RESEARCH SUMMARY

Economic Regulation and Growth: Lessons from the Empirical Research

In "The Impact of Economic Regulation on Growth: Survey and Synthesis," James Broughel and Robert Hahn review cross-country studies that use indices of regulation produced by the World Bank and the Organisation for Economic Co-operation and Development (OECD). The authors find an apparent consensus in that body of research: economic regulations appear to reduce growth and productivity.

ECONOMIC REGULATIONS CORRESPOND WITH LOWER GROWTH

Economic regulations include regulation that imposes barriers on firms seeking to enter an industry, regulation of product markets, and labor market restrictions on hiring and dismissals. A review of 25 studies that use World Bank and OECD data to assess the impact of economic regulation on growth or productivity finds an apparent consensus that economic regulations slow growth. This is consistent with several aspects of economic theory:

- *Incumbent firms will lobby for regulations that benefit them*. These firms can organize politically to support barriers to entry and other regulations that benefit them at the expense of new firms. This can lead to industrial concentration that reduces competition and the dynamics that spur economic growth.
- *Regulations hurt innovation*. Entrepreneurs wrest markets from established firms by innovating production processes and final products—and firms innovate to escape competition from potential rivals. In both cases, value is created for consumers. However, regulation can dampen competition and, with it, the innovation and creativity that drive long-term growth.
- *Regulations may be portrayed as being in the public interest, but they often limit competition*. Regulations are often defended on public-interest grounds by groups that stand to benefit from them financially. For example, physicians may defend licensing restrictions on nurse practitioners or pharmacists, framing arguments on public health grounds while actually seeking to limit competition in their industry.

OTHER REGULATIONS MAY ALSO AFFECT ECONOMIC GROWTH

These include social and process regulations. Social regulations include health and safety regulations and environmental regulations.

- In practice, *social regulations* and economic regulations tend to overlap. For example, many states have passed certificate-of-need laws that establish an approval process before a new healthcare facility can be constructed.
- Much of *environmental regulation* involves setting up roadblocks to development in the form of permitting, environmental impact statements, or bans on certain kinds of development or modes of production.

- *Process regulations* involve costly activities associated with filling out forms, such as tax forms.

More research is needed to better understand the consequences of social and other forms of regulation on growth. This is especially important given that social regulation has grown to be the dominant form of regulation in the United States.

KEY TAKEAWAY

Empirical evidence supports the theoretical hypothesis that economic regulations can reduce growth. Policymakers should be very cautious about increasing economic regulation. The burden of proof should be on policymakers to show that such regulation is likely to do more good than harm.