

# **2009 MINIMUM WAGE REVIEW**

**Submission to the  
Australian Fair Pay Commission**



**March 2009**

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This submission is made on behalf of the Australian Industry Group (Ai Group) and the Engineering Employers Association, South Australia (EEASA). The Members of EEASA recently voted to merge with Ai Group and Ai Group's National Executive has endorsed the merger. Proceedings are currently underway in the AIRC to formalise the merger.

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# 2009 MINIMUM WAGE REVIEW

## Submission

### 1. Context in which the Wage-setting Decision will be made and Ai Group's Position

1. The 2009 Minimum Wage Review takes place at a time when global economic conditions have deteriorated and Australia's economy is experiencing a sharp downturn.
2. The growing consensus now, including the IMF and World Bank, is that the global economy will see a contraction in output in 2009. This would represent the worst global economic outcome since the 1940s.
3. Australia's two largest trading partners Japan and China will see severe recession and a sharp growth slowdown respectively. This will result in cuts to global prices for two of Australia's key exports, iron ore and coal. The downturn in world trade will also reduce export volumes which will reduce the income inflows that have supported Australian growth over recent years.
4. Domestically, 2009 is shaping up to be a very tough year, the toughest in many decades.
5. High levels of debt and rising uncertainty over job prospects is causing consumers to reduce spending and rebuild savings. Businesses have cut back on investment as local and world demand falls. Labour demand is falling as a result, and contributing to rising unemployment.
6. Australia is experiencing an accelerating increase in both the unemployment rate and the number of people unemployed. Also, recorded underemployment is expected to rise sharply in the period ahead.

7. In addition to coping with the bleak economic environment, industry is facing increased costs from Government policy changes. Ai Group's conservative estimates are that the Carbon Pollution Reduction Scheme (CPRS) will add an additional \$8 billion to business costs in the 2010-11 fiscal year, rising to around \$13 billion in the 2020-21 year.
8. There is also the as yet unknown impact of the Fair Work legislation which will come into operation on 1 July 2009.
9. Further, in some industries (particularly Pay Scale reliant industries) modern awards will impose major labour cost increases from January next year. Casual loadings are set to be standardised at 25% in modern awards, up from as low as 10% in some industries. Other cost increases will be experienced in wages, weekend penalty rates, overtime penalty rates, the circumstances in which overtime is payable, and shift loadings.
10. The levelling up of wages and conditions has been particularly pronounced in the Accommodation, Cafés and Restaurants Industry and the Retail Industry, where differences of up to \$50 per week exist in minimum wage rates in Pay Scales arising from State awards. In these industries a high proportion of workers are paid minimum wage rates<sup>1</sup> and hence employers will be unable to absorb any wage increase awarded by the Fair Pay Commission.
11. While the Australian Industrial Relations Commission (AIRC) has the power to phase in cost increases arising from State differences in award wages and conditions over a period of up to 5 years, there is no guarantee that it will decide to do so. The AIRC has indicated that it will determine any transitional arrangements later this year.

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<sup>1</sup> In its 2006 Wage-setting Decision, the Fair Pay Commission reported that 43.2 per cent of employees in the Accommodation, Cafes and Restaurants Sector and 20.9% in the Retail Sector were Pay Scale reliant. These were the top two industries in terms of the proportion of employees who were Pay Scale reliant. Page 86.

12. The economic conditions and outlook plus the environment in which businesses are currently operating, dictate that the Fair Pay Commission take an extremely cautious approach this year in increasing minimum wages.
13. If the level of wage increase awarded by the Commission is too high employment will suffer and the outcome will harm the very people that the minimum wage review process is intended to benefit – that is, the low paid.
14. **This year jobs need to be the priority.**
15. Ai Group proposes that the following approach be taken to increasing the level of the safety net this year:
  - Firstly, that the Fair Pay Commission **increase minimum wages for all classifications by 22 cents per hour (ie. approximately \$8.00 per week)** from the **first pay period on or after 1 October 2009** (ie. twelve months since the last increase). This would increase the Federal Minimum Wage to \$14.53 per hour; and
  - Secondly, that the Government:
    - Increase the **Low Income Tax Offset (LITO)** from \$1,350, which is already legislated to take effect from 1 July 2009, to **\$1,500**;<sup>2</sup> and
    - Raise the **tax threshold** at which the marginal tax rate is increased from 15 per cent to 30 per cent from \$35,000, which is already legislated to take effect from 1 July 2009, to **\$37,000**.<sup>3</sup>
16. Ai Group has already made submissions to the Government about the above taxation changes in its *Submission to the 2009-10 Federal Budget*.

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<sup>2</sup> Currently the LITO is \$1200.

<sup>3</sup> Currently the threshold is \$34,000

17. Ai Group's proposal regarding minimum wages represents an increase in the Federal Minimum Wage of approximately 1.5%, but very importantly when the tax changes which Ai Group has proposed are taken into account, together with changes in Family Tax Benefit A and B, this amount increases to around \$12.55 per week or 2.5%. Higher benefits would result for low income families with children. For a single income family earning the Federal Minimum Wage, with two children, the increase would be over \$21 per week.
18. In its past minimum wage decisions, 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.
19. The level of wage increase proposed by Ai Group would assist the low paid whilst not posing undue risks to the Australian economy.
20. The increase would be fully absorbable in over-award payments.
21. A proportionate increase should be applied to wage rates for juniors, apprentices and trainees.
22. 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*.
23. 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”.*

24. 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 that a period of prospectivity of around three months is the very minimum which allows for efficient and sensible implementation of the decision. Also, this year in particular, employers need time to prepare for any additional wage costs.

## 2. Economic Conditions and Outlook

25. In this economic assessment, Ai Group takes a global perspective on this year's minimum wage adjustment. This perspective includes the deteriorating outlook for the global economy and a domestic economic outlook that is likely to see growth well below potential, at levels last seen during the recession of the early 1990s.
26. Given the unusually high levels of uncertainty around the economic outlook, this minimum wage review takes place in a climate where there is significant downside risk potential for world and Australian economic growth and therefore employment prospects.
27. According to key forecasters, including the International Monetary Fund (IMF) and World Bank, the global economy is likely to contract during 2009. This and the spillover effects of the global financial crisis on availability of finance for Australian firms mean that we are likely to see unemployment rise to over 7% during 2010.
28. The decline in world and domestic demand for the goods and services that Australian firms produce, and the consequent fall in demand for labour argue for significant caution in determining wages outcomes in the near-term.

## Global Economic Conditions

29. The most recent, January 2009, IMF forecasts for global economic growth are as follows:

**Table 1: International Monetary Fund Economic Growth Forecasts**

	2009	2010
World	0.5	3.0
United States	-1.6	1.6
Japan	-2.6	0.6
Euro-area	-2.0	0.2
China	6.7	8.0
Developing Asia (includes China and India)	5.5	6.9

30. However, these forecasts already appear obsolete, continuing a pattern of rapid downgrades of forecasts over the past six months. Illustrating this pattern, following the rapid tightening in major industrial economy finance availability which ensued after the collapse of Lehman Brothers in September 2008, the IMF's growth forecast of 3.0% in 2009 made in its October 2008 World Economic Outlook was downgraded to a forecast of only 0.5% by January 2009.
31. In addition, growth projections published by the Organisation for Economic Co-operation and Development (OECD) in November forecast that in the December quarter of 2008, GDP would fall by 2.8 per cent in annual terms in the US, by 2.1 per cent in the United Kingdom and by 1.0 per cent in the eurozone, Germany and Japan. The actual outcomes were: US GDP fell by 6.2 per cent in annual terms, United Kingdom by 6 per cent and the euro area by 6 per cent. Germany's economy contracted by 8.2 per cent and Japan's by 12.8 per cent.

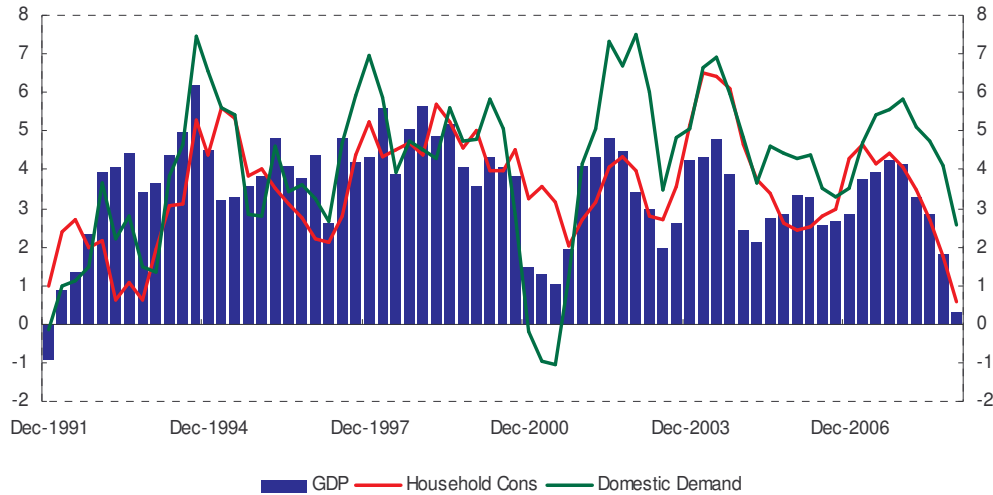
32. The growing consensus now, including the IMF and World Bank, is that the global economy will see a contraction in output in 2009. This would represent the worst global economic outcome since the 1940s.
33. Beyond 2009, if current attempts to ease the decline in availability of credit in the major industrial economies are successful, expansionary fiscal and monetary policies should see the global economy experience a modest recovery in 2010.
34. However, this outlook has more than the usual degree of uncertainty surrounding it and the timing and speed of a recovery in global economic activity depends critically on policy measures being effective. A significant downside risk is that there are ongoing concerns that efforts to recapitalise ailing lenders, notably in the United States, are falling behind the deterioration in bank assets, in part driven by the continued decline in asset prices, notably US housing prices. This is contributing to an ongoing squeeze on lending, not just for investment, but also for working capital covering input and labour costs.
35. In addition, despite sharp reductions in official interest rates in major economies, particularly in the United States and United Kingdom, commercial interest rates have fallen by significantly less, constraining the consumer spending and business investment responses to easier monetary policy.
36. Critically important for Australia's economy which has been underpinned by income derived from strong commodity prices and demand, global trade fell significantly in the December Quarter of 2008 reflecting significant falls in Chinese and Japanese import demand.,
37. The spillover effects of the global financial crisis have continued as measures aimed at improving certainty for lenders in financial markets have to date been ineffective. This has contributed to a decline in world trade as trade finance availability has been squeezed.

38. The constraints on global lending has caused further sharp falls in asset values, including housing and stock markets, across industrial and emerging economies. This process has cut household wealth and consequently caused consumers to cut back demand. This fall in consumer spending has been exacerbated by significant rises in unemployment, particularly in the US, Europe and the UK.
39. High levels of uncertainty regarding the outlook for demand and reduced finance availability have also prompted businesses to put off investment spending.
40. This uncertainty regarding the global outlook is an important reason for caution in the Commission's wage-setting decision.

### **Domestic Economic Conditions**

41. As the global economic outlook worsens, the Australian economy is now facing significant uncertainty around the economic outlook.
42. Australia's economy has slowed strongly over the past year with growth decelerating to an annual rate of 0.3% in the December Quarter of 2008, well down from its peak of 4.2% in the December Quarter of 2007 (**Chart 1**). The decline in growth has been driven by easing domestic demand reflecting in weaker domestic household consumer spending, slower dwelling investment and signs of easing in business investment. Exports growth has also weakened in line with the fall in global trade and the rapid weakening in Japanese and Chinese growth.

**Chart 1: Australian economic growth to December Quarter 2008**



Source: Australian Bureau of Statistics

43. At a national level, the current downturn in economic growth has yet to affect employment and the unemployment rate to a similar degree as previous recessions.
44. This reflects the lags between changes in economic growth and employment decisions made by firms. On average, there is roughly a two-quarters lag between falling economic activity and falling employment as employers seek to hold on to, until recently scarce, skilled labour until it is clear that demand has fallen in a sustained way.

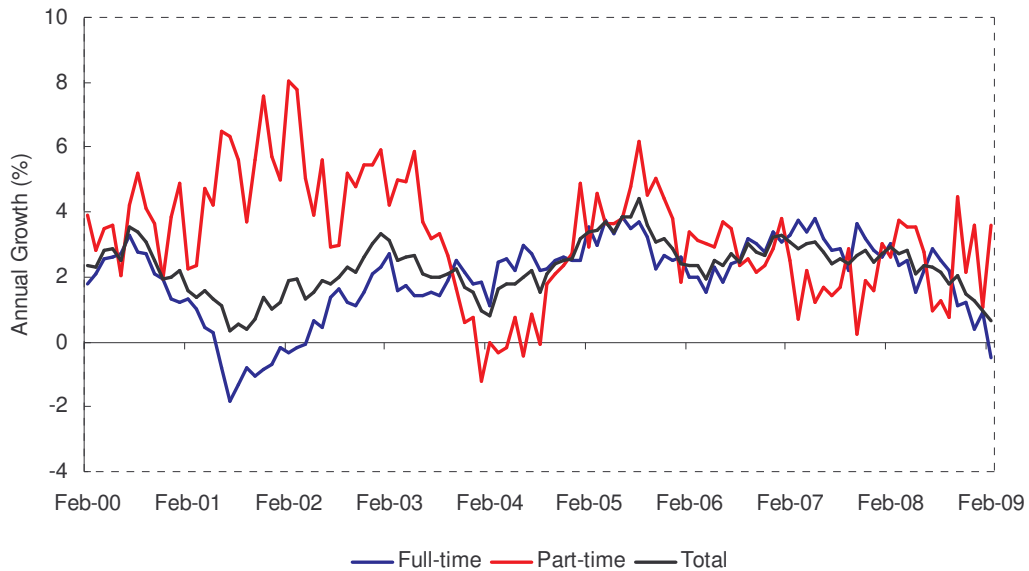
**Table 2: National Employment Market**

	Unemployment Rate (%)	Change in employment Jul 08 to Feb 09	Annual employment growth rate (%)		
			Total	Full-time	Part-time
<b>Australia</b>	5.2	+21775	0.7	-0.5	3.6

As at February 2009

45. Annual economic growth has been below the 3% generally accepted as being required to maintain a stable unemployment rate since June 2008, when it fell to 2.8%, down from a peak growth rate of 4.2% in December Quarter 2007. In line with this, total employment growth has slowed solidly since mid-2008.
46. As **Chart 2** shows, part of the adjustment to slower growth has been continued strong growth in part-time employment while full-time employment growth has fallen sharply as firms have cut back on hours worked.

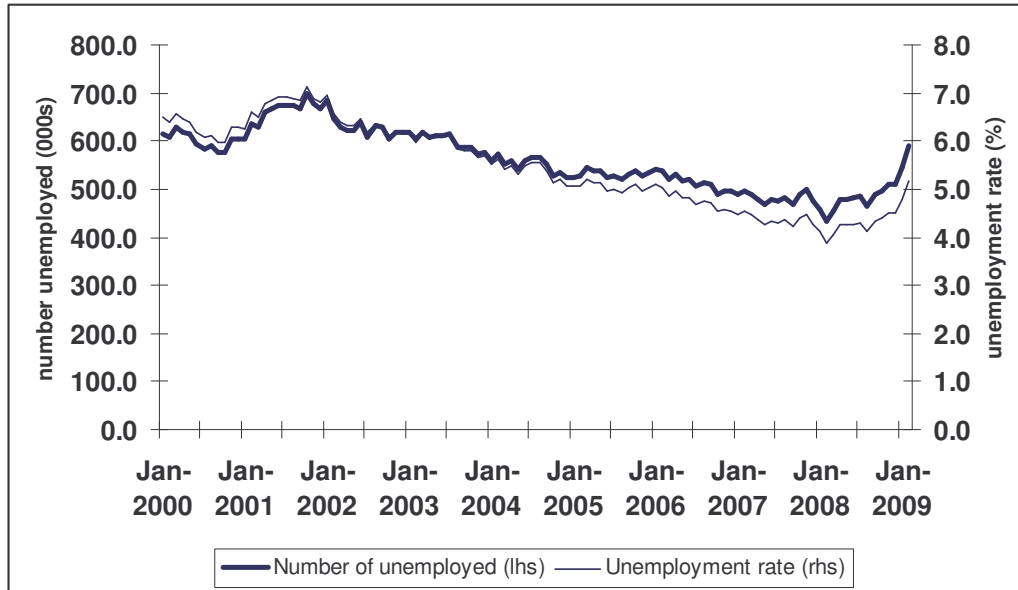
**Chart 2: Australian annual employment growth to January 2009**



Source: Australian Bureau of Statistics

47. Unemployment has begun to rise as illustrated in **Chart 3**.

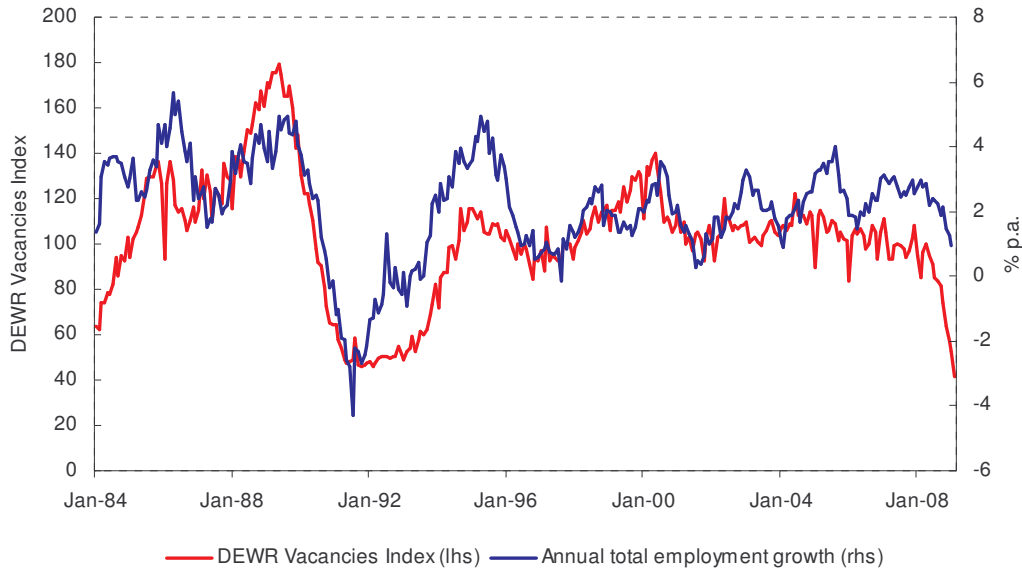
**Chart 3: Australian Unemployment, January 2000 to February 2009  
(seasonally adjusted data)**



Source: ABS 6202.0, February 2009.

48. A clearer indication of the outlook for employment is gained from job vacancies data. The Department of Education, Employment and Workplace Relations (DEEWR) skilled vacancy index tends to closely parallel employment growth outcomes and its recent sharp decline, it was 51.5% lower in February 2009 than a year ago, suggests a further sharp weakening of employment growth over coming months.

**Chart 4: Australian job vacancies to February 2009**



Source: Department of Employment and Workplace Relations

49. The outlook for the economy remains weak. Current economic forecasts for Australian economic activity and unemployment are outlined below.

**Table 3: GDP Growth Forecasts**

	2009	2010
<b>ANZ<sup>1</sup></b>	0.1	2.0
<b>NAB<sup>2</sup></b>	-0.25	1.0
<b>Treasury<sup>3</sup></b>	1.0	0.75
<b>Access Economics<sup>4</sup></b>	0.9	3.0

1. ANZ forecasts are calendar year on year.
2. NAB forecasts calendar year on year.
3. Treasury GDP forecasts are year on year for fiscal years 2008-09, 2009-10.
4. Access Economics forecasts are calendar year on year.

**Table 4: Unemployment Rate Forecasts**

	2009		2010	
	Jun-09	Dec-09	Jun-10	Dec-10
<b>ANZ<sup>1</sup></b>	5.4		6.8 reaching 7% in second half	
<b>NAB<sup>2</sup></b>	5.5	6.25	6.5	7.0
<b>Treasury<sup>3</sup></b>	5.5		7.0	
<b>Access Economics<sup>4</sup></b>	5.6	6.4		7.2
<b>Ai Group<sup>5</sup></b>		6.4		

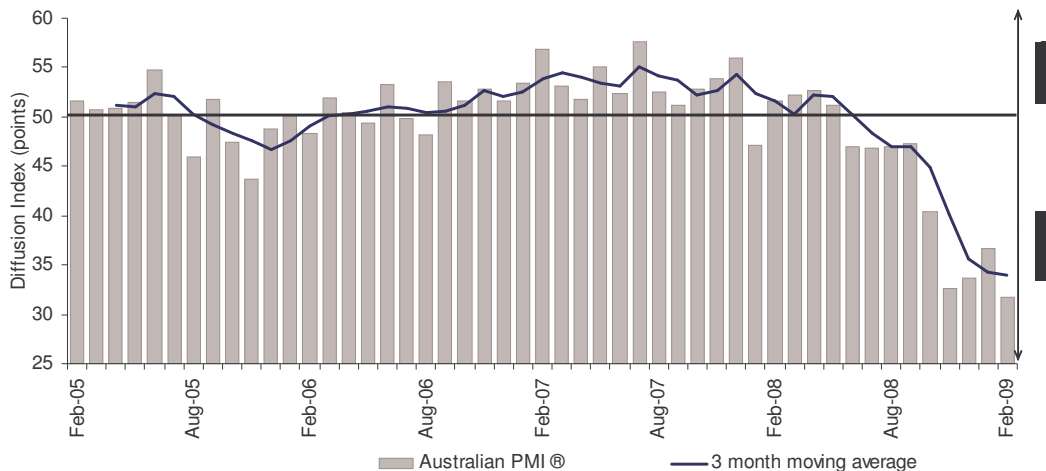
1. ANZ forecasts are calendar year averages.
2. NAB forecasts end of quarter.
3. Treasury GDP forecasts are end June quarter.
4. Access Economics forecasts for 2009 are end of quarter and for 2010, year average.
5. Ai Group forecast is at end of December quarter 2009.

50. Overall, though there is a reasonable variation in forecasts. Expectations for Australian economic growth show a significant slowing of the economy from growth of 2.3% in 2008 and 4.0% in 2007.
51. Weaker household spending, due to increased caution by consumers in the face of the increased risk of unemployment and lower wealth levels, will combine with softer business investment, constrained exports as the world economy weakens, and lower terms of trade to drive the slowing in overall economic activity.
52. The unemployment forecasts appear quite consistent in suggesting that the jobless rate will rise from around 4.5% now to near 6.5% by the end of 2009 and close to 7% by the end of 2010. Ai Group's forecast for an unemployment rate of 6.4% by end 2009 is in line with other agencies' expectations.
53. There is a clear risk that unemployment may be worse than currently forecast, given the greater than expected increase in the unemployment rate, to 5.2%, in February 2009 and the ongoing very sharp deterioration in job vacancies.

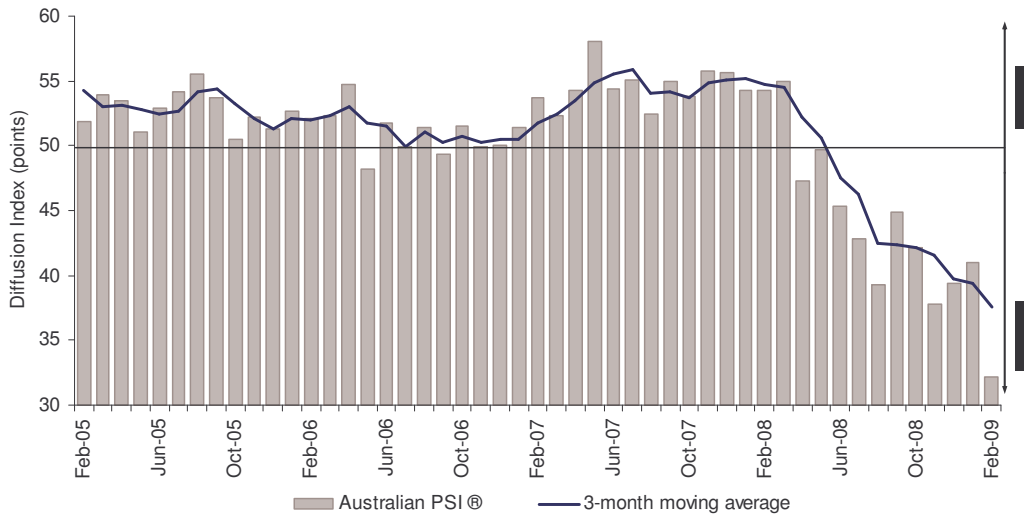
## Industry Outlook

54. The outlook for industry particularly in the manufacturing and services sectors remains very weak in line with recent developments in the Australian Industry Group's Performance of Manufacturing Index (PMI) and Performance of Services Index (PSI).
55. Industry activity in manufacturing and services has fallen consistently since mid-2008. The accelerated decline in manufacturing activity in the December Quarter 2008 and into March Quarter 2009 reflects a continual decline in new orders and run down of stocks, which has contributed to falling production and employment in the sector. The services sector has also seen sharp declines in sales, new orders and inventories which have contributed to declines in employment since mid-2008.

**Chart 5: Australian Industry Group Performance of Manufacturing Index (PMI)**



**Chart 6: Australian Industry Group Performance of Services Index (PSI)**



56. According to Ai Group’s recent assessment of the outlook for manufacturing, services and construction carried out with Deloitte – *National CEO Survey - A tough year ahead – 2009* is shaping up to be a tough year, the toughest in many decades.
57. Manufacturing sales and activity are forecast to decline in 2009, for the first time in 18 years.
58. Prospects are expected to deteriorate as manufacturers anticipate sales to fall by 3.1% to around \$380 billion. Exports are also expected to decline, by 5.3% to \$84 billion. Employment in the sector is forecast to fall by 4.4% (44,000 jobs) to 1.06 million.
59. Consistent with this outlook, expenditure on new plant and machinery, research and development and training will also be cut in 2009.
60. Selling prices on average are forecast to rise by 4.9% and wages by 3.6% in 2009.
61. The outlook for construction is similarly weak, with sales expected to fall by 4.5% in 2009. Total sales are forecast to be around \$145 billion.

62. Employment, which has grown strongly in the sector over the last seven years, is expected to fall by 5.6%, to 920,000.
63. Expenditure on research and development and training and investment in plant and machinery is also expected to fall substantially, as companies seek to cut costs to preserve margins.
64. New products as a percentage of sales are forecast to decline in 2009.
65. The outlook for services is more positive with growth to continue, although at a reduced pace. Total sales are forecast to rise 4.7% to \$1,150 billion. Services exports are also expected to lift, by 2.2% to \$52.5 billion in 2009.
66. Despite the modest sales outlook, employment is expected to fall by 0.6%, or around 40,000 jobs. Expenditure on research and development is also expected to fall.
67. Selling prices are forecast to rise by 4.3%, consistent with recent trends, while wages are expected to rise by 3.6%.
68. Reflecting a relatively more positive growth outlook, the expected cuts to discretionary spending by the services sector are more moderate than those anticipated for manufacturing and construction.
69. Relevant extracts from the Ai Group and Deloitte *National CEO Survey - A tough year ahead* are set out in **Annexure A**.

## Summary

70. The international and Australian economies are experiencing significant downturns and unprecedented levels of uncertainty at the moment.
71. Our expectation is that the global economy, at best, will see no growth during 2009. This will reflect very significant recessions in the industrial economies and slower growth in the merging economies. Australia's two largest trading partners Japan and China will see severe recession and a sharp growth slowdown respectively. This will help to cut global prices for two of Australia's key exports, iron ore and coal. The downturn in world trade will also reduce export volumes. Combined this will reduce the income inflows that have supported Australian growth over recent years.
72. Domestically, high levels of debt and rising uncertainty over job prospects will cause consumers to reduce spending and rebuild savings. Business will cut back on investment as local and world demand falls. Labour demand will fall as a result and contribute to rising unemployment.
73. The persistent uncertainty around the economic and employment outlooks argues for significant caution in adjustments in minimum wages.

### 3. Minimum Wages and the Social Safety Net

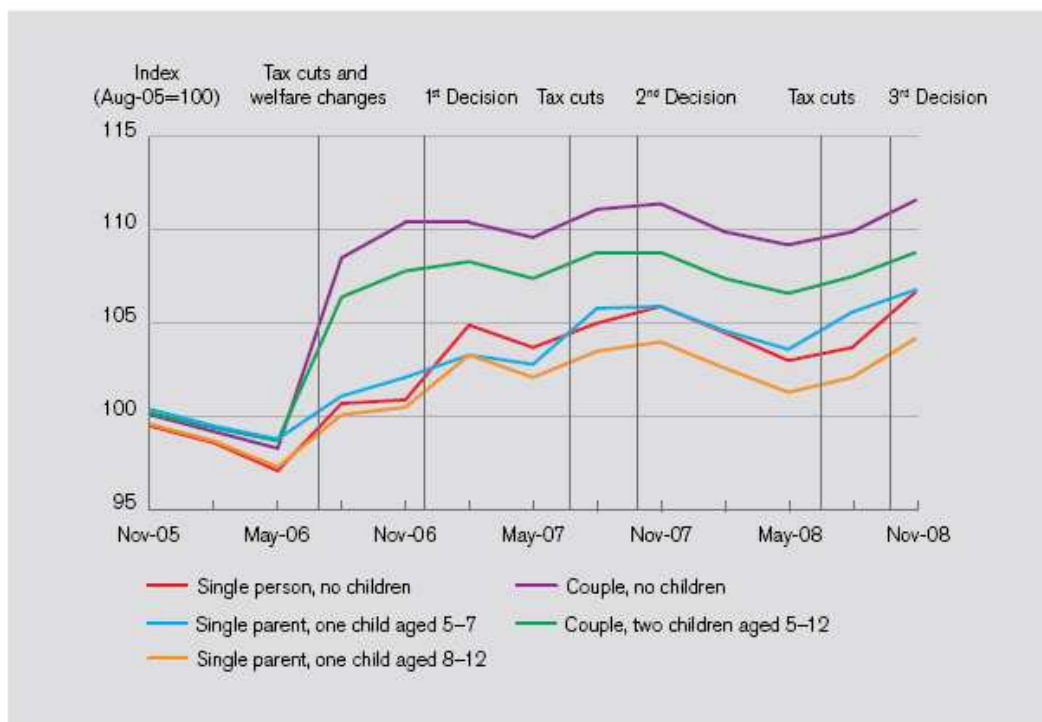
74. In performing its wage-setting function, the Fair Pay Commission is to have regard to providing a safety net for the low paid.
75. Ai Group recognises that the material welfare of households and household members is shaped not only by the market incomes of household members but also by the taxes they pay; any income support payments they receive; as well as benefits from the public provision of a range of services (including education, health and housing).
76. Of particular importance in the context of the Fair Pay Commission's annual assessment of the need to adjust minimum wages to improve or maintain the safety net is the impact on households of changes to income taxation and income support arrangements.
77. In its most recent February 2009 report, the Commission indicated that for four illustrative family types:

*“Over the period from August 2005 to November 2008, the disposable incomes of all the households that were modelled increased in real terms. The approximate real increases for each of the household types over this period were as follows:*

- *12 per cent for a couple without children;*
- *9 per cent for a couple with two children aged 5 to 12;*
- *7 per cent for a single-parent pensioner household and a single person without children; and*
- *4 per cent for a single-parent allowee with a child aged 8 to 12.”*

78. All the household types that were modelled benefited from the tax cuts in July 2008 and the minimum wage increase in October 2008. The single-parent pensioner gained most from the tax cuts, experiencing a 2 per cent increase in real disposable income, while other households experienced a 1 per cent increase. The single person household with no children received the greatest increase in their real disposable income from the increase in the Federal Minimum Wage in October 2008: a 3 per cent increase. Disposable incomes of the couple with no children and single-parent allowee with one child increased by around 2 per cent as a result of the wage increase, while those of the single-parent pensioner and couple with two children increased by just over 1 per cent.

**Chart 7: Developments in Real Disposable Incomes for Selected Families with one income earner on the Federal Minimum Wage**



Note: Disposable incomes have been adjusted according to published changes in the CPI.  
 Source: AFPCS modelling; ABS, *Consumer Price Index, Australia*, December 2008, Catalogue No. 6401.0; Australian Government, *Mid-Year Economic and Fiscal Outlook 2008-09*, released November 2008.

Source: *Economic and Social Indicators – Monitoring Report July to December 2007*, Australian Fair Pay Commission February 2008.

79. Several sets of changes to taxation and income transfers that have occurred or are set to occur are relevant to the Fair Pay Commission's deliberations. These are:
- Changes to income taxation;
  - Changes to income support payment rates and income test parameters; and
  - Cash bonuses paid or to be paid to household members as part of fiscal stimulus packages.
80. Ai Group urges that these changes in the broader social safety net be taken into account by the Commission in determining the extent of any changes in minimum wage levels.
81. 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 nature 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.
82. Ai Group further requests that the Commission takes note of the fact that Ai Group and other organisations have argued that additional income tax changes be introduced from 1 July 2009. In Ai Group's *Submission to the 2009-10 Federal Budget*, for example, we proposed that the changes to income tax arrangements impacting on low and middle income earners in particular, and currently scheduled for 2010 should be brought forward to take effect from 1 July 2009 (**Annexure B**).

## **Changes to the Broader Social Safety Net**

83. From 1 July 2009, two already-legislated changes to income tax arrangements will impact on low and middle income earners.

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

84. The Low Income Tax Offset (LITO) is set to rise from \$1,200 to \$1,350 from 1 July 2009. The changes to the LITO will:

- Remove personal income tax liabilities for people earning between \$14,000 and \$16,000;
- Reduce effective marginal tax rates in the income range \$14,000 to \$16,000 by 15 percentage points; and,
- Reduce tax liabilities for all income earners earning below \$63,750.

### **Raising the 30% Threshold**

85. From 1 July 2009 the tax threshold at which the marginal tax rate is increased from 15 percent to 30 percent will be raised from its present level of \$34,000 to \$35,000. This will:

- Reduce annual income liabilities for all people earning more than \$34,000 by up to \$150;
- Reduce effective marginal tax rates in the income range \$34,000 to \$35,000 by 15 percentage points; and
- Combine with the changes to the LITO to deliver a tax cut of up to \$300 a year (for individuals earning between \$35,000 and \$60,000).

86. 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

87. 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. The latest available information about year on year changes to Family Tax Benefit A and B and rent assistance are set out in *Table 5* below.

**Table 5 - Changes to Family Tax Benefit Parts A and B and Rent Assistance  
(as of March 2009 compared with a year earlier)**

	<i>March 2008</i>	<i>March 2009</i>	
	<i>\$ per annum</i>	<i>\$ per annum</i>	<i>Increase</i>
<b>Family Tax Benefit Part A</b>			
Maximum payment (per child under 13)	4,460.30	4,631.85	3.8%
Basic rate (per child)	1,890.70	1,945.45	2.9%
Maximum payment threshold	41,318	42,559	3.0%
<b>Family Tax Benefit Part B</b>			
Maximum rate (youngest child under 5)	3,584.30	3,693.80	3.1%
Maximum payment threshold (based on second earner's own income)	4,380	4,526	3.3%
Full payment extinguished	21,572	22,302	3.4%
<b>Rent Assistance</b> (maximum rate for family with two children)	3,226.42	3,372.42	4.5%

88. It is sometimes suggested 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, particularly for families reliant on low paid employees, Family Tax Benefit is a significant proportion of disposable income and therefore changes in this component of disposable income are also significant.
89. For example, for a single income earner on the FMW with a spouse and two young children:
- Around 38% of household disposable income would be made up of Family Tax Benefit A, Family Tax Benefit B and Rent Assistance;
  - Over the past year, the total amount received under these three elements of income support has increased by 3.8%;
  - As a consequence, without any change in wages or taxation, family disposable income would have increased by 1.4%.
90. Ai Group maintains that, in the context of the magnitude of changes to minimum wages that has applied in the past, a 1.4% change in disposable income is significant.

### **Cash Bonuses Paid to Households**

91. In response to the global financial crisis and its spread into the domestic economy, the Commonwealth Government has paid, or has undertaken to pay, a variety of cash bonuses including but not limited to the following payments:
- A payment of \$1,000 for each child in respect of whom Family Tax Benefit A is paid;
  - A payment of \$1,000 for any dependent child who receives a payment such as Youth Allowance);

- A payment of \$950 for each school-age child in respect of whom Family Tax Benefit A is paid;
  - A payment of \$900 for each family eligible for Family Tax Benefit B; and
  - A payment of \$900 for all eligible taxpayers who earned less than \$100,000 in 2007-08.
92. Many low and middle income households will receive more than one payment. For example for a single-income family with two pre-school age children, payments totaling \$3,800 either will have been paid or will shortly be paid. If the children were of school age, the total cash bonuses will total \$5,700.
93. The following examples illustrate the impacts of the cash bonuses on household disposable incomes:
- For a single person earning the FMW the \$900 payable as a cash bonus will represent a 3.4% boost to annualised disposable income. Over a year it is equivalent to a pre-tax wage increase of in excess of \$20 per week.
  - For a single income earner on the FMW with a spouse and two pre-school age children, the bonus payments of \$3,800, represent a 9.1% boost to annualised disposable income. Over a year, it is equivalent to a pre-tax wage increase of in excess of \$85 per week.
94. Ai Group submits that in considering any changes to minimum wages, the Fair Pay Commission should also consider the favourable impacts of these payments on the disposable incomes of low and middle income earners.

## Prospective Changes to Income Taxation

95. Ai Group, along with a number of other organisations, has proposed that as part of the May 2009 Budget the Commonwealth Government should reduce personal taxation by more than the reductions in personal taxation that are already scheduled to take effect from July this year. In Ai Group's *Submission to the 2009-10 Federal Budget*, for example, we proposed that:

- The Low Income Tax Offset be increased from its current level of \$1,200 to \$1,500 from 1 July 2009. As discussed above, the LITO is already scheduled to increase to \$1,350 from 1 July 2009;
- The 30% threshold be increased from its current level of \$34,000 to \$37,000 from 1 July 2009. As discussed above, this threshold is already scheduled to increase to \$35,000 from 1 July 2009.

96. These changes would roughly double the income tax reductions that are currently scheduled to take effect from 1 July 2009.

97. The Tables that follow show the impacts on household disposable incomes of the tax changes we have recommended together with changes to Family Tax Benefit A and B as discussed above and an increase in the FMW of \$8 per week. **Table 6** shows these impacts for a single-income earner and **Table 7** shows the impacts for a single-income household with two young children.

**Table 6 - Impact of an \$8 per week Wage Increase and Income Tax Changes  
(Single Income Earner)**

<b>Current Wage Income*</b>	<b>Change in Disposable Income</b>			
	<b>Tax Change Only</b>		<b>Tax and Wage Change</b>	
<b>\$ pw</b>	<b>\$ pw</b>	<b>%</b>	<b>\$ pw</b>	<b>%</b>
380.00	5.75	1.6%	10.51	2.9%
410.00	5.75	1.5%	10.88	2.8%
440.00	5.75	1.4%	11.26	2.7%
470.00	5.75	1.3%	11.63	2.6%
500.00	5.75	1.2%	12.01	2.6%
530.00	5.75	1.2%	12.38	2.5%
543.78	5.75	1.1%	12.55	2.5%
550.00	5.75	1.1%	12.55	2.5%
580.00	5.75	1.1%	12.23	2.3%
610.00	5.75	1.0%	12.23	2.2%
640.00	5.75	1.0%	12.23	2.1%
670.00	8.44	1.4%	14.92	2.5%
700.00	12.94	2.1%	19.42	3.1%
730.00	14.38	2.2%	19.66	3.1%
760.00	14.38	2.2%	19.66	3.0%
790.00	14.38	2.1%	19.66	2.9%
820.00	14.38	2.0%	19.66	2.8%
850.00	14.38	2.0%	19.66	2.7%
880.00	14.38	1.9%	19.66	2.7%
910.00	14.38	1.9%	19.66	2.6%
940.00	14.38	1.8%	19.66	2.5%
970.00	14.38	1.8%	19.66	2.5%
1,000.00	14.38	1.8%	19.66	2.4%
1,030.00	14.38	1.7%	19.66	2.3%

\* For wage levels below the FMW, it is assumed that the increase in wages is of the same proportion as the increase in the FMW (for example if the person was working less than standard hours at the FMW wage rate).

**Table 7 - Impact of an \$8 per week Wage Increase, Income Support and Tax Changes  
(Single income household with two young children)**

<b>Current Wage Income*</b>	<b>Change in Disposable Income</b>			
	<b>Tax and Income Support** Changes only</b>		<b>Tax, Income Support and Wage Changes</b>	
<b>\$pw</b>	<b>\$ pw</b>	<b>%</b>	<b>\$ pw</b>	<b>%</b>
280.00	10.40	2.0%	14.52	2.8%
330.00	14.43	2.6%	18.56	3.3%
380.00	14.43	2.4%	19.19	3.2%
430.00	14.43	2.2%	19.81	3.1%
480.00	14.43	2.1%	20.44	3.0%
530.00	14.43	2.0%	21.06	2.9%
543.78	14.43	1.9%	21.23	2.9%
550.00	14.43	1.9%	21.23	2.8%
600.00	14.43	1.8%	20.91	2.7%
650.00	14.43	1.7%	20.91	2.5%
700.00	21.62	2.5%	28.10	3.3%
750.00	23.06	2.6%	28.34	3.2%
800.00	24.58	2.6%	29.86	3.2%
850.00	27.83	2.9%	31.51	3.3%
900.00	27.83	2.9%	31.51	3.2%
950.00	27.83	2.8%	31.51	3.2%
1,000.00	27.83	2.7%	31.51	3.1%
1,050.00	27.83	2.7%	31.51	3.0%
1,100.00	27.83	2.6%	31.51	3.0%

\* For wage levels below the FMW, it is assumed that the increase in wages is of the same proportion as the increase in the FMW (for example if the person was working less than standard hours at the FMW wage rate).

\*\* Income support changes do not include changes in Rent Assistance.

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

98. Ai Group maintains that in looking at the capacity of the low paid to obtain and remain in employment the Commission should:

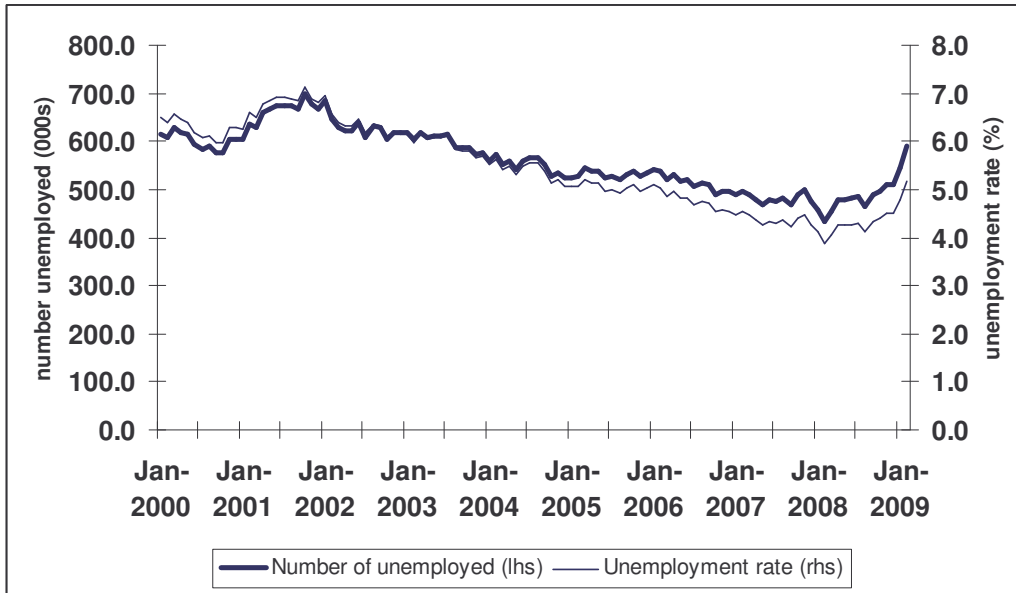
- Take close account of the accelerating increase in both the unemployment rate and the number of people unemployed over the past year; and
- Note the persistently high underutilisation of labour in Australia – with barely any sustained inroads made into Australia’s rate of underemployment over the past dozen or so years despite the extended growth phase.

99. In addition, Ai Group remains of the view that, while wage rates have an important role to play in inducing labour supply, there is very little reason for the Fair Pay Commission to use adjustments in minimum wage rates to induce labour supply.

### Unemployment

100. Official unemployment data record that, over the past year, both the number of people unemployed and the rate of unemployment have risen. This development reverses the strong inroads that have been made into unemployment over recent years. The number of unemployed people has risen particularly strongly. After reaching a low point at the beginning of 2008, the number of people unemployed had returned quickly to mid-2003 levels in February 2009.

**Chart 8: Australian Unemployment, January 2000 to February 2009  
(seasonally adjusted data)**



Source: ABS 6202.0, February 2009.

101. With official unemployment continuing to accelerate upwards, Ai Group urges the Fair Pay Commission to consider very closely the potential for its 2009 decision to exacerbate these very serious developments.

### **Labour Underutilisation**

102. Ai Group welcomes the Fair Pay Commission's receptiveness to the arguments put by Ai Group and others that, in assessing the impacts of the capacity of the low paid to obtain and remain in employment, all dimensions of labour underutilisation, and not just official unemployment, should be taken into account.

103. Broader measures of labour underutilisation record important features of the labour market that are not covered by official unemployment data. These include:

- part time workers who would like to work more hours;

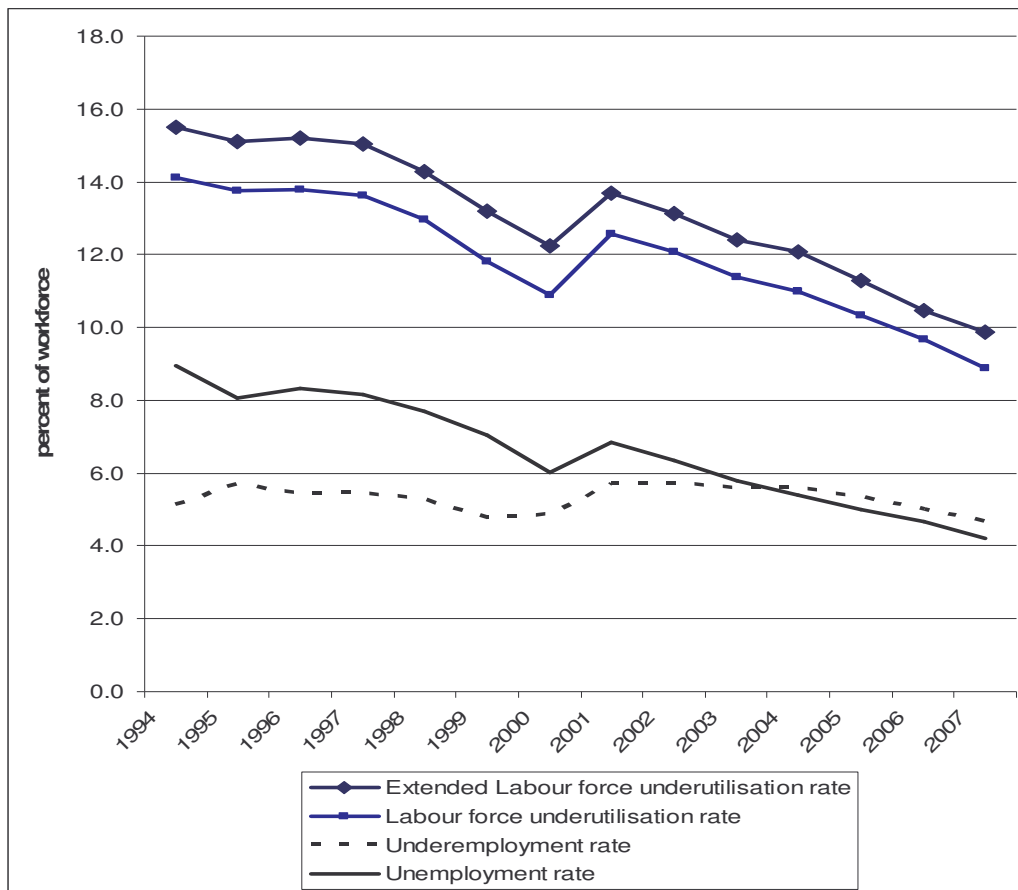
- full-time workers who are involuntarily only working part-time at the time of the ABS labour market surveys; or,
  - people marginally attached to the labour force such as discouraged jobseekers and people who are actively looking for work but would not be ready to start work within one week.
104. Ai Group expects 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.
105. As **Chart 9** below 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”.
106. A disturbing feature of the measures of labour underutilisation presented in **Chart 9** is that, over the period from 1994 to 2007, no sustained inroads were made into the rate of underemployment. In effect, the long phase of economic growth that has now come to an end saw virtually no reduction in underemployment.
107. The ABS publishes extended labour force underutilisation data only on an annual basis. In April 2009 data will be available for the period to September 2008 which is just prior to the more decisive acceleration of the deterioration of the labour market set in.
108. Fortunately the ABS also publishes quarterly labour force underutilisation rates (QLFUR) (unemployed plus the underemployed as a proportion of the labour force). In its January 2009 release of *Australian Labour Market Statistics* (ABS 6105.0), it identified the QLFUR as “an increasingly important indicator of spare capacity in the labour market.” It went on to note that:

*In seasonally adjusted terms the QLFUR was 10.8% in November 2008, an increase of 0.9 percentage points from August 2008 (9.9%). This was the largest quarter to quarter movement of the seasonally adjusted data since the*

series started in May 2001. As a result of this increase, the trend QLFUR was 10.6% in November 2008, an increase of 0.5 percentage points from the trend series low observed in May 2008 (10.1%), indicating a turning point in the series.

109. These data are preliminary at this stage and may well be revised in the near future.

**Chart 9: Measures of Labour Underutilisation in Australia 1994 to 2007**



- (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, April 2008.

110. On the basis of the ABS's most recent *Labour Force* report (ABS, 6202.0) Ai Group expects the underemployment rate to rise sharply in the near term. Since August 2008 the number of people employed full time has been trending downwards (with a total fall of 61,400 between August 2008 and February 2009). Over the same period part-time employment has been rising (by a total of 80,100) unemployed.

**Table 8 - Changes in Employment August 2008 to February 2009  
(trend data)**

<b>Change in employment between August 2008 and February 2009 (thousands)</b>	<b>Male</b>	<b>Female</b>	<b>Total</b>
Full-time employment	-49.7	-11.7	-61.4
Part-time employment	+26.5	+53.6	+80.1
<b>Total</b>	<b>-23.2</b>	<b>+42.0</b>	<b>+18.7</b>

Source: ABS, Labour Force, (6202.0), March 2009.

111. This is likely to reflect a number of developments:

- Businesses negotiating reduced work hours with employees;
- Individuals losing full-time work and taking up part-time positions; and
- More spouses entering the workforce to make up for a reduction of income (or the possibility of a reduction in income) earned by their partners.

112. The first two of these developments will not be revealed in official measures of unemployment but are likely to be revealed in measures of underemployment. The latter development may well account for a distinct share of the overall increase in total employment since August 2009.

113. These trends support considerable anecdotal evidence about recent changes in employment patterns. They point to the likelihood that recorded underemployment will rise sharply in the period ahead.

## **Changes to Minimum Wage Levels and Encouraging Labour Supply**

114. Ai Group encourages a close consideration of the argument that minimum wages should be set at a level sufficient to encourage labour force participation.
115. We note that, subject to sufficient productivity, 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 minimum wage rates.
116. 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 minimum wages are 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. Minimum wages are not relevant to these transactions.
117. There is no shortage of evidence of employers' willingness to offer wages that are above minimum levels. (In light of the labour force underutilisation rates discussed above, nor does there appear to be strong evidence of a lack of supply of labour at current minimum wage levels.)
118. In light of the existence of adequate market-based incentives for employers to induce labour force supply, Ai Group remains of the view that there is no strong reason for wage-setting decisions to assess whether minimum wage rates will be sufficient to induce adequate labour supply. If they are not, employers will offer wage rates that are above the minimum level.

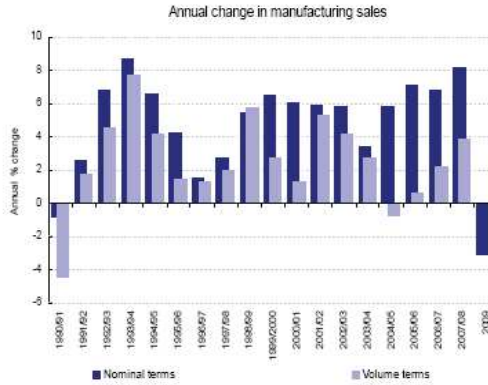
# Annexure A – Extracts from Ai Group and Deloitte’s *National CEO Survey - A tough year ahead*

## Business prospects for manufacturing in 2009

### Manufacturing sales and employment to decline

#### Sales

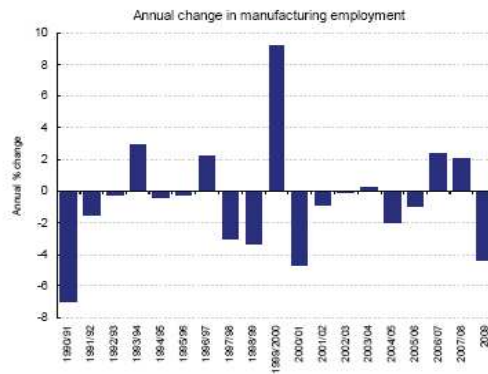
- Nominal sales (based on ABS data) grew strongly in manufacturing over the last four financial years.
- In 2007/8 sales rose by 8.2%. However, after taking into account price increases, the sector experienced an overall 3.8% rise in sales volumes, still a significant improvement on the previous two years.
- Prospects for 2009 appear set to deteriorate, as companies anticipate sales to decline for the first time in 18 years, by 3.1% to around \$380 billion. The global economic crisis, weak domestic demand, declining exports and shelved investment plans are combining, as in other developed nations, to squeeze manufacturing.
- Adjusting for goods inflation would see sales decline even further in volume terms.



Manufacturing sales to decline by 3.1% in nominal terms ...

#### Employment

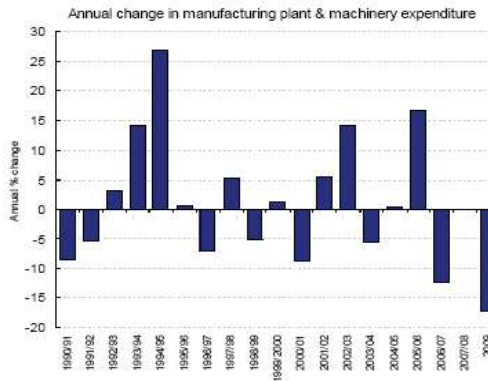
- Employment in manufacturing is forecast to fall by 4.4% in 2009, continuing the trend that emerged in the second half of 2008 as the global economic crisis started to impact on industry.
- This trend will see the gains in manufacturing employment (of over 46,000 new jobs) made over the last two financial years wiped out. Employment in 2009 is expected to fall to around 1.06 million.
- The forecast decrease reflects the expectation of negative domestic demand conditions, as well as company restructuring to reflect the changed outlook.



Employment is forecast to decline by 4.4% ...

#### Investment in plant and machinery

- Reflecting the negative sales conditions expected in 2009, manufacturers are planning to scale back appreciably their expenditure on new plant and machinery.
- ABS data shows that manufacturing investment activity can change substantially from year to year. A weak fall in investment in 2007/8, for example, was preceded by a sharp decline of 12.3% in 2006/7 and a strong surge in investment in 2005/6.
- In 2009, investment in new plant and equipment is expected to decline by 17.2%. Nevertheless, a total of \$7.6 billion is expected to be invested in new plant and machinery.



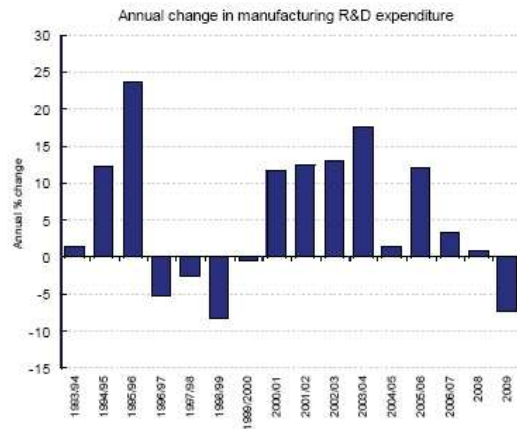
New investment is forecast to decline by 17.2% ...

## Business prospects for manufacturing in 2009

### Manufacturers propensity to invest in R&D has waned

#### Research and development

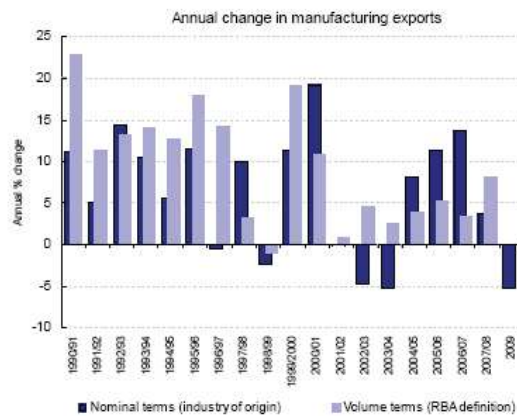
- The latest official ABS data for 2006/7 shows that research and development (R&D) spending by manufacturing rose by 3.3%. In recent years the strong gains in R&D expenditure evident in the period between 2000/1 to 2003/4 have been maintained through ongoing growth, albeit at generally lower rates.
- In 2008, the forecast<sup>1</sup> is for this trend to continue with R&D spending rising by only 0.8%. This is despite strong sales growth in both nominal and volume terms, suggesting that manufacturers' propensity to invest in R&D has waned over recent years.
- The impacts of the current slowdown are clearly evident in the 2009 forecast. Manufacturing expenditure on R&D is expected to decline by 7.3% as firms cut back to preserve margins.



Research and development expenditure to decline by 7.3% ...

#### Exports

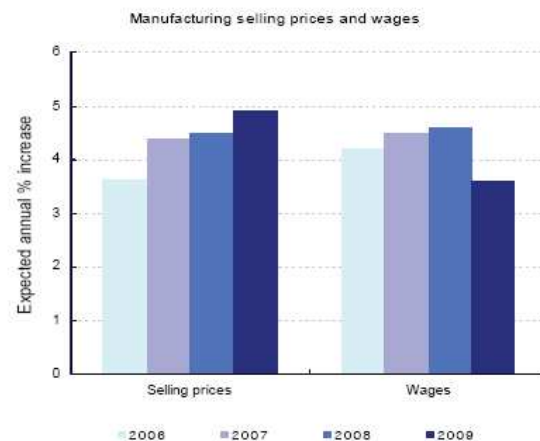
- In nominal terms, manufacturing exports grew strongly between 2004/5 and 2006/7, but slowed in 2007/8 as the high Australian dollar impacted on earnings and market share. However, in volume terms, export growth in 2007/8 was the strongest in seven years.
- Manufacturers are forecasting exports in nominal terms to fall by 5.3% to \$84 billion in 2009 (based on industry of origin).
- Despite the Australian dollar falling to levels not seen since 2003 (improving earnings), the forecast reflects the fact that many of Australia's trading partners are in recession and export demand is likely to remain weak under these conditions.



Exports sales in nominal terms to fall by 5.3% ...

#### Selling prices and wages

- Manufacturers expect selling prices to rise by 4.9% on average in 2009, an increase on the 4.5% rise predicted for the previous year.
- The pressure to lift prices reflects two possible factors, the impact of the lower Australian dollar on overseas sourced inputs (which have grown in importance over the last five years) and a desire to offset expected losses in sales.
- The expectation for average wage growth in 2009 fell from 4.6% in 2008 to 3.6% in 2009. This is in line with the weaker outlook for jobs, with manufacturing employment forecast to decline.



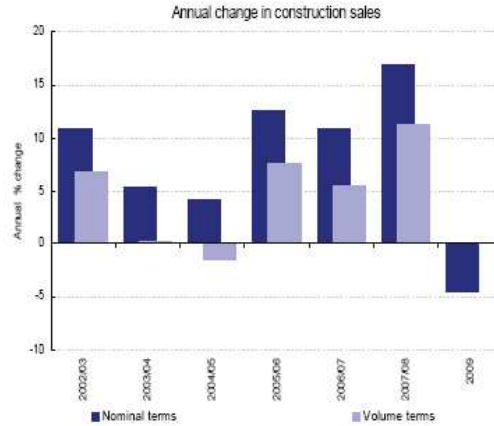
Wage growth expected to moderate to 3.6% ...

## Business prospects for construction in 2009

### Construction activity forecast to decline

#### Sales

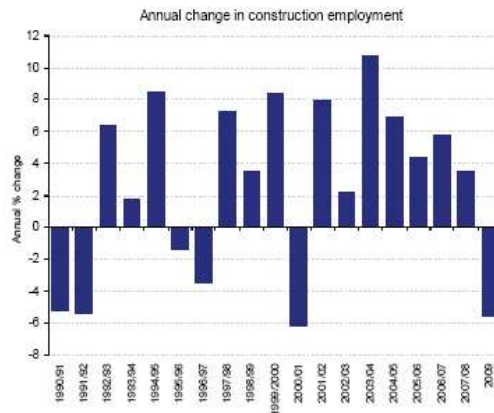
- Nominal sales (based on ABS data) grew strongly in construction over the last three financial years.
- In 2007/8 sales rose by 16.8% (and 11.2% in volume terms). This outcome reflected the resources boom, strong infrastructure spending and solid commercial construction activity, despite a softer housing and apartment market.
- Prospects for 2009 are forecast to be the weakest in over eight years, with nominal sales to fall by 4.5%. Total construction sales are estimated to be around \$145 billion in nominal terms.
- Adjusting for goods inflation would see sales decline even further in volume terms.



Nominal sales to fall by 4.5% ...

#### Employment

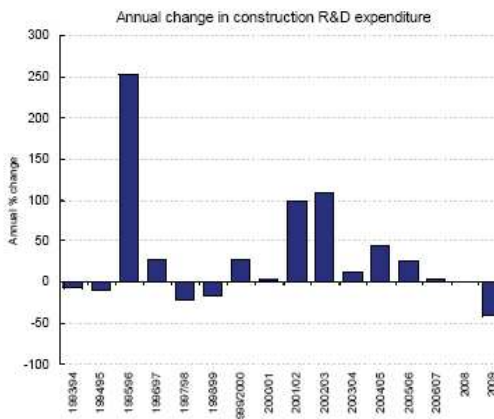
- After seven years of strong employment growth (which saw the number of jobs rise by over 320,000), employment in construction is set to fall by 5.6% in 2009.
- Total employment is expected to be 920,000, a decline of over 55,000 on 2008.
- The forecast decrease reflects expectations of continued weak demand for new house and apartment building, along with commercial construction. While government infrastructure expenditure is likely to accelerate, reduced demand in the resources sector, will partly offset these gains.



Construction employment to fall by 5.6% ...

#### Research and development

- Expenditure on R&D in the construction sector can swing widely from year to year.
- The latest official ABS data for 2006/7 shows that R&D spending in construction rose by 3.5%.
- The forecast for 2009 will see expenditure on R&D decline substantially, by 40.7%, as firms cut back to preserve margins.
- There is no forecast available for R&D expenditure in 2008.



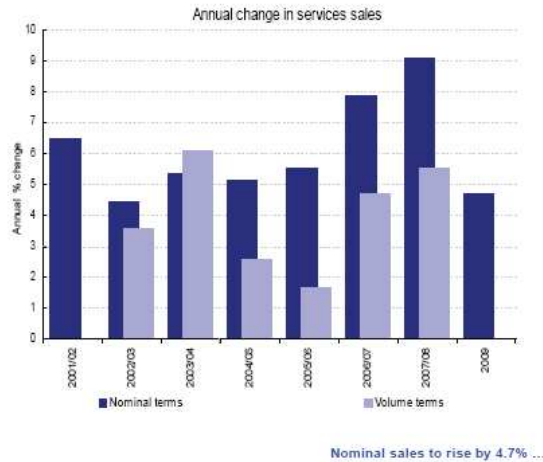
Expenditure on R&D forecast to fall by 40.7% ...

## Business prospects for services in 2009

### Services activity forecast to moderate but remain positive

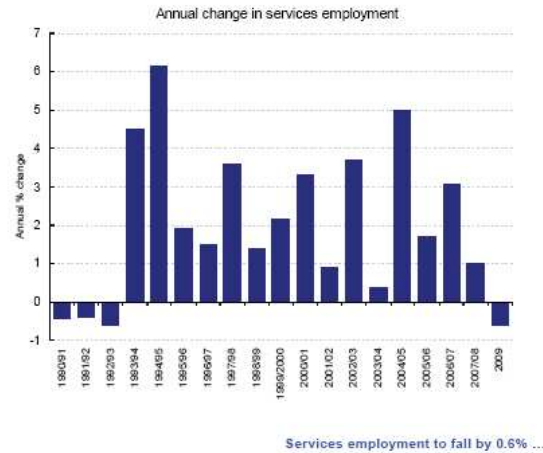
#### Sales

- Nominal sales growth (based on ABS data<sup>2</sup>) has been exceptionally strong in services over the last two financial years.
- In 2007/8 sales rose by 9.1% (and 5.5% in volume terms). The strong outcome reflected a range of factors, including the resources boom, strong consumer spending and credit growth (at least up to the middle of the financial year) and the terms of trade effect on national income.
- Prospects for 2009 are more restrained, in line with earlier years, with nominal sales to rise by 4.7% to around \$1,150 billion.
- Adjusting for services inflation would see sales growth lower in volume terms.



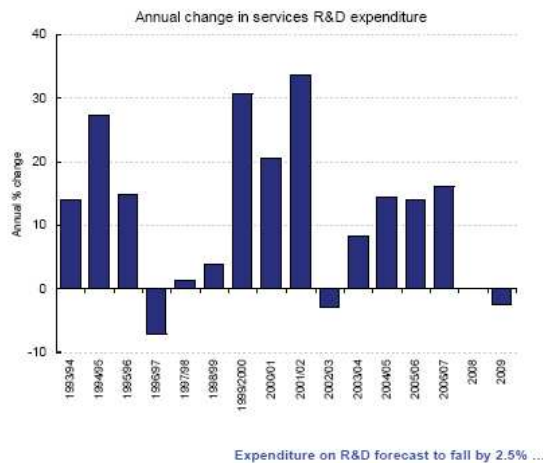
#### Employment

- Following 15 consecutive years of jobs growth in services, employment looks set to fall in this sector in 2009.
- The forecast decrease reflects expectations of continued weak demand for services from households and businesses in the wake of the global economic crisis.



#### Research and development

- Expenditure on R&D in the services sector has been growing steadily since 2003/4.
- The latest official ABS data for 2006/7 shows that R&D spending by services rose by 16.1%.
- The forecast for 2009 suggests expenditure on R&D will decline by around 2.5%, reversing the trend of previous years.
- There is no forecast available for R&D expenditure in 2008.



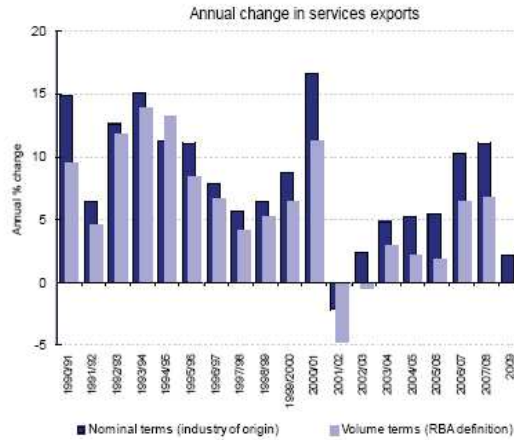
<sup>2</sup>Note, service sector sales data for 2001/2 is based on ABS experimental series

## Business prospects for services in 2009

*Services exports will continue to grow, although at a slower pace*

### Exports

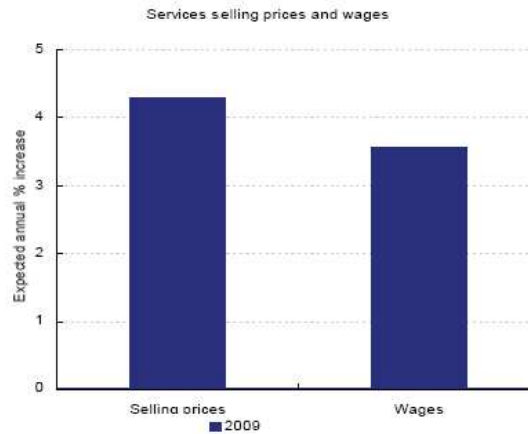
- In both nominal and volume terms, services exports have grown steadily over the last six financial years, particularly in the last two years with growth in excess of 10% in nominal terms.
- Services companies are forecasting export growth in nominal terms to slow to 2.2%, bringing total exports in 2009 to around \$52.5 billion.
- This is a reasonably positive forecast given the likelihood of weaker earnings in tourism and financial services exports.



Export earnings forecast to rise by 2.2% ...

### Selling prices and wages

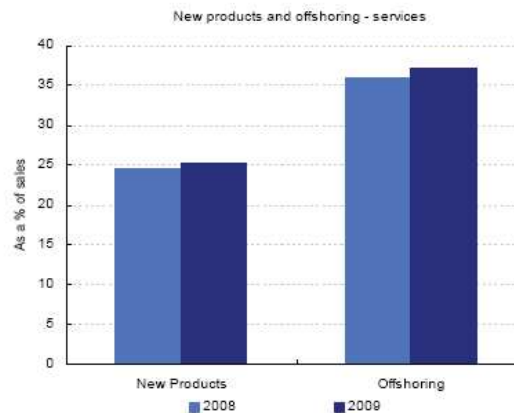
- Selling prices in the services sector are forecast to rise by 4.3% on average in 2009, slightly below the 4.6% increase (ABS data) seen in 2007/8.
- The expectation for average wage growth is 3.6% in 2009. This is in line with the weaker outlook for jobs, with services employment forecast to decline.



Selling prices forecast to rise by 4.3% ...

### New products and offshoring

- New product intensity (the percentage of sales derived from new products introduced in the last three years) is forecast to lift marginally from 24.5% in 2008 to 25.3% in 2009.
- The level of offshore intensity (offshore activity as a percentage of sales) is also forecast to rise from 35.9% in 2008 to 37.2%.



New product intensity to lift marginally to 25.3% ...

**Annexure B - Ai Group's *Submission to the 2009-10 Federal Budget***