

Raising the Minimum Wage Is No Free Lunch

By [ANTHONY DAVIES](#), [JAMES R. HARRIGAN](#)

October 21, 2013

We are rarely subjected to debate over the minimum wage apart from election season, but America's painfully sluggish return to economic normalcy has politicians scrambling to do something to help the working class. While the minimum wage debate usually plays out at the federal level, there is now a grassroots push across the country to raise wages beyond the federally mandated \$7.25 per hour. Unfortunately, success won't guarantee a happy ending for workers.

Washington state voters are considering Proposition 1, which would raise the minimum wage to \$15 per hour for workers in and around SeaTac airport. In Minneapolis there is talk of raising the minimum wage to \$9.50, and in Washington, D.C. to \$11.50. New Jersey's minimum wage is likely to rise to \$8.25. Ohio's will increase to \$7.95 in January.



It comes as no surprise that politicians love talking about and raising the minimum wage. Few are ever shown the door for being perceived as a friend of the working class. But perception and reality are rarely the same thing in the political world.

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According to the Bureau of Labor Statistics, fewer than 3 percent of U.S. workers earn the minimum wage. Those who do tend to be entry-level workers – people with little work history, less education and fewer skills than those who earn more. About one-third of minimum wage earners also earn tips, which, in many cases, actually puts them significantly above the minimum wage in reality, if not officially. In the end, the minimum wage affects very few workers.

So why should we care? For precisely the same reason that politicians do: because minimum wage workers are often the most disadvantaged among us. They cannot compete with the rest of the labor market in terms of skills, education or experience, and as a result they make less money.

For some of these people, an increase in the minimum wage is clearly a good thing – but not for everyone. This is the point that many politicians never fully grasp. Raising the minimum wage does not increase the value of the worker's labor. It increases the cost of the worker's labor. And as everyone knows, the more something costs, the less of it we buy. This is as true of workers in the labor market as it is of anything else.

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The money for an increased minimum wage has got to come from somewhere, and there are only three places from which it can come: investors, in the form of lower profits; customers, in the form of higher prices; or workers, in the form of fewer jobs. Which group pays for the minimum wage hike depends on how competitive the marketplace is.

If competition for investment funds is intense, as is often the case, businesses will resist cutting investors' profits. If competition for customers is fierce, as is nearly always the case, businesses will do almost anything not to raise prices. This leaves only the workers. There are always exceptions, but historically, firms have financed increases in the minimum wage by laying off minimum wage workers.

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The minimum wage question is not one of employers versus employees, as it is so often presented. Rather, it is a question of more-skilled low wage

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workers versus less-skilled low wage workers.

Not surprisingly, better-educated workers with better skills get the increase at the expense of their less-educated, less-skilled counterparts.

In a bizarre twist, raising the minimum wage hurts the very people it aims to help. As detailed in a forthcoming paper to be published by the Mercatus Center, national employment data from 1975 through 2012 show that on average, a 10 percent increase in the minimum wage has been followed by no change in employment among college-educated workers, a half-percentage point increase in unemployment for those with high school diplomas, and a one percentage point increase in unemployment for those without high school diplomas. Young people who have yet to finish high school are hit hardest of all. They have to contend with a two percentage point increase in unemployment, and as a result many are unable to find summer employment – employment that would help them acquire the skills to find better work in the future.

This is what happens when economics takes a back seat to political considerations. The feel-good rhetoric of increasing the minimum wage outweighs the economic reality that there is no such thing as a free lunch. Every cost must be paid by someone, and those who will pay for a minimum wage hike are the very people we are trying to help.

Antony Davies is associate professor of economics at Duquesne University and an affiliated senior scholar with the [Mercatus Center](#) at George Mason University. James R. Harrigan is a fellow of the Institute of Political Economy at Utah State University.

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