

A Sizeable Increase in the Minimum Wage and a Lower VAT: Identifying their Effects on Prices in Mexico

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Abstract

In January 2020, the minimum wage in the Mexican Border with the United States increased by a 100%. At the same time, the value-added tax (VAT) rate was halved. We develop a two-step identification strategy to estimate the effects of the minimum wage and the VAT on prices separately. We account for differential effects of the minimum wage on prices of goods with and without VAT. In the border, we find that the increase in the minimum wage is associated with a statistically significant increase in the prices of goods that pay VAT. The increases in prices due to the minimum wage were more than offset by decreases associated with the VAT, resulting in average prices that were lower than those that would have been observed in the absence of these policies.

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