Proposed Minimum Wage Legislation in Louisville

Summary of (vast) Economics Literature: Theory, Facts, Policy

by

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1. Requiring a wage rate that is higher than the market rate has the following effects:
   - Employers demand less labor
   - Households supply more labor
   - Unemployment goes up because fewer people are hired and more people want to work at the higher wage (regulation-induced labor surplus).
2. Lower wage workers that add more value than the minimum wage get a raise.
3. Businesses hiring low wage workers will try to raise prices (inflation), but higher consumer prices offset some of the wage gains to workers. As the price of domestic goods and services rise, imports become more price-competitive and low-wage jobs go out of the country. Where industry is very price-competitive, businesses will substitute capital for labor (e.g., self-service economy), and lead to more unemployment.
4. To remain price-competitive, businesses will also seek to offset the required higher wages by reducing employee benefits (health insurance, retirement contributions, free meals, clothing, training).

So, supporting a minimum wage means you favor paying above market wages to the low-skilled workers who keep their jobs. But it also means you favor higher unemployment, fewer jobs opportunities for young entry level workers, higher prices, more automation and self-service retail, shifting lower-skilled jobs to other countries, and providing fewer fringe benefits to US workers.

5. US Bureau of Labor Statistics data show that (a) half of minimum wage workers are aged 16 to 24, (b) are more likely to be never-married, (c) working part-time, and (d) to be employed in restaurants and bars (where tips supplement wages). See www.bls.gov/cps/minwage2013.pdf
6. The Congressional Budget Office issued a comprehensive analysis of the impact of the proposed $10.10 federal minimum wage. They estimate that the minimum wage would cause about sixteen million workers to receive a raise, but that it would increase unemployment by a half million people. However, higher prices mitigate the number of families who are lifted above the poverty line by the higher wages, resulting in but a two percent decrease in poverty so measured. Moreover, they point out that only 20 percent of low wage workers would be in families with income below the federal poverty line, while 35

percent of low wage workers would be in families with income of at least three times the 2016 federal poverty threshold ($24,100 for a family of four). See www.cbo.gov/sites/default/files/cbofiles/attachments/44995-MinimumWage.pdf

7. A 2007 study by University of Kentucky Professors Ken Troske and Aaron Yelowitz found similar results for Kentucky as those of the recent CBO study. Moreover, they point out much of the poverty associated with families of low-wage workers has to do with working so few hours per year. Specifically, on average, workers in poor families are out of the workforce for more than four months of the year. See http://cber.uky.edu/Downloads/Troske&Yelowitz07.pdf

8. Both the CBO and UK studies suggest that raising the minimum wage is a very ineffective way to reduce poverty, since so many low-wage workers are young and living in families that are not poor. They recommend using the Earned Income Tax Credit as a way of getting more resources to poor families who have workers. The EITC uses the tax code to provide a wage subsidy to workers in low-income households. The following quote from the CBO study, endorsed by Professor Troske, is as follows:

    To achieve any given increase in the resources of lower-income families would require a greater shift of resources in the economy if done by increasing the minimum wage than if done by increasing the EITC. The reason is that a minimum-wage increase would add to the resources of most families of low-wage workers regardless of those families' income; for example, one third of low-wage workers would be in families whose income was more than three times the federal poverty threshold in 2016, and many of those workers would see their earnings rise if the minimum wage rose. By contrast, an increase in the EITC would go almost entirely to lower-income families.

9. There is a federal EITC, but Kentucky does not supplement this with a state-level version. Twenty-three states have an EITC, including neighbors Indiana and Ohio. Of course, southern neighbor Tennessee does not tax wages and salaries in the first place. For an analysis of a KY EITC, see UK Professor Jim Ziliak's report: www.ukcpr.org/Publications/PolicyInsights-No2.pdf

10. Finally, at the local level, it should be pointed out that many businesses in Jefferson County Kentucky could easily relocate to adjacent counties in Kentucky and Indiana, where there is no minimum wage requirement. This implies that a county-level minimum wage would have more of a negative impact on local employment than a national minimum wage.

So, rather than a minimum wage in Louisville, it makes more economic sense to support a Kentucky EITC, where families earning low wages see their state income tax liability fall, thus providing them more disposable income.