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A Strong Year for Jobs Offers Lessons for Congress

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The economy added 167,000 jobs in December, above the average for the past year, the Bureau of Labor Statistics reported today. The unemployment rate held steady at a very low 4.5 percent, and wages increased due to the tight labor market. Today's report reflects an economy that is growing strongly, despite the weakened housing market. The new Congress and the President should enact policies to continue the economic expansion, such as making permanent the pro-growth tax cuts of 2003, slowing government spending, and restraining the rapid growth in entitlement spending.

A Good Year for Workers

The last year was a good one for American workers. In 2006, the economy added 1.7 million jobs, lowering the unemployment rate from 5.0 percent in January to 4.5 percent in December. The unemployment rate for the entire year is 4.6 percent, which, outside of the unsustainable tech bubble, is the lowest since the 1960s.

Employers created 154,000 jobs each month, on average, in 2006. The number of long-term unemployed workers declined, as did the average number of days an unemployed worker remained without a job. The median length of time for an unemployed worker to find a job fell sharply, dropping almost a full week to 7.3 weeks, in December.

The construction industry shed jobs in 2006, with four straight months of job losses. Construction has been one of the strongest sectors for employment over the past few years, but the weakening housing market is being felt in this sector. Overall, strong job growth in other sectors, such as professional and business services, more than offsets job losses in construction and manufacturing.

Even with this strong job growth, workers worked more hours last year. With jobs plentiful and workers scarce, employers have begun offering their employees larger raises. Wages have risen sharply in recent months. Even as inflation fell, average hourly wages rose at an annual rate of 5.8 percent in December.[1]

Average hourly wages rose by 4.2 percent in 2006. Hourly wages have not risen faster since May 1998. Even after adjusting for inflation, wages are still up 2.5 percent, the largest increase since 1998. Workers and the economy are doing well and appear poised for further gains in 2007.

New Policies for the New Year

Coming off a strong year, the new Congress should pursue policies that will continue America's economic progress, not impede it. House Speaker Nancy Pelosi (D-CA) and congressional Democrats deserve praise for their public commitment to fiscal

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discipline and spending restraint. Implementing true pay-as-you-go (PAYGO) budgeting for spending would create a much-needed barrier to new entitlement programs over the next two years. If Democrats are willing to forgo many of the expensive campaign spending promises they made before the election and instead commit to fiscal responsibility, America's workers and taxpayers stand to gain.

The driving force behind the budget deficit is entitlement spending, which makes up a majority of the federal budget.[2] With the Baby Boomers set to retire soon, spending on existing entitlement programs like Social Security and Medicare will explode, driving America into an even deeper fiscal hole.

Despite this fact, the Democrats' proposed PAYGO rule would not apply to existing entitlement programs and, thus, would do nothing to address America's real fiscal problem. PAYGO rules should be extended to cover current mandatory programs.

Although PAYGO may prevent new entitlement spending in the 110th Congress, lawmakers should rework the rule before 2010 so that it does not prevent extensions of the tax relief passed in 2001 and 2003. A massive tax hike like the expiration of these tax cuts would do lasting harm to the economy and threaten the jobs market. In addition, higher taxes on dividends and capital gains would likely depress the stock market, where most retirement savings are invested, and so an ill-conceived PAYGO rule could increase retirement insecurity at the very moment when many Americans can least afford it.[3]

Congress should also think twice before raising the minimum wage. Despite its supporters' good intentions, a higher minimum wage would not reduce poverty and would harm the very workers it is intended to help. Study after study demonstrates that higher minimum wages do not lower the poverty rate or lift low-income workers out of poverty.[4] This is not surprising, because fewer than one in five minimum wage workers live below the poverty line. Most minimum wage workers are young people between the age of 16 and 24 earning supplemental family income, not single parents working full time.[5] The minimum wage simply does not reach its intended beneficiaries.

For unskilled workers, the minimum wage does more harm than good. When the cost of hiring workers rises, employers hire fewer of them. Worse, they become particularly unlikely to hire the unskilled workers who most need work.[6] If an employer can hire a skilled worker for $7.25 an hour or an unskilled worker for the same rate, the employer will always choose the more productive employee. This effect freezes many unskilled workers out of the job market and prevents them from learning the skills that would enable them to become more productive and earn raises. Intended to help low-income workers, the minimum wage actually does more to harm than to help them.

1. Heritage Foundation calculations based on Bureau of Labor Statistics, "Employment Situation News Release," Table B-3, Jan 5, 2007, at *www.bls.gov/ces/cesbtabs.htm*.
2. Brian Riedl, "Federal Spending—By the Numbers," Heritage Foundation WebMemo No. 989, Feb 6, 2006, at *www.heritage.org/Research/Budget/upload/93690_1.pdf*.
3. Alison Acosta Fraser and Brian M. Riedl, "Memo to Speaker Pelosi: How to Make PAYGO Discipline the Federal Budget," Heritage Foundation *WebMemo* No. 1289, December 19, 2006, at *www.heritage.org/Research/Budget/wm1289.cfm*.
4. See Richard K. Vedder and Lowell E. Gallaway, "Does the Minimum Wage Reduce Poverty?" Employment Policies Institute, June 2001, at *www.epionline.org/studies/vedder_06-2001.pdf*; David Neumark, Mark Schweitzer, and William Wascher, "The Effects of Minimum Wages Throughout the Wage Distribution," *The Journal of Human Resources*, Spring 2004, pp. 425–450; David Neumark, Mark Schweitzer, and William Wascher, "The Effects of Minimum Wages on the Distribution of Family Incomes: A Non-Parametric Analysis," forthcoming in *Journal of Human Resources*; and David Neumark and William Wascher, "Do Minimum Wages Fight Poverty?" *Economic Inquiry*, July 2002, pp. 315–333.
5. Rea S. Hederman, Jr., and James Sherk, "Who Earns the Minimum Wage—Single Parents or Suburban Teenagers?" Heritage Foundation *WebMemo* No. 1186, August 3, 2006, at *www.heritage.org/Research/Economy/wm1186.cfm*.
6. James Sherk, "Minimum Wage Hikes Hurt Unskilled and Disadvantaged Workers' Job Prospects," Heritage Foundation *WebMemo* No. 1294, Jan 2, 2007, at *www.heritage.org/Research/Labor/wm1294.cfm*.

Conclusion

The American economy is strong, and so is the labor market. Jobs are up, unemployment is down, and wages are rising rapidly. The new Congress enters 2007 facing the choice to build on this prosperity or hinder it. Democrats deserve praise for their promises of fiscal discipline and for new budget rules that will make it harder to enact new entitlement programs. However, they should recognize that raising the minimum wage will make it more difficult for the most vulnerable workers in America to find jobs and that allowing the 2001 and 2003 tax cuts to expire will seriously imperil today's strong economic growth. Congress should extend those tax cuts to protect American workers.

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