The Heritage Foundation
Executive Memorandum

No. 590

April 23, 1999

Raising the Minimum Wage: Rhetoric v. Reality

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President Bill Clinton and some Members of Congress are proposing to raise the minimum wage from \$5.15 to \$6.15 per hour—an increase of nearly 20 percent over the rate established only on September 1, 1997. Such federally mandated increases in the minimum wage appeal to the compassion of Americans and appear affordable during strong economic times. But the reality is that increases in the minimum wage rarely benefit, and indeed often hold back, the very people they are intended to help—unskilled individuals seeking to join the workforce or move up the economic ladder. If federal policy makers want to improve the prosperity of low-income Americans, they should concentrate on policies that lower taxes and promote job growth.

An Unprecedented Increase. Increasing the minimum wage from \$5.15 to \$5.65 on September 1, 1999, and then to \$6.15 per hour on September 1, 2000, as the President proposes, would be unparalleled: It would amount to a 44.7 percent increase in the minimum wage, or \$1.90 per hour, since 1996, when the minimum wage was \$4.25. Congress never has raised the minimum wage by more than \$1.05 per hour over a five-year period. And that \$1.05 hike occurred between 1978 and 1982, when inflation was increasing by an average rate of 9.8 percent per year—far more than the 2.5 percent average rate over the past five years.

Most Poor Would Not Benefit. Economic analysis consistently shows that most of the benefit of mandated higher entry-level wages goes to families who already are *above* the poverty level. In 1997, nearly 60 percent of poor Americans over age 15 did not work and would not be helped by an increase. And the fewer than 10 percent of poor Americans over age 15 who could benefit from increasing the minimum wage to \$6.15 per hour work an average of only 16 hours each week. The neediest families would receive a relatively small proportion of the increased wage bill. Most of the benefit would go to families that earn more than twice the poverty threshold.

Produced by
The Thomas A. Roe Institute
for Economic Policy Studies

Published by
The Heritage Foundation
214 Massachusetts Ave., N.E.
Washington, D.C.
20002–4999
(202) 546-4400
http://www.heritage.org

Raising the minimum wage harms the working poor in ways that are not obvious from statistics that measure total employment and unemployment. For example, according to a recent survey by the Jerome Levy Economics Institute, raising the minimum wage to \$6.00 per hour would cause more than 20 percent of small business owners to reconsider their overall hiring and employment decisions. A rapidly rising minimum wage drives up the cost of entry-level jobs and encourages employers to hire higher-skilled job applicants. Any cutbacks in employment due to the increased cost of labor would affect disproportionately workers who are not high school graduates and those who work part-time for economic reasons.

Thwarting Welfare Reform. Raising the minimum wage again now also would contradict Congress's efforts to move unskilled Americans from welfare to work. As lower-wage unskilled jobs disappeared, welfare recipients would have a more difficult time in finding work. In recognizing this fact, the President proposed, and Congress passed in 1997, two tax credits for employers—the Welfare-to-Work Tax Credit and the Work Opportunity Tax Credit. Both tax credits effectively reduce the cost of entry-level jobs by 35.4 percent (an implicit recognition that the minimum wage should be about $3.33 per hour). But Americans who lack the skills they need to get a job at $5.15 per hour today probably will not have acquired those skills to get a job at $5.65 per hour in September just because Congress raised the entry-level wage requirement.

Deflating Job Training. Making work pay over the course of a lifetime starts with establishing a stable employment history and building skills through on-the-job training. Recent research by David Neumark and William Wascher, however, reveals that increasing the minimum wage reduces the amount of employer-provided training, especially formal training, that is aimed at improving skills on the current job. At the same time, there is little or no evidence that the minimum wage affects the amount of training Americans undertake to qualify for or obtain new jobs. Consequently, the minimum wage appears overall to reduce significantly the training young workers receive.

Keeping Teenagers Out of the Work. To the extent that there is an unemployment problem in the United States, it primarily affects teenagers and the unskilled. In March 1998, the unemployment rate for adults 25 years of age or older was 3.1 percent, but the teenage unemployment rate was 14.3 percent. Raising the minimum wage would do little to help teenagers or the unskilled.

Studies by David Neumark show a higher minimum wage tends to decrease school enrollment and increase the proportion of idle teenagers—those who are neither in school nor employed. After the 1996 increase in the minimum wage, the school enrollment rate for teenagers aged 16 and 17 declined by 0.4 percentage points, while their idleness rate rose by 0.3 percentage points to 4.1 percent. Although a higher minimum wage would induce some teenagers to drop out of school to work, they would be displaced from the job market as employers responded to a higher minimum wage by looking for workers with better skills.

Over time, well-intentioned child labor laws and regulations and minimum wage increases have destroyed many entry-level positions for unskilled youth, particularly children who are 14 and 15 years old. It is not surprising that almost half the youth in the federal summer jobs program are 14 and 15 years of age. Not only do government regulations strongly discourage private employers from hiring them as entry-level workers, but a higher minimum wage effectively prices them out of the labor market.

Conclusion. Raising the minimum wage would be bad public policy. It would be an ineffective way to reduce poverty and help the working poor. It would make it more difficult for unskilled Americans to move off the welfare rolls into gainful employment. It would tend to decrease school enrollment, increase the proportion of teenagers who are neither in school nor working, and reduce the availability of formal on-the-job training for young workers. A better policy would be for Congress to cut tax rates across the board on work, savings, and investment and provide state and local governments with the flexibility to improve the quality of schools, which would ensure all Americans gained the skills they need to move up the career ladder and achieve economic prosperity.

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