NEW YORK POST

Better than the minimum wage

By CHARLES LANE

Last Updated: 4:16 AM, February 23, 2013

Posted: 11:09 PM, February 22, 2013

Liberal firebrand Paul Krugman backs President Obama's plan for a phased-in 25 percent increase in the minimum wage, to $9 per hour. But he is still economist enough to note that raising it to $20 "would create a lot of problems" — among them, presumably, pricing low-skilled workers out of the job market.

There must be some level beyond which the minimum wage does more harm than good, and no one really denies it. Studies showing that higher minimum wages have little or no impact on employment generally refer to modest increments, or, as the White House's own fact sheet puts it, "the kind of minimum-wage increases we have seen in the United States."

So the issue before us is whether Obama can hit the sweet spot: all higher-income upside for the working poor, and no job-killing downside.

I'm skeptical. Economists David Neumark of the University of California at Irvine and William Wascher of the Federal Reserve have spent their careers studying minimum wages. They found that, by and large, they reduce employment of young, low-skilled people. The last time the minimum wage was increased, in July 2009, Neumark estimated a loss of 300,000 jobs.

Those who disagree start from the plausible premise that the labor market is not perfectly competitive — not many markets are — and that minimum wages correct for this.

In 2010, economist Arindrajit Dube of the University of Massachusetts and two colleagues studied county-level data for restaurants in neighboring states with different minimum wages. There was a job-killing effect in states with higher minimum wages, but it disappeared when they controlled for broader regional employment trends. Ergo, higher minimums were not to blame.

Neumark and his colleagues responded with a paper arguing that Dube & Co. failed to justify their choice of non-minimum-wage factors and that the minimum wage's job-killing effects remain. I found Neumark persuasive, but I'm no statistician.

Even if Dube is right, it's worth asking why. The answer, broadly, is that employers must have found ways to offset a higher minimum wage: raise prices, cut profits, organize their businesses more efficiently — or, in a more positive sense, reap the productivity benefits of a happier, more stable workforce.

John Schmitt of the left-leaning Center for Economic and Policy Research argues that employers probably make several small adjustments. Hard data are scarce, but the best evidence suggests that four offsets are most important, according to Schmitt: lower labor turnover, greater organizational efficiency, "wage compression" (lower wages higher up the payscale) and small price increases.

Note that two of these — wage compression and price increases — hurt other workers and consumers.

In short, Obama's proposal works if it is, in fact, equivalent to those past increases in the minimum wage, which, according to certain studies, have not harmed employment.

There are two risks: The studies are wrong; or, they're right but Obama picked the wrong wage level. Both risks are borne by the least-skilled, poorest members of the labor force.

Meanwhile, even if Obama's proposal does raise some workers' incomes without killing jobs, it would impose costs on other vulnerable members of society.

Is there no more efficient, better-targeted alternative? Yes: increasing the earned-income tax credit, a cash supplement to wages that works like a negative income tax.

Started during the Ford administration and expanded under Republican and Democratic presidents, the credit has grown into a $60 billion-plus program that pays more than $5,300 per year to a family with two children. It lifts millions out of poverty. It has offset much of the minimum wage's inflation-adjusted stagnation in recent years: You might say that, in real terms, federal anti-poverty policy has been been gradually shifting from the minimum wage to the earned-income tax credit. Ditto the states, 24 of which have their own such credits.

Krugman and others object that employers capture some of the credit, because it enables workers to work for less and firms to pay them accordingly. This strikes me as a feature, not a bug.

Poverty reduction, income equality and maximal employment can be thought of as public goods. Therefore, it’s appropriate to purchase them through a transparent tax-code subsidy that falls on the public as a whole — rather than the minimum wage, which works like an invisible tax businesses pass along to workers and consumers.

Here’s a thought: Don’t eliminate the minimum wage. Leave it at $7.25, in recognition of the fact that the labor market is competitive, but imperfectly so. Increase the earned-income tax credit. And then index both to inflation so we can lock in their value over time — and argue about something else.

Charles Lane is a member of The Washington Post’s editorial board.