Minimum Wage and Firm Response

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Abstract

What is the actual effect of the minimum wage policy on employment? What are the channels, and how much is the effect on employment? Even though a price floor is expected to decrease the quantity demanded, empirical studies show that the answers to the questions above are not straightforward. Theoretical explanations for the non-declining employment with minimum wage emphasise the monopsony power and productivity increase of the firms. Turkey has one of the highest ratios of the minimum wage to the median wage among the member countries of the Organisation for Economic Co-operation and Development. With a large share of registered workers paid around the minimum wage, a sizeable increase in the minimum wage would significantly increase firms' labour costs, and therefore, decrease the firms' demand for labour. This study examines the employment impact of the one-third increase in the minimum wage in 2016, considering the firm-side of the labour market in Turkey. The renewed version of the Annual Industry and Service Statistics micro data allows us to monitor all small and large firms' employment dynamics, profits, and competitiveness. Combining this data set with the recently published Company Accounts Statistics micro data, we estimate the markup, elasticity of substitution, and total factor productivity as well as the entry-exit of firms. In a difference-in-differences setting with heterogeneous intensity of treatment across firms, these estimates will then be used to investigate the channels through which the minimum wage and labour demand are related.

Keywords: labour demand, minimum wage, difference-in-differences

JEL Codes: D22, J23, J38