

THE IMPACT OF STATE-LEVEL REGULATORY ACCUMULATION ON ECONOMIC GROWTH

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Although federal regulations are the usual focus of popular discourse on deregulation, state-level regulations are important too. My 2024 study with John T. H. Wong examines the causal relationship between state-level regulatory accumulation and economic growth.¹ Using novel measurement techniques and robust statistical analysis, we find substantial evidence that higher levels of state regulation significantly reduce state GDP growth. Specifically, a 10 percent increase in state regulatory restrictions leads to a 0.37 percentage point reduction in annual GDP growth. Regulatory reform—specifically, reform that leads to substantial elimination of red tape—would dramatically boost economic growth. A typical state could increase its annual GDP growth rate by about 1.5 percentage points by eliminating 40 percent of its regulations.

UNDERSTANDING THE METHODOLOGY

Traditionally, researchers have struggled to measure the true economic impact of regulations owing to the lack of precise data and difficulties in identifying causal relationships. We overcome these challenges by using two key innovations:

1. *Quantitative measurement of regulation.* We employ State RegData, a database containing counts of specific restrictive terms such as “shall,” “must,” “may not,” “required,” and “prohibited” in regulatory texts. This database allows direct and consistent measurement of regulatory accumulation across different states and years.
2. *Instrumental variable analysis using state age.* To establish a causal link between regulations and growth, we utilize the concept of institutional sclerosis proposed by economist Mancur Olson. Institutional sclerosis suggests that older societies become stagnant owing to entrenched interest groups that increasingly impose restrictive regulations. Hence, state age—the number of years since a state was admitted to the Union—serves as an instrumental variable, providing a source of exogenous variation unrelated to current economic performance.

Using state age as an instrumental variable allows us to isolate the causal impact of regulation from other factors that might simultaneously influence economic growth and regulatory environments, such as political pressures or economic shocks. We can therefore infer and estimate the causal relationship between regulations and economic growth at the state level.

KEY FINDINGS AND ANALYSIS

- *Regulatory impact on GDP.* The analysis shows a strong negative relationship between the accumulation of regulatory restrictions and economic growth. The robust statistical methods employed demonstrate that reducing regulations can significantly boost economic performance.

- *Magnitude of economic effects.* A relatively moderate reduction in regulations (approximately 10 percent) can meaningfully enhance state GDP growth rates, contributing significantly to long-term economic prosperity. These findings align with other studies showing similar impacts at national and subnational levels,² although ours is the first study (to our knowledge) to show such a relationship at the state level in the United States.
- *Robustness of results.* We validate our results through multiple robustness checks, including alternative lag structures, different functional forms of regulation measurement, and geographic controls. The findings consistently indicate that the relationship between regulatory accumulation and lower GDP growth is genuine and substantial.

POLICY IMPLICATIONS

This study has several critical policy implications:

- *Prioritize regulatory reduction.* Policymakers interested in stimulating their state’s economic growth should prioritize systematic efforts to reduce regulatory accumulation. Regular reviews and sunset clauses for regulations could prevent unnecessary restrictions from persisting indefinitely.
- *Implement regulatory budgeting.* Inspired by British Columbia’s successful regulatory budgeting experiment, US states could implement regulatory budgeting frameworks requiring that any new regulation be offset by the elimination of existing ones.
- *Target regulatory complexity.* Simplifying existing regulations and reducing ambiguity can decrease compliance costs, limit opportunities for regulatory capture, and enhance economic dynamism.
- *Monitoring and transparency.* States could adopt transparent monitoring systems for regulatory accumulation, similar to State RegData, enabling informed policy decisions. Transparency facilitates accountability and encourages policymakers to justify regulations clearly and compellingly.

CONCLUSION

This research strongly supports the argument for regulatory reform as a lever to boost economic growth. By demonstrating a clear causal link between regulatory volume and GDP growth, this study provides a solid foundation for policies aimed at reducing regulatory burdens. State policymakers interested in fostering economic prosperity, resilience, and innovation should act upon these insights.

NOTES

1. Patrick A. McLaughlin and John T. H. Wong, “The Causal Effect of Regulations on Economic Growth: Evidence from the US States” (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, December 2024).
2. Bentley Coffey and Patrick A. McLaughlin, “Regulation and Economic Growth: Evidence from British Columbia’s

Experiment in Regulatory Budgeting” (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, 2021); Bentley Coffey, Patrick A. McLaughlin, and Pietro F. Peretto, “The Cumulative Cost of Regulations,” *Review of Economic Dynamics* 38 (2020): 1–21.



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