



DEREGULATION CAN FUEL ECONOMIC GROWTH IN KENTUCKY

BY WILLIAM BEACH

October 2016

Economic growth is responsible for the astonishing gains in income and standard of living that Americans have experienced since the country's founding. Small differences in the rate of economic growth can translate into huge changes in income and living standards over time. Figure 1 demonstrates the consequences of a growth rate of 2 percent versus a growth rate of 5 percent.

At a 2 percent growth rate, it would take 35 years for Kentucky's gross state product (GSP) to double. If the economy grew at 5 percent, the GSP would quadruple in even less time, just over 28 years. Accounting for population growth, if the economy grew at 2 percent, per capita income would rise to \$72,000 in 35 years, while at a 5 percent growth rate it would grow to \$157,000 in just 28.4 years.

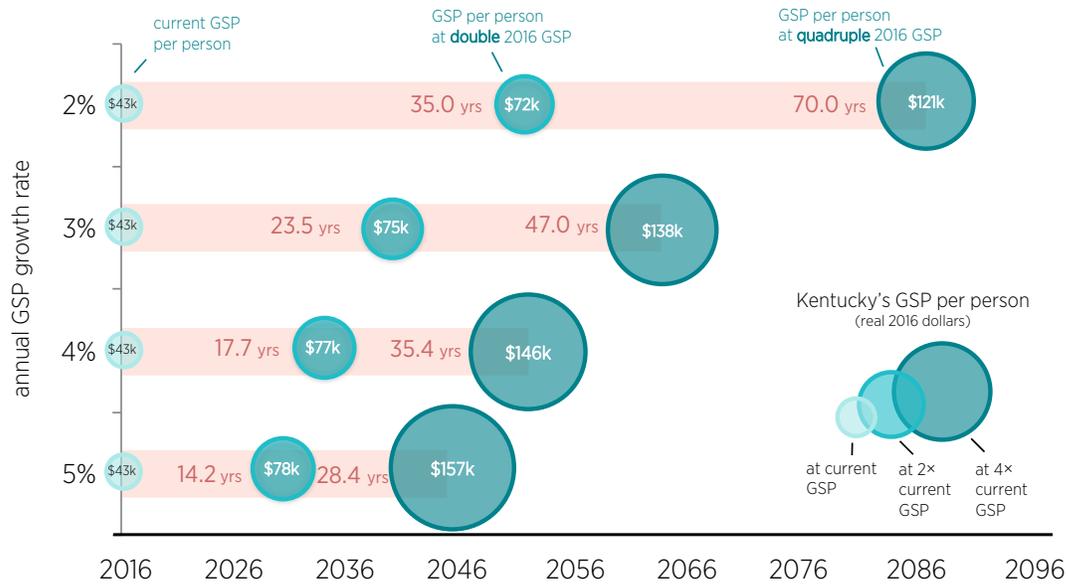
The failure of economic growth to return to its prerecession levels in Kentucky and in the rest of the United States, as figure 2 shows, is a matter of concern with respect to the effect on the income and standards of living of Kentucky residents.

One factor that contributes to slower economic growth is the burden of regulatory accumulation. In a recent study, Bentley Coffey, Patrick A. McLaughlin, and Pietro Peretto constructed a growth model of the US economy using data from the *Code of Federal Regulations* to estimate that regulation led to a \$4 trillion loss in GDP in their base year 2012.¹ That is, had regulations remained at the the same level as they were in the very heavily regulated year of 1980, then the economy would have been 25 percent larger (\$4 trillion) in 2012 than

1. Bentley Coffey, Patrick A. McLaughlin, Pietro Peretto, "The Cumulative Cost of Regulations" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, April 2016).

it actually was.² The 2012 economy employed 135 million workers in December of that year. Assuming a 25 percent greater GDP would employ a proportionally greater number of workers, the 2012 US economy was missing 34 million jobs to go with the trillions of dollars in missing output.

Figure 1. How Long Would It Take to Double or Quadruple Kentucky's GDP under Various Annual GSP Growth Rates?



Data note: GSP figures are in real 2016 dollars.
Sources: US Census Bureau projections and author's calculations.

In addition to the rising burden of state regulation in Kentucky,³ the federal regulation and state enterprise index demonstrates that federal regulation imposes a higher-than-typical burden as well. Federal regulations affect Kentucky's businesses over 30 percent more than they affect the average state's.⁴ Table 1 shows the most regulated industries in the United States.

2. McLaughlin's research on regulatory accumulation is summarized in a recent Mercatus publication. See Patrick A. McLaughlin, Nita Ghei, and Michael Wilt, "Regulatory Accumulation and Its Costs," *Economic Perspectives*, Mercatus Center at George Mason University, May 4, 2016.

3. James Broughel, "Regulation on the Rise in Kentucky" (Policy Brief, Mercatus Center at George Mason University, Arlington, VA, September 2016).

4. Patrick A. McLaughlin and Oliver Sherouse, *The Impact of Federal Regulation on the 50 States*, 2016 ed. (Arlington, VA: Mercatus Center at George Mason University, 2016), 114.

Figure 2. The Kentucky Economy: Total GSP and Average Annual GSP Growth



Sources: Federal Reserve Economic Data and author's calculations.

While reducing the burden of federal regulations for Kentucky would require federal-level reform, the state government has the power to reduce state-level rules that impede economic growth. Over the past 40 years, the number of books making up the Kentucky Administrative Regulations have more than tripled.⁵ The regulators that issue the most rules in Kentucky are the Department for Public Health and the Department for Environmental Protection.⁶

Economic growth is the key to increasing living standards for Kentuckians. Regulations reduce growth rates, and small changes in the growth rate result in large changes in per capita income over time. Regulatory reform at the federal and state levels has the potential to unleash economic growth for Kentucky.

5. Broughel, "Regulation on the Rise in Kentucky."

6. James Broughel and Oliver Sherouse, "A Snapshot of Kentucky Regulation in 2015" (Policy Brief, Mercatus Center at George Mason University, September 2016).

Table 1. McLaughlin-Sherouse Top 10 Most Regulated Industries for 2014

NAICS code	Industry name	Industry-relevant restrictions
3241	Petroleum and coal products manufacturing	25.48
2211	Electric power generation, transmission, and distribution	20.96
3361	Motor vehicle manufacturing	16.76
5222	Nondepository credit intermediation	16.58
5221	Depository credit intermediation	16.03
4811	Scheduled air transportation	13.31
1141	Fishing	13.22
5239	Other financial investment activities	12.26
2111	Oil and gas extraction	11.95
3254	Pharmaceutical and medicine manufacturing	11.51

Data note: The number of industry-relevant restrictions is divided by 1,000 for ease of reading.

Source: Patrick A. McLaughlin and Oliver Sherouse, *The Impact of Federal Regulation on the 50 States*, 2016 ed. (Arlington, VA: Mercatus Center at George Mason University, 2016), 114.

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