Trump team fails to grasp entire nature of regulatory burden

Brink Lindsey

February 24, 2017

The Trump administration is promising to kick-start economic growth by slashing federal regulations "by 75 percent, maybe more" in hyperbolic Trump-speak. The basic idea is sound — excessive regulation is a significant drag on America's long-term growth prospects. But in major respects, the administration's approach to the problem looks seriously flawed.

Policymakers intent on boosting the sputtering U.S. growth rate are well advised to look at regulation. Even though rules to protect health, safety, the environment, and workplace fairness serve important objectives, they also impose costs on business — especially on new and small firms that lack the scale to absorb all the fixed costs of regulatory compliance.

Even if every individual rule makes sense, the steady pileup of new rules, year after year, along with the unforeseen interactions among rules, can produce a policy environment that is affirmatively hostile to innovation and growth. Pruning the overgrown regulatory state is long overdue.

So far, so good. But the early indications are that the Trump administration's approach to regulatory reform is flawed in two important respects. First, the Trump team is flawed in threatening to raise regulatory burdens, perhaps disastrously, in a pair of vitally important policy areas. Second, it fails to see that some of the most serious regulatory impediments to growth aren't costs imposed on existing businesses but subsidies granted to existing businesses at the expense of the rest of us.

All the big talk about cutting regulations ignores the fact that restrictions on trade and immigration are regulations too. In this way, the Trump administration seems itching to slam businesses with huge new burdens. Trump's trade adviser, Peter Navarro, said the administration

wants to unwind U.S. multinationals' global production chains and move manufacturing back home.

In other words, Navarro advocates for a policy of deglobalization. Meanwhile, Trump's top aide, Steve Bannon, has declared that legal immigration, not illegal immigration, is the real problem and complained that there are too many Asian-born CEOs in Silicon Valley. If this rank hostility to American interdependence with the global economy is translated into policy, the long-term impact on U.S. dynamism and economic leadership could be devastating.

In addition to being jarringly inconsistent about regulatory cost-cutting, the new administration hasn't realized that there's more to pro-growth regulatory reform than cutting costs. Indeed, some of the most damaging regulatory policies today confer big subsidies on existing firms. In so doing, they generate huge waste by misdirecting economic activity and reduce innovation by shielding market incumbents from new competition.

Financial regulation, for example, lavishes subsidies on financial institutions. Access to the Federal Reserve as a lender of last resort, deposit insurance, and ad hoc bailouts when a crisis hits allow financial firms to engage in excessive risk-taking that promote fat profits now but catastrophic risk down the road.

In addition, an enormous edifice of subsidies supports mortgage finance in general — and securitization in particular — and it's only gotten worse since the housing bubble imploded. As of 2016, nearly 80 percent of all new mortgages are being bought and securitized by state-owned entities Fannie Mae and Freddie Mac.

Because of these and other policies, the bloated financial sector gobbles up capital and top talent that could be deployed more productively elsewhere, depressing economic growth even as it piles up massive fortunes for Wall Street.

Intellectual property is another policy area choked with regulatory subsidies. Wildly excessive copyright terms do nothing to incentivize artistic expression, but they're great at lining the pockets of giant media companies by keeping their cash cows out of the public domain.

At the same time, a loosening of patenting standards in recent decades has led to an almost fivefold jump in the number of patents issued annually. The result has been the creation of a legal minefield for innovators, while patent "trolls", who live off harassment litigation, have a field day.

At the state level, the proliferation of occupational licensing laws means that almost 30 percent of jobs in this country now require government permission. These laws largely fail to protect consumers — their ostensible purpose — but are highly effective at inflating the pay of regulated professionals by restricting supply. By locking in established ways of doing things, licensing requirements are a major impediment to innovation as well.

Regulatory subsidies created by these and many other policies are a massive blind spot in the new administration's plans for reform. Regarding financial regulation, all the focus is on rolling back new costs imposed by Dodd-Frank, not reducing the huge subsidies conferred by existing

law. Meanwhile, intellectual property and occupational licensing are off the radar screen entirely.

Regulatory reform is immensely important, but if you do it wrong you can discredit the whole enterprise. Right now the Trump administration looks poised to do precisely that.

Brink Lindsey is vice president for research at the Cato Institute.