Once More the Minimum Wage

Hyman P. Minsky

Washington University

Iranamuck, to use the New Republic's label for the Reagan/North Follies, a gabble of attractive candidates, and the clear failure of Reaganomics to achieve a stable and progressive economy should make the Democrats the favorite for the 1988 presidential election. But this does not take into account the death wish that regularily takes hold of Democrats, especially the Congressional liberal variety. The death wish typically takes the form of pursuing futile and counterproductive economic policies and by so doing giving the Republicans a club with which to beat them.

One form the liberal Democrat's death wish is taking this year is the appearance of raising the minimum wage as a leading item on their legislative agenda. Senator Kennedy and Congressman Hawkins have introduced legislation to raise the minimum wage from the present $3.35 to $3.85 an hour in 1988, a 15% increase, and then on to $4.65 in 1990, a rise of an additional 20%. After 1990 the legislation calls for the minimum wage to be adjusted each year so that it will be half of the average national wage.

The main fact that should inform discourse about the minimum wage is that it is $0.00 per hour for the unemployed, not the posted $3.35 per hour. Raising the statutory minimum wage to $3.85 will not change the $0.00 wage of the unemployed.

Previous experience with minimum wages indicates that the increase is likely to be inflated out. The real successes of the Reagan Administration since late 1982 are the decrease in the rate of inflation and the prevention of the multitude of financial crises from laeding to a deep recession.

The ending of inflation is very popular. The Democrats cannot afford to be cavalier about inflation. Raising the minimum wage gives the impression that inflation containmemt is not a high priority: this could be deadly for the Democrats prospects.

The New York Times story of March 25 that carried the head "Democrats Offer Bill to Raise Hourly Wage to $4.65" illustrates the superficiality of the arguments for and against raising the minimum wage. Sar Levitan, who is now director of the Center for Policy Studies at George Washington University, was my Captain during World War II. The Times quotes my former Captain as saying that "Raising the minimum wage is the only thing the Government can do for the working poor."

Captain Sar Levitan certainly knows better than that. A children's allowance of $100.00 or so a month together with an employment guarantee such as Senator Simon of Illinois advocates, will virtually eliminate the poverty that is caused by the combination of a low paying job and a large family to support. Furthermore the logic of Senator Simon's approach allows for families to have multiple jobs and income. The Simon's proposal for public employment projects will enable us to achieve a much closer approximation to full employment than has been achieved over the past 20 years. This will do more to eliminate poverty than any rise in the nominal minimum wage rate.

Of course the opposition to raising the minimum wage speaks as much economic nonsense as the advocates. Bill Brock, the Secretary of Labor, is cited as saying that raising the minimum wage would "...prevent employers from hiring more workers, particularily teen-agers." But inflation has decreased the effective minimum wage during the Reagan era and unemployment, especially of teen-agers, has become worse: the lower inflation adjusted minimum wage has been associated with more,not less, unemployment.

Unemployment is due to a shortfall of jobs at the current wage and price level. Raising the minimum wage does not create jobs, it increases the costs that employers have to recover in prices. The minimum wage may be useful for preventing a disasterous fall in wages when aggregate demand collapses, as happened over 1929-1933. But 1997 is not 1929. A collapse of aggregate demand is now impossible, for big government assures that profits and with profits aggregate demand are sustained.

This Congress will be productive on economic issues if it focuses on "Why is our economy unable to generate a sufficient number of jobs so that the unemployment rate is 3% not 7%?". Government certainly is big enough to sustain employment. The answer is that the impact of the government we have upon the economy is wrong for generating and sustaining of full employment.

Ever since the tax reductions of the Kennedy administration the philosophy of policy has been to take care of the well to do, and hope that prosperity trickles down from the well to do to the poor. Even Johnson's progressive War on Poverty reflected the view that poverty revealed faults of the poor not flaws in the economy. Our high unemployment rates and declining industries reveals that being unemployed and poor is mainly the fault of the economy and only secondarily the fault of the unemployed or poor.

To make things better we have to change the economy so that more jobs are available. To do this we need to put in place modernized versions of the New Deal institutions that provided employment to all willing and able to work. If poverty is to be radically diminished the incomes earned from employment need to be supplemented by a meaningfull children's allowance. The combination of employment programs and a children's allowance will go far to eliminate poverty

Senator Kennedy is quoted as arguing that "Six times we have made this fight (to raise the minimum wage), and six times the sky has not fallen." Equally it could be said that six times the minimum wage has been increased, and we are still faced with poverty and mass unemplyment; raising the minimum wage has not been shown to be effective in the past and there is no good reason to expect that it will be effective now. Further it can be shown that the increases in the 70's were the part of the process that bred inflation.

Raising the minimum wage increases the cost of an effective works program. The political barrier to a works program is its costs. A realistic works program will be keyed to the minimum wage. Raising the minimum wage as proposed will increase the costs of providing any particular number of jobs by 15% immediately and 40% by 1990. The higher the minimum wage the smaller the numnber of jobs a given dollar sized works program can provide.

It is necessary for policy to get priorities right and for policy programs to be consistent with what is known about the behavior of the economy. Senator Kennedy and Congressman Hawkins need to be reminded that Congress may propose, but it is the economy that disposes. Policy can and does affect what happens in the economy, but policy only rarely has only the desired effect. Meaningful economic policy is like strong medicine and can have bad side effects. Raising the minimum wage has not been effective in the past in eliminating poverty or reducing unemployment, and an undesirable side effect, inflation, can be associated with prior increases. There is no reason to believe that now is so different from the past that what has failed in the past will be successful this time around.

Designing and implementing a works program is one of the important tasks Congress needs to undertake if our economy is to be made ready for the 21st century. The movement to reform welfare and to transform it into a jobs and training program is a step in the right direction.

However welfare reform will not do anything about male unemployment or the unemployment of teen agers and young adults. One way to attack teen age and young adult unemplyment is to revive the Civilian Conservation Corps: there are a virtual infinitude of resource conservation and infrastructure maintenace jobs that need to be done.

Minimum wage legislation is a largely symbolic gesture, not the basis for effective action. The wages on the job program will set the effective minimum wage. Private employers will need to set their wages with the universal availability of minimum wage jobs in mind.

The achievement of full employment will put inflation on the policy agenda. Reaganomics has shown shown that high unemployment and union bashing will constrain inflation. For full employment to be achieved and sustained increases in private wages have to be disciplined by recognizing that they imply higher costs and prices.

The quest for for full employment opens many policy issues. It requires wage constraint. Policies to achieve an equitable distribution of the costs of wage constraint need to be developed. This may require that wage constraint be wedded to an effective progressive income tax, so that the burdens as well as the benefits of a full employment and constrained inflation are fairly allocated.

Democrats need to set first things first when they set the agenda. The priority policy aim is to achieve full employment. Placing raising the minimum wage on the agenda gets in the way of being effective.