



For faster growth, pick freedom

John Hood

September 13, 2022

When pollsters ask voters to list the issues they care about most, economic concerns usually rank high on the list — even when unemployment rates are relatively low.

There's a stolen base here, however. With very few exceptions, most people think a rapidly growing economy is critically important. They recognize that other social problems usually get better if jobs are plentiful and incomes are rising. Where voters differ is on how policymakers can most effectively boost growth. So including economic concerns in a list that also includes, say, education or tax relief can obscure what voters really value. Some will rank "the economy" as a top issue, even as they're thinking about specific policies that, in their minds, will improve the economy.

Here in North Carolina, we have for many years witnessed a robust debate about how best to enhance our state's economic competitiveness and growth rates. Republicans argue that the tax reductions and regulatory relief they've enacted were wise investments in future economic growth, in part by making it more likely that new or expanded enterprises will be in North Carolina.

Democrats argue it would have been more growth-enhancing to forego the tax cuts, in favor of spending more on education and other services, as well as to forego the regulatory relief, on the grounds that employers, entrepreneurs, professionals, and workers would place a higher value on the anticipated environmental or safety benefits of the regulations than on the lower costs that come from reforming or eliminating them.

The two alternatives represent core philosophical differences, obviously. But that doesn't mean they aren't testable propositions. I'll grade those tests in just a moment.

First, though, I want to point out that while there is a gap between these two positions, it's not the ideological equivalent of the Grand Canyon. North Carolina Republicans have enacted a series of state budgets that spent tens of billions of dollars a year on education, infrastructure, and other government services. They've also implemented policy changes, such as performance pay for teachers and school choice for parents, that they believe will boost academic achievement among North Carolina students.

I also assume, although I'm open to evidence to the contrary, that North Carolina Democrats don't want to raise our tax and regulatory burdens to the level of, say, New York — which ranks dead last in economic freedom according to indices published by the Frasier Institute and the Cato Institute.

Moreover, it's striking how many Democrats attack Republicans for cutting business taxes across the board while simultaneously criticizing them for failing to give large-enough tax breaks to favored corporations such as automakers or to favored industries such as movie production. I guess taxes really do matter, sometimes.

Now, my report card. I keep a running tally of peer-reviewed studies examining relationships between state policy factors and growth measures such as gross state product (GSP), job creation, income gains, and business starts. My database currently contains more than 1,000 such studies published since 1990.

Based on the empirical evidence, North Carolina Republicans get an A. Most studies show that, after adjusting for a range of control variables, states and localities with higher degrees of economic freedom — lower taxes, fewer regulations — have stronger economic performance than less-free jurisdictions do. For example, a 2022 paper in the journal *Small Business Economics* found that in communities that straddle state lines, entrepreneurs are more likely to start their new businesses in the lower-taxed state.

How about the Democratic thesis? I'll give it a D. Most studies do show a correlation between conditions such as educational attainment or infrastructure quality and state economic growth. But they don't find a link to expenditures. Only a third of studies find that states with larger education budgets have stronger economic performance, for example.

These findings suggest that state policymakers should find ways to boost economic freedom while making their education and infrastructure systems more productive. North Carolina's legislative leaders would say that's precisely what they've been doing.