction of choice cards to present to respondents and measurement of preferences. The experiment focused on the following three attributes that are often identified in the literature as impacted by the degradation of a region: environment, local economy and human health. The experiment assumes that the current status (*status quo*) of the environmental conditions is bad, the impact on the local economy is negative and the water is not suitable for drinking, cooking or irrigation. For each attribute, two levels of improvement are defined. Specifically, the environmental conditions can become moderate or good, the status of the local economy can be improved by 2015 or improve even further and become positive by 2027 and the water can become suitable for some uses (i.e. drinking and cooking) or for all uses (i.e. drinking, cooking and irrigation). Finally, the experiment assumes five levels of cost (these are 2, 4, 6, 8 or 12 Euros) associated to various sets of improvements and paid every three months in the water bill. Respondents were told that an independent body will assure that the collected funds will be spent for the improvement of the environmental conditions in the Asopos RB.¹

A personal interview was scheduled with each selected respondent. The interviewer presented a set of five choice cards to the respondent who was instructed to follow the following sequential choice process: First, the respondent chose the most preferred alternative out of the initial five alternatives in the choice set. This best alternative was then excluded from the choice set and the respondent was asked to select the least preferred out of the remaining four, which was also excluded. This process was repeated for the remaining three alternatives from which the respondent selected the second most preferred out of the remaining three, and finally the second

¹ A more detailed description of the design of the choice experiment can be found in Koundouri *et al.* (2012).

least preferred out of the remaining two cards. This approach, known as the “repeated best-worst” approach, provides a full preference ranking of the alternatives in each choice set. Contrary to alternative approaches, the “repeated best-worst” approach is believed to help respondents to rank their preferences (Scarpa *et al.*, 2011).

As stated before the objective of our study is twofold. First, the study aims to estimate marginal WTP for different attributes and attribute levels as described in the scenarios presented to the respondents. Second, this study also examines whether groups of respondents with different demographic and socio-economic characteristics have different attitude towards the four attributes under scrutiny. In an attempt to take advantage of the full set of information available to us, the analysis presented here use the whole set of repeated best/worst observations. So, the pseudo-choice sets used here were 60 for each respondent.

The utility gains from increasingly larger improvements on the three attributes under scrutiny are determined by means of a piece-wise linear coding. Given that the choice experiments allows for level of gradual improvements, the coding we follow is (0,0) for the status quo, (1,0) for the first level of improvement and (1,1) for the second level of improvement. Thus, the estimated coefficient for the second level of improvement measures the additional utility effect beyond that captured by the estimated coefficient of the first level of improvement.

A preliminary examination of the dataset revealed a small number of respondents (30 participants) that displayed a serial non-participation choice behaviour. In other words, some respondents consistently chose the status-quo condition across all 12 first best decisions on the full set choice tasks. For these serial non-respondents the alternative to the status-quo offering various improved scenarios were never sufficiently appealing to motivate a payment. We, therefore, choose to exclude the serial non-respondents from our analysis. For the remaining respondents, we first estimate our model thrice; once for the full sample and once for each of the two sub-populations of beneficiaries (inhabitants of Athens and Asopos). Estimates of WTPs for the different levels of policy attributes are then derived from each of these models. Finally, we investigate the effect of various demographic and socio-economic characteristics on how people form their values related to the same set of proposed categories of improvement.

3. Empirical findings and policy implications

Let us first focus on the estimation results from the full sample (all respondents) reported in Table 1. The coefficient for the *status quo* is not statistically significant indicating that there is no systematic incentive to stay with the current condition and avoid the proposed alternative scenarios (this is also the case when we estimate our model based on a sample that includes serial non-respondents). On the other hand, we obtain a negative and significant coefficient for the cost (equal to -0.088) and therefore we can use the estimated model to calculate welfare estimates.

Turning to the remaining estimates, we would expect to find positive signs in all coefficients. This is indeed the case. The only exception is the coefficient for the extreme improvement of the local economy (by the year 2027) which is negative but statistically insignificant. This means that respondents give no extra value to the additional marginal effect for the 2027 scenario. As argued by Koundouri *et al.* (2012), a possible explanation for this is that 2027 might be too far away in time for most respondents to be able to relate to it, or perhaps it was not clear in most respondents’ mind that it implied the 2015 target, or perhaps their discount rate is such that makes the net present value of benefits of these improvements

insignificant. Finally, the estimated marginal WTP for the first level of improvement in the local economy (by the year 2015) is €6.69, while the corresponding 95% confidence interval ranges from €5.24 to €8.15.

As far as the remaining two attributes are concerned (that is, environmental condition and human health), our findings suggest a significant increase in the utility in the moderate improvement levels. The estimated marginal effect is as high as €18.46 and €11.84 for the environmental condition and the human health respectively. These figures further increase by €5.53 and €14.77 when we consider the case of an extreme improvement in the environmental condition and the human health respectively. It is interesting to note that the estimated marginal effect of extending water uses from “some uses” to “all uses” (that suggests water suitable for irrigation too) is higher than the marginal effect of the first level of improvement. This clearly reveals the importance to respondents of achieving the highest possible level of improvements in the quality of the river’s water. In the case of environmental conditions, the additional increase in the utility effects from the moderate to the extreme improvement level is smaller but significant even when we account for the uncertainty that surrounds our estimates. To be more specific, the calculated 95% confidence interval indicates that the upper bound for the marginal effect for the first level of improvement in the environmental condition is €20.41 which is lower than €22.26 (calculated as $(18.46+5.53)-1.96*0.88$) that corresponds to the lower bound of the 95% confidence interval for the extreme level of environmental improvement.

We now turn our attention to the estimated models for the Athens and Asopos subsamples reported in Table 2 and 3 respectively. In both cases, the findings are qualitatively similar to those for the full sample. In other words, the coefficients for the *status quo* and the extreme improvement of the local economy are both statistically insignificant. The cost coefficient is negative, while all other estimated coefficients are positive and significant. However, we also observe some differences between the two estimated models. Respondents from Asopos seem to have slightly higher marginal effects for a moderate level of improvement in environmental conditions and human health compared to respondents from Athens. For example, the WTP estimate for the local residents of Asopos to achieve a moderate improvement in the quality of water is €12.31 compared to €11.25 for those leaving in Athens. However, respondents from Athens show a higher WTP for achieving the highest level of improvement in the aforementioned two attributes. Although our findings are, in general, qualitatively similar to those reported in Koundouri *et al.* 2012), our WTP estimates are significantly higher revealing a stronger willingness by all respondents (i.e. residents of both Athens and Asopos) to support the environmental improvements in the Asopos RB.

In what follows, we perform a series of Wald tests to investigate whether various demographic and socio-economic characteristics affect the attitude of respondents towards the four attributes considered in our analysis. Under the null hypothesis, there is no difference in the behaviour of groups of respondents with different characteristics. We first examine whether the place of living of the respondent has an effect on the way she evaluates each one of the four attributes. The results, given in Table 4, reveal no differences between residents of Athens and residents of Asopos. The only exception is when it comes to improvements in the environmental condition as suggested by the low p-value of the test (0.033) that leads to the rejection of the null hypothesis. We also divided respondents based on whether they are visitor of the Asopos lagoon, the Asopos estuary or the coastal zone. The results in Table 4 suggest that the estimate for the cost coefficient is not statistically different in all cases. However, it seems that the coefficients for the impact on the local economy and the human health depend on whether the respondent is a

visitor or not of either the Asopos lagoon or the Asopos estuary. Moreover, the estimated coefficients for the environmental conditions are statistically different for respondents who visit either the Asopos estuary or the coastal zone.

Next, we examine the effect of employment on our estimates. We consider four fields of employment: agriculture, industry, tourism, while all other fields of employment form the fourth group. On the other hand, unemployed respondents form our fifth group. The results, reported in Table 5, clearly show that unemployment affects the estimated coefficients for all four attributes. Similarly, respondents employed in tourism seem to differ in the way they evaluate all attributes except for the environmental condition compared to all other respondents. Furthermore, respondents employed in industry generate a significantly different cost coefficient. As expected, the farmers in our sample appear to have a different attitude towards the human health factor, since the quality of water is crucial for them. A similar finding holds for respondents included in the “all other fields” group.

Finally, we focus on various socio-economic characteristics, namely income, gender, age and education. The results presented in Table 6 highlight that the aforementioned characteristics affect almost all estimated coefficients. More in detail, the cost coefficient depends on all four socio-economic characteristics, while three out of four characteristics (education is the exception) affect the estimates for the environmental condition. The estimated coefficients that capture the impact on the local economy depend on the gender and the level of education, while the age and the education influence the estimates for the human health attribute.

4. Conclusions

This paper uses the results of a multi-attribute stated preference choice experiment (CE) specifically designed to estimate the use and non-use values that the respondents hold for a bundle of possible improvements in the Asopos catchment. The CE considers the following three attributes: environmental conditions, impact on the local economy and changes in potential uses of water. We estimate our rank-ordered logistic model based on the full set of choices by respondents. We initially estimate our model using the full sample and afterwards we repeat the analysis focusing on either the residents of Athens or the residents of Asopos. Finally, we investigate the effect of various demographic and socio-economic factors on our estimates in an attempt to reveal any differences among respondents with different characteristics. We, therefore, simultaneously check the robustness of the findings of previous studies in the literature and provide additional information about how various demographic and socio-economic characteristics affect the evaluation of the selected attributes.

When it comes to the willingness to pay (WTP) estimates, our results are qualitatively similar to those of Koundouri *et al.* (2012). However, we also observe some significant quantitative differences. Specifically, our WTP estimates are substantially higher revealing a stronger willingness by respondents to support the environmental improvements in the Asopos area. When we move one step forward and examine the effect of various demographic and socio-economic characteristics on the estimated coefficients that determine the evaluation of the selected attributes, we end up with some useful findings. It seems that socio-economic factors (income and especially gender, age and education) affect most of the estimates and especially the cost coefficient. Moreover, unemployment is a crucial factor that generates statistically different estimates. Similarly, respondents who are employed in tourism appear to have a different attitude towards the proposed improvements in the area compared to all other respondents. The same

holds for respondents who frequently visit either the Asopos estuary or Asopos lagoon. Finally, the place of living (Athens or Asopos) has only a minor effect on the estimations.

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