



# Australian Fair Pay Commission – 2008 Minimum Wage Review



AUSTRALIAN INDUSTRY GROUP

**Ai GROUP SUBMISSION**



March 2008

# **2008 MINIMUM WAGE REVIEW**

**Submission to the  
Australian Fair Pay Commission**



**March 2008**

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# 2008 MINIMUM WAGE REVIEW

## Submission

### 1. Introduction

1. The 2008 Minimum Wage Review takes place in a climate of increased economic risk and uncertainty.
2. The global economy is slowing to an, as yet, uncertain extent while at the same time inflation appears to be moving higher in most of the developed economies. Domestically, inflation has accelerated and there is significant doubt around the extent to which the Reserve Bank will need to slow the economy in order to reel in rising inflationary expectations.
3. These factors, together with competitive pressures due to low labour cost competition from China among other economies, and the sustained lift in the Australian dollar require that great caution be exercised in determining minimum wage outcomes this year.
4. Ai Group proposes that minimum wages be increased for all classifications by 35 cents per hour (ie. \$13.30 per week) from the first pay period on or after 1 October 2008 (ie. twelve months since the last increase). This would increase the Federal Minimum Wage (FMW) to \$14.09 per hour.
5. Ai Group's proposal represents a 2.5% increase in the minimum wage, but very importantly when the 1 July 2008 tax cuts are taken into account this amount increases to around \$20 or 4.1%. Even higher benefits result for most low income families with children. For a single income family earning the minimum wage, with two children, when the tax cuts and changes to the Family Tax Benefit are taken into account the increase in income is over \$27.

6. In both of its minimum wage decisions to date, the Fair Pay Commission has expressed the view that it is appropriate that changes to income tax and income support be taken into account in determining the level of increase in minimum wages. Changes to taxation and income support typically deliver far more cost effective and less economically risky benefits than increases to wages.
7. If the level of wage increase awarded by the Fair Pay Commission is too high inflationary pressures will be fuelled and increased pressure will be placed on interest rates. Such an outcome would harm the very people that the minimum wage review process is intended to benefit – that is, the low paid.
8. It is important that the level of increase in minimum wages determined by the Fair Pay Commission not reduce the scope for bargaining over wages at the workplace level. This would conflict with the objects of the *Workplace Relations Act*.
9. The level of wage increase proposed by Ai Group would assist the low paid whilst not posing undue risks to the Australian economy.
10. This submission is made on behalf of the Australian Industry Group (Ai Group) and the Engineering Employers Association, South Australia (EEASA).

## 2. Ai Group's Position

11. Ai Group proposes that minimum wages be increased for all classifications by **35 cents per hour** (ie. **\$13.30 per week**) from the **first pay period on or after 1 October 2008** (ie. twelve months since the last increase). This would increase the Federal Minimum Wage (FMW) to **\$14.09 per hour**.
  
12. The proposed level of increase takes into account:
  - The non-adversarial nature of the Fair Pay Commission's deliberations and the importance of avoiding "ambit" positions;
  
  - The objects of the Act and the Fair Pay Commission's wage-setting parameters;
  
  - The need to provide a fair safety net for the low paid;
  
  - Current economic conditions and the outlook for the Australian economy;
  
  - The need to avoid added inflationary pressures;
  
  - The need to avoid placing further pressure on interest rates;
  
  - Australia's current less than optimal productivity performance;
  
  - Employment and competitiveness across the economy;
  
  - The importance of taking into account the interactions between different elements of the social safety net - in particular the proposed changes to taxation and income support from 1 July 2008.

- The capacity for the unemployed and the low paid to obtain and remain in employment, as well as underemployment and marginal attachment to the labour force;
  - The need for minimum wage increases to be positioned at a level below average workplace agreement outcomes in order to avoid diminishing the primacy which is given to workplace agreement-making under the Act.
9. Ai Group proposes on this occasion that the Fair Pay Commission apply the wage increase to all classifications. This will assist in maintaining the integrity of skills-based classification structures in Pay Scales.
13. In contrast to the sensible and responsible wage increase proposed by Ai Group, the ACTU's excessive \$26.00 per week proposed wage increase represents:
- A 5% increase in the standard FMW; and
  - A 4.2% increase on the base trade rate (C10).
14. If the Fair Pay Commission increased minimum wages by \$26.00, as proposed by the ACTU, the effects would be:
- Reduced employment;
  - Higher inflation;
  - Higher interest rates; and
  - Reduced international competitiveness.
15. The ACTU's proposed \$26 wage increase would also reduce the scope for bargaining over wages at the enterprise level. This directly conflicts with the objects of the Act.

### 3. Legislative Provisions

#### Wage-setting parameters

16. Section 23 of the *Workplace Relations Act* sets out the wage-setting parameters to which the Fair Pay Commission must have regard in performing its wage-setting functions.
17. The Commission's objective, in performing its wage-setting function, is to promote the economic prosperity of the people of Australia having regard to:
  - The capacity of the unemployed and low paid to obtain and remain in employment;
  - Employment and competitiveness across the economy;
  - Providing a safety net for the low paid;
  - Providing minimum wages for junior employees, employees to whom training arrangements apply and employees with a disability that ensure those employees are competitive in the labour market.
18. As Ai Group noted in its 2007 submission, the Fair Pay Commission's wage-setting parameters place a greater emphasis on ensuring that the unemployed and the low paid are able to obtain employment and retain it, that the objects which guided the Australian Industrial Relations Commission (AIRC) in Safety Net Review Cases.
19. In **Chapter 7** of this submission the Commission is urged to pay particular attention to the issue of labour underutilisation when assessing "the capacity of the unemployed and the low paid to obtain and remain in employment".

## Changes to the Fair Pay Commission's wage-setting powers and functions

20. The *Workplace Relations Amendment (Transition to Forward with Fairness) Bill 2008* was introduced into Parliament on 13 February 2008 and will likely become law shortly after submissions to the present minimum wage review close. The Bill confines the Fair Pay Commission's wage-setting functions to conducting wage reviews and as a result, adjusting:
- The standard Federal Minimum Wage;
  - Wage rates in existing Pay Scales; and
  - Existing Special Federal Minimum Wages.
21. The Bill removes the Fair Pay Commission's powers to: determine new Pay Scales; revoke existing Pay Scales; set new Special Federal Minimum Wages; or adjust casual loadings.
22. It is noteworthy that the Bill does not make any changes to the wage-setting parameters in s.23 of the Act.

## 4. The Operative Date of the Decision

### Prospectivity

23. In its 2007 submission to the Fair Pay Commission, Ai Group urged the Commission to:
- Ensure a significant period of prospectivity between the date of the decision and the operative date of the wage increase; and
  - Provide that the increase take effect from the first pay period on or after the relevant date, rather than at midnight on the relevant date, as was the case with the Fair Pay Commission's 2006 decision.
24. Ai Group commends the Fair Pay Commission on implementing these changes in its 2007 decision.
25. As outlined in Ai Group's 2007 submission, a significant period of prospectivity between the decision and the operative date of the increase is a vital practical element of the wage-setting system. An appropriate period of prospectivity takes into account:
- The need for employers to plan for the cost increases; and
  - The linkages between the role of the Fair Pay Commission in adjusting the Federal Minimum Wage and Pay Scales, and the role of the Australian Industrial Relations Commission (AIRC) in adjusting wage rates in transitional awards and wage-related allowances in both transitional and pre-reform awards.

26. The Fair Pay Commission's 2007 Minimum Wage Review Decision was handed down in July. Following this, the AIRC conducted its *2007 Wages and Allowances Review* and handed down its decision on 16 August 2007.
27. Due to the significant period of prospectivity awarded by the Fair Pay Commission in its 2007 decision, a large number of awards were able to be varied by the AIRC prior to 1 October 2007. This meant that the award increases in remuneration were able to operate from the same date as the increases to the Federal Minimum Wage and Pay Scales, without any retrospectivity.
28. However, the situation was still far from ideal. Numerous awards were varied after 1 October 2007 and many were varied by individual AIRC Members retrospectively to 1 October 2007, despite the Full Bench stating that this should only occur in exceptional circumstances. There are substantial administrative and direct costs associated with back-paying employees to take account of retrospectivity of remuneration increases.
29. In its July 2007 Decision, at page 21, the Fair Pay Commission said:
- "In order for stakeholders and the Australian people to have certainty regarding the timing of the Commission's process for future wage reviews, the Commission has committed to an annual general wage review process.*
- Wage-setting decisions will be announced in July each year, with an implementation date in October of that year".*
30. Given the above, Ai Group assumes that the Fair Pay Commission will proceed with the above approach and that there is little point in Ai Group arguing for a greater period of prospectivity. We make the point though, as we did last year, that a period of prospectivity of around three months is the very minimum which allows for efficient and sensible implementation of the decision.

## **Importance of the concept of the ‘first pay period on or after’**

31. As Ai Group outlined in its 2007 submission, the principle of a wage increase becoming operative from the first pay period on or after the relevant date is a longstanding and practical one. The fundamental rationale is to avoid unnecessary and significant complications in implementing wage increases.
  
32. The Fair Pay Commission adopted the principle in its 2007 decision and Ai Group urges the Commission to continue with this approach. Detailed arguments and evidence in support of the approach were set out in our 2007 submission.

## **5. Economic Conditions and Outlook**

33. In the economic assessment set out below, Ai Group takes a global perspective on this year's minimum wages review. This perspective includes developments in the global economy and changes in the domestic economic outlook including in the inflation/interest rate outlook. The implications of the high exchange rate for long-term competitiveness are also discussed.
34. Overall, the 2008 Minimum Wage Review takes place in a climate of increased economic and therefore employment uncertainty.
35. The global economy is slowing to an, as yet, uncertain extent while at the same time inflation appears to be moving higher in most of the developed economies.
36. Domestically, inflation has accelerated and there is significant uncertainty around the extent to which the Reserve Bank will need to slow the economy in order to reel in rising inflationary expectations.
37. These two factors, together with competitive pressures due to low labour cost competition from China among other economies, and the sustained lift in the Australian dollar argue for significant caution in determining wages outcomes in the near-term.

### **Global economic conditions**

38. The world economy is now subject to two key uncertainties, firstly, the extent to which global economic growth will slow and, secondly, the risk of global inflationary pressures continuing to build.

39. Ai Group's view is that the global economy is likely to slow to, or just below, trend growth at around 4% in 2008, with the slowdown largely reflecting the current deterioration in the United States economy.
40. In relation to the US, our expectation is that weaker consumer demand (which makes up over 70% of US GDP) will drive a significant downturn. Slower consumer demand reflects the spill-over effects of the housing sector downturn which has driven housing prices down. Lower house prices have eroded household wealth and, consequently, the ability to borrow to finance consumption.
41. Exacerbating this, increased, though more appropriate US and global risk premia have led to tighter overall financing conditions for businesses and households. To date, significant easing of US monetary policy aimed at offsetting this tightening has yet to have a significant impact. The long-term interest rates on borrowings which finances much of the US's housing and business investment, have remained significantly higher than before the sub-prime crisis began.
42. At this stage, there is a high probability that the US economy is heading into recession, with the extent of the severity remaining uncertain. This outlook remains despite household incomes continuing to grow through moderate wages growth, corporate balance sheets remaining reasonably sound, and the US Federal Reserve acting to ease monetary policy. Fiscal policy is also in the process of being used to provide some stimulus to economic activity.
43. Debate on the extent to which the US downturn will affect global growth more generally has centred on the 'decoupling' debate. Ai Group believes that while the world economy is less sensitive to changes in US economic growth, the linkages are still significant and the risk is that they are being underestimated.

- The euro area, Japan and the emerging economies including China, remain dependent to a significant degree for exports growth on the US demand for imports.
  - In addition, the ongoing deterioration in the value of the US dollar, and consequent appreciation of the euro and yen, has put further pressure on European and Japanese net exports competitiveness and growth. This is particularly important in these economies as the composition of growth during their recent recoveries remains skewed towards some reliance on net exports.
44. Overall, Ai Group is of the view that global growth will be around, or slightly below, trend growth rates, with a risk that any severe US recession and/or contagion from the volatility on global financial markets could cause slower global growth than expected.
45. The economic impetus in the emerging economies should be sustained, notwithstanding a likely sharp easing in US growth. Domestic demand remains solid and, unlike in the period preceding the Asian Financial crisis, there are few signs of significant overvaluation of exchange rates. Policy frameworks have been significantly improved, most are running strong current account surpluses and, generally, government fiscal balances are now healthy enough to provide necessary stimulus in the event of a significant downturn in exports to the US.

## **Key risks to the global outlook**

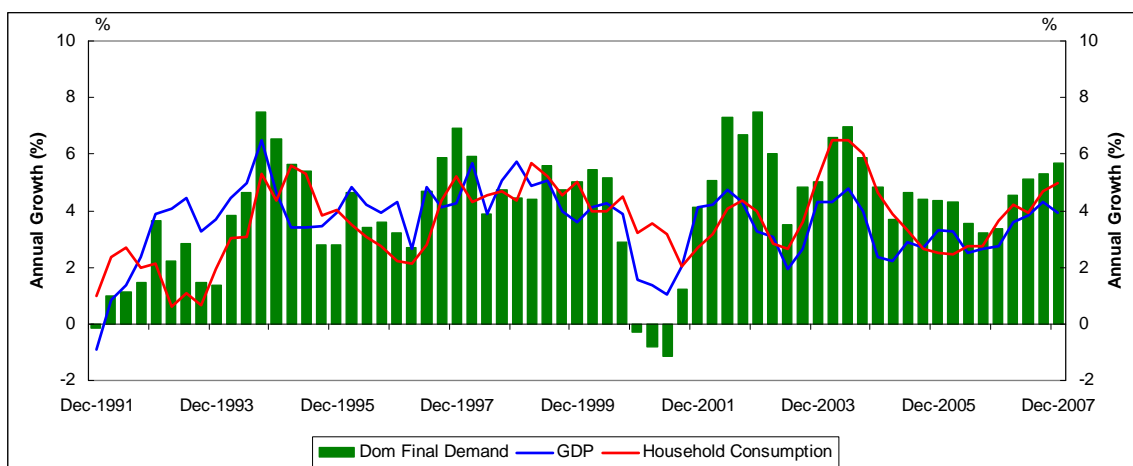
46. A developing risk to the outlook for the world economy stems in part from the emergence of significant, and likely sustained, increases in global food and energy prices. These increases reflect the rise of China and other emerging economies as key long-term drivers of demand growth for these commodities as well as the rise in production of biofuels.

47. Higher food and energy prices in part explain the unexpected lift in inflation that the US appears to be experiencing, as exemplified by a higher than expected increase in core inflation in January 2008.
48. Higher inflation is also a concern in Europe, with the European Central Bank recently lifting its 2008 forecasts for inflation to 2.6% from an earlier forecast of 2.1% and reducing those for economic growth to 1.8% from 2.2%.
49. Inflation in China, which is currently running at over 7%, poses another important risk to Australia's economy. Though weather conditions explain part of the rise in inflation, Chinese authorities are likely to continue to tighten monetary conditions. There is a risk that economic growth may ease further than expected.
50. Overall, while Ai Group expects global growth to run at around or just below trend growth of around 4%, there is continued and significant uncertainty regarding the outlook for the US economy, financial market stability and global inflation.
51. Consequently there is a significant risk that global growth may be lower, reducing the stimulus, particularly through high commodity prices that the Australian economy has benefitted from over recent years. Loss of this stimulus would potentially have a significant impact on the labour market and continued high levels of employment.
52. This uncertainty about the global outlook is an important reason why the Fair Pay Commission needs to be cautious in its decision.

## Domestic economic conditions

53. Australia's economy, like the global economy, is now facing significant uncertainty around the economic outlook.
54. Australia's economy has performed strongly over the past year with growth accelerating to an annual rate of 4.3% in the September quarter of 2007, easing back slightly to 3.9% in the December quarter (**Chart 5.1**). Growth over the year has been driven by strong domestic household consumer spending and business investment in the mining sector and due to strong infrastructure development.

**Chart 5.1: Australian economic growth to December quarter 2007**

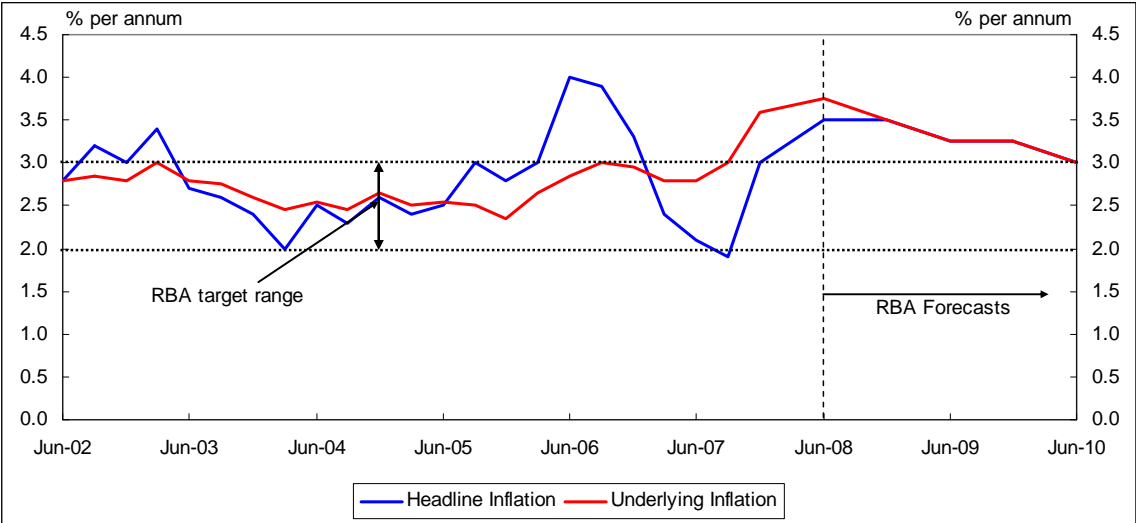


Source: Australian Bureau of Statistics

55. While GDP growth slowed a little in the December quarter 2007, domestic demand growth continued to accelerate to an annual rate of 5.7%.
56. As a result of strong economic growth, spare capacity has been absorbed and labour markets have tightened.

- 57. Unemployment is now at thirty year lows and around or just below current estimates of the non-accelerating inflation rate of unemployment (NAIRU)<sup>1</sup>.
- 58. While, generally speaking, aggregate wages growth measured by the ABS Labour Price Index has remained at around 4% and within the RBA's acceptable range for wages growth, further solid growth in domestic and labour demand would likely put upwards pressure on wages outcomes and therefore inflation outcomes.
- 59. The Reserve Bank's current inflation forecasts, which reflect monetary policy tightening to February 2008, suggest that inflation will remain uncomfortably high relative to its target range of 2-3%, on average, over the economic cycle (**Chart 5.2**).

**Chart 5.2: Australian inflation rate and forecasts**



Source: Reserve Bank of Australia *Statement on Monetary Policy* February 2008.

<sup>1</sup> A senior Commonwealth Treasury macroeconomist, Steven Kennedy, “suggests that the NAIRU is currently around 4.7 per cent, although there is a considerable band of uncertainty around this estimate. It is an unfortunate feature of NAIRU estimates that they are rarely precisely estimated”. (“Full Employment in Australia and the Implications for Policy”, Speech to Economic Society of NSW, 11 December, 2007)

60. The Reserve Bank made clear its view on the outlook for wages and inflation in its February 2008 statement on Monetary Policy released on 11 February and its Reserve Bank Board minutes following its February 2008 meeting which were released on 19 February.

61. From the Statement on Monetary Policy:

*“Wage pressures until now have been mostly confined to the mining and construction industries. Nonetheless, labour market conditions are tight, and there is some evidence of higher growth in aggregate wages in the most recent period. In particular, while the wage price index has continued to show a relatively stable rate of wage inflation, the average earnings measure, which captures a broader range of labour costs, has picked up appreciably over the latest year.”*

*“...the recent pick-up in inflation carries the risk of generating an upward drift in inflation expectations, which could feed back into wage and price-setting behaviour.”*

62. And from the press release of 19 February:

*“a significant moderation in demand will be needed if inflation is to be satisfactorily reduced over time.”*

and

*“On the current outlook... and allowing for inevitable uncertainties in forecasting, the risk of inflation remaining uncomfortably high for some time is considerable. Absent a further shift in economic risks to the downside, therefore, monetary policy is likely to need to be tighter in the period ahead.”*

63. The overall outlook therefore was for further increases in interest rates until the economy and inflationary expectations shows clear signs of slowing. In line with this the cash rate was raised by a further 25 basis points on 4 March.

64. In its press release following the 4 March Reserve Bank Board meeting, the Bank indicated that:

*“the overall tightening in financial conditions since the middle of 2007 is substantial.”*

and

*“There is tentative evidence that some moderation in household demand is beginning to occur, with business and consumer sentiment softer recently, and household credit demand slowing somewhat.”*

65. The Bank also made the point however that:

*“The extent of that moderation is uncertain, however. As the Board noted last month, a significant slowing in demand from its pace of last year is likely to be necessary to reduce inflation over time.”*

66. The acceleration in domestic demand seen in the December quarter 2007 National Accounts supports the view that the Bank will retain its bias to tighten monetary policy further if it does not see significant easing of domestic demand in the near-term.

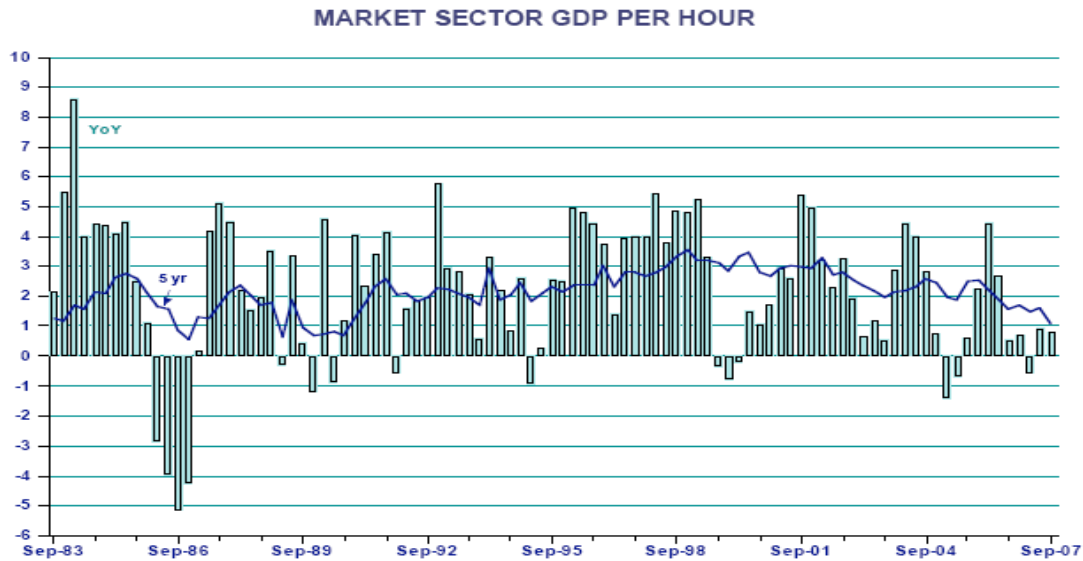
67. This raises clear risks for the labour market and employment. The use of the blunt tool of monetary policy to slow the economy is always subject to the risk of under/over-tightening – most booms/recessions are the result of monetary policy mistakes.

68. It is worth noting, in addition, that while wages data outcomes to date have generally been in line with the RBA's "line in the sand", wages have shown signs of upwards drift and this wages growth is taking place in a climate of weaker productivity growth.
69. The key issue for the transmission of inflationary pressure from a given level of wages growth is the extent to which productivity growth is offsetting increases in wages – that is, the impact of wages increases on unit labour costs.
70. As Ai Group's recent research report "*How Fast Can Australia Grow III*" indicates however:

*"The productivity retreat since the late 1990s has been widespread. Compared to the five years to 2000 average labour productivity growth over the latest five years (to September quarter 2007) is lower in no less than 11 of the 12 broad industry categories comprising the so-called 'market sector' of the economy."*

71. The overall productivity growth picture is illustrated, by the economist's favourite measure of productivity growth, market sector GDP per hour, in **Chart 5.3**. This illustrates a continued decline over the decade to date.
72. Though the analysis contained in "*How Fast Can Australia Grow III*" suggests that, in fact, the picture may not have been a continued decline in market sector productivity growth during the decade but instead a levelling off, it is the case that productivity growth has taken a step-down in comparison with the strong performance experienced in the 1990s.

**Chart 5.3: Market Sector GDP per hour**



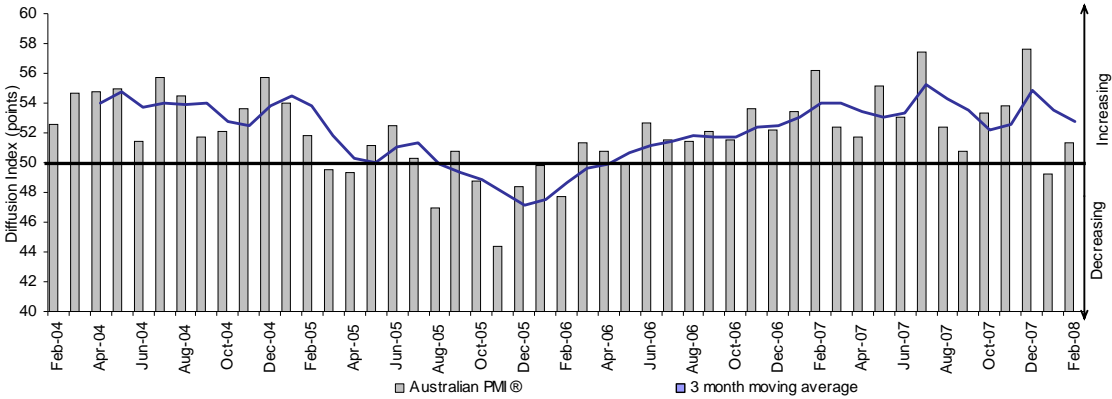
Source: 'How Fast Can Australia Grow III', Australian Industry Group

73. The clear implication is that in a climate of softer productivity growth a given level of wages growth will have a greater impact on unit labour costs than previously when productivity growth was higher. To the extent that productivity growth declines in the near term, a pick up in wages growth from current levels will lead to further inflationary pressures and the likely need for further RBA interest rate increases. In addition, to the extent that tighter monetary policy reduces inflation, rising real unit labour costs will have a negative impact on employment prospects across the economy.
74. The uncertainty around the extent to which the RBA may need to further tighten monetary policy and the risk associated with any phase of tighter monetary policy in terms of its impact on economic and employment growth suggests that decisions on minimum wages increases need to be taken with caution.

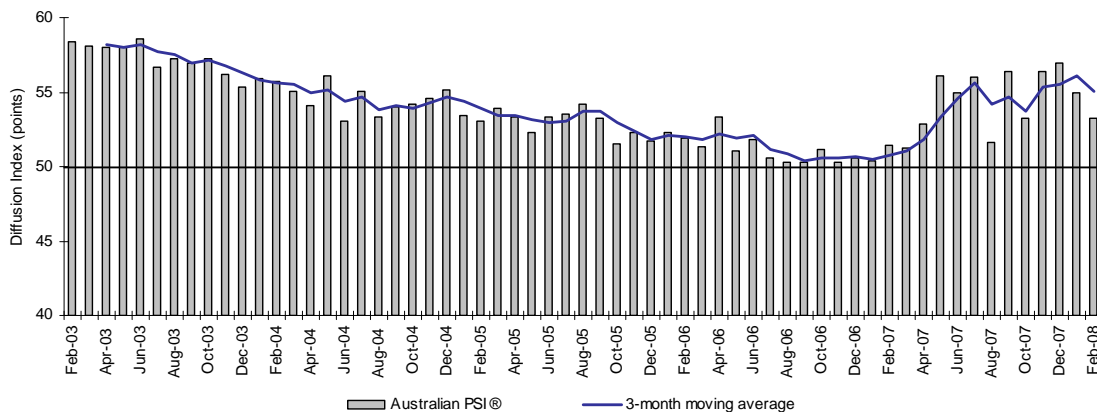
# Industry outlook

- 75. The outlook for industry particularly in the manufacturing and services sectors remains subdued in line with recent developments in Ai Group’s *Performance of Manufacturing Index (PMI)* and *Performance of Services Index (PSI)*.
- 76. Industry activity has been more subdued in manufacturing and services in early 2008. Following softer growth in manufacturing activity in the September quarter (consistent with the national accounts data), growth improved in the December quarter, before easing again in January and remaining subdued in February. (See **Chart 5.4**). The services sector has cooled in early 2008 easing back from its solid expansion path, which has been buoyed by continued strength in consumption and employment. (See **Chart 5.5**). Construction activity has expanded in the past five months.

**Chart 5.4: Australian Industry Group Performance of Manufacturing Index (PMI)**



**Chart 5.5: Australian Industry Group Performance of Services Index (PSI)**



77. According to Ai Group's recent assessment of the outlook for manufacturing, "*Business Prospects for Australian Manufacturing in 2008*" (**Annexure A**) Australian manufacturers are looking forward to moderate growth in 2008, against a background of belt tightening as the sector faces continuing global uncertainty and potential softening in demand. While nominal sales are expected to repeat the strong performance of 2006/7, growth in volume terms will remain moderate.
78. Nominal sales are expected to rise by 7.2% in 2008 (marginally higher than the 6.9% rise in 2006/7). However, adjusting for goods price movements, sales volumes are expected to increase by a modest 2.7% (just above the medium term average).
79. Much of the sales performance will be driven by domestic demand, as the continuation of a strong Australian dollar weakens export performance.
80. Nominal export growth is expected to be 7.5% in 2008, well down on the growth of 13.7% in 2006/7. Price movements, particularly for metals and fuel, however have inflated nominal export performance in recent years. Adjusting for these movements, suggests in volume terms, manufacturing exports will grow by less than 1% in 2008, down from 3.4% in 2006/7.

81. As a precaution against potential softening in demand conditions, manufacturers are tightening their belts, with growth in capital expenditure and research and development expected to slow, and companies making greater use of imported goods and production inputs.
82. Expenditure on new capital equipment is expected to fall for a second consecutive year, dropping by 1.2%, while expenditure on research and development is forecast to rise by less than 1%, after an estimated 4.2% rise in 2006/7. Use of offshore materials (as a percentage of sales) is estimated to rise to 32% from 31.7%.
83. Manufacturers are expected to make greater use of new products to improve competitiveness in 2008, the ratio of new products to sales rising from 21.2% in 2007 to 23.1%.
84. Offsetting these savings, will be an increase in manufacturing employment of 2.2% (for the second consecutive year), as manufacturers continue to lift production to meet rising demand.
85. Selling prices are expected to creep marginally higher, to 4.5%, with average wages expected to rise by 4.6%.
86. It is worth noting that the survey was conducted in late December 2007, covering over 500 manufacturers across all states. It precedes the recent reversal in financial markets and increases in official, and commercial, interest rates since January 2008. The worsening of the inflation outlook and the likelihood of further increases in interest rates suggests that the actual outcomes for the manufacturing sector in the near-term are likely to be softer than those suggested in the survey.

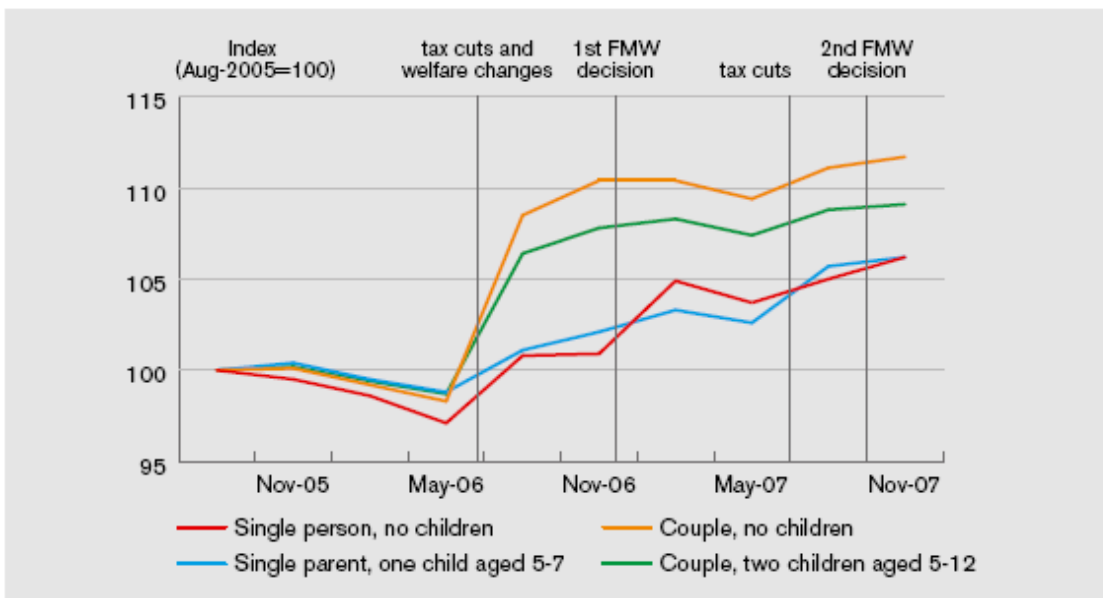
## Summary

87. The international and Australian economies are experiencing significant uncertainty at the moment.
88. While Ai Group's expectation is that the emerging economies will support global growth at around, or slightly below, trend growth rates, there are significant risks that a US recession and/or contagion from the volatility on global financial markets will cause slower global growth than expected. There is also a risk that rising inflationary pressures will constrain the ability of central banks to offset slower growth.
89. Domestically, the uncertainty primarily lies in the ability of the Reserve Bank to engineer a reduction in domestic demand and consequently inflation, without causing a significant downturn which lifts real unit labour costs and leads to a rise in unemployment.
90. The growing uncertainty around the economic and employment outlooks argues for caution in adjustments in minimum wages.

## 6. Minimum Wages and the Social Safety Net

91. In performing its wage setting function, the Fair Pay Commission is to have regard to providing a safety net for the low paid.
92. Ai Group agrees strongly with the Commission's view, expressed in both its minimum wage decisions to date, that the appropriate benchmark for the social safety net should take into account the support provided to the low paid through Australia's income tax and income support systems.
93. In its most recent February 2008 report, the Fair Pay Commission analysed changes in disposable income for four illustrative family types and highlighted the substantial impact of changes to taxation and income support arrangements in boosting household income. **Chart 6.1** is extracted from the report.

**Chart 6.1: Developments in real disposable incomes for selected families with one income earner on the Federal Minimum Wage.**



Sources: AFPCS modelling; ABS, *Consumer Price Index*, Catalogue No. 6401.0, various.

Notes: Disposable incomes have been adjusted according to published changes in the CPI.

Source: *Economic and Social Indicators – Monitoring Report July to December 2007*, AFPC, February 2008.

94. In addition to the regular changes to income support levels and income test parameters since the Fair Pay Commission's last decision, further very substantial changes in personal income taxation arrangements have been announced. These are set to take effect from 1 July 2008. These income tax changes together with the regular indexation-based changes to income support arrangements will lift disposable incomes for the low paid substantially.
95. Ai Group urges that these changes in the broader social safety net be taken into account by the Commission in determining the extent of changes in minimum wage levels.
96. Taking into account the changes to income taxation and income support arrangements in setting minimum wages gives greater coherence to the Fair Pay Commission's considerations by reflecting the complex and multifaceted realities of the Australian social safety net. It also carries the potential to assist in achieving better social and economic outcomes as a result of greater coordination between the different elements of the social safety net.
97. In addition to the important advances the Fair Pay Commission has made in taking income tax and income support changes into account, we believe there is further scope for the Commission to improve the coordination between different elements of the safety net. This could be achieved if the Commission gave more explicit guidance of how it takes changes in income tax and income support arrangements into account when determining changes in minimum wages.

## **Changes to the broader social safety net**

98. Significant reductions in personal income tax are scheduled to take effect from 1 July 2008. These include the following measures that will directly impact on low and middle income earners:

## ***Low Income Tax Offset (LITO)***

99. The Low Income Tax Offset (LITO) is set to rise from \$750 to \$1,200 from 1 July 2008. The change to the LITO will:

- Remove personal income tax liabilities for people earning between \$11,000 and \$14,000;
- Reduce effective marginal tax rates in the income range \$11,000 to \$14,000 by 15 percentage points; and
- Reduce tax liabilities for all income earners earning below \$60,000.

## ***Raising the 30% threshold***

100. From 1 July 2008 the tax threshold at which the marginal tax rate is increased from 15 per cent to 30 per cent will be raised from its present level of \$30,000 to \$34,000. This will:

- Reduce annual income liabilities for all people earning more than \$30,000 by a maximum of \$600;
- Reduce effective marginal tax rates in the income range \$30,000 to \$34,000 by 15 percentage points; and
- Combine with the changes to the LITO to deliver a tax cut of as high as \$1,050 a year (for individuals earning between \$34,000 and \$48,750).

101. **Table 6.1** below shows for a range of lower to median income levels, the impacts on disposable income of these changes to taxation arrangements.

**Table 6.1 - Impact of 1 July 2008 tax changes on lower income earners**

<i>Private Income</i>		<i>Change in Disposable Income</i>	
<i>\$ per week</i>	<i>\$ per annum</i>	<i>\$ per week</i>	<i>%</i>
250.00	13,035	5.85	2.4%
350.00	18,249	8.63	2.6%
450.00	23,463	8.63	2.1%
550.00	28,677	8.63	1.7%
650.00	33,891	19.82	3.5%
750.00	39,105	20.14	3.2%
850.00	44,319	20.14	2.9%
950.00	49,533	19.54	2.5%
1,050.00	54,747	15.54	1.9%

102. Changes to income support arrangements are also relevant to the changes in disposable income and should be taken into account when considering the strength of the overall social safety net. The wide availability of Family Tax Benefit (Parts A and B) makes its consideration particularly relevant in the context of changes to minimum wages.

### ***Changes to Family Tax Benefit***

103. The combination of regular changes in the levels of payments and the income tests applying to family tax benefit add significantly to disposable income. This is particularly the case for lower income earners for whom Family Tax Benefit payments can represent over 30% (and in some cases in excess of 40%) of disposable income.

104. The latest available information about year on year changes to Family Tax Benefit A and B are set out in **Table 6.2** below.

**Table 6.2 - Changes to Family Tax Benefit Parts A and B  
(as of March 2008 compared with a year earlier)**

	<b>March 2007</b>	<b>March 2008</b>	
<b>Family Tax Benefit Part A</b>	<b>\$ per annum</b>	<b>\$ per annum</b>	<b>Increase</b>
Maximum payment (per child under 13)	4,317.95	4,460.30	3.3%
Basic rate (per child)	1,828.65	1,890.70	3.4%
Large family income supplement (for each of the third or more children)	255.50	262.80	2.9%
Maximum payment threshold	40,000	41,318	3.3%
<b>Family Tax Benefit Part B</b>			
Maximum rate (youngest child under 5)	3,467.50	3,584.30	3.4%
Maximum payment threshold (based on second earner's own income)	4,234	4,380	3.4%
Full payment extinguished	21,572	22,302	3.4%

105. It is sometimes argued that these changes (both in levels of payments and in the income test parameters) should not be taken into account because they are 'only' designed to maintain the level of payments in real terms. However Ai Group believes they should be taken into account because they can represent a significant change in overall nominal incomes for many low-income families. Not to take these changes into account would be to ignore changes in a significant element in total household income and therefore in the broader social safety net.

***Combined changes to taxation and Family Tax Benefit for families with children***

106. **Table 6.3** below records for a family with two children under 13 (the youngest under 5) the combined impact of changes to taxation and Family Tax Benefit (FTB) arrangements. The tax changes are those effective from 1 July 2008 and the changes to FTB are changes to the year to March 2008.

**Table 6.3 - Changes to family disposable income  
(two-child, single-income family)**

<b>Family Private Income</b>		<b>Change in Disposable Income</b>	
<b>\$ per week</b>	<b>\$ per annum</b>	<b>\$ per week</b>	<b>%</b>
250.00	13,035	13.55	2.8%
350.00	18,249	16.33	2.9%
450.00	23,463	16.33	2.5%
550.00	28,677	16.33	2.2%
650.00	33,891	27.52	3.4%
750.00	39,105	27.84	3.2%
850.00	44,319	32.89	3.6%
950.00	49,533	32.29	3.3%
1,050.00	54,747	28.29	2.8%

## **Combined impacts of proposed wage and broader social safety net changes**

107. There clearly have been significant changes to disposable incomes for lower income individuals and households since minimum wages were last adjusted. In addition, Ai Group's proposes an increase of \$13.30 per week in minimum wages (35c per hour). A wage rise of this level would, when combined with the changes in the broader social safety net, result in substantial increases in disposable income for the low paid.
108. **Table 6.4** below shows the combined impacts for a single person of the 1 July 2008 personal income tax changes and a \$13.30 per week increase in the FMW. This is an increase of 2.5% in the minimum wage.

**Table 6.4 - Impact of proposed wage increase and income tax changes  
(single income earner)**

<b>Current Private Income</b>		<b>Change in Disposable Income*</b>			
		<b>Tax Change Only</b>		<b>Tax and Wage Change</b>	
<b>\$pw</b>	<b>\$pa</b>	<b>\$pw</b>	<b>%</b>	<b>\$pw</b>	<b>%</b>
340.00	17,728	8.63	2.7%	15.99	5.0%
370.00	19,292	8.63	2.5%	16.64	4.8%
400.00	20,856	8.63	2.3%	17.29	4.7%
430.00	22,420	8.63	2.2%	17.94	4.5%
460.00	23,984	8.63	2.0%	18.59	4.4%
490.00	25,549	8.63	1.9%	19.24	4.3%
<b>522.12</b>	<b>27,223</b>	<b>8.63</b>	<b>1.8%</b>	<b>19.94</b>	<b>4.2%</b>
550.00	28,677	8.63	1.7%	19.94	4.0%
580.00	30,241	9.32	1.8%	20.10	3.8%
610.00	31,805	13.82	2.5%	24.60	4.5%
640.00	33,370	18.32	3.3%	28.92	5.1%
670.00	34,934	20.14	3.5%	28.92	5.0%
700.00	36,498	20.14	3.3%	28.92	4.8%
730.00	38,062	20.14	3.2%	28.92	4.6%
760.00	39,626	20.14	3.1%	28.92	4.5%
790.00	41,191	20.14	3.0%	28.92	4.4%
820.00	42,755	20.14	3.0%	28.92	4.2%
850.00	44,319	20.14	2.9%	28.92	4.1%
880.00	45,883	20.14	2.8%	28.92	4.0%
910.00	47,447	20.14	2.7%	28.92	3.9%
940.00	49,012	19.94	2.6%	28.72	3.8%
970.00	50,576	18.74	2.4%	27.52	3.5%
1,000.00	52,140	17.54	2.2%	26.32	3.3%
1,030.00	53,704	16.34	2.0%	25.12	3.0%

\* The change in wages is assumed to be \$13.30 per week for people currently on the FMW and all income levels above this. For income levels below the current FMW, a proportional increase is assumed. For example, for a person currently earning three quarters of FMW (\$391.60 pw), the wage increase is assumed to be \$9.98 (i.e. three quarters of \$13.30).

109. **Table 6.5** below shows the combined impacts for a single income family with two children (both under 13 and the youngest under 5) of the 1 July 2008 personal income tax changes, the changes to Family Tax Benefit (FTB) and a \$13.30 per week increase in the FMW.

**Table 6.5 - Impact of proposed wage increase and income tax and FTB changes  
(two-child, single income family)**

<i>Current Private Income</i>		<i>Change in Disposable Income*</i>			
		<i>Tax and Income Support Change Only</i>		<i>Tax, Income Support and Wage Change</i>	
<i>\$pw</i>	<i>\$pa</i>	<i>\$pw</i>	<i>%</i>	<i>\$pw</i>	<i>%</i>
340.00	17,728	16.33	3.0%	23.69	4.3%
370.00	19,292	16.33	2.8%	24.34	4.2%
400.00	20,856	16.33	2.7%	24.99	4.1%
430.00	22,420	16.33	2.6%	25.64	4.1%
460.00	23,984	16.33	2.5%	26.29	4.0%
490.00	25,549	16.33	2.4%	26.94	4.0%
<b>522.12</b>	<b>27,223</b>	<b>16.33</b>	<b>2.3%</b>	<b>27.64</b>	<b>3.9%</b>
550.00	28,677	16.33	2.2%	27.64	3.8%
580.00	30,241	17.02	2.3%	27.80	3.7%
610.00	31,805	21.52	2.8%	32.30	4.2%
640.00	33,370	26.02	3.3%	36.62	4.6%
670.00	34,934	27.84	3.4%	36.62	4.5%
700.00	36,498	27.84	3.3%	36.62	4.4%
730.00	38,062	27.84	3.3%	36.62	4.3%
760.00	39,626	27.84	3.2%	36.62	4.2%
790.00	41,191	32.41	3.6%	39.01	4.4%
820.00	42,755	32.89	3.6%	39.01	4.3%
850.00	44,319	32.89	3.6%	39.01	4.3%
880.00	45,883	32.89	3.5%	39.01	4.2%
910.00	47,447	32.89	3.5%	39.01	4.1%
940.00	49,012	32.69	3.4%	38.81	4.0%
970.00	50,576	31.49	3.2%	37.61	3.9%
1,000.00	52,140	30.29	3.1%	36.41	3.7%
1,030.00	53,704	29.09	2.9%	35.21	3.5%

\* The change in wages is assumed to be \$13.30 per week for people currently on the FMW and all income levels above this. For income levels below the current FMW, a proportional increase is assumed. For example, for a person currently earning three quarters of FMW (\$391.60 pw), the wage increase is assumed to be \$9.98 (i.e. three quarters of \$13.30).

110. As illustrated in these tables, the combination of income tax, income support and the increases in the FMW proposed by Ai Group would significantly raise disposable incomes for low to middle income households.

## **Benefits of close coordination between elements of the broader social safety net**

111. For many years Ai Group has argued that in setting minimum wages, full account should be taken of changes to other elements of the broader social safety net. In particular account should be taken of changes in income tax and income support arrangements.
112. Ai Group has combined this with successful lobbying efforts for changes to income tax arrangements that would benefit low-income earners. For example, following fruitful representations in successive submissions to Commonwealth Budgets, prior to the last election Ai Group argued for further increases in the Low Income Tax Offset and a rise in the personal income tax threshold at which the 30 per cent tax rate begins to apply. Subsequently, both major parties proposed similar changes to these key elements of the personal income tax system.
113. Ai Group recognises the extent to which the Fair Pay Commission has incorporated a formal consideration of income tax and income support arrangements into its deliberations of the safety net role of minimum wages. Ai Group applauds this as an important advance and one that carries with it the potential for achieving better social and economic outcomes through closer coordination of the different elements of the broader social safety net.
114. There are well-understood shortcomings of relying excessively on changes to minimum wages to secure a social safety net for low income households. These include the following:
  - The low benefit/cost ratio of minimum wages rises due to the interplay of the eroding impacts of effective marginal tax rates on changes to employees' disposable incomes and the magnified impact on employers' costs of wages rises and rises in non-wage costs flowing from changes in minimum wage rates. Ai Group estimates that, as a rule of thumb, when

minimum wages are increased, employees receive a benefit in the form of extra disposable income that is roughly half of the additional costs faced by employers.<sup>2</sup>

- The detrimental impacts of high minimum wages on the employment opportunities facing low-income earners. These impacts mean that low income earners face higher risks of unemployment and under-employment when minimum wages are increased.
- The poor targeting of minimum wage increases to low-income households due to the fact that many low-income earners are supplementary-income earners in higher-income households and the fact that many low-income earners have additional sources of income.

115. These shortcomings of using adjustments to minimum wages mean that changing income via other elements of the broader social safety net usually provides a more effective way to maintain or improve the overall social safety net. In particular:

- Reductions in income tax and increases in non-taxable income support payments such as the Family Tax Benefit, flow directly to disposable income and are not eroded by effective marginal tax rates,<sup>3</sup>
- Reductions in income tax and increases in income support payments do not add to the costs of employment and do not adversely impact on the demand for labour. As a result, low-income people do not face higher risks of unemployment and underemployment; and

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<sup>2</sup> For example, if on top of a \$1 wage increase there are extra on-costs (such as payroll tax, worker compensation premiums and superannuation guarantee) of 25%, the total cost to the employer would be \$1.25. For an employee taxed at 30% and subject to the 20% income test under Family Tax Benefit Part A, disposable income would increase by \$0.50. In this case the employee would receive an increase in disposable income of 40% of the additional cost borne by the employer.

<sup>3</sup> To the extent that additional tax revenue is raised to finance these changes, the deadweight loss of additional taxation would need to be factored into a fuller consideration. Conversely, when the broader social safety net is improved by reducing personal income taxation, the reduction in deadweight losses would also need to be factored into calculations.

- Changes in income tax and income support arrangements can be targeted more tightly to low-income households.
116. While Ai Group recognises and applauds the important advances that have been made as a result of the Fair Pay Commission's decisions, we believe there remains further scope for the Commission to improve the coordination between different elements of the safety net. This could be achieved if the Commission gave more explicit guidance of how it takes changes in income tax and income support arrangements into account when determining changes in minimum wages.
117. An important impact of this more explicit guidance would be in informing policy makers of the extent to which changes they make in the broader social safety net would impact on changes in minimum wage levels.

## 7. The Capacity of the Low Paid to Obtain and Remain in Employment

118. In exercising its minimum wage setting powers, the Fair Pay Commission is required to have regard to the capacity of the low paid to obtain and remain in employment.
119. Ai Group maintains that in looking to the capacity of the low paid to obtain and remain in employment the Commission should:
- have regard to the full extent of labour underutilisation; and
  - question claims that changes to minimum wage levels have a role to play in encouraging labour supply.

### Labour underutilisation

120. In response to arguments, including those put by Ai Group, in its 2007 Decision the Fair Pay Commission noted (p.59) that:
- “The Commission will continue to monitor broader measures of labour underutilisation as they become available.”*
121. Ai Group commends this receptiveness to the importance of broader measures of labour market utilisation. Building on this receptiveness, we encourage the Fair Pay Commission to take closer account of the full extent of labour underutilisation.
122. As we argued in our submission to the 2007 case, broader measures of labour underutilisation record important features of the labour market that are not covered by official unemployment data. The experiences of underemployed

and people with a marginal attachment to the labour force do not count as far as official measures of unemployment are concerned. Yet it is very likely that these groups would be impacted by the decisions of the Fair Pay Commission in setting minimum wages.

123. We also noted that official measures of unemployment do not include:

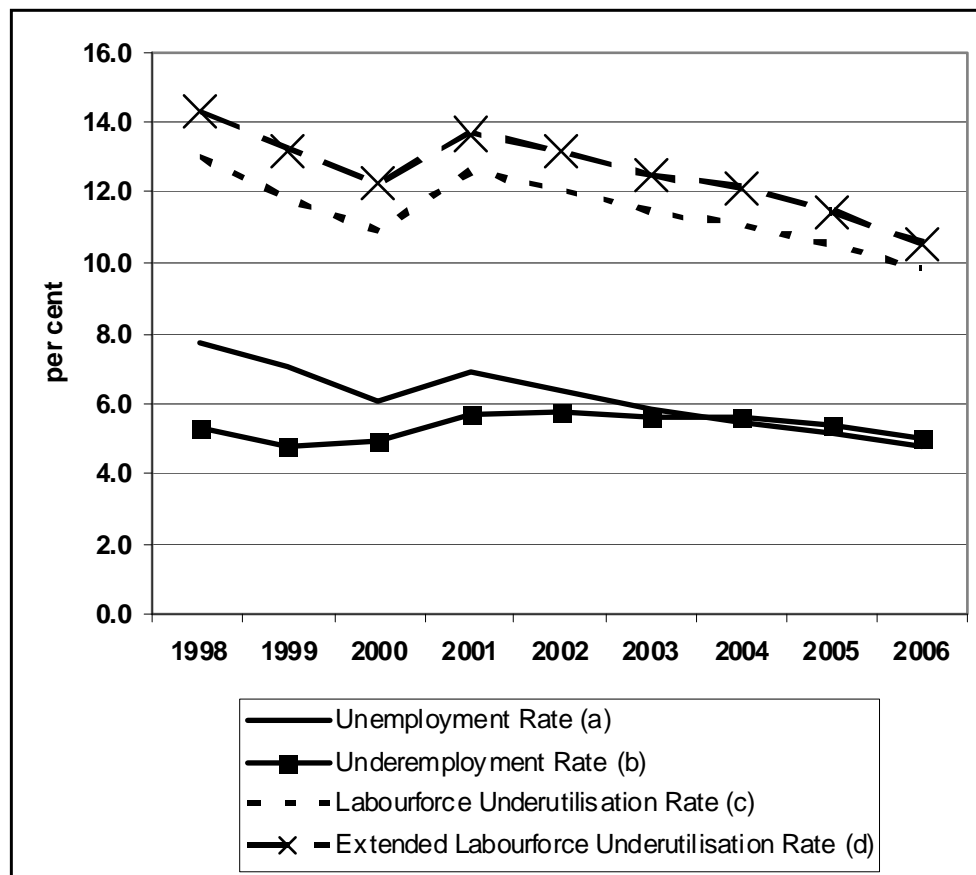
- Part time workers who would like to work more hours;
- Full-time workers who are involuntarily only working part-time at the time of the ABS labour market surveys; and
- People marginally attached to the labour force such as discouraged jobseekers and people who are actively looking for work but would not be ready to start work within one week.

124. We expect that the labour market aspirations of people who are underemployed and those with a marginal attachment to the labour force may be unfavourably impacted by decisions to raise minimum wage rates.

125. As **Chart 7.1** makes clear, the number of people who are included in broader measures of labour market underutilisation is between double and triple the number of people who are regarded officially as “unemployed”.

126. Ai Group urges the Commission to fully integrate underemployment and marginal attachment to the labour force as well as unemployment in its considerations on the full impacts of changes in minimum wage levels on the labour market.

**Chart 7.1: Measures of Labour Underutilisation in Australia 1998 to 2006**



- (a) The unemployment rate is the unemployed expressed as a proportion of the labour force.
- (b) The underemployment rate is the underemployed expressed as a proportion of the labour force. Underemployed people include part-time workers who want, and are available to work, more hours, and full-time workers who involuntarily worked part-time hours in the week of the ABS survey.
- (c) The labour force underutilisation rate is the unemployed, plus the underemployed, expressed as a proportion of the labour force.
- (d) The extended labour force underutilisation rate is the unemployed, plus the underemployed, plus a subset of persons marginally attached to the labour force, expressed as a proportion of the labour force augmented by the marginally attached persons. The marginally attached people are discouraged jobseekers and people actively looking for work and available to start after one week and within four weeks of the ABS survey.

Source: ABS, 6105.0 Australian Labour Market Statistics, January 2008.

## **Changes to minimum wage levels and encouraging labour supply**

127. In its 2007 Decision the Fair Pay Commission noted (at p.52) an argument that minimum wages should be set at a level sufficient to encourage labour force participation.
128. Ai Group encourages a close consideration of this argument.
129. In general employers have strong incentives to offer wages at a level that will encourage labour force participation. A minimum wage level will put a floor under which employers cannot test potential employees' responsiveness to offers of employment. It will not, however, prevent employers offering higher-than-minimum wages to encourage supply if they cannot find suitable applicants at the minimum wage rate.
130. Clearly levels of, and eligibility requirements for, income support are relevant to people's decisions about participation in the workforce. However the level at which the minimum wage is set does not prohibit employers offering higher-than-minimum wages if that is needed to entice people currently eligible for income support into the workforce.
131. There is no shortage of evidence of employers' willingness to offer wages that are above minimum levels.
132. In light of the existence of adequate market-based incentives for employers to induce labour force supply, Ai Group does not think there is a strong reason for the minimum wage review decision to be complicated by the need to assess whether minimum wage levels will be sufficient to induce adequate labour supply.

## 8. Impacts of Minimum Wage Increases

133. The *Workplace Relations Act* emphasises the importance and primacy of agreement-making between employers and employees with regard to the determination of wages and working conditions. The Principal Object of the Act includes:
- Ensuring that, as far as possible, the primary responsibility for determining matters affecting the employment relationship rests with the employer and employees **at the workplace or enterprise level** (s.3(d));
  - Enabling employers and employees to choose the **most appropriate form of agreement** for their particular circumstances (s.3(e)); and
  - Ensuring that awards provide minimum safety net entitlements for award-reliant employees which are consistent with Australian Fair Pay Commission decisions and **which avoid creating disincentives to bargain at the workplace level** (s.3(g)). (Emphasis added)
134. It is important that the level of increase in minimum wages determined by the Fair Pay Commission not reduce the scope for bargaining over wages at the workplace level. This would conflict with the objects of the Act.
135. **Table 8.1** sets out average annualised wage increases for collective agreements registered in the September Quarter 2007, reproduced from the *Trends in Federal Enterprise Bargaining* report of the Department of Employment and Workplace Relations.

**Table 8.1 - average annualised wage increases for collective agreements registered in the September Quarter 2007**

<b>Sector</b>	<b>AAWI</b>
All industries	3.9%
Private sector	3.8%
Employee Collective Agreements	3.6%
Union Collective Agreements	4.0%
Employer Greenfields	3.6%
Union Greenfields	3.9%
All Manufacturing	3.8%
Non-Metals Manufacturing	3.8%
Metals Manufacturing	3.9%
Construction	4.8%

136. Ai Group submits that the primacy of workplace agreement-making needs to be a foremost consideration of the Fair Pay Commission in adjusting minimum wages. The positioning of minimum wage increases need to be at a level below average enterprise agreement wage outcomes, so as not to detract from the important role of agreement making under the Act.

137. This view was shared by the Full Bench of the AIRC in its *2005 Safety Net Review* decision, in which it said:

*“We are conscious that increases in the award safety net have the potential to influence the pace at which bargaining, either formal or informal, is taken up at the enterprise level”.*<sup>4</sup>

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<sup>4</sup> Paragraph 300 of the *2005 Safety Net Review Decision*

138. The Fair Pay Commission, in its *2006 Minimum Wages Review* decision, noted that there was an “..obligation to avoid creating disincentives to bargain at the workplace level as far as possible”. The Commission said that “*In particular, the decision to award a smaller increase to those employees earning above \$700 per week is partly based on the proposition that these employees are better equipped to reach workplace agreements themselves and should be encouraged to do so.*”<sup>5</sup>
139. Indeed, Ai Group submits that the Fair Pay Commission should not only be wary of factors that may act as a disincentive to workplace bargaining, but in its own words, should encourage parties to do so.

### **Many employers pass on minimum wage increases even though employees are paid above the pay scale rates**

140. The economic impacts of minimum wage adjustments are extended by the fact that in many businesses, minimum wage increases are passed on to employees that are paid above the relevant minimum rate of pay.
141. Ai Group has made submissions to the AIRC in several Safety Net Review Cases, and to the Fair Pay Commission in 2006 and 2007, highlighting that the impact of minimum wage increases extends beyond those paid minimum wages.
142. Ai Group has conducted its own research in this area, most recently a survey in 2006, the results of which were included in our submissions to the Fair Pay Commission in the 2006 Minimum Wages Review.

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<sup>5</sup> AFPC Wage-Setting Decision October 2006, page 91

143. One of the findings from Ai Group's survey was that:

*"There is evidence of the practice by employers of passing on the minimum wage rate increases to non-award rate of pay employees. One in five firms report that they flow on the minimum wage rate increases to all employees not on award rates of pay. An additional 12 percent of firms indicate that they pass on the minimum wage rate increases to at least a proportion of those not on award rates of pay. Consequently, increases in minimum rates of pay have a broader impact on the economy than is typically recognised."*<sup>6</sup>

144. Ai Group maintains that the Fair Pay Commission, in making its decision, should take into account that many employers pass on minimum wage increases, even though their employees are paid above the minimum rate of pay. Consequently, increases in minimum wage rates have a broader impact on the economy than is typically recognised.

## **Disproportionate negative impacts of minimum wage increases on small business**

145. Small businesses are vital to the Australian economy.

146. As Ai Group highlighted in its 2006 and 2007 submissions to the Fair Pay Commission through the use of ABS statistics, a much higher proportion of the employees of small businesses are award-reliant than the employees of larger businesses.

147. Accordingly, on average, small businesses are much more likely to be impacted by minimum wage increases than larger businesses.

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<sup>6</sup> 2006 Review of Minimum Wages – Ai Group Submission to the Australian Fair Pay Commission, July 2006, pg.62

148. In its *2005 Safety Net Review Decision*, the Full Bench of the AIRC said:

*“We accept that businesses employing up to 100 employees employ a larger proportion of award-reliant employees than larger businesses. We have had regard to the impact on small business of the safety net adjustment we propose to award.”<sup>7</sup>*

149. When making its minimum wage decision it is vital that the Fair Pay Commission not lose sight of the negative impacts that a large minimum wage increase will have on small businesses.

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<sup>7</sup> PR002005 at [264]

## 9. Minimum Wages for Adults

150. Ai Group proposes that minimum wages be increased for all classifications by 35 cents per hour (ie. \$13.30 per week) operative from the first pay period on or after 1 October 2008 (ie. a twelve month period since the last increase). This would increase the Federal Minimum Wage (FMW) to \$14.09 per hour.
151. The proposed level of wage increase takes into account:
- The non-adversarial nature of the Fair Pay Commission’s deliberations and the importance of avoiding “ambit” positions;
  - The objects of the Act and the Fair Pay Commission’s wage-setting parameters (see ss.3 and 23 of the Act);
  - The need to provide a safety net for the low paid (see s.23(c));
  - Current economic conditions and the outlook for the Australian economy (see **Chapter 5**);
  - The need to avoid inflationary pressures and avoid placing further pressure on interest rates (see **Chapter 5**);
  - The capacity for the unemployed and the low paid to obtain and remain in employment as well as underemployment and marginal attachment to the labour force (see **Chapters 7** and s.23(a));
  - Employment and competitiveness across the economy (see **Chapter 5** and s.23(b));

- The importance of taking into account the interactions between different elements of the social safety net, including minimum wages, income taxation, income support and non-wage costs (see **Chapter 6**);
- The need for minimum wage increases to be positioned at a level below average workplace agreement wage outcomes in order to avoid diminishing the primacy which is given to workplace agreement-making under the Act (see **Chapter 8** and s.3(d) and (e)).

## **The application of the proposed minimum wage increase to all classifications**

152. Ai Group proposes on this occasion that the Fair Pay Commission apply the wage increase to all classifications. This will assist in maintaining the integrity of skills-based classification structures in Pay Scales.
153. The relativities within skill-based classification structures in Pay Scales are already compressed due to the many flat dollar minimum wage increases which have been awarded by the Fair Pay Commission and the AIRC over the past 15 years, but the compression has not yet reached a stage where the relativities are meaningless.
154. Compression of relativities is not necessarily a problem because market factors and the incidence of over-award payments reduce the detrimental impact of compressed relativities between minimum rates. However, the impacts should be thoroughly analysed and understood before any view is formed by the Fair Pay Commission that it is no longer important to maintain meaningful relativities between classifications.

## **The relevance, if any, of State Wage Case decisions to the the Fair Pay Commission's deliberations**

155. Ai Group maintains the view it expressed in its 2007 submission that the Fair Pay Commission should not be influenced by the various State Wage Case decisions when making its minimum wages decision.
156. The appropriate approach is for the Fair Pay Commission to make its decision on minimum wage increases for those in the national workplace relations system, and then for the State Commissions to schedule proceedings to consider whether the Fair Pay Commission decision should be flowed on to employees in the State systems. Unfortunately, this approach has not been accepted to date by State Commissions, despite Ai Group's strong advocacy of this position in the State Wage Case proceedings.
157. Notwithstanding this, the role of the Fair Pay Commission would be undermined if it gave any weight to State Wage Case decisions in its 2008 decision. To do so would encourage State Commissions to conduct wage cases in 2009, prior to the Fair Pay Commission's deliberations.
158. It is noteworthy that at the Workplace Relations Ministers' Council meeting on 1 February 2008, State Ministers for workplace relations endorsed the Federal Government's *Forward with Fairness Policy* which is directed at achieving a national workplace relations system for all employers and employees in the private sector. In achieving such a system it will be necessary to remove the differences which now exist between the wage rates in Pay Scales and State awards. This adds further weight to the argument set out above.

## 10. Minimum Wages for Juniors and Employees to Whom Training Wages Apply

159. In 2006 and 2007, the Fair Pay Commission adopted the approach of awarding a proportionate minimum wage increase to juniors, apprentices and trainees covered by Preserved Pay Scales.
160. Relativities between rates of pay were preserved by pro rating the general wage increase, based on formulas applying in the relevant pre-Work Choices instruments, or where this was not applicable, by other defined means.
161. Ai Group submits that on this occasion, it is appropriate to continue the approach followed in the 2006 and 2007 Fair Pay Commission decisions. That is, by flowing on the general wage increase to juniors, apprentices and trainees in the same manner as has been done in the previous decisions. That is, *“in ways that preserve existing relativities to the extent this is possible”*.<sup>8</sup>
162. The *Workplace Relations Amendment (Transition to Forward with Fairness) Bill 2008* removes the Fair Pay Commission’s power to determine new Special Federal Minimum Wages for juniors and employees to whom training arrangements apply. However, the Bill does not prevent the Fair Pay Commission adjusting rates of pay in Preserved Pay Scales for these categories of employees.

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<sup>8</sup> 2007 Minimum Wage Review Decision, p.73.

## **11. Minimum Wages for Employees with a Disability**

163. The Fair Pay Commission has established two special FMWs and two Special Pay Scales in relation to employees with a disability. In addition, many Preserved Pay Scales contain supported wage provisions.
164. Ai Group has not detected any difficulties with the wage structures established by the Fair Pay Commission for employees with a disability.
165. Ai Group supports the minimum wage rates in the Preserved Pay Scales, in the two Special Pay Scales and in the two Special FMWs, being increased in proportion to any general increase awarded in the 2008 Minimum Wage Review.
166. Under the *Workplace Relations Amendment (Transition to Forward with Fairness) Bill 2008*, the Fair Pay Commission retains the power to adjust minimum wage rates in Preserved Pay Scales, the existing Special Pay Scales and existing Special FMWs, but removes the power to determine new Pay Scales and new Special FMWs.

# BUSINESS PROSPECTS FOR AUSTRALIAN MANUFACTURING IN 2008

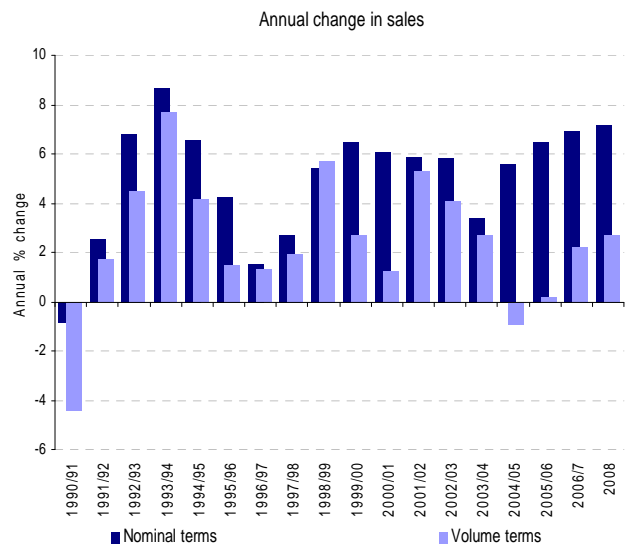
## Moderate year forecast amid belt tightening ...

### Summary

- Australian manufacturers are looking forward to moderate growth in 2008, against a background of belt tightening as the sector faces continuing global uncertainty and potential softening in demand. While nominal sales are expected to repeat the strong performance of 2006/7, growth in volume terms will remain moderate.
- Nominal sales are expected to rise by 7.2% in 2008 (marginally higher than the 6.9% rise in 2006/7). However, adjusting for goods price movements, sales volumes are expected to increase by a modest 2.7% (just above the medium term average).
- Much of the sales performance will be driven by domestic demand, as the continuation of a strong Australian dollar weakens export performance.
- Nominal export growth is expected to be 7.5% in 2008, well down on the growth of 13.7% in 2006/7. Price movements, particularly for metals and fuel, however have inflated nominal export performance in recent years. Adjusting for these movements, suggests in volume terms, manufacturing exports will grow by less than 1% in 2008, down from 3.4% in 2006/7.
- As a precaution against potential softening in demand conditions, manufacturers are tightening their belts, with growth in capital expenditure and research and development expected to slow, and companies making greater use of imported goods and production inputs.
- Expenditure on new capital equipment is expected to fall for a second consecutive year, dropping by 1.2%, while expenditure on research and development is forecast to rise by less than 1%, after an estimated 4.2% rise in 2006/7. Use of offshore materials (as a percentage of sales) is estimated to rise to 32% from 31.7%
- Manufacturers are expected to make greater use of new products to improve competitiveness in 2008, the ratio of new products to sales rising from 21.2% in 2007 to 23.1%.
- Offsetting these savings, will be an increase in manufacturing employment of 2.2% (for the second consecutive year), as manufacturers continue to lift production to meet rising demand.
- Selling prices are expected to creep marginally higher, to 4.5%, with average wages expected to rise by 4.6%.
- The survey was conducted in late December 2007, covering over 500 manufacturers across all states. It precedes the recent reversal in financial markets since January 2008.

### Sales

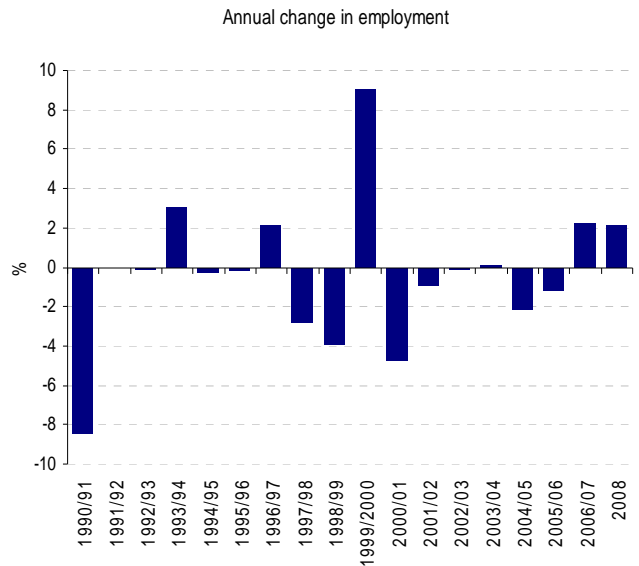
- Nominal sales (based on ABS data) rose by 6.9% in 2006/7. However, after taking into account price increase, the sector experienced an overall 2.2% rise in sales volumes, a significant improvement on the previous two years.
- Prospects for 2008 appear set to remain steady, although in volume terms the sector is forecasting only a moderate lift in sales.
- Nominal sales are forecast to rise by 7.2%, but in volume terms, forecast to grow by 2.7%.



Sales are forecast to rise by 2.7% in volume terms ...

## Employment

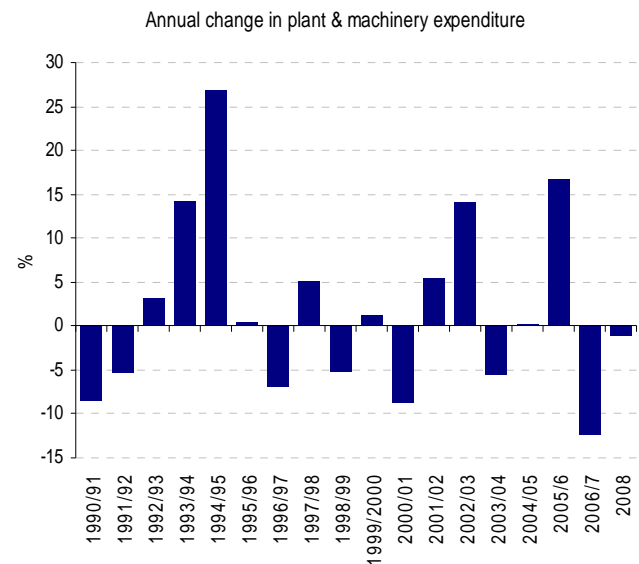
- Employment in manufacturing is forecast to rise by 2.2% in 2008, continuing the trend of the past year. In 2006/7, employment also rose by 2.2% in manufacturing (ABS).
- The forecast increase reflects both the expectation of positive domestic demand conditions, as well as the restructuring process in response to heightened global competition.
- Nevertheless, the employment forecast is optimistic, particularly if demand conditions do make an unexpected turn.



Employment is expected to rise by 2.2% ...

## Investment in plant and machinery

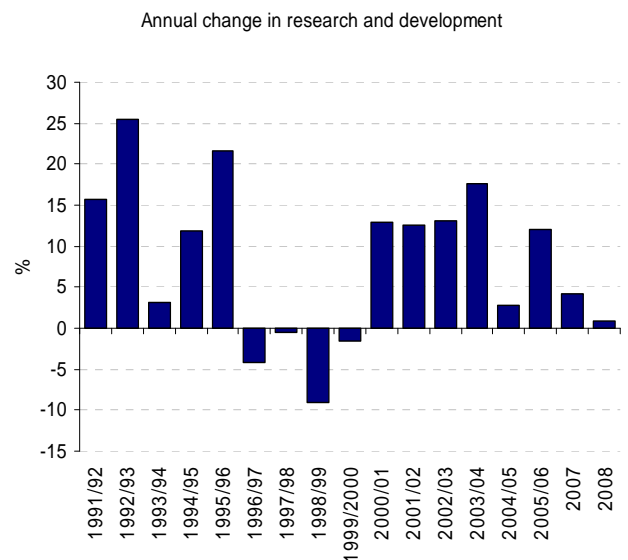
- Despite the positive sales conditions in 2006/7, ABS data shows there was a strong reduction in investment in new plant and equipment, a fall of 12.4%. However, this was after a surge in new investment in 2005/6.
- In 2008 investment in new plant and equipment is expected to continue to decline, by 1.2%.
- This is consistent with ABS forecasts that anticipate expenditure on new capital equipment in manufacturing will remain flat in 2008.



New investment spend forecast to decline by 1.2% ...

## Research and development

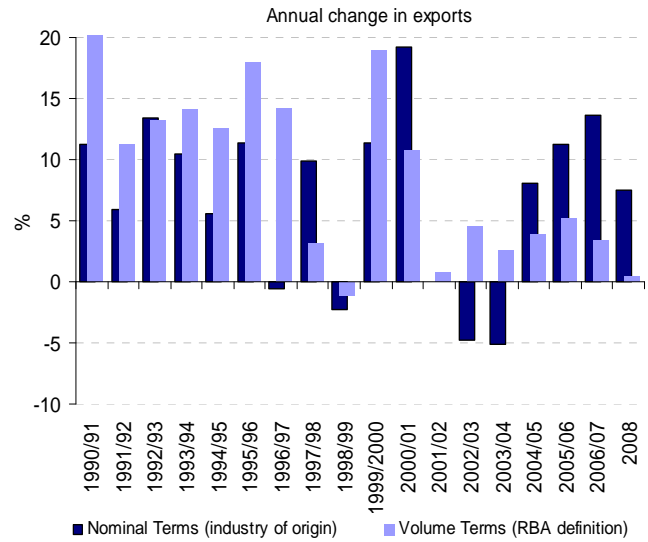
- The latest official ABS data for 2005/6 shows that research and development (R & D) spending by manufacturing rose by 12.0%.
- In 2007, along with the substantial reduction in investment spending, the forecast suggests that spending on R & D was also affected, with only a 4.2% increase expected.
- The forecast for 2008 is for a marginal increase in R & D expenditure (0.8%).



Research and development is anticipated to rise by 0.8% ...

## Exports

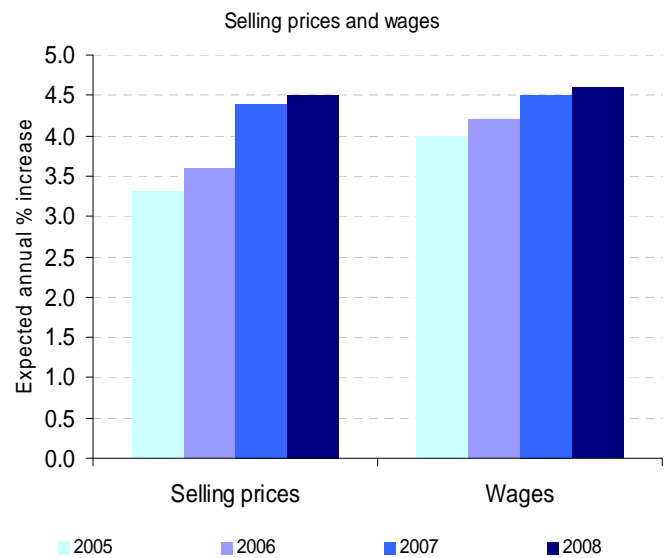
- In nominal terms, manufacturing exports rose relatively strongly in 2006/7, an increase of 13.7%, although in volume terms the increase was significantly smaller.
- Manufacturers are forecasting exports in nominal terms will rise by 7.5% in 2008. The Australian dollar is forecast to remain relatively strong for much of 2008, and this will impact on export growth.
- Adjusting for price movements, the impact of the Australian dollar will see exports in volume terms grow by just 0.5%, the weakest outcome in nine years.



Export volume growth forecast to rise by 0.5%

## Selling prices and wages

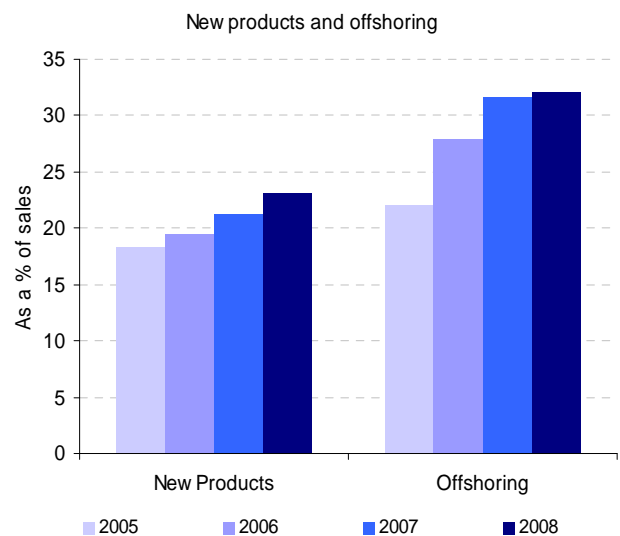
- Manufacturers expect selling prices to rise by 4.5% on average in 2008, a marginal increase on the 4.4% rise predicted for the previous year.
- The expectation for average wage growth in 2008 also rose marginally, lifting from 4.5% in 2007 to 4.6%.



Selling prices forecast to rise by 4.5% and wages by 4.6%

## New products and offshoring

- Heightened global competition is placing increasing pressures on manufacturers to be more innovative and to make better use of global supply chains.
- New product intensity (the percentage of sales derived from new products introduced in the last three years) is expected to rise from 21.2% in 2007 to 23.1% in 2008.
- Offshoring can take two forms: companies moving part or whole of their operations overseas; and/or using a greater share of imported materials in domestic production. Both are seen as a major means of achieving cost reductions.
- The level of offshore intensity (offshore activity as a percentage of sales) is forecast to rise from 31.7% (revised) in 2007 to 32.0% in 2008.



New product development and offshoring to intensify