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The Minimum Wage: Boon or Curse?

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ABSTRACT: In certain countries the choice is how to set the minimum wage rather than whether or not to provide one. The paper discusses the question of an effective minimum wage program. The minimum wage is a difficult juggling act: on the one hand, it must be reasonably high to ensure a generally acceptable standard of living. In the other hand, it should not be too high for low-performance employees to be priced off their careers. Evidence suggests that such equilibrium can be reached. When the minimum wage is set at a modest amount, there are no major job cuts and low income jobs are kept out of poverty.But the minimum wage cannot be used as an efficient method to alleviate poverty, as it is not well aimed at the disadvantaged. It can instead be used as an instrument to achieve a more equal distribution of wages. As it depends on a variety of country-specific considerations, such as labor market dynamics and shifts in job productivity across countries, sectors, professions, there is no general law as to the 'right' level of the minimum wage.The paper suggests that the rational minimum wage strategy should be focused on the study of wage allocation. The minimum wage should be adjusted in such a manner that it would not "too" limit the wage distribution of the impacted workers, such as teenagers, low-skilled workers and workers in the lagging areas.

KEYWORDS: labor market, minimum wage, labor demand, monotonicity, policy decisions, Social issues.

INTRODUCTION

There is a wide body of analytical and observational studies into the impact of minimum wages on labor market results. Theory makes straightforward predictions as to the impact of minimum wages on a dynamic labor market. In this case, a mandating minimum wage decreases wages and obviously raises unemployment. However, this case has minimal scientific relevance. As Christopher points out, "recent reports showed that the "textbook" competitive design of the labor market may have significant flaws in controlling for minimum wage impact on labor market outcomes"[1]. Indeed, observational findings, recently surveyed by Neumark et.al, point to the positive and negative impacts on work of the minimum wage[2].

In fact, only two thirds of the research analyzed by the two authors showed that minimum wages had negative job consequences, although these effects were not always statistically important. The existence of labor market imperfections complies with this methodological uncertainty.Labor markets, in particular, where monophonic businesses face sloping labor supplied curves, create a non-monotonic relationship between jobs and minimum wage. Because of this non-monotonicity, fine-tuning the minimum wage to the elasticity of labor demand and

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supply and the existence of other labor market institutions is the main question from a normative point of view. In this respect, the manner in which the minimum wage is determined is very critical as the fixing regime may influence both the degree and the responsiveness of the minimum wages to changes in the main parameters.This is because the minimum wage needs a balance between the decrease of poverty for working people and the displacement of low productivity workers. In the mechanism that leads to a minimum wage, we should consider the rate of minimum wage to be higher or lower, based on the way these two competing desires are interpreted.Therefore, the different levels of participation in the setting of minimum wages may discern between different levels of cooperation in setting minimum wages as well, and other related policies such as unemployment insurance, are also critical in interactions with other institutions setting the level of income and income [3].

In minimum wage programs, there is a large cross-country transition.It includes cases in which legislative minimum salaries are arbitrarily established by government and regimes, and the government has a passive role to play in giving legal status to these arrangements, applying their covers to non-unionized employees [4]. There is a number of intermediate situations in these two drastic examples, depending on the position of the state or collective bargaining in the concept of the minimum wage. Surprisingly, economic theory and the work carried out have so far devoted little, if any consideration, to the mechanism which leads to minimum wage determination.Political literature, primarily from the United States and Canada, has been written concerning votes on minimum pay behavior, or, more recently, on cultural determinants for minimum-wage expectations. The time series variance of minimum wages also includes some methodological literatures [5].

However, no effort has been made to connect preference for minimum wage levels to fixing regimes and to use variability in setting regimes to understand the differences on minimum wage levels across countries. In this paper I build a basic model with results on the relationship between the minimum wage standard and the setting scheme. The model assumes that the government's legislative minimum wage is smaller than the minimum wage set in collective bargaining, under a very significant set of assumptions[6]. The model has several forecasts on the relationship between minimum wages, unemployment benefits and labor demand elasticity. Then, in 66 countries with a form of national minimum pay in 1981-2005, I use the latest data set to understand the heterogeneity of the degree of minimum wages across countries, using the hypotheses above as guides in describing the methodological context[7]. In specific, I look at the impact on the ratio of minimum wage to average wage of variations in the setting of the minimum wage;I often discuss how different forms of minimum wages respond to shifts in the external world (e.g., labor market elasticity) and unemployment insurance generosity. I find that the minimum wage prescribed by government is below the wage standard laid down under labor agreements. This influence survives many robustness tests and implies a causal association between the setting system and the minimum wage standard.

What's the value and effect of the minimum wage?

The proportion of the minimum wage to the average (mean) wage is the clearest measure of the value of minimum wages. The higher the percentage, more relative the minimum wage worker status, but also the greater the "bite" of the minimum wage, the negative consequences of the minimum wage. The minimum pay / average wage is used to define and advise policy decisions regarding the minimum wage structure. A reduction in the ratio also spurs upwards minimum wage adaptations, such that the minimum wage is held at a set amount, compared to the mean wage, unless it is strategic and accepted by the social partners [8].However, the average wage is not the most acceptable comparison point for the minimum wage, although it is widely used. The explanation is that the average is heavily affected by shifts in the higher end of the distribution of incomes, such as rises in the wages of highly educated skilled employees. As such, the average pay does not reflect the conditions of the job market experienced by employees with low productivity [9].

A more important benchmark for determining the "bite" of the minimum wage is the marginal wage (which is the wage such that one-half of all workers make less than it and one-half earn more).In Colombia, for example, the minimum wage accounts for 40% of the mean wage, but for as much as 68% of the median wage. The foregoing calculation demonstrates that the salaries of minimum wage workers are very similar to the earnings of the median worker, and hence suggests that the minimum wage has a potentially important impact.In comparison, the former calculation shows that there is a substantial difference between the minimum wage worker's earnings and the abstract "average worker." In addition, if wage dispersion increases it may well be the case where the minimum wage falls as a percentage of the average wage, but increases as a percentage of the average wage [10]. In such a situation, the use of the former ratio to explain the minimum wage increase can give rise to a wrong policy decision.

What's the scientific proof?

This segment offers a brief summary of the impact of minimum wages in three main areas: housing, allocation of earnings and poverty. There appears to be a consensus that the aggregate job impact of minimum wages appear to be minimal, positive or negative. This small marginal impact for disadvantaged classes of workers, however, is considerably greater. Most studies have shown, in fact, that higher minimum wages limit jobs for young people.There is also a consensus that a 10% increase in minimum wage levels would reduce teenage employment by between 1% and 4%. As far as prime age jobs are concerned, minimum wages in OECD countries appear to have little effect on job outcomes [11]. These moderate effects on jobs are conditional on setting minimum wages at a reasonable amount compared to the average salary. When, on the other hand, the minimum wage is set so high that it slices directly into the distribution of salaries, and then it is possible that a significant decrease in jobs will result.A classic example of the imposition of US minimum wage requirements in Puerto Rico is that if the minimum wage is increased too high, the results will be deleterious. When the Puerto Rico minimum was increased to around 70 percent of the average industrial wage, as a result, the island suffered substantial job losses and a large uptick in unemployment. Whether countries with higher minimum wages have a bad job record is a significant issue.The most thorough research that discussed this topic is that of Neumark and Wascher[12]. The primary result of the report is that countries with higher minimum wage levels have lower rates of youth jobs. The inclusion of a youth sub-minimum, however, decreases the negative effects for young people of the minimum wage.

CONCLUSION

While the high-wage theory, believing that the level of aggregate demand is dictated by the level of wage rates, is most commonly correlated with the Great Depression, the implications of the doctrine on wage policy go back at least two decades. Instead of being a product of desperate times, the theory achieved broad acceptance when merchants and economists during the booming 1920s, citing the popularity of the continued high-wage policies of Henry Ford and the wage stagnation that had marked the steep depression of 1920-21, extended the demand-enhancing rationale of the doctrine to advocate for an economy-wide minimum wage.Throughout the Great Depression, American economists and policymakers mistook a symptom and curative reaction to the decline in demand for the epidemic itself, trying to prevent the outbreak of wage deflation that had marked the post-war depression, and implemented policies, including minimum wage laws, that raised real wage rates in the face of high unemployment. Although the high-wage ideology is no longer part of the accepted economic philosophy, it is still in place with minimum wage laws initially based on it.

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