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DR. EDWARD TIMMONS

CUTTING THE COMPETITION?

THE EFFECTS OF LICENSING BARBERS IN ALABAMA

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The Mackinac Center for Public Policy

Cutting the Competition? The Effects of Licensing Barbers in Alabama

By Edward Timmons

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Introduction and Summary of Results

Data released by the Bureau of Labor Statistics in 2016 suggests that 22.3 percent of employed workers in the United States held an active occupational license.[1] To obtain a license, workers are typically required to pay fees, complete minimum levels of schooling and training, pass exams and meet a variety of other requirements. As a result of the work of Morris Kleiner, the Institute for Justice, the Obama White House and a number of other researchers and public policy advocates, a renewed interest in the subject has emerged within the last several years.[2] The Mackinac Center, for example, published a comprehensive report on licensing requirements in the state of Michigan just last year.[3]

But measuring the impact that licensing has on the economy and consumers is difficult. Since unlicensed providers are operating illegally, there is no reliable data to compare their outcomes to those of licensed providers. Further, few states have ever delicensed occupations, making it difficult for economists to find a "natural experiment" to study — in this case, comparing outcomes from a period when licenses were required to a period when licenses were not required.

Despite this, there are data available to study the impact of a change in licensing that occurred in Alabama regarding barber licensure. For the 30-year period from 1983 to 2013, the state of Alabama did not require barbers to obtain a state license before they could work legally.[4] But then the Yellowhammer State reintroduced a barber licensing requirement in late 2013.[5] This provided a type of natural experiment to study, and this paper estimates the impact of the new occupational licensing requirement had on barbers and consumers in Alabama.

Barbering is universally licensed in the United States. The Institute for Justice published "License to Work" in 2012, a report that presents a snapshot of barber licensing requirements across states. Licensing fees in 2012 ranged from as little as $20 in Michigan to as much $330 in Kentucky.[6] Education and experience requirements for the profession range from 175 days in Wyoming to 890 in Nevada.[7] The wide variety of licensing requirements is a microcosm of what occupational licensing requirements look like for most professions from state to state.

In this paper, I estimate the effects of Alabama's reintroduction of barbering licensing requirements on the receipts and growth of barber shops in the state. I rely on U.S. Census Nonemployer Statistics data for 2009 to 2014. I perform state-level comparisons of barber and beauty shops in Alabama, as well as comparing these Alabama statistics to that of nearby bordering states. In addition, I compare data from Alabama border counties to data from contiguous counties in Georgia and Florida.

The results of this analysis show that after barber licensing was introduced in Alabama, barber shop receipts grew 2.6 percentage points faster than beauty shops and barber shops per person grew 6.7 percentage points slower than beauty shops in the state. In other words, barber licensing requirements appear to have limited competition for existing Alabama barbers and they benefited with higher earnings. A similar result emerges when comparing barber shops in bordering states and bordering counties in Georgia and Florida. This comparison produces evidence consistent with the economic theory that occupational licensing restricts competition and harms consumers by limiting choice and increasing prices.

Theory and Evidence on the Effects of Occupational Licensing

What effects should occupational licensing have in the marketplace? Economists have proposed two main theories on how occupational licensing should affect workers and consumers. About 50 years ago, Milton Friedman and George Stigler hypothesized that occupational licensing imposes a barrier to entry into the labor market.[8] By mandating that job seekers pay fees, complete training or education and take tests, licensing makes it more expensive for job seekers to begin work and the supply of labor decreases, forcing consumers to pay a higher fee for services from licensed workers. As a result, licensed workers will receive higher compensation. This view suggests that the effects of occupational licensing are unambiguously negative for consumers — they have fewer service providers to choose from and pay a higher price for it.

Alternative theories have also emerged in the economics literature. Building on the theory of George Akerlof, Hayne Leland suggests that occupational licensing may enhance consumer welfare by signaling high quality services.[9] The price of professional services will still rise as a result of occupational licensing, but the increase will be primarily demand driven. Leland acknowledges, however, that "if quality standards are set by the profession (or industry) itself, it is likely that the standards will be too high [relative to optimal, economically efficient standards]."[10] A subsequent paper by Carl Shapiro suggests that licensing increases workers' skills and may therefore enhance the quality of services delivered to consumers.[11]

Despite these different theoretical estimates on the impact of licenses, it should be noted that there is general agreement that occupational licensing increases the price of professional services. The important question then is whether the increase in prices is primarily supply-driven, as suggested by Friedman and Stigler, or demand-driven, as suggested by Leland and Shapiro.

Looking at the available price data, national estimates suggest that licensed workers earn as much as a 15 percent wage premium.[12] There is little evidence that occupational licensing improves the quality of services provided consumers. A 2015 paper prepared by the Obama administration's Council of Economic Advisors, the U.S. Department of Treasury and the U.S. Department of Labor notes that only two of 12 studies on the subject find evidence that stricter occupational licensing standards result in an improvement in the quality of services delivered to consumers.[13]

A handful of papers have specifically focused on the effects of barber licensing, as this report does. Robert Thornton and Andrew Weintraub in 1979 found little evidence that stricter barber licensing requirements are associated with any change in the number of practicing barbers.[14] A study by Morris Kleiner in 2000 finds little evidence that licensing has increased barber earnings.[15] More recently, an analysis I co-authored finds evidence that stricter barber licensing correlates with higher barber pay (between 11 and 22 percent) and a reduction in the number of practicing barbers.[16] I have also estimated the effects of Alabama removing barber licensing requirements in 1983 and find evidence that the removal is associated with a reduction in barber pay and a reduction in cosmetologist employment.[*] Another recent paper finds evidence that stricter barber licensing is associated with a reduction in the number of barber shops.[17]

The contribution of this paper will be to focus on Alabama's reinstitution of barber licensing in 2013. Economic theory suggests that licensing should increase the earnings of barbers, but is less clear with respect to the effect on the number of practicing barbers. Finding evidence of a reduction in the number of barbers would be more closely associated with the supply-driven explanation of the effects of licensing and be more consistent with the theory of Friedman and Stigler. Less convincing evidence of a supply effect may lend some support to the theories of Leland and Shapiro.

Occupational Licensing Reform Efforts

Before turning to the empirical analysis of this paper, it is important to note the history of recent reforms to occupational licensing. Historically, the removal of occupational licensing laws has rarely occurred. In an analysis that I co-wrote for the Bureau of Labor Statistics, we were able to find just eight instances of successful removal of occupational licensing laws in the last 40 years.[18] Interest in reform has grown in recent years, however. From 2011 to mid-2016, 12 states proposed comprehensive occupational licensing reform.[19] Interestingly, the state of Michigan was the most active of the 12 states in actually implementing reform — having delicensed a handful of occupations.[20]

Interest in reform has been growing at the federal level as well. In addition to the publication of the aforementioned white paper by the Obama administration in 2015, the Federal Trade Commission has become a more vocal advocate for reform. In early 2017, the FTC launched the Economic Liberty Task Force that serves as a resource for informing the public on the negative effects of occupational licensing.[†]

As states begin to implement occupational licensing reform, what benefits should accrue to consumers and prospective workers? Economic theory would suggest that prices of services provided by licensed workers should decrease. By examining the effects of Alabama establishing barber licensing requirements in 2013, it is possible to identify the benefits that Alabama consumers may have relinquished as a result of the new law.[‡] This might provide insights into the potential benefits of licensing reforms being discussed in states around the country.

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[*] Cosmetologists offer similar services to barbers, but are generally subject to different regulations. See Edward J. Timmons and Robert J. Thornton, "Here, There and Back Again: The Licensing, De-Licensing, and Re-Licensing of Barbers in Alabama," Dec. 21, 2016, https://perma.cc/CXY7-X28K.

[†] "Economic Liberty: Opening Doors to Opportunity" (Federal Trade Commission, 2017), https://perma.cc/Q67D-GBEB. It should be noted that the FTC has consistently promoted occupational licensing reform through its research and advocacy since the late 1970s.

[‡] For more background on Alabama regulation of barbers, see: Edward J. Timmons and Robert J. Thornton, "Here, There and Back Again: The Licensing, De-Licensing, and Re-Licensing of Barbers in Alabama," Dec. 21, 2016, https://perma.cc/CXY7-X28K.

Data and Empirical Method

To analyze the effect of Alabama's reintroduction of barber licensing, I rely on data obtained from U.S. Census Nonemployer Statistics. The data contain annual counts of the number of businesses and total receipts by industry for businesses with no paid employees and that are subject to federal income tax.* Most barber shops are small, owner-operated businesses and so fit this category.

I perform state-level analysis comparing Alabama to the bordering states of Florida, Georgia, Mississippi, North Carolina, South Carolina and Tennessee. I also perform county-level comparisons between neighboring states of Alabama, but data allow me to examine only bordering counties in Georgia and Florida.

I also examine trends in barber shops compared to beauty shops. Other things held equal, we might expect to see similar trends over time with respect to both barber and beauty shops. Beauty shops employ or may be owned and operated by cosmetologists. Cosmetologists, in addition to cutting hair, offer additional services and have traditionally been the service provider of choice for females. Alabama beauty shops were not directly affected by the change in barber licensing in 2013 and serve as the closest comparison group within the state.

Using data from 2009 to 2014, I compute the number of barber and beauty shops per person in each of the analyzed states. I then compute an annual growth rate in the number of barber and beauty shops for each state. I perform a similar calculation for each border county.

I also compute the average receipts per shop by dividing total receipts by the number of shops in each state. Receipts include sales, commissions and income as reported on annual business income tax returns.[21] It should be pointed out that the receipts published may be subject to underreporting — particularly if the business is cash-based. There is no reason to believe, however, that underreporting should differ significantly as a result of occupational licensing. Thus, the underreporting should not bias the analysis that follows.

All theories of the effects of occupational licensing would suggest that Alabama's adding of new licensing requirements should increase average receipts for existing barber shops. Existing barber shops were also not subject to the new regulation — the licensing law contained a "grandfather" provision, meaning only new barbers needed to become licensed. With the bar raised to market entry and facing less competitive pressure, barbers may have the luxury of charging higher prices and thus receiving more revenue.

What is less clear is how the number of shops would be affected. If the number of shops falls, this would be more consistent with the theory of Friedman and Stigler that licensing is primarily restricting competition. On the other hand, if the number of shops increases or does not change much, this might be more in line with the theories of Leland and Shapiro — that licensing has

* See https://www.census.gov/econ/nonemployer/ for more information on this data.

less of an effect on supply and could potentially work towards enhancing the quality of services delivered to consumers.* In the analysis that follows, I will examine the evidence presented in the data.

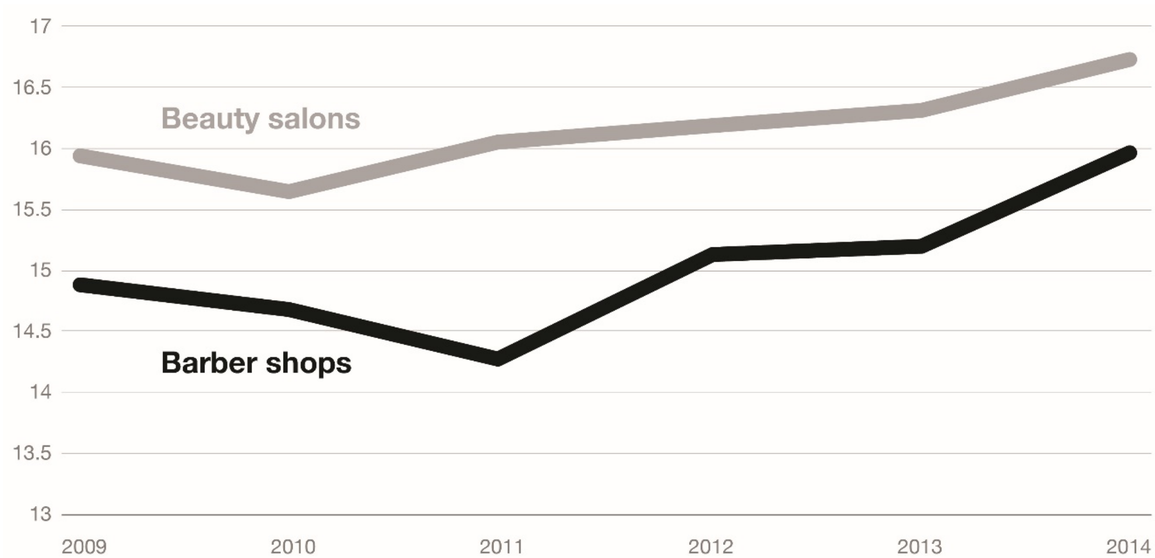
Statistical Analysis

State-Level Analysis

To examine the effect of new barber licensing in Alabama, I first compare average receipts for barber and beauty shops in the state, shown in Graphic 1. As noted previously, barbers and cosmetologists offer similar services and the demand for both services should be affected similarly by macroeconomic events — for example, drops in consumer income. In the graphs that follow, Alabama barber shops are represented by the solid black line and beauty shops are represented by the gray line. Receipts per shop — in thousands of dollars — are measured on the vertical axis.

Average receipts for barber shops increased from $15,200 in 2013 to $15,970 in 2014, a 5.1 percent increase. Average receipts for beauty shops increased from $16,300 in 2013 to $16,700 in 2014, a 2.5 percent increase. Following the adoption of barber licensing in Alabama, barber shop average receipts grew faster — a 2.6 percentage point difference — than beauty shop receipts. This suggests that the new licensing requirements resulting in increased earnings for incumbent barbers and squares with the general agreement in economic theory.

Graphic 1: Average Receipts in Barber and Beauty Shops in Alabama, 2009-2014



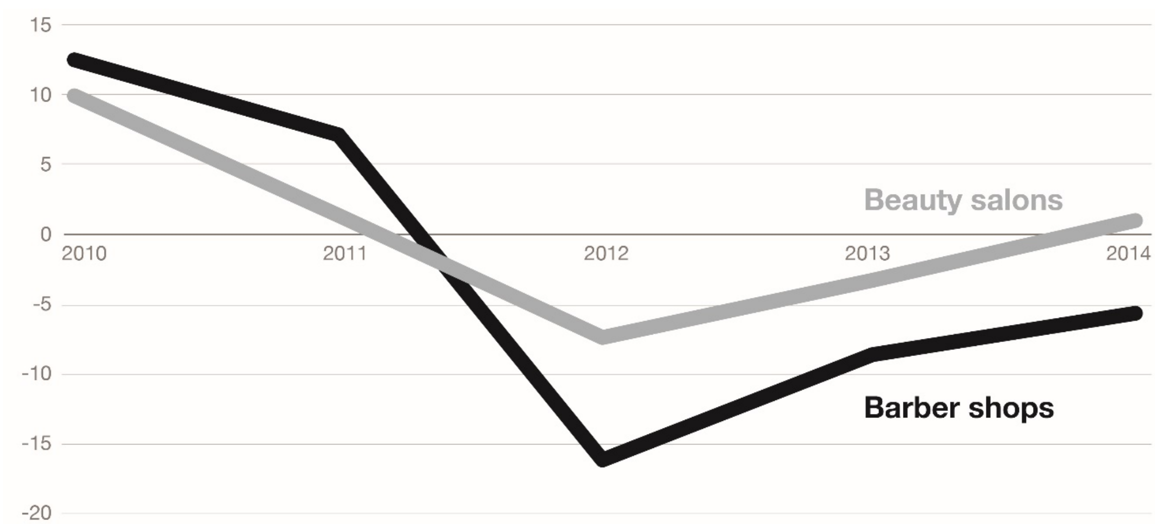
Note: All data from U.S. Census Nonemployer Statistics, 2009-2014.

* Without directly observing quality, it is not possible to definitively test Leland and Shapiro's theory. Instead, I am looking for evidence supporting Friedman and Stigler's theory.

Although all theories of the effects of occupational licensing would suggest a result like what is presented in Graphic 1, there is disagreement with respect to how the number of barber shops will be affected. In Graphic 2, I measure growth in barber and beauty shops per person per year in percentage terms.

Barber shops per person in Alabama shrank from 2013 to 2014 — falling by 5.7 percent. Beauty shops per person, on the other hand, increased in from 2013 to 2014 — growing by nearly 1 percent for the year. The gap in growth rates between the two shops is approximately 6.7 percentage points. It is possible that consumers in Alabama may be choosing to substitute cosmetology services for barbering services with more frequency after licensing takes effect. This result is supportive of the hypothesis that barber licensing is primarily restricting competition as hypothesized by Friedman and Stigler.

Graphic 2: Annual Barber and Beauty Shop Per Capita Growth in Alabama, 2010-2014

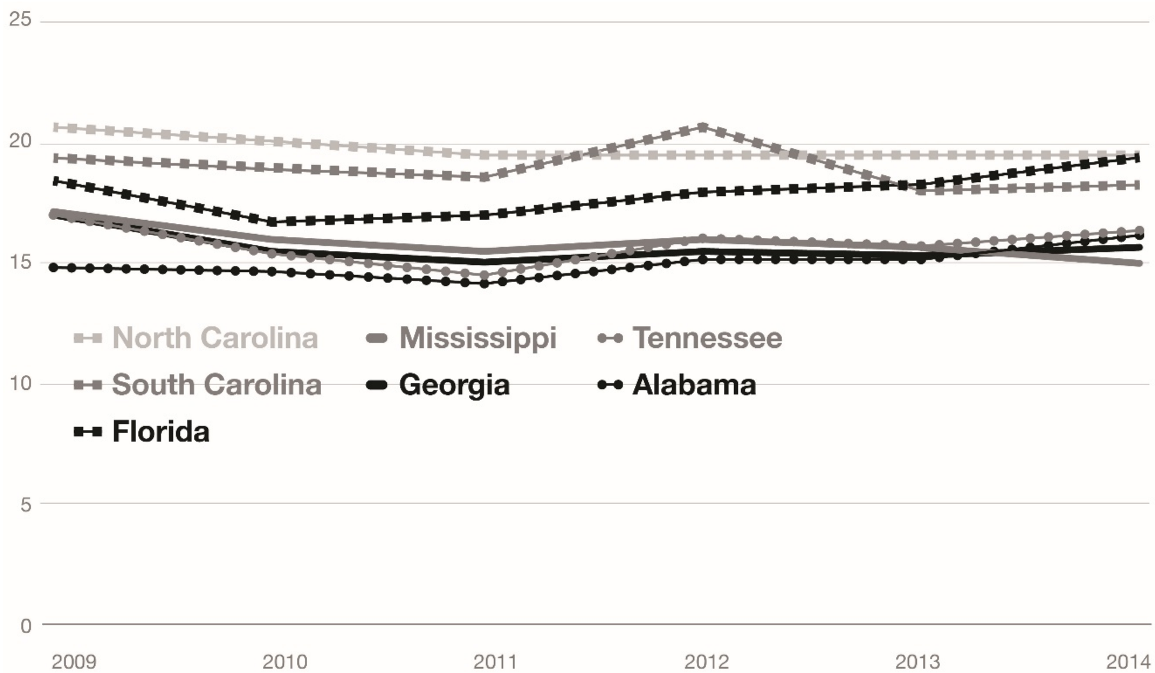


Note: Data from U.S. Census Nonemployer Statistics, 2009-2014. Population data is extracted from the U.S. Census.

Although barber and beauty shops offer similar services, it is possible that slightly different trends may emerge for each of these different businesses. The clientele of beauty shops may have different tastes or preferences and this might cause unrelated differences to emerge. To address this potential inherent difference, I compare the same two variables for barber shops — average gross receipts and businesses per person — in Alabama to those in the bordering states of Florida, Georgia, Mississippi, North Carolina, South Carolina and Tennessee. In Graphic 3, receipts per barber shop — in thousands of dollars — are again measured on the vertical axis. Like beauty shops in Graphics 1 and 2, barber shops in these bordering states experience no change in licensing regulation in 2013.

Before Alabama introduced new barber licensing requirements, receipts per shop in Alabama were generally below bordering states. Alabama had average receipts of $14,890 in the years preceding 2013, while the next closest state was Tennessee at $16,820 and the average for all six bordering states was $18,160, or approximately 22 percent more prior to 2013. Following the implementation of new licensing in 2014, Alabama's average receipts were $15,970, much closer to bordering states' average of $17,160 and actually ahead of Georgia and Mississippi. This result is consistent with theory, namely that Alabama adding barber licensing requirements allowed barbers the opportunity to charge higher prices for their services.

Graphic 3: Average Receipts in Barber Shops in Alabama and Bordering States, 2009-2014

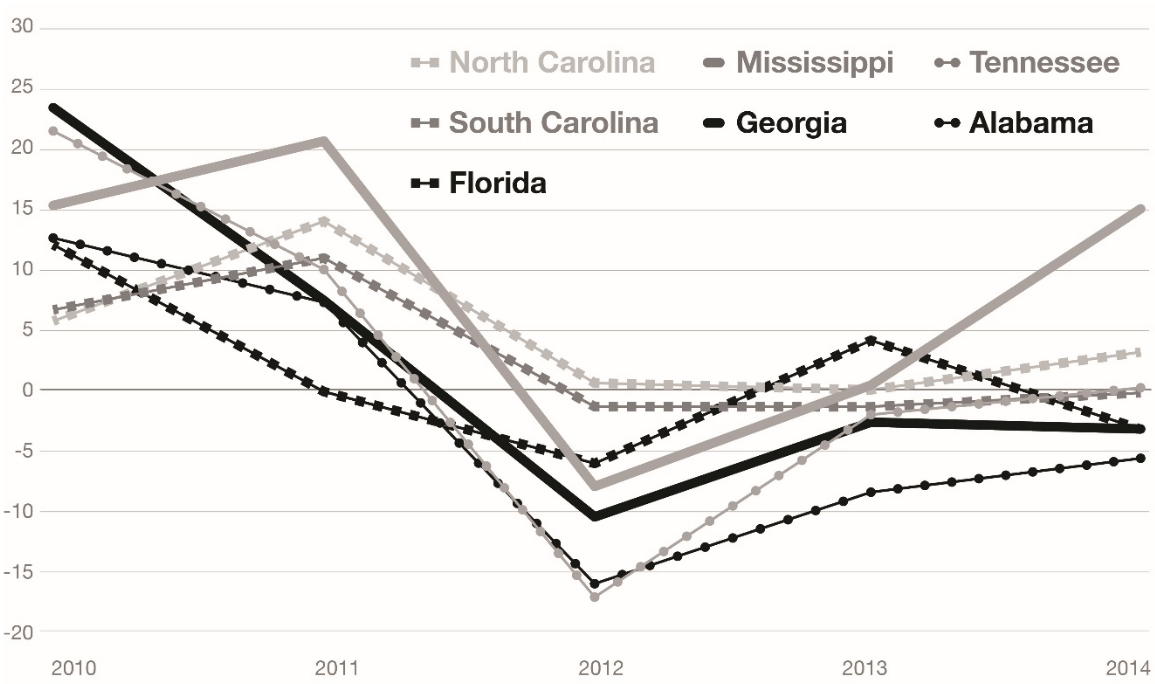


Note: All data from U.S. Census Nonemployer Statistics, 2009-2014.

Turning to growth in barber shops per person — displayed in percentage terms on the vertical axis in Graphic 4 — Alabama's average growth was slightly below the average of contiguous states in the years preceding 2013: 1.2 percent in Alabama versus 5.8 percent in bordering states. After new licensing requirements were instituted, Alabama's growth in barber shops per person fell significantly below the average of bordering states. In 2014, bordering states experienced shop growth per person of 2 percent on average. Alabama's shops per person actually fell by 5.7 percent — a 7.7 percentage point difference relative to bordering states. This result also seems to support the Friedman and Stigler's supply-side effect hypothesis that Alabama's new licensing requirement is restricting competition.

In summary, both of these comparisons — barber and beauty shops in Alabama and barber shops in Alabama and bordering states — shed some light on the effects that new barber licensing had in Alabama. Barber licensing seems to have resulted in higher profits for existing barber shops and fewer opportunities for new barber shops. Relative to both beauty shops in the state and barber shops in bordering states, Alabama barber shop growth was notably lower. Taken together, it would appear that new barber licensing in Alabama is harmful to consumers and has the effect of restricting competition in the marketplace.

Graphic 4: Annual Barber Shop Per Capita Growth (%) in Alabama and Bordering States, 2010-2014



Note: Data from U.S. Census Nonemployer Statistics, 2009-2014. Population data is extracted from the U.S. Census.

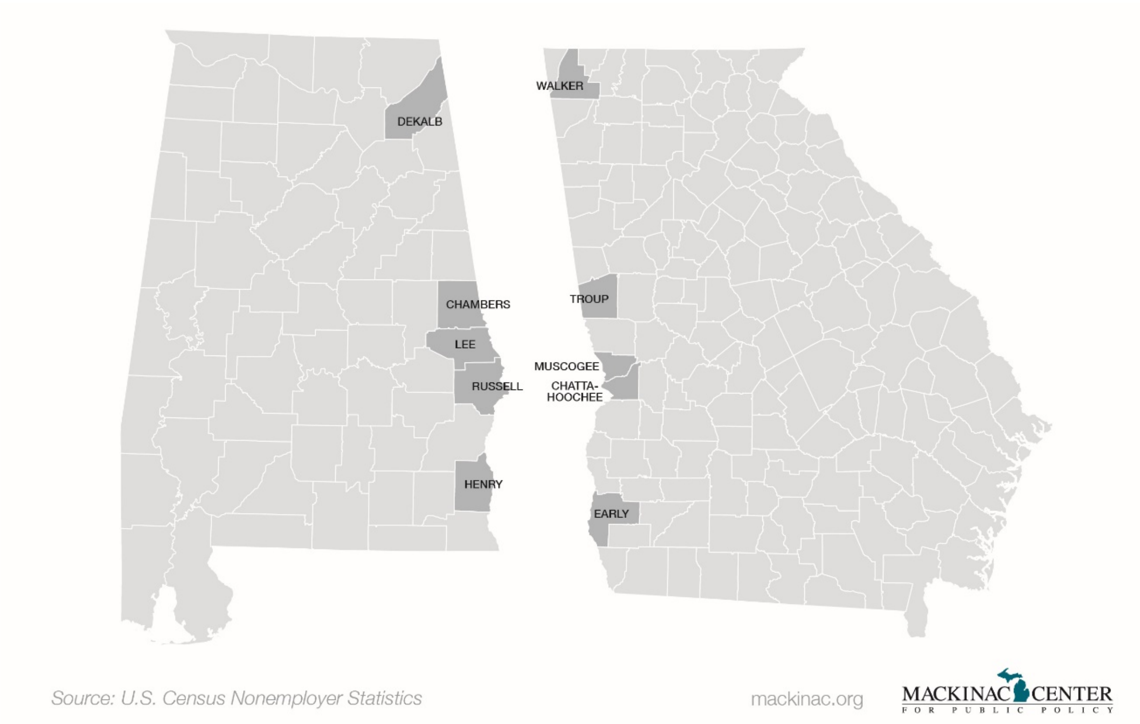
County-Level Analysis

For this analysis, I compare county-level data from Alabama border counties to contiguous counties in Georgia and Florida. Data were unfortunately very limited for other bordering states and it was not feasible to produce similar comparisons at the county level. In addition, data from several bordering counties in Georgia and Florida were sometimes redacted by the Census Bureau for privacy concerns resulting from a small sample size. I use the same set of outcome variables from the previous state-level analysis — receipts per shop and barber shop per person growth. The graphics below identify the bordering counties of Alabama and Georgia used in the analysis.

Graphic 5: Border Counties in Alabama and Georgia Used in Analysis

Georgia	Alabama
Chattahoochee	Chambers
Early	DeKalb
Muscogee	Henry
Troup	Lee
Walker	Russell

Graphic 6: Alabama and Georgia Bordering Counties Used in Analysis



Graphic 7 contains a comparison of barber shops in Alabama and Georgia counties before and after the adoption of barber licensing in Alabama in 2013. Prior to the adoption of licensing, Alabama experienced much faster growth in barber shops per person in its border counties compared to those in Georgia border counties. Barber shops per person grew by 5.9 percent on average from 2009 to 2013 in Alabama border counties compared to a decline of 15 percent of the same measure in Georgia border counties.

Immediately after the adoption of licensing, growth in barber shops per person in Alabama border counties slowed to an average of 1.9 percent and bordering Georgia counties entirely reversed the recent trend of decline and grew at a 2.2 percent average rate. This suggests that consumers in Alabama may now be frequenting shops in Georgia as a result of the new barber licensing law. Relative to the period before the adoption of licensing, Alabama border county shop growth is a full four percentage points lower.

Graphic 7: Georgia-Alabama Border County Comparison

Without Barber License, 2009-2013	Barber Shop Growth Per Capita	Average Receipts Per Barber Shop
Georgia border counties	-15%	$13,600
Alabama border counties	5.9%	$15,100
With Barber License, 2013-2014	**Barber Shop Growth Per Capita**	**Average Receipts Per Barber Shop**
Georgia border counties	2.2%	$15,600
Alabama border counties	1.9%	$19,000

Note: Data (except population) from U.S. Census Nonemployer Statistics 2009 to 2014. Population data is extracted from the U.S. Census.

Receipts per shop grew in both sets of bordering counties after licensing went into effect in 2013, but grew much more quickly in Alabama. Receipts per shop increase by $2,000, or 14.7 percent, in Georgia counties, but increased by $3,100, or 25.8 percent, in Alabama counties. Both of these comparisons yield information very similar to the state-level analysis from the preceding section.

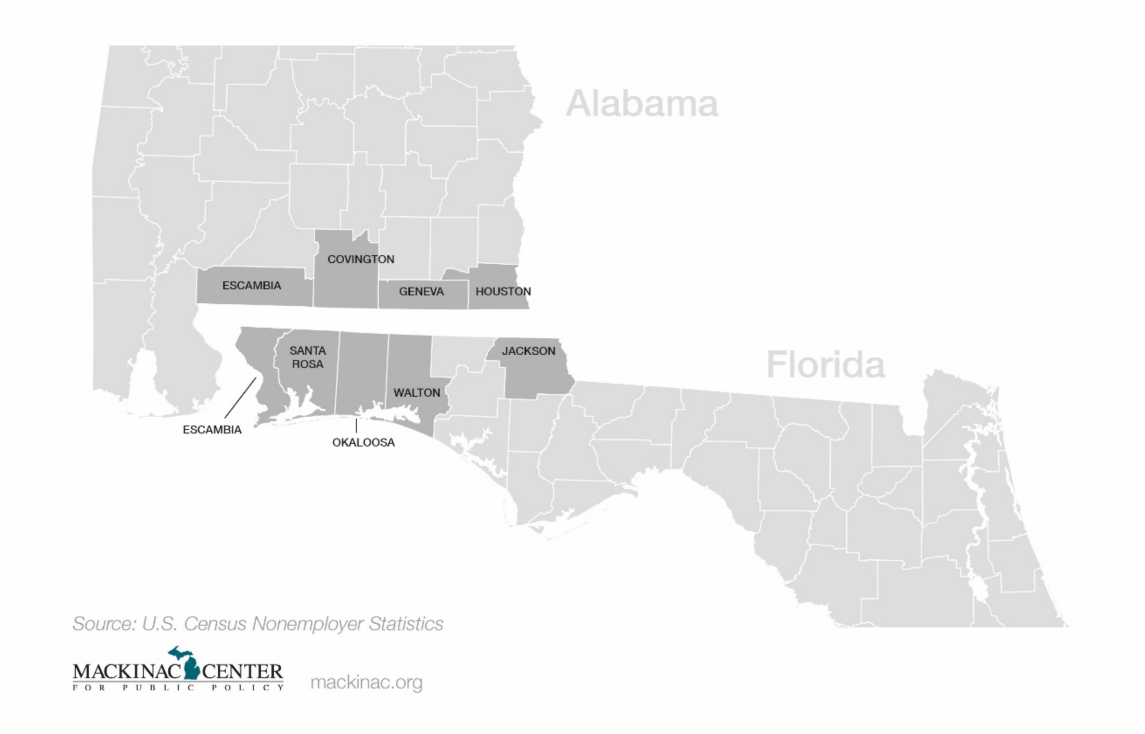
In summary, barber licensing is associated with a drop in barber shop growth and an increase in receipts per existing barber shop in Alabama. This is consistent with the theory of licensing inhibiting competition in the market for haircutting services in the state. I also observe evidence consistent with possible shifts in consumer demand from barbering services in Alabama to barbers in Georgia.

Graphics 8 and 9 identify bordering counties of Alabama and Florida used in this analysis for comparison purposes. Once again, data are not reported for some border counties by the Census Bureau as a result of the small sample.

Graphic 8: Border Counties in Florida and Alabama Used in Analysis

Florida	Alabama
Escambia	Covington
Jackson	Escambia
Okaloosa	Geneva
Santa Rosa	Houston
Walton	

Graphic 9: Florida and Alabama Bordering Counties Used in Analysis



Focusing first on average barber shop per person growth, the comparison here is consistent with the previous analyses. Although shop growth falls after 2013 in both Florida and Alabama counties, growth decreases by a much larger magnitude in Alabama border counties compared to those in Florida: -7.8 percent to -3.6 percent, respectively. Interestingly, receipts per shop decrease in both Florida and Alabama bordering counties and by a similar amount.

Graphic 10: Florida-Alabama Border County Comparison

Without Barber License, 2009-2013	Barber Shop Growth Per Capita	Average Receipts Per Barber Shop
Florida border counties	2.9%	$19,900
Alabama border counties	1.0%	$16,700
With Barber License, 2013-2014	**Barber Shop Growth Per Capita**	**Average Receipts Per Barber Shop**
Florida border counties	-0.7%	$18,900
Alabama border counties	-6.8%	$15,400

Note: All data (except population) from US Census Nonemployer Statistics 2009 to 2014. Population data is extracted from the US Census.

Conclusion

In this paper, I analyze the effect that the introduction of barber licensing requirements in Alabama has had on the market for barbering services in the state. By comparing data on beauty shops and barber shops in Alabama, barber shops in Alabama and bordering states, and barber shops in Alabama counties bordering Georgia and Florida, I consistently find evidence suggesting that the introduction of barber licensing in Alabama is associated with a reduction in barber shop growth in the state. I also generally find evidence that barber shop receipts increases in Alabama after the adoption of barber licensing. These results are supportive of the economic theory that licensing primarily has negative supply-side effects, restricting competition in the marketplace and thus harming consumers. As policymakers reconsider the costs and benefits of occupational licensing, this case study of barbering services in Alabama should serve as an example of the possible negative consequences of such laws.

About the Author

Edward Timmons is the associate professor of economics and director of the Knee Center for the Study of Occupational Regulation at Saint Francis University. He received his Ph.D. in economics from Lehigh University. His research on the effects of occupational licensing has been published in The Journal of Law and Economics, the Journal of Labor Research, the British Journal of Industrial Relations, Health Policy, Monthly Labor Review and Eastern Economic Journal. His research has been heavily cited by the popular press, by the Federal Trade Commission, the Obama White House and also in a Senate hearing titled “License to Compete: Occupational Licensing and the State Action Doctrine.” In May of 2014 he worked as a visiting research fellow at the Collegio Carlo Alberto in Moncalieri, Italy. He is a member of the Board of Policy Advisors of the Heartland Institute.

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