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Higher Minimum Wage No Longer Seen as Sure-Fire U.S. Job Killer

By Kim Chipman - Aug 07, 2006

Aug. 7 (Bloomberg) -- Prominent economists of all ideological persuasions long believed that raising the U.S. minimum wage would retard job growth, creating unintended hardship for those at the bottom of the ladder.

Today, that consensus is eroding, and a vigorous debate has developed as some argue that boosting the wage would pull millions out of poverty.

A moderate increase in the minimum wage won't raise unemployment among low-skilled workers, according to recent studies, many economists say. They are joined by some business executives who say they can live with that, especially if it's coupled with tax relief.

"My thinking on this has changed dramatically," says Alan Blinder, a former Federal Reserve vice chairman who teaches economics at Princeton University in Princeton, New Jersey. "The evidence appears to be against the simple-minded theory that a modest increase in the minimum wage causes substantial job loss."

The debate over how to help struggling American workers was at the center of a battle in Congress last week over whether to increase the federal minimum wage to \$7.25 an hour by 2009 from the current \$5.15. The measure failed after Democrats objected that the wage increase had been linked to a plan to roll back the federal estate tax for many multimillion-dollar estates.

Democrats said they would try to revive the measure before the November elections without the estate tax provision. "The Senate won't adjourn until hard-working Americans get the help they need," said Senate Minority Leader Harry Reid of Nevada.

Keeping Pace

Blinder and others note that the federal minimum wage, last raised in 1997, is at its lowest level in 50 years when adjusted for inflation.

"Workers' wages need to at least keep pace with inflation," says Andrew Puzder, chief executive officer of Carpinteria, California-based CKE Restaurants Inc., which owns the Hardee's and Carl's Jr. fast-food restaurant chains. Puzder says he supports a reasonable increase in the minimum wage along with some form of tax relief for small businesses.

In a Wells Fargo-Gallup poll taken in March, 46 percent of small-business owners said the minimum wage should be increased, and 86 percent said the wage had no effect on them.

“The wage has been left at such a low level for so many years now that inflation has eroded it,” says Scott Anderson, a senior economist at San Francisco-based Wells Fargo & Co., the fifth-biggest U.S. bank. “It’s not as onerous to employers as it once was.”

Traditional View

Edward Lazear, chairman of the White House Council of Economic Advisers, says President George W. Bush is willing to work with Congress on finding ways to boost the minimum wage that won’t significantly harm businesses. “He’s not opposed to changing the minimum wage, but it has to be done in a sensible way,” Lazear said in a July 24 interview.

Other economists still argue that the traditional view is right.

“The law of demand says simply that the higher the price of anything, the lower the quantity that will be taken,” says William Dunkelberg, chief economist of the Washington-based National Federation of Independent Business. “This law has never been incorrect in predicting market behavior.”

Most evidence suggests “that a minimum wage increase causes some job loss among low-skilled workers,” says David Neumark of the University of California, Irvine. Neumark has written studies critical of research casting doubt on that view and has testified before Congress against minimum-wage increases.

Changing Views

This view once was widespread. A 1978 American Economic Review survey found that 90 percent of economists said the minimum wage boosted unemployment among low-skilled workers.

Today, that number would probably be cut in half, says Robert Solow, an economist at the Massachusetts Institute of Technology in Cambridge who won the 1987 Nobel Prize in economics.

A turning point in the debate came in the 1990s as states such as New Jersey began boosting their mandated wages above the federal level.

In 1995, Princeton economists David Card and Alan Krueger published research on unemployment trends among fast-food restaurants in New Jersey and neighboring Pennsylvania. They found that the number of jobs rose in New Jersey compared with Pennsylvania, even though New Jersey had a higher minimum wage.

The study, while not perfect, “provided evidence that went against the common view,” Solow says. “It changed the way many economists look at minimum wage.”

'How Small the Effect'

'The debate now has become over how small the effect is as opposed to how large," says Arindrajit Dube, a labor economist at the University of California at Berkeley.

Binder acknowledges that it's an "intellectual puzzle" why a boost in the minimum wage wouldn't lead to wider unemployment, because the economic laws of supply and demand dictate that it should.

Explanations include cost savings from reduced job turnover, increased productivity as a result of better worker morale and the attraction of higher-quality employees through higher wages, Blinder says.

To workers whose pay is at or near the minimum wage, raising it makes sense.

"I want a raise in the wage not just to boost me up, but because it will help us out as a country," says Sandy Mayes, a 39-year-old mother of four from Louisville, Kentucky, who says she sometimes takes minimum-wage jobs to supplement the \$17,800 a year she earns as a teachers' assistant. "Working in a school, I see parents who work themselves to death to live below average, and their kids suffer tremendously."

Social Consequences

A boost in the minimum wage would benefit about 15 million people, according to the Economic Policy Institute, a Washington research group partially funded by labor unions. Jared Bernstein, a senior economist at the institute, estimates that the average minimum-wage worker generates 54 percent of his or her family's total weekly earnings.

"The social consequences of raising the wage have become increasingly important," says Nobel Prize-winning economist Joseph Stiglitz, former chief economist for the World Bank in Washington and now a professor at Columbia University in New York.

Some economists say the 1997 increase had no impact on job growth.

"We saw no ripple effect at all in the unemployment rate," Stiglitz says. "Unemployment just continued to go down." The minimum wage increase, he said, "was totally swamped by other factors going on in the economy."

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