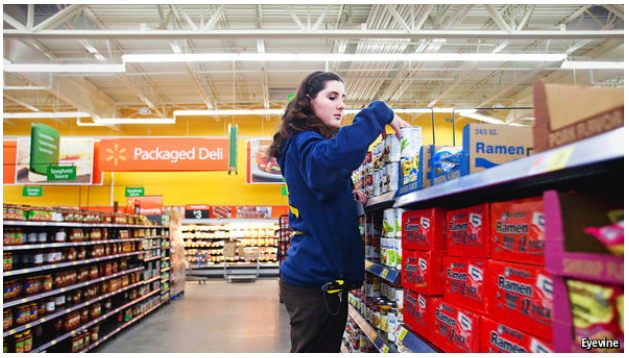
The Economist

Walmart and low-wage America

High expectations

What a big pay rise at Walmart means for the minimum-wage debate

Jan 30th 2016 | WASHINGTON DC | From the print edition



NO FIRM in the world matches the economic imprint of Walmart. The retailer, based in Arkansas and known across America for its vast "supercentres" and low prices, is the world's largest company by revenue. Its 2.2m worldwide workforce is about the same size as China's army, excluding reservists. Sam Walton built his empire with a relentless focus on costs: "Control your expenses better than your competition. This is where you can always find the competitive advantage," he said. Yet change is afoot at "Wally world". In April 2015 Walmart abruptly raised the wages of its lowest-paid staff: all now earn at least $9 an hour. On February 1st that will rise to $10 an hour for trained-up workers—fully one-third higher than the federal minimum wage.

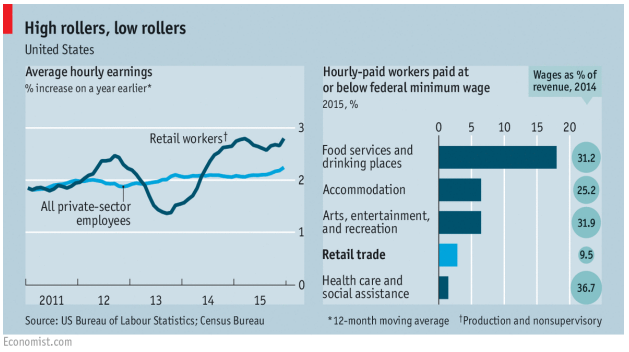
The change is curious, because in the past Walmart has paid notoriously little. In 2014 the average hourly wage of an American cashier was $9.93. According to data from Glassdoor, a jobs website, Walmart's cashiers then took home $8.62. Retail salesmen made $12.38 nationwide; at Walmart, they earned only $8.53.

Walmart wages were low, but not pitifully so; for both cashiers and salesmen, average pay at Walmart was close to the 25th percentile nationwide. What has made Walmart look mean is the firm's enormous size. It employs 1.4m of America's 16m retail workers. Almost 4.5m others toil in small shops with fewer than 100 employees. Wages there are expected to be low. But, typically, big firms pay more. One study from 2014 found that high-school graduates earn 15% more at retailers with more than 1,000 workers, compared with those who have fewer than ten staff. Not so at Walmart, which paid corner store wages while making megachain profits.

This—combined with a fierce resistance to unions—made the firm a target for campaigners. One common accusation against Walmart—whose shareholders made a 17% return in the year to January 2015—is that its low wages mean it benefits from hidden government

subsidies. Many low-wage workers rely on government programmes to top up their low wages, and on Medicaid for health insurance. Without this support—the argument goes—firms relying on cheap labour would collapse. In May 2013 congressional Democrats produced a report which furiously alleged that a typical Walmart supercentre in Wisconsin, employing 300, costs the taxpayer $900,000 a year in welfare payments to its staff.

That was hyperbole; it assumes some other employer would be willing to hire Walmart's workers at higher wages. Looks matter, though, and the benefit of today's pay rises is partly cosmetic. Other factors are in play, too. "In some ways it demonstrated leadership, in other ways it [was] a market reaction," Doug McMillon, Walmart's boss, told investors in October 2015. Recently wage growth has been higher for junior retail staff than for other workers, suggesting that competition for staff may be hotting up (see chart). Walmart's first pay rise, to $9 an hour, was emulated by Target and TJX, which owns the retailers T.J. Maxx, Marshalls and HomeGoods.



The pay rise is also a strategic investment. Walmart wants to boost its productivity and give its workers more freedom to innovate, as it seeks to make its stores more pleasant and, perhaps, appealing to more affluent customers. That requires motivated staff. It is too soon to judge conclusively whether the rise to $9 an hour has worked, although Walmart says that the number of stores rated as sufficiently "clean, fast, friendly" by customers has increased from 16% in February 2015 to over 70% today.

That will please advocates for higher minimum wages, who argue that better-paid workers are more productive. Economists call this the "efficiency wage" hypothesis. Opponents of higher minimum wages note that pay rises cannot be free. Some combination of Walmart's customers, shareholders, suppliers and other employees must be paying for the increase.

Walmart's customers are unlikely to feel the pinch soon; low prices are a cornerstone of the brand. But the firm now says that higher wages come before price cuts: "You clean up your house before you invite people over," argues Mr McMillon.

Wage rises are certainly denting profits. Walmart's share price barely moved when they were first announced in February last year, suggesting that investors thought them immaterial at first. But in October the firm warned that it expected profits to fall by 6-12% in 2017, with higher wages responsible for three-quarters of the shortfall. Following that announcement, the share price fell by 10%—its biggest one-day drop since 1988.

A transfer from capital to labour, though, is precisely what campaigners want to achieve. A more potent criticism of higher wages is that they cause job losses. And on January 15th

Walmart announced that it would close 154 stores in America, with the possible loss of 10,000 jobs.

The firm says that wage costs are not to blame. The closures mostly reflect Walmart's wholesale abandonment of its small "Walmart Express" stores. Elsewhere, Walmart hired 8,000 new department managers at the same time as raising pay. Adding middle-management is hardly the hallmark of a firm set on trimming its labour force (though some say hours have been cut instead).

Not every firm would find it easy to copy Walmart. Wages only cost retailers 9.5% of their revenues. In the food-and-drink industry—a prime target of the "Fight for $15" campaign to raise the minimum wage—wages amount to 31% of revenues (see chart). A much higher fraction of workers in the food, drink and hotel industries make the minimum wage, so any rise would have a greater effect on those industries. Even within retailing, there are nearly 600,000 small firms with fewer than 20 workers. In Mississippi, half of all cashiers make less than $8.79 an hour; a big increase there would have unpredictable effects.

Walmart has had some difficulty with the move. Long-serving staff who already earn more than $10 are miffed at missing out on a bumper rise. A section of Reddit, an online message board, for Walmart employees is filled with complaints. "I'm mad at the company...for invalidating 15 years of my hard work," writes one.

Incrementally higher wages will not much reduce the welfare bill for Walmart's workers; campaigners will go on claiming that low-wage firms are subsidised. Whether they are right depends on who bears ultimate responsibility for caring for the poor and sick. Campaigners think it is employers, which implies that government-funded health care in Britain or Canada is primarily a subsidy for businesses. And employers, unlike governments, can disappear in response to regulation.

It is usually more efficient to let market outcomes play out and leave transfers to the government. Still, minimum wages, set carefully, are beneficial—perhaps even for the firms who pay them. Another piece of Sam Walton's advice: "High expectations are the key to everything."

From the print edition: United States