NATIONAL REVIEW ONLINE

The Minimum Wage: Not What It Used to Be?

By: Veronique de Rugy – December 10, 2013

One of the problem with advocates of large and larger government interventions is that they don't often adjust their prescriptions to changes in society and conditions. For instance, when Social Security was implemented in 1935, seniors, as a group, were struggling financially, and life expectancy was much lower. Leaving aside the disincentives created by that kind of program, there was a real justification for Social Security, and the projected costs of the program weren't as steep as they are today. But things have changed quite dramatically for seniors: According to combined recent data from 15 federal agencies published in 2010, Americans over the age of 65 today are in remarkably good shape compared with those from previous generations. Their average net worth has increased almost 80 percent over the past 20 years; they form a larger share of the high-income group and a smaller share in the lower-income group than their predecessors; they are far better-educated, and they live longer and healthier lives. Yet compared with previous decades, Social Security itself is now in remarkably bad shape.

And yet most of the discourse about Social Security tends to assume that things haven't changed or that the need for the program is as great as it used to be. Some seniors still need this assistance, and they should get it, but the situation has changed and we shouldn't pretend otherwise. The changes mean that there's a lot of room for reforming the program.

The same seems to be true about the minimum wage. Today professor David Neumark, a professor of economics and director of the Center for Economics and Public Policy at the University of California, Irvine, has a great piece explaining how complaints about the decline in the real value of the minimum wage aren't taking into consideration the fact that federal policy aimed at low-wage work and low-income families has rightly shifted "toward a generous earned-income tax credit, which is better focused on poor families." That means that we're relying less on the minimum wage than we did 20 years ago, but doesn't mean that there's a lower level of assistance to lower-income Americans. He writes:

There has been a significant policy shift, however, in how to guarantee a minimally acceptable income to families with low-wage workers. In particular, the earned-income tax credit was instituted in 1976, and its generosity has since been expanded considerably.

Through the tax system, the earned-income tax credit pays benefits to families with low income and employed workers. For example, in 2013 a low-income family with two children could receive a refundable tax credit of 40 percent of its income up to a maximum credit of $5,372. This maximum applied to families with income of $13,430, and it is phased out as their income rises. In addition, many states supplement this with their own earned-income tax credits. The benefits are a little higher for three-child families, a little lower for one-child families, and negligible for families with no children (a maximum of $487, or a subsidy of only 7.6 percent). So like the minimum wage, the earned-income tax credit provides an income floor for working people that exceeds what they would earn in the absence of either policy.

Reflecting this change in how we support low-income families, federal government spending on the earned-income tax credit rose to $55 billion in 2011, about twice the spending on welfare. The figure below shows the real minimum wage (as above), and the maximum credit for a household with two children. The policy shift is obvious. And indexing of the earned-income tax credit ensures that, unlike the minimum wage, it is not eroded by inflation.

He has much more in his piece from the virtues of the EITC to the effects, positive and negative, of a mix of higher minimum wages and the EITC. As he explains, as with most government interventions, there will be winners and losers. The piece is a must-read. He concludes:

These factors are some of the reasons the earned-income tax credit has attracted widespread political support, and — as shown above — has to some extent supplanted the minimum wage as a means of helping low-income families. That the minimum wage has declined in real value is not necessarily an indication that we, as a society, have abandoned our obligations to low-income families. It may be more of an indication that we have found a better way to meet these obligations.

The whole thing is here. This morning, Cato Institute's Chris Edwards, also writes about the minimum wage and talks about another of Neumark's contributions to the debate, this NBER study with William Wascher. Edwards ends his piece with a nice Milton Friedman quote:

As with many things, Milton Friedman said it best: "The minimum wage law is most properly described as a law saying employers must discriminate against people who have low skills."

Finally, last week, the *Washington Post*'s fact checker looked at our president's claim that there is "no solid evidence that a higher minimum wage costs jobs." Pinocchios!