

The minimum wage

The law of demand is a bummer

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THE debate over the minimum wage, which, thanks to Barack Obama's state-of-the-union address, we appear to be having again, is a debate over the question of whether raising the price of something—low-skilled labour, in this case—will reduce demand for that thing. That is to say, it is a debate over the relevance of the law of demand, an enormously robust generalisation about human behaviour confirmed and re-confirmed each day by billions of individual decisions.

Which is not to say that economic "laws" capture strict relations of physical necessity. Economics is not physics. Demand does not have to go down, by dint of creation's quiddity, when price goes up. Economics, like psychology, trucks in propositions that hold other things being equal. Steady or rising demand in the face of rising prices does not flout the law of the conservation of mass, or any such strict basic rule of the universe, but it does call for an explanation of the nature of the exception to the rule. What, exactly, is supposed not to be equal, such that in this case, applying the law of demand will mislead us about the expected effect of raising a price floor?

There are conditions under which raising the minimum wage will increase demand, as well as economic efficiency. According to one story, monopsony conditions for low-wage labour, ie, imperfectly competitive labour-market conditions in which there is but a single buyer of low-wage labour (or a colluding band of buyers) that is able to set wages at a level workers have little choice but to accept. Good old Econ 101 shows that under such conditions, a bump in the minimum wage, within a certain range, can boost employment and enhance efficiency. So there's that. And such conditions no doubt exist in some sectors at some places at some times. One famous, and egregiously misused, study suggests that monopsony-like conditions applied to fast-food restaurants in Pennsylvania and New Jersey in the mid-1990s. But there is basically no reason whatsoever to think that such conditions apply generally, across all sector and regions of the American labour market.

In the absence of special conditions, we have every reason to expect the law of demand to hold, such that raising the minimum wage will make it harder for inexperienced workers—workers whose output is worth less to employers than the mandated wage, and especially teenagers from low-income families looking to get a first footing in the labour market—to find work. And this is, in fact, what empirical studies tend to conclude. A comprehensive 2008 survey of the empirical literature from David Neumark, a professor of economics at the University of California, Irvine, and William Wascher, an economist for the Federal Reserve, found that, as one would expect, "[M]inimum wages reduce employment opportunities for less-skilled workers, especially those who are most directly affected by the minimum wage."

Again, it doesn't have to work this way. Employers can cut hours rather than hiring fewer workers. They can turn down the air-conditioner, strictly police the length of breaks, and otherwise reduce the cost of amenities previously enjoyed by employees. They can shift to off-the-books employees willing to work for less than the legally-mandated minimum. They can raise prices, passing on increased labour costs to consumers. It's conceivable that the only consequence would be that a larger share of profits gets distributed to low-wage workers. Conceivable and exceedingly unlikely. In reality, we probably get small adjustments along each of these dimensions.

Of course, there is some newish empirical research contesting the disemployment effect of increases in the minimum wage, and then there is even newer research debunking it. I'm not about to offer a blow-by-blow of this tedious and technical debate for the same reason I'm not inclined to delve into the "debate" over the reality of global warming. The basic science is sound, and I don't think it is at this juncture especially fruitful to "teach the debate" when deliberating about policy.

I suspect that the reason left-leaning academics and journalists are so ready to tout research shooting holes in the law of demand has more to do with politics than a dogged commitment to truth in economic science. Raising the minimum wage is a very popular policy. It's smart for the Democratic Party to get behind it. So Democratic opinion leaders will be inclined to provide intellectual cover, either by soft-pedaling the downside of the policy, or by selflessly making their minds available to believe whatever most benefits their party. Democratic journalists may find themselves eager to talk about the fascinating new research that contests the conventional wisdom about the effects of raising the minimum wage. None of this is especially surprising or scandalous, and it's naive to think public intellectual life in a closely-divided democracy will ever be much different. Still, it's a tonic to square up now and again to the way things work, and it's worth taking note when Democrats, who are in my opinion generally less prone than Republicans to baldly wishful and/or strategic cognition, behave like thoroughly political animals.

Perhaps it's wishful on my part to think, as I do, that most economically literate observers really do understand that raising the minimum wage will screw up the prospects of a fair number of poor young workers. Those who favour raising the minimum wage anyway just think that, all things considered, that's a price we ought to be willing to pay. But they can't say that, just as second-amendment enthusiasts can't say that an occasional grim harvest of kindergartners is a price we ought to be willing to pay for the freedom to own guns. One of the most maddening things about political debate is that it's rhetorical suicide to accept tragic trade-offs. So one must deny that there are trade-offs. It's got to be all benefit, no cost. And that's why we find so few willing to step forward and say, yes, "minimum wages pose a tradeoff of higher wages for some against job losses for others", but let's raise the minimum wage anyway, because, in the final analysis, the benefit to those who enjoy higher wages will be greater than the cost suffered by those put out of work, and this distribution of burdens and benefits is not too unfair to stomach.

I dearly wish somebody would say this, because then we could go on to have a useful, meaty debate about the mix of policies most likely to succeed in helping low-wage workers. My sense is that we'd do best with no minimum wage, wage subsidies, and transfers to low-income households that phase out in a way that does not tax small increases in income at absurdly punitive rates. As it is, we're left wasting our time debating the minutiae of conditions under which we can expect stones to float.