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A PANDEMIC MAY BE A RISKY TIME FOR A HIGHER MINIMUM WAGE

Pandemic's outsize hit to sectors where wages and productivity are low heightens risks of sharp rise in the minimum wage.

By Greg Ip
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The US labor market has been through more turmoil lately than at any time in modern memory. Total employment is down by 10 million from February 2020, predominantly among low-wage workers. The pandemic is sorting employers into winners and losers, boosting some such as those in e-commerce at the expense of small bricks-and-mortar retailers.

Is this the time for a major intervention in the labor market? Democrats think so: They are pushing to double the federal minimum wage from $7.25 an hour to $15 by 2025 and then index it to the median wage. While the Senate is unlikely to keep the proposed higher minimum wage in the current Covid-19 relief legislative package, President Biden will likely keep looking for alternative ways to act.

To advocates, an increase is more urgent because the coronavirus pandemic has fallen so hard on low-paid workers who can't work remotely. Jobs in food preparation and serving, personal care and service, where the median wage ranges from $11 to $13 an hour, plummeted 23 percent in the year through January, compared with a 5 percent drop for all occupations.

Yet that also makes a big minimum-wage boost now especially risky. Pay is low in these industries because productivity, as measured by revenue per employee, is also low. The pandemic has further hurt revenue by devastating demand and adding capacity restrictions, testing and disinfection requirements. A higher minimum will bite those employers much more deeply than usual, while largely sparing those where business has boomed, such as big-box retailers.

Several decades of research indicate that moderate increases in the minimum wage reduce poverty while causing little job loss. Those findings may be less applicable to the present. The magnitude of the proposed increase and the uncertainty around the economic backdrop have little precedent.

"It was a lot easier to be sanguine about the effect of raising the minimum wage when you were in a tight labor market with rapidly rising earnings at the bottom," said David Autor, an economist at the Massachusetts Institute of Technology who studies disparities in work and pay. "It's a lot harder to be sanguine now."

The last federal minimum-wage increase coincided with the deep 2007-09 recession. Jeffrey Clemens, an economist at the University of California, San Diego, compared how employment fared in states where the policy raised wages with states where it didn't because the local minimum wage was already higher. He concluded the increase significantly hurt employment among high-school dropouts aged 16 to 30.

Larry Mishel, an economist at the liberal Economic Policy Institute, counters that in its early stages, the current proposal will affect few employers because low-end wages are already higher in most states. By 2023, when the minimum wage is scheduled to reach $12.50, unemployment is projected to be quite low. “By the time it starts to bite, we won’t be in a recession any more,” he said.

Still, over the long term the pandemic will still create what economists call a “reallocation shock,” shifting activity from some regions and sectors to others. For example, Mr. Autor says business travel likely won’t return to its pre-pandemic level, depressing employment throughout its ecosystem of hotel staff, limousine drivers, and dry cleaners in big cities.

The pandemic has accelerated the shift of activity from the physical to the digital realm, from shopping malls to e-commerce, from theaters to streaming video. Digital businesses invest heavily in technology to deliver their products with fewer employees. It is no surprise that Amazon.com Inc. backs a boost in the federal minimum wage to $15: its sales per employee are far above other retailers’, so it can afford to pay more.

Research has found that employers respond to a higher minimum wage in a number of ways. Some had enough control over local labor markets before the increase to underpay workers; those will absorb the higher wage in their profit margins. Some will pass it on through prices. A recent study by Orley Ashenfelter and Štěpán Jurajda found that McDonald’s restaurants that raised pay because of local minimum wages between 2016 and 2020 didn’t tend to close stores or invest more in labor-saving technology such as touch-screen ordering kiosks. Rather, they raised prices.

But Mr. Clemens said companies avoid overhauling their business models when times are good; that changes in recessions when survival is at stake. “The fact the restaurant sector is going to be building itself back up from the ashes of the pandemic means a lot of those choices will be made afresh. I’d expect to see a larger minimum wage increase met with a more substantial shift towards online retail, or . . . relying less on low paying jobs.”

Indeed, a 2012 study found that 88 percent of the loss of routine, middle-skill jobs since the 1980s has occurred in and around recessions. Separately, the McKinsey Global Institute noted robot installations shot up after the 2007-09 recession and expects a similar rush to labor-replacing technology now. The firm conducted a survey that found 68 percent of executives world-wide accelerated investment in automation and artificial intelligence since the Covid-19 outbreak began.

This doesn’t kill the case for a higher minimum wage; much of this investment will happen anyway, and a higher minimum wage could ensure workers share in some of the benefits. It does argue for examining whether alternatives, such as a later or longer phase-in or enhanced aid for the working poor could reduce poverty as much with fewer unintended consequences.