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Minimum Wages and the West Michigan Labor Market

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Recently, President Clinton enacted a rise in the minimum wage. Nonetheless, minimum wage legislation remains controversial. Advocates of the increase argue that it is long overdue since the purchasing power of the current minimum wage is near a historical low. Moreover, they argue that the increase will not hurt the economy. On the other hand, critics of the increase believe the bill will hurt the very people the legislation is supposed to help—low wage workers—since employers will reduce their employment in the face of the mandated higher wage. Also, there is concern that businesses will raise prices to offset their increased costs. Robert Shapiro, an economic adviser to the Clinton campaign, argues, “Businesses don’t simply absorb increased wage costs. They pass them on in the form of higher prices which are regressive because they’re borne equally by all.” Others argue that a “ripple effect” may result, meaning that employers will attempt to maintain the wage structure within the firm by raising the wages of workers who are already above the minimum wage. This ripple effect, if it is significant, would result in further job loss and price increases. What do economists know about the effects of minimum wages? What will be the likely effects on the local economy?

Until recently, there was near universal consensus among economists concerning the employment effects of minimum wage legislation. Basic economic theory suggests that when the wage rises the quantity demanded of labor will fall. Thus, setting a wage floor above the market wage will cause disemployment. This effect should be largest for low wage workers such as teenagers. A long history of empirical studies has confirmed the theory. By the early 1980s the standard estimate was that a 10 percent rise in the wage floor would cause a 1 to 3 percent decrease in teenage employment—that is, an employment elasticity of between −.1 and −.3 (Brown, Gilroy and Kohen, 1982).

Using this estimate, the $.90 increase (a 21% increase) would
Minimum wage legislation is a hotly debated topic. House Republican leader Richard Armey promised to fight an increase "with every fiber of my body." President Clinton, on the other hand, argues that the increase is necessary so that working mothers can feed their children. Both sides overstate the importance of the minimum wage. An increase to $5.15 per hour would still mean that a family of four relying solely on a minimum wage worker would still be below the poverty line. Also, even if we accept the conventional wisdom that generally minimum wages cause disemployment, the proposed minimum wage will have virtually no local employment effect.

References


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**International Business Activity of West Michigan Firms in 1995: Results of First Annual Survey**

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In early 1996, the Seidman School of Business sent a survey to managers of 561 West Michigan manufacturing firms located in Allegan, Kent, Muskegon, and Ottawa counties. The purpose of the survey was to learn how and to what extent West Michigan firms are involved in international sales. We chose manufacturing companies because manufactured goods made up 98% of all exports from Michigan in 1993. Also, manufacturing activity in West Michigan is expanding while it is shrinking in other parts of the country, according to a 1996 report of the Grand Rapids Area Chamber of Commerce. One report suggests that exports from West Michigan increased 81% since 1990, and many firms expect export growth to continue. Nevertheless, exports probably represent no more than 5% of sales of West Michigan firms at this time suggesting that there is potential for increased export activity in the region.

**Demographics.** We mailed the survey to the CEOs of each firm, asking them to give it to the individual who could best respond to questions regarding international business activity. About 100 companies responded to the survey. Most of the companies that responded were located in Kent County (49%), and in Ottawa County (29%). Most companies were small, employing under 150 people (69%), while 4% of companies