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Environmental investments: Too much of a good thing?¹

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Abstract: Using an original and large database on more than 6000 French firms over a 5 years period we add empirical evidence regarding the effect of environmental investments on economic performance, measured by firms’ net profits. We apply a fixed-effects model at the firm year level which controls for unobserved heterogeneity. We show that this effect follows an almost U-inverted curve, implying that there is an optimal level of environmental investment. Too little or too much environmental effort can be detrimental to firms’ economic performance. Looking more specifically at the shape of the curve, we found that the effect of green investments on economic performance does not exactly follow a perfectly balanced U-inverted function. The part of the curve where investing more in greenness improves profits is reduced and the optimal point is quickly reached, implying that for most firms in our sample, only ‘limited’ green investments are profitable. In other words, win-win strategies exist but they are likely to be quickly ‘exhausted’. This finding also suggests that ‘systematically’ encouraging firms to be always greener can be detrimental to economic performance, when the firms are located beyond the turning point. In a dynamic perspective, managing finely the tensions between green commitments in relation with various stakeholders and the pursuit of profitability can become increasingly complex and costly, but this ability can constitute the key determining whether the chosen level of green investments will be conducive or detrimental to economic performance improvement.

Key-words: environmental investment, economic performance, inverted U-shape, panel, fixed effects.

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