EMPLOYMENT POLICIES INSTITUTE

The Employment Impact of a Comprehensive Living Wage Law

Evidence From California

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Introduction

The concept of a "living wage" is rapidly gaining support in city councils and county governments across the nation. In most areas, the idea behind this movement is that contractors who receive public funds as payment for their services should in turn be required to pay wage rates of at least $7.50 to $14.50 per hour — rates that are far higher than the federal minimum wage. More than two dozen cities have implemented living wage requirements, and dozens more are debating such proposals today.

At the end of 1998, pressured by organized labor and related special interests, the city of San Jose passed a $10.75 per hour "living wage" that applies to employees of firms receiving municipal tax assistance or doing business with the city. This wage level represents a 109% increase over the federal minimum wage. At the time the bill was passed, San Jose set the standard for the highest wage mandate in the country.

Living wage advocates have plainly stated that their ultimate hope is to implement policies that extend beyond municipal boundaries and cover all employers, not just those with municipal contracts. **This report takes the first step toward answering the logical question: if living wage advocates reach their goal, what would be the employment consequences?**

Guiding Methodology

Current research on the effects of living wage mandates is difficult to find, largely because the living wage movement (which began in earnest just four years ago) is so young. For guidance, policy makers often must turn to research on the minimum wage. In March 1998, for instance, the Employment Policies Institute published a study by Florida State economist Dr. David Macpherson on the overall economic impact of the 1998 California minimum wage increase from $5.15 to $5.75 per hour. The results indicated more than 25,000 lost job opportunities, approximately $230 million in lost annual California worker income and $790 million more per year in labor costs.

If an 11% hike creates such substantial costs, what would happen if the California State Assembly were convinced that *all* employers should pay their workers a minimum "living wage" of $10.75? What would happen to entry-

Living Wage advocates, in their own words …

"Let us consider then, a more ambitious aim: to create a living wage policy with... a national scope."

Robert Pollin
and Stephanie Luce
The Living Wage, page 166

level employment levels across California? Who would be most affected? How much would labor costs rise? How much income would laid-off workers lose?

Drawing on Dr. Macpherson's methodology for estimating the potential effects and distribution of an increase in the California minimum wage, the Employment Policies Institute has calculated the potential effects of a statewide $10.75 minimum wage in California.

A $10.75 Minimum Wage: How Many Workers Would be Laid Off?

An important effect of any potential minimum wage increase is that some workers would lose their jobs because firms would no longer be able to profitably employ them. To estimate the job loss, the following procedure was used: First, the fractional wage gain due to the potential minimum wage increase is computed for each affected worker and then averaged across the sample. Second, the estimated fractional wage gain is used in the following formula to calculate the employment loss:

(1) Employment = Fractional Wage * Affected Worker * Labor Demand
    Loss   Gain   Employment   Elasticity

This study uses an estimate of labor demand elasticity (–0.22) for minimum wage workers reported by Neumark and Wascher (1998). An elasticity of –0.22 implies that a 10% increase in wages results in a 2.2% decrease in employment of the affected group.[1]

Table 1 presents the results of these calculations for all of the affected workers as well as for subgroups of workers. Overall, the analysis indicates that 612,783 workers are projected to lose their jobs should the California minimum wage increase to $10.75. The breakdowns by demographic groups and location are not surprising: 39.4% have not finished high school; 36.4% are under age 25; 43% have a family income below $20,000 a year; and 48.9% are Hispanic. Slightly less than one-half (49.2%) of the job losses (301,638) would occur in the Los Angeles area and another 15.3% would occur in the San Francisco region.

The results by industry indicate that just under one-third (29.3%) of the projected job losses would occur in the retail trade industry (179,479 jobs). This is not surprising since more than one-half of the workers in retail trade would be affected by this increase. Another 199,750 jobs, or 32.5% of the projected losses, would occur for workers in the service industries.

The findings by occupation show that 41.8% of the losses are predicted to be for those in sales and service occupations. Another 29.2% would occur for those in blue-collar jobs.

A $10.75 Minimum Wage: What Would Be the Cost to Employers and the Income Loss to Laid-off Workers?

Another critical issue would be the cost to employers arising from the minimum wage increase. These higher costs would be either passed on to consumers through higher prices or there would be reductions in firm profits. Also, an important cost to workers would be the loss in income due to the layoffs caused by the potential $10.75 minimum wage.

These costs are calculated in the following manner: First, the increase in labor costs that would occur if no workers are laid off is calculated. This figure is estimated by multiplying the annual increase in wages due to the minimum wage increase times the number of affected workers. Second, the lost income to workers (and thus reduction in labor cost) due to the layoffs is estimated.[2] This number is calculated by multiplying the number of workers who are projected to lose their jobs times their average wage before the minimum wage increase. Third, the net increase in labor cost to employers is calculated by taking the difference between the cost to employers if no layoffs occurred and the reduction in costs due to the layoffs of employees.

Table 2 presents the results of these calculations. The first row of the table indicates that if no layoffs occurred, then the cost of labor to employers would rise by $31.09 billion. The projected worker layoffs of 612,783 would cause $8.3 billion of worker income to be lost. The potential net rise in the cost of labor to employers is estimated to be $22.8 billion.

The results by industry and location indicate these costs would clearly be concentrated in certain industries and locations. In the retail trade industry, net labor costs would rise by $5.7 billion and the income of laid-off workers would be reduced by $2.1 billion. For the service industry, the net employer cost would rise by $7.1 billion and the income loss to displaced workers would be $2.6 billion. The net labor cost to employers in the Los Angeles-Long Beach area would rise by $7.6 billion, while laid-off workers would suffer an income loss of $2.8 billion. For the entire Los Angeles region, the employer costs would rise by more than $11.3 billion, while laid-off workers would have a projected $4.2 billion reduction in income.

A $10.75 California Minimum Wage:

More than 612,000 lost jobs—179,000 in retail alone. Who would they be?

■ 66.3% would have a high-school education or less. These workers have limited job prospects due to lower relative skills and a lack of educational attainment;

■ 63.6% would be adults aged 25 or older, meaning they would be atypical of "usual" minimum wage workers and more likely to have dependents;

■ 43.0% would have a family income below $20,000 per year;

■ 48.9% would be Hispanic;

■ 49.2% live in the Los Angeles area.

Summary and Conclusions

This report examines in a variety of dimensions the effects of a potential rise in the California minimum wage from $5.15 to $10.75. While this hypothetical jump in the wage floor is large, a $10.75 minimum wage has already been implemented for some employers in San Jose. Moreover, living wage advocates have acknowledged that their ultimate goal is a national living wage mandate.

Two main conclusions can be drawn from this report. First, the minimum wage increase could cause 612,783 workers to lose their jobs, with approximately one-third of the job losses in the retail trade industry. This would cause an annual income loss to all affected workers of $8.3 billion. Second, the cost to employers would be quite substantial. The wage mandate would raise labor costs by $22.8 billion per year (even after adjusting for reduced employment), with the costs concentrated in the retail and service industries.

Lost in the living wage debate is the fact that failing to acquire even basic skills can mean a significant decrease in earnings potential. Many low-skill workers develop these skills at entry-level jobs often at the minimum wage. As their skill base increases, so do their wages. Enacting ultra-high "living wages" means denying low-skilled workers the skill-building opportunities they need to make a "living" for themselves and their families.

Table 1: Employment Levels and Potential Job Losses by Sector

Group	Employment		Projected Job Loss	Percent of all Job Loss
	All Workers	Affected Workers		
All	12,511,029	5,198,803	612,783	100.00%
Industry:				
Agriculture	386,707	300,485	45,632	7.40%
Mining	30,083	4,344	500	0.10%
Construction	571,434	187,668	18,402	3.00%
Durable Manufacturing	1,359,191	451,463	45,247	7.40%
Nondurable Manufacturing	792,055	382,782	52,204	8.50%
Transportation, Communication, and Utilities	904,967	240,748	19,823	3.20%
Wholesale Trade	557,905	216,694	21,711	3.50%
Retail Trade	2,010,420	1,292,377	179,479	29.30%
Finance, Insurance, and Real Estate	784,757	242,735	20,139	3.30%
Business and Repair Services	985,838	431,380	49,821	8.10%
Personal Services	487,350	337,208	45,506	7.40%
Entertainment and Recreation Services	352,009	169,602	22,027	3.60%
Other Professional Services	2,691,069	838,856	82,396	13.40%
Public Administration	597,244	102,461	9,894	1.60%
Occupation:				
Executives, Administrators, and Managers	1,753,810	263,191	22,664	3.70%
Professionals	1,883,690	270,369	23,306	3.80%
Technicians	433,006	77,623	5,864	1.00%
Sales Occupations	1,382,641	687,435	92,313	15.10%
Administrative Support Occupations	1,972,404	923,094	77,542	12.70%
Service Occupations	1,735,037	1,174,773	163,848	26.70%
Farming, Forestry, and Fishing Occupations	401,443	318,467	48,958	8.00%
Precision Production, Craft & Repair Occupations	1,186,048	398,383	38,316	6.30%
Machine Operators, Assemblers, and Inspectors	788,911	528,158	73,740	12.00%
Transportation and Material Moving Occupations	468,073	216,859	21,772	3.60%
Handlers, Equipment Cleaners, Laborers	505,966	340,451	44,460	7.30%
Age:				
16-19	569,834	491,670	85,474	13.90%
20-24	1,398,764	1,059,887	137,624	22.50%
25-29	1,704,975	809,033	86,340	14.10%
30-39	3,711,892	1,320,925	142,101	23.20%
40-64	4,910,883	1,414,121	148,771	24.30%
65-99	214,681	103,167	12,473	2.00%

Group	Employment		Projected Job Loss	Percent of all Job Loss
	All Workers	Affected Workers		
Family Income:				
< $10,000	848,810	658,272	100,411	16.40%
$10,000-$19,999	1,641,208	1,257,022	163,164	26.60%
$20,000-$29,999	1,751,911	994,806	113,235	18.50%
$30,000-$39,999	1,710,538	705,484	73,444	12.00%
$40,000-$49,999	1,370,634	465,052	45,489	7.40%
$50,000-$50,999	1,288,496	376,581	38,690	6.30%
$60,000-$74,999	1,288,995	299,074	29,355	4.80%
$75,000 or more	2,525,573	462,053	48,994	8.00%
Location:				
Non-Metro/Small Metro Areas	667,242	240,741	30,389	5.00%
Los Angeles CMSA				
Los Angeles-Long Beach PMSA	3,546,083	1,642,466	201,237	32.80%
Riverside-San Bernardino PMSA	950,352	391,097	44,530	7.30%
Orange County PMSA	1,188,629	470,477	55,871	9.10%
San Francisco CMSA				
Oakland PMSA	904,977	256,297	25,799	4.20%
San Francisco PMSA	800,163	258,117	27,596	4.50%
San Jose PMSA	786,920	250,962	26,468	4.30%
Other San Francisco PMSAs	389,449	131,825	13,845	2.30%
San Diego, MSA	1,038,145	481,296	54,393	8.90%
Sacramento, MSA	647,125	227,769	23,608	3.80%
Fresno, MSA	341,964	157,201	19,062	3.10%
Bakersfield, MSA	226,055	108,563	14,685	2.40%
Stockton, MSA	177,093	83,093	10,426	1.70%
Other MSAs	865,556	527,995	65,797	10.70%
Gender:				
Male	6,829,259	2,656,500	312,853	51.10%
Female	5,681,770	2,542,303	299,930	48.90%
Race:				
White	10,134,758	4,225,371	502,879	82.10%
Black	804,936	324,280	35,995	5.90%
Asian	1,289,907	500,402	55,014	9.00%
Other Race	281,428	148,750	18,894	3.10%
Ethnic Status:				
Hispanic	3,567,550	2,264,349	299,657	48.90%
Non Hispanic	8,943,479	2,934,454	313,126	51.10%
Years of Schooling:				
0 to 8	1,025,014	809,015	119,515	19.50%
9 to 11	1,095,440	807,213	122,070	19.90%
12	2,972,718	1,495,087	164,919	26.90%
13 to 15	4,079,125	1,597,086	165,124	26.90%
16 or more	3,338,732	490,402	41,154	6.70%

Table 2: Cost to Employers and Lost Income to Workers of a Potential $10.75 California Minimum Wage

Group	Rise in Labor Cost if no Layoffs of Workers	Lost Income due to Layoffs	Net Rise in Cost of Labor to Employers
All	$31,099,948,151	$8,316,415,157	$22,783,532,994
Industry:			
Agriculture	$2,739,420,983	$664,962,021	$2,074,458,962
Mining	$27,101,846	$7,100,971	$20,000,875
Construction	$1,022,173,517	$279,914,889	$742,258,628
Durable Manufacturing	$2,750,436,588	$733,815,701	$2,016,620,887
Nondurable Manufacturing	$2,825,202,199	$734,444,602	$2,090,757,597
Transportation, Communication, and Utilities	$1,187,003,552	$324,110,224	$862,893,328
Wholesale Trade	$1,266,575,444	$350,024,559	$916,550,885
Retail Trade	$7,854,055,213	$2,131,163,920	$5,722,891,293
Finance, Insurance, and Real Estate	$1,112,606,469	$305,783,918	$806,822,551
Business and Repair Services	$2,654,919,079	$705,767,831	$1,949,151,248
Personal Services	$2,180,894,810	$559,159,095	$1,621,735,715
Entertainment and Recreation Services	$954,439,714	$271,657,584	$682,782,130
Other Professional Services	$3,993,995,814	$1,098,234,197	$2,895,761,617
Public Administration	$531,122,923	$150,275,645	$380,847,278
Location:			
Non-Metro/Small Metro Areas	$1,457,149,802	$403,392,845	$1,053,756,957
Los Angeles CMSA			
Los Angeles-Long Beach PMSA	$10,461,583,371	$2,799,030,681	$7,662,552,690
Riverside-San Bernardino PMSA	$2,224,471,703	$619,290,932	$1,605,180,771
Orange County PMSA	$2,791,195,387	$743,558,382	$2,047,637,005
San Francisco CMSA			
Oakland PMSA	$1,293,195,331	$363,910,546	$929,284,785
San Francisco PMSA	$1,449,419,152	$390,666,793	$1,058,752,359
San Jose PMSA	$1,350,824,299	$375,929,563	$974,894,736
Other San Francisco PMSAs	$751,808,555	$205,252,759	$546,555,796
San Diego, MSA	$2,650,268,542	$731,652,778	$1,918,615,764
Sacramento, MSA	$1,201,454,633	$339,501,523	$861,953,110
Fresno, MSA	$1,001,302,777	$267,099,342	$734,203,435
Bakersfield, MSA	$772,631,830	$202,329,483	$570,302,347
Stockton, MSA	$467,991,717	$131,032,361	$336,959,356
Other MSAs	$3,215,893,113	$869,422,429	$2,346,470,684

Endnotes

[1] The average elasticity reported by a survey of labor economists at leading universities is -0.21. See Fuchs, Krueger and Poterba (1997).

[2] Workers may reduce this income loss if they are able to obtain employment in a job not covered by the new minimum wage.

References

Fuchs, Victor R., Alan B. Krueger and James M. Poterba. *Why Do Economists Disagree About Policy? The Roles of Beliefs About Parameters and Values*. NBER Working Paper No. 6151, August 1997.

Hirsch, Barry T., and David A. Macpherson. *Union Membership and Earnings Data Book: Compilations from the Current Population Survey* (1997 edition). Washington, D.C.: Bureau of National Affairs, 1997.

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Data Appendix

Hourly Wage

This study uses data from the January 1995 through October 1997 Current Population Survey (CPS) Outgoing Rotation Group (ORG) files. The main sub-sample of the CPS data employed here includes wage and salary workers who are residents of California, 16 years of age or older, and whose hourly wage is between $5.15 and $10.75 in March 1998 dollars.

The hourly wage is constructed to account for problems caused by workers with variable hours, "top coded" or "capped" earnings, tips, commissions and overtime, inflation and changes in the minimum wage.

The first step is to assign a wage for workers who don't have these difficulties. Non-top coded workers who are paid by the hour and don't receive tips, commissions or overtime are assigned their reported hourly earnings. For all non-hourly workers, the hourly wage is constructed by dividing usual weekly earnings (which includes tips, commissions and overtime pay) by usual hours worked per week.

The second step is to estimate usual weekly earnings for workers whose weekly earnings are top coded or capped at a maximum value. The CPS ORG files have a topcode of $1,923 per week or about $100,000 per year for year-round workers. If the earnings of topcoded workers were not adjusted, average earnings would be understated. To estimate the mean earnings of topcoded workers it is assumed that the upper tail of weekly earnings distribution follows a Pareto distribution. These estimated mean values for the CPS ORG files using this approach are presented in Hirsch and Macpherson (1997) by gender and year and are used in this study. The reported 1996 values are assigned for 1997 observations (the values change little from year to year).

The third step is to estimate usual weekly hours for workers who indicate their weekly hours are variable. This is calculated by using the results of a regression model based on a sample of workers that have non-missing data on usual hours worked. The model is estimated by gender and year and includes controls for hours worked in the prior week, full-time status, marital status, years of schooling, age, race and ethnic status, broad occupation, and broad occupation interacted with full-time status. The parameters from this regression model are then used to estimate the usual hours for those whose weekly hours are variable.

Living Wage advocates, in their own words …

"What is needed, as a next logical step, is for the livable-wage demand to be framed at the national level."

Adolph Reed Jr.
The Village Voice
February 11, 1997

The next step is to assign a wage for hourly workers who receive tips, commissions, or overtime pay or are topcoded workers. In this case, their hourly wage is constructed by dividing usual weekly earnings (adjusted for topcodes) by usual hours worked (or estimated usual hours if usual hours is missing).

The last step is to adjust the wages of workers for inflation and changes in the minimum wage. Wages of workers are adjusted for inflation to March 1998 using the CPI-U (a 3% percent annual inflation rate is assumed for the period between October 1997 and March 1998). For workers whose inflation-adjusted wage is less than $5.15 in September 1997 dollars, a wage of $5.15 in March 1998 dollars is assigned. Workers whose wage at the time of the survey was less than the legal minimum wage were deleted from the sample. The minimum wage for California workers was $4.25 between January 1995 and September 1996; $4.75 between October 1996 and February 1997; $5.00 between March 1997 and August 1997; and $5.15 between September 1997 and October 1997.

Family Income

Family income is reported as categorical variable in the CPS ORG and includes all sources of money income received in the prior 12 months. The income ranges are: less than $5,000; $5,000-$7,499; $7,500-$9,999; $10,000-$12,499; $12,500-14,999; $15,000-$17,499; $17,500-$19,999; $20,000-$24,999; $25,000-$29,999; $30,000-$34,999; $35,000-$39,999; $40,000-$49,999; $50,000-$74,999; and $75,000 and up. To assign a dollar value to these categories, mean values of family income for persons in each income range was calculated from a sample of California residents in the March 1995 and 1996 CPS (which reports family income received in the prior year as a continuous variable). Very similar results occurred when a national rather than a California based sample was employed to generate the mean income values. The 1995 values are used for the 1995 observations, and the 1996 values for the 1996 and 1997 observations.

Annual Income

Though the CPS ORG provides measures of hourly earnings and hours worked, it does not indicate the number of weeks worked per year. Thus, to generate annual income estimates for workers affected by the higher minimum wage, an alternative data source must be used and merged with the CPS ORG. Fortunately, the April 1993 CPS provides such a measure and the mean usual weeks worked was calculated for all California workers earning $5.15-$10.75 per hour in March 1998 dollars.

Location

The CPS ORG used 1983 Census metropolitan area identifiers for January 1995-May 1995 to provide sub-state location information. For the period of June 1995-August 1995, no metropolitan identifiers were provided. Since September 1995, the CPS ORG has used the 1993 Census metropolitan area identifiers. The location identifiers were made as time consistent as possible and the resulting measurement error is quite modest.

Since the months of June 1995-August 1995 contained no location information, these months were deleted from the sample when the sub-state analysis was conducted and the sample weights were adjusted accordingly. As a result, the total employment counts differ slightly for the sub-state and state-level analysis.

The Employment Policies Institute is a nonprofit research organization dedicated to studying public policy issues surrounding employment growth. In particular, EPI research focuses on issues that affect entry-level employment. Among other issues, EPI research has quantified the impact of new labor costs on job creation, explored the connection between entry-level employment and welfare reform, and analyzed the demographic distribution of mandated benefits. EPI sponsors nonpartisan research which is conducted by independent economists at major universities around the country.