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WILL CONGRESS BOOST THE MINIMUM WAGE?

According to opinion polls, more than eighty percent of Americans support raising the minimum wage by two dollars, from \$5.15 to \$7.15 per hour, with almost half of the country strongly in favor of doing so. Such lopsided majorities explain why congressional Democrats are forcing votes on the issue with four months to go before national elections. They have launched their offensive as congressional Republicans review internal polls showing they could lose control of the House and see their Senate majority shrivel from 55 to 51 seats this November. Although raising the minimum wage may be bad public policy, Republican politicians are loath to buck large majorities when they fear control of Congress at stake. Adding to the sense of inevitability is that the current \$5.15 rate took effect almost nine years ago, on September 1997. On average, Congress has raised the minimum wage every three years.

The combination of electoral defeat with the time lag since the last increase raises the danger of owning the securities of firms that employ many minimum wage workers. Their costs could go up significantly and their profits go down if the Republican Congress raises the minimum wage – especially if the increase is 39 percent, to \$7.25 per hour, as Senator Kennedy proposes.

What Industries Are Most At Risk?

Department of Labor statistics show that the owners of restaurants, hotels, and amusement parks have the greatest percentage of minimum wage workers. The Department has reported that 1.2 million workers in the “leisure and hospitality industry” earn “at or below \$5.15 hour.” (see Table 5 of <http://www.bls.gov/cps/minwage2005.pdf>, “The Characteristics of the Minimum Wage Worker”). Since total employment in the leisure and hospitality industry stands at 12.8 million (<http://www.bls.gov/iag/leisurehosp.htm>), the direct cost of employing ten percent of the workers in the industry could rise if Congress mandates an increase in the federal minimum wage. Indirectly, the cost of hiring another ten percent of industry workers also could go up if Congress acts, as workers now earning \$8 to \$10 an hour, for example, demand raises to restore the relative pay scale. Finally, minimum wage increases link indirectly into other industries through collective bargaining; some union contracts tie pay raises to minimum wage rate increases.

Leisure and Hospitality Firms in the South and West Face the Most Danger

While ten percent of all leisure and hospitality workers earn the minimum or less, this disguises the impact of local laws. Under federal law, cities and States have the option to raise the minimum wage above the federal floor of \$5.15 per hour in their jurisdictions. Twenty-three states, plus a few cities, have chosen to do so. In fact, sixty percent of American workers live in

areas where the minimum wage has been raised above the federal minimum. Furthermore, there are important regional patterns; ten of eleven states in the northeast have raised the minimum while ten of thirteen southern states, and sixteen of twenty-six western and midwestern states, have not done so. If ten percent of all workers in the leisure and hospitality industry earn \$5.15 or less, then the percentage of employees earning this amount is likely to be higher for firms that are concentrated in the south, west, and midwest magnifying the impact on the bottom line. Similarly, firms that do business exclusively in the Northeast may have little to fear from a federal boost in the minimum wage. Under State laws, they already pay more than \$7 per hour.

Current or Legislated Future Minimum Wage Rates No Later than 2008

Twenty- Seven States where the \$5.15 per hour federal minimum applies:

The South: Alabama, Georgia, Kentucky, Louisiana, Mississippi, Oklahoma, South Carolina, Tennessee, Texas, Virginia

The West: Arizona, Colorado, Idaho, Montana, Nevada, New Mexico, Oklahoma, Utah, Wyoming

The Midwest: Indiana, Iowa, Kansas, Missouri, Nebraska, North Dakota, Ohio, and South Dakota

The Northeast: New Hampshire

Twenty-Three States where state law mandates, or will be by 2008, a wage higher than the \$5.15 per hour federal minimum:

The South: Arkansas (\$6.25), Florida (\$6.40), and North Carolina (\$6.15)

The West: Alaska (\$7.15), California (\$6.75), Hawaii (&.25), Oregon (\$7.50), Washington (\$7.63)

The Midwest: Illinois (\$6.50), Michigan (\$7.40), Minnesota (\$6.15), West Virginia (\$5.85), Wisconsin (\$6.50)

The Northeast: Connecticut (\$7.40), Delaware (\$6.15), Maine (\$7.00), Maryland (\$6.15), Massachusetts (\$7.50), New Jersey (\$7.15), New York (\$7.15), Pennsylvania (\$7.15), Rhode Island (\$7.40), and Vermont (\$7.25)

Sources: National Conference of State Legislatures, NC and PA local news reports

Here are some publicly-held leisure and hospitality firms that could feel the largest impact of a boost in the minimum wage:

- ▶ Large Caps: McDonald's (**MCD**), Yum Brands (**YUM**), Wendy's (**WEN**)
- ▶ Mid-Caps: Aramark (**RMK**), Darden Restaurants (**DRI**), Outback Steakhouse (**OSI**)
- ▶ Small Caps: Sonic Corp (**SONC**), Ruby Tuesday (**RI**), Papa John's (**PZZA**), Cracker Barrel (**CBRL**), Cedar Fair (**FUN**), Six Flags (**SIX**)

With both national and international operations, McDonalds, YUM Brands, and Wendy's have less exposure than smaller fast-food chains, but they would still be harmed by a rise in the national minimum wage. Mid-cap and small-cap vulnerability is heightened because of believed high regional sales concentrations outside the northeast, as determined by reviewing public

filings and the companies' web pages which show their operating locations. Interestingly, we can not identify any major hotel vulnerabilities. The hotel chains we reviewed have most of their operations in states or cities with high minimum wages, greatly diminishing the impact on them of a national minimum wage increase, and they also are diversified internationally.

Wily Congressional Republicans Might Evade the Threat Without Passing a Law

Before a bill can become law, both the House and Senate must pass an identical measure and the President must sign it. This creates the possibility that the House and Senate each could pass different measures boosting the minimum wage but deliberately not reconcile the measures and send a bill down to President Bush before the fall elections. Individual Republican Representatives and Senators could truthfully say they had voted to raise the minimum wage, with each member inoculating himself against charges he was ignoring 80 percent majorities that want to see the minimum wage lifted.

Another possibility is to offer Senate Democrats an unpalatable choice: put an increase in the minimum wage inside a package that contains features they oppose more strongly than they support raising the minimum wage. This maneuver would allow almost all Senate Republicans to claim they had voted for an increase in the minimum wage and yet claim it was defeated by Democratic opposition. This is, in fact, what has happened. On June 21, 2006 45 Senate Republicans voted in favor of a package that:

- Raises the federal minimum wage \$1.10, from \$5.15 to \$6.25 per hour.
- Raises the small business exemption from federal overtime and minimum wage laws to companies with \$1 million in revenue, up from \$500,000.
- Permits bi-weekly "flex-time," so that workers could work 30 hours one week and fifty hours the next week, without earning "time-and-one-half."
- Overrides the laws of Alaska, California, Minnesota, Montana, Nevada, Oregon, and Washington so that restaurant owners there can apply a "tip credit" allowing them to pay \$3.02 less than the federal minimum wage to workers who get most of their compensation in tips, as is done in the other 43 states.
- Grants 15 year depreciation lives, down from the current 39.5 years, for new long-lived restaurant assets placed in service or for newly built restaurants.

Democratic opposition to flex time, to the boost in the small business exemption, and to the national imposition of a "\$3.02 tip credit" led Democratic Senators to vote 44 to 0 against Senator Enzi's (R-WY) proposal. These 45 Democrats were joined in opposition by eight Republicans who apparently do not favor an increase in the minimum wage even as part of a pro-business package, plus one other Republican, who shared the Democrats' hostility to the tradeoff. Therefore, the GOP proposal fell, 45 to 53.

The Next Legislative Step

Before Congress takes its August recess, the House is expected to approve a Republican package proposal that will combine an increase in the minimum wage with tax breaks for companies adversely impacted by a boost in the minimum wage.

Odds of Final Passage of a Harmful Bill This Year: 40 Percent

Last month, the Senate Republicans strategy of linking a boost in the minimum wage to other changes in labor laws that Democrats oppose led to the derailment of the bill. Unless Senate Democrats or Senate Republicans relent, this pattern will be repeated and no bill will become law, despite House passage of a hike.

However, one side or the other may blink, which is why CAN recommends steering clear of securities most likely to be affected. A forty percent probability is more than a minimum chance of occurrence.

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