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# Examining the Lack of Consensus on the Minimum Wage

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# Examining the Lack of Consensus on the Minimum Wage

A Thesis Presented to
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Northeastern Illinois University

In Partial Fulfillment of the Requirements
of the NEIU Honors Program
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Belma Ramic
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Examining the Lack of Consensus on the Minimum Wage

This thesis has been reviewed by the faculty of the NEIU Honors Program and is found to be in good order in content, style, and mechanical accuracy. It is accepted in partial fulfillment of the requirements of the NEIU Honors Program and graduation with honors.

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## ABSTRACT

The economic impacts of minimum wage laws have been the subject of debate for over a century within the United States (US). This paper summarizes this and reviews the body of academic literature studying the effects of minimum wage laws, much of which center around their employment effects. This paper also examines how the ongoing debate can be attributed to factors that have not been as comprehensively reviewed, such as disagreements over politics, poverty, and impact on prices. The purpose of this paper is to achieve an understanding of the complexities surrounding the minimum wage and its overall implications. From this research, it is evident that various analyses of the minimum wage exist due to personal biases and interpretations of the data at hand, and therefore, a consensus is not possible.

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TABLE OF CONTENTS

LIST OF TABLES

# INTRODUCTION

The minimum wage is a price floor on workers' hourly wages set by the government. The concept is quite simple in theory but actually has the ability to cause a large ripple effect throughout the economy. The impacts of minimum wage laws on the economy have been studied since it was first implemented federally in 1938 and continue to this day. Confirmed by President Franklin D. Roosevelt during his Statement on the National Industrial Recovery Act (1933), the minimum wage was intended to be a "living wage", meaning more than a bare subsistence level. Effects on employment in particular became the central point of the debate. According to the basic economic laws of supply and demand, increasing the minimum wage above the market rate should result in a surplus of workers and subsequently, an increase in unemployment. This was a widely accepted conclusion until the 1990's when new empirical research on the minimum wage and its employment effects emerged. Economists continued to arrive at different conclusions depending on the methodologies of their studies. The validity of the most well-known studies continues to be challenged. The question of which studies are most valid is a point of contention that contributes to the general debate on the minimum wage. With this honors thesis project, I intend to explore the minimum wage debate to better understand the lack of consensus from an economic and political standpoint. Keeping the original goal of a living wage in mind, I also examine the often overlooked role of poverty in the debate.

This involves a combination of reviewing existing literature and examining how biases play a role in the interpretation of the data.

## HISTORY AND POLITICS OF THE MINIMUM WAGE

The idea of a minimum wage in the United States was a focal point during the progressive era, a period of social activism in the early 1900's. The initial interest behind implementing it was sparked by concerns over harsh labor conditions in sweatshops. Although reformers were interested in a minimum wage that would apply to all workers, they found it most productive to advocate for a minimum wage for women and children. The goal was to end "sweated" labor which was a phrase used to describe hard work for low pay. Massachusetts was the first state to establish its own minimum wage in 1912. Shortly after, several other states followed suit. Table 1 shows the 28 states (sorted by year) that had enacted their own minimum wage between the years of 1912-1937 before the establishment of a federal minimum wage.

The goal of the minimum wage became less clear as arguments used to justify minimum wage laws started to shift in different directions. Sidney Webb (1912) and Matthew Hammond (1915) used information from minimum wages set in Australia, New Zealand, and the United Kingdom to argue that minimum wages provided wage increases without any significant negative consequences. Webb also argued that a minimum wage would increase productivity and result in more efficient organization of labor (Fishback 2021). On the other hand, John Bates Clark (1913), Frank Taussig (1916), A. C. Pigou (1913), and Frank Fetter (1917) argued that a minimum wage would reduce employment and ultimately a reduction of business output. Fetter and Taussig maintained the idea that better education and training would be a more efficient method of preventing poverty. While these arguments were all valid in some form, they addressed different consequences of the minimum wage. Without a single goal in mind, economists were bound to disagree.

*Table 1: State Minimum Wages*

| **State** | **Year Enacted** |
|---|---|
| Arizona | 1917 |
| Arkansas | 1915 |
| California | 1913 |
| Colorado | 1913 |
| Connecticut | 1933 |
| District of Columbia | 1918 |
| Illinois | 1933 |
| Kansas | 1915 |
| Kentucky | 1938 |
| Louisiana | 1938 |
| Massachusetts | 1912 |
| Minnesota | 1913 |
| Nebraska | 1913 |
| Nevada | 1937 |
| New Hampshire | 1933 |
| New York | 1933 |
| New Jersey | 1933 |
| North Dakota | 1919 |
| Ohio | 1933 |
| Oklahoma | 1937 |
| Oregon | 1913 |
| Pennsylvania | 1937 |
| Rhode Island | 1936 |
| South Dakota | 1923 |
| Texas | 1919 |
| Utah | 1913 |
| Washington | 1913 |
| Wisconsin | 1913 |

*Note*. From "The Legislative Background of the Fair Labor Standards Act," by O.W. Phelps, 1939, Chicago: University of Chicago Press. Copyright 2009 by Orme W. Phelps.

Early state-level minimum wage laws were repeatedly challenged by the courts and, as a consequence, states continued to revise their minimum wage laws. Enforcement also proved to be a problem. There was no true enforcement mechanism and there were often not real adverse consequences to employers for noncompliance. The state of Massachusetts, which was the first to implement minimum wage laws, did not enforce compliance. Because laws in other minimum wage states were largely ignored, a federal agreement was deemed necessary. In the 1930's, The Bureau of Labor Statistics showed support for the new state minimum wage laws by declaring that these laws protected "the public health, morals and welfare" after the Great Depression made it clear that unfair wages were a threat to stability (US Bureau of Labor Statistics 1933b, p. 1346).

The legality of early minimum wage laws was also the subject of much debate. The courts made contrasting decisions regarding state minimum wages during the 1930s. In 1936, the U.S. Supreme Court ruled against the 1933 New York minimum wage law in *Morehead v. New York ex. Rel. Tipaldo* (298 US 587 [1936]). In 1937 however, one of the judges that had ruled the New York law unconstitutional and declared that the Washington minimum wage from 1913 was constitutional in W*est Coast Hotel v. Parrish*, a case where a female employee was seeking to be compensated the amount owed to her according to Washington's minimum wage law (300 US 379 [1937]). The judge's reasoning was that women were especially susceptible to exploitation by employers.

The *West Coast Hotel v. Parrish* case demonstrated that the courts were open to ruling in favor of state minimum wage laws targeting vulnerable groups. Consequently, additional states passed minimum wage laws for women and children.

In 1937, the Franklin D. Roosevelt administration first introduced the Fair Labor Standards Act (FLSA). The FLSA was supposed to provide for an initial $0.25 hourly federal minimum wage (equivalent to $4.60 today) that was to gradually increase over time. The act also allowed industry insiders and members of the public to set industry-specific rates as high as 80 cents an hour (Fishback & Seltzer, 2021). Members of Congress were split on their support of the act. President Roosevelt specified that there was a need to end "starvation wages", implying that the minimum wage was intended to do just that. Once the act was passed by the Senate, it languished in the House of Representatives due to arguments between the northern and southern state representatives.

The north and the south were vastly different in terms of occupations, workers, and cost of living. The economics in the North and the South were vastly different in terms of industry, occupations, and the cost living. The North contained more high-wage industrial jobs whereas the South was primarily agricultural with high concentrations in low-wage, low-productivity industries such as textiles and lumber (Levin-Waldman 2000). As a result, a considerable wage differential persisted between the North and South.[1] This differential made it obvious that a federal minimum wage would have varying effects across regions. The South was heavily opposed to a minimum wage for a couple of reasons (Levin-Waldman 2002). The main fear was that a federal minimum wage would raise wages and reduce employment. Wages were already considerably lower in the South compared to the North, so the implementation of a federal minimum wage would disproportionately affect southern employers. It also was seen as an

[1] A wage differential refers to differences in wages between workers with similar skills due to differences in location or industry.

unacceptable government intrusion. Southern politicians feared that minimum wage rates would to as high as 80 cents an hour, a large increase from the less-than-40 cents per hour that many southern workers were earning at the time (Seltzer 1995; Wright 1987). Employers in the North supported the act in hopes that it would eliminate their southern states' competitive wage advantage.

Advocates for a regionally indexed minimum wage came about in order to account for these differences, but this idea also faced opposition. An indexed minimum wage was supposed to account for the wage differential by enacting different, yet proportional, minimum wage rates across the North and South. Congress refused to introduce an indexed minimum wage out of fear that it would lead to inflation (Levin-Waldman 1998). Instead of modernizing upon the introduction of the federal minimum wage, many states in the South passed right-to-work laws in an attempt to maintain lower wages. The idea was that right-to-work laws would impede on the growth of unions (Levin-Waldman 1999). As a compromise to both sides, the Fair Labor Standards Act of 1938 introduced a federal minimum wage of $0.25 an hour and included steady increases over time, industry-specific minimums, and it was applicable to only about half of the workforce at the time (Fishback & Seltzer, 2021). This revised act allowed industry insiders and members of the public to set industry-specific rates as high as 40 cents per hour, thus helping to alleviate the earlier fear of many southern politicians and employers.

At the time of its implementation, the federal minimum wage was broadly supported by the public. According to a January 1939 Gallup poll, 71 percent of survey respondents expressed support for the act (Roper Center, 2020). The initial effects of the minimum wage varied, as a majority of the workers who were covered under the act were earning more than the minimum wage at the time; many other jobs were exempt. According to the US Bureau of Labor Statistics (1951, p. 2), a full-time worker earning the minimum wage in 1940 could not cover the estimated budget for a family of four. Many states responded to this perceived weakness in the federal law by introducing their own minimum wage rates, which were higher than the federal minimum, in order to supplement the national rate.

In 1950, the federal government raised the minimum wage to 75 cents and to $1.00 in 1956. In 1955, President Eisenhower showed support for an increase to $0.90 an hour and he signed a bill into law that raised the minimum wage to $1.00 an hour. Proponents of the minimum wage were largely liberal Democrats while opponents were southern Democrats and some Republicans. The arguments both in favor of and against the minimum wage had changed since circumstances changed. The Great Depression was over and regional wage differentials had diminished.

During the 1940's, economists were mostly in support of raising the minimum wage. It was widely agreed upon that minimum wages would raise wages and employment and improve productivity. George Stigler (1946) however, was one noteworthy economist who argued the opposite. Stigler maintained that the minimum wage was not a method to be used for reducing poverty rates. The major argument in support of the minimum wage in the 1950's was in regards to providing an adequate standard of living for workers. The idea of an adequate standard of living was in line with FDR's idea of eliminating starving wages. Much like Stigler, opponents of the minimum wage during this time argued that the minimum wage was not a solution to the problem at hand. Still, labor effects seemed to remain the crux of the debate. In the 1960's, a general consensus on the minimum wage was becoming more difficult to achieve. Studies by the U.S. Department of Labor that showed no ill effects from minimum wage on employment rates were met with criticism by economists. By the 1960's and 1970's, the primary findings of studies on the minimum wage showed negative employment effects.

From the late 1960's to the 1990's, there was less attention on the minimum wage. In 1981, Ronald Reagan was the first US president to oppose increases to the minimum wage (Fishback & Seltzer, 2021). The minimum wage became a hot topic of debate again in the 1990s after David Card and Alan B. Krueger published studies that showed little to no employment effects upon an increase to the minimum wage. David Newmark and William Wascher responded to Card and Krueger with their own studies that showed opposite findings.

The sudden spur of research on the minimum wage in the 1990's contributed to the uncertainty on the matter that persists to this day. The introduction of empirical data made the debate labor focused more than ever. It is important to factor in the political aspect of the debate since legislation occurs within politics. Politics has been defined by Harold Laswell as who gets what, where, and how (1936). In the context of the minimum wage, this translates to the question of who benefits and who loses from an increase in the minimum wage. If the goal of the minimum wage is to reduce poverty, figuring out who loses from this should be the main objective. Levin-Waldman argues that political disagreements persist because there are no definitive conclusions to be made about who loses (1998). However, the strong partisan divide in the US between Democrats and Republicans has kept this question up in the air. This divide can be demonstrated through examples of minimum wage legislation in individual states involving both parties during the 2000's. According to Johnson (2002), the majority of Democrats in the House and Senate voted for an increase in Hawaii's minimum wage in the early 2000's while the majority of Republicans voted against it. In 2000, a Democratic governor in Alaska had proposed an increase in the minimum wage but it was never passed due to a Republican-dominated legislature. Tensions in political institutions were a result of the partisan divide and varying views on labor legislation.

It is clear that political and economic disagreement surrounding the minimum wage had reached a peak in the early 2000's. A poll from 2015 asked economists whether or not an increase in the minimum wage would result in negative employment effects amongst low-skilled workers. According to the results, 26% agreed, 24% disagreed, 38% were uncertain, and the rest did not provide an answer (IGM Forum, 2020). In 2019, the Congressional Budget Office reported that 60% of workers in the United States reside in states where the minimum wage is higher than the federal minimum of $7.25 an hour (Congressional Budget Office, 2019). At this time, the data shows there is an overall lack of consensus regarding the minimum wage in the United States and many individual states have returned to varying minimum wage rates that surpass the federal rate of $7.25 an hour.

## EMPLOYMENT EFFECTS

The majority of the empirical research studying the minimum wage focuses on its employment effects. While hundreds of studies have been conducted on the minimum wage and its effects on labor, a handful of studies are regarded as being the most influential due to their compelling methodologies and arguments. For the sake of simplicity, the two most common but contradicting studies will be reviewed in an attempt to flesh out the matter.

The general consensus on the minimum wage varied throughout the 1900's. Towards the late 1900's, economists used simple competitive models to argue that raising the minimum wage would cause ill effects on employment and this view became the standard. Frey et al. (1994) reported that almost nine out of ten economists agreed with the statement "A minimum wage increases unemployment among young and unskilled workers". Economists used standard models to support the idea that minimum wage raises lead to unemployment. The supply and demand model assumes a price floor (minimum wage) causes the quantity supplied of labor to exceed the quantity demanded. In the context of labor and a minimum wage, this means that the demand for workers decreases while the supply of workers increases. The resulting surplus of workers translates into a surplus of unemployed individuals in the market. This theory was frequently the basis of arguments against the minimum wage throughout history.

David Card and Alan Krueger challenged this view in the 1990's after publishing *Myth and Measurement*. This paper that investigated the effects of New Jersey's increase in the minimum wage from $4.25 to $5.05 an hour. In 1992, Card and Krueger surveyed fast-food restaurants in New Jersey months before the new minimum wage took effect.

They asked restaurants a series of questions pertaining to employment, staff sizes, and similar information. They repeated the survey months after the new minimum wage took effect. To serve as a control, they did the same to neighboring Pennsylvania which remained at the federal rate of $4.25 that year. The purpose of this study was to attribute changes in employment in New Jersey to the minimum wage raise *if* significant changes were evident. This research was particularly groundbreaking because of its use of empirical research and its findings.[2] Card and Krueger (1995) summarized their findings as “a new body of evidence showing that recent minimum-wage increases have not had the negative employment effects predicted by the textbook model” (p. 1). They also added, “some of the new evidence points toward a positive effect of the minimum wage on employment; most shows no effect at all”. This conclusion contradicts the logic of the simple market model to such a degree that Ehrenberg characterized it as an assault on the law of demand (1995). The study was met with criticism surrounding its methodology and consequently faulty results. Dan Hamermesh (1995) claimed that examining the “before and after” is not appropriate since it fails to address the fact that minimum wage increases are announced ahead of time. This would have given employers time to adjust before the new minimum took effect, making Card and Krueger’s observations void. Finis Welch (1995) argued that the data contained too much random noise for it to be considered valid.

Criticism of Card and Kreuger’s study became more intense when David Neumark and William Wascher directly challenged their findings. Neumark and Wascher obtained payroll records from restaurants in New Jersey and Pennsylvania from before

[2] Empirical research refers to research with conclusions that are drawn strictly from verifiable evidence as opposed to economic models which rely on assumptions.

and after the minimum wage increase. Their data indicated a negative effect on employment. Card & Krueger responded to these findings by interpreting Neumark and Wascher's data and concluding that it supports the conclusion originally reached by Card and Krueger (Card et al., 1994). They went back and forth with their findings and ultimately did not reach an agreement but instead brought more available data to the table for other economists to analyze. All of the studies mentioned have received reasonable amounts of praise and criticisms, indicating that the perceived validity of research on the topic is subjective and susceptible to bias. This is due to the difference in methodological approach used. Neumark and Wascher used all cross-state variation in minimum wages over time to predict effects. Card and Krueger compared neighboring areas with different minimum wages during the time of a policy change. Critics of Neumark and Wascher reject the validity of their studies because "traditional approaches tend to produce spurious negative effects due to spatial hetero geneities in employment trends that are unrelated to minimum wage policies" (Dube et al., 2010). Both studies made an impact in the field of economics but lacked any real influence on policy due to this, raising the question of how change in policy can be made possible if disagreement persists.

Studies completed by these economists are still regularly referenced in research today. The results from the previously mentioned poll by IGM Forum demonstrate how the contrasting findings of Card & Krueger and Neumark & Wascher have contributed to the ongoing uncertainty among economists compared to decades ago, when general consensus on the topic was more common. In more recent years, the most preeminent studies on minimum wage have found limited, small, or no unemployment impact from minimum wage increases. A study by Dube, Lester, and Reich (2010) analyzed an extensive amount of data and found no evidence of negative employment effects. An IGM survey (2013) found that most economists believed the benefits of raising the minimum wage outweighed the costs. The question of how researchers can reliably identify the employment effects of the minimum wage remains. Perhaps it is an indication of the need to switch the topic of conversation to something more relevant to the common goal.

## POVERTY

One can argue that the issue of poverty is more central to the minimum wage debate than employment effects are. President Franklin D. Roosevelt's commitment to end "starvation wages" demonstrates the goal of the minimum wage: to provide a minimum sustenance wage. Although more often studied, employment effects alone do not provide enough information to tell whether or not a minimum wage raise has met its intended goal. It appears that the ideal outcome includes a combination of reduced poverty rates and increased or unchanged employment rates. However, the potential benefits to a minimum wage increase come with a cost according to basic economic theory. The question then arises, "what are the costs?" If it is true that potentially reduced poverty rates come at the cost of lower employment rates (or vice versa), then the minimum wage debate shifts to a separate cost-benefit analysis.

### Poverty Thresholds

To begin to understand the discussion around minimum wage and poverty, it is important to look into how the two are related. Eliminating poverty as a goal of increasing minimum wage is senseless if those who earn minimum wage are not considered to be in poverty to begin with. Poverty thresholds are decided by the U.S. Census Bureau and depend on the size of family unit and children.[3] It is important to note that this data only takes into account earnings in relation to the federal minimum wage. Workers who live in cities with a higher cost of living (and higher minimum wage) could

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[3] Poverty thresholds by size of family and number of children can be found at https://www.census.gov/data/tables/time-series/demo/income-poverty/historical-poverty-thresholds.html

still potentially remain under the poverty threshold even with a federal minimum wage increase.

Assuming an individual made just under the poverty threshold with a minimum wage job, a rise in the minimum wage would not necessarily translate to being lifted out of poverty. Even if it is assumed the minimum wage increase does not lead to a loss of employment for the worker, other factors must be considered. A decrease in hours, for example, could lead to a lower income despite the increase in hourly wage and keep the individual under the poverty threshold. In *Do Minimum Wages Fight Poverty* (1997), Neumark and Wascher (1997) examine the effects of the minimum wage on low income families who are above the poverty line. Perhaps the goal of lifting more families out of poverty is misguided. The current measure of the poverty line by the government is arguably arbitrary. If the minimum wage does indeed lift many families out of poverty, it does not guarantee the "living wage" that was an initial objective. The concept of a living wage as a goal was established by President Roosevelt during his statement on the National Industrial Recovery Act (1933). Roosevelt argued, "no business which depends for existence on paying less than living wages to its workers has any right to continue in this country...and by living wages I mean more than a bare subsistence level-I mean the wages of decent living". More recent empirical studies have found inequality-reducing effects in a range of countries including the U.S. Belman and Wolfson (2014) found that a total of up to 25 percent of employees earning up to 150 percent of the minimum wage benefitted from an increase. A 2004 study of Brazil found evidence of minimum wages reducing wage inequality (Lemos). Although different countries vary in terms of policies and their respective economies, economists can use data from other countries to draw conclusions about minimum wage effects in the U.S.

**Living Wage**

The concept of a living wage is also arbitrary and defined and calculated differently by economists, politicians, the government, and society. In his book *A Living Wage: American Workers and the Making of Consumer Society*, Lawrence Glickman (1997) defines a living wage as “a wage level that offers workers the ability to support families to maintain self-respect and to have both the means and the leisure to participate in the civic life of the nation” (p. 66). This definition must be translated quantitatively in order for it to actually be implemented. The original approach to this from the 1990’s equated a living wage with the federal poverty line. While some are content with this, others would argue that this is outdated and fails to take regional differences into consideration. Organizations more biased towards a higher minimum wage, such as the Economic Policy Institute, form their own estimates based on region and common expenses such as food, housing, and transportation. Proponents of a living wage urge policymakers to also take inflation and productivity into consideration; in 2017, the federal minimum wage had lost about 9.6 percent of its purchasing power due to inflation since it was last raised to $7.25 in 2009 (DeSilver). In 2021, the federal minimum wage remains at $7.25. Opponents reject a living wage on the basis that it is not necessary for a minimum job because minimum wage jobs employ many teenagers. According to the U.S. Bureau of Labor Statistics (2021), 48 percent of workers under the age of 25 make up those who are paid the federal minimum wage or less. Whether or not 48 percent is a significant enough number to support a living wage is subjective. It is clear that the minimum wage is an issue on many levels. Even if legislators can come to an agreement about providing an adequate standard of living, further issues such as exact numbers remain and highlight the intricacies involved in the decision-making process. Whether labor effects or poverty become the central focus of the minimum wage debate, smaller disagreements prevent consensus.

When arbitrary factors such as poverty cutoffs and living wages become a roadblock to consensus, it is possible to analyze the quantifiable impact the minimum wage has solely on incomes for minimum wage earners. Research from Dube, Lester, and Reich (2010) suggests that minimum wage increases significantly increase earnings for minimum wage workers. A study by Harry J. Holzer and Karin Martinson (2006) suggests that there is evidence that high turnover rates are common among low wage earners. This leads us to believe that an increase in the minimum wage would cause some low wage earners to take longer to find a new job rather than it resulting in long term unemployment. If true, an increased hourly rate would make up for the decrease in hours for the worker caused by the short period of unemployment. Assuming the minimum wage does increase earnings for minimum wage workers, whether the increase is sufficient enough remains subjective and up for debate. In the article *The Effect of the Minimum Wage on Prices* (2004), Sara Lemos establishes that the literature lacks studies on the profit and price effects of the minimum wage. Using the literature available, she concludes that most studies find that “a 10% US minimum wage increase raises food prices by no more than 4% and overall prices by no more than 0.4%”. While this is indeed a small effect, it does not entirely negate other potential negative effects of the minimum wage. As demonstrated by many studies, no amount of empirical research on the minimum wage will lead to a consensus due to personal biases and differences in opinion on validity of research.

# CONCLUSION

With the rise of "Fight for $15", a political movement advocating for a $15 federal minimum wage, the minimum wage resurfaced in the arena of public debate. There is general awareness of the minimum wage being a political issue especially with recent elections. However, I would argue that not many people are aware of the scope and length of the debate. There is a long history of politics and research surrounding the debate. What appears to be a simple solution to poverty in the US is actually a combination of many other factors that must be taken into consideration for the sake of economic and political harmony. This research was an attempt to review the relevant literature related to the topic and gain an understanding of why such a debate persists today. I find that a combination of differing methodologies, political objectives, and personal biases are the answer. Table 3 provides a brief synopsis of the history surrounding the minimum wage since the early 1900s. The most recent decades suggest that a consensus is not within the near future.

*Table 2: Timeline of Minimum Wage*

| | |
|---|---|
| 1910-1940 | Concerns over working conditions lead to an interest in the minimum wage. Several States enact their own minimum wage. President FDR enacts first federal minimum wage in 1938. Economists disagree over the effects. The North and the South disagree over the minimum wage due to cost-of-living differences. |
| 1940s | General public and economists show support for the minimum wage. |
| 1950s-1960 | Federal minimum wage is increased throughout the years. The idea of a living wage becomes a major point in the debate. General consensus becomes more difficult to achieve. |
| 1960s-1990 | Primary findings of studies show negative employment effects. Attention on the minimum wage declines. |
| 1990s | A new wave of research begins because of David Card and Alan Krueger's study using empirical research. |
| 2000s-2010s | Uncertainty persists. Polls show disagreement amongst economists. |

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