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What Impact, If Any, Will Higher Minimum Wages Have on Retailers and Low-income Workers?

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The struggle to raise pay for low-income workers, once fought in agricultural fields and on factory floors, is moving to the aisles of big retailers in Chicago where large national chains like Wal-Mart and Target may be forced to offer higher wages along with every-day low prices.

While retailers complain the legislation may lead them to stall plans for new downtown stores, Wharton faculty say Chicago's proposed living wage law is largely symbolic and would have little real impact on large retail chains or their employees. "The bottom line is it's feel-good legislation that won't have an effect on firm location or firm costs -- or on low-income families in Chicago, either," says Wharton finance professorRobert Inman.

Under a proposal passed by Chicago's City Council in July, retail chains with sales of more than $1 billion or stores larger than 90,000 square feet will be required to pay workers $10 an hour in wages and $3 in benefits by 2010. Illinois' current minimum wage is $6.50 an hour, while the federal minimum wage -- last increased in September 1997 -- remains at $5.15 an hour.

"It's a bit of a transfer to low-income families, but not significant enough to end poverty in the City of Chicago, if that's what the objective is. I can't imagine it's going to drive any of these stores out of town," Inman adds.

Support for the EITC

In the past decade, more than 140 cities and counties have passed so-called living wage laws -- setting their own hourly wage above the federal minimum -- designed to provide workers with a decent standard of living. The rate of pay and conditions vary from place to place, but most living wage statutes target firms doing business with government.

Eighteen states require employers to pay rates above the federal minimum wage and six states will have ballot initiatives this fall to raise state minimums. The U.S. House of Representatives this summer passed legislation to raise the federal minimum wage to $7.25 an hour, but the measure -- which also included estate tax changes -- was defeated in the Senate.

Some Democrats hope living wage initiatives will provide an added boost at the polls in this fall's mid-term elections. A recent Wall Street Journal/NBC News poll found that 59% of adults surveyed strongly support an increase in the minimum wage to $7.25.

The Chicago legislation focusing on retailers adds a new twist to the living wage campaign, Inman points out. By targeting the large retailers which are beginning to push into urban neighborhoods after saturating suburban and rural locations, it focuses on a single business segment that may have the ability to pay, or little choice not to.

"If you're going to tax somebody, you want to tax people who won't change their decision and will definitely be in that location unless there's a significant change in profitability," says Inman. "This isn't going to affect the profit margins of these stores very much and a presence in Chicago is important to them. I suspect they will make a lot of money by being in Chicago."

Mayor Richard Daley has threatened to veto the measure, but council supporters contend they have the 34 votes needed to override a veto. A study by the University of Illinois found the ordinance would cover 35 stores in Chicago with 16,250 employees.

According to Inman, living wage requirements would have relatively little impact on the so-called big-box retailers because the bulk of their business costs lie in inventory, not labor. However, he says, the impact could be crippling for a small service firm. For example, in many cities where janitorial services have been outsourced to private contractors, small contractors are required to pay high living wages in order to win city contracts.

Wharton management professor Bernard Anderson agrees the living wage is not a very effective tool to address growing wage inequality in the United States. He notes that 25% of all full-time employees earn less than the federal poverty standard of $20,000 a year for an urban family of four. "While low-income workers have been pretty much stuck in their earnings, the price of gas and the price of a lot of other products has increased so that there has been a widening gap in the distribution of income and earnings for the American worker," says Anderson, a former U.S. assistant secretary of labor during the Clinton Administration.

Living wage laws have had little impact because they usually only target small groups of workers, and could have the effect of pushing up wages to the point where employers cut back on hiring. "If you set the wage at a rate that is high, say at $10 or $11 an hour, some low-wage jobs clearly will be eliminated," says Anderson. "Those people won't be lifted out of poverty by earning more. They will be thrown deeper into poverty by losing their jobs."

Anderson argues that a more effective policy tool is the Earned Income Tax Credit (EITC), which exempts low-income workers from federal taxes and provides an additional payment -- up to $4,400 for an individual worker -- paid by the U.S. treasury.

An analysis of 2003 U.S. Census data by the Center on Budget and Policy Priorities found that the EITC lifted 4.4 million people out of poverty, including 2.4 million children. According to the study, EITC reduced the number of Americans with below-poverty disposable income from 35.3 million to 30.9 million.

"Concern about low-wage jobs and the widening distribution of income has been exacerbated by the Wal-Mart phenomenon and I think some of it has been stimulated by unions that have been trying to organize Wal-Mart without much apparent success," says Anderson. "The bottom line for me is that wage policy -- whether it is the minimum wage or the living wage -- is not an efficient device for eliminating poverty."

"Minimum Wage on Steroids"

William Cody, managing director of the Jay H. Baker Retailing Initiative at Wharton, questions why the Chicago legislation singles out retailers, particularly when they are expanding and offering new employment in low-income cities. "Obviously this can be a publicity-driven issue, but when you try to target one class of trade it doesn't seem to make a whole lot of sense."

Marc Freedman, director of labor law policy at the U.S. Chamber of Commerce, says the targeted approach to living wage campaigns only seems to indicate that proponents fear it could backfire and lead to job declines if enacted on a broad scale. "If it's such a great idea, why don't they just apply it to everyone in the city? When they limit themselves, it suggests to me they appreciate the downsides to this idea."

Freedman also objects to living wage laws, as well as minimum wage laws, because they seem to focus on a random number without a sense of how the economics will play out for workers and business. "The living wage is like the minimum wage on steroids. It just tries to up the minimum wage by some other random number. Nobody I've seen yet has set a specific formula. They are just grabbing numbers out of the air that make them feel good."

Paul Sonn, deputy director of the poverty program at New York University's Brennan Center for Justice, says other cities, including Washington, D.C., and Santa Cruz, Calif., are considering similar measures that would focus on retailers, or firms that receive tax breaks or economic development subsidies.

A report issued by the Brennan Center as part of the Chicago City Council deliberations on the ordinance says that Chicago has the authority to single out retailers for a living wage under state Home Rule provisions and other court decisions allowing jurisdictions to take on problems "one step at a time." The report argues that state law permits Chicago to target one industry as part of a larger solution to broad income inequality.

Sonn also argues that the Chicago ordinance complies with a recent Maryland decision in which the court struck down a state law requiring Wal-Mart to provide employee health benefits as a violation of the federal Employee Retirement Income Security Act (ERISA). The Chicago law, he says, tracks other court decisions, including a recent Emeryville, Calif., ruling upholding living wage laws that require the payment of a cash equivalent for benefits. "Maryland's law was a straight health mandate, not a wage law. If you give the option of benefits or higher wages, that is the approach the federal courts have approved," Sonn says.

Wharton marketing professor Stephen J. Hoch contends that retailers should be able to come up with the additional wages and are not likely to walk away from Chicago or other urban neighborhoods with living wage laws. "Why not pay it? Chicago is a big city and it's expensive to live there," he says. "The arguments about not raising the minimum wage seem ridiculous seeing as it hasn't changed in so many years."

Hoch stresses that since the legislation would apply to all big-box retailers, no one chain would be at a disadvantage. "The standard argument by the retailer is that they can't afford to do it, but if everybody has to, then the playing field is level."

He notes that some retailers, including Costco and Trader Joe's, already pay higher wages and offer employee-benefit packages. "Costco has been criticized by Wall Street but that's their competitive advantage -- they pay more and expect higher productivity."

Hoch also points out that Wal-Mart has been lobbying for an increase in the federal minimum wage, perhaps as a way to reduce negative publicity stemming from union opposition to the company's move into 50 new locations in urban areas and the Northeastern United States. "Wal-Mart recognizes that its competitors would have to pay the same. So why not take some of the heat off them?"

Getting Creative with Real Estate

Following the Chicago City Council vote, Target Corp. wrote a letter to Mayor Daley, threatening to halt plans to build two new stores in Chicago unless the ordinance is vetoed. The response led to protests against Target in Chicago and other parts of the country. The Minneapolis discount retailer, which has enjoyed a relatively good public image especially when compared to Wal-Mart, earned some negative publicity and the nickname "Tar-Mart."

Wal-Mart is scheduled to open its first store within Chicago's city limits, on the West Side, by the end of this year. The company recently opened a unit just over the Chicago border in Evergreen Park, Ill., which drew more job applicants than any other Wal-Mart ever. Wal-Mart stores typically attract 3,000 to 4,000 applicants for every 350 to 400 positions. The Evergreen Park store had 25,000 job seekers.

Wal-Mart has not issued a direct threat to abandon Chicago, but released a statement after the City Council approved the living wage law: "Dozens of communities around ... Chicago already welcome the savings, job opportunities and tax revenue we bring with each store opening. It's sad to see the City Council make this unfortunate choice to stand in the way of these benefits for Chicago's working families."

Cody says Wal-Mart has used various real estate strategies to get around local policies designed to limit its growth. In towns where politicians have tried to block Wal-Mart by restricting store size, the retail chain has simply come in slightly lower than the restriction. "There are ways Wal-Mart can get creative with real estate," he says. "They could build an 89,000-square-foot store for Chicago and make that work."

Or Wal-Mart could just pack up and move to surrounding areas of Chicago where it would be met with open arms. "Ultimately I think the store will open," says Cody, adding that the new Wal-Mart will probably also be mobbed with applicants. "Wal-Mart could try to build a popular case by opening the doors and telling consumers 'You be the judge of whether Wal-Mart should stay.' It could be difficult for local legislators to go against what their constituents want. The consumers will vote with their wallets."