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Something to Think About

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COMMON CENTS

This week, I read a column written by a man by the name of Cass Sunstein. This man is very much a political policy wonk, and let's just say I don't ordinarily agree with what he has to say, scratch the ordinarily. We simply have differing world views, and, you know, that is okay. However, I read differing opinions when digesting news, so I can have a better understanding of what other people think.

In his column, he maintained expanding the EITC (Earned Income Tax Credit) to a wider swath of people would be great for alleviating poverty and growing the economy. He backed up his contention with enough statistics for a 600 word column, and his argument was reasonably well thought out and presented. However, that doesn't mean he was right, even if he was horribly clever.

Gov. Andrew Cuomo of New York was also a clever fellow last week when he circumnavigated state parliamentary procedure, and crammed through an increase in the hourly minimum wage for fast food workers to $15. I won't bore you with the details, but if I was a resident of New York I would be extremely concerned with his actions, even if I agreed with his policy. In any event, this, too, is supposed to good for the economy, as it lifts people out of poverty, and all of that.

Well intentioned, all of it, but effective? Only The Shadow knows, but the rest of us have our sneaky suspicions, one way or the other. Don't we?

Now, if things like a high minimum wage were actually good for economic growth, it would make sense the country with the highest minimum wage would have the highest per capita GDP, or living standards, wouldn't it? At least to some degree.

By most reports I could easily find, Australia has the highest absolute minimum wage in the developed world, with unskilled labor able to bring home around US$22,000/year *(based on something called purchasing power parity),* which would be about 50% of the current per capita income in that country. That is the bomb. What is not to like?

However, the country that has the highest set minimum wage in the world as a percent of per capita income is a place called the Central African Republic. There, the minimum wage is an estimated 270% of the average person's output, which really isn't all that much because per capita income is only around $600 or so. Still, what is 270% of $600? Around $1,600? That isn't that much, so it would seem as though setting the bar there would raise overall output, wouldn't it? Again, that would the logic in some salons.

What's more, the Central African Republic, from what I can tell, has an unemployment rate of less than 10%....7.6% according to the World Bank. So, if the minimum wage is 270% of per capita GDP and the country has a reasonably low level of unemployment, why is per capita income so low? Why is the country so poor? That doesn't compute. Well, it is because the vast majority of the workforce is engaged in subsistence agriculture and the underground economy, and, as such, is exempt from the official labor market data and minimum wage rules.

But, wouldn't it make sense for someone earning $400 scratching out a living in the dirt to move to the city to make $1,600? Of course it would, if only their output was actually worth $1,600 to employers. Therein lies the problem with trying to run the economy through tax policies and things like

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Wishful thinking is not sound public policy.

Bjorn Lomborg

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minimum wage laws: the governing authorities in any location can put a number on the value of a worker's output, but it doesn't make it so. You might call it a light, fluffy angel food cake with a rich, creamy filling….I still call it a Twinkie, and I will pass on it thank you.

Similarly, expanding the EITC, as Sunstein proposes, is so much pushing on a string. It might give certain members of society more pocket change, and that is desirable; however, it doesn't increase their output or their relative value in the economy. It is simply a transference of wealth through the tax code, as opposed to the creation of wealth through increased individual output.

Imagine a group of three people. One person has $10, another person has two baseball cards, and the last doesn't have either. However, the person with the $10 wants the person with nothing to have the baseball card, so he gives his money to him. The person with the card forks over one card for the 10 spot, and all is well with the world. What has happened here? Obviously, in aggregate, nothing has changed. One person has $10 and a baseball card, another has a baseball card, and the last doesn't have anything. All we have done is transferred assets, as opposed to creating them, and they can continue trading between themselves until Doomsday, but the end result will be the same.

This is a pretty easy concept to understand in a simplistic example, but there are those who would assume it falls apart when you compile a number of like situations. However, an economy is really nothing more than an amalgam of individual transactions, and the struggle for finite resources. As such, the only way to truly grow your economy is to: 1) grow your population, du, and; 2) grow the type and amount of goods and services available to your population. Absent those two things, you got nothing.

If you can accept this, you can accept the best thing you can do for economic growth is grow a well-trained, productive, entrepreneurial, and creative workforce/population. It isn't a mistake the world's wealthiest countries are also the most well-educated and productive, and the world's poorest generally have the largest availability of unskilled and unproductive labor. In essence, fiddling with the tax code isn't as important as turning your workforce into a group of economic zealots.

But that takes time, and doesn't feel as good as giving people some extra money...regardless from whence it came. Frankly, it requires a heckuva lot less work on "our" end, doesn't it? And there is also someone to blame if the policies don't work as envisioned: "thus and so isn't paying their fair share." That sort of thing. Still, hopefully, in the back of everyone's mind is the old adage often attributed to either Maimonides, the Chinese, or to a certain Anne Ritchie, but has been known for a very long time: "give a man a fish and you feed him for a day; teach a man to fish and you feed him for a lifetime."

Admittedly, this is an old saw of mine, and it would seem I am beating a horse that has long since died. However, amazingly enough, I hear far more about giving people more money for the same amount of economic output than I do valid ways of increasing the output in order to get more money. It seems I read about carving up the pie far more often than actually increasing the size. Sure, there are those who would argue you can take away a portion of my piece to give to someone else and somehow magically grow the whole pie, but their logic seems to fail apart pretty quickly.

Disclosure

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The thing is, worker productivity in the United States stinks. That is the reason why wages aren't going up rapidly for the unskilled and semi-skilled. It has very little to do with greedy CEOs. Simply put, adding headcount doesn't necessarily add anything to the bottom line.

Consider this from the 'Productivity and Costs' report for 2Q 2015 the Bureau of Labor Statistics (BLS) released this past Tuesday:

Nonfarm Business productivity of labor:

2Q 2015	**1.3%**
1Q 2015	**(1.3%)**
2014	**0.7%**
2013	**0.0%**
2012	**0.9%**
2011	**0.2%**
2010	**3.3%**

As the table clearly suggests, for the last 4.5 years worker productivity in the United States has been mediocre at best. Since the productivity of labor is really nothing more than a function of economic output and the increase in overall hours worked, if the BLS is accurate, well, I think you get the picture. The average American worker hasn't really been cranking it out since 2010

So, output isn't going up but there are plenty out there who would like for pay to do so. How does that really make sense? How can a fast food franchise owner hope to make ends meet by paying ***its existing*** staff over 50% more than they currently are (in NY, from roughly $9 to $15 per Andrew Cuomo's wishes).

The easy answer is: they aren't or won't. Franchisees will simply replace existing workers with those potentially worth $15, and there will be no shortage of recent college and community college graduates making $12 at places like The Gap or Bank of America who will suddenly be willing to work at, say, McDonald's.

As a result, for all the good intentions, monkeying around with the minimum wage in the fast food industry will lead to employers replacing those very workers the government wants to help. In the meantime, places, again, like The Gap, will automate more, focus more heavily on their online platforms, and instead of hiring 3 people worth $11/hour, they will hire 2 actually worth $15.

Now, IF worker productivity were going through the rood, the story might be a little different, but it isn't. Artificially high wages for unskilled labor in one industry which simply attract semi-skilled labor from other industries. As a result, the unskilled labor in the former gets the proverbial squeeze.

While the end result is as certain to me as the nose on my face, by the time we get there, the powers that be will have tired of patting themselves on their backs and will have moved on to something else….either not fully comprehending or caring they have given modest raises to semi-skilled labor as opposed to a so-called living wage to unskilled labor, which is what they intended to do. The funny part? The Unemployment Rate won't go down, so they can claim it a success! Instead, those workers worth $8-9/hour will increasingly drop out of the workforce, so they won't be included in the statistics. They will participate in the shadow economy, with straight cash for their labor while maximizing their benefits which many were getting while working at, again, McDonald's. So, none of the numbers really change…..just their legitimacy, as well as the worker's ability to pay into SSA and gain valuable 'experience' from a qualified employer they can use on a job application.

You know, a nice little experiment would be to canvass the existing employees at a McDonald's in Brooklyn, Staten Island, or Queens, and then go back to the same restaurants in, I don't know, 12 months time and see how many of the original workers are still there. I would be willing to bet a relatively small percentage of them will be, and I would be even more willing to bet the new workforce will have more education and less time in the fast food industry.

That is just the way it goes when policy is focused on shifting money around the economy, as opposed to actually creating wealth. If the goal is to give a portion of society a little extra spending cash, than simply admit it and be done with it. We are big people here; come on. However, if the goal is to actually create wealth, then let's come up with fresher ideas than increasing the minimum wage or expanding EITC…..a good place to start would be refocusing a lot of our education dollars on vocational technical training.

That will have a much more pronounced effect on alleviating poverty and growing the economy.