November 3, 2014

Councilman David Tandy
Chair, Labor and Economic Development Committee
Louisville Metro Council

Dear Chairman Tandy and Members of the Metro Council:

Thank you for the opportunity to speak to the council's Labor and Economic Development Committee on October 30th about Louisville's proposed minimum wage ordinance. I address, in more detail, a number of questions that arose from the session.

1. Cost of Living

Councilman King asked about cost-of-living adjustments, because prices are lower in Louisville than the nation as a whole. The U.S. Census Bureau's Statistical Abstract of the United States, 2012, publishes cost of living indices for 325 selected urban areas, including Louisville. See https://www.census.gov/compendia/statab/2012/tables/12s0728.pdf .

The publicly available index was for 2010, but there is little reason to think that metro areas have jumped around much in relative terms between 2010 and 2014. The index is weighted such that 13% goes to grocery items, 29% to housing, 10% to utilities, 12% to transportation, 4% to health care, and 32% to other goods and services. These weights seem reasonable. A composite index of 100.0 indicates prices at the national average. Out of the 325 urban areas, Louisville's cost-of-living is the 19th lowest, at 87.68% of the national average. Harlingen, TX has the lowest cost-of-living (at 82.8% of the national average) and unsurprisingly New York, NY has the highest (at 216.66% of the national average).

Not all urban areas are listed (i.e. neither Santa Fe, NM nor Lexington, KY). The table below illustrates Louisville and some cities with citywide minimum wages that I discussed. I located the nearest New Mexico city to Santa Fe (Los Alamos), and include the composite cost-of-living index for it in Exhibit 1:

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Exhibit 1				
Ranking (out of 325 areas)	City	Composite Cost-of-Living Index	Citywide Minimum Wage	Equivalent Minimum Wage in Louisville
19	Louisville, KY	87.68	$10.10 (proposed)	---
270	Los Alamos, NM (for Santa Fe)	109.66	$10.66	$8.52
295	Seattle, WA	121.35	$15.00 (in 2017)	$10.84 (in 2017)
315	Washington-Arlington-Alexandria, DC-VA	140.09	$9.50	$5.95
322	San Francisco, CA	164.05	$10.74	$5.74
Source: 2012 Statistical Abstract of the United States				

Seattle's minimum wage ordinance is not yet in effect; the minimum wage is scheduled to increase to $11/hour in 2015, $13/hour in 2016, and $15/hour in 2017 (See http://murray.seattle.gov/minimumwage/#sthash.7TJJiH7R.dpbs). Of the other citywide minimum wages listed in Exhibit 1, the real, adjusted for cost-of-living minimum wage in Santa Fe is far closer – but still significantly lower – than Louisville's proposal and as discussed below, Santa Fe's ordinances had significant effects on the labor market.

2. Lessons from Santa Fe's Experience

Although no one would argue that Santa Fe's cost-of-living or economy is a perfect comparison for forecasting Louisville's experience, of the limited cities that have citywide minimum wages and where there is credible evidence, it is by far the most comparable. Cities like Lexington, KY, Cincinnati, OH, Indianapolis, IN, Knoxville, TN, St. Louis, MO, or Cleveland, OH would be far better comparisons, but no city within 500 miles of Louisville (except Washington DC) has a citywide minimum wage.

Santa Fe's initial minimum wage implementation in June 2004 provides a compelling case study for the discussion of Louisville. The change was dramatic (a 65% increase, going from $5.15 to $8.50 per hour) and unlike other cities, other confounding labor market policies that affect low-wage workers were not present

(like San Francisco's health insurance mandate or Seattle's paid sick leave mandate). Santa Fe was supposed to implement a $9.50 minimum wage in 2006 and a $10.50 minimum wage in 2008, but the last increase didn't occur. Santa Fe modified a number of provisions (like the minimum wage exception for small businesses, which created a "cliff" for hiring the 25th employee) and then indexed the $9.50 minimum wage for inflation. Had Santa Fe not slowed down their minimum wage schedule, the citywide minimum wage would be approximately $1 per hour higher than the current $10.66 per hour. At the same time, other localities (Albuquerque, Santa Fe County, and the entire state of New Mexico) made changes from the federal minimum wage, making clean comparisons with Santa Fe far more difficult.

There are two sets of studies done on Santa Fe's $8.50/hour implementation. One group (Yelowitz 2005a, 2005b; Pollin and Wicks-Lim 2005) relies on publicly-available data from the U.S. Census Bureau's Current Population Survey, and examines Santa Fe's labor market experience relative to the rest of New Mexico. Another (Potter, 2006) relies on non-public ES-202 data. I discuss both sets of studies below.

A. *Studies relying on the Current Population Survey (CPS)*

Both economists at the October 30th hearing (Drs. Wicks-Lim and Yelowitz) worked with monthly CPS data in their analysis. By reading the abstracts or introductions of the papers, one might think significant differences exist, but a more careful reading shows this is not the case. Yelowitz (2005b) finds that there is complete agreement about the appropriateness of the CPS micro-data set for the analysis of the minimum wage ordinance, the time period analyzed (January 2003-June 2005), the empirical methodology, the included demographic variables, and the inherently flawed approach of observing trends in Santa Fe alone. Most notably, Drs. Pollin and Wicks-Lim independently replicate the large negative effects of the Santa Fe citywide minimum wage ordinance on the labor market. They explicitly present evidence that the probability of unemployment went up by 9.0 percentage points among individuals with 12 or fewer years of education. This compares with the 9.1 percentage point increase found in Yelowitz (2005a). Nor do Drs. Pollin and

Wick-Lim dispute the 3.5 reduction in weekly work hours for this same group. Given the baseline work hours of 38.16 per week, this translates into a 9.2% reduction in full-time equivalent employment.

Given these similarities, where is the disagreement? Is a rise in unemployment a bad thing? As noted by Dr. Pollin in his March 2004 report *before* the Santa Fe minimum wage ordinance went into effect, "Since the purpose or raising minimum wage laws is to improve living standards and create better employment opportunities for the working poor, a rise in unemployment or business flight from the city would obviously be unintended and undesirable consequences of passing such a measure into law." The idea of a high unemployment rate being a measure of the poor health of the labor market is echoed in July 2013 by Dr. Wicks-Lim; see http://www.youtube.com/watch?v=5--Fu76af4Y (around 5 minutes in) where she notes that at the national-level, there does not appear to be a correlation between the inflation-adjusted minimum wage and the unemployment rate.

Despite using unemployment as a measure of poor labor market health both before and after the Santa Fe ordinance in other contexts, Drs. Pollin and Wicks-Lim make the argument in Santa Fe's context that rising unemployment is a sign of improving labor market health and increased opportunities. They note that the unemployment rate is defined by unemployed workers relative to the labor force (those employed plus those searching for a job). If more people search for but are unsuccessful at finding a job, both the labor force participation rate and the unemployment rate rise. Thus, in the Santa Fe context, they interpret rising unemployment in conjunction with rising labor force participation as a sign of a better labor market, not a worse labor market.

Do the numbers support such a conclusion? Using their own analysis (Pollin and Wicks, 2005, Tables 2 and 3, p. 8-9), the answer is no. Table 3 shows that unemployment went up by 9.0 percentage points and labor force participation went up by 5.1 percentage points. However, the increase was not one-for-one; although rising labor force participation explains part of the increase in unemployment, job loss explains an important part as well. To illustrate this, consider Table 2 (column 1). Prior to the minimum wage ordinance,

the Santa Fe adult population with 12 or fewer years of education was 32,199, the labor force participation rate was 70.3% and the unemployment rate was 5.1%. Although Drs. Pollin and Wicks-Lim then compare what happened in Santa Fe in columns (2) and (3) of that table, they do not compare Santa Fe to other cities; thus they are missing other confounding time-series factors (like the growing economy) that mask the true impact of the minimum wage ordinance. Using their own estimates, labor force participation went up by 5.1 percentage points due to the minimum wage ordinance. Thus, it grew from 70.3% to 75.4%, or from 22,631 people to 24,278 people (75.4% x 32,199 adult population), a change of 1,647 participants in the labor force. The unemployment rate went up by 9.0 percentage points due to the minimum wage ordinance. It grew from 5.1% to 14.1%, or from 1,155 people to 3,423 (14.1% x 24,278 labor force participants), a change of 2,268 in the unemployed. By correctly applying the numbers of their model in Table 3, we find that approximately **621 more individuals became unemployed than entered the labor force**. The unemployment rate was driven upwards by both increased labor force participation *and* job loss/layoffs.

B. *Studies relying on ES-202 Data*

In addition to the studies using the CPS, researchers at University of New Mexico (UNM) have conducted a series of studies primarily relying on ES-202 data, a data collection program compiled by New Mexico's Department of Labor. See http://bber.unm.edu/pubs/sflw.htm for a full listing. The most comparable reports examine the minimum wage increase to $8.50 per hour (for example Potter, August 2006). These reports generally find little effect on the labor market, but the UNM reports suffer from some drawbacks relative the CPS analysis.

First, they rely on non-public data. Openness and transparency are critical in these kinds of public policy debates. Yelowitz (2005a, p. 2) states, "The data and STATA programs used in this study are available from the author." Even without using this offer, and with no communication between the authors, Drs. Pollin and Wicks-Lim were able to replicate my findings because the CPS data are in the public domain and

the methods to create the data are transparent. This allows for the healthy back-and-forth exchange in Yelowitz (2005a, 2005b) and Pollin and Wicks-Lim (2005).

Second, and more importantly, the ES-202 administrative data fundamentally limit the questions that can be asked. Recall that CPS studies found negative effects for those with 12 or fewer years of education and no effects for those with more education. The UNM studies do not separate the analysis by less educated workers, presumably because the data do not permit such a distinction. Nor do these studies examine hours of work, an important labor market outcome that responded (with a reduction of 3.5 hours for those with 12 or fewer years of education) in addition to the unemployment rate.

Third, in many of their conclusions, the UNM studies use small businesses (those with less than 25 employees) as a "control group." For example, Potter (August 2006, p. 5, "Executive Summary") states:

> *"The main part of the analysis compares average quarterly earnings over the year prior to the living wage ordinance with earnings after the living wage ordinance. This difference in earnings for employees of large (25 or more employees) Santa Fe businesses is compared with the difference in earnings for employees of large Albuquerque businesses* ***as well as the difference for employees of small Santa Fe businesses****. We are also interested in the number of jobs gained or lost in Santa Fe and Albuquerque, and by looking at the number of workers in the wage file who worked for Santa Fe or Albuquerque businesses during a given quarter, we can examine this aspect as well."*

The logic of using small businesses as a control group is deeply flawed. In this context, by "control group", economists mean a group that would respond in much the same fashion to all other aspects of the economy except that the group is unaffected by the minimum wage policy. Santa Fe's ordinance dramatically affected small businesses, by creating strong incentives for them not to grow. A simple illustration may help. Consider a business with 24 full-time employees, each earning $5.15 per hour. How much does it cost to hire the 25th employee? The Santa Fe ordinance creates a "cliff", because then all employees would be required to be paid $8.50 per hour rather than $5.15. Thus, the cost – in addition to the 25th employee – would be $3.35 per hour x 2000 hours x 24 employees, or $160,800 for the first 24 employees.

Finally, and curiously, the UNM studies – which were largely published after the studies using the CPS, never attempt to replicate the findings with CPS data.

3. Concluding Remarks

Very few analyses of citywide minimum wages exist. My work on Santa Fe – subsequently replicated by University of Massachusetts economists – shows that unemployment went up by 9.0 percentage points and usual hours of work went down by 3.5 hours per week for workers with a high school degree or less. Importantly, 621 individuals became unemployed above-and-beyond the effects on labor force participation.

There is full agreement about what sort of outcomes are desirable for Louisville. Strong job growth, a flourishing population, a vibrant city center, a low unemployment rate, and opportunities for all individuals are things that all policymakers and citizens want. Should Louisville implement a minimum wage to reach these goals? The decision involves considerations related to politics, economics, and morality. The economic evidence is clear: such policies create unintended consequences that harm precisely the groups they are intended to help. A statewide Earned Income Tax Credit better targets working families while avoiding the job loss of minimum wages. Please let me know if I can be of further assistance.

Respectfully,

Aaron Yelowitz