

Revised Version, Comments Welcome

Wal-Mart: A Progressive Success Story

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Productivity is the principal driver of economic progress. It is the only force that can make everyone better off: workers, consumers, and owners of capital. Wal-Mart has indisputably made a tremendous contribution to productivity. From its sophisticated inventory systems to its pricing innovations, Wal-Mart has blazed a path that numerous other retailers are now following, many of them vigorously competing with Wal-Mart. Today, Wal-Mart is the largest private employer in the country, the largest grocery store in the country, and the third largest pharmacy. Eight in ten Americans shop at Wal-Mart.

There is little dispute that Wal-Mart's price reductions have benefited the 120 million American workers employed outside of the retail sector. Plausible estimates of the magnitude of the savings from Wal-Mart are enormous – a total of \$263 billion in 2004, or \$2,329 per household.² Even if you grant that Wal-Mart hurts workers in the retail sector – and the evidence for this is far from clear – the magnitude of any potential harm is small in comparison. One study, for example, found that the “Wal-Mart effect” lowered retail wages by \$4.7 billion in 2000.³

But Wal-Mart, like other retailers and employers of less-skilled workers, does not pay enough for a family to live the dignified life Americans have come to expect and demand. That is where a second progressive success story comes in: the transformation of our social safety net from a support for the indigent to a system that makes work pay. In the 1990s, President Clinton fought for expansions in support for low-income workers, including a more generous Earned Income Tax Credit (EITC) and efforts to ensure that children did not lose their Medicaid if their parents took a low-paid job. The bulk of the benefits of these expansions go to the workers that receive them, not to the corporations that employ them.

Attempts to limit the spread of Wal-Mart and similar “big box” stores do not just limit the benefits of lower prices to moderate-income consumers, they also limit the job opportunities that Wal-Mart and other retailers provide. More puzzling is that some progressives have described Medicaid, food stamps, the EITC, and public housing assistance as “corporate welfare.”⁴ The

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² Global Insight, 2005, *The Economic Impact of Wal-Mart*.

³ Arindrajit Dube, Barry Eidlin, and Bill Lester, October 2005, “The Impact of Wal-Mart Growth on Earnings throughout the Retail Sector in Urban and Rural Counties,” Institute of Industrial Relations Working Paper Series, University of California, Berkeley.

⁴ Wal-Mart Watch, 2005, *Low Prices At What Cost? Annual Report 2005*.

right response to Wal-Mart is not to scale back these programs but to expand them in order to fulfill the goal of making work pay.

If Wal-Mart were committed to the welfare of its more than 1.3 million “associates,” as it calls its workers, then it would push to expand these public programs. Instead, Wal-Mart and the Walton family have generally worked against the progressive issues that would benefit its employees, including funding campaigns advocating the repeal of the estate tax. Recently, Wal-Mart has come around to endorsing a higher minimum wage, but this limited step is outweighed by its consistent funding for attempts to roll back progressive priorities that would benefit its workers. Unlike support for true corporate welfare, advocating steps to make work pay would have little impact on Wal-Mart’s shareholders or its bottom line; it could, however, make a large difference for its employees.

The American economy has witnessed a large increase in the return for skills over the last decades. Driven largely by technology, but also by globalization, the benefits of education and training are larger than ever before. The most fundamental solution to this is to invest in the education and training necessary to ensure that all workers can succeed in the global economy.

This note reviews the economic evidence on the impact of Wal-Mart on consumers, the impact of Wal-Mart on its own workers and workers in the retail sector, and the impact of public subsidies on Wal-Mart. It then asks if Wal-Mart could make significant changes in wages and benefits and concludes with a recommended progressive policy response to Wal-Mart.

The Progressive Benefits of Everyday Low Prices

A range of studies have found that prices at Wal-Mart are anywhere from 8 to 39 percent less than its major competitors. For example, Emek Basker summarizes research by UBS Warburg and herself:

[The UBS Warburg] study found that Wal-Mart’s prices were 17-39% lower than competitors’ prices in the three “Wal-Mart cities,” and that average prices at other grocery stores were 13% lower in the Wal-Mart cities than in Sacramento. I repeated Currie and Jain’s analysis using a subset of 24 drugstore products from their data set... For these items, Wal-Mart’s prices were 23% lower on average than competitors’ prices in the Wal-Mart cities. Competitors’ prices in Wal-Mart cities were lower than Sacramento prices for most, but not all, items; on average, drugstore prices were 15% lower in Wal-Mart cities.⁵

Some of the largest price differentials are for groceries, with Wal-Mart’s prices substantially below the prices at unionized chains like Kroger and Safeway.

⁵ Emek Basker, 2005, “Selling a Cheaper Mousetrap: Wal-Mart’s Effect on Retail Prices.”

The most careful economic estimate of the benefits of lower prices and the increased variety of retail establishments is in a paper by MIT economist Jerry Hausman and Ephraim Leibtag (neither researcher received support from Wal-Mart).⁶ They estimated that the *direct* benefit of lower prices at superstores, mass merchandisers and club stores (including but not limited to Wal-Mart) made consumers better off by the equivalent of 20.2 percent of food spending.⁷ In addition, the *indirect* benefit of lower prices at competing supermarkets was worth another 4.8 percent of income. In total, the existence of big box stores makes consumers better off by the equivalent of 25 percent of annual food spending. That is the equivalent of an additional \$782 per household in 2003.

Because moderate-income families spend a higher percentage of their incomes on food than upper-income families, these benefits are distributed very progressively. As shown in Table 1, the benefits from big box grocery stores are equivalent to a 6.5 percent increase in income for the bottom quintile (average income of \$8,201) and a 0.9 percent increase in income for the top quintile (average income \$127,146).

	Income (pre-tax)	Food At Home	Food Share of Income	Total Welfare Increase	Welfare Increase (% of Income)
Bottom Quintile	\$8,201	\$2,119	25.8%	\$530	6.5%
Second Quintile	\$21,478	\$2,713	12.6%	\$678	3.2%
Third Quintile	\$37,542	\$3,114	8.3%	\$779	2.1%
Fourth Quintile	\$61,132	\$3,726	6.1%	\$932	1.5%
Top Quintile	\$127,146	\$4,503	3.5%	\$1,126	0.9%
All	\$51,128	\$3,129	6.1%	\$782	1.5%

Source: Data from Bureau of Labor Statistics, June 2005, *Consumer Expenditures in 2003* and author's calculations.

Although the Hausman-Leibtag study is suggestive of the potentially huge impact of Wal-Mart, it only considers food prices, does not sum up the benefits for the country as a whole, and includes the impact of superstores other than Wal-Mart.

Global Insight was hired by Wal-Mart to quantify the national benefits of Wal-Mart's low prices. It estimated that "the expansion of Wal-Mart over the 1985-2004 period can be associated with a cumulative decline of 9.1% in food-at-home prices, a 4.2% decline in commodities (goods) prices, and a 3.1% decline in overall consumer prices... This amounts to a total consumer savings of \$263 billion by 2004, which is the equivalent of \$895 per person or \$2,329 per household."⁸

According to Global Insight's macroeconomic model, the lower rate of inflation led to smaller nominal wage increases throughout the economy, although this estimate is grounded in

⁶ Jerry Hausman and Ephraim Leibtag, October 2005, "Consumer Benefits from Increased Competition in Shopping Outlets: Measuring the Effect of Wal-Mart."

⁷ Note that this estimate effectively incorporates the difference in convenience from shopping at Wal-Mart, a factor generally omitted from other estimates of this kind.

⁸ Global Insight, 2005, *The Economic Impact of Wal-Mart*.

macroeconomic modeling assumptions and is not based on any data on the impact of Wal-Mart on retail or other wages. As a result, they estimated that the *net* increase in purchasing power in 2004 was \$118 billion, or \$1,046 per household. This increase in purchasing power is primarily the result of Wal-Mart's contribution to total factor productivity, but is also due to its ability to bargain for lower prices for imported goods.

Although Global Insight is a highly respected economic consulting firm and the study was reviewed by several independent economists, its results should still be taken cautiously both because they have not undergone intensive peer review and for some technical reasons (if anything, some of these technical issues could mean that Global Insight *underestimated* the benefits of Wal-Mart).⁹ The Global Insight results are generally consistent with Hausman-Leibtag and with Basker, who found that the entry of a Wal-Mart leads to a 1.5 to 3 percent reduction in selected retail prices in the short run and a 7 to 13 percent reduction in prices in the long run.

The Impact of Wal-Mart on Retail Workers

In the spring of 2004, a new Wal-Mart opened up in Glendale, Arizona. The store received 8,000 applications for 525 jobs with wages starting as low as \$6.75 per hour.¹⁰ A Harvard applicant has a higher chance of being accepted than a person applying for a job at that Wal-Mart. Wal-Mart experiences similarly high application ratios at other jobs. These anecdotes strongly suggest that jobs at Wal-Mart are better than the opportunities these workers would have in the absence of Wal-Mart, either other jobs or unemployment.

Workers in the retail sector tend to have below-average skills and experience and, consequently, tend to be paid below-average wages. The median hourly wage for a retail worker in the United States is about 25 percent below the average hourly wage. This differential has been roughly stable for the last two decades and is consistent with the earnings differential in other industrial economies and in parts of the United States that do not have any Wal-Marts. While retail jobs are great for some people at some times, they are by no stretch of the imagination the best jobs in the economy.

The key questions are how jobs at Wal-Mart compare to other jobs in terms of wages and benefits and how Wal-Mart affects the local job market. The following subsections address these questions.

⁹ One issue is that the Global Insight study relies on the officially measured CPI, which does not reflect the direct effect of lower prices at Wal-Mart, a factor known as "outlet substitution bias." If Global Insight used an unbiased measure of prices, they would have found larger effects. Two other technical issues could also affect the results, although the direction of these effects is unclear. Unlike the Hausman-Leibtag study, Global Insight estimates "savings" not "welfare improvements." It does not take into account the change in convenience as a result of shopping at Wal-Mart. In addition, Global Insight made no attempt to control for the potential endogeneity of Wal-Mart's decision to open stores.

¹⁰ Christine L. Romero, 4/17/2004, "Job Hunters Flock to New Wal-Mart," *Arizona Republic*.

Wages at Wal-Mart Jobs Compared to Other Retail Jobs

The mere fact that more than 1.3 million Americans work at Wal-Mart demonstrates that its compensation is at least as good as the alternatives, which could mean similar jobs in the retail sector, jobs in other sectors or unemployment. One might want to know how jobs at Wal-Mart compare to similar jobs in the retail sector. Ideally these estimates would compare similar occupations and levels of experience in the same geographical location and incorporate factors like the quality of the work experience and the prospects for advancement. Nothing resembling these ideal data are available.

Nevertheless, the available data is consistent with the premise that Wal-Mart pays wages that are comparable to the retail sector. Global Insight used a new data set provided by Wal-Mart to compare wages for seven positions at Wal-Mart to similar occupations in the same geographical area in 2004. It found that Wal-Mart paid an average wage of \$9.17 for these positions, compared to \$8.46 for a sample from the Bureau of Labor Statistics (BLS) weighted to match the geographic distribution of Wal-Mart jobs. Global Insight, however, did not publish results for a full set of occupations or wages.

The Global Insight story is consistent with other data. Arindrajit Dube and Ken Jacobs estimate that Wal-Mart's *median* hourly wage was just below \$9 in 2001.¹¹ This is similar to the national median wage for jobs in general merchandise (Wal-Mart's category of retailing) which paid \$8.34 per hour, and in retail more broadly which paid about \$9.24 per hour.¹² Note that these national medians are not adjusted to reflect the fact that Wal-Mart jobs are more concentrated in low-wage states and thus overstate the relevant comparison wage.

Wal-Mart itself reports *mean* hourly wages of \$9.68. These are somewhat below the 2004 national average of \$10.29 for general merchandise and \$12.58 for retail as a whole. Dube and Steve Wertheim adjust retail wages to match Wal-Mart's geography and find that Wal-Mart's *mean* wages are 12.4 percent lower than the retail sector.¹³ Dube and Wertheim do not attempt to control for occupation, experience or other job-related factors that are standard in labor economics studies and thus their data do not prove that Wal-Mart pays similar employees less. In addition, they did not analyze median wages which appear to behave differently from mean wages.

Wal-Mart does, however, pay significantly lower wages than those earned by one group of employees: unionized grocery workers in major cities. These unionized workers make an estimated 20-40 percent more than Wal-Mart workers, a fact that is reflected in a similar magnitude mark-up of prices at unionized grocery stores.

¹¹ Dube and Jacobs, *op. cit.* They use data provided by Wal-Mart in the course of discovery for a lawsuit and report that 54 percent of workers are paid less than \$9 per hour.

¹² Dube and Jacobs themselves, however, report average wages of \$9.70 at Wal-Mart compared to \$14.01 at other stores. It appears that their \$14.01 is for California (a higher wage state) and that they limit their data to large retailers (although Wal-Mart replaces both small and large retailers). Moreover, this nearly \$9,000 annual difference is implausibly large. It is hard to imagine Wal-Mart being able to fill jobs if it pays \$9,000 less than other employers – unless the other employers are paying well above market wages and causing unemployment.

¹³ Arindrajit Dube and Steve Wertheim, October 16, 2005, "Wal-Mart and Job Quality – What Do We Know, and Should We Care?"

In addition to wages, Wal-Mart reports that 76 percent of its store management started in hourly positions, although a comparison to other companies is not available. Wal-Mart also reports that that 74 percent of its hourly workers are full-time, compared to 20-40 percent in the retail industry as a whole. Finally, Wal-Mart reports that only 7 percent of its workers are raising a family with children on only one salary.¹⁴

Health Benefits at Wal-Mart Compared to Other Retail Employers

Wal-Mart's health benefits are similar to or better than benefits at comparable employers. Some key comparisons are summarized in Table 2.

Table 2. Comparison of Health Plans			
	Wal-Mart	Retail	Total
Offers Insurance to Full-time Workers	Yes	n.a.	60%
Offers Insurance to Part-time Workers	Yes	n.a.	17%
Company Contribution (single / family)	74 / 67%	77 / 68%	85 / 75%
Workers Eligible (%)	81%	61%	80%
Workers Covered (%)	48%	46%	66%
Wait for Eligibility (average)	6 months*	3.0 months	1.7 months
Median Deductible (single, in/out network)	\$350**	\$300 / \$500	\$500
Median Deductible (family, in/out network)	\$1,050**	\$700 / \$1,200	\$1,000
Lifetime Maximum (% Firms)	None	71%	60%
Median Lifetime Maximum	None	\$1 million	\$2 million

Source: Wal-Mart data, Kaiser Family Foundation *Employer Health Benefits 2005* and Mercer *2004 National Survey of Employer-Sponsored Health Plans*.

*6 months for most full-time employees; part-time employees have a 24 month waiting period.

**Lowest deductible Wal-Mart plan, this appears to be the plan held by the median Wal-Mart employee.

Wal-Mart is relatively unusual in that it offers health insurance both to full- and part-time employees. By comparison, only 60 percent of firms economywide offer health benefits and only 17 percent of firms offer health benefits to part-time workers. Target, for example, does not offer benefits to people working less than 20 hours per week. Wal-Mart, however, has longer waiting periods for eligibility for benefits than many other firms, 6 months for full-time workers and 24 months for part-time workers.

Wal-Mart pays about 70 percent of the cost of health benefits, similar to the retail industry and somewhat below the national average.

Substantially more Wal-Mart employees are eligible for health insurance than in the retail sector as a whole and even slightly more than the nationwide total. Wal-Mart employees, however, are less likely to take up their health insurance.

¹⁴ See www.walmartfacts.com.

As a result, 48 percent of Wal-Mart’s workers have health insurance, compared to 46 percent in the retail industry as a whole. Dube and Wertheim find similar results. They adjust health coverage to match Wal-Mart’s geography and find that 45 percent of retail employees and 53 percent of large retail employees have employer-sponsored health insurance. The retail industry has lower employer-sponsored health insurance than the economy as a whole, a fact that reflects the generally lower compensation in the retail sector and the greater likelihood that a retail employee will be covered through a spouse’s more generous employer-sponsored policy.

Wal-Mart reports that 620,000 of its employees have health insurance, covering a total of about one million people. Some 34 percent of Wal-Mart employees are offered health insurance but choose not to enroll, either because they are covered through another family member, prefer to be on Medicaid than pay the premium, or choose not to have health insurance.

Finally, Wal-Mart has similar deductibles to other PPO plans and is in the minority of firms in having no lifetime maximum for coverage.

In total, as shown in Table 4, 5 percent of Wal-Mart employees are on Medicaid, which is similar to the percentage for other large retailers and is comparable to the national average of 4 percent.¹⁵ The children of Wal-Mart employees receive Medicaid and S-CHIP slightly less often than the retail sector as a whole and slightly more than the national average. The fraction of children is relatively large, reflecting the expansion of public health coverage for children in low- and moderate-income families. The fact that Wal-Mart employees top the Medicaid rolls in a number of states is simply a reflection of Wal-Mart’s enormous size, not the higher likelihood that its employees will be on Medicaid.

Table 4. Medicaid/S-CHIP Coverage			
	<u>Wal-Mart</u>	<u>Retail</u>	<u>National</u>
Employees	5%	6%	4%
Children of employees	27%	36%	22%

Source: Susan Chambers, 2005, “Reviewing and Revising Wal-Mart’s Benefits Strategy: Memorandum to the Board of Directors.”

For some Wal-Mart employees, Medicaid is the sensible choice. A family policy costs \$1,800 annually for a Wal-Mart worker, similar to the cost for other retailers. A Medicaid-eligible worker has the choice of taking home an additional \$1,800 in take-home pay and being insured through Medicaid or taking home less pay and instead getting Wal-Mart’s insurance. The beneficiary of choosing Medicaid is the worker – who gets to keep an additional \$1,800 – not Wal-Mart (see the further discussion of this issue below).

Wal-Mart – like every other business – is interested in paying the lowest possible total compensation (wages and benefits) consistent with recruiting, motivating and retaining a

¹⁵ Susan Chambers, 2005, “Reviewing and Revising Wal-Mart’s Benefits Strategy: Memorandum to the Board of Directors.”

qualified workforce. As a corporation, it does not fundamentally care whether this cost is in the form of wages or benefits.¹⁶

Its workers, however, do care. The notorious Wal-Mart benefits memo, which was not meant for public release and thus can be trusted as a candid assessment, reports that, “Our benefits offering played a key role in attracting just 3 percent of our Associates. Moreover, satisfaction with benefits does not correlate with satisfaction with Wal-Mart.”¹⁷ Wal-Mart workers, like other workers in the retail sector, are paid less than the economywide average wage. They have to pay for food, housing, transportation and numerous other costs. It is not surprising that in a choice-based system they would choose to get more money in the form of wages and less in the form of health benefits.

Moreover, our fiscal system gives much less of an incentive for low-income employees to get employer provided health insurance. High-income employees face a lower marginal tax rate on health benefits than wages. For low-income employees it can be the exact opposite.

Consider a company that wants to compensate a woman in the 25 percent bracket with an additional \$3,000. If she chooses to get it in the form of wages, she will pay 25 percent in taxes and keep the remaining \$2,250. If she chooses to get it in the form of better health benefits, she will get a \$3,000 policy. Compare that to a low-income mother. She is in the 0 percent tax bracket so she would keep the entire \$3,000 if she gets wages. But if she gets the \$3,000 in the form of health benefits, she will lose her Medicaid. This is like a large effective tax on the provision of benefits.

Impact of Wal-Mart on the Local Labor Market

Even if Wal-Mart pays as much as comparable employees, it could still have a deleterious impact on labor markets as a whole. When Wal-Mart enters a new county, it could kill jobs or lower wages, leaving everyone worse off.

Statistically this is a difficult problem, because Wal-Mart bases its decision on whether or not to enter a county, in part, on local market conditions. Simply observing what happens in a county after Wal-Mart enters could lead to statistically biased results. Three careful recent studies have attempted to control for this effect. Nevertheless, the results should be treated with caution because, unlike the observation of large price differences discussed earlier, estimates of Wal-Mart’s effects on jobs appears to be very dependent on the statistical procedure and only one of the papers has been through the peer-review process. In addition, the papers find somewhat contradictory results.

The one study that was published in a peer-reviewed economics journal found that “Wal-Mart entry [in a county] increases retail employment by 100 jobs in the year of entry. Half of

¹⁶ With one huge caveat: the cost of health benefits rises more quickly than the cost of wages, so this should be thought of in something like present value terms, not in any particular year.

¹⁷ Susan Chambers, 2005, “Reviewing and Revising Wal-Mart’s Benefits Strategy: Memorandum to the Board of Directors.”

this gain disappears over the next five years as other retail establishments exit and contract, leaving a long-run statistically significant net gain of 50 jobs.”¹⁸ The paper also found a small negative impact on jobs at wholesalers “due to Wal-Mart’s vertical integration” and no statistically significant effect on other industries.

David Neumark (a respected economist at the University of California – Irvine), Junfu Zhang, and Stephen Ciccarrella find the exact opposite: the entry of a Wal-Mart store reduces retail employment and there is “some evidence that Wal-Mart stores increase total employment on the order of two percent, although not all of the evidence supports this conclusion.”¹⁹

Neumark et al. and another paper by Dube, Barry Eidlin and Bill Lester also studied the impact of Wal-Mart entry on *nominal* wages. Both papers used a similar estimation strategy but employed different data sets and sample periods. Neumark et al. find “some evidence that payrolls per worker also decline, by about 3.5 percent, but this conclusion is less robust” than the finding on employment. Somewhat at variance with this, Dube et al. find that the entry of Wal-Mart leads to a decline in wages of general merchandise workers in urban areas and an increase in wages for general merchandise workers in rural areas. All these declines are less than 1 percentage point. The paper also finds that grocery workers’ wages go down in both urban and rural areas and other workers see no significant change in wages. In total, Dube et al. estimate a \$4.7 billion annual reduction in retail earnings.

Neither paper estimated the impact of Wal-Mart on *real* wages. Presumably the workers in the retail sector and more broadly also benefit from the lower prices that follow the entry of a Wal-Mart. The *nominal* wage effects in both papers have to be compared to the 7 to 13 percent retail price effect in the long run found by Basker or the reduction in the broader CPI found by Global Insight. Taken together, the evidence appears to suggest that, even for retail workers, the benefits of lower prices could outweigh any potential cost of lower wages – potentially leading to *higher real wages even in the retail sector*.

(Also, neither of the authors estimates the impact of Wal-Mart on profit margins. The aggregate evidence and at least some anecdotal evidence at the local level suggest that the entrance of Wal-Mart into new markets squeezes profit margins. If correct, then it could be the case that the entry of Wal-Mart increases competition, lowering the oligopolistic rents that go to both labor and capital – and providing more benefits for consumers.)

The long-run employment effects of Wal-Mart depend on macroeconomic factors. The Federal Reserve can create or destroy aggregate jobs as it wishes. A company like Wal-Mart will only lead to more or less jobs nationally to the degree that it changes the level of unemployment consistent with stable inflation. As a matter of economic theory, the productivity, scale, and competition associated with Wal-Mart all should help lower the sustainable level of unemployment, leading to a higher level of jobs. Quantifying this effect, however, is extremely difficult and very sensitive to modeling assumptions. Global Insight used a complex economic

¹⁸ Emek Basker, 2005, “Job Creation or Destruction? Labor-Market Effects of Wal-Mart Expansion,” *Review of Economics and Statistics*.

¹⁹ David Neumark, Junfu Zhang, and Stephen Ciccarrella, 2005, “The Effects of Wal-Mart on Local Labor Markets.”

model and found that the existence of Wal-Mart allowed 210,000 additional jobs nationwide in 2004. The assumptions underlying this estimate are much more difficult to understand or check than the assumptions that went into Global Insight's total cost savings estimate, making it hard to confidently state whether the 210,000 number is accurate, too high, or too low.

Further research on all of these questions is needed. The results of the existing studies should be taken with a large grain of salt because many of them are contradictory and dependent on complex econometric models. The existing studies generally find mixed evidence for the short-run employment effects of Wal-Mart at the county level but the theory would predict positive long-term employment effects nationally. More importantly, the existing evidence – taken together – shows that the entry of Wal-Mart raises *real* wages for workers in general merchandise, grocery, and retail more broadly. But these estimates of the impact on workers are considerably less robustly estimated than the benefits for consumers.

Public Subsidies for Wal-Mart's Employees

In his first campaign, then Governor Clinton promised to “make work pay”:

People who work shouldn't be poor. In a Clinton Administration, we'll do everything we can to break the cycle of dependency and help the poor climb out of poverty. First, we need to make work pay by expanding the Earned Income Tax Credit for the working poor... At the same time, we need to assure all Americans that they'll have access to health care when they go to work.²⁰

Clinton, building on some smaller previous steps, radically changed the nature of social assistance in America, shifting from assistance for the non-working indigent to assistance that supports families that work. According to leading poverty researchers Rebecca Blank and David Elwood, total spending on the principal programs for low-income *working* families increased six-fold in inflation-adjusted terms from 1988 to 1999. This included expanding the EITC and ensuring that children would not lose Medicaid coverage if a parent took a low-paying job.

In 2006, a married couple with two children making up to \$38,000 will receive the EITC. In some states Medicaid eligibility extends up to as much as 200 percent of the poverty line for parents and 300 percent of the poverty line for children (for a family of four, that is \$38,700 and \$58,050 respectively).

The result of this shift to supporting work has been a large increase in the incentives to work, as shown in Table 3. In 1988, a single mother with two children would only earn an additional \$2,325 if she went to work full-time, and she would likely lose Medicaid coverage for

²⁰ Bill Clinton, 10/23/1991, “The New Covenant: Responsibility and Rebuilding the American Community,” Remarks at Georgetown, quoted in Rebecca Blank and David Ellwood, “The Clinton Legacy for America's Poor,” *American Economic Policy in the 1990s*, Jeffrey A. Frankel and Peter R. Orszag (eds.) MIT Press, Cambridge: 2002.

her children. By 1999, working would earn her an additional \$7,051 and would not result in the loss of Medicaid, at least for her children.

Table 3. Disposable Income For a Single Mother With Two Children		
	Not Working	Working Full-time at Minimum Wage
1988	\$8,612 (Medicaid eligible)	\$10,937 (Not Medicaid eligible)
1999	\$7,967 (Medicaid eligible)	\$15,018 (Children under 16 Medicaid eligible)

Source: Blank and Ellwood (2001). Note “disposable income” includes the effects of labor earnings, AFDC/TANF, payroll taxes, the EITC, childcare expenses, and childcare support. All estimates are in 1999 dollars.

The intention of these expansions was two-fold: to get more low-income people, especially mothers, into work and to ensure that even low-paid, unskilled jobs come with a decent wage and benefits. Wal-Mart employees would seem like perfect candidates on both scores.

Critics of Wal-Mart, however, have harshly criticized the fact that Wal-Mart employees receive benefits through these programs. Wal-Mart Watch, for example, states:

Wal-Mart is one of the biggest recipients of corporate welfare in the world. Year after year, Wal-Mart’s low pay and insufficient employee benefits programs leave hundreds of thousands of Wal-Mart workers to rely on Medicaid, food stamps, and public housing assistance to make ends meet. Call it the “Wal-Mart Tax.” It costs American taxpayers at least \$1.5 billion in federal tax dollars every year, and hundreds of millions more in state and local subsidy costs.²¹

This section addresses two questions. First, if Wal-Mart pays lower wages, does it cost taxpayers \$1.5 billion annually? And second, who benefits from the subsidies for low-income workers, the workers themselves or Wal-Mart?

Do Wal-Mart Employees Cost the Treasury More?

The overall fiscal impact of Wal-Mart is overwhelmingly positive. In its last fiscal year it set aside \$5.6 billion for corporate tax payments. In addition, its employees pay taxes on their tens of billions of dollars of earnings. Together with indirect effects, like driving up real estate values, their total tax bill is much larger than the claimed \$1.5 billion in federal subsidies for its low-income employees.²²

²¹ Wal-Mart Watch, *op. cit.*

²² The \$1.5 billion estimate is a rough back-of-the-envelope estimate by the Democratic Staff of the House Committee on Education and the Workforce, 2/16/2004, “Everyday Low Wages: The Hidden Price We All Pay For Wal-Mart.”

The total tax bill, however, is not the relevant question. Instead the question is whether Wal-Mart and its employees pay their “fair share” in a way that is consistent with businesses and workers in similar circumstances. Dube and Jacobs ask one version of this later question. They argue that Wal-Mart pays less than comparable employers (as discussed earlier, the evidence suggests this is not the case) and ask the question: how much do Wal-Mart’s low wages cost taxpayers? They estimate that Wal-Mart pays its full-time workers \$8,620 less than comparable employers. They further estimate that Wal-Mart workers get \$1,952 in public assistance annually (including Medicaid, EITC, food stamps, and other programs), or \$551 more than comparable employers.²³ They assert that this difference is a “hidden cost” of Wal-Mart.

Their analysis, however, is incomplete and as a result features the wrong answer. Assume that the Dube and Jacobs’ numbers are accurate. If Wal-Mart pays the employee \$8,620 less, that money has to go somewhere. If this money goes into corporate profits or executive compensation, it will result in an additional \$3,017 in taxes at the 35 percent marginal rate. If even one-fifth of Wal-Mart’s lower wages went to corporate profits or top executives, that would be enough to make its low wages – by the Dube-Jacobs estimate – a net revenue increaser for the federal government. *Based on the Dube-Jacobs results, it is overwhelmingly likely that if Wal-Mart pays lower wages, then this would improve the government’s fiscal situation.*

But encouraging private-sector companies to distribute their compensation to maximize net government revenues is peculiar and backwards. Who would recommend, for instance, that a corporation cut pay for its middle-income workers in order to raise executive compensation on the theory that this will raise total tax collections because executives are in a higher tax bracket?

Who Benefits When Low-Income Workers Get Benefits?

Wal-Mart Watch and other groups argue that the claimed \$1.5 billion increases Wal-Mart’s profits, thus the term “corporate welfare.” This goes against the assumption that motivated President Clinton, for example, whose earlier comment indicates that he believed that the beneficiaries of higher minimum wages, expanded Medicaid, larger EITCs, and other work-related benefits would be the employees, not the companies they worked for. What then is the evidence for these contrasting views?

The standard incidence analysis used by the Congressional Budget Office (CBO), the Treasury, the Joint Committee on Taxation (JCT), and other researchers generally assumes that the entire cost/benefit of labor-related taxes/benefits is borne by labor.²⁴ That means if taxes go up by \$1,000, a person’s wages will not change – he or she will pay the full cost of the \$1,000. Similarly, if an EITC refund goes up by \$1,000, the worker’s wages also will not change and he or she will get the full benefit. The same goes for Medicaid benefits.

²³ Note that Dube and Jacobs essentially estimate an effective marginal rate of 6 percent – that is an additional dollar earned results in a \$0.06 reduction in the EITC and other means tested benefits. That, however, seems relatively low. For a family with children, at least, the effective marginal rate would be much higher.

²⁴ Technically, this is based on the result that the tax incidence falls on the “inelastic” side of the market and the observation that labor demand is relatively inelastic.

Three caveats are in order. First, studies have consistently found that the EITC leads more people to enter the labor force and find work. As a matter of economic theory, this would lead to an increase in labor supply, driving down wages and providing some benefit for employers.²⁵ Note this analysis would not apply to other means-tested benefits because they do not increase with work, as the EITC does for the first \$11,000 of earnings.

Second, although economic theory predicts the benefit of Medicaid will go entirely to the worker, it is conceivable that the employer will also get some of the benefit, especially in the short run. In this case, Medicaid would lower the cost of hiring a new employee, boosting employment. This is precisely the effect touted by many progressive advocates of an expanded government role in health care. They argue that high health costs “limits employers’ willingness to create jobs” and that lowering health costs will help create jobs.²⁶

Finally, there is no reason to imagine that the split in the benefits of public assistance between the employer and the employee would be different at Wal-Mart than any other employer. To the degree that public assistance provides \$1.5 billion in corporate welfare for Wal-Mart, then it likely provides hundreds of billions of dollars of corporate welfare economywide.

America’s policies to make work pay are targeted at less-skilled, lower-paid workers. They were not designed specifically to benefit smaller employers or companies with relatively low revenues. There is little reason to believe they should be designed this way: Wal-Mart workers would make roughly the same amount wherever they worked and thus a fair and economically sensible tax/benefit system would provide them with the same amount regardless of the size or identity of their employer. Would anyone want to deny the EITC to people who work at large companies?

Could Wal-Mart Do Much Better For Workers?

Implicit in much of the criticism of Wal-Mart is the belief that the company has enormous resources and could easily pay higher wages or more benefits without making a major sacrifice. After all, Wal-Mart’s mind-boggling \$10 billion in profits last year make it appear as if the company could wave a wand and do anything it wants. But Wal-Mart also has a staggering 1.3 million American employees, multiplying the costs of even a modest change in compensation.

Overall, it is no easier for Wal-Mart to change compensation than many other companies. This year Wal-Mart will earn about \$6,000 per employee. This is virtually identical to the average for the retail sector and somewhat below the national average of \$9,000 in profits per employee in the corporate sector. Some companies make substantially more, like Microsoft

²⁵ The same does not apply to the other public assistance programs because, unlike the EITC, they *decrease* with work.

²⁶ Jeanne M. Lambrew, John D. Podesta, and Teresa L. Shaw, March 2005, “Change in Challenging Times: A Plan for Extending and Improving Health Coverage,” *Health Affairs*.

(\$143,000 per employee) or General Motors (\$12,000 per employee). Overall, it is not much easier for Wal-Mart to change compensation than, say, a small business making \$24,000 a year and employing four people.

If Microsoft paid each of its employees an additional \$5,000 or expanded its health benefits, its profits would be largely unchanged. If Wal-Mart took the same step – and did not pass the cost on to consumers – it would be virtually wiped out.

In the last fiscal year, Wal-Mart had revenues of \$288 billion and costs (including taxes and other charges) of \$277 billion – a razor-thin profit margin of 3.7 percent of revenues. Even a very small increase in its costs, without a corresponding increase in revenues, would wipe Wal-Mart's profits out entirely.

The image of Wal-Mart as all powerful is at least six years out of date. Although still a rapidly growing mega-corporation, Wal-Mart “is losing customers, especially for higher-margin products, to the likes of Target Corp. Sales at Wal-Mart stores open at least a year are up about 3.5% so far this year, compared with 5.9% for Target.”²⁷ On November 15, 1999, Wal-Mart's stock price closed at 58.94. Six years later it had fallen to 49.3. Including dividends, Wal-Mart stockholders have enjoyed a 2.3 percent annual return over the last five years, which is not even enough to keep up with inflation and well below the 7.2 percent for the “broadline retailers” category as a whole. A company facing this degree of competition will have a hard time taking large costs out of profits or passing them onto consumers by raising prices.

Some have pointed to Costco (which has higher wages and more generous benefits), arguing that if Wal-Mart were more generous with its employees it would do better at attracting, motivating, and retaining them, increasing its total profits. I have no ability to judge whether or not this is true, although given the choice I would trust Wal-Mart to know more about maximizing profits and shareholder value than its critics.

The Costco model is largely irrelevant for Wal-Mart. Costco shoppers have an average income of \$74,000, which is twice the \$35,000 average income for Wal-Mart shoppers (Target is in the middle with average incomes of \$50,000 per shopping family).²⁸ Costco is primarily in or near urban areas and is, among other facts, the country's leading seller of fine wines. The Chairman of Costco, Jeff Brotman, described its target customer to *Fortune*: “We understood that small-business owners, as a rule, are the wealthiest people in a community... So they would not only spend significant money on their businesses, they'd spend a lot on themselves if you gave them quality and value.” *Fortune* goes on to explain, “What Costco has come to stand for is a retail segment where high-end products meet deep-discount prices.... they've redefined discounting. Time was when only the great unwashed shopped at off-price stores. But warehouse clubs attracted a breed of urban sophisticates – detractors would call them yuppie scum – attuned to what retail consultant Michael Silverstein calls the ‘new luxury.’”²⁹

²⁷ Ann Zimmerman, 11/12/2005, “Wal-Mart: Working on Image and Earnings,” *Wall Street Journal*.

²⁸ Marianne Lavelle, 6/27/2005 “Wal-Mart's Most Wanted,” *US News and World Report* and Steven Greenhouse, 7/17/2005, “How Costco Became the Anti-Wal-Mart,” *New York Times*.

²⁹ John Helyar, 11/24/2003, “The Only Company Wal-Mart Fears,” *Fortune*.

As a result of higher margin goods and larger volumes, sales per employee are considerably larger at Costco. This enables it to be more generous with its employees, helping it to attract the more skilled and experienced workers that its higher-income customers expect. This is a reasonable business model; it just isn't Wal-Mart's. Telling Wal-Mart to ape Costco's wages is like telling Best Buy it should pay its employees as much as the high-end boutique plasma television dealer across the street.

Finally, Wal-Mart should obey labor laws that bar gender discrimination, unpaid overtime and environmental laws like the Clean Air Act. I do not know whether or not Wal-Mart has systematically broken these laws; to the degree it has, the remedy is through the legal system, not through restricting the expansion of Wal-Mart into new areas or applying new mandates to a single company.

Making Work Pay in the Wal-Mart Economy

Well-intentioned Wal-Mart critics are sincerely interested in an America where workers are better off. They understandably want higher wages and higher benefits for everyone. Wal-Mart's low prices help to increase real wages for the 120 million Americans employed in other sectors of the economy. And the company itself does not appear to pay lower wages or benefits than similar companies, or to cause substantially lower wages in the retail sector. Although there may be a dispute about the magnitude of the cost savings for consumers, no one disputes that they are large. In contrast, the effect on workers is relatively smaller and far from obviously negative.

There is relatively little scope to pressure Wal-Mart – and almost no scope to pressure other smaller and less visible companies – into paying higher compensation. Even if the campaign resulted in, say, some expansion of health benefits to placate one of Wal-Mart's most visible public relations problems, the result could well be lower wages.

At worst, to the degree the anti-Wal-Mart campaign slows or halts the spread of Wal-Mart to new areas, it will lead to higher prices that disproportionately harm lower-income families.

In the process, some of the campaign's rhetoric risks undermining public support for making work pay, and in particular for publicly provided health benefits for less-skilled and less-experienced workers who earn lower wages.

A much better strategy would be to recognize that Wal-Mart is a progressive success story. By acting in the interests of its shareholders, Wal-Mart has innovated and expanded competition, resulting in huge benefits for the American middle class and even proportionately larger benefits for moderate-income Americans.

Even more important is to recognize the success of the progressive programs that make work pay and fight to expand them. Most progressives support expanded government-funded health insurance – and many support a single-payer national health insurance system. It is odd to

criticize Wal-Mart because 5 percent of its employees receive Medicaid when the health policy you believe in would ensure that 100 percent of Wal-Mart's employees received (a better version of) Medicaid.

Wal-Mart should, however, lead to a serious re-examination of the ways we provide health insurance. Our current system provides more of an incentive to pay low-income families in cash rather than health benefits and *vice versa* for more highly paid workers. Our system also gives companies and health insurers an incentive to undertake distasteful "cherry picking" to lower their health costs by, for example, discouraging older and potentially more costly employees from working or being insured. Piecemeal expansions of the health system – like the Children's Health Insurance Program – may on net lead to much more insurance, but also lead some employers to drop health insurance coverage for some workers. Alternative approaches, like mandating employers or individuals to purchase health insurance or a single-payer health system, would avoid many of these problems but create problems of their own.

Wal-Mart claims to care about all its stakeholders, including the workers it calls "associates." But it has done relatively little to push for public policies that would benefit these workers and has done a lot – like promoting repeal of the estate tax – that is inimical to the interests of these worker. It recently endorsed a higher minimum wage (a step that would cost it very little since relatively few of its workers are paid at or near the minimum wage), but it could do a lot more both to reduce its opposition to progressive issues and to actively promote these issues. Costco, for example, promotes the welfare of its employees not just with its wages and benefits but also with its advocacy of a higher minimum wage and a better health insurance system.

A progressive agenda to make work pay have many steps, including:

- Raise the minimum wage in stages to \$7.25 an hour, a \$2.10 increase.
- Expand the EITC by ending the marriage penalty and adding a "third tier" for families with three or more children. Or adopt more far reaching and progressive tax reform to benefit working families.
- Help families save and invest by making saving easier and more rewarding for moderate-income families.
- Expand health insurance, moving to a system in which every American has affordable, quality health insurance.

Finally, most fundamentally, the "Wal-Mart economy" is not about an economy in which corporations are squeezing workers. It's about an economy in which the return to skills is rapidly growing, and technological change, among other forces, is leading to increased inequality. The most fundamental solution to these challenges is to invest in the education and training necessary to ensure that all Americans have the skills to be successful in a technologically sophisticated, global economy.