

THE MINIMUM WAGE LAW ONCE AGAIN



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Abstract:

The minimum wage law is a snare and a delusion. The present paper attempts to demonstrate that such legislation boosts unemployment rates for unskilled workers. Which element of society notoriously favors this enactment? Organized labor.

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INTRODUCTION

When evaluating any public policy, it is important to look not at the intentions of those advocating the proposal⁴, but at the

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⁴ Which are often but not always good; see on this Sowell (2005, 2015)

policy's actual effect. Furthermore, it is pertinent to look not only at the short run effects of a law and those directly affected by it, but also at the long run effects of the law and the effects the law has which are indirect (Hazlitt, 1946). The purpose of the present paper is to cast a harsh light on the minimum wage law; we shall demonstrate that amongst his most signal failures is that it enhances unemployment for those least able to bear it: the unskilled.

In section II we discuss wage floors. The purpose of section III is to review the case for concluding that wage floors increase crime rates. In section IV we ask Why hire workers? Section V is given over to a discussion of loopholes in this law. The burden of section VI is to consider the role of unions in promulgating this pernicious legislation. We conclude in section VII.

II. WAGE FLOORS

The widespread favor that minimum wage laws have garnered ever since the New Deal is a perfect example of people not following these guidelines. This legislation is said to help the needy and the poor in our society by legally requiring employers to pay them at or above a given rate. Without such laws many think that employees would be paid at a near subsistence level, that workers would be taken advantage of, or at the very least that they would receive less than at present. All these claims are far from the truth and stem from knee-jerk reactions instead of a clear understanding of economics.

It is a basic premise of economics that wages tend to equal productivity in a competitive market.⁵ That means that if a worker has a productivity level of, say, \$10 an hour (meaning he adds \$10 to the firm's revenue for each hour worked) and is being paid \$5,

⁵ By this we do not refer to "perfect competition." Rather, to free enterprise, untrammelled by government regulation.

there is an incentive for other employers to offer the worker more than \$5 but less than \$10 in order to make the difference in profit. Where will this process end? Assuming no transactions costs, at precisely \$10, in equilibrium.⁶ On the other hand, if an employer makes the mistake of paying a worker \$15 an hour when his productivity is actually only \$10, then the firm will lose \$5 an hour and there will be an incentive to lower employee pay, or if the employer errs in this manner once too often, he will go bankrupt.

When a minimum wage law is set lower than a worker's productivity level, it seemingly has very little effect.⁷ The same is true when a minimum wage law is equal to what the employee can produce. However, when it is set that is above this point, the laborer will tend to be unemployed. These laws either have very little effect on wages or they lower them to zero through unemploying workers outright.

The minimum wage laws have a negative effect even when set at or below the marginal revenue product of low skilled labor; they reduce producer confidence. If employers observe wage floor laws on the books they are likely to be concerned with rises in such a floor. When or if such an increase takes place, employers will be hurt. They will have to substitute other forms of labor or capital to replace the low skilled labor they are now legally restricted from hiring on a profitable basis. An increase in the general level of automation and the development of greater levels of human capital takes place naturally as economies grow and technology progresses. But these are not to be confused with the inefficient escalations brought about through price floors for labor

⁶ True, we are never at equilibrium, but, always tending in that direction.

⁷ Well, at least not according to the textbook supply and demand curve analysis. However, out in the real world, such an enactment "sends a message" to entrepreneurs that all is not well. *Ceteris paribus*, they are now more likely than before to at least think in terms of "greener" pastures.

services. One example is the grocery boy. Before minimum wage laws were enacted the small children of grocery store owners would often collect and bag the groceries for customers while the patrons played chess or checkers to pass the time. Since the implementation of wage floors in the United States in 1938 (United States Department of Labor Wage and Hour Division) those and similar jobs have disappeared from existence, meaning a net loss for the economy through the reduction in the gains from trade realized through the law of voluntary exchange⁸.

Minimum wage laws have a large effect on those whose productivity is less than the legal amount needed to be hired. This means those with low productivity levels such as young people or blacks will be hurt disproportionately by minimum wage laws while those with higher productivity levels such as college graduates or adults will be hurt much less. This is the reason why the youth black unemployment rate is 28% while that for white adults is 4% (Labor Statistics 2016). Before minimum wage laws were enacted in 1938, the unemployment differential between whites and blacks and the young and old was close to zero (Sowell 2015).

There is only one scenario in which minimum wage laws have the opportunity to permanently raise the wages of workers - the oligopsony/monopsony model (from now on referred to as the monopsony model). Here, there is a single buyer of a specific type of labor services, in which case he will offer workers a wage rate below the competitive equilibrium rate because the firm is a price maker instead of a price taker. In a perfectly competitive market for labor services (infinitely many buyers and sellers) a firm which offers wages below the equilibrium level will not be able to bid any workers away from other employers or people

⁸ The Law of Voluntary Exchange: All voluntary exchange is mutually beneficial in the ex ante sense of anticipation.

enjoying leisure time, and will therefore have no labor with which to utilize their capital equipment for production processes. Furthermore, it will have a very strong tendency to lose its control over capital equipment through bankruptcy.

In monopsony a firm which offers below equilibrium wage rates will not per se have a shortage of labor, for if no other firms are available for workers to seek employment at, the only alternative for a worker taking a wage below his marginal revenue product is leisure time⁹.

However, this case is not relevant to the low skilled labor market. There is no labor market in the modern, or in fact throughout any time in the world's history with as many buyers and sellers of labor as that of the low skilled labor market. Thus, the use of the monopsony model to object to the denigration of minimum wage laws is inappropriate.

There are some small company towns in which one employer does dominate the labor market. But, with modern transportation, all such monopsonistic powers must evaporate. In any case, this ability, if it exists, can only apply to skilled workers, those earning more than at a minimum wage level.¹⁰

III. WAGE FLOORS AND CRIME

Minimum wage laws are a contributing factor to incarceration in the United States. This is due to the drug war, for those with low productivity levels are in effect prohibited from working in the legal market due to minimum wage laws. This

⁹ Leisure time is generally a superior good.

¹⁰ In addition, there are theoretical difficulties with the very concept of monopsony. For one thing, it logically implies invalid interpersonal comparisons of utility. See on this Block and Barnett, 2009

means that for low skilled individuals in the United States, entering the drug trade is very attractive, since there are no options open for a legal job. A young man with a productivity level below the minimum wage rate can still work outside the law as a drug dealer, and even if he has a high enough productivity to attain a legal job the potential loss of welfare payments, unemployment benefits, and public housing all provide an incentive to stay legally unemployed and look for black market employment.

The recent uproar about the shooting of unarmed black men by white police officers and the rise of the Black Lives Matter movement stems, partially, from minimum wage laws and the crime they create, not blatant racism in police forces. Although the shooting of innocent or unarmed inner city blacks is problematic to say the least, the evidence for racism in this regard is non-existent with the percentage of whites shot by police officers higher than that of blacks when violent crime is taken into account¹¹. One reason why young black men are shooting each other over drug turf during our current drug prohibition while young Italian men were shooting each other during alcohol prohibition is because of these abnormal opportunity costs created by government intervention in the economy.

¹¹ Population, Crime, and Police Shooting Statistics Whites as a Percentage of Total U.S. Population 77.1% (QuickFacts 2015) Blacks as a Percentage of Total U.S. Population 13.3% (QuickFacts 2015 Violent Crime Perpetrated by Whites 59.4% (Crime in the United States 2011) Violent Crime Perpetrated by Blacks 38.3% (Crime in the United States 2011) Police Shootings of Whites 54% (Heather MacDonald 2016) Police Shootings of Blacks 28% (Heather MacDonald 2016) $54\%/59.4\%=0.90909090909$ $28\%/38.3\%=0.73107049608$

IV. WHY HIRE WORKERS?

Some may be wondering, why would an employer even hire a worker with low productivity in the first place? Profit is the motivation for hiring labor.¹² Therefore, it will be acceptable to employ anyone whose productivity surpasses the cost of his labor. For example, if productivity is \$6 per hour, and the wage is \$4 hourly, then the firm can earn \$2 per hour on the transaction, and, the job seeker will be successful. On the other hand, with a minimum wage of \$7, while productivity remains at \$6, the employer will lose \$1, not a paying proposition. Thus, the minimum wage imposes a barrier against those who can't produce at the required rate, rather than improve their living standards. As Reynolds (1995, p. 90) points out:

"The most disadvantaged and least valuable are most likely to lose their jobs or not be hired at all. This effect generally would be viewed as undesirable because the minimum wage is supposed to be an antipoverty device. In fact, studies of the minimum wage law show that adult females and white teenagers have not lost jobs, but black teenagers have. Milton Friedman (1972) calls the minimum wage the most antiblack law on the books."

The old, the unskilled, and the disabled are very capable of producing and generating profits for employers, just as much good as anyone else, and this is based in their core competency, plus the ability to work for a lower wage. As Block (2008, p. 138) points out using an analogy from biology: "There are certain animals that are weak compared to others. For example, the porcupine is defenseless except for its quills, the deer is vulnerable except for its speed." This can be compared to the old, unskilled, and disabled in their ability to work for lower wages. They are capable

¹² As it is for all of commercial activity. This goes for consumers too! If a woman buys a dress for \$100 that she valued at \$150, she would have paid that amount if she had to do so, then she earns a profit of \$50.