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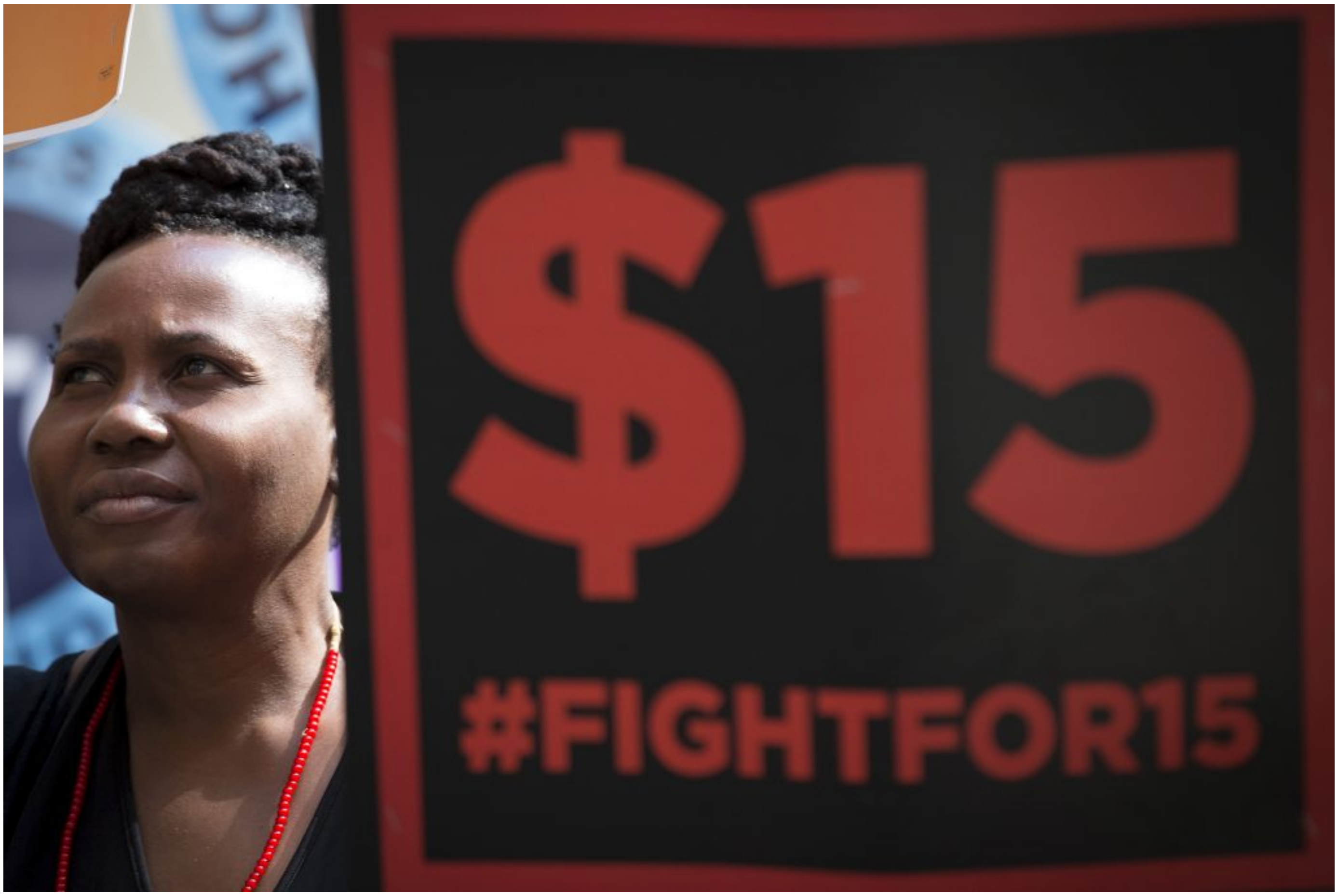
Column: The claim that if wages go up, jobs will go down is not a theory – it's a scam

BY NICK HANAUER *October 5, 2016 at 12:40 PM EST*



The claim that if wages go up, jobs go down isn't a description of reality at all. It is a negotiating strategy used by employers to keep wages down and profits high, writes billionaire venture capitalist and $15 minimum wage proponent Nick Hanauer. Photo by Brendan McDermid/Reuters

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Few issues have moved more quickly from fringe to consensus than the "Fight for $15." When colleagues and I suggested at a Democratic political conference in early November 2012 that we should raise the minimum wage to $15, people in the audience literally laughed. When New York City fast-food workers first walked off the job two weeks later demanding a $15 minimum wage (more than twice the federal $7.25 rate, both then and now), the number was widely dismissed as overreaching and symbolic — a mere bargaining tactic on the part of workers who had little if any bargaining power at all. Nobody predicted what would follow. As an early and vocal advocate for $15, even I was surprised by how fast the dominoes would fall.

But as remarkable as this political progress has been, the political rhetoric surrounding the minimum wage remains surprisingly unchanged. Minimum wage opponents continue to deride every proposed increase as a surefire job killer, while reporters and pundits reliably characterize the passage of every minimum wage ordinance and statute as a dangerous experiment that threatens to harm the very people it's intended to help. "California makes itself a guinea pig in a massive and risky minimum wage experiment," tweeted the New York Times's Noam Scheiber. "Raising minimum wage risky," the Lexington, Kentucky Herald Leader's headline tersely warned its readers following $15 victories in faraway California and New York. "Raising minimum wage hurts low-skill workers," the Detroit News bluntly chimed in. "Even left-leaning economists say it's a gamble," Vox solemnly cautioned (without actually managing to cite a single left-leaning economist willing to pejoratively editorialize $15 as a "gamble.")

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No one captured this conventional economic orthodoxy better than Noah Smith, a very smart economist and writer for Bloomberg. Smith, in an article titled "Finally, an Answer to the Minimum Wage Question," welcomed "the fact that, finally, we'll have some data on how the $15 minimum wage would affect jobs." In his article, Smith said he considered it a test because "in theory a higher minimum wage should cause increased unemployment." Smith's implication is that we have never run a minimum wage experiment before and that the increase is unprecedented in economic history. But the core assumption of Smith's piece is a so-called "economic theory" — asserted as if it is a law of nature — that if the minimum wage goes up, employment must come down.

To be fair, Smith and the others above are not the first to predict economic Armageddon if the minimum wage was increased. The story of the minimum wage as a job killing tradeoff is deeply rooted in classical economics. It is the law of supply and demand in action: "When you raise the price of employment, guess what happens, you get less of it," former House Speaker John Boehner explained succinctly. James Buchanan, a Nobel Prize-winning economist, compared this theory to a force of nature when he wrote:

> *The inverse relationship between quantity demanded and price is the core proposition in economic science, which embodies the presupposition that human choice behavior is sufficiently rational to allow predictions to be made. Just as no physicist would claim that 'water runs uphill,' no self-respecting economist would claim that increases in the minimum wage increase employment. Such a claim, if seriously advanced, becomes equivalent to a denial that there is even minimal scientific content in economics.*

But the confidence of the doomsayers and the anxiety of the pundits might make more sense to me if they hadn't been making the same dire predictions since the minimum wage was invented 78 years ago — or if at least some of these dire predictions had actually managed to come true. In fact, contrary to the cautionary headlines, there is nothing "experimental" about raising the minimum wage. The federal minimum wage has been raised 22 times since it was first established in 1938 (state and local minimum wages have been raised hundreds of times), sometimes by as much as 87.5 percent in a single year — far more than the annual increases $15 advocates propose. So if the minimum wage opponents were correct, it should be incredibly easy to find overwhelming empirical evidence that minimum wage hikes cause the job losses they *always* predict:

- "High hourly wages mean nothing to a worker if he has no job," the Southern States Industrial Council subtly threatened in 1938.
- "[A] national minimum wage within our industry is impractical and dangerous," the National Restaurant Association warned in 1949.
- "[I]f the minimum wage were increased to anywhere between the low of $2.50 and the high of $3.00, between 2 and 3.1 million jobs would be lost," claimed the Chamber of Commerce in 1975.
- "The minimum wage has caused more misery and unemployment than anything since the Great Depression," Ronald Reagan imagined while campaigning for president in 1980.
- "[The minimum wage] hurts exactly those workers it intends to help — the poor, the unskilled, and the young," Representative Jim Saxton opined in 1996.
- "The minimum wage systematically hurts the most vulnerable," Ted Cruz recently echoed on the 2016 presidential campaign trail.

So the theory is simple: The minimum wage goes up, jobs come down. But what about reality?

A small army of economists has tried to test this theory over the past few decades. It is tricky, because unlike the simplified models in Econ 101 textbooks, real economies are messy and complex: technologies change, the Fed moves interest rates, oil prices fluctuate, the business cycle swings, a hurricane hits and so on. The challenge is to isolate the impact of the minimum wage from all of these other factors that might affect growth or employment. Through various sophisticated statistical techniques, researchers have attempted to separate the minimum wage signal from the economic noise, and while economists never agree on anything, they have produced a range of consistent results: from zero to zip to nada to a very small effect. In a 2014 letter to President Obama and congressional leaders signed by more than 600 economists (including seven Nobel Prize winners), the authors concluded that "the weight of evidence now show[s] that increases in the minimum wage have had little or no negative effect on the employment of minimum-wage workers, even during times of weakness in the labor market."

Even in the minority of studies that do find a small negative effect, one has to be careful interpreting the results. Contrary to what the press and some politicians would have you believe, these studies are *not* saying that the minimum wage caused jobs to be lost or growth to be slowed in *absolute* terms. Rather, these studies are making a much narrower claim. They postulate an imaginary economy where everything but the minimum wage is held constant and then compare *relative* to that. But what matters to real people is whether employment is growing or shrinking in the *actual* economy where plenty of things other than the minimum wage are changing too.

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After all, what should matter most to people and policymakers is what happens in practice, not in theory. If raising the minimum wage was the "risky job killer" its opponents claim, you would expect to see that clearly reflected in overall employment data. Amazingly, while the federal minimum wage has been raised 22 times, no one had ever answered the most practical question that should inform policy: What happened to overall employment after each increase? Until now.

In a first-of-its-kind study, economist William Lester from the University of North Carolina, in cooperation with researchers from the National Employment Law Project, pored over employment data from every federal increase since the minimum wage was first established, making "simple before-and-after comparisons of job growth trends twelve months after each minimum-wage increase." And the paper's title says it all: "Raise Wages, Kill Jobs? Seven Decades of Historical Data Finds No Correlation Between Minimum Wage Increases and Employment Levels."

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The results were clear: Of the nearly two dozen federal minimum wage hikes since 1938, total year-over-year employment actually *increased* 68 percent of the time. In those industries most affected by the minimum wage, employment increases were even more common: Fully 73 percent of the time in the retail sector and 82 percent in low-wage leisure and hospitality. "[T]hese basic economic indicators show no correlation between federal minimum-wage increases and lower employment levels," the authors write. In fact, if anything, the data suggest that increases in the federal minimum appeared to encourage job growth and hiring. Perhaps even more striking, of the only eight times total or industry-specific employment declined following a minimum wage increase, the U.S. economy was either already in recession (five times), technically just emerging from recession (twice) or about to head into a recession (once). Clearly, this handful of employment downturns would be better explained by the normal business cycle than by the minimum wage. "As those results mirror the findings of decades of more sophisticated academic research," the authors conclude, "they provide simple confirmation that opponents' perennial predictions of job losses are rooted in ideology, not evidence."

A simple way to interpret this finding is that any impact of the minimum wage on employment — positive or negative — is so small as to be lost in the churning of the economy as a whole. Or to use Buchanan's metaphor, in the real world, water does sometimes run uphill — for example when a tide flows upstream into a river. Likewise, the larger tidal forces of the economy have historically overwhelmed any small effect the minimum wage might have had on employment. Despite apocalyptic predictions, the sky has not fallen, and the economy has kept chugging along, creating jobs, even in the face of 22 minimum wage hikes.

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But while there's no evidence that raising the minimum wage is the "risky gamble" doomsayers describe, the devastating economic costs of keeping wages too low are very well documented. After decades of stagnant wages, 73 million Americans — nearly one quarter of our population — now live in households eligible for the Earned Income Tax Credit, a benefit exclusively available to *the working poor*. And according to a 2014 report from the Organization for Economic Cooperation and Development, rising income inequality (and the reduced consumer demand that comes with it) knocked 6 to 9 percent off U.S. economic growth over the previous two decades. Wow. If the U.S. economy were 9 percent bigger than it is today, it would support about 11 million additional jobs. So the data would seem to indicate the opposite of the conventional wisdom. The job killer turns out to be keeping the minimum wage too low.

How is this possible? How could self-respecting economists suggest that an increase in the minimum wage might encourage job growth and hiring? Well, first of all, there's what economist Michael Reich calls "income effect": People on the minimum wage tend to spend everything they earn. Increases in the minimum wage thus flow back into the economy (again, like the tide flowing upstream), generating increased demand, which in turn increases hiring and investment. It is a basic principle of capitalism that when workers have more money, businesses have more customers, and when businesses have more customers, they hire more workers. This income effect may not have left a large mark on the historical data, because historically, most minimum wage increases have been relatively small. But it is real and should be taken into account. And in an era of depressed demand and consumer spending, as we are now, higher wages are exactly what our economy needs.

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I am a businessperson, not an economist. But I have had an unusually broad career as an entrepreneur and investor participating in the founding or building of 35 companies across a broad range of industries. And while the idea that higher wages for workers might create jobs, not kill them, may elude the instincts and logic of orthodox economic thinking, as a businessperson, it makes perfect intuitive sense to me. That's because the first, second and third most important thing to any business is customers. The more of them there are and the more money they have, the better things get. Without customers, there is no business and no jobs. Period. And while every businessperson would like to keep his or her own labor costs low, if every business paid poverty wages, whose workers would buy the stuff that sustains the economy?

There are a bunch of other really obvious reasons why increasing the minimum wage benefits the economy in ways beyond sustaining demand and creating jobs. Evidence shows that better-paid workers are simply more productive. When workers earn a decent wage they tend to stay in their jobs longer, gaining more experience and specialized skills and serving customers better.

Obviously, a higher minimum wage also pays dividends to taxpayers by reducing demand for costly anti-poverty programs. In the low-wage fast-food industry, over half of all families — 52 percent — are enrolled in at least one public assistance program, at a combined cost of $7 billion a year. (McDonald's even provided a "McResources" hotline to help its impoverished workers apply for government aid.) And Wal-Mart alone, according to a 2014 report from Americans for Tax Fairness, costs U.S. taxpayers an estimated $6.2 billion a year in public assistance to its 1.4 million mostly low-wage workers — coincidentally, an amount roughly equal to the $6.5 billion a year the company lavished on stock buybacks over the previous decade.

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Finally, as the real purchasing power of the minimum wage has eroded away over the past half-century, workforce participation rates have declined with it — when a minimum wage job doesn't earn you enough to live on, why bother looking for work? Conventional economic thinking holds that high executive pay and low tax rates are necessary to incentivize the wealthy to work hard. But oddly there is very little discussion of similar incentives for the poor. A higher minimum wage incentivizes people to come back into the workforce, boosting both economic growth and workers' self-esteem. And we shouldn't underestimate the importance of this last point.

Some economists like to say that increasing the Earned Income Tax Credit is a better way to deal with low incomes than raising the minimum wage. The Earned Income Tax Credit is the federal government's most important and effective anti-poverty program. But it is still a government anti-poverty program, a handout that says you can't make it on your own. It is important to remember that making a living, being able to pay your way and feeling that society values what you do has a social impact that goes well beyond economics. If the minimum wage doesn't hurt employment, then why wouldn't we prefer that people get higher incomes through work rather than a government program?

Taken together, all these factors help explain why increasing the minimum wage doesn't necessarily result in less employment or a worse economy: The higher cost of labor is at least partially mitigated by the host of economic benefits higher wages produce. Which is not to suggest that there is no limit to how high we can reasonably raise the minimum wage. "If $15 is so great, why not $50 or $100?" critics sometimes mockingly ask. Well, because that would be stupid. The positive benefits of a $100 per hour minimum wage would almost certainly be overwhelmed by the costs. So no one is proposing $100; instead we are proposing $15, which is roughly halfway between what the minimum wage would be had it tracked either productivity gains ($21) or inflation ($10).

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But minimum wage opponents are not haggling over a number; indeed, many have been perfectly honest that they would prefer no minimum wage at all. They are not arguing that a minimum wage might be bad for some people if it's too high, phased in too fast or if the economy is too weak to absorb the blow. No, they speak about the minimum wage in far more absolute (and often apocalyptic) macroeconomic terms. Their core claim is that the minimum wage *always* hurts the whole economy — that it will always suppress employment and reduce growth: "When you raise the price of employment, you get less of it." That is the economic theory that has long dominated our minimum wage debate. And the evidence proves that it is clearly and definitively wrong. The data seem to indicate that the higher it goes the better things might get. At the very least, the data show that we have never raised the minimum wage enough in our nation's history to ever see any of the job-killing effects predicted.

In fact, this claim is so wrong that it is reasonable to question whether it is rightly a "theory" at all. In order for something to legitimately be called a scientific theory, it must result in accurate and consistent predictions in an empirically verifiable way. For example, Newton's theory of gravitation asserts that the attraction force between two objects is inversely proportional to the square of their separation distance. And in every case ever tested, when the distance goes up, the attraction force goes down. Always. But the same cannot be said for the "theory" that if wages go up, employment will go down. It is not always true. It's not even mostly true. It isn't even *usually* true. So if Buchanan's claim that there is an "inverse relationship" between wages and employment isn't really a legitimate scientific "theory" and certainly not a law of nature, then what is it?

And this brings us to the main point. The claim that if wages go up, jobs go down isn't a description of reality at all. Nor, in my opinion, does it reflect legitimate economics. *It is a negotiating strategy*. It is a scam, a con job, a threat — more precisely, it is an intimidation tactic *masquerading* as a legitimate economic theory. I believe this is where being a businessperson and not an economist leads to greater clarity. Very few economists have ever run a business or negotiated wages. But the first rule in the businessman's handbook on wage negotiation and suppression is always, *always* when they ask for a raise, threaten their jobs. It works like a charm and has since the invention of capitalism. You see, the claim if wages go up, employment goes down isn't made because it is true. It's made because if people like me can get people like you to believe it is true, I'm going to get richer, and you are going to get poorer. The lower your wages are the higher my profits will be. It's that simple.

The claim that if wages go up, jobs go down isn't a description of reality at all… *It is a negotiating strategy*.

I realize this is harsh, but I believe this claim is best understood as a way of subtly and legally threatening the economic and thus physical security of the most vulnerable people in our society. If you haven't already lived through it yourself, imagine what life must be like for a typical minimum wage worker, barely hanging on, always a paycheck away from financial ruin and the economic abyss. And by abyss, think homelessness — think real hunger: not the hunger that comes from working through lunch or from starting a new diet, but from not having enough money in your pocket at the end of the week to buy food. Imagine seeing your own children go without the basics that all children need to succeed and thrive. Imagine not having enough savings or credit to smooth over the rough patches; imagine not having a safety net, because your friends and family are as desperately poor as you. It must be terrifying, particularly if you have children, to be constantly threatened in this way.

For most readers of this journal, losing a job might be hurtful, inconvenient, even economically challenging, but it wouldn't be an existential threat. But if you *are* living the life of economic insecurity shared by an increasing number of Americans and I can get you to believe that a couple-buck hike in the minimum wage would likely result in unemployment for you or a loved one or your neighbors — if I can get you to believe that when wages go up, employment goes down — then as your employer, I have *power* over you. And that power means I will get more and you will get less. This explains why, in the face of overwhelming evidence that it isn't true, the claim is made again and again. It explains why people who prefer wages to be low and profits to be high will never, ever stop making this claim or similar claims. The claim isn't made because it is true. It is made because bullying people is extraordinarily effective.

"[R]aising the minimum wage is a job killer," Domino's Pizza CEO David Brandon declared in 2004, back when the minimum wage was just $5.15 an hour. "If the minimum wage increased there would be price inflation for consumers or we would likely employ fewer people." Brandon's message to his poverty-wage employees was clear: You better think twice before recklessly demanding a higher minimum wage. (For the record, according to its 10-K filings, Domino's now employs 30 percent more people with the federal minimum wage at $7.25 an hour than it did at $5.15, and here in Seattle where the minimum wage now stands at $13, Domino's still sells a two-topping medium pizza for just $5.99.)

This threat — that when wages go up, employment goes down — falls neatly into what is commonly known as "trickle-down economics." It's not really economics in any scientific sense. It is simply a time-tested way for the powerful to assert control over the less powerful. For the real magic of trickle-down economics isn't convincing you that if the rich get richer, that's *good* for the economy. The real power comes from convincing you that if the poor get richer, that would be *bad*. It is a clever Catch-22: A low minimum wage may trap you and your children in a vicious circle of poverty, but it is the only thing that guarantees you any wage at all.

The two cornerstones of trickle-down economics are:

1. If wages for the poor go up, employment goes down; and

2. If taxes on the rich go up, employment goes down.

But this isn't a scientific theory or a law of nature that describes the world in any empirically verifiable way. This is a threat — a moral claim aimed at *social control*. As such, it is repeated again and again and again, not because it is true, or because the powerful believe it to be true (although some might — self-deception can be a soothing psychic balm). The rich and the powerful relentlessly repeat this claim because if they can persuade the poor and the weak to believe it, it will be very advantageous to the powerful and the rich.

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Trickle-down economics is about status, power and economic privilege, not truth; and given what's at stake, the people who benefit most from trickle down are desperate to maintain its ever more tenuous grip on the economic debate. You can see this desperation — you can all but smell it — in the breathless rhetoric spewing from the guardians of the economic elite: For example, the tortured math of the American Enterprise Institute or the contorted libertarian word jumble smeared across the pages of Forbes or on the opinion pages of The Wall Street Journal. For decades, these trickle-down apologists grew fat and lazy in the unchallenged sinecure of the dominant economic faith, leaving them totally unprepared for the speed at which the $15 heresy would take hold. And now, with each city or state that passes $15, the tighter the faithful cling to the old-time religion: "When you raise the price of employment, you get less of it," they desperately preach. But while they have no empirical evidence to back up this claim, they sure have plenty of motive to believe it. Because if you think about it, you realize — they have to believe it.

That's because trillions of dollars are at stake. *Literally trillions*. Thanks in part to this trickle-down scam, corporate profits' share of the U.S. economy has grown from about 6 percent of GDP 40 years ago to about 12 percent today, while wages' share of GDP has fallen by a comparable amount. That's about a trillion dollars a year that used to go to wages that now go to profits. But if the 99 percent of Americans who have seen their real incomes stagnate or decline over the past couple decades came to realize that there really is no inevitable tradeoff between higher wages and jobs, then why wouldn't they demand higher wages? Much higher wages? Much of which would come out of the windfall profits and giant bonuses of the people who fund AEI and read Forbes. Is it any surprise that these shameless propaganda mills would refuse to bend their "theory" to the facts?

But what is most dispiriting to me is the credulity of the broader media. They probably mostly believe that they are responsibly reporting the truth when they naively warn of the "job-killing risks" of raising wages. What they are actually doing is inadvertently bullying poor people on behalf of rich people. But I guess "risk" sells ads. So there is that.

The real threat to the opponents of the minimum wage posed by the fight for $15 isn't that it would raise wages for nearly half of Americans (although it would certainly do that). It is that it exposes trickle-down economics for what it truly is — an intimidation tactic, a con job, a scam — a rhetorical negotiating strategy that has been deftly used to pick the pockets of American workers for the past 40 years. The opponents of a $15 minimum wage don't oppose it, because they are afraid it will harm the economy. They are terrified that it will help the economy, and by so doing, demolish a lie that has rationalized a set of economic policies that have suppressed the wages of tens of millions of Americans for decades. A $15 minimum wage won't solve the enormous structural problems in the U.S. economy. But in lifting up our poorest workers and in opening the eyes of everyone else to the way in which they have been scammed, it would be a very good start.

Nick Hanauer
Nick Hanauer is a Seattle-based entrepreneur, venture capitalist, philanthropist and author.