Testimony on:
"Why Should Taxpayers Subsidize Poverty Wages at Large Profitable Corporations?"

United States Senate

Committee on the Budget

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Chairman Sanders, Ranking Member Graham, and members of the Committee, thank you for the privilege of appearing today to share my views on the issue of the interaction between the social safety net and the labor market. I wish to make three main points:

- The most recent data suggest that up to 1 in 5 workers receive federal aid in the form of either Medicaid or Supplemental Nutrition Assistance Program (SNAP);
- It is a mistake to assume that these facts imply that firms are subsidized by the taxpayers, as the economics indicate the opposite – the presence of the social safety net forces firms to pay higher wages; and
- Raising the federal minimum wage significantly at this time would be a dramatic policy error.

Let me discuss these in turn.

Workers and the Social Safety Net

The data show clearly that the employed population and those being supported by the social safety net overlap. To illustrate this point, consider Tables 1 through 3 (below), which show the fraction of full-time workers and part-time workers who also participated in Medicaid or SNAP. These data are from March 2018, a time when the labor market was performing well: The unemployment rate was 4.0 percent, and average hourly earnings were growing at a year-over-year rate of 2.8 percent.

The tables differ by the wages received by the workers under consideration. Table 1 shows those workers making $7.25 (the federal minimum wage) per hour or less. Among full-time workers, 20.7 percent were covered by Medicaid and 13.6 percent received SNAP assistance. Table 2 repeats the computations for workers making $10 per hour or less. The rates of program participation among full-time workers fall to 17.5 and 12.3 percent, respectively. Finally, Table 3 raises the threshold to $15 per hour, a level sufficient for a full-time worker to exceed the 2021 federal poverty threshold for a family of four ($26,500). Nevertheless, 14.4 percent of full-time workers were covered by Medicaid and 8.9 percent of workers received SNAP assistance.

Table 1:

Percent of Workers Making $7.25 an Hour or Less that Receive Medicaid or SNAP

	Full-time Workers	*Part-time Workers*
Percent Covered by Medicaid	20.7	20.1
Percent Receiving SNAP	13.6	11.4

Source: Author's computations based on March 2018 Current Population Survey

Table 2:
Percent of Workers Making $10.00 an Hour or Less that Receive Medicaid or SNAP

	Full-time Workers	***Part-time Workers***
Percent Covered by Medicaid	17.5	19.40
Percent Receiving SNAP	12.3	11.9

Source: Author's computations based on March 2018 Current Population Survey

Table 3:
Percent of Workers Making $15.00 an Hour or Less that Receive Medicaid or SNAP

	Full-time Workers	***Part-time Workers***
Percent Covered by Medicaid	14.4	18.6
Percent Receiving SNAP	8.9	11.1

Source: Author's computations based on March 2018 Current Population Survey

The upshot is that many – whether on thinks of 14 percent as "large" is in the eye of the beholder – full-time and part-time workers participate in the federal social safety net. In addition, merely insisting that companies pay "non-poverty" wages will not eliminate this phenomenon.

Does the Social Safety Net Subsidize Employers?

The overlap of the working population and social safety net population documented above is frequently characterized as a "subsidy," with the implication that firms can pay lower wages because of the presence of these government programs.

This is 100 percent wrong.

The reality is that low-wage employers compete with income support programs for the time of workers. If the programs become more generous, the value of not working increases, and employers have to raise wages to attract workers. Far from subsidizing the employers of low-wage workers, the income support raises their cost of doing business. In the process, those programs may contribute to pricing low-skilled workers out of jobs and increasing the incentive to substitute modernization and technologies. This is not an argument against the provision of income support or a social safety net. Even valuable government programs have economic consequences, however, and these should be clearly understood.

This debate is not new; I felt compelled to write a short piece on exactly this topic six years ago. I will not repeat the entire analysis here but will note that the economics of the impact of more generous income support programs on wages and low-wage work are quite simple. Other things being the same, more generous programs will lure some workers or, for others, some part of their current hours of work out of the employment market. This is an entirely understandable and predictable response to having more money. At the same time, restaurants, drinking establishments, retail stores, and other low-wage employers will find themselves competing for a shrunken pool of workers and forced to raise pay to get the employees needed to satisfy their customers.

The empirical estimates suggest that a 10 percent increase in the generosity of the social safety net could force wages to be as little as 0.08 percent, or as much as 1.9 percent, higher. Thus, the data underlying the House Budget Committee report on poverty programs indicate that income support spending – excluding the Earned Income Tax Credit, which has a clear positive impact on labor supply – has expanded by roughly 50 percent since 2003. Using the range (above), this implies that the expansion has driven up wages by anywhere from 0.5 percent to nearly 10 percent. These examples may or may not seem significant, but consider the cumulative impact of small expansions income support by imagining the reverse: a 100 percent elimination of the net. This would generate as much as a 19 percent decline in wages.

In any event, the data and logic indicate that the social safety net does not subsidize employers.

Raising the Minimum Wage to $15 Per Hour

Notwithstanding the data and arguments presented thus far, many people argue that the "solution" to this "problem" is to raise the minimum wage. At present, the most prominent proposal is to raise the minimum wage to $15 per hour by 2025.

The first thing to point out is that the main lesson of Table 3 is that this will not eliminate the phenomenon of workers participating in safety net programs. The second observation is that, as AAF's Isabel Soto puts it: "The consequences of rapid, large increases to the federal minimum wage are well documented, with much of the research finding negative employment effects. The Congressional Budget Office, for example, projected that an increase to a $15 minimum wage by 2025 could mean an average of 1.4 million jobs lost, a fall in business revenues leading to a $9 billion drop in real income, and increases in the prices of goods and services across the economy."

The third important point is that raising the minimum wage is perversely unfair. Who is most likely to get hurt by a minimum wage hike? The relatively inexperienced and least educated who have the weakest skills and lowest pay. Notice that if the president were to sign into law a $15 minimum wage, there would be no additional income available to pay the higher wages. That means to pay the higher wages (for the entry level and those above them who will also get a raise), the money will have to be taken from someone else. If you are the small business owner who now cannot afford to re-open, the money will have taken from you who are out of business and given to someone who has a job. If you are the waiter who will not get recalled because the restaurant decides to re-open with a smaller staff, it is taken from those who are out of work and given to someone who has a job. This outcome is plainly unfair.

The fourth point is that now is a terrible time to raise the minimum wage and to do so would be a grievous policy error. According to Bureau of Labor Statistics data, the industry with the highest percentage of workers earning hourly wages at or below the federal minimum wage is the leisure and hospitality sector. Roughly 60 percent of all workers paid at or below the federal minimum wage were employed in this industry, largely in restaurants and other food services. This is the sector of the economy that has been most damaged by the COVID-19 pandemic.

Employment in leisure and hospitality fell by 8.3 million jobs in March and April, recovered for seven months, and then fell by 498,000 in December. The upshot is that the industry has recovered only 4.4 million, or 53 percent, of the initial job loss. Food services and drinking places employment remains 2.5 million below February's peak. Arts employment remains 797,000 below its peak, and accommodation employment is 674,000 below its peak in December 2019.

These job losses in part reflect the fact that the pandemic has forced many small businesses to close. April 2020 saw the largest percent change in the number of open small businesses,

a 44 percent decline from January 2020. The leisure and hospitality industry saw a nearly 50 percent reduction in open small businesses relative to January 2020.

Raising the minimum wage now would dramatically impede the recovery of this hard-hit sector, diminish the survival chances of hundreds of thousands of small businesses, and end the re-employment prospects of some of the most marginal workers in the U.S. labor market. It would be a step in the wrong direction.

More generally, a Congressional Budget Office study finds that "From 2021 to 2031, the cumulative pay of affected people would increase, on net, by $333 billion." Also, "That net increase would result from higher pay ($509 billion) for people who were employed at higher hourly wages under the bill, offset by lower pay ($175 billion) because of reduced employment under the bill." In short, this is an enormously expensive mandate on the private sector at exactly the wrong time.

Thank you, and I look forward to your questions.