

## **Increasing the Minimum Wage: Ineffective at Reducing Poverty**

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Most people who earn the minimum wage or slightly more are the only earners in their households and, therefore, are poor, right? And so, if the federal government or state governments raise the minimum wage, that will be a nicely targeted way of helping poor people, right?

Well, no. Wrong on both counts. Most workers earning at or close to the minimum wage are not the sole earners in a household and most of them are not in poor households. For those two reasons, raising the minimum wage will do little to help poor people.

Between 2003 and 2007, 28 states increased their minimum wages to a level higher than the federal minimum. San Diego State University economics professor Joseph J. Sabia and Cornell University economics professor Richard V. Burkhauser examined the effects of these increases and report their results in the prestigious *Southern Economic Journal*.<sup>1</sup> They “find no evidence that minimum wage increases between 2003 and 2007 lowered state poverty rates.”

In that same article, they write that a proposed increase in the minimum wage from \$7.25 to \$9.50 per hour “is not well targeted to the working poor.”

Specifically, they find that if the federal minimum wage were increased to \$9.50 per hour:

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<sup>1</sup> Joseph J. Sabia and Richard V. Burkhauser, “Minimum Wages and Poverty: Will a \$9.50 Federal Minimum Wage Really Help the Working Poor?” *Southern Economic Journal*.

- Only 11.3 percent of workers who would gain from the increase live in households officially defined as poor.
- A whopping 63.2 percent of workers who would gain are second or even third earners living in households with incomes equal to twice the poverty line or more.
- Some 42.3 percent of workers who would gain are second or even third earners who live in households that have incomes equal to three times the poverty line or more.

They reached their conclusions by carefully examining U.S. Census data on household incomes and wages reported in the Current Population Survey. Thus:

- The net increase in wage income to households containing low-wage workers would be \$4.03 billion per month.
- The net increase in wages to poor households containing low-wage workers would only be \$439 million per month.

Moreover, note Sabia and Burkhauser, an estimate of gains in income to households with low-wage workers necessarily overstates those gains if the estimate does not take account of one of the most well-documented effects of the minimum wage: it destroys low-wage jobs. For over 60 years, economists have been aware that increases in the minimum wage cause some low-wage workers to lose their jobs. The reason: at a higher wage, the value of their output per hour (productivity) is not high enough for employers to gain by hiring them.

When they take this job-loss effect into account, Sabia and Burkhauser conclude that an increase in the minimum wage will be even *less* effective at reducing poverty. A

low-end estimate of the reduction in jobs due to an increase in the minimum wage is that a 10 percent increase in the minimum wage would reduce the number of low-wage jobs by only one percent. Economists refer to this as an elasticity of 0.1 (1 divided by 10). But even in this best case, the proposed increase in the minimum wage to \$9.50 per hour would destroy 468,000 jobs. This means that the benefits of a higher minimum wage to households containing low-wage workers would be even lower than their original estimates concluded. With the 468,000 job loss noted above:

- The net benefit to households containing low-wage workers would be \$3.56 billion per month.
- The net benefit to poor households containing low-wage workers would be \$389 million per month.

Another reasonable estimate from earlier studies is that a 10 percent increase in the minimum wage would destroy 3 percent of low-wage jobs, an elasticity of 0.3. If that estimate is correct, then the proposed minimum wage increase to \$9.50 per hour would destroy 1.4 million jobs. If that job destruction occurs, the net benefit of the minimum wage to households containing low-wage workers would be only \$2.63 billion per month, of which only \$287 million would be a gain to households in poverty.

Even these estimates are an overstatement of the gains to households from increasing the minimum wage. Why? Because, to the extent they are able, employers will offset the higher minimum wage by reducing non-money components of worker compensation. Burkhauser notes that such an effect will not show up in the government data because the data do not measure these non-money parts of the compensation

package.<sup>2</sup> But that is small comfort to those who would find themselves with higher-paying but reduced-benefit jobs.

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<b>Effects of an Increase in the Minimum Wage from \$7.25 to \$9.50</b>		
	Minimum wage workers living in households with poverty level incomes or less	Minimum wage workers living in households with incomes 2 to 3 times the poverty level
Percentage of minimum wage workers	11.3%	63.2%
Monthly gains to households if there are no job losses	\$439 million	\$4.03 billion
Monthly gains to households if there are 468,000 job losses (low estimate)	\$389 million	\$3.56 billion
Monthly gains to households if there are 1,402,000 job losses (higher estimate)	\$287 million	\$2.63 billion

<sup>2</sup> E-mail correspondence, December 17, 2013.