Minimum Wages

Pro:
The role of the minimum wage in the modern welfare state

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For several decades, economic growth in the OECD countries served to keep poverty at bay by ensuring that individuals were in work. Fom the beginning of the 1980s, however, it seems that in many countries (most notably in the UK and the USA) the inverse link between growth and poverty began to break down. Rising wage inequality and an increase in the proportion of households headed by low-wage workers (typically single parents or households with a single earner) seem to have brought about this new trend. Hence, low wages are now a key issue in the struggle to alleviate poverty. In this scenario, minimum wages, despite the harsh judgement given by standard economic analysis, have emerged forcefully, both in the academic arena and in policy discussions, as a proper tool to distribute income, with the traditional slogan "make work pay more than welfare" being back in play.

The conventional arguments against the minimum wage are as follows:

- Labour demand will fall if it is set above the competitive wage and, moreover, the adverse employment effects are the larger the more open is the economy; thus, far from helping the poor, a minimum wage is more likely to leave them worse off , and
- it may be ineffective as a redistribution tool since relatively few of the lowest-paid workers are from poor families and furthermore it may lower the amount of specific training provided by firms for the least educated workers since part of the financing cannot be shifted onto workers due to the minimum wage.

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Is that picture accurate? The new revisionist view on the minimum wage claims that, with few exceptions, such might not be the case. So, the burgeoning empirical evidence on the employment effects shows that those effects are bound to be negligible, and even in the more negative cases it turns out that the minimum wage is an effective distributive tool: at worst, it is estimated, a 10% increase in the minimum wage reduces employment by just 2% to 3% and hence increases the share of income received by minimum wage earners by 7% to 8%. However, one may still have to concede that even if a few workers lose their jobs, there may be some undesirable distributive effects, particularly in countries where labour turnover is low and unemployment duration is high, as it happens in Europe. Thus, there is the risk that the minimum wage will divide the low-paid workforce into lucky winners and unlucky losers. Moreover, the effects of the minimum wage in different countries do depend strongly on how it fits in their labour relations systems. For example, if the wage-setting system is such that higher-paid workers restore the differentials that increases in the minimum reduce, then the redistributive purpose of the minimum wage could be subverted. This is particularly the case in countries where minima agreed in collective bargaining are superimposed on statutory minima. Another case where job losses have been found to be sizeable, especially among teenage workers, is where a single national minimum wage is imposed without allowing for lower levels for young people whose equilibrium wage is bound to be lower than that of adult workers.

With regard to training, the evidence is again very inconclusive: It might even be true that a binding minimum wage induces workers to raise their productivity to the level of the minimum by acquiring education which otherwise would not have been taken. As for the characteristics of minimum wage earners, while young workers used to account for a high proportion of the low paid in the past, their importance has declined with increases in school enrolment and in female activity rates. So, while youngsters who are not in poor families may be some of the beneficiaries of the minimum wage, an increasing fraction seems to be accounted for by older people, typically women above 20 with some type of temporary contract.

In sum, it seems sensible to conclude that though a minimum wage is not a panacea for poverty, it definitely helps to redistribute income. One should not forget that the long-term well-being of workers depends ultimately on increasing their productivity, and setting a minimum wage might not help in this respect. However, general policies to raise skills and potential earnings will do little to alleviate poverty in the short run. Thus, if judiciously chosen (setting different rates across ages and possibly sectors), without interfering with the available wage-setting procedures (better in decentralised systems) or with existing in-work benefit systems (it ought to raise participation) or payroll taxes (there might be a case for subsidising the social security payments of minimum wage earners), it can do more good than harm in breaking the lock of the poverty trap.

Minimum Wage per Hour, end-1997[a)]
in the 17 OECD countries which have national or statutory minimum wages

Country	In US$, using PPPs	in % of full-time mean earnings	Country	In US$, using PPPs	in % of full-time mean earnings
Belgium	6.40	52.6			
Canada	5.33	..	Mexico	0.59	..
Czech Republic	0.92	..	Netherlands	6.00	51.1
France	5.56	55.3	New Zealand	4.46	41.0
Greece	3.06	..	Poland	1.57	..
Hungary	1.05	..	Portugal	2.32	49.6
Japan	3.38	34.9	Spain	2.94	28.8
Korea	2.15	27.4	Turkey[c)]	1.38	..
Luxembourg	6.91	..	United States	5.15	34.9

[a)] In all cases, the minimum wage refers to the basic rate for adults. – [b)] For countries where the minimum wage is not usually expressed as an hourly rate, the given rate has been converted to an hourly basis assuming a working time of 8 hours per day, 40 hours per week, 173.3 hours per month. – [c)] In thousand of Turkish lira.

Source: OECD, Employment Outlook 1998.