

OFFICE OF THE MINISTER OF LABOUR

Chair
CABINET BUSINESS COMMITTEE

MINIMUM WAGE REVIEW 2005**Purpose**

1. This paper presents the results of the 2005 minimum wage review and indicates a path towards achieving the government's aspirational goal of \$12 per hour (adult rate), if economic conditions permit.
2. This paper also presents a range of options for increases in the minimum wage paid to adults (those over 18 years old) from \$9.50 per hour (the current minimum wage) through to \$12 per hour. The paper recommends no change to the relativities between the adult minimum wage and the youth (16 and 17 year olds) and training minimum wages.

Executive summary

3. The Minister of Labour has a statutory requirement to review the minimum wage by 31 December each year.
4. I have undertaken this year's review in the context of government's aspirational goal of achieving a minimum wage of \$12 an hour (for those aged 18 and older) by the end of 2008, economic conditions permitting.
5. Following a report from the Department of Labour, on which this paper is based, I consider that there are benefits to be gained in identifying and signaling an intended path to reach the government's aspirational goal, including the level of increases and when they will happen. Each step would be checked annually against prevailing and forecast economic conditions and, if necessary, modified. I therefore recommend that the intended path is communicated at the same time as announcements are made about the minimum wage increase for 2006.
6. Identifying and signalling an intended goal:
 - a. will allow greater certainty for businesses, employers and employees around minimum wage changes to 2008
 - b. will allow a longer notice period to be provided to businesses
 - c. is consistent with the statutory requirement for an annual review, but will focus the review on whether the signalled increases remain appropriate.
7. The government's aspirational goal is dependent on economic conditions. I consider that the criteria for determining whether economic conditions permit the planned increase should be transparent. The Department of Labour is undertaking work to

identify appropriate indicators and will use these in future reviews to assess prevailing economic conditions and whether the intended step should be modified.

8. In addition to considerations around economic sustainability, I recommend that the annual review should continue to assess minimum wage levels against the government's agreed objectives and criteria (and corresponding benchmarks) for the minimum wage (FIN (00) M 29/1 and CAB (00) M 33/1E refer).
9. I received nine submissions on the 2005 review (and three additional submissions in response to my invitation to address progression towards achieving the government's aspirational goal). Submitters' views vary and are summarised in Appendix D, and are also referred to in various parts of the main body of this paper.
10. The 2005 review considered a range of options for changes to minimum wages, from 'no change' (recommended by Business New Zealand, Federated Farmers, the Hospitality Association and the Small Business Advisory Group) through to an immediate increase to \$12 an hour (recommended by the New Zealand Council of Trade Unions). The review has also considered three paths towards achieving the aspirational goal of \$12 an hour for adults by the end of 2008, if economic conditions permit (these paths are described in more detail in paragraphs 48 to 50, and involve increases following this review of between 63 cents and 75 cents).
11. There are different costs and benefits at the sectoral and firm level for employers and employees associated with the different options and deciding on a preferred option at this time will involve trade-offs between these costs and benefits. These trade-offs are primarily between the income and social benefits accruing to minimum wage earners by a large increase in hourly earnings early on in the timeframe (a 'frontloaded' increase) - which would see a higher weighting given to the government's objectives and criteria for the minimum wage - versus the reduced cost impacts for sectors and firms that would occur if a large increase was postponed until later in the timeframe (a 'backloaded' increase). An even ('smooth') progression would theoretically spread the different costs and benefits, but hourly rates needed to achieve a smooth progression would not make wage calculations easy, and so could exacerbate non-compliance with minimum wage rates. A progression that gave a larger increase at the front and the back of the series could also be seen to balance the various costs and benefits.
12. Based on the Department of Labour's view of current economic and labour market conditions (summarized in paragraphs 27 - 33), I consider that:
 - a. retaining the existing minimum wage (\$9.50 per hour) will erode the real value of these wages and would not further contribute to the government's objectives for the minimum wage. There would, however, be no constraint on job growth or other impacts on employers and employees. No tangible movement would be made towards the aspirational goal
 - b. an increase in the minimum wage in 2006 to maintain relativity to average wages (\$9.83 per hour) will preserve the real value of the minimum wage and could be made with confidence in the current economic and labour market conditions

- c. an increase in the minimum wage above the rate needed to maintain relativity to the average wage (e.g. \$10 an hour or more) could be made to reflect a stronger view of the contribution of the minimum wage to its objectives. A rate over \$10 an hour (e.g. \$10.25 or \$10.50 an hour) would exceed the recent trends of fifty cents an hour increases and so would signal a stronger message in 2006 about a commitment to reach the government's aspirational goal
 - d. an increase over \$10.50 an hour could mean a higher risk that the rate of growth of minimum wage jobs would slow, especially if there is a downturn in the economy or a further softening in economic conditions
 - e. that the 80% relativity between the adult minimum wage and the youth minimum wage and the training minimum wage should be retained and that the youth minimum wage should continue to apply for 16 and 17 year olds at this time.
13. Increases in minimum wages would particularly benefit women, younger workers, Maori and Pacific peoples, new migrants, people with disabilities, the low-skilled, and people with non-English speaking backgrounds who are over-represented among minimum wage earners.¹ Changes in the minimum wage also affect employees in the agriculture, retail and related trades, and accommodation and catering sectors, and small/medium enterprises due to the higher proportion of low wage employees in these sectors and SMEs.
14. Correspondingly, employers in these sectors and SMEs are more likely to need to respond to increases in minimum wages. Currently the Department of Labour has a limited and theoretical understanding of how businesses actually respond to increases in minimum wages. Over the next year the Department intends to develop a programme of work (evaluation strategy) to better evaluate the impacts of minimum wage changes and businesses responses to these changes.
15. The Department of Labour will also review relativities between the adult, youth and training rates and will carry out further work on reported non-compliance with minimum wage rates should be a priority in our research and evaluation programme for the 2006 minimum wage review.

SECTION A BACKGROUND AND CONTEXT

16. The minimum wage is part of the government's general responsibility to ensure socially acceptable employment standards that are prescribed and enforceable. In addition, there are formal international commitments that establish an explicit obligation on the government to ensure an adequate minimum wage, including under ILO Convention 26 which obliges the government to create minimum wage fixing machinery where "no arrangements exist for the effective regulation of wages ...and wages are exceptionally low", and recommends that minimum wages should be set according to the "general level of wages prevailing in the country".

¹ Detail on the impact of minimum wage changes on subgroups is contained in Appendix C.

17. Minimum wages are set through an Order in Council made under Section 4 of the Minimum Wage Act 1983 (the Act). The minimum wage provides a floor for wages paid to employees, and it is an offence to pay wages below the prescribed hourly rate.
18. Where a minimum wage is set, the Minister of Labour has a statutory obligation under Section 5 of the Act to review the level of the minimum wage by 31 December each year.
19. Since 2000 there have been a number of changes in the structure of minimum wages:
- a. the age of eligibility for the adult minimum wage was lowered from 20 years to 18 years in 2001. This change provided consistency with the age for general eligibility to benefits and the UNCROC age for children, as well as providing a fairer wage to young people
 - b. the youth (16 and 17 year olds) minimum wage increased from 60% to 80% of the adult minimum wage, in two steps in 2001 and 2002, to provide a fairer wage for young people
 - c. a training minimum wage was introduced in June 2003 to replace an exemption from the minimum wage for employees enrolled in training. The training minimum wage was set at the youth minimum wage for 16 and 17 year olds, as their lower rate implicitly reflects extra training that the group usually requires.
20. Since 2002, the adult minimum wage rate has increased by \$0.50 a year, a rate which has slightly outpaced annual increases in the average wage. Changes in minimum wage rates are set out in a table in Appendix A.

Assessing options for changes to minimum wage rates

21. In assessing the appropriate level of the minimum wage, this report considers the current political context in which agreements have been made around reaching an aspirational goal for the minimum wage, the current and projected economic and labour market conditions, the government's objectives for the minimum wage (set out below) the costs and benefits to employers and employees of an increase in the minimum wage, and the views of submitters.

Political context - the government's aspirational goal

22. The 2005 pre-election Labour Party manifesto contained a commitment to continue to make annual adjustments to the minimum wage. Additionally, in the Labour-led government's Confidence and Supply Agreement with NZ First and the Co-operation Agreement with the Green Party, the government has committed to continue the practice of annually increasing the minimum wage, with a view to it being set at \$12.00 per hour by the end of 2008, if economic conditions permit.
23. In her address to the New Zealand Council of Trade Unions (NZCTU) on 18 October, the Prime Minister indicated that "*the aspiration over the next four adjustments is to see it move close to \$12 an hour for the adult rate*".

24. I consider that there are benefits to be gained in identifying (and communicating publicly) an intended progression towards this goal at the outset. Such communication would, however, need to emphasize the provisional nature of the path, so that the flexibility to modify the progression in response to changes in economic circumstances is retained. Communicating an intended path would enable affected sectors and firms to plan ahead for the adjustments they will need to make. For the same reasons, several submitters stated a preference to know from 2006 onwards the size and timing of adjustments.
- 25 I intend to publicise an intended path, including the size and timing of steps to reach \$12 an hour, subject to economic conditions, at the same time as announcements are made on an adjustment for 2006. This announcement would not over-ride the requirement to review minimum wages annually.
- 26 Paragraphs 31 - 33 below outline how the Department will assess prevailing economic conditions for the purposes of future reviews.

Economic context - the labour market outlook to 2009

- 27 The current review of the minimum wage takes place against a background of a strong labour market. In the September 2005 quarter, the unemployment rate was the lowest in the OECD at 3.4%. The labour force participation rate rose to a record high of 68.2%, and labour shortage indicators fell but remained very high. This labour market performance has been supported by robust economic growth of 3.1% in the year to June 2005.
- 28 The past year's economic growth of 3.1% is, however, the lowest rate since 2001 and it is likely to slow further. In the Pre-Election Economic and Fiscal Update 2005, Treasury forecast a fall in economic growth to 2.2% in the year to March 2006, followed by 2.6% growth the next year. A further lift to 3.5% and 3.1% is then forecast for the years to March 2008 and March 2009 respectively.
- 29 Based on consensus economic forecasting, the Department of Labour expects labour market conditions to ease slightly over the next two years. Four main factors underpin the Department's labour market outlook:
- a. an easing of employment growth and skill shortages due to the recent and expected slowing of growth in the New Zealand economy
 - b. a small rise in the unemployment rate to around 4.0% in the March 2007 quarter
 - c. a continued high rate of participation and a stabilisation of net migration inflows, and
 - d. a gradual rise in labour productivity growth due to factors such as strong growth in business investment.
- 30 There are also risks to the labour market outlook. Major risk factors surround inflation, business confidence, oil prices, interest rates, the exchange rate, and the housing market. An additional risk factor is net migration (inflows of 6,000-8,000

people per annum are currently expected in the short-term), where a swing into outflows would affect the labour market directly.²

- 31 Currently the Department's assessment of economic conditions is based on an aggregate assessment of consensus opinion around prevailing and forecast economic and labour market conditions. The information contained in this aggregate assessment could be disaggregated to provide a richer understanding of prevailing economic conditions, and increase transparency around decision-making. The Department is currently exploring work around different indicators that would be appropriate to use in this case (known as 'leading indicators of employment') as a separate exercise, and intends to feed this work into future reviews to increase transparency around the assessment of prevailing economic conditions. To illustrate what leading indicators might include, indicators already identified by the Treasury as leading indicators of employment are:
- a. aggregate economic activity
 - b. consumption demand
 - c. investment demand
 - d. trade indicators
 - e. financial and monetary indicators
 - f. consumer and business confidence indicators
 - g. labour market indicators, and
 - h. foreign indicators.
- 32 The Department's work will confirm the use of these, or other, indicators in future reviews.
- 33 While the interpretation of economic conditions is an art as well as a science and macroeconomic indicators cannot be used in a mechanistic way, significant changes in some or all of these (or other) indicators may suggest that the intended progression towards \$12 an hour should be modified (up or down).

Objectives and criteria for the minimum wage

- 34 Changes to the minimum wages are part of a wider mix of approaches to support higher quality working lives and productive workplaces. These approaches include work underway on workplace productivity, work life balance, the Working for Families package, initiatives to address skill and labour shortages, work to promote pay and employment equity, and work to enhance parents' and other carers' choices.
- 35 The government has previously agreed to objectives for the minimum wage (FIN (00) M 29/1 and CAB (00) M 33/1E refer) that form the basis of this minimum wage

² Department of Labour report "Labour Market Outlook – October 2005" refers, www.dol.govt.nz/publications/lmr/index.asp

review. The objectives for the minimum wage, and associated benchmarks to help set the minimum wage are:

1. **Objective 1: Fairness – to ensure that wages paid are no lower than a socially acceptable minimum.** There are two main views on what constitutes a socially acceptable minimum. One option is to determine social acceptability as a proportion of how much other workers earn (e.g. average wages). A target of 2/3 of average wages is the long term target recommended by the NZCTU. Another option is to view social acceptability through determining the amount needed to maintain a set standard of living, adjusted for inflation. **Benchmarks:** average wages, CPI.
2. **Objective 2: Protection – to offer wage protection to vulnerable workers so that workers are paid wages that reflect their worth or productivity.** Workers may be “underpaid” on this measure when they have a relative lack of bargaining power, such as when they have limited bargaining strength (e.g. are not collectivised and unable to strike for higher wages), or face risks in leaving and finding another job (e.g. poor English, disability), or have poor income or employment alternatives (e.g. they do not qualify for unemployment benefits). **Benchmarks:** minimum wages paid under collective agreements.
3. **Objective 3: Income Distribution – to ensure that earnings of people on low incomes do not deteriorate relative to those of other workers.** This is likely to reflect a preference that society has for the degree of wage (and income) equality, and this may promote greater social cohesion. The effectiveness of minimum wages to achieve this objective depends on whether employment effects occur, since the income of workers is significantly lowered where they may lose their jobs or have their work hours cut. **Benchmarks:** changes in average and median wages.
4. **Objective 4: Work Incentives – to increase the incentives to work for people considering work.** Creating the correct incentives requires the minimum wage to be set at a level that makes work attractive compared to not working. This may be relevant if skill shortages exist for certain low pay occupations. The minimum wage needs to be above benefit levels and associated employment costs such as childcare and transport costs that are payable by a worker. At some point, however, a higher minimum wage can “frustrate” work incentives through economic effects that restrict job opportunities available to low skilled workers. **Benchmarks:** benefit levels and costs associated with working.

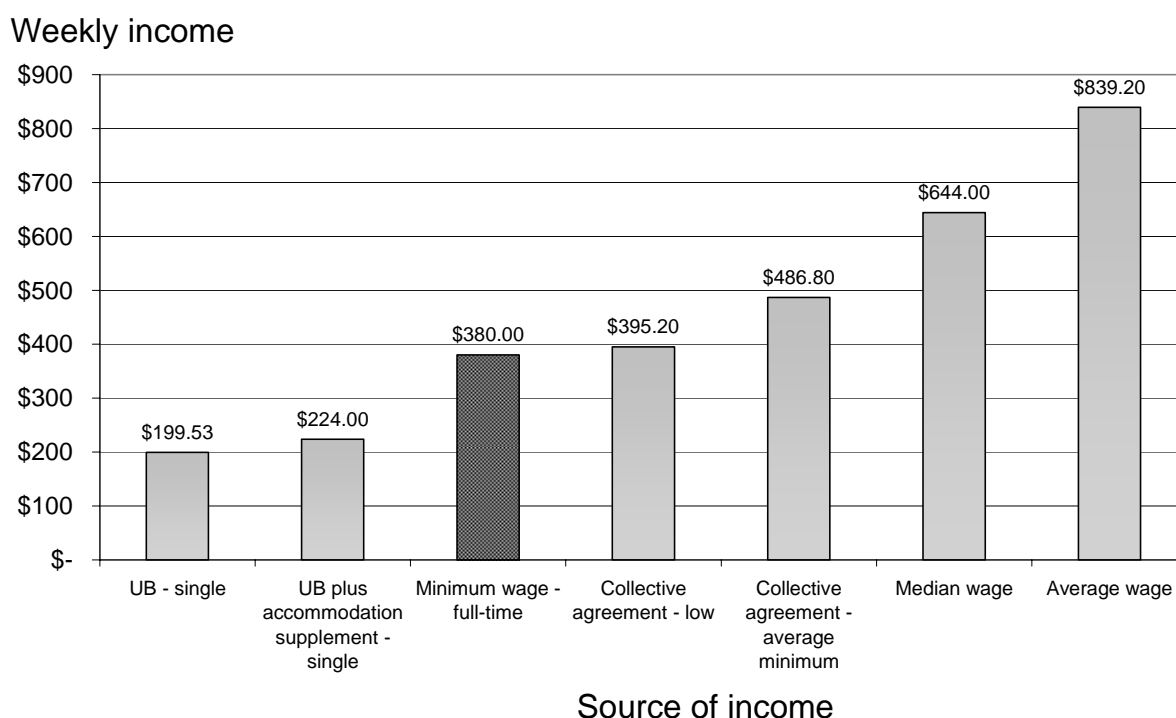
36 The agreed criteria for assessing changes to the minimum wage are:

- a. do changes in the minimum wage produce gains that are more significant than any losses?
- b. is the minimum wage the lowest cost way of implementing the objectives of the policy?
- c. does the level of the minimum wage form part of the most appropriate mix of measures to meet the broader objectives of the government?

Benchmarks arising from the objectives

37 The following chart compares the current minimum wage to several other income benchmarks. It shows that the current minimum wage is 90.4% higher than the unemployment benefit (for a single adult with no supplementary assistance such as Accommodation Supplement, if the Accommodation Supplement is added, a single adult could receive an additional \$24 dollars a week on top of their main benefit). The current minimum wage is approximately 45.3% of average hourly earnings (using the Quarterly Employment Survey) and 59.0% of median hourly earnings (according to the HLFIS Income Supplement).

Figure 1: Comparison of current minimum wage with other gross weekly income benchmarks



International benchmarks

38 The most recent report of the UK Low Pay Commission (February 2005) suggests that the New Zealand minimum wage is slightly above average compared with other countries (as at June last year). Looking at the adult minimum wage relative to full-time median earnings, our minimum wage was 53.6% of the median wage.³ The Australian ratio is between 55.1%-58.8% (depending on what survey is used), the UK ratio was 43.2% and the US ratio was 32.2%. Out of the 13 countries surveyed, only France had a higher ratio at 56.6%. When comparing what a single unit of currency will buy across different countries ('purchasing power parity', or PPP ratings), however, a slightly different story is told. Australia has the highest rate at 5.37 PPP, the UK is next at 4.85, followed by NZ at 4.01, and the US is the lowest at 3.37 PPPs.

³ "National Minimum Wage, Low Pay Commission Report 2005, p.237.

SECTION B ACHIEVING THE \$12 AN HOUR GOAL FOR THE MINIMUM WAGE

Possible steps to reach \$12 an hour by the end of 2008

- 39 Achieving \$12 an hour for adults would represent an increase of 26.3% from the current minimum wage rate for the adult, and youth and trainee rates if current relativities between the rates are maintained. As a point of comparison, the percentage increase over the past four years (2001-2005) was 23.7%.
- 40 Below are four credible options for reaching the government's goal by the end of 2008, if economic conditions permit. The progressions vary according to the different incremental increases suggested across the timeframe. If shown in graph form, the resulting curves would respectively appear 'smooth', 'frontloaded', 'double spiked' or 'bell-shaped curve', and are labelled accordingly.
- 41 The tables indicate four steps to reach \$12 an hour. Minimum wage changes are agreed by Cabinet in December and generally implemented in the following March, so the first step would take effect in March 2006. The rates shown assume the 80% relativity between the adult, youth and training minimum wages is retained.

'Smooth'

- 42 The progression set out in table 1 is as even as possible over four adjustment periods. If economic conditions remain fairly stable over four years, this progression would spread the impacts of the change evenly over the period.

Table 1: Smooth progression towards \$12 an hour by end 2008

Step	Adult minimum wage rate	Dollar Increase	40 hour week	Youth/trainee minimum wage rate
March 2006	\$10.13	\$0.63	\$405.20	\$8.10*
March 2007	\$10.75	\$0.62	\$430	\$8.60
March 2008	\$11.38	\$0.63	\$455.20	\$9.10*
March 2009	\$12	\$0.62	\$480	\$9.60

*numbers are rounded to nearest cent.

'Frontloaded'

- 43 Table 2 sets out two \$0.75 increases followed by two, \$0.50 increases. This 'frontloading' would send a strong signal about the government's intention to achieving the aspirational goal by 2008.

Table 2: Frontloaded progression

Step	Adult minimum wage rate	Dollar Increase	40 hour week	Youth/trainee minimum wage rate
March 2006	\$10.25	\$0.75	\$410	\$8.20
March 2007	\$11.00	\$0.75	\$440	\$8.80
March 2008	\$11.50	\$0.50	\$460	\$9.20

March 2009	\$12	\$0.50	\$480	\$9.60
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'Double spiked'

44 Table 3 shows a \$0.75 increase in the first year and final years; with \$0.50 increases in the two middle years, if economic conditions permit.

Table 3: Double spike progression

Step	Adult minimum wage rate	Dollar Increase	40 hour week	Youth/trainee minimum wage rate
March 2006	\$10.25	\$0.75	\$410	\$8.20
March 2007	\$10.75	\$0.50	\$430	\$8.60
March 2008	\$11.25	\$0.50	\$450	\$9.00
March 2009	\$12	\$0.75	\$480	\$9.60

'Bell-shaped curve'

45 The table below sets out a three-step progression for incremental adjustments which would achieve the government's goal of \$12 an hour before the next scheduled general election.

Table 4: Bell-shaped curve

Step	Adult minimum wage rate	Dollar Increase	40 hour week	Youth/trainee minimum wage rate
March 2006	\$10.25	\$0.75	\$410	\$8.20
March 2007	\$11.25	\$1.00	\$450	\$9.00
March 2008	\$12.00	\$0.75	\$480	\$9.60

Assessment of path options

46 The assessment below attempts to identify and weigh different costs and benefits associated with each of the different paths identified for delivering on the aspiration to reach \$12 an hour. I consider that at the macroeconomic level there is little difference between these options. There may be some limited constraint on economic (job) growth and some inflationary pressures resulting from the increases. There are different costs and benefits, however, at the sector and firm level for employers and for employees that are associated with the options, and, in deciding on a preferred option at this time will essentially involve a trade-off between these different costs and benefits. Depending on the rate of change, there may also be some trade-offs between the government's social objectives (for example, if hours of work are reduced for minimum wage earners in firms unable to adjust quickly to increases). I consider that prevailing economic and labour market conditions indicate that an increase to \$12 an hour by the end of 2008 appears sustainable, therefore determining the most appropriate steps to achieve that goal will involve a political

decision around the trade-offs between larger increments occurring earlier in the timeframe ('frontloading') or later ('backloading' the increase).

- 47 More income and social benefits will accrue to minimum wage and low paid workers from the frontloaded option, and this option also will also send a clear signal about the government's intention to reach the aspirational goal. If economic conditions soften in the latter half of the timeframe, then relatively smaller increases in later years are more likely to be sustainable and less likely to represent a constraint on future economic growth.
- 48 Leaving a large increase until later, or last in the series of steps to \$12 may mean that fewer people are impacted by that change than if the large increase is introduced early on (this assumes people earning just over the minimum wage rates will move up the wage distribution scale as nominal base line wage changes occur during the period).
- 49 A larger increase early on will directly affect more people, and they would benefit for a longer period (from 2006 rather than, say, 2009). The need to manage cost increases will be reduced for sectors and firms when larger increases occur later in the cycle, or are 'backloaded'. This is because backloading the larger increases as in the 'double spiked' option, will reduce the overall real and proportional costs for employers. It will also give them more time to plan for the adjustments they might make, for example by investing in skill development or other ways to increase productivity.
- 50 The 'smooth' option would spread the different costs and benefits evenly over the timeframe. The 'double spiked' option, which involves frontloading and backloading increases, could also be considered to balance the trade-offs with a strong signal of the intention to reach the aspirational goal of \$12 an hour, as well as providing an opportunity for employers to manage and respond to minimum wage increases.
- 51 As a secondary consideration (but a practical one), anecdotally employers prefer to pay wages in 'rounded up' amounts as this simplifies pay calculations.⁴ Round number minimum wages are also advantageous for employees as it is easier to recall wages in round numbers, and this may aid compliance from both employee and employer perspectives. (Of course, employers can choose to round wages up to a rate above the minimum wage if they perceive the benefits arising from ease of wage calculation outweigh the cost of the additional wage bill). In this sense, the 'smooth' option is the least helpful (a small amount of rounding of this progression would resolve this problem to some extent).

Forecasted growth and the options to achieve \$12 an hour

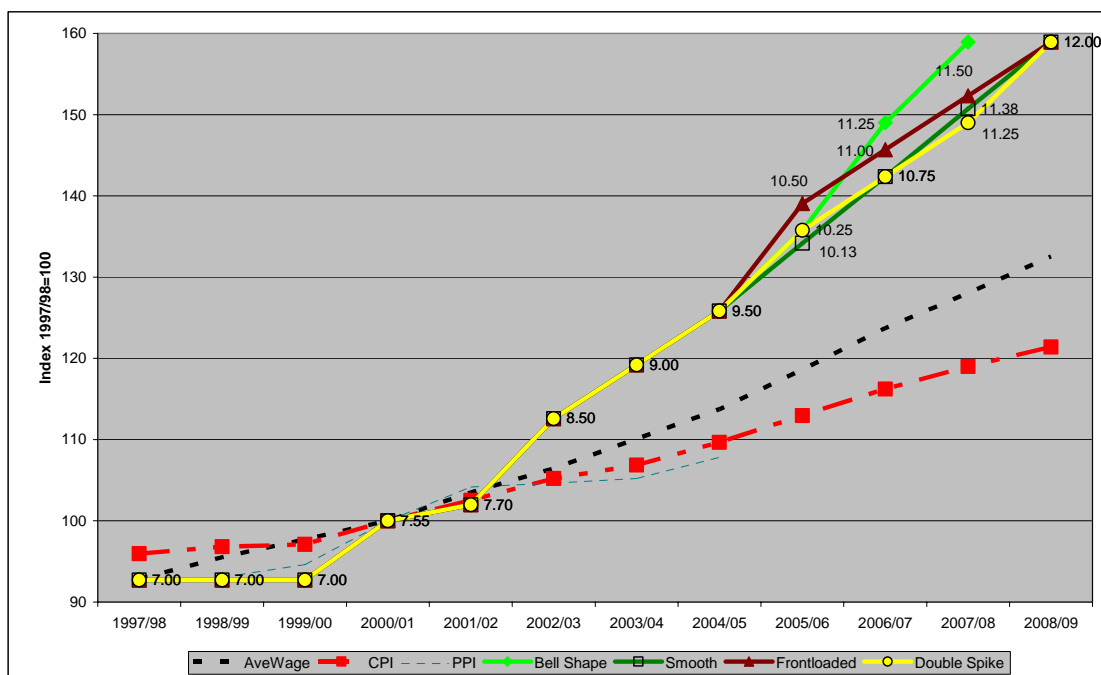
- 52 The growth rate trajectories of the various minimum wage options to reach \$12 an hour are compared in the figure below. This figure illustrates how the options compare with each other and with the growth rates of the (private sector) average wage in the economy, the Producers Price Index (PPI) (output prices) and the

⁴ Anecdotal evidence from Labour inspectors, October 2005.

Consumers Price Index (CPI).⁵ This figure shows that all selected paths grow faster than the rate of growth of the average wage, CPI inflation, and the PPI, and that the rate of outpacing varies somewhat between them by year, but that the differences are essentially marginal.

- 53 The figure shows that since 2002, the rate of growth of the minimum wage has started to outpace the PPI, CPI and the average wage in the private sector. In the recent past, minimum wage rates have been either catching up with (i.e., in 2003) and/or kept up with average wage rate levels. Since 2003, minimum wage rates have outpaced the growth in average wage rates.
- 54 Given the aspirational goal of a \$12.00 minimum wage by the end of 2008, the gap between the growth rates of the minimum and average wage are expected to increase considerably in the next 4 years (i.e. the minimum wage is getting closer to the average wage over that time). The increase of the minimum wage in proportion to the average wage will increase the real value of the minimum wage, will raise the level of protection, improve income distribution levels and increase the incentives to work. I consider that such an increase would have negligible risks of constraining job growth.

Figure 2: Average Wage, PPI, CPI and various minimum wage options (2000=100)



Source: NZIER (Average Wage in Private Sector, PPI, CPI), Department of Labour (Minimum Wage Options)

⁵ Actual data is used up to 2004/05, and NZIER forecasts are used to 2008/09 (for the years ending March). Data are derived and presented in index format (Base 2000=100) (in Figure 1) as well as in terms of annual % change (in Figure 2) for the years ending March.

SECTION C OPTIONS FOR THE FIRST STEP IN 2006

Identification of options for the first step in 2006

55 Analysis of submissions on the review (see Appendix D), benchmarks arising from the government's agreed objectives for the minimum wage and incorporating possible first steps towards the government's aspirational goal based on the paths outlined above suggests a range of options for the minimum wage for implementation in 2006.

I. **Option 1: retain the existing minimum wage (\$9.50 per hour or \$380 per week)** Leaving minimum wages at this level would see those wages erode in real value, and decrease relative to benefit payments (which are indexed to CPI). This option is recommended by Business New Zealand, the Hospitality Association of New Zealand, the National Association of Retail Grocers and Supermarkets of New Zealand, the Small Business Advisory Group and Federated Farmers.

II. **Option 2: maintaining relativity with average wages and recent trends**

Option 2A: Increase to \$9.83 or \$393.20 per week which reflects the movement in average wages. This represents an increase of 33 cents an hour or an increase of 3.5% which equates to the movement in average hourly earnings as measured by the Quarterly Employment Survey, or QES. This option is considered 'fair' by the Retailers Association of New Zealand. This is also close to the lowest minimum pay rate in collective agreements (\$9.88).

Option 2B: Increase to \$10.00 per hour (or \$400 per week) in line with trend set since 2000. This is a 5.3% or 50 cents increase on the current rate, which is consistent with recent adjustments. This increase would also continue the accelerated rate of change (relative to the average wage) that has occurred since 2003 (i.e. minimum wage increases are outpacing average wage increases at a fairly constant pace⁶, e.g. a 1.8% increase compared with 1.2% last year).

III. **Option 3: increase above the rate needed to maintain relativity with average wages and recent trends, in order to achieve the government's aspirational goal of \$12 an hour for adults by the end of 2008**

Option 3A: Increase to \$10.13 an hour (\$405 a week) as a step towards \$12 an hour. This represents an increase of 63 cents per hour or a 6.6% increase on the current rate. This increase represents the first step in the 'smooth' progression towards reaching \$12 an hour.

Option 3B: Increase to \$10.25 an hour (\$410 a week) as a step towards \$12 an hour. This represents an increase of 75 cents per hour or a 7.9% increase on the current rate. This increase represents the first step in the

⁶ In 2004 the minimum wage increase outpaced the average wage increase by 1.08%. The present option would mean the minimum wage is outpacing the average wage by 1.2%.

'frontloaded' progression towards reaching \$12 an hour, with \$0.75 being the biggest increase in this progression.

Option 3C: Increase to \$10.50 per hour or \$420 per week. This represents an increase of \$1.00 per hour, which would be a 10.5% increase on the current rate.

- IV. **Option 4: increase above the rate needed to maintain relativity with average wages and recent trends, NZCTU option. Increase to \$12.00 per hour or \$480 per week.** This represents an increase of \$2.50 per hour which would be a 26.3% increase on the current rate. This option is recommended by the New Zealand Council of Trade Unions (NZCTU).

- 56 I recommend that the current relativities between the adult, youth, and training minimum wages remain as they are, that is, the youth and training minimum wage rates remain at 80% of the adult rate. The Department of Labour will continue to review the relativities between minimum wage rates as progression is made towards reaching \$12 an hour for adults, to ensure that the relativities remain appropriate.
- 57 For the first step in 2006, an increase beyond that needed to retain relativity with average wages (e.g. beyond \$9.83) will increase the real value of the minimum wage, will raise the level of protection, improve income distribution levels and increase the incentives to work. I consider such an increase would have negligible risks of constraining job growth. I consider that an increase of up to one dollar in the hourly minimum wage rate can be made in the current economic and labour market conditions.

Summary of other options assessment

- 58 A progression that implements an adjustment in the first year (2006) that is larger than the fifty cent an hour increase that has been the trend in recent years will send a clear signal about the intention to reach the aspirational goal. This reasoning would support an increase to beyond \$10.00 an hour i.e. an adjustment to \$10.25 or \$10.50 an hour in 2006 for adults. I consider that such an adjustment could be made with confidence in the current economic and labour market environment, but that an adjustment beyond \$10.50 would create more risks of slowing job growth and increasing inflationary pressures, particularly if there is an economic downturn, or if economic conditions soften.
- 59 The number of people who would receive an hourly pay rise (number of people aged 18 and over 'directly affected' by the various options) jumps significantly after increases of more than 50 cents an hour. This is because comparatively large numbers of people earn exactly \$10 an hour, and these people would not be directly affected by an increase to \$10 an hour but would be directly affected by an increase over \$10.
- 60 A fifty cent an hour increase will directly affect **28,400** workers (or 1.8% of all employees aged 18 years and over), a seventy-five cent an hour increase will directly affect **91,000** workers (5.9%), and a \$1.00 increase will directly affect **103,500** (6.7%), as at June 2005. If relativities between adult and youth rates remain the

same, the corresponding numbers for youth are 3, 500 (6.3% of 16 -17 year old employees), 10,000 (16.9%) and 11,000 (18.7%). If people who currently report non-compliance with the minimum wage rate (55,000 or 3.4% of adults) and people who are close to the wage bands also receive an increase in their hourly rate as a result of an increase in the wage band, more people will be affected by the increases (these numbers are difficult to quantify, however, because of uncertainties about the impacts on these groups), (Appendix C refers).

- 61 More detail on the potential impacts of different options for the level of minimum wages for 2006 on population groups, on sectors and firms, and on employers, is provided in Appendix B. An assessment of the impacts of changes to the minimum wage for recipients of Working for Families package is provided in paragraphs 65 – 71 below.
- 62 The two tables below indicate the numbers of adults and youth directly affected by an increase in the minimum wage.

Table 5: Impact of minimum wage options - adults (18 years and over)

Option for 2006	Hourly rate	Weekly rate	Cumulative no. of people who would receive a wage rise and percentage of employees cohort
1	\$9.50	\$380	0
2A	\$9.83	\$393	24,900 (1.6%)
2B	\$10.00	\$400	28,400 (1.8%)
3A	\$10.13	\$405	86,140 (5.6%)
3B	\$10.25	\$408	91,000 (5.7%)
3C	\$10.50	\$420	103,500 (6.5%)
4	\$12.00	\$480	246,600 (15.5%)

Table 6: Impact of Youth (16 and 17 years) Minimum Wage Options

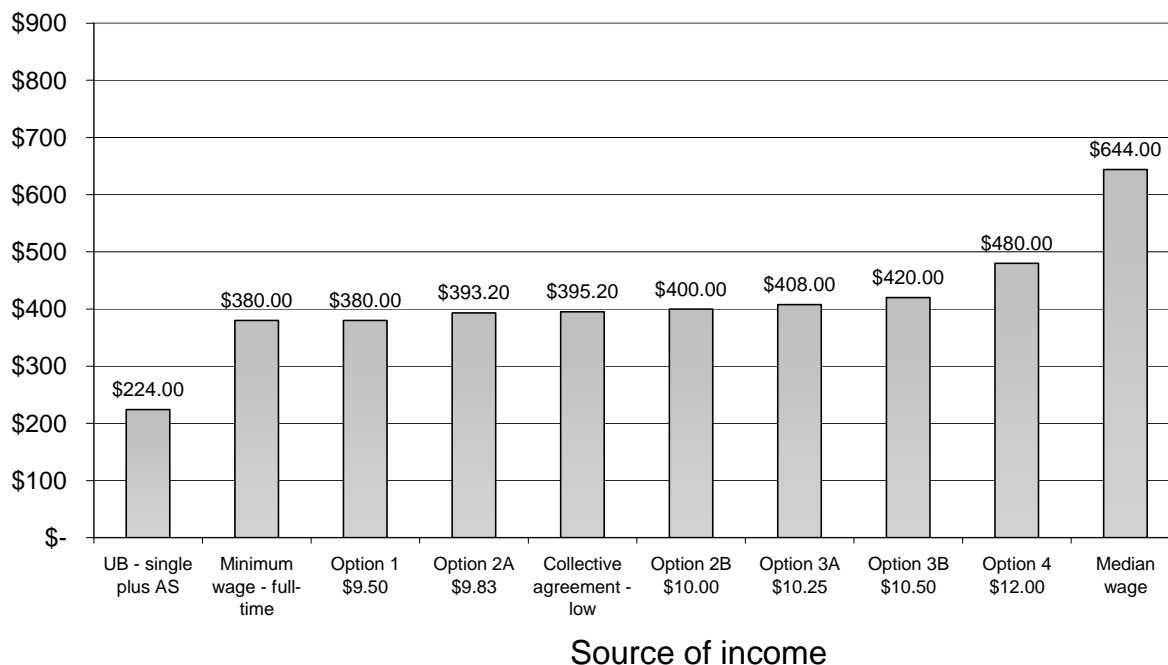
Option for 2006	Hourly rate	Weekly rate	Cumulative no. of people who would receive a wage rise and percentage of youth workforce
1	\$7.60	\$304	0
2A	\$7.86	\$315	3,500 (5.8%)
2B	\$8.00	\$320	3,700 (6.3%)
3A	\$8.10	\$324	9,420 (18.6%)
3B	\$8.20	\$328	10,000 (16.9%)
3C	\$8.40	\$336	11,000 (18.7%)
4	\$9.60	\$384	24,700 (41.8%)

- 63 The figure below shows how the various options given above compare with median wage, the unemployment benefit and the lowest wage in collective agreements (as at

June 2005). These are among the key indicators the Department of Labour uses to compare changes in the minimum wage.

Figure 3: Options compared with some key indicators

Weekly income



64 The table below indicates where the options for the first step are located in relation to the benchmarks. As points of comparison, the table also shows other benchmarks against which minimum wage changes can be measured, and the objectives associated with these benchmarks.

Table 7: Options for first step assessed against benchmarks

Option	Objective(s) prioritised through option	Per hour	40 hour week
1 - current minimum wage Recommended by Business NZ, Federated Farmers and Hospitality Association, SBAG first preference	Erodes existing levels of fairness, protection, income distribution and work incentives	\$9.50	\$380
2A – current minimum wage increased by average wage growth of 3.5%. SBAG third preference, considered 'fair' by Retailers	Maintains existing levels of fairness, protection, income distribution and work incentives	\$9.83	\$393

Association			
2B – maintain trend of fifty cents an hour increases	Protection	\$10.00	\$400
3A – first step in a “smooth” progression		\$9.63	\$405
3B – first step in a “frontloaded’ or ‘double spiked’ progressions	Protection, income distribution, work incentives	\$10.25	\$410
3C – a one dollar increase on current rate	Protection, income distribution, work incentives	\$10.50	\$420
4 – NZCTU recommendation for 2006	Fairness, protection, income distribution, work incentives (reflecting NZCTU’s submission)	\$12.00	\$480
Benchmarks			
Unemployment Benefit – single person aged under 20	Work incentives		\$165
Unemployment Benefit – single person aged 25 years and over	Work incentives		\$200
Unemployment Benefit and Accommodation Supplement – single person aged 25 years +	Work incentives		\$224
Collective Agreements – lowest minimum wage	Protection	\$9.88	\$305
50% of average wage	Fairness	\$10.49	\$420
2/3 rd median wage	Fairness	\$10.73	\$430
Collective Agreements– average minimum wage	Protection	\$12.17	\$487
66% of average wage – CTU ‘longer term’	Fairness	\$13.85	\$554

recommendation			
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Working for Families assistance package

- 65 The interface between the minimum wage and in-work assistance to low and middle income working families (“Working for Families”) is important for assessing the overall effectiveness and impacts of changes to the minimum wage. Working for Families is arguably better suited to meeting household income needs, and the needs of these families. However, not all minimum wage earners will be eligible for Working for Families, so the two policy mechanisms need to work together to ensure the government’s overall income adequacy objectives are achieved.
- 66 This minimum wage review is the first review to seriously consider these interface issues between Working for Families and minimum wage increases. For people who are in receipt of family assistance that is abated against income (for example the Accommodation Supplement, Family Support and Childcare Subsidy), increases in income resulting from rises in the minimum wage will result in a decrease in the level of these forms of assistance for some people.
- 67 Preliminary Ministry of Social Development modelling work indicates that much of the re-distributional gains from gross increases in the minimum wage for these employees and their families will be limited due to the impact of:
- a individual marginal tax rates (15 cents or 24 cents in the dollar)
 - b abatement of first, second and third tier benefits (including the Accommodation Supplement), and
 - c abatement of Family Assistance as the minimum wage increases.
- 68 Generally, however, the decrease in supplementary assistance will be less than the increase from the minimum wage and these families will therefore experience a net gain.
- 69 Minimum wages will however continue to raise incomes for individuals or families which do not receive Working for Families assistance. These are either people or couples in families without children, or people on low wage jobs living in well-off families. Increases in the minimum wage will also be continue to be important in raising the incomes of families that do not access their full entitlements under Working for Families.
- 70 More detail on the Ministry of Social Development’s indicative modelling is available. This modelling sets out outcomes for four different family types, and the net distributional impacts on their Working for Families and other (tax/benefit) entitlements when the minimum wage is raised by either \$0.50 or \$1.00 an hour.
- 71 The Department of Labour will work with the Ministry of Social Development to provide firmer modelling in the 2006 review around the impact of minimum wage

increases on Working for Families recipients following the implementation of additional Working for Families assistance next year.

Evaluation strategy

- 72 The Department of Labour is proposing to do further work to examine the effect of minimum wage increases. This work would include:
- a case studies of adjustment to the change of particular firms in the sectors where most minimum wage workers are to be found
 - b an HLFS time series econometric study of employment rates of potentially vulnerable groups (including women, youth, Maori and Pacific peoples, recent migrants, the low-skilled) along the lines of previous *Chapple* (1997) and *Maloney* (1995), work which is now well outdated
 - c examination of PAYE/LEED data to monitor pay changes
 - d examination of 'flow-on' effects up the earnings distribution via looking at changes in the Income Supplement (IS) of the HLFS earnings distribution before and after increases, and
 - e further work to monitor and explain the high levels of non-compliance with the minimum wage that are reported in the income supplement to the HLFS, with a view to providing more advice on this matter in the Department of Labour's 2006 minimum wage review report.

Implementation, timing and publicity of the minimum wage decision

- 73 I intend to make a media statement on the decisions about minimum wages following Cabinet confirmation, including decisions around an intended path to reach \$12 an hour by the end of 2008, if economic conditions permit, and for the first step towards this goal in 2006.
- 74 Changes to minimum wage rates are implemented by Order in Council. The process for authorisation by Cabinet, drafting and the 28 day waiting period for regulations mean that minimum wage changes generally come into force in March. I consider that an appropriate date for minimum wage increases from this paper to come into force is Monday 27 March 2006.

Fiscal implications

- 75 The overall fiscal impact of increases in adult and youth minimum wages is unclear, but is likely to be small as a relatively small proportion of the workforce earn minimum wages. If some people's hours of work are reduced or they remain unemployed as a result of the increases, benefit payments would be affected. For others, higher wages may mean a slight increase in tax paid or a reduction in income support payments.

76 There are a number of state sector employees (and contractors) that earn wages of \$12 per hour or less, particularly in the public health and compulsory education sectors. Future increases in the minimum wage are therefore likely to have direct (and possibly also indirect or 'flow-on') costs for some state sector employers. These costs and the likelihood that organisations will seek additional funding to compensate for them, will be higher if Ministers wish to make large movements towards the minimum wage goal of \$12 per hour early in the 4 year period

Human rights implications

77 The proposed adjustment of minimum wage rates draws a distinction between workers on the basis of age. This proposal is consistent with the New Zealand Bill of Rights Act 1990, as it is specifically provided for under the Human Rights Act 1993.

Gender implications

78 Women are over-represented amongst those earning low wages. This is especially so for Maori and Pacific women and women of 'other' ethnicities. These groups, therefore, would be expected to benefit from any resulting wage increases.

Implications for people with disabilities

79 People with disabilities are over-represented amongst those earning low wages. People with disabilities would be expected to benefit from increases in the minimum wage.

Regulatory impact and business compliance cost statements

80 A Regulatory Impact Statement / Business Compliance Cost Statement (RIS/BCCS) that complies with the requirements set out by the Cabinet Office is attached. Based on the information provided in the attached RIS/BCCS, the Business Compliance Costs Unit considers that the disclosure of information is adequate, and the level of analysis is appropriate given the likely impacts of the proposal.

81 If the minimum wage is increased, employers will be required to raise the wages of those employees earning less than the new minimum wage from the time that the new minimum wage comes into force. Making wage adjustment will require minor changes to payroll systems, but otherwise, the regulatory requirements would remain unchanged. Adjusting to higher minimum wage rates may impact more on some employers operating on relatively tight margins.

Consultation

82 Submissions were invited from a number of organisations as part of this review. In addition, the Department of Labour met separately with the New Zealand Council of Trade Unions, the Small Business Advisory Group and Business New Zealand to discuss some of the key issues relating to their submissions (see Appendix D for a summary of submissions).

- 83 The Treasury, Ministries of Education, Women's Affairs, Pacific Island Affairs, Social Development, Economic Development, and Youth Development, Te Puni Kokiri, Tertiary Education Commission, the Office for Disability Issues, and the Department of the Prime Minister and Cabinet have been consulted on this paper.
- 84 The Ministry of Social Development (MSD) supports the improvement in work incentives resulting from minimum wage increases, but notes that the impact on work incentives, even from such a large rise, is comparatively small. MSD notes their concerns about the unknown disemployment effects of pushing minimum wages significantly above historic levels, especially for highly disadvantaged people, and the downside risks it may create for the government's sustainable employment goal.
- 85 MSD also notes concern about the extent to which extra pay resulting from the rise actually ends up with taxpayers, rather than taken home by low paid workers to low income families. MSD observes that in the current post-Working for Families environment raising the minimum wage is not a particularly effective way to improve the take-home income of poor working families. In terms of transition paths, MSD's judgement of possible risks/possible returns from the policy is that MSD would favour the slowest transitional path to \$12.00 per hour. MSD considers that the path should be pre-announced.
- 86 Additionally MSD strongly advocate rigorous ongoing evaluation of possible disemployment & re-distributional impacts.
- 87 The Treasury notes that an increase in the minimum wage to above \$10 per hour in 2006 would directly affect a considerably larger number of workers than have been affected by previous increases in the minimum wage. The proportion of young workers affected would be particularly high.
- 88 The Treasury forecasts that an increase in the minimum wage to \$12 per hour in 2008 would increase the number of directly affected workers to around 50 percent of those aged 18 or 19 and 10 percent of all adults. An increase to \$12 per hour in 2008 would lead to direct income gains for many of these workers. It would also increase the likelihood of a significant reduction in employment opportunities, particularly for vulnerable groups, and of wider economic losses. The extent of these potential losses cannot be quantified. However negative effects will be exacerbated if current buoyant economic and labour market conditions soften.
- 89 The Treasury notes that a minimum wage of \$12 per hour in 2008 would be likely to be one of the highest among OECD countries on a relative-to-median wage basis.
- 90 The Treasury considers that publicly announcing the government's aspirational goal to reach a minimum wage of \$12 per hour in 2008 is likely to have some benefits for business planning. Communication of an intended pathway to reach the aspirational goal may have some additional benefits in this regard, but will also reduce Ministers' flexibility to modify the pathway at future reviews in response to economic circumstances. The Treasury therefore recommends that Ministers do not agree on the size and timing of adjustments to the minimum wage beyond 2006, but continue

to review minimum wage settings annually within the context of the government's goal of reaching \$12 an hour by the end of 2008 if economic conditions permit.

- 91 The Ministry of Economic Development (MED) considers that a minimum wage increase of 75 cents in 2006 is a significant absolute rise relative to previous years and will affect a large number of workers. However, the likely effects, particularly pressure on wage margins, and firms' responses are unclear. Economic and labour market conditions are predicted to soften and there is the potential that a large rise could exacerbate this deterioration. Therefore, MED is of the opinion that a 'stepping up' approach, whereby larger increases occur in later years, will give firms more time to adjust and plan for changes in the minimum wage, while still giving a clear intention of the government's goal of \$12 and its broader drive to create a high-wage economy through greater productivity.
- 92 The Ministry of Women's Affairs supports a 'frontloaded' progression towards \$12 an hour as the current and forecast economic climate makes such an increase both possible and sustainable. The Ministry notes that increasing the minimum wage will particularly benefit women as women are over-represented amongst low waged workers.
- 93 The Ministry of Pacific Island Affairs acknowledges the importance of the Government's aspirational goal of achieving a minimum wage of \$12 an hour for those aged 18 and above by the end of 2008. Given that statistics indicate Pacific peoples earn only 83 percent of the general population median hourly earnings⁷ the Ministry recognises the proposed increase will assist in improving income levels and increase the participation rate of Pacific peoples of working age population, which in addition contributes to Pacific people's social and economic prosperity.
- 94 Te Puni Kokiri supports a 'frontloading' of minimum wage increases to reach the goal of \$12 an hour as this will raise the household incomes of low income Maori households, improve work incentives for low skilled Maori to seek employment, have less risk of a 'slow down' in job growth at this time, and signal a strong commitment towards reaching the aspirational goal. Te Puni Kokiri is generally supportive of the minimum wage review 2005.

RECOMMENDATIONS

95 I recommend that Cabinet Business Committee:

Communication of size and timing of minimum wage adjustments to 2008

either

- 1.1 **agree** that the size and timing of the adjustments to the minimum wage to the end of 2008 (if economic conditions permit) should be publicly signalled to allow affected sectors and firms time to plan for the adjustments

⁷ The median hourly income for Pacific has risen since 2000 (from \$10.50 to \$15.13 to 2004), it is still well below the national figure of \$18.24 per hour (Statistics New Zealand 2005). In addition 61 percent of Pacific peoples over 15 years of age earn less than \$20,000 per annum, compared with only 53 percent of the general population that earn less than \$20,000 per annum.

or (Treasury preference)

- 1.2 **note** that communication of an intended pathway for the minimum wage to the end of 2008 may have some benefits for business planning, but will also reduce Ministers' flexibility to modify the pathway at future reviews in response to economic circumstances,

and

- 1.3 **agree** to publicly communicate that the Government will make decisions each year about an appropriate adjustment to the minimum wage within the context of the goal of reaching \$12 an hour (adult rate) by the end of 2008 if economic conditions permit
- 2 **note** that, if you agree to the recommendation **1.1** above, I intend to make an announcement about the size and timing of intended incremental adjustments to the minimum wage at the same time as I make a media statement about Cabinet's decision with respect to an increase in 2006

Options to reach the government's goal of \$12 an hour (adult rate) by the end of 2008, if economic conditions permit**either (Treasury preference)**

- 3 **agree** that the Government will make decisions each year about an appropriate adjustment to the minimum wage within the context of the goal of reaching \$12 an hour (adult rate) by the end of 2008 if economic conditions permit

or

- 4 **agree** in principle to aim for a progression towards the aspirational goal of \$12 an hour minimum wage rate for adults to be achieved through the following adjustments to the minimum wage:

either

a \$0.63 increase to be implemented in March 2006 followed by a \$0.62 increase, a \$0.63 increase, and a \$0.62 increase, by the end of 2008, if economic conditions permit ('smooth' option)

or

a \$0.75 increase taking effect in 2006 followed by a second \$0.75 increase, a \$0.50 increase, and ending with a second \$0.50 increase, by the end of 2008, if economic conditions permit (a 'frontloaded' progression)

or

a \$0.75 increase taking effect in 2006 followed by a \$0.50 increase, followed by a \$0.50 increase, and ending with a \$0.75 increase, by the end of 2008, if economic conditions permit ('double spiked' progression)

or

a \$10.75 increase taking effect in March 2006, followed by a \$1.00 increase to take effect in March 2007, and ending with a \$0.75 increase taking effect in March 2008 ('bell-shaped curve' progression)

- 5 **agree** that the above paths should be subject to assessment in future minimum wage reviews in light of prevailing economic conditions

Options for the 2006 adjustment

- 6 **note** that I consider an increase in the minimum wage in 2006 to maintain relativity to average wages (\$9.83 per hour) will preserve the real value of the minimum wage and could be made with confidence in the current economic and labour market conditions. Such an increase will provide benefits to an estimated 28,400 recipients with minimal likelihood of constraining job growth
- 7 **note** that I consider that an increase in the minimum wage in 2006 above the rate needed to maintain relativity to the average wage (e.g. a \$0.75 increase on the current rate) could be made with confidence in the current economic and labour market conditions, and to reflect a stronger view of the contribution of the minimum wage to its objectives and to communicate a stronger message about reaching the government's aspirational goal for the minimum wage. The current labour market and economic conditions are likely to be able to accommodate a larger increase now than in the coming years, if there is an economic downturn or the economy softens. Increases above \$1.00 would, however, involve increased likelihood of constraining potential job growth
- 8 **note** that women, younger workers, Maori, Pacific peoples, disabled people, recent migrants, the low skilled and people with non-English speaking backgrounds are over-represented amongst the low paid workforce, and that they would be expected to benefit from any resulting wage increases
- 9 **agree** that the adult minimum wage rate for 2006 should be:
- either**
- \$9.50 per hour or \$380 for a forty hour week (option 1 - status quo – Business New Zealand, Federated Farmers, Hospitality Association and SBAG position)
- or**
- \$9.83 per hour or \$393 for a forty hour week (option 2A - same increase as the increase in average hourly earnings between June 2004 and June 2005, Retailers Association position)
- or**
- \$10.00 per hour or \$400 for a forty hour week (option 2B)
- or**
- \$10.13 per hour or \$405 for a forty hour week (option 3A)

or

\$10.25 per hour or \$410 for a forty hour week (option 3B)

or

\$10.50 per hour or \$420 for a forty hour week (option 3C)

or

\$12.00 per hour or \$480 for a forty hour week (option 4 - NZCTU position)

- 10 **agree** that the youth minimum wage rate should continue to apply for 16 and 17 year old employees and remain at 80% of the adult rate for 2006
- 11 **agree** that the training minimum wage rate should remain at 80% of the adult rate for 2006

Future minimum wage reviews to the end of 2008

- 12 **note** that the ILO Convention 26 “Minimum Wage Fixing Machinery”, Article 3 requires that consultation with employers and employees takes place in determining minimum wage rates as part of wage fixing machinery
- 13 **agree** that reviews to 2008 continue to assess minimum wage rates against the government’s agreed objectives and goals for the minimum wage (including an assessment against corresponding benchmarks, for example relativity with the average wage)
- 14 **note** that the Department of Labour is undertaking work to:
- identify leading indicators of employment, and that leading indicators could be used in future reviews to provide disaggregated information around economic conditions
 - review the relativities between adult, youth and trainee minimum wages, to provide more advice on this matter in the 2006 minimum wage review paper
- 15 **note** that the issue of minimum wages for young people under the age of 16 years will be reconsidered once government has reached a decision around ratification of ILO Convention 138 (minimum age for employment)
- 16 **note** that the Department of Labour will work with the Ministry of Social Development to provide firmer modelling in the 2006 review around the impact of minimum wage increases on Working for Families recipients following the implementation of Working for Families phase 2
- 17 **note** that the Department of Labour is to undertake work to evaluate minimum wage increases, including:
- case studies of adjustment to the change of particular firms in the sectors where most minimum wage workers are to be found
 - an HLFS time series econometric study of employment rates of potentially vulnerable groups (women, youth, Maori and Pacific peoples, recent

migrants, etc.) along the lines of previous Chapple (1997) and Maloney (1995), work which is now outdated

examination of PAYE/LEED data to explore pay changes

examination of 'flow on' effects up the earnings distribution by looking at changes in the Income Supplement of the HLFS earnings distribution

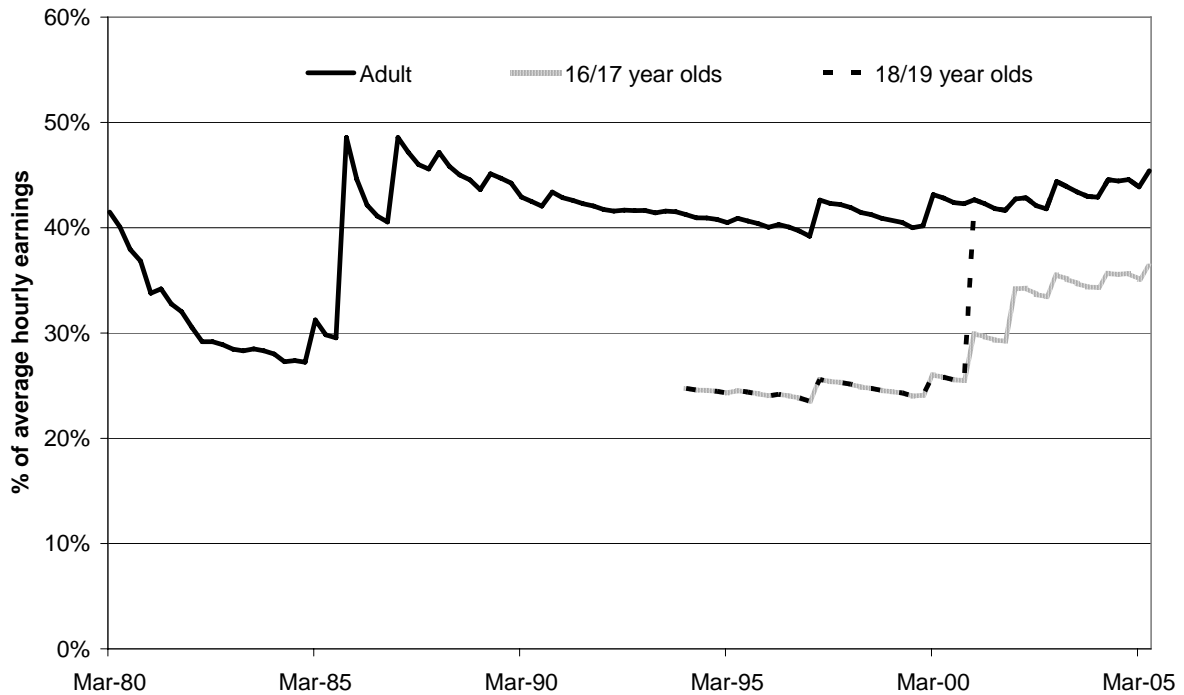
further work to monitor and explain the high levels of non-compliance with the minimum wage that are reported in the income supplement to the HLFS, with a view to more advice on this matter in the Department of Labour's 2006 minimum wage review report.

Hon Ruth Dyson
Minister of Labour

RECENT CHANGES IN THE MINIMUM WAGE

1 Minimum wages have grown steadily as a percentage of average earnings since 2000. The following figure shows how minimum wages have tracked over time as a proportion of average earnings measured using the QES.⁸

Figure 1: Minimum wages as a proportion of average earnings⁹



⁸ Because QES average wages are higher than those in the NZIS these percentages will not match comparison with the NZIS average outlined in Figure 1.

⁹ The administration of the Quarterly Employment Survey changed from the Department of Labour to Statistics NZ in February 1989 resulting in slight changes in coverage. Youth minimum wages first came into effect in March 1994.

2 The following table sets out changes in minimum wage rates since 1999.

Table 1: Recent changes in minimum wage rates

	Key changes in minimum wages	Minimum Wage Rates		
		% increase % mean average (+ % median) wages		
		Adult	18/19 year olds	16/17 year olds
1997-1999	No changes.	\$7.00 42.6(56.0)	\$4.20	\$4.20
2000	All minimum wages increased to restore relative to average wage in 1997, when minimum wages were last increased.	\$7.55 7.9% 43.0(56.3)	\$4.55 8.3%	\$4.55 8.3% ¹⁰
2001	Adult wages raised by increase in average wages. Age of eligibility for adult minimum lowered from 20 to 18 years. Youth minimum wage rate raised from 60% of adult to 70% (target of 80% announced for next year).	\$7.70 2.0% 42.5(56.8)	\$7.70 69.2%	\$5.40 18.7%
2002	Adult minimum wage rate raised by increase in average wages. Youth minimum wage rate rose from 70% to 80% of adult rate.	\$8.00 3.9% 42.6(57.1)	\$8.00 3.9%	\$6.40 18.5%
2003	All minimum wages increased by 6.3% (\$0.50 increase for adult), higher than average wage increase of 2.7%. Training minimum wage set at youth rate comes into effect from 1 July 2003.	\$8.50 6.3% 43.8(56.7)	\$8.50 6.3%	\$6.80 6.3%
2004	All minimum wages increased by 5.9% (\$0.50 increase for adult), higher than average wage increase of 3.7%.	\$9.00 5.9% 44.4(58.7)	\$9.00 5.9%	\$7.20 5.9%
2005	The adult rate increased by 5.6% (\$0.50 increase) and by 5.5% for youth rate and for the trainee rate (\$0.40 increase for both rates), adult increase greater than average wage increase of 2.7%.	\$9.50 5.6% 45.3(59.0)	\$9.50 5.6%	\$7.60 5.5%

¹⁰ This number differs from 7.9% due to rounding of youth rate to nearest 5 cents.

APPENDIX B

POTENTIAL IMPACTS OF INCREASING THE MINIMUM WAGE

Who benefits?

- 1 The benefits of minimum wage increases are likely to be felt most strongly among women, younger workers, Maori, Pacific peoples, people with disabilities, recent migrants, the low skilled and people with non-English speaking backgrounds. It must also be said, however, that these groups would be the first to experience any negative impacts that could result from a minimum wage increase, particularly if there was a big increase (for example reduced hours worked, or substitution of some groups of workers by other).¹¹ The groups listed are over-represented in earners on low wages. For example, 68% of workers paid between \$9.50 and \$10.50 per hour (6.5% of all workers) are female (c.f. 47% of all wage and salary earners), 12% are Maori (c.f. 10%), 7% are Pacific (c.f. 5%) and 39% are 18 to 24 years old (c.f. 15%).
- 2 Of this group, many work part-time (approximately 50% of low wage employees work part time (less than 30 hours per week) compared to 20% of higher paid workers). Because of this, any increase in weekly incomes will reflect the fewer hours worked by low wage workers and will reduce the absolute increase in income arising from minimum wage increases.¹²
- 3 Many of the group who are likely to benefit from minimum wage increases live in low income working households. For example, the Department estimates that approximately 75% of low wage earners (between \$9.50 and \$10.50 per hour) live in households below the median gross equivalised household income for working households of \$660 per week.¹³
- 4 Of those receiving the youth minimum wage, the beneficiaries are likely to be youth who are working while still at school (75% of 16 and 17 year olds are still at school or in some form of study) and retail workers (64% of 16 and 17 year olds are employed in the retail industry). For youth, the increase in weekly income from an increase in the minimum wage is likely to be small, because the majority of young people work short hours (32% work less than 10 hours per week, 33% work between 10 and 20 hours and 20% are working a fulltime 40-50 hour per week job).
- 5 As the youth minimum wage increases, the Department of Labour considers that it will be important to monitor the potential substitution of workers aged 16 -17 years with workers aged 15 years (and continue monitoring and investigating levels of reported non-compliance).

More detail on impacts for women and the gender pay equity

- 6 For some groups of women, an increase in the minimum wage is the only direct lever government has to ensure an adequate earned income – they may be in fairly un-unionised areas and/or have limited market power, or may be in jobs in which pay

¹¹ See Appendix D for a breakdown of the subgroups affected by the options.

¹² This is based on hours worked by those earning between \$9.50 and \$10.50.

¹³ These categories are based on equivalised income using Jensen and account for differences in numbers of adults and children in a household (e.g. a couple without children is effectively “richer” than a couple with children on the same level of income). A single individual has the base reference value of 1, and larger household groupings involve discounting actual gross income e.g. the adjustment value for a 2 adult 2 child family is 2.163. The median gross equivalised household income was calculated using the 2005 New Zealand Income Survey and includes income information for individuals aged 15 years and over.

equity strategies have little effect. The objectives sought through the minimum wage of improving levels of fairness and protection are particularly relevant for these groups of more vulnerable women.

- 7 Analysis of the June 2005 HLFS IS suggest that:
- a raising the minimum wage can make a small contribution towards reducing the gender pay gap (see below)
 - b more women than men report non-compliance with minimum wage rates (2.02% c.f. 1.33%)
 - c most working women are in jobs that pay over \$10.50 an hour, but women are more than twice as likely as men to be in low paid jobs (under \$10.50 an hour)
 - d women are employed in low paid jobs across all sectors rather than being concentrated in low paid sectors (except for young women) – although there is some ‘clumping’ in particular sectors
 - e most women are in full time employment (30 hours and more a week), but women are more likely than men to work part time (less than 30 hours a week), and are more likely than men to work part time for low wages
 - f Maori and Pacific women, and women of ‘other’ ethnicities are over-represented amongst part time low waged women.
- 8 Increasing the minimum wage can make a small contribution to reducing the gender pay gap. This is because more women than men will have their wages increased as a result of an increase in the minimum wage (74% of minimum wage earners recorded in the June 2005 HLFS IS are women). For example, an increase in the minimum wage from \$9.50 to \$10.50 will improve the gender pay ratio by three tenths of a percentage point (0.3) to 82.1%.¹⁴
- 9 The Department considers that other policies that assist women into higher paid jobs in all sectors (e.g. childcare assistance, work life balance, policies to improve opportunities to acquire skills or to up-skill, or to train) will be more effective overall in reducing the gender pay gap than raising the minimum wage. This does not detract from the impact that increases in the minimum wage may have for improving the incomes of the vulnerable groups of women described in the paragraph opening this section.

The impacts of minimum wage increases on sectors and firms

Sectors

- 10 Some sectors will be impacted on more than others because they employ relatively large numbers of minimum wage workers and/or their wage bands are lower and

¹⁴ The NZ Income Survey for the June 2005 quarter (Statistics New Zealand) shows that pay for male full time employees went up approximately 6.3% since the June 2004 quarter, compared with 3.2% for women. The rates for male part-time employees increased by 8%, compared to 2.8% for women. Overall, this means that the gender pay gap has increased – with women earning 82% on average of what men do, as compared to 85% in 2004. This increased gap is largely explained by increased hourly earnings in male-dominated occupations, for example, agricultural and fisheries workers, trades workers, and plant and machine operators and assemblers.

relatively narrow. In these terms, the sectors most likely to be affected are agriculture and related services, retail, accommodation & catering, community services and textile and clothing. These sectors can expect higher than average increases in their wage bill when minimum wage increases are implemented.

- 11 While we cannot be sure how minimum wage increases in recent years have affected low pay sectors, we do know that in general, these sectors are growing at the same average rate as other sectors in the economy (with the exception of business services which is growing at much higher rates as it includes high growth pockets, and the textile & manufacturing sector which is growing at much lower rate and is in a long term structural decline). Experiences overseas suggest that the effects of adjustment to minimum wages may vary across these sectors, ranging from reduced hours during off-peak times to substitution towards qualified staff, increased labour productivity and increased output prices. (The Department of Labour is proposing to research the range of responses made to minimum wage increases by New Zealand employers as part of an evaluation strategy, see below).
- 12 Overall, for small and medium sized enterprises (SMEs, which employ fewer than 19 people) employment growth is faster than for large firms. SMEs have recorded lower employment growth than for large firms in some low pay sectors, however, including in the food processing sector and the food and other retailing sector. The Department of Labour notes that SMEs in some low pay sectors are more vulnerable to minimum wage increases than large firms.
- 13 There are also a number of state sector employees (and contractors) that earn wages of \$12 per hour or less, particularly in the public health and compulsory education sectors. Future increases in the minimum wage are therefore likely to have direct (and possibly also indirect or 'flow-on') costs for some state sector employers. These costs and the likelihood that organisations will seek additional funding to compensate for them, will be higher for larger movements towards the minimum wage goal of \$12 per hour earlier in the 4 year period.

Firms

- 14 Assessing the impacts of increases to the minimum wage on firms involves trying to isolate the nature of the employment impacts due to minimum wages from other employment changes occurring in the economy. It is difficult to do this with the level of certainty that would be preferable in a review of this type. Submitters' views on the impacts of increases to the minimum wage on firm behaviour vary according to whether they represent employer or employee perspectives, but they are nevertheless firmly held by the different groups.
- 15 Firms may invest in the skill development of low paid workers (and other ways of increasing firm productivity) to offset additional wage costs in anticipation of an increase in minimum wages to \$12 an hour.
- 16 The following section sets out themes common to submissions on the review made by employer groups.

Impacts on employers

- 17 Business submitters comment that raising minimum wages increases wage costs to employers. These costs may be passed onto consumers of goods and services that low wage workers produce, with resulting inflationary pressures. Alternatively they

may result in negative impacts on employment levels (see below) and/or reduced production and/or reduced profits for businesses.

- 18 Business submitters also comment that there may be indirect impacts on workers paid above the minimum wage ('flow-on' effects) as these workers bargain to retain their wage relativity with minimum wage workers. It is likely that flow-on effects would particularly affect small firms (as minimum wage changes are most likely to affect these firms and because of a generally narrow range of wages paid within small firms).
- 19 The Department of Labour notes that there is some evidence of flow-on effects, but that there is little evidence of the extent of these effects. Further research into wage profiles within firms and the flow on effects of minimum wages are required to accurately assess this effect. The Department is proposing to do some exploratory work in this area as part of its evaluation strategy (see below).
- 20 Submitters point out that these potential costs will be in addition to other employment related costs imposed by government in recent years, such as the Holidays Act requirement to pay time and a half on public holidays and implementation of four weeks' annual leave in 2007. The former cost is particularly likely to affect accommodation and retail sectors.

Impacts on employment and other firm responses to minimum wage increases

- 21 Business submitters argue that increases in the minimum wage (which make minimum wage workers more expensive) may also have effects on the levels of employment for minimum wage earners ("employment effects") such as reduced hours worked, firms dismissing workers (particularly young and/or unskilled workers), reduced hiring by a firm, potential new firms being dissuaded from entering business, or firms becoming unviable and going out of business.
- 22 There is no consistent or robust New Zealand evidence that such employment effects have been experienced over the last four years (which has seen a 23.7% increase in the minimum wage for adults during a period of strong economic growth). Quantitative evidence that exists for youth varies between weak positive effects and very small negative effects (*Hyslop and Stillman, 2004, 2005*). In its recent submission, however, SBAG has reported a perception amongst its members of reduced opportunities for young people in small/medium enterprises within that timeframe.
- 23 The OECD's view of the consensus on employment effects is "that statutory minimum wages at typical OECD levels do not have major negative effects on total employment, but a high minimum wage reduces the employment prospects of disadvantaged groups".¹⁵ The latest report of the UK Low Pay Commission (February 2005) suggests that New Zealand's minimum wage (at June 2004) was slightly higher than average (but still within the 'typical' OECD range) when compared with the minimum wages of other OECD countries.

Assessing Impacts on employment and job growth

- 24 All business submitters comment about a possible reduction in employment levels if minimum wages increase. How we think firms will respond to minimum wage

¹⁵ OECD Economic Survey: New Zealand, 2004, page 127.

changes depends on how we think firms make employment decisions. In most of its analysis the Department of Labour has used a typical neo-classical model of firm decision-making, whereby firms operating in perfectly competitive markets adjust output and inputs, including labour, in response to relative prices, in order to evaluate these claims.

- 25 This modelling approach does not adequately reflect the dynamic nature of employment responses to changes in minimum wages, and, in particular, any investments that employers may make to increase the productivity of low paid workers. With an increase in the minimum wage relative to the average wage, employers will have an increased incentive to invest in the productivity of workers.
- 26 Important relative prices for considering minimum wage impacts are:
- a the relative price of labour to output¹⁶, and
 - b the relative price of minimum wage labour (typically low skilled) to other labour.¹⁷
- 27 Minimum wages have a small effect on average wages because relatively few workers are directly affected (28,400 people would be directly affected by a fifty cents increase, while 103,500 would be affected by a dollar increase). Accordingly minimum wage increases are likely to have a small impact on the relative price of labour to output in the total economy. This impact would be more intense, however, if significant 'flow-on' effects were experienced following a rise in the minimum wage.
- 28 An important consideration for the impact on the demand for low wage workers is how minimum wages change relative to average wages. If minimum wages keep pace with average wages then we would expect to see little change in the relative demand for low wage workers or low wage jobs. We have shown earlier that the minimum wage is currently growing faster than the average wage, and is expected to grow faster still to reach \$12 an hour, and therefore the relative value of low wage workers and low wage jobs is changing.
- 29 The frame of reference used by analysts is important for assessing potential employment impacts. In past reviews the Department of Labour has presented the change as occurring overnight (the difference in employment immediately before and after a change in the minimum wage). However, in practice, over a year the real value of the minimum wage declines relative to the average wage (which increases over the year, while the minimum wage is fixed for the year). Theoretically there would be a reversal of the employment impact (minimum wage workers become cheaper and more attractive to employers). As long as the relative minimum wage remains constant from year to year, it can be argued that there will be no overall change in employment year on year relative to other labour that is paid above the minimum wage. If the reference point is taken as immediately before a change to minimum wages the impacts may appear larger than if the reference point is the same time last year. The Department of Labour considers that the longer (annual) timeframe is more appropriate for assessing the impacts of minimum wage changes.

¹⁶ This variable is important for determining how much labour is used by a firm to produce goods and services (relative to other inputs such as machinery). Indicators for this variable will often be based on average wages relative to producer output prices (often called real product wages).

¹⁷ This determines whether firms use low or higher skilled workers (skill mix) in their workforce (or how a new firm might choose to make its products or services). If the minimum wage accelerates relative to the average wage employers will tend to favour higher skilled workers who become relatively cheaper.

- 30 The Department of Labour intends to work with firms in sectors most likely to be affected by changes in the minimum wage, and to develop case studies to investigate how firms respond in practice to minimum wage increases, as part of its evaluation strategy. This work would enable us to explore the anecdotal evidence (and our understanding of the theory) we have around such responses.
- 31 The Department of Labour considers that when the following two factors are taken into account, a negative effect on employment levels from an increase in the minimum wage of between fifty cents and \$1.00 is unlikely:
- a an annual frame of reference as described above which means that, as long as the relativity between the minimum wage and average wages remains fairly constant from year to year (which is more or less what the trend in NZ is) there should be little negative effects on employment levels relative to labour that is paid the average wage
 - b the slight outpacing of the minimum wage relative to the average wage in recent years has apparently been offset by a growing economy which requires more labour
- 32 It is possible, however, that increases in minimum wages could constrain projected increases in job growth, with larger increases more likely to act as a constrain. This effect becomes more significant for increases of over one dollar an hour.
- 33 The following table sets out estimates of level of job constraint that could result from minimum wage increases.¹⁸ The results show that baseline employment growth, estimated to be around 31,000 in the year to March 2006 could potentially be constrained by about 1,000 jobs if the minimum wage is increased to \$10.25. It is unclear which jobs would be forgone in the economy, but it is likely that these would be low wage jobs. The Department of Labour's planned case studies of firm responses to increases in the minimum wage will give us more insight into this question.

Table 1: Estimated numbers of forgone jobs

	Minimum wage hourly rate	Projected job growth March 2006	Potential level of constraint on job growth *
Number of jobs	Current total no. of jobs is 2,054,000	Projected to increase by 31,000 jobs to 2,086,000 jobs	
Option 1	\$9.50 (status quo)	31,000	0
Option2A	\$9.83	30,800	200
Option 2B	\$10.00	30,700	300
Option 3A	\$10.25	39,900	1,100

¹⁸ Projected job growth figures are from the Department of Labour's recent Labour Market Outlook, (October 2005). Estimates of the constraint on job growth potentially caused by increases in minimum wage rates are derived using the mean of the various wage bands, the numbers of people directly affected in each wage band, and a labour demand elasticity of 0.3.

Option 3B	\$10.50	29,000	2,000
Option 4	\$12	20,100	10,900

*Using a demand elasticity of 0.3.

APPENDIX C

NUMBERS OF PEOPLE AND SUBGROUPS AFFECTED BY OPTIONS

- 1 The tables below provide details on the number of people (by age group) who should receive wage increases as a result of an increase in minimum wage rates (are 'directly affected' by changes in the minimum wage).

Table 1: Impact of minimum wage options - adults (18 years and over)

Option for 2006	Hourly rate	Weekly rate	No. of people who would receive a wage rise and percentage of employees cohort
1	\$9.50	\$380	0
2A	\$9.83	\$393	24,900 (1.6%)
2B	\$10.00	\$400	28,400 (1.8%)
3A	\$10.13	\$405	86,140 (5.6%)
3B	\$10.25	\$408	91,000 (5.7%)
3C	\$10.50	\$420	103,500 (6.5%)
4	\$12.00	\$480	246,600 (15.5%)

Table 2: Impact of minimum wage options - those aged 25 years and over

Option for 2006	Hourly rate	Weekly rate	No. of people who would receive a wage rise and percentage of adult workforce cohort
1	\$9.50	\$380	0
2A	\$9.83	\$393	13,300 (1%)
2B	\$10.00	\$400	16,000 (1.2%)
3A	\$10.13	\$405	49,906 (2.6%)
3B	\$10.25	\$408	53,600 (3.9%)
3C	\$10.50	\$420	63,100 (4.7%)
4	\$12.00	\$480	169,400 (12.5%)

Table 3: Impact of minimum wage option – 20 - 24 years

Option for 2006	Hourly rate	Weekly rate	No. of people who would receive a wage rise and percentage of adult workforce
1	\$9.50	\$380	0
2A	\$9.83	\$393	4,400 (2.4%)
2B	\$10.00	\$400	5,200 (2,8%)
3A	\$10.13	\$405	21,223 (12.1%)
3B	\$10.25	\$408	21,600 (11.8%)
3C	\$10.50	\$420	24,000 (13.1%)
4	\$12.00	\$480	49,200 (26.9%)

Table 4: Impact of minimum wage option – 18 - 19 years

Option for 2006	Hourly rate	Weekly rate	No. of people who would receive a wage rise and percentage of adult workforce cohort
1	\$9.50	\$380	0
2A	\$9.83	\$393	7,200 (11.7%)
2B	\$10.00	\$400	7,200 (11.7%)
3A	\$10.13	\$405	15,011 (30.8%)
3B	\$10.25	\$408	15,900 (25.8%)
3C	\$10.50	\$420	16,400 (26.7%)
4	\$12.00	\$480	28,000 (45.5%)

Table 5: Impact of Youth (16 and 17 years) Minimum Wage Options

Option for 2006	Hourly rate	Weekly rate	No. of people who would receive a wage rise and percentage of youth workforce
1	\$7.60	\$304	0
2A	\$7.86	\$315	3,500 (5.8%)
2B	\$8.00	\$320	3,700 (6.3%)
3A	\$8.10	\$324	9,420 (18.6%)
3B	\$8.20	\$328	10,000 (16.9%)
3C	\$8.40	\$336	11,000 (18.7%)
4	\$9.60	\$384	24,700 (41.8%)

Subgroups affected

- 2 The following provides further information on the extent to which various sub-groups are affected by minimum wage changes.

Table 6: Sub-groups affected by analysed option*

Option for Adult Minimum Wage (per week) % increase (% average ¹⁹)	No of adults directly affected (% total) Subgroups (% of wage group)		Youth Minimum Wage (80% of Adult)	No of youth directly affected (% total)
Reported below \$9.50	Total (3.4%)	54,800	<\$7.60	8,500 (14.4%)
	Female (58%)	31,600		
	Maori (12%)	6,600		
	Pacific (4%)	1,900		
Option 1 - \$9.50 (\$380) No increase (48.0%)			\$7.60 (\$304)	
Option 2A - \$9.83 (\$393)	Total (1.6%)	24,900	\$7.86 (\$315)	3,500 (5.8%)
3.5% (49.7%)	Female (2%)	17,000		
	Maori (3%)	3,700		
	Pacific (2%)	1,600		
Option 2B - \$10.00 (\$400)	Total (1.8%)	28,400	\$8.00 (\$320)	3,700 (6.3%)
5.2% (50.5%)	Female (3%)	19,900		
	Maori (3%)	4,200		
	Pacific (6%) ²⁰	1,600		
Option 3A - \$10.13 (\$405)	Total (5%)	86,140	\$8.10 (\$324)	
	Female (8%)	57,643		
	Maori (7%)	9,644		
	Pacific (9%)	6,288		
Option 3B - \$10.25 (\$410)	Total (5.9%)	91,000	\$8.20 (\$326)	10,000 (16.9%)
7.3% (51.5%)	Female (8%)	61,000		
	Maori (7%)	10,246		
	Pacific (9%)	6,713		
Option 3C - \$10.50 (\$420)	Total (6.5%)	103,500	\$8.40 (\$338)	11,000 (18.7%)
10.6% (53.1%)	Female (9%)	60,961		
	Maori (12%)	12,000		
	Pacific (11%)	7,600		
Option 4 - \$12.00 (\$480)	Total (15.5%)	246,600	\$9.60 (\$384)	24,700 (41.8%)

¹⁹ The average hourly wage rate is calculated from reported earnings for all individuals and includes those earning less than the minimum wage. The average hourly wage rate for adults (aged 18 and over) is \$19.79 and \$9.56 for young people (aged 16 to 17 years).

²⁰ There are no Pacific adults in the Income Survey with an hourly wage rate between \$9.83 and (less than) \$10.

26.3% (60.6%)				
	Female (22%)	162,200		
	Maori (21%)	31,500		
	Pacific (20%)	21,500		
Total	Total (100%)	1,593,900	Total	59,100 (100%)
(includes those reporting below minimum wage)	Female (47%)	750,100		
	Maori (10%)	154,300		
	Pacific (5%)	74,400		

* (this table excludes the numbers of people who report earnings under the minimum wage)

Population counts have been rounded to the nearest hundred.

Source: 2005 New Zealand Income Survey, Statistics New Zealand;

- 3 The table over the page provides more detail on the numbers of people who are directly affected by a minimum wage increase, using HLFS Income Supplement data for June 2005 and mid-point, mean and median points of the wage band options as reference points. The table also provides hypothetical estimates of the constraint on job growth that could result from an increase in the minimum wage, using low (0.04), medium (0.3) and high (0.5) labour demand elasticities.

Table 7: Number of people directly affected by changes in the minimum wage

Impact on Employment Growth							
18+				16-17			
A: 18+ based on midpoint of wage band							
				0.04	0.30	0.50	
				low elas	med elas	hi elas	
	midpoi	no of	workers	negative	negative	negative	
	nt	workers in	affected	impact on	impact on	impact on	
	wage	band		job growth	job growth	job growth	
	for						
	band						
9.50	9.50	54,832	0	0	0	0	
9.50	9.83	24,907	24,900	0	100	200	
9.83	10.00	3,452	28,400	0	300	400	
10.00	10.20	65,283	93,600	100	600	1,100	
10.20	10.50	9,833	103,500	200	1,500	2,500	
10.50	11.00	40,945	144,400	400	3,400	5,600	
11.00	12.00	102,183	246,600	1,200	8,900	14,900	
12.00	14.00	13.00	210,565	457,200	3,700	27,600	46,000
B: 16-17 based on midpoint of wage band							
				0.10	0.30	0.50	
				low elas	med elas	hi elas	
	midpoi	no of	workers	negative	negative	negative	
	nt	workers in	affected	impact on	impact on	impact on	
	wage	band		job growth	job growth	job growth	
	for						
	band						
7.60	7.60	8,523	0	0	0	0	
7.60	7.88	3,451	3,500	0	0	0	
7.88	8.00	271	3,700	0	0	100	
8.00	8.16	6,257	10,000	0	100	100	
8.16	8.40	1,070	11,000	100	200	300	
8.40	8.80	4,232	15,300	100	400	600	
8.80	9.60	9,424	24,700	300	900	1,600	
9.60	11.20	10.40	16,816	41,500	900	2,700	4,500
C: 18+ based on mean of wage band							
				0.04	0.30	0.50	
				low elas	med elas	hi elas	
	Mean	no of	workers	negative	negative	negative	
	wage	workers in	affected	impact on	impact on	impact on	
	for	band		job growth	job growth	job growth	
	band						
9.50	7.37	54,832	0	0	0	0	
9.50	9.83	24,907	24,900	0	200	300	
9.83	10.00	3,452	28,400	0	300	600	
10.00	10.20	65,283	93,600	100	900	1,400	
10.20	10.50	9,833	103,500	200	1,700	2,900	
10.50	11.00	40,945	144,400	500	3,700	6,200	
11.00	12.00	11.33	102,183	246,600	1,300	9,800	16,400
12.00	14.00	12.77	210,565	457,200	4,000	29,900	49,800
D: 16-17 based on mean of wage band							
				0.10	0.30	0.50	
				low elas	med elas	hi elas	
	Mean	no of	workers	negative	negative	negative	
	wage	workers in	affected	impact on	impact on	impact on	
	for	band		job growth	job growth	job growth	
	band						
7.60	6.80	8,523	0	0	0	0	
7.60	7.88	3,451	3,500	0	0	0	
7.88	8.00	271	3,700	0	0	100	
8.00	8.16	6,257	10,000	0	100	200	
8.16	8.40	1,070	11,000	100	200	300	
8.40	8.80	4,232	15,300	100	400	700	
8.80	9.60	9,424	24,700	300	1,000	1,600	
9.60	11.20	10.23	16,816	41,500	900	2,800	4,700
E: 18+ based on median of wage band							
				0.04	0.30	0.50	
				low elas	med elas	hi elas	
	Media	no of	workers	negative	negative	negative	
	n	workers in	affected	impact on	impact on	impact on	
	wage	band		job growth	job growth	job growth	
	for						
	band						
9.50	8.20	54,832	0	0	0	0	
9.50	9.83	24,907	24,900	0	300	400	
9.83	10.00	3,452	28,400	100	400	700	
10.00	10.20	65,283	93,600	100	1,000	1,600	
10.20	10.50	9,833	103,500	200	1,900	3,100	
10.50	11.00	40,945	144,400	500	3,900	6,600	
11.00	12.00	11.28	102,183	246,600	1,400	10,200	17,000
F: 16-17 based on median of wage band							
				0.10	0.30	0.50	
				low elas	med elas	hi elas	
	Media	no of	workers	negative	negative	negative	
	n	workers in	affected	impact on	impact on	impact on	
	wage	band		job growth	job growth	job growth	
	for						
	band						
7.60	7.20	8,523	0	0	0	0	
7.60	7.88	3,451	3,500	0	0	100	
7.88	8.00	271	3,700	0	100	100	
8.00	8.16	6,257	10,000	0	100	200	
8.16	8.40	1,070	11,000	100	200	400	
8.40	8.80	4,232	15,300	100	400	700	
8.80	9.60	9,424	24,700	300	1,000	1,600	

Source: Income Supplement of HLFs and Department of Labour calculations

APPENDIX D

SUMMARY OF SUBMISSIONS

- 1 Submissions were received from the New Zealand Council of Trade Unions, the Youth Union Movement, Business New Zealand, Federated Farmers, Small Business Advisory Group, the National Association of Retail Grocers and Supermarkets of New Zealand, the New Zealand Association of Retailers, the Small Business Advisory Group, the Mayors Taskforce for Jobs, the Hospitality Association of New Zealand, and the National Advisory Council on the Employment of Women (NACEW).
- 2 The main points made in each submission are outlined in the table below

<p>Federated Farmers</p>	<p>Federated Farmers broadly agrees with the government's goals for the minimum wage and accepts the need for a statutory requirement to protect the most vulnerable.</p> <p>Substantially increasing minimum wages is neither a credible nor sustainable policy tool to achieve higher wages. An artificial, centrally imposed intervention can never reflect either competitiveness or productivity but will squeeze already tight business margins and discourage employment and increase inflationary pressures.</p> <p>Two impacts of recent increases – harmed the employment and training prospects for youth, and led to increased costs for businesses, eroding competitiveness with no increases in productivity.</p> <p>There should be no increase in the minimum wage. Government policies should focus on improving skills, improving incentives to work, improving the business environment, and so lead to better competition and productivity, and so to higher wages.</p> <p>The union movement's focus on across-the-board wage increases (including minimum wage increases) is inconsistent with its support for increasing productivity.</p> <p>Federated Farmers had input into and endorses the submission from Business NZ.</p> <p>The government's social objectives around the minimum wage would be better delivered through social welfare and taxation policies.</p> <p>An increase to \$12 an hour would have wide impacts across the labour market, especially at a time when many businesses are facing cost pressures.</p>
<p>Mayors Taskforce for Jobs</p>	<p>Notes that recent minimum wage increases have not resulted in constraints or fewer jobs for young people.</p> <p>Lifting the minimum wage could lead to investment in skill training and increases in productivity.</p> <p>Minimum wage protection is necessary for young people, to encourage employers to invest in skill development and trade and to avoid increasing wage disparities between Australia and NZ.</p> <p>2004 concerns around skills and labour shortages remain.</p> <p>Lifting minimum wages will help address skills and labour shortages, industries' ability to attract and retain young people, and staff retention.</p>

Business New Zealand	<p>Recommends that:</p> <p>There be no further increases in either the youth or adult minimum wage rates, or extensions in coverage.</p> <p>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 people is removed</p> <p>The Government should consider tax cuts rather than increases in minimum wage rates as a more effective way of increasing real wages for relatively low paid workers</p> <p>Statistics New Zealand is provided with funding for the development of a Cost of Living indices (or real disposable income indices), as a guide for increases to the minimum wage.</p> <p>Also:</p> <p>Government focus should be on increased access to training and employment to achieve higher productivity and real earnings over time.</p> <p>Legislatively set minimum wages create employment obstacles for the young and unskilled.</p> <p>Concerned about inflationary pressures due to flow-on effects.</p> <p>Youth minimum wage has a distortionary effect on the labour market.</p> <p>Business NZ provides survey information that shows that 65% of employers are generally prepared to accept increases at about the level of the rate of inflation only. Around 20% were prepared to accept an increase to \$12 an hour for adults.</p> <p>Economic indicators suggest increases may not continue to be sustainable, especially for the Manufacturing, Accommodation, cafés and restaurants, Retail Trades, and Construction industries. Recent increases that have been greater than the rate of inflation may have negative impacts on employment in these industries when economic growth slows, especially for young/unskilled.</p>
Small Business Advisory Group (SBAG)	<p>Notes that minimum wage increases are most likely to affect small firms.</p> <p>SBAG prefers that the minimum wage remain at its current level unless there was sufficient evidence to justify an increase. If there was such evidence, SBAG recommended the minimum wage increase in-line with inflation.</p> <p>SBAG believe the case for an increase from present rates is not strong, and should stay at present rates for at least next 12 months, and also perceives SMEs to be struggling with impacts of workers above minimum wage seeking to retain wage relativities with minimum wage workers.</p> <p>Youth minimum wage should retain existing relativity with adult rate.</p> <p>SBAG members perceive a reduction in work and work opportunities in SMEs for younger people as a result of increases to youth rate.</p> <p>SBAG considers that significant econometric modelling should be undertaken before increases [to \$12 an hour] are contemplated.</p>
National Association of	<p>Recommends that there is no increase in minimum wages and that there is an increased focus on youth training.</p>

<p>Retail Grocers and Supermarkets of New Zealand (NARGON)</p>	<p>Grocery retail is a fast growing sector and large employer, particularly of casual, part-time and young workers.</p> <p>Grocery is a low-margin industry selling essential foodstuffs in which increased wages directly affect business viability, hence service and employment levels.</p> <p>Minimum wages are important in setting wage rates and any increases may have flow on effects (wage costs – via relativity) and hence inflationary effects.</p> <p>Costs of training to lift the productivity of young and unskilled workers are significant. NARGON outlines anecdotal evidence from members that opportunities for 18 and 19 year olds have been adversely affected by increasing their minimum wage to the adult rate (as employers substitute older people for 18 and 19 year olds).</p> <p>'After-school' workers may lose opportunities for skill development and work, while they receive message that further training/education is unwarranted.</p> <p>Significant increases only sustainable if based on increases in productivity. Without this it conflicts with promoting productivity and economic growth.</p>
<p>Retailers Association</p>	<p>Concerned that minimum wages are becoming a barrier to employment in the retail industry and the development of industry training programmes.</p> <p>A modest increase in minimum wage in line with average wage growth is fair.</p> <p>Businesses find it hard to absorb increases that are higher than general wage increases.</p> <p>Employers may delay or abandon their recruitment decisions to focus on experienced staff only.</p> <p>Previous increases in youth rate had flow-on effects for other workers to maintain relativities, and further increases would probably have flow-on effects through the whole hierarchy.</p> <p>Recommend no increase in training minimum rates. Association has seen an increase in numbers training and consider training minimum wage has contributed to this.</p> <p>The artificial relativity between the youth and adult rates is neither rational nor sustainable and alternative solutions should be explored, e.g. training incentives, tax rebates.</p> <p>Movement to \$12 an hour would cost the industry an additional \$760m p.a. Would lead to increased costs for consumers, loss in job opportunities (especially part-time work) and unnecessary economic impacts, e.g. inflationary pressures.</p> <p>Recommends that the youth minimum wage is not increased, and its relativity to the adult rate is dropped.</p> <p>Recommends increase to the adult rate no greater than general wage increase, and robust economic consideration is applied to subsequent increases.</p> <p>These two recommendations would deliver on government's stated minimum wage objectives.</p>

Youth Union Movement	<p>The Youth Union Movement calls for the elimination of discrimination on the grounds of age in the minimum wage provisions.</p> <p>Recommends that the minimum wage for those aged 16-17 years should be immediately lifted to the adult rate, and that a minimum wage at the adult rate should be instituted for those under 16.</p>
<p>New Zealand Council of Trade Unions</p> <p>(NZCTU)</p>	<p>The NZCTU recommends that the minimum wage should initially be raised to \$12.00 per hour or \$480 per week. This is equivalent to 56.7% of the average ordinary time hourly rate.</p> <p>Supports an indexation of the minimum wage to the average wage but only once there is a commitment to lift the ratio to two-thirds.</p> <p>For those aged below 18 years, the NZCTU submits that the lower rate based on age should be removed. Support the continuation of an exemption for trainees but submits that this rate should be at 90% of the minimum wage which would be \$10.80 an hour.</p> <p>Supports the minimum wage applying regardless of age and this includes (with some exceptions) those aged under 16 years of age.</p> <p>The 2005 Minimum Wage Review needs to take account of the recommendations of the Pay and Employment Equity Taskforce. An increase in the minimum wage can make a small but important contribution to reducing the gender pay gap.</p> <p>Steps need to be taken to re-establish a reliable database on low pay, so that the impacts of the minimum wage on the lower rates in the pay structure, and on young workers, can be considerations in subsequent reviews.</p> <p>Resources allocated to policing the minimum must be increased, the inspectorate should commence inspection on its own motion, and the inspectorate should instigate a policy of prosecuting employers who breach the minimum wage.</p> <p>The government should amend the law so that in the event of an employer being found to be paying less than the minimum wage, the penalty is twice the amount of underpayment, payable to the victim of the underpayment (the worker).</p>
	<p>The submission reviews local and international evidence on the impact of the minimum wage on employment levels and concludes that at least within the range of adjustment being sought here, the case for raising the minimum can be judged on equity grounds, since it is not likely to have a detrimental effect on employment.</p> <p>The Government must acknowledge the devastating effect on workers of the removal of the award system. The Government needs to properly address the plight of low wage workers by ensuring that the minimum wage is significantly increased. This may require a Low Pay Commission. But, the crucial issue is to build on the acceptance by most (even in business) that our pay rates are too low by ensuring that there is a concerted range of measures that can lift pay rates.</p> <p>The NZCTU notes the inclusion in the Confidence and Supply Agreement with NZ First and the Co-operation Agreement with the Green Party that the Government will “continue the practice of annually</p>

<p>NZCTU cont'd</p>	<p>increasing the minimum wage, with a view to it being set at \$12.00 per hour by the end of 2008 if economic conditions" permit.</p> <p>The NZCTU view is to welcome the commitment to an initial target of \$12.00 an hour. However, the NZCTU submits that there should be an immediate increase to \$12.00 an hour and the issue of removing the youth rate also needs to be addressed. The NZCTU also notes that the Government target of \$12.00 an hour also is subject to the qualification of whether economic circumstances would permit such an increase. The NZCTU anticipates that some employer groups will continue to argue that economic conditions would not allow such a move. In addition, they will argue that a significant increase in the minimum wage at the same time as the fourth week's annual leave will be too great a burden. The NZCTU submits that the government needs to be resolute in the face of such arguments.</p> <p>This means that it is imperative that the Government takes the initiative in this review for a significant increase rather than wait until 2007 or 2008.</p>
<p>National Advisory Council on the Employment of Women NACEW</p>	<p>It is still the view of NACEW that, on balance, moderate increases in the minimum wage are likely to have a positive effect on the employment experiences of women. The minimum wage is recognised as one of a range of mechanisms that can increase the likelihood of women receiving equal pay for work of equal value.</p> <p>Cites Pay and Employment Equity Taskforce 2004 finding that there is positive evidence that raising the minimum wage would have a positive effect on closing the gender pay gap.</p> <p>An increase in the minimum wage could stimulate women to increase their labour market participation, as well as helping to address pay and employment equity issues for women.</p> <p>Raising the minimum wage is also likely to have positive, implications for the work-life balance of people on low-incomes and/or in precarious employment.</p> <p>For example, enabling families to better balance work and caring responsibilities by raising income (e.g. to afford childcare) will benefit business and labour force participation.</p> <p>Calls for better monitoring and evaluation of income distribution by gender and ethnicity, esp. important as population is ageing.</p> <p>Calls for more research into impacts of minimum wage increases on SMEs, and on productivity.</p> <p>Calls for research into impacts of moving to \$12 an hour on low-wage earners, businesses (esp. SMEs), productivity and the economy.</p> <p>Asks Minister to note the research NACEW will be doing on the motivations behind the decision-making of people with caring responsibilities and their labour force participation.</p>
<p>The Hospitality Association of New Zealand</p>	<p>The Association supports the submission by Business NZ.</p> <p>Recommends no further increase in youth or adult rates.</p> <p>Further changes to the rates and eligibility for adult and youth rates will severely impact on the ability of the hospitality and tourism industries to</p>

	<p>provide jobs and training opportunities for less skilled workers.</p> <p>The government should focus on increasing training and employment to achieve higher productivity and increased real earnings over time.</p> <p>The minimum wage places additional obstacles on particular workers.</p> <p>When minimum wage rates reach market rates it can have significant negative impact at the micro level on the employment opportunities for young and unskilled workers in industries that pay minimum rates.</p> <p>The industry employs many entry level people. The minimum wage is a benchmark for other wages in the industry; therefore increases in the minimum wage reduce industry profitability, and place businesses/employment levels in the industry at risk.</p> <p>The majority of members are affected by minimum wage changes.</p> <p>Concerned about increased labour costs caused by other workers seeking to maintain wage relativities with minimum wage workers.</p> <p>Minimum wage increases may reduce employers' flexibility to reward higher-performing workers.</p> <p>Inflationary pressures caused by increased wages may lead to higher interest rates and reduced investment and job availability.</p> <p>Training minimum wage deters employers from offering training, and so conflicts with government's objectives around life-long learning, development of a skilled workforce and investment in vocational training.</p> <p>Youth minimum wage could incentivise young people to substitute work for education.</p> <p>A two-fold unemployment effect may occur when labour force participation increases at the same time that job opportunities are reduced.</p> <p>A rise in the minimum wage may compromise job opportunities for beneficiaries through the industry's programme with the Ministry of Social Development.</p>
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Views on achieving \$12 an hour

- 3 Key submitters were invited to provide additional submissions on the government's aspirational goal to reach \$12 an hour for adults by the end of 2008, if economic conditions permit. Three submitters provided additional material on this matter, and their views are summarised below.

NACEW

- 4 NACEW recommend that research is conducted as to the impact of such an adjustment on the gender pay gap, low income earners, business, workplace productivity, and the wider economy. NACEW also recommends that the number, level and timing of increases is signalled early on to employers.

Federated Farmers

- 5 Federated Farmers does not believe economic conditions will sustain a \$2.50 increase over the next three years. The Reserve Bank is clearly concerned about inflationary pressures, and there is a need for tighter monetary policy. Increasing the

minimum wage will squeeze already tight business margins, discourage employment and increase inflationary pressures. Market forces appear to be working in the sector as wages and salaries experienced a large increase between June 2004 and June 2005: there is no need to artificially increase minimum wages. The impact on the agricultural sector would be particularly severe (which is the largest contributor to productivity, exports and sustainable economic growth in New Zealand) – an increase in the minimum wage could reduce the standard of living for all New Zealanders.

NZCTU

- 6 NZCTU's first preference is for an immediate move to \$12 an hour. If the government's view is to move to the goal over three years, then NZCTU supports a significant move being made in 2006, rather than three even moves, or a significant increase being made in 2008. While some businesses may want certainty around the steps, NZCTU values the annual review process, and does not support a decision that supplants the annual review.

Other issues raised in discussion

- 7 The Department of Labour met separately with the New Zealand Council of Trade Unions, the Small Business Advisory Group and Business New Zealand to discuss some of the key issues relating to their submissions. Additional issues raised in these discussions are set out below.
- 8 Business New Zealand continues to support the development of cost of living indices to assist in setting changes to minimum wages (relevant to objective 1). The Business NZ submission is also supported by Federated Farmers. Statistics NZ is preparing a possible budget bid for 2006/07 to develop such indices.
- 9 Business NZ argues that the international cost of labour is zero, and that the government needs to give careful consideration to the potential impacts of raising the minimum wage for vulnerable and disadvantaged workers. These impacts take 10/15 years to work through (and can include the substitution of capital and technology for labour).
- 10 With respect to the youth and the training rates, the NZCTU submit that using age as a proxy for productivity is flawed (and discriminatory), and that, if employers are genuinely investing in training junior staff, it should be done formally (and so warrant a training rate). NZCTU submit that this policy would act as an incentive for employers to invest in industry training.

REGULATORY IMPACT STATEMENT

Statement of the nature and magnitude of the problem and the need for government action

Subsection 5(1) of the Minimum Wage Act 1983 states that "The Minister of Labour shall, in each year ending on the 31st day of December, review any minimum rate prescribed pursuant to section 4 of this Act". The current specified minimum rate for people aged 18 years and over (the "adult" rate) is \$9.50 per hour and for those aged 16 or 17 years (the "youth" rate is 80% of the adult rate, or \$7.60 per hour) therefore need to be reviewed by 31 December 2005.

Minimum wage rates provide a minimum acceptable standard for pay rates, and therefore are particularly relevant to the low paid.

Women, Maori and Pacific Island people and young people are over-represented among minimum wage earners, and would expect to benefit from increases in the minimum wage. Changes in the minimum wage particularly affect the agricultural, accommodation and catering and retail trades sectors, and small and medium enterprises.

The training minimum wage was introduced in July 2003 and allows for a lower minimum wage (at 80% of the adult rate) to be paid if an employee is undertaking training of at least 60 credits annually towards a qualification registered by the National Qualifications Framework.

The minimum wage was last increased on 21 March 2005. Since then, consumer prices have increased by 2.8% and average hourly earnings have increased by 3.5% (for the year to June 2005) resulting in a decrease in the real value of the minimum wage. Benefit rates are indexed to the Consumer Price Index, (and have therefore increased at that rate) so the incentive for some people to work may have reduced. The current unemployment level is 3.4% for the overall population aged 18 years or over (September Quarter 2005).

Statement of the public policy objective(s)

The minimum wage is part of the government's general responsibility to ensure socially acceptable employment standards that are prescribed and enforceable. In addition, there are formal international commitments that establish an explicit obligation on the government to ensure an adequate minimum wage, including under ILO Convention 26 which obliges the government to create minimum wage fixing machinery where "no arrangements exist for the effective regulation of wages...and wages are exceptionally low", and recommends that minimum wages should be set according to the "general level of wages prevailing in the country".

The government's objectives for the minimum wage are:

- A. to ensure that wages paid are no lower than a socially acceptable minimum (fairness). Changes to reflect average wages or inflation are relevant for maintaining this objective.
- B. to offer wage protection to vulnerable workers (protection)

- C. to ensure that incomes of people on low incomes do not deteriorate relative to those of other workers (income distribution)
- D. to increase the incentives to work for people considering work who are not currently in paid employment (work incentives).

The government has also announced an aspirational goal of reaching \$12 an hour (for adults) by the end of 2008, if economic conditions permit. The Minister of Labour will make an announcement about the path to reach the government's goal at the same time as an announcement is made about the outcome of this year's review. However, an identified path will be indicative only, and will be confirmed following further minimum wage reviews, if economic conditions permit. Changes will be announced in advance, however, to allow businesses time to adjust.

Changes would not come into effect until March to allow employers time to adjust to the change. Annual adjustments to reach the government's aspirational goal of \$12 an hour (adult rate) by the end of 2008, if economic conditions permit, will continue to be subject to an annual review.

Statement of feasible options (regulatory and/or non-regulatory) that may constitute viable means for achieving the desired objectives(s) AND Statement of the net benefit of the proposal, including the total regulatory costs (administrative, compliance and economic costs) and benefits (including non-quantifiable benefits) of the proposal, and other feasible options.

Options for the 2006 adjustment (or first step towards the goal of \$12 an hour)

Seven options for the adult minimum wage have been considered. Tables 1 and 2 below indicate total numbers of adults and youth affected by each of the minimum wage options. Minimum wage changes would come into effect on Monday 27 March 2006.

Table 1: Impact of Adult (18 years and over) Minimum Wage

Option for 2006	Hourly rate	Weekly rate	Cumulative no. of people who would receive a wage rise and percentage of employees
1	\$9.50	\$380	0
2A	\$9.83	\$393	24,900 (1.6%)
2B	\$10.00	\$400	28,400 (1.8%)
3A	\$10.13	\$405	86,140 (5.6%)
3B	\$10.25	\$408	91,000 (5.7%)
3C	\$10.50	\$420	103,500 (6.5%)
4	\$12.00	\$480	246,600 (15.5%)

Table 2: Impact of Youth (16 and 17 years) Minimum Wage

Option for 2006	Hourly rate	Weekly rate	Cumulative no. of people who would receive a wage rise and percentage of youth workforce
1	\$7.60	\$304	0

2A	\$7.86	\$315	3,500 (5.8%)
2B	\$8.00	\$320	3,700 (6.3%)
3A	\$8.10	\$324	9,420 (18.6%)
3B	\$8.20	\$328	10,000 (16.9%)
3C	\$8.40	\$336	11,000 (18.7%)
4	\$9.60	\$384	24,700 (41.8%)

Status quo – Option 1: leaving the minimum wage unchanged at \$9.50 (\$7.60 for youth and trainees)

Leaving the minimum wage unchanged would not require any adjustment by employers. However, it would mean that the minimum wage would decrease in real terms, and relative to average wages. There would also be a reduction in the margin between benefit rates (which increase by the rate of inflation each April) and the minimum wage, which may reduce incentives for some people to work. The current minimum wage is 90.4% higher than the unemployment benefit (for a single adult with no supplementary assistance included).

Retaining the existing minimum wage (\$9.50 per hour) will erode the real value of these wages and would not further contribute to the government's objectives for the minimum wage.

Increasing the minimum wage by a relatively small amount (Option 2A by 3.5% to \$9.83, and option 2B by 5.3% to \$10.00)

A small increase equivalent to the increase in average wages (to around \$9.83), and an increase in line with recent annual fifty cent an hour increases (to \$10.00 an hour) would be consistent with the Government's concern that the minimum wage should not lose its value over time. It would also contribute to the fairness and income protection objectives of the minimum wage. An increase of at least the rate of inflation would also preserve the margin between benefit rates and the minimum wage (relevant to the work incentives objective). The slightly larger increase proposed in this option would increase the margin between benefit rates and wages, and also increase the ratio of the minimum wage to the average wage.

An increase in the minimum wage in 2006 to maintain relativity to average wages (\$9.83 per hour) will preserve the real value of the minimum wage and can be made with confidence in the current economic and labour market conditions. It would mean that larger increases would be required in future years to reach the government's aspirational goal of reach \$12 an hour by the end of 2008 (adult rate), if economic conditions permit.

Increasing the minimum wage by a larger amount, either Option 3A by 6.6% or \$10.13, or Option 3B: by 7.9% to \$10.25, Option 3C: by 10.5% to \$10.50, or Option 4: by 26.3% to \$12.00

Those on low incomes could expect larger increases in their earnings as a result of a larger increase in the minimum wage. This would help to narrow the earnings distribution, although it could also create 'flow on' effects for firms as employees further up the earnings distribution seek wage increases to preserve relativities. A larger increase in 2006 would require smaller increases in future years to reach the government's aspirational goal of \$12 an hour (adult rate) by the end of 2008, if economic conditions permit.

A larger increase in the minimum wage could also lead to business seeking to improve the productivity of lower wage workers. Evidence from the UK Low Pay Commission suggests that a significant proportion of businesses adjusted to the minimum wage by seeking to increase productivity of their workers. Firms also responded by exercising tighter control on labour costs (including reducing employment and hours worked), and some 'positive' adjustments such as changing work organisation, increasing investment in training and development, improved quality of service, and increased use of technology.

A rate over \$10 an hour (e.g. \$10.25 or \$10.50 an hour) would exceed the recent trends of fifty cents an hour increases and so would signal a stronger message in 2006 about a commitment to reach the government's aspirational goal. An increase over \$10.50 an hour could also mean a higher risk that the rate of growth of minimum wage jobs would slow, especially if there is a downturn in the economy or a further softening in economic conditions.

Youth and training minimum wage rates for 2006

The recommended option for 2006 is that the youth and training minimum wage rates retain their current relativity with the adult rate (at 80% of the adult rate). Young people report higher levels of non-compliance with the youth minimum wage and a large increase in the youth rate (irrespective of its relativity with the adult rate) may result in a corresponding rise in reported non-compliance for this group.

Overall net impacts of an increase in the minimum wage

Costs

Unless they are readily able to absorb the increased labour costs associated with an increased minimum wage, businesses will need to adjust to a minimum wage increase in some other way. The adjustment needed will be greater the larger the increase in the minimum wage. Those employees who would benefit from an increase in the minimum wage would also be the first to be affected by any costs, for example, through shortened working hours, the substitution of higher for lower skilled workers, delayed employment decisions, reduced non-wage terms and conditions, increased pressure on worker productivity, or reduced training. Sectors most likely to be affected will be agriculture, accommodation and catering, and retail sectors. Small firms are also more likely to be affected than larger firms.

The impact on costs to government is unclear, but likely to be small. There are a number of state sector employees (and contractors) that earn wages of \$12 per hour or less, particularly in the public health and compulsory education sectors. Future increases in the minimum wage are therefore likely to have direct (and possibly also indirect or 'flow-on') costs for some state sector employers. These costs and the likelihood that organisations will seek additional funding to compensate for them, will be higher for larger movements towards the aspirational goal of \$12 per hour.

Benefit payments may increase for people who have their hours of work reduced, but for those who receive wage increases; there may be some offsetting benefit abatement. There will also be a small increase in tax paid by people who receive pay rises. Overall, these factors mean the direct fiscal impacts are likely to be small however, detailed estimates of these costs and off-setting benefits have not been prepared.

If wage increases are contained to those moving up to the new minimum wage, the impact on prices is likely to be small. Businesses who are affected by minimum wage increases have suggested that they may adjust by passing on the cost of wage rises to customers by increases prices.

Compliance costs arising out of any increase in the minimum wage are detailed in the Business Compliance Cost Statement.

Benefits

Any increase in the minimum wage will mean that some low-wage workers will receive wage increases ensuring that their earnings do not deteriorate relative to other workers. There may also be flow-on effects to the wages of some workers above the minimum wage, as they seek to maintain wage relativities. If the margin between wages and benefit rates is increased through a minimum wage increase, the incentive to work relative to remaining on benefit is also increased.

The benefits of minimum wage increases are likely to be felt most strongly among women, younger workers, Maori, Pacific peoples, people with disabilities, recent migrants, the low skilled and people with non-English speaking backgrounds. These groups would, however also be more likely to experience any negative impacts that could result from a minimum wage increase, particularly if there was a big increase (for example, reduced hours worked, or substitution of some groups of workers by others).

Fifty percent of low wage workers work part-time. Because of this, any increase in weekly incomes will reflect the fewer hours worked by low wage workers and will reduce the absolute increase in income arising from minimum wage increases.

For some groups of women, an increase in the minimum wage is the only direct lever the government has to ensure an adequate earned income (they may be non-unionised and/or, have weak bargaining power). Increasing the minimum wage will also play a small role in reducing the gender pay gap. The objectives sought through the minimum wage of improving levels of fairness and protection are particularly relevant for these groups of more vulnerable women.

Increasing the minimum wage can make a small contribution to reducing the gender pay gap. For example an increase in the minimum wage from \$9.50 to \$10.50 will improve the gender pay ratio by three tenths of a percentage point (0.3) to 82.1%.

Of those receiving the youth minimum wage, the beneficiaries are likely to be youth who are working while still at school (75% of 16 and 17 year olds are still at school or in some form of study) and these workers are likely to be in the retail sector (64% of 16 and 17 year olds are employed in the retail industry). For youth, the increase in weekly income from an increase in the minimum wage is likely to be small, because the majority of young people work short hours.

There may be savings to government through abated income assistance as a result of increased earned income for people in receipt of such assistance (including Working for Families assistance). However, despite abated income assistance, people will still be better off as a result of the increases to their wages.

Statement of consultation undertaken

Submissions for the 2005 Minimum Wage Review were received from a number of organisations reflecting women's interests (the National Advisory Council on the Employment of Women) and worker (New Zealand Council of Trade Unions and Youth Union Movement) and business interests (Business New Zealand, the NZ Retailers Association, The Hospitality Association, the Federation of Farmers, and New Zealand Association of Retail Grocers and Supermarkets and the Small Business Advisory Group). In addition, the Department of Labour met separately with the New Zealand Council of Trade Unions, Business New Zealand and the Small Business Advisory Group to discuss some of the key issues relating to their submissions. Submissions representing employer interests, emphasised the costs of wage increases (refer above) and sought no or small increases in minimum wages. Employee representatives recommended large increases in the minimum wage, emphasising the benefits to low waged workers.

The Treasury, Ministries of Education, Women's Affairs, Pacific Island Affairs, Social Development, Economic Development, and Youth Development, Te Puni Kokiri, Tertiary Education Commission, the Office for Disability Issues, and the Department of the Prime Minister and Cabinet have been consulted on the 2005 Minimum Wage Review.

The Ministry of Social Development (MSD), the Treasury and the Ministry of Economic Development have raised concerns that larger increases in minimum wage rates, which would directly affect a considerably larger number of workers than have been affected by previous increases, involve risks of a significant reduction in employment opportunities, particularly for vulnerable groups, and of wider economic losses. The extent of these potential losses cannot be quantified, however, these negative effects will be exacerbated if current buoyant economic and labour market conditions soften.

These risks have been noted in the 2005 Minimum Wage Review. The Department of Labour considers that, given current economic and labour market conditions, an increase in the minimum wage above the rate needed to maintain relativity to the average wage (e.g. \$10 an hour or more) could be made to reflect a stronger view of the contribution of the minimum wage to its objectives. An increase over \$10.50 an hour could, however, mean a higher risk that the rate of growth of minimum wage jobs would slow, especially if there is a downturn in the economy or a further softening in economic conditions.

MSD has also noted a concern that much of the re-distributional gains from gross increases in the minimum wage for low paid workers and low income families will be limited. MSD observes that in the current post-Working for Families environment raising the minimum wage is not a particularly effective way to improve the take home income of poor working families. The Department of Labour and MSD will undertake further research to better understand the interface between minimum wage increases and Working for Families.

Business compliance cost statement

This statement is based on the assumption that the minimum wage will be increased – there will be no incremental compliance costs if the minimum wage is left unchanged.

Changes to minimum wages require firms that currently pay less than the new minimum wage to their employees to raise those wages from the time that the new minimum wage rates come into force. This adjustment will require minor changes to data in payroll

systems, but otherwise, the regulatory requirements remain unchanged by changing minimum wage rates. There may be compliance costs for employers adjusting to an increased minimum wage and these adjustments are likely to disproportionately affect small businesses because small businesses employ proportionally large numbers of minimum wage earners and tend to offer a narrow wage band (so flow on effects may occur). Early notice of an increase will reduce these costs. These costs may change depending on the particular path taken to achieve the government's goal of \$12 an hour.

Employers employing workers who are paid less than the new minimum wage rates will be affected. Information from the July 2004 to June 2005 Statistics New Zealand Household Labour Force Survey Income Supplement suggests that these employers are most likely to be in agriculture and agricultural services, parts of manufacturing (food, beverage and tobacco; textiles, clothing, footwear and leather), retail trades, restaurants and hotels, business services, education and health and community services.

The Minister of Labour will undertake a communications strategy to outline the changes to minimum wage rates. Changes would not come into effect until March to allow employers time to adjust to the change.