THE WALL STREET JOURNAL

Minimum Wage vs. Supply and Demand

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What's News—

Congress will soon vote on whether to increase the minimum wage to $5.15 an hour from $4.25 an hour. As usual, the economic arguments for and against a raise in the minimum wage have been obscured by rhetoric. While some economists have become caught up in the rhetorical excess preceding the vote, this does not obscure the real economic effects of raising the minimum wage. We asked a group of prestigious economists what those effects were, and whether there is still a general consensus among economists on this issue.

William Poole, professor of economics at Brown University

Almost all economists supporting a higher minimum wage, including the president's chief economic adviser, believe that a higher minimum wage will reduce employment. The employment cost may be small, but that is because the wage effect is also small for a small increase in the minimum wage. Minimum wage advocates believe that the employment cost is worth the small wage increase received by those who remain employed.

I do not understand this callous position. The current minimum wage proposal, if enacted, will cost about 400,000 jobs. Those who will lose their jobs are the weakest and most vulnerable members of the labor force. I have a question for those who lose their jobs: Are you quite happy to sacrifice your job and hope for a better future so middle-class teenagers can enjoy a higher wage? If not, blame the president and Congress, not your employer.

Milton Friedman, senior research fellow at the Hoover Institution

Raising by law the price of any commodity or service will reduce the quantity that purchasers of that commodity or service wish to purchase, whether the item in question is gasoline or wheat or milk or labor. The only issue is by how much.

A higher minimum wage would therefore mean that fewer people would be employed. Fewer people would produce less than more people, so that the basic cost of a higher minimum wage would be smaller total output. Some people would benefit -- those current minimum wage workers who are retained at the higher minimum wage. Some people would lose -- those current minimum wage workers who become unemployed. It is difficult for me to see how this kind of redistribution of income among low income workers compensates for the loss in total output.

Finis Welch, professor of economics at Texas A&M University

When wages or other prices are artificially increased, less will be bought. This well-trod soil, the economists' law of demand, is as true today as when Adam Smith first described it more than two centuries ago. Wishing it were not so, or regretting that some have earning capabilities far below others, will not change the basics of human behavior. As employers or consumers we try to get the most for our money. An arbitrary minimum wage increases the cost of hiring those who would otherwise earn less, but it does nothing to make them more productive.

In recent years there have been a handful of ad hoc examples or studies reporting cases where the minimum wage has increased and employment apparently did not fall. Foremost among these is the New Jersey/Pennsylvania comparison by Princeton Professors David Card and Alan Krueger. But re-examination of their data has raised so many questions that the study is generally dismissed by professional economists. Their finding, and that of a handful of other examples, should not surprise. Many things affect employment, and the minimum wage is only one. If we can disprove the law of demand by presenting seemingly anomalous examples, we can also prove that smoking does not cause cancer by pointing to a few old people who smoke.

The proof is not in the isolated example. Rather it is in the preponderance of the data, and there the picture is clear. On April 1, 1990, the federal minimum hourly wage was increased from $3.25 to $3.80. One year later it was increased to $4.25. Over the course of these two increases national average employment of low wage labor fell relative to other employment; teenage employment fell relative to adult employment; employment of high school dropouts fell relative to employment of those with more education; employment of blacks fell relative to that of whites and employment of Hispanics fell relative to that of non-Hispanics. If the minimum is again increased, we can expect a repeat performance. Increasing the minimum will make some jobs more attractive -- it will also make them harder to get.

David F. Bradford, professor of economics and public affairs at Princeton University

Apart from the details of enforcement, the minimum wage law can be described as saying to the potential worker: "Unless you can find a job paying at least the minimum wage, you may not accept employment." When it is put this way, it is hard to understand why anyone would think such a law a good idea, and it is hard to imagine that it could be to the advantage of many workers. I do not think that many economists regard the minimum wage as more than a political palliative. About the best one can say is that if it isn't too high it won't do too much harm.

David Neumark, professor of economics at Michigan State University

Minimum wages do reduce the employment of the most affected workers, such as teenagers and young adults. While the overall effects appear to be quite small, the disemployment for the lowest-wage workers is quite substantial.

There is still a general consensus about this among economists. This consensus may have weakened slightly, but most economists are quite skeptical of the research claiming that minimum wages either raise employment or do not reduce employment.

Robert Eisner, professor emeritus of Northwestern University

With perfect competition, the higher the price the lower the quantity demanded. Thus, forcing wages higher must certainly reduce employment. Some economists may consider that argument relevant yet support raising the minimum wage because the increases in incomes for those still employed will outweigh the employment losses. And low wage employers, facing modest increases in costs similar to those of their competitors, will be able to pass them on in slightly higher prices.

But economists have learned that labor markets are far from perfect. Low wage workers may not be able to find the employers that will pay them what they are worth. And employers may refuse to offer the higher wage necessary to attract needed new workers if that higher wage necessitates the added expense of higher wages for current employees. If existing employee wages were already higher because of a higher minimum wage, the additional workers could and would be recruited without that extra cost. Thus, most economists may now accept recent studies that found that raising minimum wages caused little or no reduction in employment, and in some cases apparently increased it. They may see that the very modest minimum wage boost currently proposed would clearly raise incomes of low wage workers and that neither modern economic theory nor the facts indicate that it would cost them their jobs.

Martin Feldstein, professor of economics at Harvard University

An increase in the minimum wage would undoubtedly reduce employment and total working hours. The decline in employment would be concentrated among the least skilled and least educated. Minority youth would be the most seriously affected group in the population.

Although economists may differ in their estimates of the magnitude of the employment declines that would result from a rise in the minimum wage, I believe that there is an overwhelming consensus that the higher minimum wage would reduce employment and that those who are displaced will be the low-skilled youth who now have the hardest time in getting work. The experience of Europe, where the unemployment rate has now reached twice that of the United States, shows the danger of traveling along the road to higher minimum wages.

Brad Schiller, professor of economics at American University

President Clinton and his secretary of labor would have us believe that low wage workers are "trapped" in minimum-wage jobs forever, and are therefore unable to support their families. The real issue, then, is not who is holding a minimum wage job on any given day, but how long workers stay at minimum wage jobs.

A multiyear Labor Department-funded survey (The National Longitudinal Surveys of Youth) reveals that few workers stay at minimum wage jobs very long. After one year, six out of 10 minimum wage entrants no longer work at any minimum wage job (including secondary jobs). Only 1.5 out of 10 minimum wage entrants has any minimum wage job after three years of labor-force activity. If workers don't stay long at a McDonald's outlet, the wages paid in such outlets don't gauge living standards very well.

The evident upward mobility of low wage workers shifts the focus of the minimum wage debate from arguments over the effects of a higher minimum (e.g. the extent of job losses) to its intended purpose. If the motivation behind a minimum-wage increase is to raise living standards, upward mobility renders that policy less effective and less necessary. Any job losses on the first rung of the income ladder cause larger income losses over time. The extent of job losses on that first rung are distorted by coverage gaps in the Fair Labor Standards Act -- most entry-level jobs for teens are exempt. That's why economic studies of employment generate such conflicting results, not because there's been any change in economic theory.

William A. Niskanen, chairman of the Cato Institute

The minimum wage helps some low skilled workers at the expense of those who are even less skilled. Most of those who benefit are secondary workers from families that are not poor. Many of those who lose the opportunity for legal employment are from poor families.

On these issues, there is still a substantial consensus among economists. A large body of empirical studies suggests that the proposed increase in the minimum wage by 90 cents over two years, as currently proposed, would reduce legal employment for low skilled workers by about 4%. Those who are most concerned about the employment opportunities of low skilled workers from poor families should oppose the minimum wage but support the earned income tax credit.

Arthur Laffer, chairman of Laffer Canto & Associates, financial consultants in San Diego

A minimum wage guarantees that there are more people willing to work than there are employers willing to hire. A rise in that minimum wage pushes more people out of work and allows those left with jobs to be paid more. The workers who lose their jobs are clearly worse off, even if they get welfare. The taxpayers who pay the welfare are clearly worse off as well. The workers who keep their jobs at the higher minimum pay are clearly better off by the exact amount by which the employers who are paying those workers more are worse off. On balance the whole idea of raising the minimum wage looks like a loser to me.

Robert Barro, professor of economics at Harvard University

The minimum wage prohibits people from working if their productivity falls short of the stated level. The overall consequences for economic efficiency are adverse and show up especially as reduced levels of employment for low productivity workers. Some workers gain from an increased minimum, notably the more able, who can retain and find the higher wage jobs. However, the overall consequences for income distribution are adverse because the increased joblessness tends to be concentrated among the least advantaged persons, notably minority teenagers. If the ratio of the minimum wage to the average wage is small -- as currently in the U.S. -- then a rise in the minimum has small effects on aggregate employment and overall income distribution, but there is no reason to think that the net effects are positive. Thus, the previously strong consensus of economists in opposition to the minimum wage remains correct, and the minimum-wage law ought to be abolished.

James Buchanan,
"A commentary on the minimum wage", April 25, 1996
"The inverse relationship between quantity demanded and price is the core proposition in economic science, which embodies the presupposition that human choice behavior is sufficiently rational to allow predictions to be made. Just as no physicist would claim that "water runs uphill," no self-respecting economist would claim that increases in the minimum wage increase employment. 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."

Merton Miller, April 25, 1996
"It sure plays well in the opinion polls. I tremble for my profession."