

**Safety Net Review –  
Wages**

**2004**

**Reply**

**Commonwealth Submission**

**16 March 2004**

# Table of Contents

<b>SECTION 1:</b>	<b>COMMONWEALTH POSITION</b> .....	<b>1</b>
Introduction	.....	1
Reply	.....	1
Conclusion	.....	2
<b>SECTION 2:</b>	<b>ECONOMIC OUTLOOK</b> .....	<b>3</b>
Introduction	.....	3
Economic updates	.....	3
Company profits	.....	3
Conclusion	.....	6
<b>SECTION 3:</b>	<b>WAGES DEVELOPMENTS</b> .....	<b>7</b>
Introduction	.....	7
Recent developments	.....	7
Workplace agreements	.....	8
Living standards and the WCI	.....	9
Real value of the Federal Minimum Wage	.....	9
Conclusion	.....	11
<b>SECTION 4:</b>	<b>PRODUCTIVITY AND WORKPLACE BARGAINING</b> .....	<b>12</b>
Introduction	.....	12
Productivity growth in award-reliant industries	.....	12
Impact on labour costs	.....	15
Distribution of productivity gains	.....	16
Conclusion	.....	16
<b>SECTION 5:</b>	<b>IMPACT ON EMPLOYMENT</b> .....	<b>17</b>
Introduction	.....	17
Minimum wages survey	.....	17
Cost of the claim	.....	19
Other research	.....	20
Sectoral impact	.....	21
Inequality and the minimum wage	.....	23
Conclusion	.....	24

<b>SECTION 6:</b>	<b>LIVING STANDARDS</b> .....	<b>25</b>
Introduction	.....	25
Budget standards	.....	25
Conclusion	.....	26

# SECTION 1: COMMONWEALTH POSITION

## Introduction

- R1.1 The Commonwealth welcomes the opportunity to respond to the Australian Council of Trade Unions (ACTU) reply submission of 9 March 2004.
- R1.2 The Commonwealth remains unconvinced by the assertions made by the ACTU that the Safety Net Review 2004 (SNR 2004) claim for an increase of \$26.60 per week in all award wage rates is moderate and economically responsible.

## Reply

- R1.3 This reply reinforces the Commonwealth position submitted to the Australian Industrial Relations Commission (the Commission) on 18 February 2004.
- R1.4 In this reply the Commonwealth provides updates for relevant economic data. Nonetheless, a short deferral of the SNR decision would enable the Commission to be informed by 2004-05 Federal Budget information.
- R1.5 The ACTU reply submission dismisses the evidence presented by the Commonwealth that large minimum wage claims have an impact on employment, particularly in award-reliant sectors of the economy and in small and medium enterprises (SMEs).
- R1.6 The ACTU reply submission pays inadequate regard to the requirement under the *Workplace Relations Act 1996* (WR Act) that the Commission must perform its functions in a way that furthers the objects of the WR Act.

- R1.7 This includes giving due regard to the public interest such as the state of the national economy and the effects that any award made may have on it, particularly any effects on inflation and the level of employment, and encouraging the making of workplace agreements.
- R1.8 The Commonwealth is of the view that the Commission must take into account that the ACTU claim for a further large safety net adjustment (SNA) comes on top of two large SNAs in 2002 and 2003.
- R1.9 The submission of the National Motor Industry<sup>1</sup> states that the potential impact of the redundancy claim coupled with the SNR 2004 claim would impose a serious financial burden and affect ongoing viability of small businesses in this industry. The Commonwealth regards this is an important consideration.
- R1.10 The Commission should also take into account in addressing the needs of the low paid, that all employees, but particularly low paid employees, benefited from personal income tax cuts from 1 July 2003.

## Conclusion

- R1.11 The Commonwealth position remains that it will not oppose an increase of up to \$10 per week in award rates up to and including the equivalent of the Tradesperson's rate – Level C10 in the *Metal Engineering and Associated Industries Award*.
- R1.12 The adjustment must apply until the next SNR and be fully absorbed into all above award payments including enterprise agreements and informal over-award agreements. There must also be at least a twelve month gap between the operative date of the previous SNA and the operative date of any adjustment awarded in this case.

---

<sup>1</sup> National Motor Industry Response to ACTU Minimum Wages Claim, Safety Net Review 2004, pp 13 and 14.

## SECTION 2: ECONOMIC OUTLOOK

### Introduction

- R2.1 The Commonwealth provides updates for recent economic data.
- R2.2 The outlook remains positive with some medium term risks around the domestic and international outlook.

### Economic updates

- R2.3 National Accounts for the December quarter 2003 confirm that Australia's growth continued to be accompanied by low inflation, with the household consumption chain price index rising by 1.5 per cent over the year.
- R2.4 The CPI increased by 2.4 per cent over the same period. Non-farm average earnings increased by 3.4 per cent over the year slightly below the annual growth in the Wage Cost Index (WCI).
- R2.5 In the year to February 2004, employment grew by 85 800 persons, or 0.9 per cent, and the unemployment rate declined to 5.9 per cent. All of this growth was in the second half of the year, with over 109 100 jobs created in the six months to February 2004.
- R2.6 The global recovery to date continues to be dependent on the United States. Strong US growth and the deterioration of the US federal budget have contributed to the large US Current Account Deficit (CAD). In these circumstances, there is continuing concern over the sustainability of the US CAD and how a subsequent correction may play out.

### Company Profits

- R2.7 The Commonwealth submission contained considerable material contesting the ACTU position that the good economic

performance of the award-reliant industries as measured by profit levels supports a large Safety Net adjustment (SNA).

- R2.8 The ACTU reply submission, at paragraphs R2.6 and R2.7, argues that Gross Mixed Income should not be included in profit measures. The Commonwealth contends that Gross Mixed Income which includes return to owners by way of wages and profits is relevant as a measure of overall business performance.
- R2.9 Whether the owner of an unincorporated business receives income by way of wages or profits is irrelevant as an indicator of capacity to pay a wage claim. If the ACTU is of the view that it is relevant, should wage claims be reduced when business owners take income by way of wages rather than profits?
- R2.10 At paragraphs R2.8 to R2.12, the ACTU further criticises the Commonwealth for using accounting rates of return as the superior measure for industry profits.
- R2.11 The Commonwealth acknowledges the point made by the ACTU that the use of economic rates of return are superior to accounting rates of return. However, the economic rate of return is not able to be calculated from the available data. The Commonwealth subtracts capital consumption from profits (gross operating surplus plus mixed income) in order to reduce the deficiencies of the accounting rates of return and address some of the ACTU's concerns.
- R2.12 Further, the Commonwealth shows that the profits data used by the ACTU only cover incorporated businesses with 20 or more employees, a point conceded in the ACTU (paragraph R2.6). The data on which the ACTU relies exclude businesses that employ less than 20 employees and unincorporated businesses. As such, it ignores the trend for small business to increasingly become incorporated.
- R2.13 These flaws are demonstrated clearly in the restaurants and catering component of the Accommodation, cafes and restaurants industry where over 90 per cent of businesses have fewer than 20 employees. The overall average profit rate for a restaurant, café

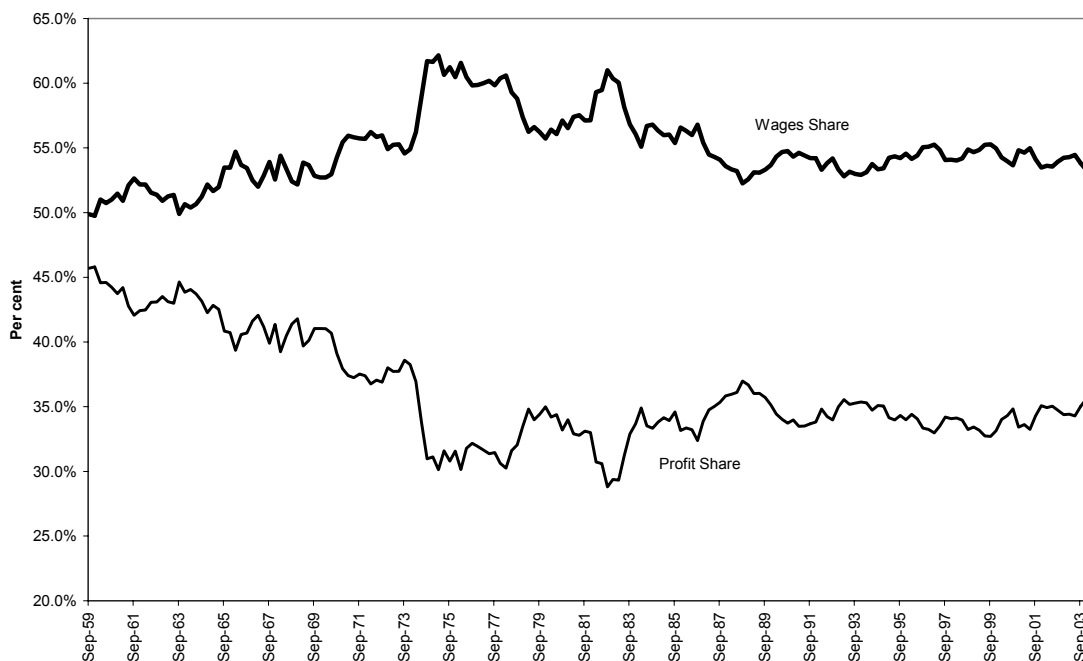
or caterer is just 1.5 per cent before tax, which is in stark contrast to the figures given by the ACTU.

R2.14 The alternative data provided in the ACTU reply submission (paragraph R2.13 and R2.14) largely confirm that there is no evidence of any significant increases in profits in the three most award-reliant industries. The data show that in each of these industries, the profit rates have been relatively stable since 1996-97 and were actually lower in 2000-01 than in 1996-97.

R2.15 The Commonwealth is not of the view that profitability in award-reliant industries is so strong that an increase in award rates of the size claimed by the ACTU will have no adverse employment or economic effects.

R2.16 Chart R2.1 below updates Chart 2.2 in the Commonwealth submission.

**Chart R2.1: Movements in profit and wages shares of total factor income**



Source: ABS, National Income, Expenditure and Product (Cat. No. 5206.0)

## Conclusion

R2.17 The Australian economy continues to maintain solid economic and employment growth. However, there remain moderate risks around the medium term outlook and the economic performance of the most award-reliant industries does not justify the granting of the ACTU claim.

## SECTION 3: WAGES DEVELOPMENTS

### Introduction

- R3.1 The Commonwealth provides new data on wage movements in the December quarter 2003.
- R3.2 Award rates that ought to be the focus of the SNR – that is, rates up to and including the Tradesperson's rate – have more than kept pace with general wages growth over the last six years.

### Recent developments

- R3.3 The trend growth in the Wage Cost Index (WCI) for December 2003 was 3.6 per cent (3.7 per cent in original terms). Trend quarterly growth has been steady over the last two years.
- R3.4 In original terms, the private sector WCI for the most award-reliant industries, Accommodation, cafes and restaurants, Retail and Health and community services, increased by 2.8 per cent, 3.1 per cent and 3.0 per cent respectively.
- R3.5 According to the DEWR Workplace Agreements Database, the average annualised wage increase (AAWI) for employees covered by Federal certified agreements current in the December quarter 2003 was 3.9 per cent. Increases for Accommodation, cafes and restaurants, Retail and Health and community services were 2.8 per cent, 3.1 per cent and 3.9 per cent respectively.
- R3.6 Under both the AAWI and the WCI the increases for the award-reliant industries tend to be well below the aggregate increases. In the same period, the FMW increased by 3.9 per cent and the tradesperson rate (C10) increased by 3.2 per cent. Both these wage rates grew faster than all but one of the award-reliant industry wage measures.

- R3.7 The ACTU asserts at paragraph R1.12 that no opposing party disputes that ‘in recent years award only workers have received average increases less than other aggregate wage measures’. The Commonwealth submission (Chart 3.5 on page 27) shows that the increases for award rates up to C10 have not lagged behind movements in the WCI. In May 2002, 44.7 per cent of all award employees earned the equivalent of C10 or less<sup>1</sup>.
- R3.8 There is no reason why increases in award wages should reflect the average increase across all wages. As noted above and on pages 22 to 24 of the Commonwealth submission, there is a considerable degree of dispersion of wage increases around the average increase, as well as across industries.
- R3.9 Increasing all award rates in line with the WCI would increase the disincentive to engage in bargaining at the workplace level and decrease the opportunity for productivity improvements.

## Workplace Agreements

- R3.10 In the 2002 SNR decision, the Commission recognised that increases in award wages have the potential to influence the speed at which agreement-making is taken up. At paragraphs R2.31 to R2.33 and R4.16 the ACTU contests the econometric worth of the analysis undertaken by the Commonwealth to support this view.
- R3.11 The ACTU criticises the Commonwealth for developing models which employ too little data or use data which while sufficient in quantity suffers from high standard errors.
- R3.12 The Commonwealth notes the criticisms but asserts that in broad terms the analysis undertaken confirms that increases in award wages do have the potential to affect the pace of agreement-making. The Commonwealth reiterates that the Commission should be mindful of this when considering the claim by the ACTU for a large increase in award rates.

---

<sup>1</sup>ABS, Employee, Earnings and Hours, May 2002, Cat. No. 6306.0, unpublished data.

- R3.13 Charts 3.7, 3.8 and 3.9 on pages 33 and 34 of the Commonwealth submission clearly demonstrate that in the three most award reliant industries of Accommodation, cafes and restaurants, Retail and Health and community services the gap between award wage increases and those achieved through agreement making is very small. Consequently large award wage increases can quickly encroach on wages achieved through workplace agreements.
- R3.14 To further illustrate this point, 46 per cent of Federal agreements in the Retail sector certified in the December quarter 2003 have wage outcomes that are in the lowest 10% of wage outcomes. The percentage is even higher for Accommodation, cafes and restaurants, with 56% having wage outcomes in the bottom 10 per cent of agreement outcomes.

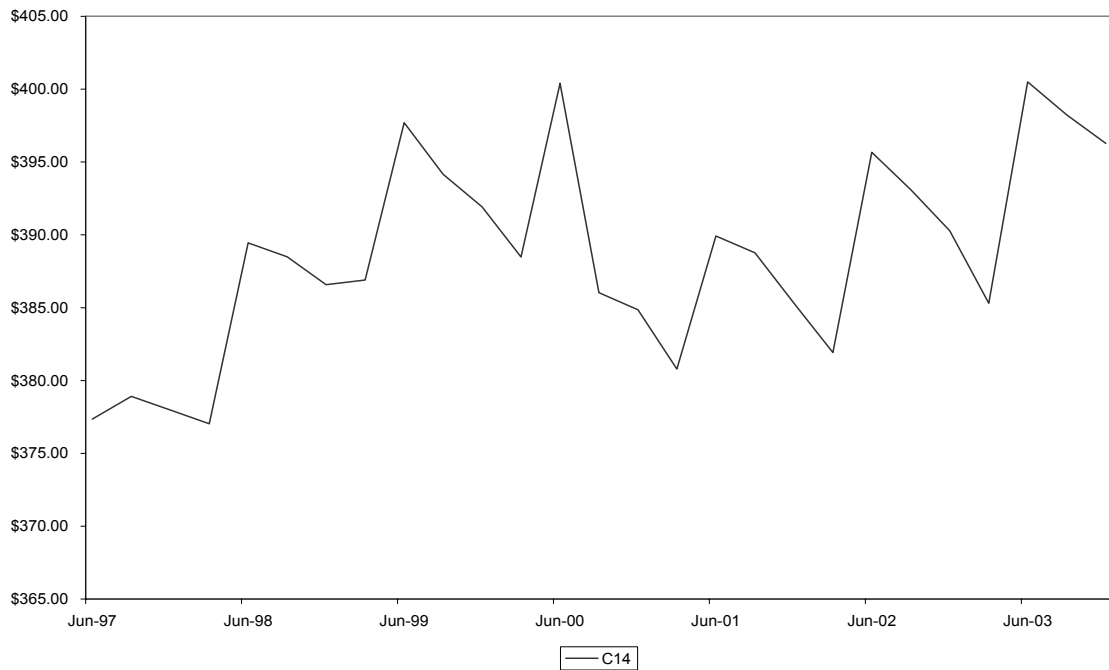
## **Living standards and the WCI**

- R3.15 At paragraph R4.15 the ACTU states that 'comparisons with earnings measures are appropriate when a consideration of living standards is apposite'. Earnings are affected by factors other than wages, such as length of employment, skill or qualification levels etc. Employers may respond to excessive wage increases by seeking more flexibility through part-time and casual employment. Of all award employees in May 2002, 57.7 per cent were part-time and 46.4 per cent were casual.
- R3.16 The Commonwealth submission, in paragraphs 3.4 to 3.12, outlines why the use of earnings measures should be disregarded by the Commission. The WCI is by far the best measure of wage movements.

## **Real value of the FMW**

- R3.17 At paragraph R2.44 the ACTU states that the real after tax FMW has barely increased since 1999, and the real after tax wages for C11 and C10 have declined.

- R3.18 The following examples show the improvements in the real disposable incomes of workers in various family types on the FMW and on C10, for the period March 2000 to March 2004.
- R3.19 For workers on the FMW, real disposable income has increased by 3.2 per cent for a single person with no children, by 8.4 per cent for a lone parent with a child under 5, and by 8.8 per cent for a single earner couple with two children, one under 5.
- R3.20 For workers on C10, real disposable income has increased by 1.5 per cent for a single person with no children, by 7.2 per cent for a lone parent with a child under 5, and by 3.8 per cent for a single earner couple with two children, one under 5.
- R3.21 Thus the real disposable income has increased for all these family types at both the FMW and C10 wage rates, and the increases are quite significant for families with children.
- R3.22 In paragraph R2.44 of its reply submission the ACTU finds it noteworthy that the Commonwealth has charted the real value of the FMW (C14) since 1990. This was done simply because the series started in 1990. Another appropriate starting point would be the first SNR in 1997.
- R3.23 The resulting Chart R3.1 shows a more consistent increase in the FMW, apart from the effects of the GST. Even so, the real value of the FMW increased by 1.0 per cent per annum over the six years to June 2003, or by 1.4 per cent per annum after discounting the inflationary impact of the GST, which was compensated through tax cuts.

**Chart R3.1: Real value of FMW, June 1997 to December 2003**

Source: DEWR (using June 2000 dollars).

## Conclusion

R3.24 In the award-reliant industries in particular, a large wage increase would place a higher floor under the range of wage outcomes that could be achieved through workplace bargaining.

R3.25 The Commonwealth reiterates that it is crucial that any impediments to productivity growth such as undue reliance on award wage increases are reduced by the encouragement of workplace agreements.

## **SECTION 4: PRODUCTIVITY AND WORKPLACE BARGAINING**

### **Introduction**

- R4.1 The Commonwealth submission has shown that over the medium term productivity growth in award-reliant industries was below the level recorded for all industries.
- R4.2 Contrary to this the ACTU has attempted to show that productivity growth was strong in the three most award reliant industries. However, the starting point of that analysis was a low point or near-low point for productivity growth in these industries and the ACTU does not contest this in its reply submission.

### **Productivity Growth in Award-reliant Industries**

- R4.3 The Commonwealth has presented aggregate level and the workplace level evidence that workplace bargaining is encouraging productivity growth. The ACTU reply submission does not contest the evidence presented at the workplace level nor the results from academic studies at the macro level.
- R4.4 Rather, the ACTU focuses on the regression exercises presented by the Commonwealth in Appendix A of its submission and provides a critique of these exercises by Professor W Mitchell (R2.31 in the ACTU reply submission).
- R4.5 The purpose of the Commonwealth's regression exercises was to answer a specific question about the relationship between award-reliance and productivity growth in the presence of other variables that affect productivity growth and to provide the Commission with information on this issue, given the limited data available.

- R4.6 The regression analysis builds on work undertaken by the Commonwealth for the 2003 SNR by addressing the criticisms from the Commission<sup>1</sup>, the ACTU<sup>2</sup> and the State and Territory Governments<sup>3</sup>.
- R4.7 The Commission stated that the 2003 regression exercise masked the underlying capacity for productivity growth between various sectors<sup>4</sup>. To account for this, average productivity levels were used in the 2004 regressions as an appropriate measure of an industry's capacity for productivity growth.
- R4.8 The ACTU is not correct when it asserts that the regressions do not account for technological change (ACTU reply submission R2.30). The inclusion in the 2004 regressions of a variable reflecting industry productivity levels took account of differences between 'high-tech' and 'low-tech' industries. The inclusion of this variable is not criticised by either the ACTU or Professor Mitchell.
- R4.9 The Commonwealth also controlled for 'capital deepening' through the inclusion of an industry's capital-labour ratio. Capital deepening increases productivity through a more efficient use of capital<sup>5</sup>. Capital deepening, at least to some degree, is also a measure of technological change. The inclusion of this variable in the regression analysis is also not criticised by either the ACTU or Professor Mitchell.
- R4.10 There is a solid economic foundation for the use of the variables employed by the Commonwealth to test the relationship between award reliance and productivity growth. The Commonwealth's approach, therefore, is more advanced than the ACTU's dismissive approach (ACTU reply R2.30).

---

<sup>1</sup> Safety Net Review – Wages May 2003, Print PR002003, paragraphs 181 and 182.

<sup>2</sup> Safety Net Review – Wages May 2003, transcript, 31 March 2003, PN454 to PN456.

<sup>3</sup> Safety Net Review – Wages May 2003, transcript, 1 April 2003, PN739 to PN748.

<sup>4</sup> Safety Net Review – Wages May 2003, Print PR002003, paragraph 181.

<sup>5</sup> See, for example, J Loundes, M Wooden and Y-P Tseng 'Enterprise Bargaining in Australia: What do we know?' *The Economic Record*, Vol 79, No 245, June 2003 pages 248-249.

- R4.11 Moreover the case studies used in the Commonwealth submission to the 2003 SNR supports the judgement that the regression analysis is not simply picking up statistical correlations without causation. These studies show that workplace bargaining does improve productivity.
- R4.12 Professor Mitchell (ACTU reply R2.31) criticises the Commonwealth for using an insufficient number of observations in these regressions. For example, Professor Mitchell says that a ‘stunning (and inappropriately) low’ 7 observations are used in Model C. As stated in the Commonwealth’s submission, only 7 industries can be used to examine award change between 1990 and 2002 due to ABS data limitations<sup>6</sup>. The Commonwealth has used the maximum number of observations available.
- R4.13 Professor Mitchell also accuses the Commonwealth of not being clear in the measure of labour productivity (ACTU reply R2.31). On the contrary, the data in Appendix A (AusStats Table 5204.025) shows Gross Domestic Product per hour worked by industry. This is the official measure of labour productivity by industry.
- R4.14 Both Professor Mitchell and the ACTU argue that there has been a change in the definition of award coverage between 1990 and 2002 and this may cause some measurement error in the data in Tables A.3 and A.4. While it is true that there has been change in the definition between surveys, these remain official ABS estimates of award coverage and should be used to examine award change over time. Further, given the significant change in award coverage in each industry over this time any measurement errors are likely to have little effect on the regression results.
- R4.15 The Commonwealth chose to use award change between 1990 and 2002 and award-reliance in 2002 in two separate regressions. The regression results presented in Tables A.4 and A.5 show that the ‘award’ variable was significant in both regressions.

---

<sup>6</sup> Commonwealth Written Submission, Safety Net Review – Wages, 18 February 2004, paragraph 4.16.

- R4.16 The change in the definition of award-reliance between the ABS surveys does not affect the regression results presented in Table A.5 which do not contain this variable. Instead this regression uses the percentage of the workforce award paid in May 2002 as the 'award' variable.
- R4.17 The results in Table A.5 are also adjusted for the presence of heteroskedasticity, as suggested by Professor Mitchell (ACTU reply R2.31). It should be noted that the t-statistic for the award reliance variable is -4.74, well below the value of -1.94 which is sufficient to show a significant relationship between this variable and productivity growth.
- R4.18 In summary, despite the criticisms of the ACTU and Professor Mitchell, the regression analysis undertaken by the Commonwealth relating to productivity growth makes good use of the limited data available.
- R4.19 The results provide evidence that award-reliance hampers productivity growth. These findings are supported by a number of academic studies at both the aggregate and workplace level that show a positive relationship between workplace bargaining and productivity. The results of these studies are not contested by the ACTU.

## **Impact on labour costs**

- R4.20 The ACTU at paragraph R2.24 to R2.27 refutes the Commonwealth's contentions that if nominal wage increases (that is wage increases paid by employers) exceed real productivity increases then there will be negative economic consequences. These can take the form of an increase in prices, decrease in profits or decrease in employment.
- R4.21 Table R2.3 presented by the ACTU confirms the above. For example, in the Accommodation, cafes, and restaurants industry, nominal wage increases have far exceeded real productivity growth since 1996, the result of which was an increase in prices of approximately 20 per cent.

R4.22 This is demonstrated by the fact that nominal productivity growth is 19.8 per cent higher than real productivity growth.

### **Distribution of productivity gains**

R4.23 In general, however, the ACTU does not contest evidence provided by the Commonwealth that consumers, including award workers, have been the beneficiaries of productivity growth through lower prices. Therefore, award workers are sharing in the benefits of productivity growth.

### **Conclusion**

R4.24 The Commonwealth maintains the view that the shift to workplace bargaining has led to improvements in productivity.

## SECTION 5: IMPACT ON EMPLOYMENT

### Introduction

- R5.1 The Commonwealth submission highlighted the sectoral impact of the ACTU claim. Importantly, growth in employment of award-reliant workers is not increasing as fast as employment for workers on agreements in the same industry sectors.
- R5.2 In response to Full Bench Decision PR944225 of 4 March 2004 the Commonwealth filed with the Commission on 16 March 2004 a report entitled *Minimum wages in Australia: an analysis of the impact on small and medium sized businesses* (minimum wages report).
- R5.3 The findings of the minimum wages report give additional weight to the conclusion in the Commonwealth submission that caution must be exercised when considering the rate at which minimum wages should be allowed to rise because of the negative impact on employment.

### Minimum wages report

- R5.4 The minimum wages report was prepared for DEWR by Turning Point Research Pty Ltd. The authors were commissioned by DEWR to design a survey questionnaire for inclusion as a supplement in the October/November 2003 Yellow Pages Survey of 1800 SMEs. They were also commissioned to analyse and report to DEWR on the findings.
- R5.5 The survey questions were designed to provide information that would help answer the following research questions:
- How many businesses and employees have their wages adjusted through the annual Safety Net case and its flow-on effects?
  - What is the effect of annual Safety Net decision on wage setting and labour costs?

- What was the effect of the 2003 Safety Net adjustment on employment?
- What is the effect of Safety Net adjustments on employment levels?

- R5.6 A principal instruction from DEWR was that the survey and analysis be methodologically sound. The task was considered complex as it required research and analysis that paid attention to both economic and statistical theory and was explicit about methods used and assumptions made.
- R5.7 DEWR sought additional validation work when it became apparent that the response rates to the survey, at 20 to 22 percent, were lower than were expected.
- R5.8 With regard to the response rates it is important to note that it took Sensis Pty Ltd (Yellow Pages) 9,887 business contacts to obtain the required 1,800 interviews. This method ensures that the respondents represented a valid stratification of Australian SMEs. The low response rate is therefore not attributable to reactions to the survey questions for the minimum wage survey.
- R5.9 The findings of the report reveal that SNR decisions do have negative impacts on employment levels in SMEs. The report adds weight to the evidence presented in the Commonwealth submission that a cautious approach should be taken to adjusting minimum wages because of negative employment consequences.
- R5.10 The short-run impact of the 2003 SNR decision over a three month period on employment demand was found to be 14,000 fewer jobs than would have otherwise been the case. This represents an elasticity of demand of about -0.2. That is, for every 1 per cent increase in award wages, employment demand for award workers will fall by 0.2 per cent.

## Cost of the claim

- R5.11 Paragraphs R4.1 and R4.2 of the ACTU reply submission state that no opposing party provides evidence disputing the cost of the claim. This is incorrect.
- R5.12 Paragraphs 5.5 and 5.6 of the Commonwealth submission refer to past criticisms of the ACTU's costing methodology. The net impact measure used by the ACTU does not reflect the full effect of the claims nor does it take into account that the claim would put upward pressure on wage rates negotiated in agreements.
- R5.13 The ACTU argues that employers have in some way already factored in an increase in award wages and this reduces the impact of the claim on employment.
- R5.14 The minimum wages report prepared for DEWR found that when award wages were not increased through the SNR over a period of five years, the wages of some award workers still increased at the discretion of employers.
- R5.15 Importantly, however when wages were not increased through awards and employers provided discretionary increases, employment demand increased by 245,000 jobs.
- R5.16 The minimum wages report also found that employers wanted to maintain some flexibility to be able to respond to business cycles by having the discretion to adjust wages and that this is achieved when there is some gap between award wages and actual wages paid to workers. This implies that maintaining the level of award wages close to the level of actual wages imposes a cost on employers in terms of workplace flexibility.
- R5.17 A further Commonwealth criticism of the ACTU's costing methodology is the omission of the flow-on effect of award increases into over-award wages.

- R5.18 The minimum wages report found that around 1.1 million employees who were paid over award wages received an automatic pass on of the May 2003 SNA. Another 1.4 million employees who were paid over award wages had received or were expected to receive discretionary pass on of the May 2003 SNA.
- R5.19 Therefore the SNA influences the wages of around 2.5 million employees of SMEs who are paid over award wages. The ACTU costing therefore substantially understates the macroeconomic cost to the economy of their claim.

## Other Research

- R5.20 The ACTU does not respond to the study by Bazen and Marimoutou cited by the Commonwealth, which indicates a consistent negative relationship between teenage employment and the minimum wage in the United States over the period 1954 to 1999.
- R5.21 The ACTU cites the work of Hyslop and Stillman (ACTU reply submission R6.13 to R6.16), noting the high level of non-compliance with the new minimum wage in New Zealand, but failing to address its potential impact on the results.
- R5.22 This study relies, in part, on the method of differences-in-differences, about which Dr Ian Watson notes 'such estimators have been subject to considerable criticism in recent years'<sup>1</sup>. The study may be of little relevance to Australia given the very low level of the minimum wage in New Zealand.
- R5.23 In 2001, when the positive employment effects were found after substantial increases in youth minimum wages, the minimum hourly wage in New Zealand was \$NZ7.70 for 18 years and over. This equates to \$6.25 compared with the Australian FMW of \$10.90 an hour.

---

<sup>1</sup> I Watson, 'A needle in a haystack. Do increases in the minimum wage cause employment losses?', ACIRRT Working Paper 90, March 2004, page 7.

- R5.24 The ACTU quotes selectively from the book *Monopsony in Motion – Imperfect Competition in Labour Markets* (Princeton University Press, 2003)<sup>2</sup>. The Commonwealth notes Manning’s caution that, even under his framework, ‘the potential down-side from excessively high minimum wages exceeds the potential up-side for a well chosen one’<sup>3</sup>.
- R5.25 Manning develops theoretical monopsonistic models that explain conditions under which there might be concurrent increases in the minimum wage and employment levels. He does not, however, go so far as to identify where such conditions arise, noting that this must be the subject of empirical research<sup>4</sup>.
- R5.26 The minimum wages report prepared for DEWR also found that award-reliant industries in Australia are not monopsonistic, and that award wage rises do indeed cost jobs.

## Sectoral Impact

- R5.27 The ACTU makes the simplistic assertion that employment has increased in award-reliant industries therefore SNAs have not had an adverse impact.
- R5.28 The Commonwealth has provided analysis showing that even in award-reliant industries employment growth has generally been in areas where there are workplace agreements, with award-reliant employment declining. The ACTU states that the data on which these findings are based is unreliable.
- R5.29 While the movements in proportions of award-only employees are not statistically significant in a number of individual cases, the fact remains that based on ABS best estimates from May 2000 to May 2002 the number of award employees fell in all but five industries, while the number of non-award employees increased in all but three industries.

---

<sup>2</sup> ACTU Written Submission, Minimum Wages Case, 28 January 2004, pages 90 to 92.

<sup>3</sup> A Manning, *Monopsony in Motion – Imperfect Competition in Labour Markets*, Princeton University Press, Princeton and Oxford, 2003, page 347.

<sup>4</sup> A Manning, *Monopsony in Motion – Imperfect Competition in Labour Markets*, Princeton University Press, Princeton and Oxford, 2003, page 365.

- R5.30 The Commonwealth submission to the 2003 SNR revealed that there was a significant negative relationship between changes in employment growth and changes in award coverage<sup>5</sup>. This was a sound statistical relationship, with a very small probability of occurring by chance.
- R5.31 Paragraph R2.18 of the ACTU reply submission notes, quite correctly, that employment in Accommodation, cafes and restaurants would have increased in 2000 due to the Olympics, and decreased in 2003 due to SARS and the war in Iraq. This is in keeping with the Commonwealth contention that the impact of wage increases on employment cannot be tested in isolation, and the need to control for such effects where possible, in order to examine the impact of safety net adjustments.
- R5.32 The ACTU at paragraph R 2.18 also indicates that trend employment has grown strongly in Accommodation, cafes, and restaurants in 2003. While stressing the reasons for the preceding downturn, the ACTU ignores the significant increase in demand for Accommodation, cafes and restaurant services in the November quarter 2003 due to the Rugby World Cup. This will have significantly affected the trend estimates, and could easily be revised away in coming quarters.
- R5.33 The ACTU also notes that employment in Accommodation, cafes and restaurants in November 2003 'exceeds its previous Olympics inflated highs', but this has taken three years. This is due entirely to the strong growth in part-time employment. The Commission should note that full-time employment in this sector declined by 7.1 per cent over this period, and total hours worked remained 4.9 per cent lower in November 2003.
- R5.34 While the trend data used by the ACTU do smooth out quarter on quarter fluctuations, the latest estimates are subject to substantial revision as more data become available.

---

<sup>5</sup> Commonwealth Reply Submission, 2002-2003 Safety Net Review – Wages, pages 38 and 39.

- R5.35 The use of employment numbers can mask changes in overall demand for labour, which is better illustrated using hours worked. Annual averages are preferred because they address the problems of seasonality and volatility.
- R5.36 In terms of hours, Retail has grown strongly over recent quarters, fuelled by high levels of consumption. However, its growth from 1996 to 2003 has still been less than average. Hours worked in Accommodation, cafes and restaurants fell by only 0.1 per cent from 2002 to 2003. Hours worked in Health declined by 1.2 per cent from 2002 to 2003. In addition, the incidence of part-time work in both these industries appears to be increasing faster than average.
- R5.37 In summary, employment growth in Retail has been strong over recent quarters due to strong consumer spending, but may be sensitive to any decline in consumption growth. However, employment as measured by hours is declining in Health, and is yet to show any signs of recovery in Accommodation, cafes and restaurants.

## Inequality and the minimum wage

- R5.38 A significant body of research shows that minimum wage increases do not have welfare improving potential and in some cases actually decrease real incomes of those at, or near to, the minimum wage. The ACTU's reply submission does not contest the evidence presented by the Commonwealth on this issue.
- R5.39 Revised data released in the ABS Household Income and Income Distribution 2000-01 survey<sup>6</sup> does, as the ACTU contends, reveal some growth in income inequality in the late 1990s.
- R5.40 The Gini coefficient, a single statistic that summarises the degree of inequality in income distribution indicates a small rise in inequality over the past six years. It should be noted, however, that this increase is barely statistically significant.

---

<sup>6</sup> ABS, Household Income and Income Distribution (Cat. No. 6523.0)

- R5.41 Most of the increase in inequality occurred between 1997-98 and 1999-00, with the distribution of income remaining essentially unchanged between 1999-00 and 2000-01.
- R5.42 The rise in the value of the Gini coefficient prompted the ABS to comment that there has been “some possible rise in income inequality over the second half of the 1990s”<sup>7</sup>. Any possible “rise in inequality”, however has been driven by a divergence in growth rates of those at the extreme ends on the income distribution. While the lowest income households have experienced real growth in their income, high income households have experienced a significantly higher rate of growth.
- R5.43 It is important that the Commission note that real disposable income has increased for all groups across the income distribution over the past six years, including the lowest percentile.

## Conclusion

- R5.44 The ACTU reply submission does not alter the Commonwealth position that the claim, if granted, would add significantly to labour costs and have a detrimental effect on employment growth.

---

<sup>7</sup> ABS, Household Income and Income Distribution (Cat. No. 6523.0), p.10.

## SECTION 6: LIVING STANDARDS

### Introduction

R6.1 The Commonwealth remains of the view that SNAs are a poor means of addressing the needs of low paid households.

### Budget Standards

R6.2 The ACTU claims that the Commonwealth has not acknowledged that the Social Policy Research Centre (SPRC) dealt with the Commonwealth criticisms of the 'budget standards' methodology in the 1998-99 SNR. While the budget standards have been updated for price changes, there have been no fundamental changes to the actual methodology.

R6.3 The ACTU also claims that the SPRC acknowledged the Commonwealth's concerns about the variability of housing costs and dealt with these concerns<sup>1</sup>. Due to the regional variation in housing, the SPRC states categorically that "the treatment of housing costs is thus a limitation" and suggest that there are issues in comparing living standards across regions in Australia in all methods, not just budget standards. The variability in housing costs is a significant issue as housing costs are a substantial element of the estimated budgets - between 25-41% of the total budget.

R6.4 The ACTU<sup>2</sup> notes that as rent assistance can be higher if rent is higher, this can make up some of the rent differentials. This is precisely the point the Commonwealth makes in paragraph 6.14 of its submission – that the tax-transfer system targets assistance to those most in need and is a much better tool for addressing the needs of the low paid. Many households with one earner on or near FMW would receive rent assistance.

---

<sup>1</sup> ACTU Written Submission, Tag 8, Table B.1

<sup>2</sup> ACTU Written Submission, Minimum Wages Case 2004, paragraph 7.55

- R6.5 The SPRC budget standards also do not reflect the flexibility and trade-offs that Australian households undertake to make ends meet. The SPRC acknowledges that application of the ownership rule separately to each item can lead to an upward bias in the standards as the rule does not take into account the trade-offs that people make in practice.
- R6.6 Concerns about the budget standards approach were recently echoed in a UK Government report on measuring child poverty. The report rejected the use of budget standards to identify adequate levels of income noting<sup>3</sup>:

*'First and foremost, despite a wide range of research into budget standards, there is no simple answer to the question of what level of income is adequate. Different research methods tend to make different assumptions that are essentially subjective. Even methods that purport to define the cost of a 'scientifically determined diet' in effect have to make a number of subjective assumptions about needs. This can produce inconsistent answers to the same questions'.*

## Conclusion

- R6.7 The living standards of the low paid are best addressed through the tax-transfer system. The severe costs of unemployment should be taken into account when the Commission is considering the ACTU claim.

---

<sup>3</sup>United Kingdom Department for Work and Pensions 2003, measuring child poverty: preliminary conclusions, P44.