

**Submission**

by



to the

**Department of Labour**

on the

**Review of the Minimum Wage**

**26 September 2008**

# Annual Review of the Minimum Wage

## 1. Introduction

- 1.2 Business New Zealand welcomes the invitation by the Minister of Labour to submit on the 2009 minimum wage review consultation.
- 1.3 We recommend that the present rate be held for the coming year, while at the same time undertaking a review of the role and affect of the minimum wage in light of the very significant movements in it over the past 9 years.
- 1.4 Minimum rates have increased steadily and significantly since 1999. More significantly, the minimum wage is now at a level where it figures significantly in setting the minimum rates for many jobs, particularly those covered by collective bargaining. We believe a period of consolidation is required before further increases are contemplated. In the interim (and beyond) the Government would ideally focus on increased access to training and employment to achieve higher productivity and hence increased real earnings over time. Business New Zealand recommends that:
- There be no further increases in either the youth or adult minimum wage rate within the next 12 months;
  - The Government should focus on increased access to training and employment opportunities, particularly for young people
  - The Government seriously considers tax cuts rather than increases in the minimum wage rates as a more effective way of increasing real wages for relatively low paid workers.
- 2 Minimum wage laws can set minimum wages, but they cannot guarantee jobs. It is Business New Zealand's view that minimum wage laws place additional obstacles in the path of particular workers (particularly those who are young and unskilled) at the bottom end of the economic ladder.
- 3 The benefits of minimum wage have been (and continue to be) debated for many years. Views that argue neutral or positive effects on employment of increasing minimum wage rates<sup>1</sup>, are countered by other views that, in a 9 country OECD analysis for instance, a 10% increase in the minimum wage rate also generates as much as a 3-5% rise in unemployment in low income groups (and higher for young low paid workers). More recent research suggest the impacts in New Zealand may be higher than the OECD estimates, as high as 19% for 16 – 17 year old and 10% for 17 – 18 year olds.<sup>2</sup>
- 4 Maori also stand out as a subgroup most adversely affected by a higher minimum wage. The same research suggests that a 10% rise in the real minimum wage results in Maori on the minimum wage suffering from a 15.8% point drop in employment propensity (roughly equating to 5.0 hours less a week)

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<sup>1</sup> Card and Kruger "Myth and Measurement: the New Economics of the Minimum Wage", 1997.

<sup>2</sup> Pacheco 2006

- 5 The changes brought about by the Minimum Wage (Abolition of Age Discrimination) Amendment Bill were essentially a revamp of youth rates. New mechanisms and timelines have been introduced, yet the concept of a (initially) lower rate for youth workers remains.
- 6 Business New Zealand has outlined in prior minimum wage review submissions specific reasons why increases in the minimum wage rates (particularly the youth rate) negatively affect employment. To recap, these include:
  - Most employees on the youth minimum wage are not in a vulnerable position and do not rely on the minimum wage as a long term source of income;
  - 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;
  - Increases in minimum wage rates reduce job and training opportunities for youth, 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; and
  - 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.
- 7 Aside from the effect on youth employment, Business New Zealand believes increases in the minimum wage create unnecessary artificial inflationary pressures. Typically, increases in the minimum wage create relativity concerns among employees who are paid a margin over the minimum rate.
- 8 For these reasons Business New Zealand believes further increases to the current minimum wage will not bring the espoused benefits and should be dropped, or at least minimised, in favour of approaches that generate higher skills and greater productivity, the key ingredients to sustainable increases in income.

### **Recent Reviews of the Minimum Wage**

- 9 The table below summarises increases in both the adult and youth minimum wage since the current Government took office. Since 1999, there have been extensive increases in both the minimum wage rates for adults and youth workers. The adult minimum wage has increased by 60%, while the youth rate has increased at a much stronger rate of 114%. In addition, the age criterion for receiving the adult minimum wage rate has dropped from 20 to 18 years, while those doing at least 60 points or more towards a qualification from the National Qualifications Framework are paid the youth minimum wage level. Collectively this represents a very substantial cost increase for employers over a relatively short period of time.

Time Period	Youth Minimum Wage Rate	Adult Minimum Wage Rate	% Change from Previous Year
March 1999	\$4.20	\$7.00	-
March 2000	\$4.55	\$7.55	7.9%
March 2001	\$5.40	\$7.70	2.0%
March 2002	\$6.40	\$8.00	3.9%
March 2003	\$6.80	\$8.50	6.25%
April 2004	\$7.20	\$9.00	5.9%
March 2005	\$7.60	\$9.50	5.6%
March 2006	\$8.20	\$10.25	7.9%
April 2007	\$9.00	\$11.25	9.75%
April 2008	\$9.60	\$12.00	6.6%

Table 1: Adult and Youth Minimum Wage Rates and Changes (1999-2007)

- 10 A survey of employers conducted at the time of the government's announcement of the goal of having the minimum wage at \$12 by 2008 suggested that most employers can live with increases approximating inflation, but not increases that have distortionary effects on the wage structure as a whole.
- 11 Specifically, around 65% of employers were prepared to accept an increase in the adult and youth minimum wage rate of 3%, which was around the then current level of inflation. At around a 5% rise, employers were less enthusiastic, with 58.6% prepared to accept the increase. Once the adult rate moves beyond \$10, acceptance of minimum wage rate increases takes a significant drop. Less than one-third of employers were willing to accept an increase of around 10% from the current rate, equating to a \$10.50 minimum adult rate and an \$8.40 youth rate.
- 12 Moves towards a \$12 adult minimum wage rate attracted to strong opposition from employers. The \$12 threshold has been reached. No conclusive data on its impact has been gathered. However, it can be said with some certainty that the minimum wage has encroached a long way into the freedom of employers to set wages.
- 13 The 2006 census informs us that roughly 2/3 of all wage and salary earners in New Zealand earn less than \$35,000 per annum. This sum is equivalent to \$16.76 per hour (and \$15 per hour is equivalent to an annual wage of approximately \$31,300). Straightforward mathematics informs us that in setting the minimum wage higher than its present level of \$12, the government would in

fact be arbitrarily setting the wages of at least half of all wage and salary earners. The scope for relativity based pressures on other wages and rates is inescapable. This in turn impacts on the ability of employers to provide other enhancements to conditions of employment, as the capacity to accommodate compulsory increases to wages and other enhancements together is diminished.

- 14 The sustained high value of the New Zealand dollar over recent times (especially against the U.S dollar) has caused problems for certain sectors, such as export-orientated manufacturers. The Business New Zealand Performance of Manufacturing Index (PMI) shows that on a month by month basis, the strong value of the New Zealand dollar has led to falling international orders as well as constraining expansion. This has obvious flow-on effects for growth and capacity for retaining jobs in the sector. Further increases in minimum wage rates can exacerbate the problem, leading to further redundancies that might not have been the case if minimum wage rates had previously not increased at levels far exceeding that of general inflation. The increasing phenomenon of manufacturing moving offshore also becomes part of this equation.
- 15 Manufacturing is not the only sector to feel the early effects of an economic slowdown, nor the only one affected by changes to minimum wage rates. There are other industries that are more likely to have minimum wage recipients, given the nature of the work and the training and qualifications involved. In addition to Manufacturing the lowest average hourly earnings wages tend to be in sectors such as Accommodation, Cafes & Restaurants, Retail Trade and Construction. These industries are also more likely to suffer a more sustained period of downturn compared with other sectors of the economy.
- 16 Business New Zealand believes that recent increases in minimum wage rates (particularly for the youth rate) will lead to a much stronger negative impact on employment in these groups given the economy is now in recession, compared with previous increases that were adjusted for general inflation levels. Any further increases (in the short term) in either the adult or youth rate will continue to exacerbate the problem, which will deny many youth workers the opportunity to gain relevant skills and work experience. That is not to say that there should no increases at all in the future. Rather, employers need time to absorb the effects of the rapid increases in recent times. Future increases should be aligned with real costs and inflation in the first instance.
- 17 **Recommendation:** There are no further increases in either the youth or adult minimum wage rate in the next 12 months.

### **Minimum Wage Rates and Productivity**

- 18 While Business New Zealand believes further increases to minimum wage rates are effectively increasing the chances of job losses for those who are young and/or unskilled, we also believe continued minimum wage increases are inconsistent with the Government's priority placed on raising productivity and growth.

- 19 Action on labour productivity is needed sooner rather than later. New Zealand's labour productivity growth has been consistently less than the OECD average from the late 1970s. Comparing New Zealand with our closest economic neighbours shows that Australia's average annual productivity growth rate over the period 1998-2006 is 1.9%, compared with 1.6% for New Zealand. Clearly, New Zealand has to do better to compete on an international setting.
- 20 Remuneration is a key factor in getting higher productivity, but only where it can be linked to specific individual or team outcomes, such as throughput at a freezing works. Increases in minimum wage rates boost wages but of themselves do not boost productivity. Furthermore increased costs that are not offset by increase productivity typically flow through either into increased prices or, if the market cannot sustain higher prices, cost cutting and, often, job losses.
- 21 We believe Government should focus on providing employment opportunities and training schemes, aimed at equipping young people with higher skill levels at the point of entry to full time employment, thus enhancing their productive capacity and, ultimately, earning potential.
- 22 **Recommendation: The Government should focus on increased access to training and employment opportunities, particularly for young people.**

### **A Better Approach – Reducing Tax Rates**

- 23 Business New Zealand believes there is a more viable alternative to raises in the minimum wage rates to ensure a highly productive and high wage economy – the reduction of taxes on both individuals and businesses.
- 24 If the Government is focused on raising New Zealand's productivity and growth rate, as well as raising the standard of savings which is found to be lower when compared with other countries<sup>3</sup>, we believe a better way in which to provide all New Zealanders with the opportunity to save and invest more is through personal and company tax rate cuts.
- 25 By instigating a broad-base, low rate approach to taxes while containing Government spending to levels around 30% of GDP, most New Zealanders will have more cash in hand in which to repay debt, save for a house deposit or invest for retirement savings. For example, consider a person working a typical 40-hour week at the current adult minimum wage of \$12. After tax of 19.5% (excluding any rebates and ACC payments that may come into account), the person ends up with \$20,090 cash in hand. With a low personal tax rate of say 15%, cash in hand would rise to \$21,216 a year - an increase of \$1,126. The net result of this change would give an equivalent rate in today's terms of \$12.54 per hour, with out affecting overall costs to employers and therefore employment opportunities.

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<sup>3</sup> Whether this is a fundamental problem for New Zealand is debatable, as Business New Zealand has raised this issue in previous submissions and consultations relating to other issues.

26 The advantages of a tax cut over an increase in the minimum wage rates for low paid workers are numerous. Firstly, the rise in the hourly rate through a tax cut does not increase the wage costs for the business. Therefore, there is little likelihood of the position being made redundant, and even less likelihood of the position being withdrawn once the current employee takes on another position. Secondly, the relativity of those earning slightly more than those on the minimum wage because of extra responsibilities or qualifications is kept as their wages also experience an increase.

27 **Recommendation:** That the Government seriously consider tax cuts rather than increases in the minimum wage rates as a more effective way of increasing wages for relatively low paid workers.

## **Conclusion**

28 Business New Zealand strongly supports the policy of providing workers with every opportunity to raise their skill levels, and to achieve recognition based on skills and productivity. Straight increases or extensions of the minimum wage rate distort the labour market, encourage job reduction, and potentially conflict with promoting productivity and economic growth. Furthermore, the minimum wage is already at a level where an increase would result in the government becoming the de facto employer with respect to wage fixing for over half of all wage and salary earners in New Zealand. With an economy that shows signs of slowing, further increases in minimum wage rates therefore will exacerbate existing pressure to cut the least productive jobs, affecting particularly those who are young and/or unskilled. To counter such effects we strongly support the introduction of upskilling strategies and lower tax rates as a better alternative to raising minimum wage rates.

## **Appendix**

Encompassing four regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce, and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 67-member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is 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.

In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.

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 (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services). It is widely acknowledged that consistent, sustainable growth well in excess of 4% per capita per year would be required to achieve this goal in the medium term.