Symposium on Wages: Introduction

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With the ACTU's 'living wage' claim currently before the Industrial Relations Commission, this symposium is particularly timely. However, it is not confined to issues directly relevant to the 'living wage' claim. Two articles in the December 1995 issue of the **Economic and Labour Relations Review** are a good introduction to the symposium. The first of these by John Burgess, focuses on the way movements in wages are measured. Burgess points out that 'the analysis and interpretation of aggregate wage data has become more difficult' (p. 216). He gives five reasons for this:

(a) falling award coverage,
(b) the development and uneven spread of enterprise bargaining,
(c) the industrial and demographic restructuring of the workforce,
(d) the growth in non-wage benefits, and
(e) the growth in non-standard employment.

Burgess concludes with the warning that there is now no single wage series that can be used with confidence as an indicator of wage movements across the board. Increasingly there will be greater dispersion in wage rises and all aggregate wages series 'require careful evaluation and analysis before being interpreted' (p. 299).

The second article, by David Plowman, gives a history of minimum wage determination and discusses legacies of that history which raise issues today. The two most important of these issues are the role of minimum wages in a decentralized system of fixing wage rates and the weight to be given to needs as against capacity to pay (including consideration of differences between men's and women's wages and price and productivity measures to be used in wage rate discussions).

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The symposium in this issue begins with two articles focussing on the effects of minimum wage rates on employment. That by Valentine sets out the traditional arguments supporting the conclusion that an increase in the minimum wage rate leads to a fall in employment. At the microeconomic level, with a rise in the minimum wage, substitution effects lead a firm to replace some unskilled labour with other classes of labour or capital. Also, as costs of production will rise, firms will reduce the level of production. The extent to which this occurs will depend on expectations about how much a higher price will reduce demand.

Valentine also points out that a rise in the minimum wage will probably also have an impact on the supply of unskilled labour. It is likely to increase the number of housewives who enter the workforce and may lead young people to terminate their education earlier than they would otherwise have done. Also a rise in the minimum wage may reduce the extent to which unskilled workers upgrade their skills.

When he shifts to look at the macroeconomic effects, Valentine is concerned to counter the argument that higher wages will lead to greater expenditure and hence higher employment. His most important argument is that, if the share of wages in income rises, that of profits must fall and this will have a negative impact on business investment.

Valentine then turns to an influential study by Card and Kreuger, which found that a rise in the minimum wage rates actually increased employment in fast food restaurants in New Jersey. He argues that the circumstances in this particular industry are such that changes in the minimum wage are likely to have less effect on employment than in many other industries, at least in the short run. If a longer time had been allowed to elapse the study may have found more substitution of capital for unskilled labour. Valentine also queries the data collection procedures used in the study and concludes that the study 'gives economists no reason to revise their traditional view on this subject'.

The second article, by Nevile, takes an opposing position on the effects of minimum wage rises on employment, but puts it in a wider context. After pointing out that trends to increasing income inequalities in Australian society increase the need to protect the incomes of low income families, it argues that it is very difficult for the taxation and social security system alone to do this. Minimum wage rates have an important role to play. Thus, the question of their effects on employment is one which can not be sidestepped.

Nevile points out that the traditional analysis leading to the view that rises in minimum wage rates will reduce employment treats the labour market as a market just like any other market and assumes perfect competition. He argues that the labour market is not the same as the typical competitive market. Many firms require firm-specific experience and skills that are learnt on the job. Acquiring information about the likely work performance of the potential employees and other costs of hiring are significant. Implicit and explicit long term contracts are common, to name just some of the distinguishing features of the labour markets. Moreover, the traditional model of the labour market is a particular equilibrium model which assumes that a single market can be considered in isolation from other markets. Many economists believe that an analysis of employment and unemployment must consider feedbacks between the labour market and other markets. Nevile concludes that theory can lead to no firm position on the effects of minimum wage rises on employment except agnosticism.

Nevile then surveys a large number of empirical studies, and discusses the controversy between Card and Kreuger and Neumark and Wascher. He finds a widespread consensus that effects of minimum wage rises on adult employment are virtually non-existent. A number of studies find significant effects on teenage employment. A number of others do not. However, even those who find statistically significant effects agree that they are small. For example, in their revised study Neumark and Wascher (1995) find that a 10 per cent increase in the minimum wage reduces employment in the fast food restaurants by 2.4 per cent.

Both Valentine and Nevile discuss North American studies at some length. This reflects the paucity of Australian empirical studies on the effects of minimum wage rises on employment. North American studies, and the European ones also discussed by Nevile, are about overall minimum wages, the lowest wage it is legally permissible to pay. Therefore, the literature surveyed is only relevant to part of the ACTU 'living wage' claim. That claim places considerable emphasis on increasing the earnings of those at the bottom end of the wage distribution, especially those who have only received safety net adjustments since 1991. But it also includes claims for increases in the minimum wages to be paid over a range of award classifications which includes highly paid workers and those in the middle. The articles by Valentine and Nevile are only directly relevant to wage increases claimed for relatively lowly skilled workers.

There is widespread agreement that wage rises should be commisurate with productivity gains, but how are productivity gains to be measured. This issue is taken up in the article by Colm Kearney for the case of public enterprises, but most of what he has to say could be applied to firms in the private sector as well. Kearney reviews the three best known measures. He argues that the most widely used measure, output per unit of labour, is only appropriate when capital and labour inputs are increasing at approximately the same rate. If the amount of capital per head is increasing strongly then increasing wages in proportion to growth in this measure will reduce the return on capital and may depress the level of investment. In the specific case of public enterprises where capital per worker has been substantially increased as part of microeconomic reform, tying wage rises to increases in output per head may alienate key contributors to the microeconomic reform process. Kearney's conclusion, that the emphasis on output per unit of labour or average labour productivity, should be replaced with more sophisticated measures of performance applies equally well to the private sector as it does to public enterprises.

The article by Roy Green considers the role of comparative wage justice in the current transition in Australia to a more decentralized wage bargaining system. Comparative wage justice is the principle that wage rates are determined both by the context of the work itself and fair comparison with wage rates for similar work in the same and other industries. The move to decentralized bargaining was thought to sound the death knell for comparative wage justice but Green argues that reports of its demise are exaggerated. Moreover, he says that the death of comparative wage justice would be undesirable. 'Fairness' is a force that can only be suppressed at the cost of major disruption which will occur in the longer run and not just during the transition period. The challenge is to accommodate comparative wage justice in an enterprise bargaining system in order to achieve a stable and orderly determination of pay.

Green shows that the 1989 national wage case decision setting out a new 'Minimum Rates Adjustment Principle' rests on the principle of comparative wage justice. The minimum rates adjustment process set 'more coherent relativities within and between awards'. However, so far comparative wage justice has not been applied in any form with respect to the growing earnings disparity between the award and the enterprise bargaining streams. The current 'Living Wage' case, says Green, gives the Australian Industrial Relations Commission an opportunity to apply comparative wage justice more widely, balancing equity and productivity criteria. This is important argues Green, since 'there is no rational or civilised substitute in a modern industrial society for the operation of a principle of fairness .... by a central tribunal on the basis of submissions put to it by the parties'.

The final article in the symposium is something completely different. In Western Australia the **Minimum Conditions of Employment Act** gives the Minister for Labour Relations power to proclaim a minimum wage which is the lowest weekly wage or wage rate payable to an able-bodied, full-time employee. The rate proclaimed to come into operation on the 5th November 1996 is based on an analysis of data in the 1993-94 Household

Expenditure Survey. That analysis was carried out by Plowman, Taplin and Henstridge and their article describes what they did. Readers can see how an actual minimum wage in one Australian state was set.

The minimum wage proclaimed under the Act is determined by the needs of a single adult employee, who has no dependents, and who falls in the unskilled 'labourer and related' worker classification. The analysis could be based on the average expenditure of such a worker but if this method were to be applied to data from the Household Expenditure Survey, the resulting sample would be too small to give reliable results. Therefore Plowman, Taplin and Henstridge used regression analysis.

After some 'dependent' and 'luxury' items were deleted the remaining expenditure by a household in the survey was regressed on a series of categories or variables which had the value of 1 if the household fell within a specific sub-category in each category group and zero if it did not. Six category groups or classes were used, namely age, occupation, principal source of income, employment status, household type and household size. In this type of analysis it is necessary to omit one subcategory in each group of categories. When combined the omitted subcategories define a person who is a single adult without dependents aged 20 to 34 years old and a full-time wage and salary earner in the labourer and related occupational class. Thus such a person's expenditure is represented by the constant in the regression analysis and this is considered to be the appropriate minimum wage.

The analysis gives a minimum wage of $332, after adjustment for inflation since 1993-94. It also gives other interesting information about expenditure patterns by the subcategories in each of the category groups used, so that the results are of interest in themselves, apart from their interest as the mechanism by which the minimum wage was determined.

Reference

Neumark D. and Wascher W. (1995) 'The Effect of New Jersey's Minimum Wage Increase on Fast-Food Employment: A Re-Evaluation Using Payroll Records', National Bureau of Economic Research, Working Paper No. 5224.