MINIMUM WAGES STRANGLE THE ECONOMY
(A RESPONSE)

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Imagine you're an entrepreneur. As a businessperson, would you open a MacDonald's where you were forced to pay workers $100 an hour, a rate which is well beyond what you could earn from them? No, you wouldn't open a new enterprise if you were guaranteed a loss. Therefore, the only businesses that will thrive under such conditions are those which are sure to recover the cost of labour plus the cost of capital, and also compensate themselves for the enormous market risk of opening a business in the first place. This argument, which makes eminent sense with a $100 per hour wage rate, can be repeated incrementally down the ladder.

A handful of commentators have put forth a 1995 study, *Myth and Measurement: The New Economics of the Minimum Wage*, by American economists David Card (Berkeley) and Alan Krueger (Princeton) to substantiate their claims in support of minimum wages. Unfortunately, this study fails on the most basic point. It propagates the misconception that, because total employment continued to grow in a majority of the fast-food outlets surveyed each time the minimum wage was raised, those who claim the minimum wage causes job loss must be wrong. But the study is faulty, because it doesn't recognise that predictions of positive economics involve the influence of one variable on another, holding *all* other variables constant. Another problem with the study is that it focuses on a small niche of the world – two American states – and doesn't take into account global trends.

Truth be told, employment growth is affected by a number of factors besides the minimum wage. There have been attempts to debunk the tried and true fact that imposing a minimum wage which isn't a token amount, stunts an economy's overall growth. Zach Alexopoulos, a Sydney University economics graduate, writes that there is a point of equilibrium in his essay on the topic: "Of course, there is a point where a high enough minimum wage would indeed cost more jobs than it created, but the evidence of Card and Krueger shows that we're not as that point yet."

What he, and others, neglect to understand is that there's no known theoretically established rate which can be rationally fixed as a minimum wage. In other words, there's no person in the world who has a Ph.D. in market interference, and who knows exactly when and where to interfere with the market.

The minimum wage law could indeed cause job loss in the sense that, in its absence, employment would have grown to an even greater extent. Thus, job loss occurs if, holding other factors constant, there are fewer jobs created than there might otherwise have been.

Labour economists have devoted much effort to empirically estimating the magnitudes of the effects of minimum wage legislation on the employment levels of various age, race and gender groups. It is now widely agreed that increases in minimum wages do reduce employment opportunities, especially among teenagers. This was never more evident than in 1980 in Zimbabwe, when a government decision to set a minimum wage of $45 a month backfired dramatically, causing the dismissal of more than 5,000 workers. (New York Times, July 7, 1980).

The size of any group's employment reduction depends not only on how much in demand the group is, but also on the extent to which the minimum wage exceeds the market-clearing level. Teenagers as a group are miles behind adults in terms of productivity, if only because they have less education and experience, and so a statutory minimum

wage creates a much larger employment gap for them than for other groups. Hence the youth wage, which stemmed from proposals to eliminate teenagers from minimum wage coverage altogether, or else have a much lower "sub minimum" wage apply to them.

Opponents of these proposals feared that they would cause some firms to substitute teenagers for adult workers, but the alternative was worse, and youth wages still retain majority support. Alexopoulos writes that, "Employees whose pay is boosted by a minimum wage spend their income, and low-earning individuals spend very high proportions of their income, saving little if any." What he overlooks is this: even with a standard rate, in general employers *prefer* to pay above the minimum wage, as this attracts a higher calibre of people.

Without a minimum wage, people would be paid according to supply and demand, and there would be a lot more people getting paid. As Alexopoulos states, low-income workers tend to spend rather than save, and without a set wage rate, spend they shall. Businesses will be able to afford to hire more employees, and as a result enterprises will eventually produce more and expand their area of operations. In this way, money and produce is getting pushed back into the economy and the result is growth. If a minimum wage free environment were allowed to run its own course, the effects would be marked.

There are both winners and losers from the imposition of the minimum wage. The unskilled workers who retain their jobs earn more as a result. Those who lose their jobs obviously earn less. Whether the net effect is to increase the amount of income earned by unskilled workers depends on the elasticity of demand for that category of labour. But wait a minute – what about all those unskilled workers who've lost their jobs because they are legally not allowed to be paid what an employer can afford to pay? This is where the broader effects of a government controlled minimum wage should not be toned down.

All those unemployed workers that would otherwise be working are supported by the taxpayer in the form of subsidies. They spend their days queuing up at CentreLink, and become an unnecessary drain on the budget. Studies on the subject of poverty have found that minimum wage legislation has only a minor effect on the distribution of income. This finding is not surprising, because not all low-wage workers are members of low-income families; many low-wage workers, especially teenagers, are second earners in middle or upper class families. It is clear that the poorest and unskilled labourers are the ones who are crowded out of organised job markets and into 'informal' sectors such as drugs and crime, when minimum wages are imposed and markets are interfered with.

The Great Depression of 1929 changed the way people view the role of government. Socialistic and "charitable" ideas have no place in the business place. And it's no secret that there are many people in Australia currently working below the minimum wage set by the Federal Government. Every so often, the media tells of the police exposing another business that employs illegal immigrants. Yet it isn't just these relatively rare cases that demonstrate how the minimum wage can alienate. Employees of the little-known but thriving 'informal' employment sector (the type of employment that only deals with cash), which can include positions such as pamphlet distributor, door-to-door salesperson or trolley pusher, are also earning below the minimum wage.

The common pattern here is of unskilled labour in relatively lightly scrutinised areas of work. There are other ways to protect those who might be exploited. Workplace unions are one of the most effective. All employees in Australia have a legal right to join a union, and more often than not, members of unions have higher award rates and greater bargaining power. The unskilled don't stay unskilled. If there was no minimum wage, someone somewhere would have hired them, they would have gained valuable experience, and they would automatically be eligible for a higher wage.

It is worthwhile noting that the minimum wage would not be such an issue if it weren't for politicians who – in their zest for grabbing votes – have succumbed to the general public's perception that minimum wages are protecting the poor from exploitation. Alexopoulos puts forth a hypothetical case of a monopsony. This scenario is hardly possible in Australia, or any developed nation, because the de-linking of religion from politics and the freer movement of labour across borders has rendered the proletariat worker much choice.

It may however, be possible in some developing nations. But a monopsony in such a case would be the result of other bungled policies, and an enforced minimum wage would just make things worse, unless other infrastructure problems are solved first. Even so, a monopsonistic employer would have one basic toe-line that they must follow. They must pay their workers a sustenance wage – one that enables them to live – as they can't have their workers dying on them or they'd get no work done. Needless to say, this is a desperate and extreme scenario, and is less and less plausible nowadays.

As nations become more civilised and modern, the safeguard against exploitation a regulated minimum wage provides is not needed as much. Transportation and communication are the infrastructure essentials of what villages in developing countries need, in order to prosper through trade. Until this is made available, a minimum wage will have an almost insignificant impact on poverty stricken regions where people live on a day-to-day basis, and will stifle development.

Imposing restraints on wages prevents entrepreneurs from opening new enterprises and prevents banks from lending money since capital costs cannot be recovered. Despite there being a large number of workers who are willing to work below the minimum wage, no downward pressure can be exerted on the money wage because by law the wage cannot be reduced below the nominal minimum. If the minimum wage is kept quite low, there isn't much of an adverse effect on the economy, particularly when technological innovation is at a peak.

If the poor are in trouble, what is required is to upgrade their skills, and to shift their supply to sectors where market demand is growing. This avenue isn't always realistic, and Australia has its own social security system to help the needy in other ways. In conclusion, it will not do to penalise a small businessman for the burden of making unskilled labourers "richer" than the market will support, and it is imperative that we don't kill the hen (entrepreneur) that lays the golden egg (of jobs).

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