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Improving labor freedom in Minnesota: Minimum wage

STATE LAWMAKERS SHOULD:

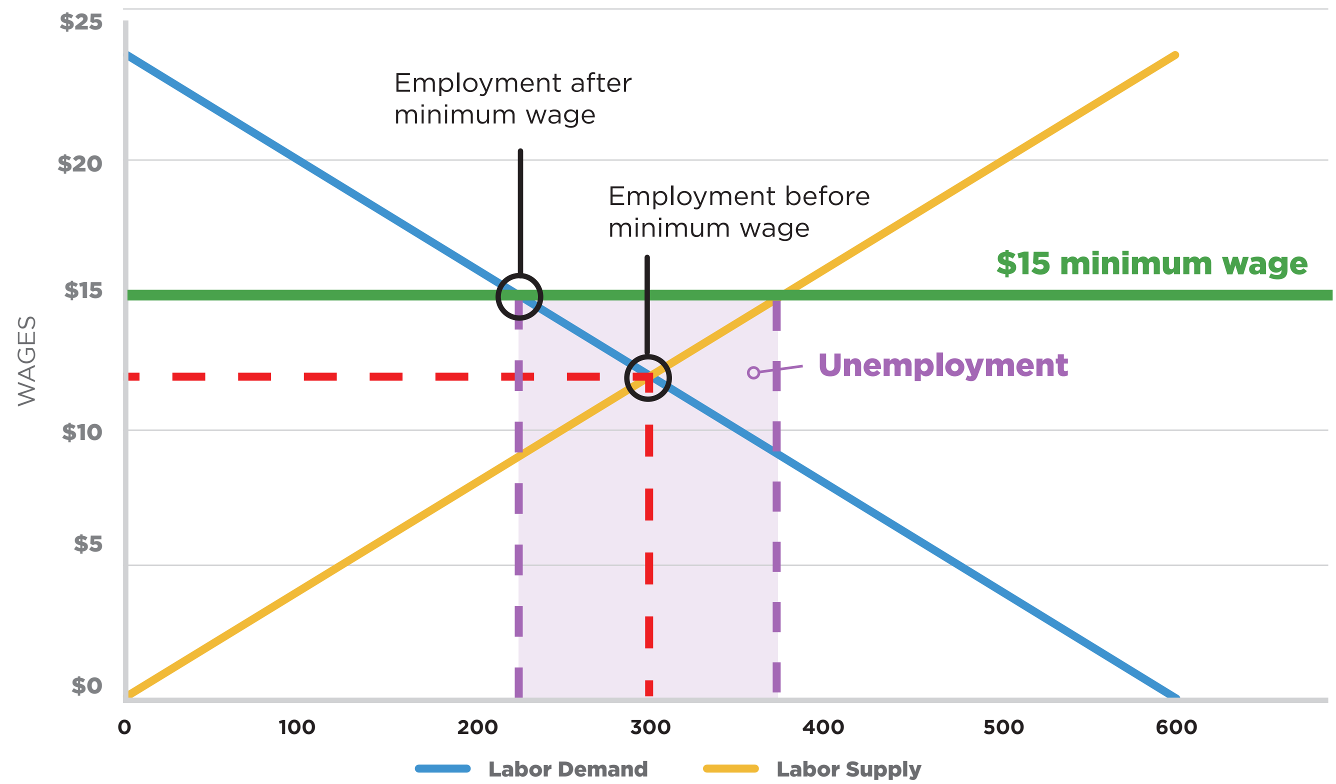
- **Abolish the state-wide minimum wage**

Minimum wage in Minnesota

Due to recent ordinances, the Twin Cities per hour minimum wage is slated to reach $15 for all businesses in 2024 for Minneapolis and 2027 for St. Paul, both higher than Minnesota's current statewide mandated minimum wage of $10.08 for big businesses and $8.21 for small businesses.

Yet, despite having a minimum wage higher than the federal government's $7.25 per hour, numerous proposals have been floated to raise the state's minimum wage.

FIGURE 1
LABOR MARKET WITH A $15 MINIMUM WAGE



SOURCE: CENTER OF THE AMERICAN EXPERIMENT

Minimum wage laws are harmful

Minimum wage is what economists call a price floor — a price control mechanism that keeps minimum prices higher than the market clearing level. Price floors are problematic because they reduce demand for goods or services while increasing supply, leading to a surplus.

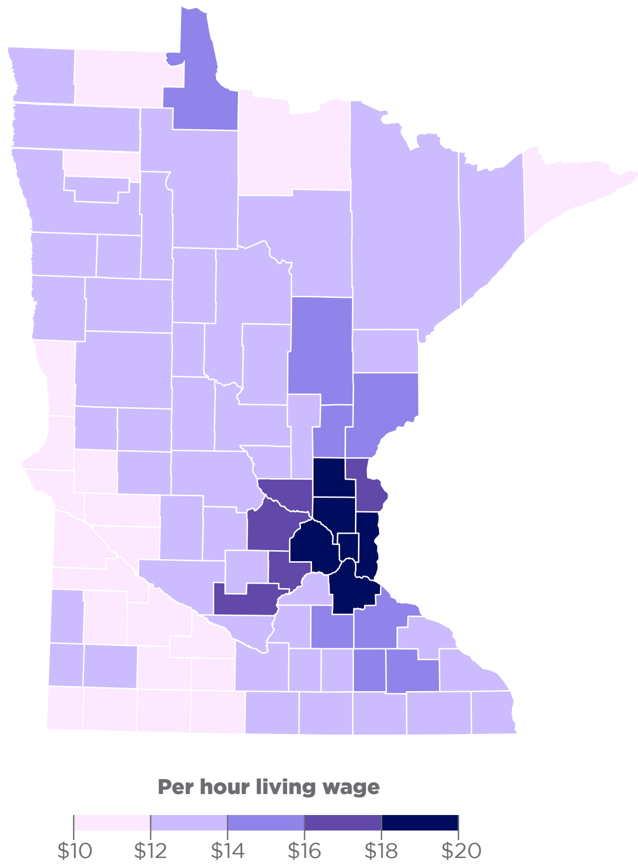
Consider a job market with a market clearing wage of $12 per hour as shown in figure 1. If a $15 minimum wage is introduced in such a market, labor demand is reduced by 75 jobs, while 75 more workers enter the market, thereby increasing unemployment by 150 jobs.

To put it more generally, a minimum wage hike above what employers are willing to pay reduces labor demand while incentivizing more people to enter the labor force — depending on how responsive labor supply is to wage changes — creating extra unemployment.

How this happens

In the labor market, businesses will hire a worker only if his marginal productivity is higher than his marginal cost to the employer. A minimum wage raises the marginal cost of hiring an unskilled worker while leaving his marginal productivity unchanged. Accordingly, employers are reluctant to hire unskilled or lower-productive workers when the minimum wage is higher than the marginal cost and may compensate by cutting jobs, cutting hours, reducing future hires, reducing other benefits, automating, or making current workers work harder.

FIGURE 2
PER HOUR LIVING WAGE BY COUNTY, 2020



SOURCE: MINNESOTA DEPARTMENT OF EMPLOYMENT AND ECONOMIC DEVELOPMENT

The negative effects of minimum wage on employment, especially that of young and low-skilled workers, are well documented. A 2018 report by the Center for Research on the Wisconsin Economy (CROWE) found that compared to Wisconsin, Minnesota experienced a 4 percent decline in employment in limited-service restaurants after the 2014 minimum wage hike. Furthermore, youth employment declined by 9 percent in Minnesota while it increased by 10.6 percent in Wisconsin. Moreover, higher labor costs were passed on to consumers through higher prices.

Overall, studies estimate negative effects of minimum wage on employment as being more defined for young adults, teens, and lower-skilled and low-educated workers.

Abolish the state-wide minimum wage law

Minimum wage reform at the state level is limited since the federal government mandates that all employers pay a minimum wage of $7.25. States can either preempt local minimum wage laws, abolish their state minimum wage laws, or do both.

Currently, more than half of all states preempt local minimum wage laws, including three of our neighbors. While similar efforts have been tried in Minnesota, they have not been successful. Legislators opposing preemption claim that it deprives local leaders, specifically those in high-wage, high-cost regions, of a useful tool to address the needs of their residents, namely higher pay. Opponents also claim that local leaders are best suited to make decisions regarding their constituents after accounting for economic differences.

But if indeed these differences were a strong motivation for local minimum wage laws, advocates of such laws would also support abolishing the statewide minimum wage. The state law overrides the power of local lawmakers and fails to account for regional economic differences thereby imposing disproportionate costs on low-cost, low-wage regions of the state.

Cost of living differences matter

The value of a dollar is what it can buy you, and what a dollar can buy you in Minnesota depends on where you live in the state. According to the Department of Employment and Economic Development (DEED), in 2020, a family of two parents — both working full-time — and one child living in Cook County had to earn $11.10 per hour to afford basic needs. However, the same family needed to earn $18.80 an hour to afford basic needs if living in Hennepin County.

Therefore, in low-cost regions like Cook County, a dollar is worth much more compared to the metro region where the cost of living is much higher. These differences in purchasing power mean that the true value of Minneapolis'$15 minimum wage — adjusted to account for the cost of living — is much higher in greater Minnesota.

The statewide minimum wage places the same level of burden regardless of these differences. This raises labor costs more disproportionately for businesses in greater Minnesota compared to those in the metro area, meaning that a disproportionate number of workers are priced out of the labor force.

Certainly, high-wage high-cost areas are not immune from the destructive effects of minimum wage laws. Just recently, for example, the Federal Reserve Bank of Minneapolis published two studies showing that minimum wage hikes in the Twin Cities led to job losses, especially in the restaurant industry. But when it comes to low-cost, low-wage areas, these effects are merely multiplied manyfold.

Conclusions

If high-cost localities can make their own local minimum wage laws on the account of the high cost of living, low-cost localities should not be bound by the state's high minimum wage on the account of their relatively low cost of living. The statewide minimum wage law fails to consider local economic differences and imposes disproportionate costs on small businesses as well as low-skilled workers in low-income, low-cost regions of the state. It should be abolished.

Martha Njolomole is an economist at the Center of the American Experiment.