

Submission

by

Business|NZ

to the

**Labour Market Policy Group, Department  
of Labour**

on the

**Annual Review of the Minimum Wage**

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# Annual Review of the Minimum Wage

## 1. Introduction

- 1.1. This submission is made on behalf of Business New Zealand, incorporating regional employers' and manufacturers' organisations. The regional organisations consist of the Employers' and Manufacturers' Association (Northern), the Employers' and Manufacturers' Association (Central), Canterbury Manufacturers' Association, Canterbury Employers' Chambers of Commerce, and the Otago-Southland Employers' Association.

Business New Zealand's Affiliated Industries Group (AIG) also includes 49 national industry associations. With its regional organisations and the AIG, Business New Zealand is therefore able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

- 1.2. Business New Zealand's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD in per capita GDP terms. This is a goal that is shared by the Government. It is widely acknowledged that consistent, sustainable growth in real GDP per capita of well in excess of 4% per annum would be required to achieve this goal. Continued growth of around 2% (our long-run average) would only continue New Zealand's relative decline.
- 1.3. Increased access to training and employment is one way to achieve higher growth. However, increases in the minimum wage rate and/or extensions to its coverage may limit this access, as businesses no longer find it economically viable to hire workers at an increased minimum rate. Increases can be particularly severe on those earning the youth minimum wage rate, as opportunities for valuable work-place learning and skill development become increasingly harder to obtain.
- 1.4. There have already been extensive changes to the rates and eligibility of the adult and youth minimum wage since the current Government was elected in

1999. Both the youth and adult minimum wage rate have increased every year since 2000, the age of eligibility for the adult minimum wage rate has decreased from 20 to 18, and coverage of the minimum wage has been extended to those undertaking at least 60 credits of training towards a qualification on the National Qualifications Framework. Because of these changes - particularly to the youth rate - Business New Zealand is concerned that any further rises will severely impact on the ability of businesses to provide jobs and training opportunities. We believe that Government focus should be on increased access to training and employment to achieve higher economic growth, and that consideration be given to abolishing the youth minimum wage rate if research shows it is an impediment to young people obtaining a job.

## **2. Minimum Wage Rates and the Consumers Price Index**

- 2.1. The Consumers Price Index (CPI) has traditionally been used as a key indicator for adjustments of the minimum wage rate on an annual basis. However, we have concerns about the use of the CPI for this purpose. The CPI measures changes in prices affecting the average household, but does not provide information on what has been happening with incomes and does not cover all household expenditure. Because Government policy changes have had a much stronger impact on the CPI than other inflation measures, this has resulted in a higher level of average annual movement than most other broader measures of inflation.

### **Alternative Inflation Measures**

	% Annual Change- Year ended June 2003	Ten-year annual average between June 1993 & June 2003
Consumer Price Index	1.5	2.1
Producer Price Index	-0.6	1.9
Retail Prices (unofficial series)	-0.5	1.1
CPI Excluding Government Charges	1.3	2.0
Home Ownership	5.3	4.1
Central & Local Government Charges	3.8	4.1

- 2.2. Over the ten years from June 1993 to June 2003, the CPI increased by an average of 2.1 % while retail prices (unofficial series) had an average increase of just 1.1%. Increases in the level of Central and Local Government charges have meant the Statistics New Zealand index of selected government charges shows an average annual increase of 4.1% between 1993 and 2003. Since the Government has been able to offset increases in charges through lowering tax rates and introducing assistance measures, it is incorrect to link annual wage increases, and especially statutory minimum wage increases to the movements of the CPI.
- 2.3. In 1997, the Consumer Price Index Revision Advisory Committee discussed this issue extensively during the review of the CPI. The committee decided that an index of disposable incomes, adjusted for price level change, tax and benefit changes would be an appropriate measure for social policy objectives than solely relying on the CPI measure to adjust benefits or minimum wage levels. However, the Government has not agreed to provide funding for the development of the Real Disposable Income (RDI) measure, which means there is still insufficient information on whether any increase in minimum wage rates is justified.
- 2.4. The CPI has never been a satisfactory indicator on which to base adjustments to the minimum wage rate. Given the low levels of inflation over the last decade, Business NZ does not believe that in the absence of an RDI measure there is any strong justification for a further increase in either the adult or youth minimum wage rate.

***Recommendation: That Statistics New Zealand is given funding for development of a Real Disposable Income Index.***

### **3. Youth Minimum Wage Rates**

- 3.1. Two key objectives of the minimum wage set out by the Government are wage protection to vulnerable workers and ensuring the wages of workers on low incomes do not deteriorate relative to those of other workers. However,

most of those receiving the minimum wage are not in a vulnerable position and do not rely on the minimum wage as a long term source of income. The group most likely to receive minimum wage rates is younger people (aged 15-19), living at home, in a temporary job with few or no skills. Their productivity is often low, and their wage levels reflect this.

- 3.2. Under the current Government, the youth minimum wage rate has increased for four consecutive years. In 2000, it rose by 8.3%, then in 2001 and 2002 by almost 19%. The latest increase in 2003 saw it rise further by 6.2%. In other words, the youth minimum wage has increased from \$4.20 in 1999, to \$6.80 in 2003, representing an overall increase of 62%. During the same time period, the adult minimum wage rate increased by 21.4%, while the age criterion for receiving the adult minimum wage rate dropped from 20 to 18 years.
- 3.3. Given the large increases in both the adult and youth minimum wage rates from 2000 onwards, Business NZ would be deeply concerned if the Government were using minimum wage increases to pursue the social objective of raising the wage rate of lower paid individuals. Such a policy of this kind would inevitably lead to price increases since wage increases without any corresponding increase in productivity are not sustainable. The result would be better pay for those who keep their jobs, but reduced paid employment opportunities for those who lose them, particularly as employers look at capital-labour substitution to compensate for unsupportable expenditure.
- 3.4. As it is still too early to assess the total impacts of these changes, current statistics, such as the Household Labour Force Survey (HLFS) from Statistics New Zealand, which may provide some indication, have a high sampling error when data is disaggregated. Therefore, a longer time series is required to assess the impact. Overall, the HLFS June 2003 quarter shows that for those aged 15-19, the current unemployment rate of 13.6% for this age group is still the highest of any age group. This is almost double the next highest

group of those aged 20-24 with an unemployment rate at 6.9%, and is almost three times larger than the national average of 4.6%.

- 3.5. Although the 15-19, 20-24 and overall unemployment rate has fallen in comparison with the June 1999 quarter (the last year in which minimum wage rates remained unchanged), the relative difference between the 15-19 year old unemployment rate and the overall unemployment has increased. In the June 1999 quarter, the 15-19 year old unemployment rate was 2.44 times more than the national unemployment rate, compared with 2.95 times more than the national unemployment rate in the June 2003 quarter. Although a longer time series would be more appropriate to fully take into account effects of minimum wage increases, preliminary data shows that increasing the minimum wage for youth has lifted the unemployment rate for the 15-19 year old group in relation to the national unemployment rate, not decreased it.
- 3.6. There are various reasons for younger people to have a higher unemployment rate. They are not as committed to the labour force as older individuals, and often they do not have any dependents and can rely on family members to provide for them if they wish to pursue other activities beyond the workforce. In contrast, those who are older commonly have dependents and/or other financial responsibilities, and in many cases have to hurriedly find new employment if they become unemployed.
- 3.7. Because of these inherent differences, any Government policies aimed towards those in the younger age bracket should primarily focus on providing employment opportunities and training schemes, so young people have a higher level of skills when fully committed to the workforce, and can provide employers with a signal of their productivity. Business New Zealand considers that any increase in minimum wage rates reduces job and training opportunities for this group, as does the extension of the youth minimum wage to employees on training agreements. Raising and/or extending minimum wage rates may well mean many workers receiving such rates would find their jobs no longer sustainable, as their productivity is below their

comparable wage level. Often, their work responsibilities will either be shared amongst other co-workers, or a capital-labour substitution will take place.

- 3.8. In addition, many businesses have indicated to Business New Zealand that many of those receiving the youth minimum wage rate are 'after-school' workers, who are generally employed from a goodwill or social standpoint. This type of work provides young workers with the opportunity to learn fiscal responsibility and to develop a work ethic, as well as providing additional pocket money and work experience that may be added to a CV. Increasing the youth minimum wage rate would lead many businesses to eliminate such jobs.
- 3.9. Business New Zealand is also concerned about inflationary pressures due to increases in the minimum wage rate. Any increase will lead to higher skilled workers who earn slightly higher pay rates than those in the same firm on the minimum wage rate seeing their relative advantage eroded and consequently expecting a corresponding increase in their own wage rate. Also, many employers have pointed out to Business New Zealand that wage rates for employees are often set just above the minimum wage rate. Any increase in the minimum wage rate will mean these employers too will have to increase their employees' wage levels so that relativity with the minimum wage rate is maintained. This clearly shows that any increase in the minimum wage rate affects more workers than just those receiving it. The consequence is a wage-push cycle, which places further costs on the firm and continued inflationary pressures on the whole economy.
- 3.10. Although there have been no recent significant studies into the effects of the minimum wage rate increases on employment, previous studies have shown that an increase in the minimum wage rate negatively affects teenage employment. A recent cross-country analysis on the topic was an OECD study in 1998 *Making the Most of the Minimum: Statutory Minimum Wages, Employment and Poverty*, which analysed data from nine countries from

1975 to 1996. The study found that teenage employment was reduced by 2-4% for every 10% increase in the minimum wage rate.

- 3.11. Studies specific to New Zealand have also shown that a rise in the minimum wage rate leads to a fall in employment. A report by the NZ Business Roundtable *What Future for New Zealand Minimum Wage Law?* in 1994 found that a 10% increase in the minimum wage rate caused employment to drop between 1 to 3%. A further study by Tim Maloney in 1995, *Does the Adult Minimum Wage Affect Employment and Unemployment in New Zealand?*, found that a 10% increase in the minimum wage rate reduces employment for all young adults (20-24 year olds) by 3.5%, and increases the unemployment rate by 3.5%. The same increase in the minimum wage rate causes employment for those young adults without school or post-school qualifications to drop by 5.7% and increases their unemployment rate by 6.5%. While these studies date from the 1990s, there is nothing to suggest that the situation today is in any way different.
- 3.12. Those who advocate continued increases in the minimum wage rate often refer to a \$10 minimum for the adult minimum wage. That would represent a 17.65% increase from the current adult minimum wage rate of \$8.50. Taking into account the findings of section 3.10 above, a 17.65% increase in the adult minimum wage would mean a 1.8 – 5.3% decrease in employment. Similarly, if the youth minimum wage rate were to remain at 80% of the adult rate (as it has for the last two years), the youth rate would correspondingly rise 17.65% to match the increase to \$10 for the adult rate. Given the OECD findings in section 3.9, teenage employment would also fall by 3.5 – 7.0%.
- 3.13. A further objective of the minimum wage outlined by the Government is to increase the incentives to work for people considering work. Obviously, such a focus on people about to enter the workforce is supported by Business New Zealand. However, it is likely that continued increases and extensions of coverage to the minimum wage rate may instead send a signal to younger people that further education and training is not warranted. Many young people may not see the need to increase their skill levels if they are receiving



a higher rate of pay, without realizing over time the possibility of becoming trapped in a low skilled, low paid job. Raising the minimum wage rate may lead to a two-fold unemployment effect, whereby unemployment may rise due to previous minimum wage recipients finding their jobs no longer sustainable by employers, and because some individuals who were previously not part of the labour force seek to enter it as they know they are guaranteed a higher minimum wage rate. Because the latter are generally unskilled, they may have the same difficulties finding employment as previous recipients of the minimum wage whose jobs have become unsustainable. The total numbers unemployed will rise as a consequence.

- 3.14. In light of the barriers that the youth minimum wage rate creates, and on the weight of empirical evidence showing the adverse effects of increasing the minimum wage particularly harming employment prospects for younger workers, we submit that the Government should focus on increased access to training and employment for young people, and that the youth minimum wage rate be abolished so that this restriction on the employment of young persons is removed.

***Recommendations:***

***(a) There are no further increases in either the youth and adult minimum wage rate.***

***(b) The Government should focus on increased access to training and employment for young people, and that the youth minimum wage rate be abolished so that this restriction on the employment of young persons is removed.***

## **4. Extension of Minimum Wage Coverage**

- 4.1. Business New Zealand is strongly opposed to the recent introduction of a minimum training wage rate to those undertaking 60 credits or more of training towards a qualification on the National Qualifications Framework. The primary goal of undertaking such forms of study is to specifically raise

the skill level of participants and to create a signal to employers that they are more productive. Often, it is young people who devote more time to investment in training so that their skill base is improved. Considering the Government's goal of 250,000 people being in some type of training scheme by 2007, it is important that no barriers are put up to reduce the ability of people, especially young persons, to enter into formal training. The introduction of the minimum training wage rate simply undermines the Government's attempt to increase access to training. Many firms that provide training for workers often invest considerable amounts of time and money so that those receiving the training raise their skill base. The extension of the minimum wage to those undertaking 60 credits or more of training prevents many employers offering training opportunities for young people, being an additional cost on top of what is already invested in the worker through training.

- 4.2. Business New Zealand strongly supports a return to the continuation of the exemption from the minimum wage applying to individuals undertaking 60 or more credits of training towards a qualification on the National Qualifications Framework. Considering that young people are devoting more time towards investment in training, it is important that those providing training are able to focus resources on quality training, not higher short-term wage levels.

***Recommendation: That the exemption from the minimum wage applying to individuals undertaking 60 or more credits of training towards a qualification on the National Qualifications Framework be re-instated.***

## **5. Conclusion**

- 5.1. Business New Zealand strongly supports the motion that workers should be granted every opportunity to raise their skill levels. Any increases or extensions of the minimum wage rate distort the labour market by reducing jobs, and directly conflict with promoting economic growth. We believe that Government focus should be on increased access to training and

employment for young people, and that the youth minimum wage rate should be abolished so that the restriction on employment of young persons is removed. Young people would not then need to achieve a certain level of productivity in order to support their entry into the workforce and would be better able to proceed to gain skills and experience to further them in the labour market. We are opposed to extension that occurred in 2003 regarding minimum wage coverage to those undertaking at least 60 credits of training towards a qualification on the National Qualifications. We also believe that Statistics New Zealand be given funding for development of a Real Disposable Income Index.

## **6. Recommendations**

6.1. Business New Zealand recommends that:

- (a) Statistics New Zealand is given funding for development of a Real Disposable Income Index.*
- (b) There are no further increases in either the youth and adult minimum wage rate.*
- (c) Government focus on increased access to training and employment for young people, and that the youth minimum wage rate be abolished so that this restriction on employment of young persons is removed.*
- (d) The exemption from the minimum wage rate applying to individuals undertaking 60 or more credits of training towards a qualification on the National Qualifications Framework is re-instated.*