



ECONOMIC CONCERNS DEMAND CAUTION ON MINIMUM WAGES

The Australian Fair Pay Commission (AFPC) is expected to announce the outcome of its 2008 minimum wage review in July, with any increase in minimum wage rates expected to come into effect from October 2008, 12 months from the preceding 2007 minimum wage rise.

This year's minimum wage review takes place in a vastly different economic context to minimum wage setting across the past decade. It occurs in the context of a slowing economy, and levels of risk and declining confidence essentially unknown to minimum wage setters for more than a decade. These considerations favour a genuinely moderate and cautious approach to increasing minimum wages during 2008.

BACKGROUND

Australia does not have a single minimum wage, but over 100,000 separate minimum wage rates, reflecting the ad-hoc evolution of our industrial award system across the 20th Century. When minimum wages are varied in Australia, it is not only the lowest paid who are affected (as is the case in most countries), but also many employees on higher rates of pay.

The AFPC assumed responsibility for setting minimum wages at the federal level in early 2006, replacing the previous arbitrated process used by the Australian Industrial Relations Commission (AIRC). The AFPC uses a less formal, inquiry-based, approach to set minimum wages and is not restricted by an adversarial or highly legalistic process.

There have been two AFPC decisions / minimum wage increases to date:

- In 2006, there was an increase of \$27.36. This was a 5.6% increase at the minimum wage level. At that time, ACCI described the wage increase as “disappointing and excessive”; and
- In 2007, there was a more moderate increase of \$10.25 per week, which equated to 2.0% at the minimum wage level.

The 2008 review is the AFPC's third examination of minimum wages. From 2010, its responsibilities are to be subsumed into the proposed Fair Work Australia (FWA).

ECONOMIC RISK AND UNCERTAINTY

A key contrast between the 2008 minimum wage review and preceding reviews in recent years, lies in the emergence of economic and labour market risk.

There have been a number of quite significant recent changes in the economic landscape and in perceptions of the economy's short and medium term performance. They should be material considerations for the AFPC in setting minimum wages, and ACCI considers favour confining minimum wage increases to a properly merited and genuinely moderate level.

These changes include:

- RBA statements pointing to sustained inflation and scope for further tightening of monetary policy and the emergence of substantial economic risks and international downturns;
- Lowered OECD growth forecasts for Australia;
- Widespread market and commentator concerns regarding domestic inflation; and
- An emerging consensus towards global economic weakening and an increasingly risky international economy – flowing through to the cost of capital, labour and inputs.

INFLATION

A key challenge for our economy as a whole and for minimum wage setters is rising inflation, and forecast further rises into the medium term.

The extent to which prices will continue to rise beyond the RBA's target band is a key challenge for not only minimum wage setters, but also for the RBA when it sets interest rates, and for government and all with an interest in the operation of our economy.

Some claim that minimum wages in 2008/09 should keep pace with, or effectively chase, price increases, particularly in volatile areas such as petrol and housing prices.

It is this type of thinking which led countries into a wage price spiral in previous periods of inflationary challenge, from which it proved difficult to escape. It is this type of thinking which will lead Australia away from productivity-based wages which have proved so effective in increasing living standards and economic confidence and stability across more than a decade.

ACCI argues instead that:

- Substantial domestic and international inflationary risks confront Australia in mid-2008;
- Attempts to have wages chase prices carry the very real risk of themselves stimulating further inflation;
- The AFPC should avoid basing any minimum wage increases on short run price fluctuations, particularly in relation to fuel and lending costs; and
- Both tax cuts and minimum wages should be taken into account in considering the adequacy of incomes against recent changes in prices. From this perspective, a non-excessive minimum wage increase can be awarded in 2008 which does not threaten further inflationary pressures, and which will provide real wage maintenance.

DECLINING CONSUMER AND BUSINESS CONFIDENCE

There is also a sea change in perceptions of economic certainty and confidence.

Sentiment and forecasts have been progressively revised downward over the past few months. This is a domestic and international phenomenon, and again it is directly relevant to minimum wage setting.

This includes:

- Uncertainty from central bankers and regulators regarding the domestic and international economies, and risks to economic outlooks;
- Consumer confidence reaching 15 year lows, with low expectations for the medium and longer term; and
- Significant falls in business confidence. The March quarter Commonwealth Bank – ACCI Business Expectations Survey showed a significant fall in business confidence and reported business conditions. Business confidence fell to the lowest level since the survey began in 1994, while general business conditions were at the lowest level for five years.

Such uncertainty and risk further favours a cautious approach to minimum wage setting for 2008/09. It favours at best a broad continuation of the approach of 2007. Current economic conditions certainly could not favour abandoning the more moderate 2007 level of increase in favour of an increase based on attempting to meet price fluctuations in full solely through minimum wages.

ACCI'S PROPOSED OUTCOME FOR 2008

Taking into account the previous AFPC decisions, their timing, the timing of the 2008 review, and in particular the economic and labour market circumstances in which it is being undertaken and the considerations which the AFPC is to have regard to, ACCI considers any minimum wage increases arising from the 2008 minimum wage review should:

- Be of a genuinely moderate nature only;
- Take proper account of increases to incomes as a consequence of tax cuts from 1 July;
- Take proper account of inflationary pressures which have emerged in the economy, the moderation of economic activity and low levels of productivity growth;
- Be based on minimum wages playing a safety net role in a bargaining based system;
- Take proper account of the nature and circumstances of small and medium sized employers primarily affected by these increases; and
- On this basis and taking into account the 1 July 2008 tax cuts, be comparable in quantum and application to that determined by the AFPC in 2007.

Figure 1: Real after tax impact of combined 2008 tax cut and minimum wage increase.

Current Rate	Wage Increase \$	Tax Cut \$ ²	Combined Increase \$	Net Real Increase \$	Net Real Increase %
\$522.12 (min wage)	\$10.25	\$9	\$19.25	\$3	0.6%
\$616 (Trades Rate ³)	\$10.25	\$15	\$25.25	\$6	1.2%
\$700	\$10.25	\$20	\$30.25	\$9	1.5%

ACCI proposes that real incomes for the lower paid be broadly maintained by a combination of the July 2008 tax cuts and a minimum wage increase of comparable size to that of 2007 ¹ (outlined in the above table). This is vastly preferable for the economy to having minimum wages attempt to chase prices.

The combination of a minimum wage rise in the terms ACCI recommends, plus tax cuts, will ensure that the lower paid working on minimum wages will see their real incomes maintained or marginally increased.

Despite the significant domestic and international economic challenges facing the nation, ACCI recognises that a balanced approach to wages policy justifies a moderate increase to minimum wages, the factoring in of the value of tax cuts, and the overriding priority of linking wages to productivity, rather than prices.

A higher level of increase, which potentially ignored changes in incomes through tax cuts, or which erroneously sought to chase fluctuations in fuel or housing prices, risks threatening the very outcomes the AFPC is directed to deliver upon, including:

- The overall economic prosperity of the people of Australia;
- The capacity for the unemployed and low paid to obtain and remain in employment;
- Employment and competitiveness across the economy;
- Providing a sustainable and effective safety net for the low paid; and
- Ensuring junior employees, employees to whom training arrangements apply, and employees with disabilities, are competitive in the labour market.

ACCI's full, 150 page, written submission is available on the ACCI website at: www.fairpay.gov.au/fairpay/MinimumWageReview2008/Submissions/Employerorganisationsubmissions.htm

1 In 2007 the AFPC awarded increases of: (a) \$10.25 per week (\$0.27 per hour) to minimum wage rates up to \$700 per week, and (b) \$5.30 per week (\$0.14 per hour) to minimum wage rates above \$700 per week.

2 Assuming CPI growth rate of 3.0 percent, no HECS, single person, no dependants, indexed Medicare Levy thresholds and unchanged rates, no private health insurance.

3 C10 Rate from the *Metals, Engineering and Associated Industries Award*