General Equilibrium Effects of the Minimum Wage

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Abstract

We examine the impact of a large minimum wage increase on macroeconomic outcomes by developing a search-matching model with heterogeneous households and an endogenously determined unemployment rate. The model is calibrated to replicate the U.S. economy, allowing us to simulate minimum wage increases. We find negative nonlinear effects of a substantial nationwide minimum wage increase on macroeconomic outcomes, including employment. In the \$15 minimum wage scenario, output falls by approximately 12% relative to the baseline while the unemployment rate increases to 9.6% from 5% in the baseline. The net job loss is relatively small during the transition path immediately after a minimum wage increase, which has implications for the appropriate design of empirical analyses using natural experiments.

Keywords: Minimum Wage, Search and Matching, Heterogeneous Agents, Mean Field Game

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