Two new studies diverge on the impact of a higher minimum wage

In Los Angeles County, minimum wage will rise to $15 by 2021, and will become statewide in 2022. Here's how it could affect apparel companies in Los Angeles. (Jan. 3, 2017)

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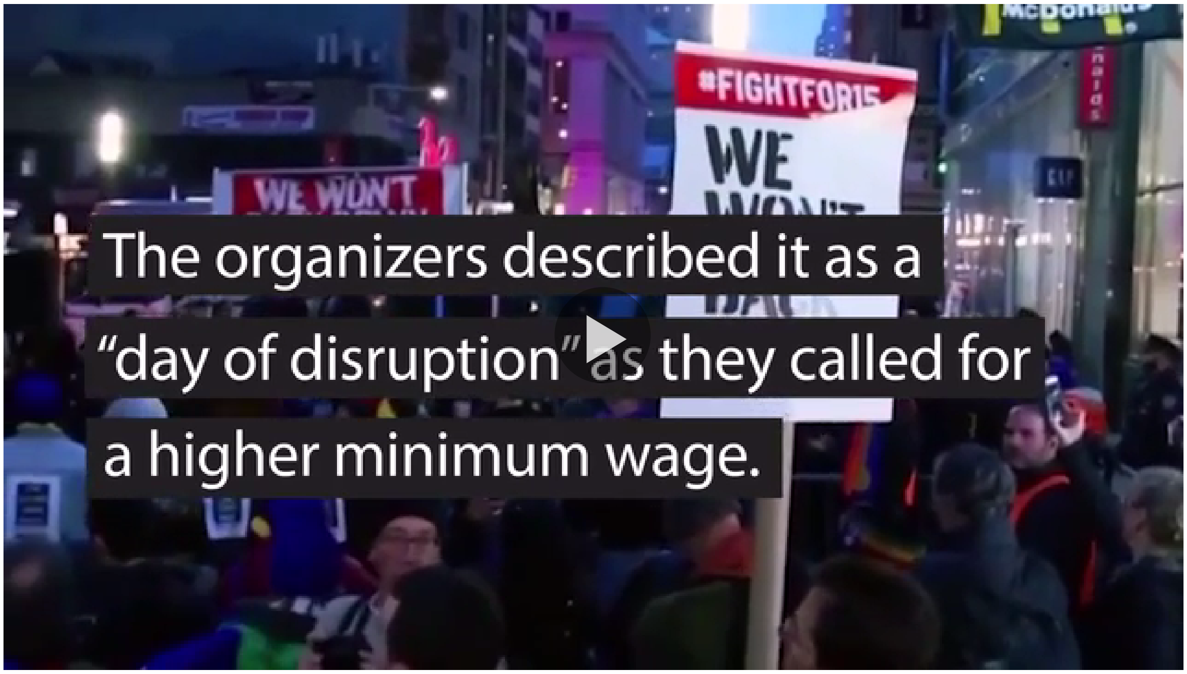
The federal government set its first minimum wage, at 25 cents an hour, in 1938. Since then, liberals have cheered attempts to raise the minimum as blows against worker exploitation, while businesses lament that the hikes will kill jobs.

But nearly 80 years later, economists still aren't sure how a higher minimum wage actually affects companies and their customers.



Two recent studies out of California and Washington, which are both well on their way to a $15 floor, show just how hard it is to pin down exactly how businesses respond to higher labor costs.

One report, published Wednesday by UC Berkeley researchers, suggests that California will actually gain jobs because of the minimum wage hike. Another, released by University of Washington economists in November, offers a more negative view.

Ripple effects from the minimum wage are sure to draw even more scrutiny now. Nineteen states, including California, raised the wage floor on Jan. 1. And Andrew Puzder, President-elect Donald Trump’s pick for Labor secretary who has criticized a $15 wage, is scheduled to have a confirmation hearing Jan. 17, though that may be pushed back to February.

Of course, even the most careful accounting of the pros and cons of a wage hike hinges on methodology and assumptions about the extent to which labor costs can sway companies to raise prices, slash hours and lay off employees.

The new Berkeley report is based on an economic model that predicts how much businesses will raise prices or replace humans with machines, and the likelihood that poor workers will spend all of their new paychecks.

Using that model, researchers found that giving low-wage workers a pay bump will prompt them to spend more. And while retailers and restaurants may raise prices to cover their higher labor costs, that will be offset by the increased spending. The researchers, led by economist Michael Reich, say that extra spending will support enough jobs to compensate for cuts by employers who decide to replace humans with robots.

Employers will also save some of the money they spend on replenishing the bottom rung, the researchers theorize, because higher wages tend to keep workers in their jobs longer. Bigger salaries also make people more productive, which can boost sales and revenue.

Puzder has said that it doesn't make sense to raise the minimum wage in areas that are less economically vibrant than, say, San Francisco. But the Berkeley economists looked specifically at Fresno, one of the poorest counties in California, and they still predict that a wage hike would add jobs on net.

Much of the economic activity in Fresno happens on farms, where machines have been making their presence known for years, so the local labor force might seem like an easy target for automation. Not so, the report finds.

"Raising wages by itself is unlikely to raise the rate of mechanization," Reich said. The researchers base some of their optimism about Fresno handling a $15 wage on its ability to keep growing even as the minimum wage went from $8 in 2013 to $10 today.

Of course, Berkeley's conclusion is essentially a best guess of what will happen, not an account of what has happened. Other independent economists have expressed skepticism about the model, which is similar to the one Berkeley researchers used to study the effects of the minimum wage in Los Angeles and Santa Clara.

"They make assumptions very favorable to the view that minimum wages aren't going to have much of an adverse impact," says David Neumark, an economist at UC Irvine. "They point to a set of studies that are at one extreme of what people find."

Plus, Neumark says, the sharp rise to $15 is relatively unprecedented in American history, so it might not make sense to use the past as a guide. The fact that Fresno's companies could withstand a rise from $8 to $10, for example, may not be a sign that they'll be as resilient when $15 kicks in.

Reich said that he could not analyze what would happen to workers' hours, because the state didn't provide hourly data.

"I was very careful to make the inputs into the model objectively, based on the best research out there," Reich said. Forecasts are, for now, the only way to understand how businesses will respond to a $15 wage.

"If we were adding a zero and looking at a $150 minimum wage, there would be a negative effect. But between $10 to $150, we don't know when that negative effect will kick in," he said.

The report released in November by researchers at the University of Washington looks at how businesses actually responded when Seattle upped its wage from $9.47 per hour in 2014 to $11 per hour in April 2015, compared with what happened in a group of areas that are economically similar to Seattle but which didn't raise the minimum wage.

Workers who already had minimum wage jobs did not become unemployed because of the wage hike, the researchers found. Those employees also didn't lose hours, and ended up earning about $10 more per week during the summer, when the city's economy is at its busiest.

That finding differs from an earlier version of the study, which was widely publicized when released in July and found that the minimum wage increase did lead businesses to fire existing low-wage workers and reduce hours.

Jacob Vigdor, who led the study, says the November report suggests that the July results were not statistically significant.

"For experienced workers, for people already in the labor market, things don't look so bad," Vigdor said. "They look a little bit better than the picture painted in the July report."

For job seekers in Seattle, the news was less positive. By December 2015, Seattle had a couple of thousand fewer new low-wage jobs than it should have based on its past and what occurred in surrounding areas.

"It's becoming a harder place to get a start in the labor market," Vigdor said.

All of the new jobs created in Seattle on net since 2014 are positions that pay more than $25 per hour, the study showed. Vigdor said it's also possible that low-wage jobs are disappearing faster in Seattle because the city has become too expensive for poor workers to live, even with their new raises.

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