

MINIMUM WAGES, EMPLOYMENT AND PRICES: Evidence from hairdressing in Germany

Do minimum wages harm employment or do they increase prices? A new study of minimum wages for German hairdressers shows that even very large minimum wages do not necessarily harm employment. Instead, employers are able to pass on increased wage costs to consumers via higher prices.

The research by **Max Kunaschk**, to be presented at the annual congress of the European Economic Association in Manchester in August 2019, suggests that it is not the absolute size of a minimum wage that is important, but rather the population that is affected by such a reform.

Where most people work in jobs that are hard to substitute, even fairly large minimum wages can have a small short-term impact on employment. At the same time, this comes at a price for consumers, who have to pay for the wage increases of minimum wage workers.

Hairdressers have traditionally been among the lowest paid employees in Germany. Figure 1 shows average daily wages for hairdressers compared with other, typically low-wage, occupations. Even when comparing hairdressers with other low-wage workers, their pay is remarkably low.

In order to combat these extremely low wages, the German hairdressing sector introduced a minimum wage in 2013. The minimum wage for hairdressers was set extremely high compared with the average wage in the sector: over 40% of employees were affected by the minimum wage.

Due to the large number of affected individuals, many economists would predict large negative employment effects of this reform. But this is only the case if employers are unable to pass on increased wage costs to consumers via higher prices. If firms can raise prices without stark declines in demand for their product or service, we would not expect large negative employment effects of a minimum wage.

Indeed, employers were able to pass on the increased wage costs to consumers. Figure 2 shows the development of the overall consumer price index and of the consumer price index for hairdressing services around the introduction of the hairdressers' minimum wage. By the end of the observation period, hairdresser prices had increased by around ten percentage points more than overall prices.

Further analysis suggests that a 10% increase in the share of affected workers leads to 1.8% larger price increases. The wage effects are of similar magnitude: an increase in the share of affected workers by 10% increased average hourly wages by 1.5%.

With respect to employment, the reform had no large effects overall. But after the minimum wage was increased, some small negative employment effects became apparent. After the increase, a 10% higher share of affected workers decreased employment by 0.3%.

This study shows that even very large minimum wages do not necessarily harm employment. These findings have important implications.

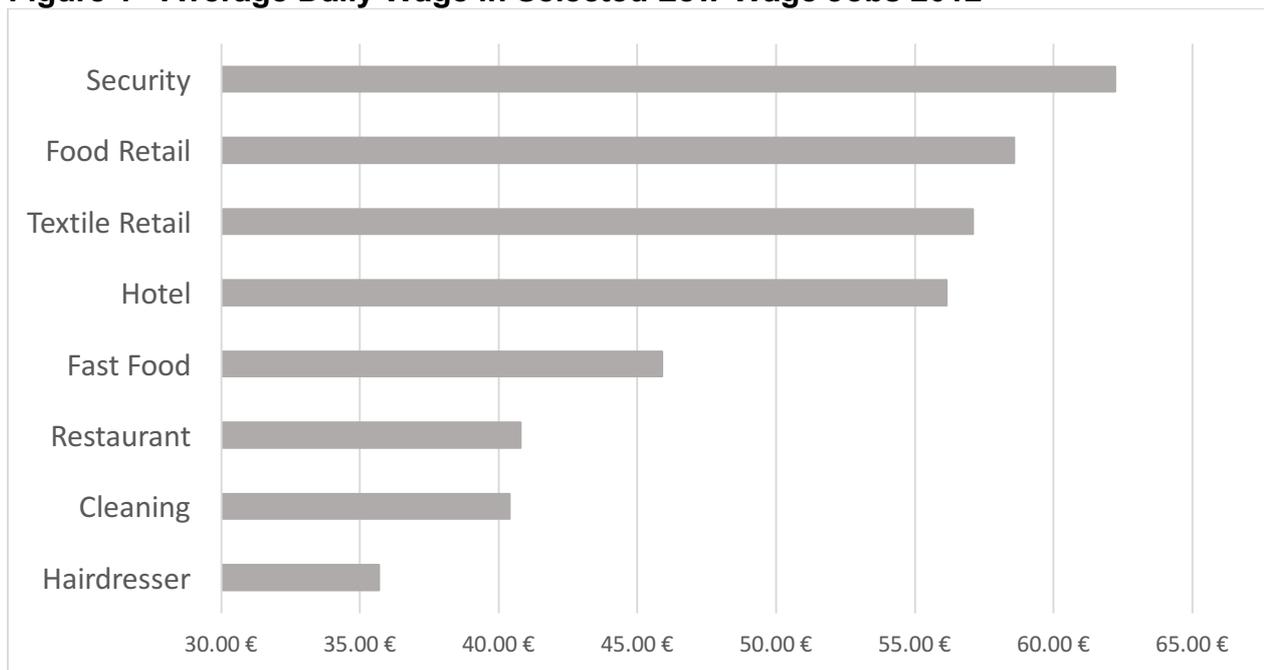
For example, many US states are planning to introduce very high minimum wages, up to \$15. While many fear such policies may have large negative consequences for employment, the results from this study show that it is not the absolute size of the minimum wage that is important, but rather the population that is affected by such a reform.

Where most people work in jobs that are hard to substitute, even fairly large minimum wages can have a small short-term impact on employment. At the same time, this comes at a price for consumers, who have to pay for the wage increases of minimum wage workers.

But these findings do not mean that minimum wages can be infinitely high. Consumers will stop purchasing most products or services if prices increase too much, as is evident from the negative employment effects after the minimum wage increase. Furthermore, where minimum wage work is easier to substitute, employment effects can be much more substantial.

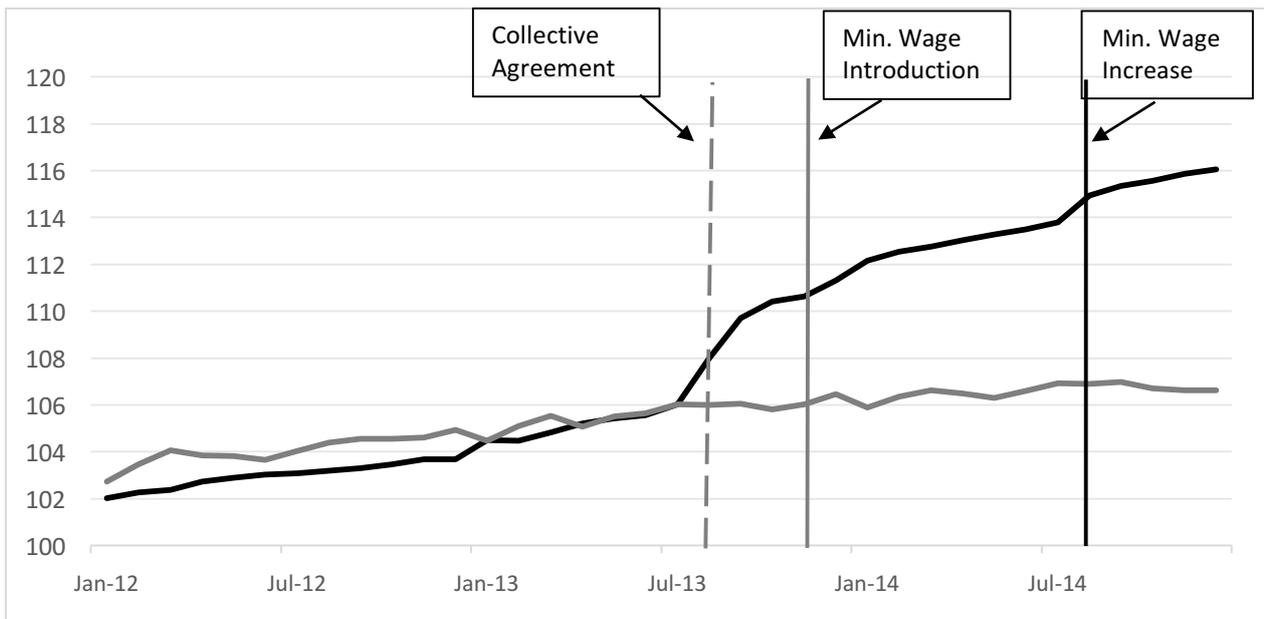
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Figure 1 - Average Daily Wage in Selected Low-Wage Jobs 2012



This figure shows the average nominal daily wages for selected occupations in Germany in June 2012. The sample includes 2% of all dependent workers in Germany and contains regular full- and part-time employees. Source: Integrated Employment Biographies (Federal Employment Agency, 2018).

Figure 2: Consumer Price Index 2012-2014



This figure shows the overall consumer price index (black) and the consumer price index for hairdressing services (grey) in Germany from 2012 to 2014.

Source: Federal Statistical Office, 2017, and State Statistical Offices, 2017.

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