

Minimum Wages: One View From the U.S

John DiNardo



Outline

1 Introduction

- Preliminaries
- Everyone Thinks Minimum Wage Laws Are A Good Idea ...
- Quale cose sono più popolari?
- Una delle costrutti più crudeli di una società spesso crudele?

2 Some of The Politics and History

- American History of Minimum Wage

3 The English Language Debate

4 The Biggest Experiment

5 Today and Key Questions



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Preliminaries

- 1 Arguably no market exhibits more diversity across countries than the labor market.
- 2 The U.S. labor market is characterized by unusually low rates of unionization and (weakened) labor unions. Less than 8% of the private employment is unionized.
- 3 Almost all decisions about wages and employment are “decentralized.”



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Everyone Thinks Minimum Wage Laws are A Good Idea ...

Do you support raising the minimum wage? (2006)

Your Income	Yes	No
Less than \$20,000 per year	94	3
\$20,000 < Income < 29,999	87	11
\$30,000 < Income < 49,999	83	14
\$50,000 < Income < 74,999	79	14
\$75,000 or more	79	14



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Solo il Dio è il Paradiso

Do you believe in:	Yes	No	Not Sure
God	92%	5	3
Heaven	85%	10	5
Raise Minimum Wage	83%	14	3
Miracles	82%	14	4
Angels	78%	15	7
Hell	74%	20	6
The Devil	71%	24	5

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¹FOX News and Opinion Dynamics, 2004

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Except Economists

”one of the cruelest constructs of an often cruel society”

Finis Welch

The inverse relationship between quantity demanded and price is the core proposition in economic science, . . . [Denial of such a claim,] if seriously advanced, becomes equivalent to a denial that there is even minimal scientific content in economics, and that, in consequence, economists can do nothing but write as advocates for ideological interests. Fortunately, only a handful of economists are willing to throw over the teaching of two centuries; we have not yet become a bevy of camp-following whores.

James Buchanan, 1986 Nobel Laureate in Economic Science



Except Economists

A poll of Economists in the U.S. when asked: The federal minimum wage in the U.S. should be:

- | | |
|--|--------------|
| a. Eliminated. | 46.8% |
| b. Decreased. | 1.3 |
| c. kept at the current level. | 14.3 |
| d. increased by about 50 cents per hour. | 5.2 |
| e. increased by about \$1 per hour. | 15.6 |
| f. increased by more than \$1 per hour. | 16.9 |

Slightly more popular among labor economists. 43% of labor economists disagreed with the idea of increasing the minimum wage. 57% of were in favor of increasing. (Fall 2005)



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Even Small Business Owners Are Indifferent or Support (2006)

- 1 Overall, small business owners seem supportive of a minimum wage.
 - ▶ In fact, 46% would favor an increase in the minimum wage.
 - ▶ Another 34% believe it is at the appropriate level right now.
 - ▶ Just 16% want to see the minimum wage either reduced (2%) or eliminated altogether (14%).
- 2 Still, 86% of business owners say the minimum wage has no effect on them
 - ▶ 5% say it has a positive effect
 - ▶ 8% say negative.

The fast food lobby is a big exception!



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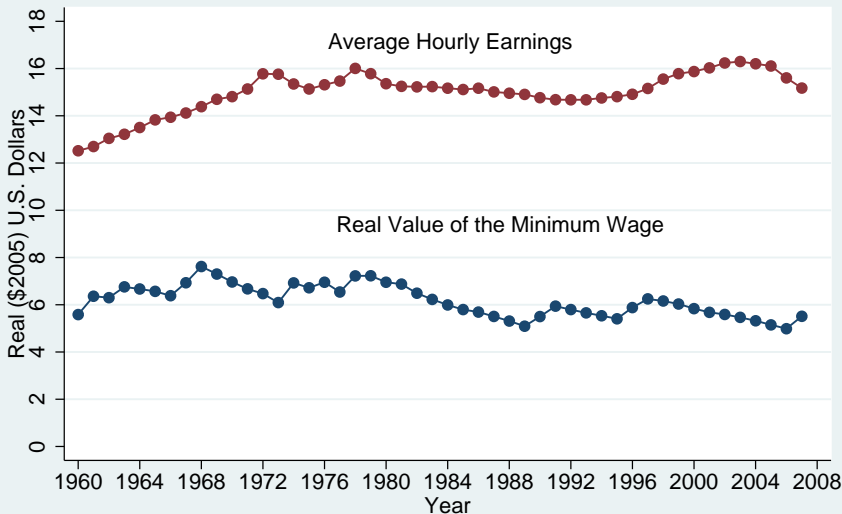
Why do so many US Economists Dislike the Minimum Wage

- 1 Among many, the belief that minimum wages lower employment is a “core proposition of economic science.”
- 2 Hence, a tremendous focus on employment for “at risk” groups (young people, etc.)



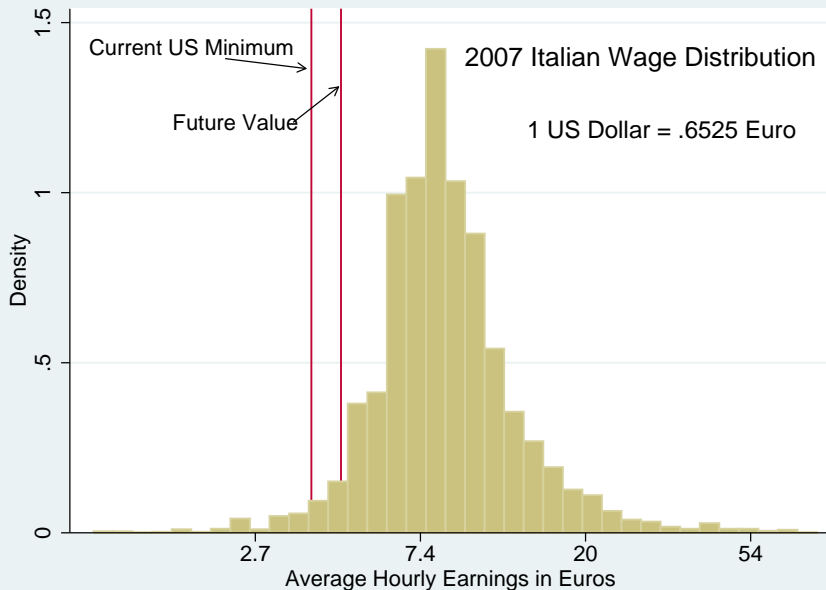
The Minimum Wage Has Been Quite Low

The (Real) Minimum Wage and Average Hourly Earnings:
1960 – 2007



A U.S. level of Minimum wages in Italy would be low.

A Very Rough Approximation



And Has been Adjusted Politically

Used sometimes by Democrats to (lightly) beat Republicans. Used sometimes by Republicans to win additional tax cuts.

- 1 First Clinton Term, Democratic President and Democratic Congress, **no increase** in minimum wage.
- 2 Second Clinton Term, Democratic President and Republican Congress, **increase in minimum wage**. (along with tax cuts)



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Some History

- 1 Serious labor agitation in 1900 - 1929 period. Some attempts at state minimum wage laws before the new deal generally ruled illegal.
- 2 *Hammer v. Dagenhar* the Supreme Court made it illegal to even ban child labor.
- 3 *Adkins v. Children's Hospital* 1923, rules that minimum wages (applied only to women) were illegal.
- 4 FDR, 1938 (Fair Labor Standards Act):
“Do not let any calamity-howling executive with an income of \$1,000 a day, . . . tell you . . . that a wage of \$11 a week is going to have a disastrous effect on all American industry”
- 5 Supreme Court continued to fight against it.
- 6 Only 48% of workers were covered. “Low wage” sectors originally exempt. Expansions in the 1970s lead to about 86% of workers being covered.



Usual Practice

- When demand for an increase becomes too great to ignore, it is raised in *nominal* terms. (Not indexed to inflation.)
- Inflation erodes the value of the minimum wage until demand again becomes too great.

Nominal Wage Increase in Federal Minimum

Actual Changes		Recent & Future Changes	
January 1978	\$2.65	July 24, 2007	\$5.85
January 1979	\$2.90	July 24, 2008	\$6.55
January 1980	\$3.10	July 24, 2009	\$7.25
January 1981	\$3.35		
October 1996	\$4.75		
Sept. 1997	\$5.15		



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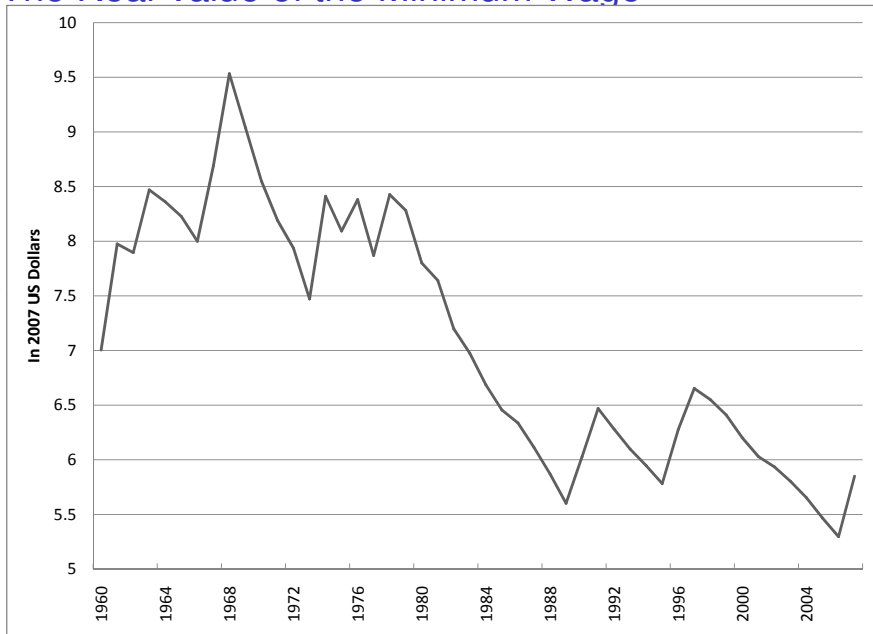
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The Real Value of the Minimum Wage

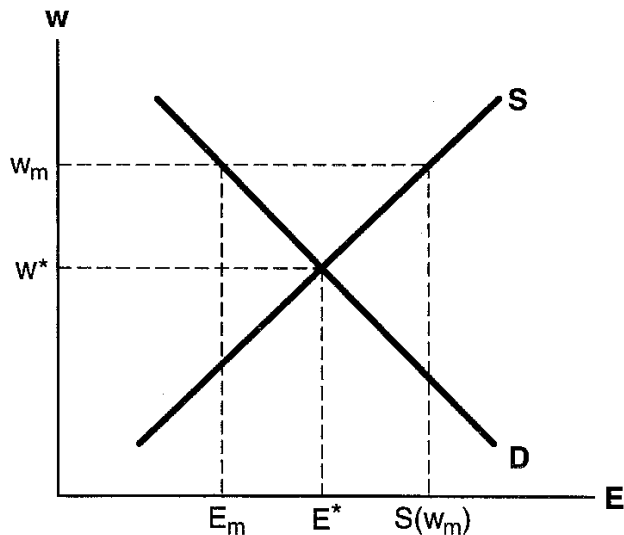


An Old Argument

- 1 Economists' opposition to the minimum wage is co-terminus with the development of modern “neo-classical” economists.
- 2 Alfred Marshall (1890) (and the Residuum).
- 3 Left to its own, “markets work” and best deploys all resources (including labor) to maximum output consistent with technology, etc.
- 4 Given this situation, minimum wages can't increase output, it can only lower or redistribute output.
- 5 Evidence? Theoretical Model



The Totem



Data is Introduced

- 1 “Social Revisionist” – Clark, Dunlop, Lester, Reynolds, Slichter etc. Took empirical approach:
 - 1 Interviewed businesses, wage surveys.
 - 2 Generally equivocal. Problem with economist theory: Workers of identical skill, etc. (contrary to “theory”) were paid different amounts that depended on “non–economic” factors.”
 - 3 Minimum wage could have no effect, positive effect, or negative effect – depended on context.
- 2 Evidence was soon ignored by economists.



Data is Introduced

- 1 Time series analyses. Use a simple model to predict path of employment, etc. in absence of the observed minimum wage increase. That “predicted” change is compared to what happened.
 - 1 In *some* markets (teenagers), a 10% increase in minimum wage lead to 1 to 3% decline in employment. Problem?
 - 2 Very weak research design. Model predicting employment in absence of minimum wage increase explains little. The estimates are not robust to rather minor changes.
 - 3 Same type of evidence today leads to even smaller estimates of the effect.



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The Card Krueger Studies

- 1 “Natural Experiment” approach.
 - 1 Pre-specified research design.
 - 2 Transparent research design. What constitutes evidence for or against a model is obvious.
- 2 Compare before and after a minimum wage increase in two similar places.
 - 1 Famous Case Study. New Jersey vs. Pennsylvania
 - 2 High wage areas in NJ to Low wage areas.
- 3 Cities in CA to comparable non CA cities
- 4 High wage states to low wage states after Federal Increase.

Conclusion: Minimum wage increases associated with small positive increases in minimum. Very small negatives values or slightly larger positive values could not be ruled out.



Reaction?

- 1 Interest in natural experiments in other areas of economics increased among young economists.
- 2 A lot of “controversy”
 - 1 Data not good enough.
 - 2 Other factors **must** have played a role since we **know** it couldn't have happened
- 3 Criticism of alternative models of labor market proposed by Card and Krueger and development of models to explain results.
- 4 Problem with criticism? Failure to come up with pre-specified research designs as good or better that demonstrate the employment effects.
- 5 In my view, a fair amount of skepticism is warranted about the “conventional story.”

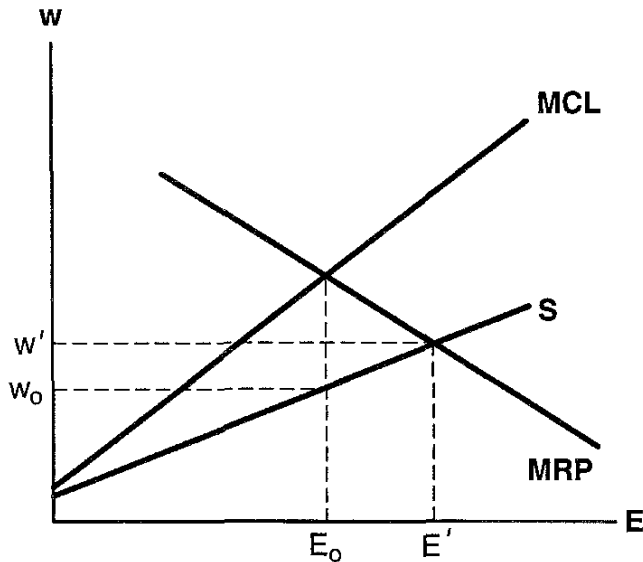


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The Only Other Game in Town?



Monopsony is **One** Alternative

- 1 Simple neoclassical model assumes that hiring is essentially instantaneous: If the firm lowers the wage by a single "cent", what fraction of the workers are there tomorrow.
- 2 Interesting work suggests the possibility that in some cases a higher minimum wage could lower turnover rates (if not set "too high.")
 - ▶ Basic intuition. Firm is in a "low wage/high turnover" equilibrium. Output "too low."
 - ▶ Hiring new workers would be socially ideal, but requires raising the wage to attract new workers.
 - ▶ Firms don't do this because attracting new workers would require them to pay current workers more.
- 3 Surprising implication of monopsony prices could go down if employment increases after a minimum wage.
- 4 Evidence for this not particularly strong, however.

Another possibility is that none of the models are particularly helpful



The Biggest Experiment

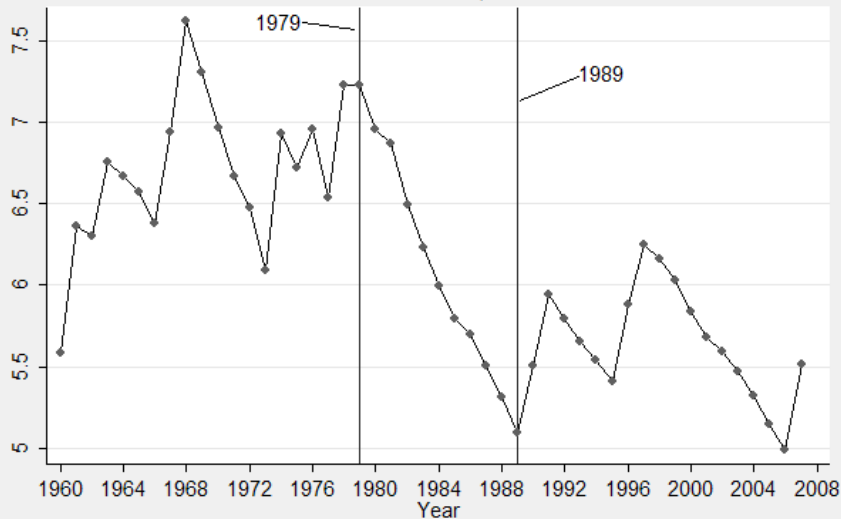
- 1979 Paul Volker and huge increase in interest rates.
- Minimum Wage reaches its effectively highest point. \$2.90 per hour.
- 1980 Minimum Wage Commission conclude 10% increase in minimum wage results in a 1 to 3% decrease in employment among *teenagers*
- 1980 Reagan.
- No large change in minimum wage for 10 years.



The Biggest Experiment

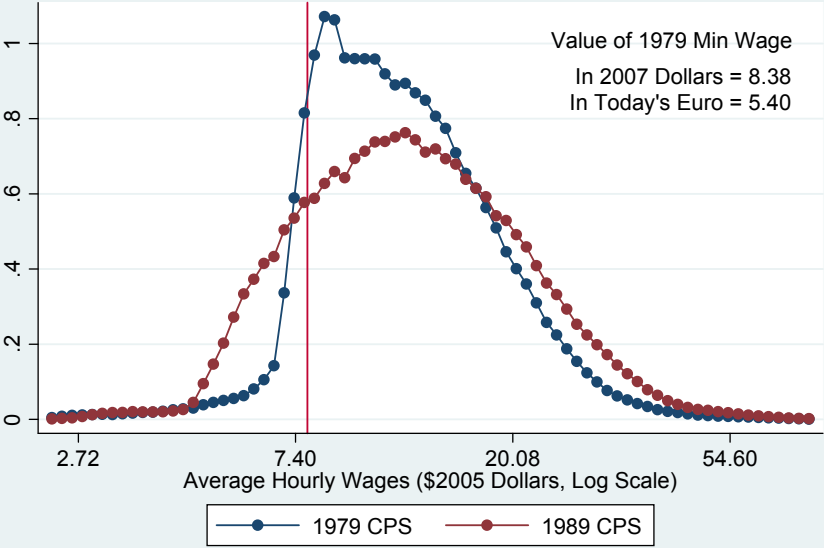
Real Value of the Minimum Wage

2005 US \$



But it Does Matter – For Some

Women, 1979 and 1989



Clear evidence that it Matters

In 1979, more women were paid at the minimum or 10 cents higher than the minimum than any other value of the wage.
Subsequent changes tended to be smaller



Today?

- 1 States are much more active in implementing their own minimum wage laws. In May of 1997, 32 states had state minimum wage laws higher than the Federal.
- 2 Four *cities* have implemented minimum wage laws – Albuquerque, San Francisco, Santa Fe and Washington, D.C.
- 3 Dube, Lester, Reich (2007) exploit comparisons of labor markets that are near state borders with different minimum laws. They find no employment effects (but big wage impacts). Likewise with San Francisco. Small increases in prices at fast food restaurants.



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Key Questions

- 1 How high to set minimum?
- 2 How relevant is US experience to other labor markets?
 - 1 Unusually weak unions.
 - 2 Very decentralized wage setting.
 - 3 Relatively mobile workforce.
 - 4 Fairly low minimum wage.
- 3 Does mandating a higher minimum wage have other affects?
- 4 More aggressive alternatives? “Living Wages” – mandates requiring minimum wages to be consistent with a level of ”survival”.

