

BRIEF ANALYSIS

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The Minimum Wage Trap

President Clinton is asking Congress to raise the minimum wage by 90 cents over two years to \$5.15 per hour, a 21 percent increase. The president made the request even though most studies confirm a 1981 estimate by the congressionally mandated Minimum Wage Study Commission that a 10 percent increase in the minimum wage reduces teenage employment by 1 percent to 3 percent. This suggests that between 130,000 and 400,000 jobs will be lost if the Clinton plan is approved by Congress.

The Clinton administration has promoted studies of how increases in the state minimum wage in New Jersey and California affected employment in fast food restaurants. Economists David Card and Alan Krueger, both of Princeton, found no evidence the increases caused job losses. However, other researchers found errors in the data that cast serious doubt on the validity of the Card-Krueger conclusions. Nobel Prize-winning economist Gary Becker of the University of Chicago concluded that "the Card-Krueger studies are flawed and cannot justify going against the accumulated evidence from many past and present studies that find sizable negative effects of higher minimums on employment."

With the exception of the Card-Krueger findings, virtually every major study that has ever been done has found significant job losses from an increase in the minimum wage. But even if one accepts the Card-Krueger findings, evidence of other unfavorable effects makes an overwhelming case that the minimum wage should not be raised and that, in fact, abolishing it would do more for those it is intended to help.

Among wage and salary workers, 98.2 percent already earn more than the minimum or are not covered by

the law. However, for workers in low-wage industries, those without skills, members of minority groups and those living in areas where wages tend to be lower, the impact can be severe.

Reducing Opportunities for Youths. The unemployment rate for black teenage males has tended to rise and fall with changes in the real minimum wage [see Figure I].

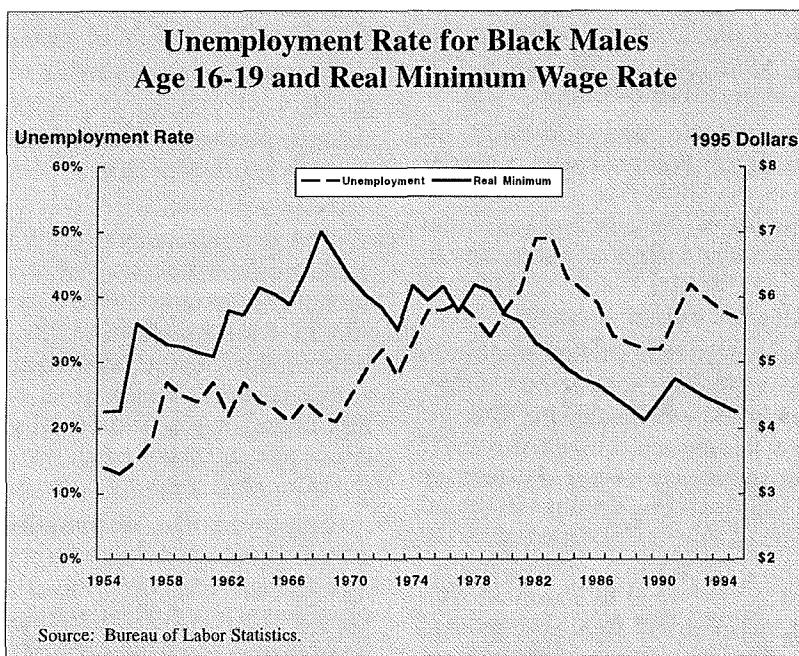
■ In 1948, when the minimum wage covered a much smaller portion of the labor force, the unemployment rate for black males age 16 and 17 was just 9.4 percent, while the comparable unemployment rate for whites was 10.2 percent.

■ In 1995, unemployment among black teenage males was 37.1 percent, while the unemployment rate for white teenage males was 15.6 percent.

Current unemployment is just a part of the long-term price that teenagers of all races pay for the minimum wage. A number of studies have shown that increases in the minimum wage lead employers to cut back on work hours and training. Combined with the loss of job opportunities, this means that many

youths, especially minorities, are prevented from reaching the first rung on the ladder of success, with consequences that can last a lifetime. Even some liberals recognize that this may be the worst effect of the minimum wage law. For example, in 1992 former Senator and Democratic presidential candidate George McGovern wrote in the *Los Angeles Times*:

Unfortunately, many entry-level jobs are being phased out as employment costs grow faster than productivity. In that situation, employers are pressured to replace marginal employees with self-service or automation or to eliminate the service altogether. When



Source: Bureau of Labor Statistics.

these jobs disappear, where will young people and those with minimal skills get a start in learning the “invisible curriculum” we all learn on the job? The inexperienced applicant cannot learn about work without a job.

Other Bad Effects. When people cannot get legitimate jobs, it is not surprising that they turn to crime and the underground economy.

- Studies by Professors Masanori Hashimoto of Ohio State and Llad Phillips of the University of California at Santa Barbara both show that increases in the minimum wage increase teenage crime.
- A study by Professor William Beranek of the University of Georgia found that the minimum wage increases employment of illegal aliens, who are unlikely to report any violations of the Fair Labor Standards Act to the Department of Labor.

Research also shows that the minimum wage increases welfare dependency. For example, a recent study by Peter Brandon of the University of Wisconsin found that the average time on welfare among states that raised the minimum wage was 44 percent higher than in states that did not. Much of the reason is reduced employment opportunities for welfare mothers.

Intuitively, one would expect a higher minimum wage to make work more rewarding for those on welfare. However, the interaction of the welfare and tax systems means that some working people are actually worse off after an increase in the minimum wage. Economist Carlos Bonilla of the Employment Policies Institute found a dramatic example of this in California after the minimum wage rose from \$3.35 to \$4.25. After accounting for the phase-out of AFDC (Aid to Families with Dependent Children), Medicaid and food stamps, and for federal, state and local taxes, a single parent earning the minimum wage was \$1,800 per year worse off after the increase than before.

Finally, the latest research has shown that increases in the minimum wage encourage high school students to drop out—enticed by the lure of higher pay for unskilled work. This reduces their lifetime earnings and displaces lower-skilled workers at the same time.

Given these kinds of effects, it is not surprising that the minimum wage has almost no impact on poverty or on increasing the incomes of the poor. Although some poor people are better off because they get higher wages, others are worse off because they lose their jobs. One study found that the 22 percent increase in the minimum wage in 1976 added just \$200 million to the aggregate

income of those in the lowest 10 percent of the income distribution. Indeed, much of the benefit of the minimum wage actually accrues to the well-off whose children work part-time.

Little Impact on Families. Talk about the difficulty of supporting a family on the minimum wage ignores the fact that only a very small number of workers earning the minimum wage actually support a family. According to the Bureau of Labor Statistics:

- Only 22,000 men and 191,000 women nationwide maintained families on a minimum wage job in 1993.
- Thirty-seven percent of minimum wage workers in 1995 were teenagers, probably living at home, and 59 percent were age 24 or younger.
- About 17 percent of minimum wage workers are wives, and thus are likely to be secondary earners.
- Sixty-six percent of minimum wage workers work only part-time; these include students, the elderly with pension or Social Security income and people simply looking for a little extra cash.

These data actually overstate the number of minimum wage workers, because 49 percent work in retail trade, such as restaurants, where tips and commissions may add to their income but are not counted as wages. Further, the data include only money wages and exclude fringe benefits, which push the total income of most minimum wage workers well above the minimum. As a consequence, many employers respond to increases in the minimum wage by cutting back on benefits.

Employers also respond by cutting back on hours, installing labor-saving equipment and by changing the mix of part-time and full-time workers. This is one reason why it is difficult to find a bank teller or someone to wait on you at the local department store. Between 1963 and 1995, average weekly hours worked in retail trade, the industry most affected by the minimum wage, fell from 37.3 to 28.9, while hours worked in higher-paid industries that are basically unaffected by the minimum wage, such as mining and construction, increased.

Even the *New York Times*, a bastion of liberalism, has called for the abolition of the minimum wage. The headline on its January 14, 1987 lead editorial said, “The Right Minimum Wage: \$0.00.” Indeed, according to Professors Robert Meyer of the University of Chicago and David Wise of Harvard, abolition would actually increase the aggregate income of youth in this country.

This Brief Analysis was prepared by NCPA Senior Fellow Bruce Bartlett.