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# **Why Raising the Minimum Wage Is a Poor Way to Help the Working Poor**

**An Analysis of Senators Kerry and Kennedy's Minimum Wage Proposal**

Richard V. Burkhauser, Cornell University  
Joseph J. Sabia, Cornell University



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**Richard V. Burkhauser** is the Sarah Gibson Blanding Professor of Policy Analysis and Chair of the Department of Policy Analysis and Management, Cornell University. He has published widely on the behavioral and distributional consequences of government policies. He received his Ph.D. in Economics from the University of Chicago.

**Joseph J. Sabia** received his Ph.D. in Economics from Cornell University in 2004. His research areas include labor economics and public policy analysis. He will be joining Abt Associates this fall.

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## Executive Summary

Politicians from Democratic Presidential candidate John Kerry to Senator Ted Kennedy are pushing to increase the minimum wage to \$7.00 an hour. This 36 percent increase in the wage floor will only serve to decrease employment opportunities for entry-level employees—particularly the low-skilled employees minimum wage hikes are intended to help. Supporters of these wage increases claim that this increase will help Americans in poverty. In particular, Senator Kerry states that the main beneficiaries will be women, many of whom are primary breadwinners in their family.

This study reveals that the majority of beneficiaries from a minimum wage hike are not in poverty nor are they the primary earner in their family. In fact, according to U.S. government data, employees earning the minimum wage are more likely to live in families earning three times above the poverty line than in poor families. The authors found that the vast majority of families who are living in poverty will *not* benefit from the proposed increase. Only 15 percent of the benefits from a wage increase to \$7.00 an hour would go to families in poverty; 60 percent of the benefits would go to families earning more than twice the poverty line.

The authors also found that the majority of beneficiaries are not the primary earner in their family. While supporters of wage increases often claim that the increase will help sole earners attempting to raise a family on a minimum wage income, (particularly single females), these individuals represent a dramatically small minority of beneficiaries. Only 12.6 percent of beneficiaries from the proposed increase are unmarried women with children. Over 82 percent either are not the highest earner in their family, are single adults, or are married without children.

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“According to U.S. government data, employees earning the minimum wage are more likely to live in families earning three times the poverty line than in poor families.”

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The especially poor targeting of this social program makes it highly inefficient and often ineffective means of combating poverty. The majority of beneficiaries are not families struggling to survive on the minimum wage but rather second earners and teenagers. The effect of a minimum wage increase is even worse when one considers the well-documented job loss resulting from a hike. The authors cite several

studies that show that increasing the minimum wage not only decreases employment but that these employment losses are concentrated on the least-skilled employees in the economy. For example, a 10 percent increase in the minimum wage causes four times more employment loss for employees without a high school diploma and African-American young adults than it does for more educated and non-black employees.

— Craig Garthwaite  
*Director of Research*

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Richard V. Burkhauser and Joseph J. Sabia, Cornell University

## Introduction

Minimum wage fever is spreading among policymakers. A number of state legislatures are considering state minimum wage hikes and Democratic Presidential candidate John Kerry has called for an increase in the federal minimum wage from \$5.15 to \$7.00 per hour. In addition, a number of United States Senators, led by Sen. Ted Kennedy, are pushing a similar increase to \$7.00 an hour. Proponents of his proposal insist that a minimum wage hike will alleviate poverty among the working poor. But, as we will show, even under the best economic assumptions, hikes in the minimum wage will fail to achieve this goal.

On June 18, 2004, Sen. Kerry announced his minimum wage plan, saying:

“I’m running for President to build a stronger economy that lifts up families and expands opportunity for hardworking Americans. Today, there are workers—many of them working women—struggling to get by on the minimum wage. That’s wrong. We can do better. And together, we’re going to change it. ... I want to build

an America where working families can get ahead, where a family working full-time does not have to raise their children in poverty. With this increase, we will lift up millions of workers and build a stronger America as a result.”<sup>1</sup>

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“The majority of the working poor are not helped by a minimum wage hike and the vast majority of those who are helped do not live in poor families.”

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Much of the debate over raising the minimum wage has focused on the trade off between ameliorating poverty—as argued above by Sen. Kerry—and the potential adverse employment effects caused by increasing the price of labor. But research (Burkhauser and Finnegan, 1989; Burkhauser, Couch, and Glenn, 1996; Burkhauser, Couch, and Wittenburg, 1996; Burkhauser and Harrison, 1999) suggests that even assuming no adverse employ-

ment effects, the minimum wage is a poor policy tool to reduce poverty because most individuals earning the minimum wage do not live in families with low incomes.

This research confirms what economist George Stigler argued almost 60 years ago. In his seminal 1946 *American Economic Review* article, Stigler wrote:

“The connection between hourly wages and the standard of living of a family is remote and fuzzy. Unless the minimum wage varies

with the amount of employment, number of earners, non-wage income, family size, and many other factors, it will be an inept device for combating poverty even for those who succeed in retaining employment.”<sup>2</sup>

The “fuzzy” relationship between an individual’s hourly wage rate and family income has only become fuzzier over time. In 1939, the first year that a minimum wage was enacted in the U.S., the correlation between wages of workers and their families’ income-to-needs ratio was 0.207. By 1989, the correlation fell to 0.053.<sup>3</sup> These facts suggest that even if minimum wage hikes had no employment effects, the policy may be ineffective at reducing poverty.

In this study, we present evidence on “who gets what” from an increase in the federal minimum wage from \$5.15 to \$7.00 per hour. Our findings suggest that (1) the majority of workers living in poor families have wage rates higher than \$7.00 per hour and would not be helped by a minimum wage increase, and (2) workers earning the minimum wage are more likely to live in families with incomes three times the poverty line than in poor families. Hence, the minimum wage is not especially target-efficient and is unlikely to reduce poverty, as supporters suggest.

## “Who Gets What” from a Minimum Wage Hike

We examine “who gets what” from an increase in the minimum wage using a sample of workers aged 16 to 64 taken from the March 2003 Current Population Survey (CPS). We use data from the outgoing rotation groups, which contain information on workers’ usual gross weekly earnings in their primary job and how many

hours per week they usually work in that job. Workers paid by the hour are asked directly for their hourly wage rate. As argued in Burkhauser, Couch, and Glenn (1996), these data are better suited for simulating the effects of a rise in the minimum wage because they do not require workers to recall earnings and hours from the previous year.

Table 1 contains a weighted sample of workers aged 16 to 64 that arrays workers’ wage rates by the income-to-needs ratios of their families. The income-to-needs ratio is defined as the ratio of total family income to the official poverty line for a given family. For example, in 2003, the poverty line for a family of three was \$15,260. Hence, a worker living in a family with three members and a total income of \$30,520 would have an income-to-needs ratio of 2.0.

From Table 1, we find that less than 9 percent of workers earned between \$5.00 and \$7.00 per hour.<sup>4</sup> A small percentage of workers (1.6 percent) reported earning less than \$5.15 per hour. Many of these workers may be in jobs uncovered by minimum wage laws.<sup>5</sup> But the vast majority of workers (89.9 percent) earn hourly wage rates higher than the proposed new minimum wage of \$7.00 per hour.

More important, the vast majority of the working poor—those living in families with income-to-needs ratios of 1 or less—would *not* benefit from such a hike. This is because 70.7 percent of workers living in poor families earn wage rates greater than \$7.00 per hour. They live in poor families because (1) they work less than full-time, and/or (2) their family size is too large for their hourly wage rate to pull them above the poverty line.<sup>6</sup>

**Table 1****Wage Distribution of Workers by Income-to-Needs Ratio of Their Family, 2003**

	Hourly Wage Categories							Total	Percent of		
	\$0.01 to \$4.99	\$5.00 to \$5.14	\$5.15 to \$6.99	\$7.00 to \$8.99	\$9.00 to \$14.99	\$15.00 and over	All Workers		Workers Earning More Than \$5.00 & Less Than \$7.00	Total Benefits*	
	<b>Income-to-Needs Ratio</b>										
Less Than 1.00	4.0	2.2	23.2	32.0	30.4	8.3	100	5.3	15.3	15.1	
1.00 to 1.24	2.6	1.4	16.3	33.8	38.8	7.1	100	2.5	5.0	5.5	
1.25 to 1.49	3.7	1.2	16.9	30.6	35.6	12.0	100	3.4	7.2	7.0	
1.50 to 1.99	2.8	0.9	13.1	23.7	41.0	18.6	100	6.8	11.1	11.4	
2.00 to 2.99	1.7	0.5	9.9	16.8	45.7	25.4	100	17.7	21.4	24.5	
3.00 or Greater	1.1	0.4	5.0	8.4	28.0	57.2	100	64.4	40.0	36.5	
Whole Category Share	1.6	0.6	8.1	13.6	32.7	43.6	100	100	100	100	

Source: March 2003 CPS outgoing rotation groups. Weighted sample of workers includes all non-military, non-self employed workers ages 16-64 in each year. Calculations based on wage reported for currently held job and income reported for 2002. | \* Assumes no change in employment status or hours worked.

The majority of the working poor are not helped by a minimum wage hike and the vast majority of those who are helped do not live in poor families. The reason for this is that only 5.3 percent of all workers live in poor families and only 5.9 percent of all workers live in near-poor families (those with an income-to-needs ratio between 1.0 and 1.5). More minimum wage workers live in families with incomes three times the poverty line or more (40.0 percent) than live in poor or near-poor families combined (27.5 percent). Hence, raising the minimum wage from \$5.15 to \$7.00 will be extremely ineffective in reducing poverty among America's families.

The final column in Table 1 shows the distribution of benefits from the minimum wage hike. The reported benefits assume no work-

ers lose their jobs or have their work hours reduced. We find that workers in poor families receive only 15.1 percent of the benefits from an increase in the minimum wage, while workers in families with incomes twice the poverty line or more receive over 60 percent of the benefits.

But minimum wage increases will cause some workers to lose their jobs. Evidence by Burkhauser, Couch, and Wittenburg (2000) suggests that young African Americans, young non-high school graduates, and teenagers are most likely to lose their jobs as a result of a minimum wage hike. A 10 percent increase in the minimum wage causes an 8.5 percent decline in the employment of African-Americans (aged 16-24), a 5.7 percent reduction in teenage (aged 16-19) employment, and

an 8.5 percent decline in non-high school graduate employment (aged 20-24).<sup>7</sup>

Hence, our estimates of the benefits of an increase in the minimum wage are likely upper-bound estimates. We present the “best case” scenario for reducing poverty by assuming that workers’ employment status and hours remain the same. And even using these optimistic assumptions, we find that increasing the minimum wage is a poor policy mechanism to reduce poverty.

Table 2 shows the demographic characteristics of workers affected by an increase in the minimum wage. Nearly 64 percent of minimum wage workers are not the highest earner in their family. Most are second earners, but some are third earners, often dependent teenagers. Among the 36.4 percent of high earners who earn the minimum wage, 11.6 percent are

unmarried individuals who live in a single person “family.” A further 6.8 percent have no children. Only 12.6 percent of minimum wage workers are unmarried women with children under the age of 18.

Table 3 shows that while Senators Kerry and Kennedy are correct that a majority of workers helped by a minimum wage hike are women (62.4 percent), over half of all workers are under the age of 25 (53.3 percent) and over 30 percent are teenagers aged 16 to 19. Moreover, Table 2 shows that the majority of women are not the highest earner in their family.

Taken together, these findings are consistent with Stigler’s assertion of a “fuzzy” relationship between a worker’s wage rate and the economic well-being of the family in which the person lives. Raising the minimum wage for the purpose of reducing poverty will be

Family Type	Total	Male	Female
Not high-earner in family	63.63	24.62	39.01
High-earner, unmarried female with children younger than 18 years old	12.55	—	12.55
High-earner, unmarried male with children younger than 18 years old	5.42	5.42	—
High-earner, family size greater than 1, no children	6.79	2.71	4.08
High-earner, single, family size equal to 1	11.60	4.83	6.77
Whole category share	100	37.59	62.41

Note: Weighted sample of workers includes all non-military, non-self employed workers who earned between \$5.00 and \$7.00 per hour in 2003, based on the March 2003 CPS outgoing rotation group.

**Table 3****Demographic Characteristics of New Workers Affected by an Increase in the Minimum Wage, 2003: Age, Gender, Race**

Age Group	Total	Male	Female	Non-White	White
16 to 19	30.34	14.11	16.23	5.08	25.26
20 to 25	22.96	9.81	13.15	5.86	17.10
26 to 39	22.12	7.30	14.82	7.13	14.99
Over 40	24.58	6.36	18.22	8.65	15.93
Whole Category Share	100	37.59	62.41	26.72	73.28

Note: Weighted sample of workers includes all non-military, non-self employed workers who earned between \$5.00 and \$7.00 per hour in 2003, based on the March 2003 CPS outgoing rotation group.

largely unsuccessful for two key reasons: (1) most workers in poor families earn more than \$7.00 per hour, and (2) most minimum wage workers live in non-poor families. Thus, even under the “best case” scenario of individuals continuing to work the same number of hours after a minimum wage hike, the policy will not achieve the stated goal of poverty reduction because it is target-inefficient.

### **The EITC: An Effective Alternative to the Minimum Wage**

The Earned Income Tax Credit (EITC) is a far better policy tool than the minimum wage for rewarding low-wage workers who live in poor families. For every dollar in wages earned by a low-income family with two children, the federal government provides a tax credit of 40 cents.<sup>8</sup> Workers with one child have an effective minimum wage of \$6.90 per hour (the \$5.15 per hour minimum wage plus an additional 34 percent credit of \$1.75) and workers

with two or more children have an effective minimum wage of \$7.21 per hour (the \$5.15 minimum wage plus an additional 40 percent credit of \$2.06).

Evidence by Burkhauser, Couch, and Glenn (1996) suggests that, unlike a minimum wage hike, an increase in the EITC primarily benefits workers in poor or near-poor families. The rules of the program ensure this. Unlike the minimum wage, which is based solely on a worker’s hourly wage rate, the EITC is based on family income. Hence, all of the families in poor or near-poor families in Table 1 would benefit from the EITC.

A worker earning more than \$7.00 per hour but who lived in a low-income family would gain nothing from a minimum wage hike, but would be eligible for additional EITC benefits. Additionally, because employers do not directly pay for the EITC—as they do for the minimum wage—there will be no reduction in employers’ demand for low-skilled workers.

## Conclusion

Senators Kerry and Kennedy's recent proposal to raise the federal minimum wage from \$5.15 per hour to \$7.00 per hour is trumpeted by proponents as a means to lift the working poor out of poverty. The perception remains that most minimum wage earners are single mothers living in poor families. But as Mark Twain once noted, "The trouble with the world is not that people know too little, but that they know so many things that ain't so."

The vast majority of Americans who would gain from a minimum wage hike are not the highest earner in their families—they are second or third earners. And only 13

percent are single women with young children. Moreover, most workers from poor families earn more than \$7.00 per hour and 40 percent live in families with income-to-needs ratios greater than 3.00.

Our evidence suggests that raising the federal minimum wage will be ineffective in raising the working poor out of poverty because such a policy is not target-efficient. The minimum wage is an anachronism with respect to redistributing income and/or protecting workers against poverty. Policymakers wishing to help the working poor should focus on expanding the EITC, a far better mechanism than the minimum wage to help the working poor.

**Appendix A****Average Hours, Weeks, and Potential Wage Increase of Workers Affected by the Change in the Minimum Wage Law, 2003**

<b>Income-to-Needs Ratio</b>	<b>Average Hours per Week</b>	<b>Average Weeks per Year</b>	<b>Average Difference Between Current Wage and \$7.00</b>
Less than 1.00	29.46	38.59	1.02
1.00 to 1.24	30.75	40.88	1.08
1.25 to 1.49	30.92	45.48	0.92
1.50 to 1.99	30.96	42.99	1.01
2.00 to 2.99	29.63	44.05	1.01
3.00 or greater	25.04	40.41	1.02
All Households	28.07	41.58	1.01

Note: Weighted sample of workers includes all non-military, non-self employed workers who earned between \$5.00 and \$7.00 per hour in 2003, based on the March 2003 CPS outgoing rotation group.

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## Endnotes

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2. Stigler, George J. 1946. "The Economics of Minimum Wage Legislation," *American Economic Review* 36: 358-365.
3. Burkhauser, Richard V., Kenneth A. Couch, and Andrew J. Glenn. 1996. "Public Policies for the Working Poor: The Earned Income Tax Credit versus Minimum Wage Legislation," *Research in Labor Economics* 15: 65-109.
4. We define workers who earn between \$5.00 and \$6.99 as minimum wage workers. That is, we assume workers who report earning \$5.00 and \$5.14 per hour are "covered" workers who have underreported their wage rate. We repeated the analysis, excluding these workers, and the results were similar to those reported above.
5. Census estimates indicate that approximately 5.3 percent of private sector workers are employed in "uncovered" jobs.
6. *Ibid.*
7. Burkhauser, Richard V., Kenneth A. Couch, and David C. Wittenburg. 2000. "Who Minimum Wage Increases Bite: An Analysis Using Monthly Data from the SIPP and CPS," *Southern Economic Journal*, 67 (1): 16-40.
8. Some states have earned income credits that supplement the federal rate. For instance, in the state of New York, workers who qualify for the EITC gain an additional 12 cents per dollar in wages.

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## Selected Publications

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- Helping Working-Poor Families: Advantages of Wage-Based Tax Credits Over the EITC and Minimum Wages**, by Dr. Thomas MaCurdy, Stanford University, and Dr. Frank McIntyre, Brigham Young University, April 2004.
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- Welfare Reform and Its Effects on the Dynamics of Welfare Receipt, Employment, and Earnings**, by Dr. Peter Mueser and Dr. Kenneth R. Troske, The University of Missouri, September 2003.
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