



TESTIMONY

June 16, 2015

ON INCREASING THE MINIMUM WAGE IN SAINT LOUIS

By Michael Rathbone

Testimony Before the Saint Louis Board of Aldermen

To the Honorable Members of the Committee,

Thank you for the opportunity to testify. My name is Michael Rathbone, and I am a policy researcher at the Show-Me Institute, a nonprofit, nonpartisan Missouri-based think tank that advances sensible, well-researched, free-market solutions to state and local policy issues. The ideas presented here are my own. This testimony is intended to summarize research regarding minimum wage increases and in particular the potential effects of Board Bill Number 83.

Minimum wage laws are popular. In 2014, four states (Alaska, Nebraska, South Dakota, and Arkansas) voted to increase their states' minimum wage by large margins.¹ People in favor of raising the minimum wage argue that it will help poor and low-income families. For example, the late

Sen. Edward Kennedy argued, "The minimum wage was one of the first—and is still one of the best—anti-poverty programs we have."² Board Bill Number 83 states that "low-wage workers in the St. Louis region struggle to meet their most basic needs and to provide their children a stable foundation, a safe dwelling, and an opportunity to obtain a high-quality education."³ It also states that "minimum wage laws promote the general welfare, health, and prosperity of the City of St. Louis by ensuring that workers can better support and care for their families and fully participate in the community."⁴

Most people, me included, want higher wages for everybody. However, mandating a higher minimum wage as a way to improve the economic conditions of poor families is suspect.

ADVANCING LIBERTY WITH RESPONSIBILITY
BY PROMOTING MARKET SOLUTIONS
FOR MISSOURI PUBLIC POLICY

Outline of the Proposal

Board Bill Number 83 contains the following provisions:⁵

- Once enacted, the minimum wage will be increased to ten dollars (\$10) an hour.
- Beginning Jan. 1, 2017: The minimum wage shall increase in increments of one dollar and twenty-five cents (\$1.25) per year for four years. By Jan. 1, 2020, the minimum wage will be fifteen dollars (\$15) an hour.
- Beginning Jan. 1, 2021, and each successive year thereafter: The minimum wage shall be increased or decreased annually on a percentage basis to reflect the rate of inflation. The rate shall not be less than fifteen dollars (\$15) an hour.
- If at any time the state or federal minimum wage is higher than that established by Board Bill 83, then the greater rate shall be the minimum wage rate for the city of Saint Louis.
- Employees who earn more than thirty dollars (\$30) per month in tips shall be paid a base wage not less than fifty percent (50%) of the minimum wage specified in this ordinance.
- Tips are to be counted as part of employees' wages. If tips along with the base wage do not equal the minimum wage, the employer shall pay the employee the difference.
- Employers that have gross

volume of sales that is less than five hundred thousand (\$500,000) a year and/or employs fifteen (15) or fewer employees shall not be counted as "Employers" for the purposes of this ordinance and thus not be required to pay this new minimum wage.

Economic Effects of Raising the Minimum Wage

One of the reasons why raising the minimum wage might not improve the conditions of poor families is that a higher minimum wage could discourage employers from hiring low-skilled workers that proponents of the minimum wage are trying to help. A large body of evidence confirms that minimum wages reduce employment for these workers.⁶ In one analysis of proposed federal minimum wage increases, the Congressional Budget Office (CBO) estimated that increasing the federal minimum wage to \$10.10 an hour would reduce employment by 500,000 jobs.⁷

In simple economic analysis there are two main reasons for this reduction. First, employers will start using relatively less labor due to the increase in labor costs. They instead will substitute other inputs, such as capital, that may have a lower cost because of the increase in wages. In other words, some employers will reduce the number of their employees.⁸ Second, since costs are higher due to higher wages, product prices will probably rise, reducing the demand for each firm's product and leading to a reduction in the scale of

each firm's operation.⁹

This ordinance eventually would raise the minimum wage above the \$10.10 an hour examined in the CBO study.¹⁰ If raising the minimum wage up to \$10.10 an hour is enough to cause significant job losses nationally, raising it to \$15 an hour could have serious negative effects on employment in the area.¹¹ An increased minimum wage, coupled with the presence of an earnings tax, provides an incentive for businesses already in Saint Louis to relocate elsewhere.¹²

Another reason why raising the minimum wage is suspect is that it harms the earnings power of low-skilled workers. Dr. Jeffrey Clemens of the University of California, San Diego and Michael Wither, a graduate student at the University of California, San Diego estimated the minimum wage's impact on employment and income growth for low-skilled workers.¹³ They found that increasing the minimum wage reduced the chances of low-skilled workers eventually reaching salaries of \$1,500 a month.¹⁴ Clemens and Wither believe that this reduction in mobility occurs because an increased minimum wage reduces the number of jobs available for poorer workers. Numerous studies, including the CBO, lend evidence to support that finding.¹⁵

Specifically, the authors state that:

It appears that binding minimum wage increases blunted these workers' prospects for medium-run economic mobility by reducing their short-run access to

opportunities for accumulating experience and developing skills. This period's minimum wage increases may thus have made the first rung on the earnings ladder more difficult for low-skilled workers to reach.¹⁶

This observation makes sense given that minimum wage workers are on the steep portion of the wage-experience profile (i.e., small gains in experience correspond to large increases in wages) and a lack of employment will hold back these workers' wage growth.¹⁷ In fact, according to one study, the average minimum wage worker will experience a 20 percent increase in wages if employed at the same job after a full year.¹⁸ Again, in this instance, increasing the minimum wage actually hurts those people proponents aim to help.

Finally, increasing the minimum wage is not a very effective means of helping low-income families. David Neumark, in his 2012 Policy Study for the Show-Me Institute examining the economic effects of the minimum wage, found that "...there is no basis for concluding that minimum wages reduce the proportion of families living in poverty or near poverty."¹⁹ The reason why the minimum wage is not especially helpful at lifting people out of poverty is because it benefits **low-income workers**, not **low-income families**. According to Neumark's calculations, only 12.7 percent of workers making the minimum wage or less are at or below the poverty line. In fact, nearly half (44.6 percent) of workers making at or less than the minimum wage were in households with

incomes three times the poverty line or higher.²⁰

This is the reason why even proponents of the minimum wage argue that it is a "blunt instrument" for helping low-income families.²¹ Christina Romer, President Obama's former head of the Council of Economic Advisers, agrees that increasing the minimum wage is not a very well-targeted anti-poverty proposal.²²

Summary

Raising the minimum wage sounds like good policy. Mandating raises for low-income workers is appealing to many people (as evidenced by its continued support at the ballot box). However, from an economic perspective, increasing the minimum wage can hurt those whom it is meant to help. At the same time, the increase could have little to no effect at helping poor families. People from across the ideological spectrum believe there are more effective means of helping the working poor than increasing the minimum wage.²³

NOTES

¹ Josh Barro, "Four States Vote to Raise the Minimum Wage," *The Upshot* (November 3, 2014), <http://www.nytimes.com/2014/11/05/upshot/election-results-2014-minimum-wage.html?ref=2014-midterm-elections&abt=0002&cabg=1>.

² Quoted in Andrew Clymer, *Edward M. Kennedy: A Biography* (New York: William Morrow & Co. 1999), 449.

³ Shane Cohn, "Board Bill Number 83," Saint Louis City Board of Alderman, June 5, 2015, <https://www.stlouis-mo.gov/internal-apps/legislative/upload/boardbill/BB83-wd251.pdf>.

⁴ Ibid.

⁵ Ibid.

⁶ David Neumark and William Wascher, "Minimum Wages and Employment," *Foundations and Trends in Microeconomics*, 3, nos. 1-2 (2007): 1-186, http://www.socsci.uci.edu/~dneumark/min_wage_review.pdf.

⁷ Congressional Budget Office, "The Effects of a Minimum-Wage Increase on Employment and Family Income" (Washington, D.C.: Congressional Budget Office Report, February 2014), <http://www.cbo.gov/sites/default/files/cbofiles/attachments/44995-MinimumWage.pdf>.

⁸ In the real world, laborers have different skill levels. Instead of reducing total employment, employers might substitute low-skilled workers for higher-skilled workers in response to a minimum wage increase. This is important, as any measure of effects on overall employment due to a minimum wage increase might be quite small. However, the negative employment effects on low-skilled, low-wage workers the minimum wage is intended to help can be quite large.

⁹ David Neumark, "Should Missouri Raise Its Minimum Wage?" (Policy Study, Show-Me Institute, September 2012), <http://www.showmeinstitute.org/publications/policy-study/red-tape/821-should-missouri-raise-its-minimum-wage.html>.

¹⁰ Cohn, "Board Bill Number 83."

¹¹ The CBO estimate is an analysis of a federal minimum wage increase. The potential negative effects on employment are heightened when considering minimum wage increases in states and municipalities since it is generally easier for a business to move across state or city lines than it is to relocate to another country. For more on state-level differences in the minimum wage and employment see: David Neumark and William Wascher, "The Effect of New Jersey's Minimum Wage Increase on Fast-Food Employment: A Re-Evaluation Using Payroll Records," National Bureau of Economic Research Working Paper No. 5224 (August 1995), <http://www.nber.org/papers/w5224.pdf>.

¹² For more on the negative effects of the earnings tax on city growth see: Howard Wall, "New Evidence of the Effects of City Earnings Taxes on Growth" (Essay, Show-Me Institute, 2013), http://www.showmeinstitute.org/papers/new_evidence_of_the_effects_of_city_earnings_taxes_on_growth.pdf.

showmeinstitute.org/publications/essay/taxes/1035-new-evidence-of-the-effects-of-city-earnings-taxes-on-growth.html, Joseph Haslag, “How an Earnings Tax Harms Cities Like Saint Louis and Kansas City” (Policy Study, Show-Me Institute, 2006), <http://www.showmeinstitute.org/publications/policy-study/taxes/343-how-an-earnings-tax-harms-cities.html>.

¹³ Jeffrey Clemens and Michael Wither, “The Minimum Wage and the Great Recession: Evidence on Effects on the Employment and Income Trajectories of Low-Skilled Workers,” *NBER Working Paper 20724* (November 24, 2014), <http://econweb.ucsd.edu/~mwither/pdfs/Effects%20of%20Min%20Wage%20on%20Wages%20Employment%20and%20Earnings.pdf>.

¹⁴ The authors determined that \$1,500 a month was the threshold for lower-middle-class salaries.

¹⁵ Neumark and Wascher, “Minimum Wages and Employment”; Congressional Budget Office, “The Effects of a Minimum-Wage Increase on Employment and Family Income.”

¹⁶ Clemens and Wither, “The Minimum Wage and the Great Recession.”

¹⁷ Clemens and Wither cite: K.M. Murphy and F. Welch, “Empirical-age Earnings Profiles,” *Journal of Labor Economics* (1990): 202-229, <http://people.terry.uga.edu/mustard/courses/e8420/Murphy-Welch-Age.pdf>. This report also supports the fact that many minimum wage workers are in a position where wage increases are most pronounced. See: US Bureau of Labor Statistics, “Characteristics of Minimum Wage Workers, 2013,” BLS Reports Report 1048 (March 2014), <http://www.bls.gov/cps/minwage2013.pdf>.

¹⁸ R.E. Smith and B. Vavrichek, “The Wage Mobility of Minimum-Wage Workers,” *Industrial and Labor Relations Review*, 82-88, <http://ilr.sagepub.com/content/46/1/82.full.pdf>.

¹⁹ Neumark, “Should Missouri Raise Its Minimum Wage?”

²⁰ Ibid.

²¹ David Card and Alan B. Kruger, *Myth and Measurement: The New Economics of the Minimum Wage* (Princeton, N.J.: Princeton University Press. 1995).

²² Christina D. Romer, “The Business of the Minimum Wage,” *The New York Times* (March 2, 2013), http://www.nytimes.com/2013/03/03/business/the-minimum-wage-employment-and-income-distribution.html?_r=0.

²³ The Neumark policy study (2012), the Clemens and Wither paper, the CBO report, and Romer all agree that increasing the Earned Income Tax Credit (EITC) is a more effective means at helping poor families. Whether doing so is a practical option for this jurisdiction is up for the jurisdiction to determine.



5297 Washington Place | Saint Louis, MO 63108 | 314-454-0647 | www.showmeinstitute.org

Read Our Blog:
showmedaily.org

Use Our Interactive Database:
showmedata.org

View State Government Spending:
showmeliving.org

Find Us on Facebook:
facebook.com/showmeinstitute

Follow Us on Twitter:
twitter.com/showme