



Australian Government

**Australian Government
Submission**

to the

**Fair Work Commission
Annual Wage Review 2016**

6 April 2016

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Acronyms and abbreviations

ABS	Australian Bureau of Statistics
ACCI	Australian Chamber of Commerce and Industry
ASX	Australian Stock Exchange
CPI	Consumer Price Index
EEH	Employee Earnings and Hours
FT	Full-time
GDP	Gross Domestic Product
HILDA	Household, Income and Labour Dynamics in Australia
LNG	Liquefied Natural Gas
MYEFO	Mid-Year Economic and Fiscal Outlook
NMW	National Minimum Wage
NSA	Newstart Allowance
OECD	Organisation for Economic Co-operation and Development
PPP	Parenting Payment Partnered
PPS	Parenting Payment Single
PT	Part-time
RBA	Reserve Bank of Australia
SME	Small and/or medium enterprise
UK	United Kingdom
US	United States
YA	Youth Allowance

1 The Australian Government's Position

1. The Australian economy continues to perform well, transitioning from strong resource investment-led growth to broader-based drivers of economic activity. Employment growth has strengthened and conditions conducive to stronger business investment are in place. However, the 2016 Annual Wage Review takes place during a period of ongoing economic transition, as the economy adjusts to the fall in the terms of trade.
2. During this transition, the unemployment rate of 5.8 per cent remains above the last decade's troughs, but it has declined by 0.5 percentage points over the last 12 months. The youth unemployment rate is 12.2 per cent as of February 2016.
3. As discussed in the *2015-16 Mid-Year Economic and Fiscal Outlook*, risks to the global outlook are elevated, with the world economy struggling to regain sustained momentum. The significant transitions underway in the global economy, while welcome, may not be smooth in practice. China's shift from investment-led growth to a greater reliance on consumption and services has implications for regional and global activity, while also presenting new opportunities for Australian businesses.
4. Long-term unemployment is higher than the level recorded prior to the global financial crisis (23.2 per cent of the unemployed in February 2016). The Expert Panel for Annual Wage Reviews ('the Panel') should take into account the need to help long-term unemployed people enter the workforce, noting that low-paid employment is an important 'stepping stone' to sustained employment and higher paying jobs.
5. Aggregate wages continue to grow. Growth, whilst positive, remains low by historical standards (2.2 per cent over the year to December 2015). Moderate wages growth occurs in the context of low consumer price inflation. Headline inflation is 1.7 per cent through the year to December 2015.
6. Wage flexibility is an important mechanism to support employment during this ongoing structural adjustment. Employment growth is driven by a range of factors, including the cost of wages, the broad economic environment and specific business conditions. Indeed, moderate wage growth has been helping to support employment. Wage increases that are not supported by higher productivity or higher prices for customers and consumers will most likely cost jobs.
7. Excessive increases in minimum wages are likely to reduce employment in award-reliant industries, particularly for youth, and especially when wages growth elsewhere in the economy remains moderate. While one wage decision may not have a large effect on employment, the cumulative impact of multiple decisions will be greater. The Panel should carefully consider the potential long-term impacts of its successive decisions on employment.
8. Being in work has significant benefits for individuals and households, providing higher incomes and higher levels of personal wellbeing, as well as significant flow-on benefits for the community in terms of lower spending on welfare and health. Long-term unemployment can be particularly damaging to people's motivation, skills, future earnings potential and retirement income, magnifying the costs of unemployment to the community. For youth,

unemployment can permanently reduce earnings potential with flow-on effects for lifetime outcomes, incomes and for overall economic growth.

9. Furthermore, in 2014, under Australia's presidency, G20 leaders agreed to reduce the gap between male and female participation rates by 25 per cent by 2025. The Government is working to achieve this ambitious goal through a range of strategies, including accessible, affordable and flexible child care, supporting women out of the workplace to become job-ready, and supporting small business to generate more jobs.
10. The minimum wage and award classification wages are part of Australia's comprehensive safety net of workplace relations policies and transfer payments although only a small number of employees are paid the national minimum wage rate. However, given that low-paid work is temporary for a majority of low-paid workers and serves as a pathway to sustainable higher paid work, increasing the national minimum wage is not an efficient way to address relative living standards or the needs of the low-paid. For low-income households, the tax-transfer system provides considerable redistribution of income. In fact, low-paid employees are often found in high-income households.
11. There is ongoing uncertainty around the economic outlook, as the economic transition out of the mining boom continues, and as economic rebalancing continues in China. The Productivity Commission's report on the Workplace Relations Framework encouraged the Panel to take more account of the risk of variations in economic performance across the country in the Annual Wage Review.
12. In this complex and uncertain economic and labour market environment, the Panel should take a cautious approach, taking into account the risks to the economic outlook and the need to boost employment and job creation, as well as maintaining wages for those on the minimum wage and those on award classification wages.

1.1 Minimum and award classification wages and the low-paid

13. The Panel's decision impacts 122 modern awards, incorporating over 2,000 adult rates of pay, not just those on the national minimum wage. Around 1.9 million Australians are paid an award rate as of May 2014. Of these 1.9 million, the majority (66.0 per cent) are not low-paid and approximately 18.2 per cent are paid more than the median hourly wage (of \$28.00 per hour as at May 2014). The Panel should keep in mind the diversity of award classification wages which range from the current national minimum wage, approximately \$34,000 per year, up to around \$162,000 per year (*Air Pilots Award 2010*).
14. The Department of Employment estimates that in May 2014 (latest data) less than 2 per cent of all employees, or 157,100 employees, were paid the national minimum wage rate, while almost 19 per cent of employees are on award classification rates.¹ In recent years, Annual Wage Review decisions have flowed through to all award classification wages at the same percentage as the increase in the national minimum wage.
15. Even among the low-paid, household financial situations are diverse. Minimum wage increases have a limited and uncertain effect on income inequality, noting that a significant

¹ Some employees paid the national minimum wage rate are award-reliant.

proportion of the low-paid are members of higher-income households - with only 16.9 per cent of low-paid workers in the bottom two household income deciles, and 14.4 per cent in the top two household income deciles.

1.2 Economic environment

16. The global economy is expected to improve modestly and the Australian economy is continuing to transition to broader-based drivers of economic activity (Chapter 3). The outlook as presented in the *2015-16 Mid-Year Economic and Fiscal Outlook* is for a gradual improvement in real GDP growth.
17. The transition from resource investment-led growth towards broader-based drivers of economic activity is underway, supported by historically low interest rates, the fall in the Australian dollar and lower oil prices. Employment growth has strengthened recently as the economy transitions to more labour intensive sectors such as services and has been supported by moderate wage growth. Business investment intentions currently remain subdued, but conditions conducive to stronger business investment are in place.
18. Risks to the global outlook are elevated, with significant transitions underway. China's shift towards a greater reliance on consumption and services has implications for global activity and commodity prices, while decisions around the normalisation of monetary policy in the United States (US) from near-zero interest rates have the potential to contribute to financial market volatility. The Productivity Commission's report on the Workplace Relations Framework encouraged the Panel to take more account of the risk of variations in economic performance in the Annual Wage Review.
19. Wage growth remains moderate, which continues to support employment outcomes and help the economy more generally in its adjustment to broader-based growth. In making its decision, the Panel should have regard to the role of wage flexibility during this period of economic transition.
20. Recent moderate growth in wages and continuing low inflation suggest that employers will continue to find it difficult to afford wage increases, particularly if competition on prices makes it harder to pass on cost increases.
21. Labour market conditions in Australia have improved (Chapter 4). Australia's unemployment rate has edged lower over the last 12 months – the unemployment rate stood at 5.8 per cent in February 2016, down from 6.3 per cent in February 2015. The unemployment rate is currently forecast to remain around 6 per cent through 2016-17.
22. The latest annual data show that over the past five years, labour productivity growth in the market sector was higher than the five years prior (2.1 per cent and 1.6 per cent respectively) (Chapter 6). However, the Panel should note that productivity data can be volatile and subject to revision.
23. Enterprise bargaining provides a direct avenue for firms and workers to negotiate productivity improvements to support wage increases. The Reserve Bank of Australia (2015) has noted that some employees seem willing to trade off wage increases for job security in the current period of subdued economic performance.
24. Award-reliant employees are more likely to work in small businesses (Chapter 5). Small businesses also currently face challenging trading conditions, and some business surveys

indicate that many small businesses are reducing the size of their workforces. In making its decision, the Panel needs to carefully consider the impact on small businesses, in order to ensure their ongoing viability and growth, which will in turn support employment. Small businesses are significant employers, employing around 44 per cent of non-financial private sector employees and 38 per cent of employees on award classification wages.

1.3 Minimum and award classification wage impacts

1.3.1 Impacts on employment

25. The economic literature on the impacts of minimum wages is complex and contested. However, economists generally concur that beyond a certain level, excessive increases in minimum wages are likely to have deleterious effects on employment, particularly for young people and the low-skilled. Research on minimum wages and employment growth also tends to suggest that these effects are greater in periods of subdued economic performance (Chapter 7).
26. Many young and low-skilled people are already finding it difficult to get a job, and long-term unemployment remains higher than the level recorded prior to the global financial crisis. Excessive increases in the minimum wage and award classification wages are likely to impact on employment and/or inflation, and make it harder for the long-term unemployed and young people to get into the labour market.
27. Low-paid and low-skilled employment often serves as an important entry point to the workforce and a stepping stone to higher paid employment. Using the *Household, Income and Labour Dynamics Australia* (HILDA) survey, more than half of those who are low-paid in one year move into a higher paying job the following year.
28. The Panel's decision should balance an appropriate concern for the needs of the low-paid and award-reliant employees against the need to support job opportunities for long-term unemployed people, the low-skilled and young people.

1.3.2 Impacts on inequality

29. According to the inequality researcher Peter Whiteford (2014), "*The most important source of inequality in Australia is whether you have a job or not*".
30. Inequality has risen across the developed world in recent decades, driven in large part by strong growth in wages for high skilled jobs. But the minimum wage and award classification wage rates have not been a key factor driving higher inequality, either in Australia or internationally.
31. The rise in household income inequality in Australia has been less dramatic than in other English-speaking countries, particularly the United States (Chapter 8). Furthermore, the Australian tax-transfer system is highly targeted towards low-income households, particularly families with children.
32. In contrast, only part of an increase to the minimum wage and award classification wages flows through to employees when taxes and transfers are taken into account. The Government shares the view of the Panel's 2014 decision, which stated that "*increases in*

minimum wages are a blunt instrument for addressing the needs of the low-paid” (Paragraph 360).

33. Since many low-paid workers are in households in the top half of the income distribution, there are better ways to address inequality than increases in the minimum wage and award classification wages.
34. Similarly, the Panel’s decision on the minimum wage and award classification wages is not well suited to addressing the complex factors underlying gender pay inequity, since the gender pay gap is greatest among high-income earners. Furthermore, since they are a larger proportion of the low-paid, women are likely to be particularly at risk from any impacts on employment.

2 Minimum wage and low-paid workers

Key Points

- Relatively few Australians (around 157,100 or 1.6 per cent of employees in May 2014) are paid the national minimum wage rate of \$17.29 per hour.
- Most of the 1.9 million award-reliant workers are not low-paid (low-paid is defined as less than two-thirds of the median hourly wage).
- Low-paid workers have a diverse range of living standards and levels of household income. Nearly half of low-paid workers are in the top 50 per cent of household income.
- Increases in minimum and award wages are poorly targeted to improve low-paid workers' relative living standards and address the needs of the low-paid.

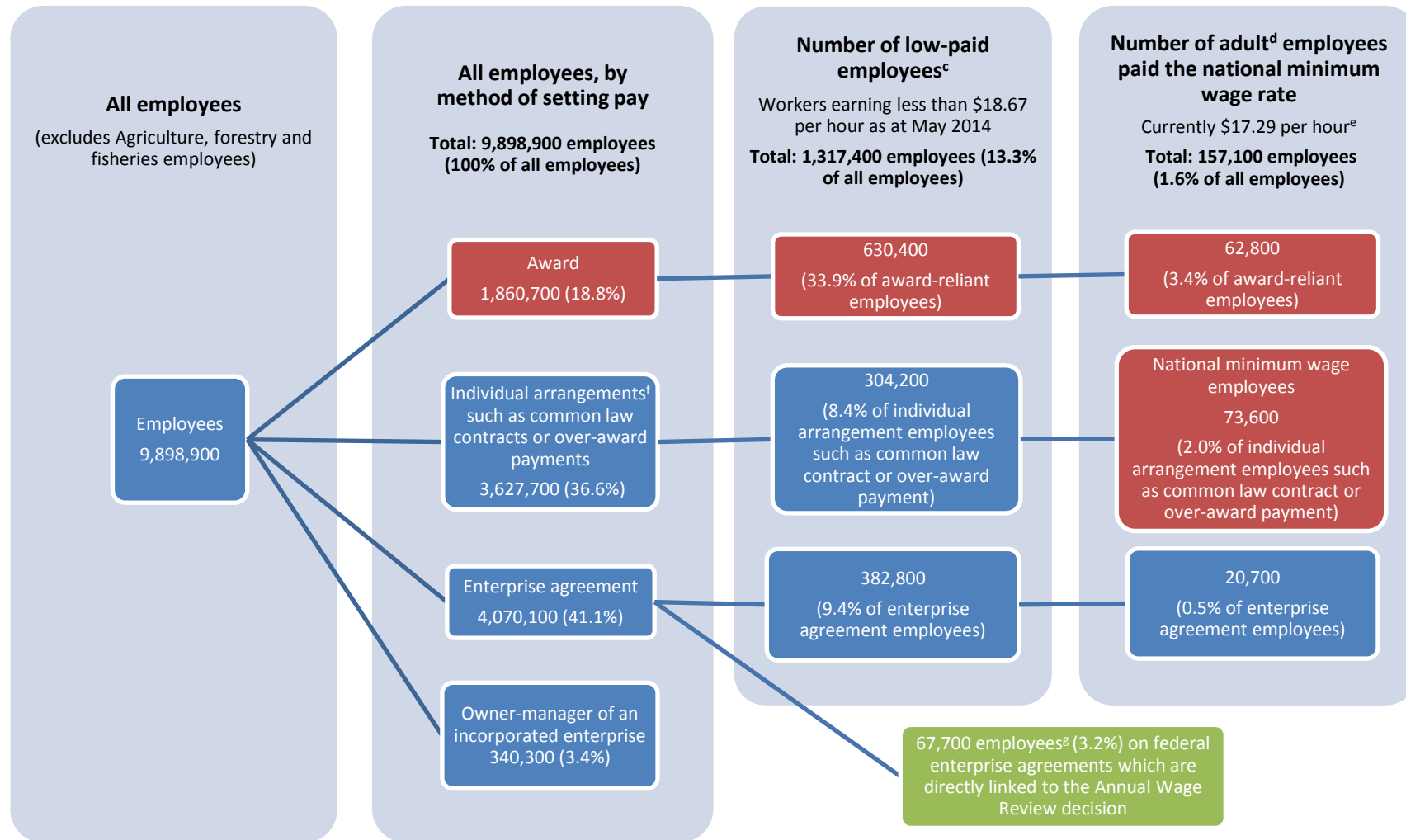
2.1 Coverage of the Panel's decision

35. Australia's minimum wage system is unique among developed countries. Australia not only has a national minimum wage but also 122 modern awards which set minimum wages and conditions in certain occupations and industries. There are around 2,000 adult award rates of pay across the hundreds of classifications in the modern awards and these rates of pay vary widely.
36. The Panel's decision will directly affect employees paid the national minimum wage and employees whose pay is set by a modern award. In the past five Annual Wage Reviews, the Panel has increased modern award wages by the same percentage increase as the national minimum wage. The wages of some other workers will also be affected by the Panel's decision, including workers paid close to the minimum wage and workers whose pay is set by a collective agreement which is linked to the outcome of the Annual Wage Review.
37. Chart 2.1 shows the number of Australian employees by how their pay is set. The Chart also shows how many of these employees are low-paid and how many are likely to be paid the national minimum wage rate.

2.1.1 National minimum wage employees

38. The national minimum wage is the lowest hourly rate of pay that can be paid to an adult employee. There are special national minimum wage rates for juniors, apprentices, trainees and workers with disability.
39. The adult national minimum wage is currently \$656.90 per week (\$17.29 per hour or \$34,158.80 per year). This is around 2.5 times the base rate of Newstart Allowance for singles (\$263.80 per week) and just above half of full-time median weekly earnings (\$1,200.00 per week, ABS 2015d).

Chart 2.1: Number of employees by method of setting pay and whether they are low-paid, May 2014(a)(b)



Source: ABS 2015e, *Employee Earnings and Hours, May 2014*, Cat. No. 6306.0, published and unpublished data (including Department of Employment calculations); Department of Employment 2015, *Workplace Agreements Database*, September 2015.

Note: (a) All numbers are for May 2014, except for the number of employees on agreements linked to the Annual Wage Review decision (in green), which is for 30 September 2015. (b) The Fair Work Commission sets award classification wages and the national minimum wage, these workers are coloured red in the chart. (c) Low-paid employees are defined as employees earning less than two-thirds of the median hourly wage. In May 2014, the median hourly wage was \$28.00 and employees earning below \$18.67 per hour were considered low-paid. (d) This excludes workers paid junior, apprentice and disability rates of pay. (e) The national minimum wage in May 2014 was \$16.37. Employees paid at or below \$16.50 per hour in May 2014 are considered to be paid the national minimum wage rate (this uses an upper error band of 13 cents). (f) The ABS classifies employees in the individual arrangement category if they have their pay set by an individual common law contract or arrangement, whether or not written, including where employees receive over-award payments. (g) This data is derived from the Workplace Agreements Database. It includes the number of employees covered by an agreement with a clause which states that the entirety of the Annual Wage Review decision will be applied in full and automatically to wages. These workers may also be low-paid or earning the national minimum wage rate and thus also covered in the boxes above.

40. Relatively few Australians have their pay set at the national minimum wage. Using the 2014 *Employee Earnings and Hours* survey, the Government estimates that around 157,100 Australian employees (1.6 per cent) are paid the national minimum wage rate.²
41. This is similar to estimates from the *Australian Workplace Relations Study* (Fair Work Commission 2015a) which shows that around one per cent of enterprises set at least one employee's pay using the national minimum wage and that less than one per cent of employees are paid the national minimum wage.

2.1.2 Award-reliant employees

42. In 2014, 18.8 per cent of Australian employees (or 1.9 million) had their pay set by an award. Award-reliant workers are diverse and work in a range of businesses. In its submission last year, the Government outlined a range of characteristics of award-reliant workers. In general, award-reliant workers tended to be:
 - Women
 - Working part-time
 - Casually employed
 - Working in small to medium sized businesses
 - Working as Community and personal service workers, Labourers and Sales workers
 - Working in the Accommodation and food services, Administrative and support services Retail trade, Other services, Health care and social assistance, Rental, hiring and real estate services and Arts and recreation services industries
43. There is a considerable spread in award wage rates. Award minimum wages range from the national minimum wage rate of \$656.90 per week up to \$3,114.52 per week (\$161,955.00 per year, *Air Pilots Award 2010*). The national minimum wage rate of \$656.90 per week features in just 45 of the 122 modern awards.³ In the remaining 77 modern awards, all wage rates are above the national minimum wage.
44. In the Government's submission last year, an 'award wage bite' measure was developed to compare the median earnings of full-time award-reliant workers to the median earnings of all full-time workers. In 2014, the median full-time award-reliant wage (\$1,001.00) was 74.8 per cent of the median full-time wage among all workers (\$1,338.00), reflecting that the vast majority of award-reliant workers are paid higher

² National minimum wage employees are classified as employees who are; (a) paid the adult rate, (b) non-managerial, (c) have their pay set through an unregistered individual arrangement, (d) with average ordinary time earnings of up to \$16.50 per hour. The earnings of casual employees are divided by 1.25 to adjust for the casual loading.

³ Of the 45 awards, 25 express the lowest adult wage rate as both the hourly national minimum wage of \$17.29 and the weekly national minimum wage of \$656.90, a further 19 refer only to the weekly rate and the remaining one states the lowest adult wage as an hourly amount. However, in one of these awards, workers may receive commission on top of the weekly national minimum wage, and in a further two awards, workers have shorter ordinary working hours resulting in a higher hourly wage than the national minimum wage. Also, in several of the 45 awards, the lowest rate is paid as an introductory rate or a trainee rate.

wages than the national minimum wage (56.2 per cent higher on average).⁴ The results also showed that the award wage bite had risen since 2010.

45. The increase in the award wage bite between 2010 and 2014, from 67.6 per cent to 74.8 per cent, may be due to compositional factors. For example, Department of Employment analysis using the *Employee Earnings and Hours* survey shows that from 2010 to 2014 there was large growth in the number of full-time award-reliant employees⁵ working in the Public administration and safety and Health care and social assistance industries. For both industries, this was accompanied by significant growth in median award wages relative to growth in median wages for all employees.

2.1.3 Other employees

46. Other employees may also be affected by the Panel's decision. For example:
- There will be wage implications for workers who are paid at or around the minimum wage, but have their pay set through an individual arrangement or collective agreement;
 - The minimum wage adjustment may be passed on to higher wage earners in order to maintain wage relativities;
 - Wage outcomes in many collective agreements are explicitly linked to Annual Wage Review outcomes. As of September 2015, there were 303,300 employees whose collective agreement was formally linked in some way⁶ to the Panel's decision. For 67,700 of these employees the link was direct and automatic.⁷

2.2 Who are the low-paid?

47. In reviewing and determining minimum award wages, the Panel must have regard to the relative living standards and needs of low-paid workers. In this submission, low-paid workers are defined as workers earning less than two-thirds of the median hourly wage. Using the May 2014 *Employee Earnings and Hours* data, workers earning below \$18.67 per hour are considered low-paid. This is similar to the \$18.42 per hour low-paid threshold set using the 2014 *Household, Income and Labour Dynamics in Australia* (HILDA) survey. Appendix A contains a detailed discussion of the methodology used by the Government to calculate the number of low-paid workers.
48. Government analysis using the *Employee Earnings and Hours* survey shows there were about 1.3 million low-paid employees in 2014, comprising 13.3 per cent of all employees. Around one-third of award-reliant workers were low-paid (see Chart 2.1).

⁴ ABS (2015e), *Employee Earnings and Hours*. The full-time median wage for award-reliant workers only includes non-managerial adults.

⁵ Refers to full-time adult non-managerial employees.

⁶ This includes agreements in which a) there is a reference to the operation of the Fair Work Act that employee wages will not fall below the minimum wage, or b) Annual Wage Review decisions will be passed on in part or full, or c) Annual Wage Review decisions will be taken into consideration during employee wage reviews.

⁷ This includes agreements in which the entirety of the Annual Wage Review decision is applied in full and automatically to wages.

49. In general, low-paid workers are more likely to be young, female, single or without children. They also have varied living standards and levels of household income with nearly half of low-paid workers in the top 50 per cent of household income.
50. Given this, minimum wage increases are not well-targeted at lifting the relative incomes of low-paid households, as wage increases will also be directed to well-off households. Furthermore, as discussed in Chapter 7, low-paid work is temporary for a majority of low-paid workers (in both low- and high-income households) and often serves as a stepping stone to higher paid work.
51. As also discussed in Chapter 8, minimum wage increases have a limited and uncertain effect on income inequality, noting that a significant proportion of the low-paid are members of higher-income households.

2.2.1 Characteristics of low-paid workers

52. Low-paid workers have a diverse range of characteristics. Analysis from the HILDA Survey shows that in 2014:
 - Low-paid workers were more likely to be female. About 56.3 per cent of low-paid workers were female, while 43.7 per cent were male.
 - Low-paid work tended to be concentrated among younger workers.⁸ Over half (55.5 per cent) of low-paid workers were aged under 30, with 15.9 per cent aged between 15 and 19 years old, and slightly above a quarter (27.4 per cent) in the 20 to 24 year old age cohort. About 11.6 per cent of low-paid workers were aged over 55 years old.
 - Around one in four low-paid workers were full-time students (26.0 per cent).
 - Low-paid workers lived in a broad range of household types. About 58.9 per cent of low-paid workers were single without children, 14.2 per cent were a member of a couple with children, 22.4 per cent were a member of a couple without children and 4.6 per cent were single parents.⁹
 - Low-paid workers were more likely to be casuals. About 61.7 per cent of low-paid workers were casuals, while 38.3 per cent were permanent employees. Casual employees are paid a loading of typically 25 per cent. This means that casual employees paid at the national minimum wage of \$17.29 per hour receive \$21.61 per hour once the casual loading is included.
53. Further detailed characteristics of low-paid workers, including occupation, industry and education are listed in Appendix A.

2.2.2 Low-paid workers and household income

54. The living standards of low-paid workers are determined not just by personal earnings from work, but also through the earnings of other household members and the impacts

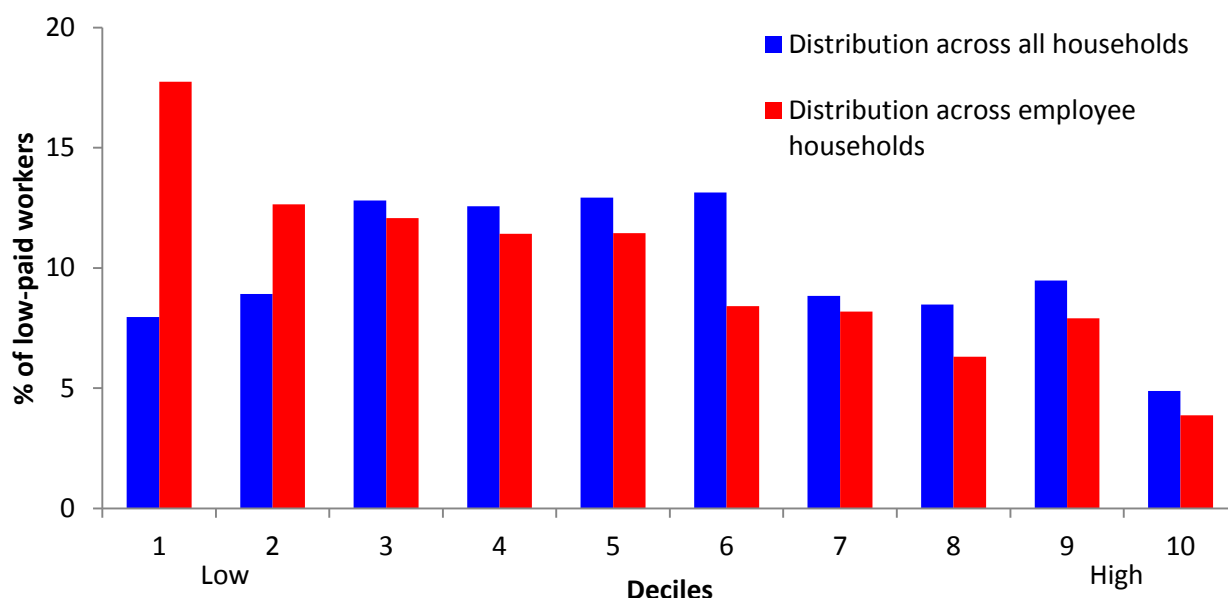
⁸ Low-paid thresholds for workers aged under 21 have been deflated by the relevant junior minimum wage rates. See Appendix A for further detail.

⁹ The 'children' households refer to households with a resident child aged under 15. Households with either non-resident children or resident children aged 15 and over are classified in the 'no children' households.

of the tax-transfer system (discussed further in Chapter 8). Low-paid workers live in a diverse range of household types and will thus have a diverse set of living standards. In general, household income is a better proxy of economic wellbeing than individual income.¹⁰

55. The spread of low-paid workers across the household income distribution can be examined in two ways. The first is to examine the distribution of low-paid workers across households with at least one employee (referred to as employee households). The second is across all households (including jobless households and retiree households).
56. Under both methods, it is important to ensure that income is adjusted for household needs, due to differences in size and composition.¹¹ Chart 2.2 compares the distribution of low-paid employees across the disposable household income distribution using both of these methods.¹² Across *all* households, low-paid workers tend to be concentrated in the middle of the income distribution, with only 16.9 per cent of low-paid workers in the bottom two income deciles, and 14.4 per cent in the top two deciles.¹³

Chart 2.2: Distribution of low-paid employees, by equivalised household disposable income, comparing all households and employee households, 2014



Source: HILDA Survey, release 14 (December 2015), wave 14.

57. When considering *employee* households only, low-paid workers remain scattered across the income distribution although there are a higher proportion of low-paid employees in the lower deciles than the top deciles. For example, 65.3 per cent of low-paid employees

¹⁰ However, the Government acknowledges that in some households, household income is not shared among household members, e.g. shared household arrangements.

¹¹ Household income is adjusted for household needs, including household size and composition, using the OECD equivalence scale. This gives a weight of 1 to the first household member, 0.5 to each subsequent adult and 0.3 to each child aged under 15.

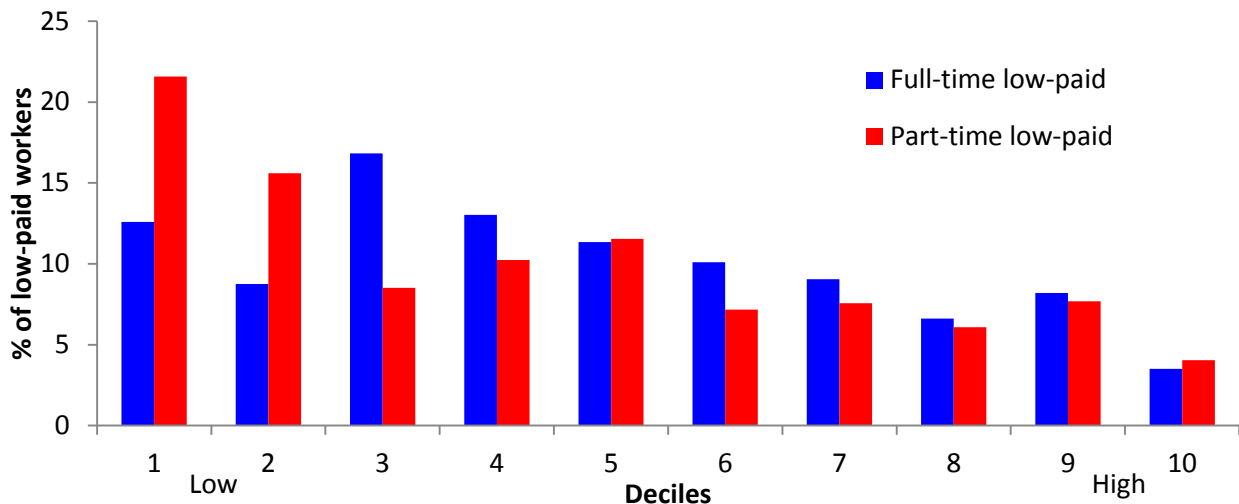
¹² Disposable household income refers to household private income plus government transfers, less taxes.

¹³ The first decile includes the bottom 10 per cent of employees as ranked by household disposable income; similarly the second decile includes the next 10 per cent of employees, and so on.

are in the bottom five income deciles, with 30.4 per cent in the bottom two deciles. This means that 34.7 per cent are in the top five deciles, with 11.8 per cent in the top two deciles. The following detailed analysis of the income distribution is likewise limited to households with at least one employee.

58. Chart 2.3 shows the distribution of low-paid workers across the household income distribution, broken down by full-time or part-time employment status. This shows that low-paid part-time workers are more likely to be in the lower household income deciles than low-paid full-time workers. For example, 21.6 per cent of low-paid part-time employees live in the bottom income decile, compared to 12.6 per cent of full-time low-paid employees. This suggests that the low income of some households is not just due to low hourly wages but also a result of lower working hours.

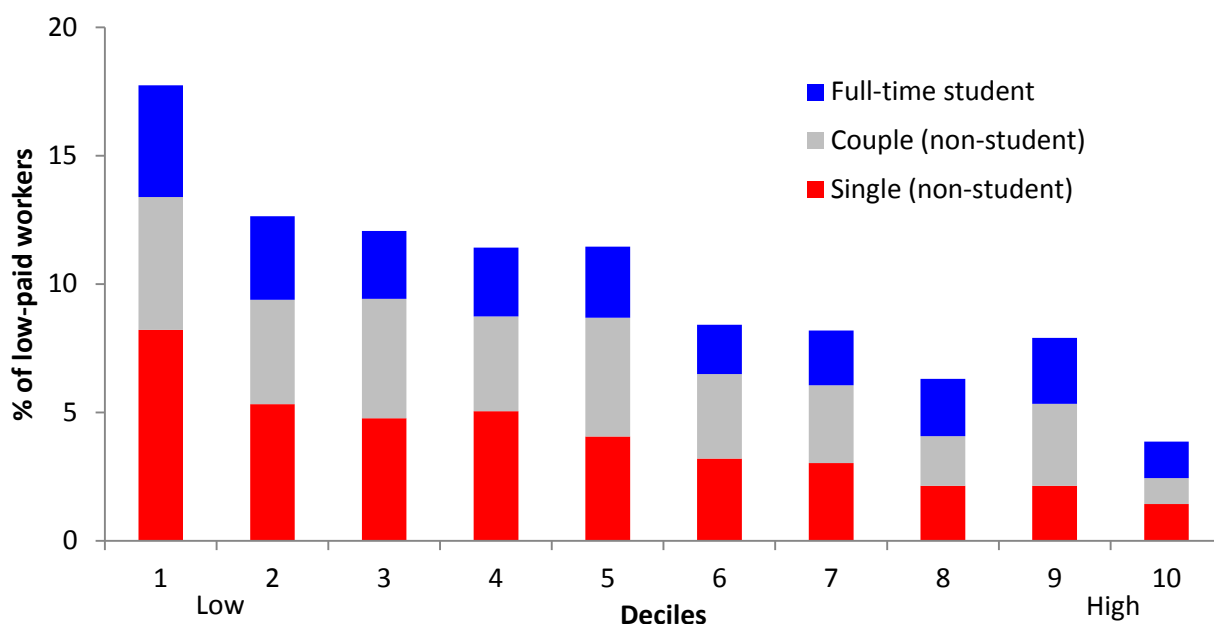
Chart 2.3: Distribution of low-paid employees, by equivalised household disposable income, employee households only, 2014



Source: *HILDA Survey*, release 14 (December 2015), wave 14.

59. For the 26.0 per cent of low-paid workers who are full-time students, over two-thirds of them are dependent students. Their household income and living standards are likely to be largely determined by their parents' earnings, rather than their own. Hence, as shown in Chart 2.4, they are spread rather evenly across the income distribution.

Chart 2.4: Distribution of low-paid employees, by equivalised household disposable income and partnered status, employee households only, 2014



Source: *HILDA Survey*, release 14 (December 2015), wave 14.

Note: Calculations for singles and partnered categories exclude full-time students in order to create mutually exclusive groupings.

60. There is also a substantial spread in household income across all coupled low-paid workers. As shown in Table 2.1, around 15.2 per cent were with a partner earning less than \$25,000 per year, compared with 26.9 per cent with partner's earnings between \$25,000 and \$50,000, 24.5 per cent with partner's earnings between \$50,000 and \$100,000 and 15.3 per cent with partner's earnings of more than \$100,000. Also, 18.2 per cent of coupled low-paid employees have a partner who is not employed.

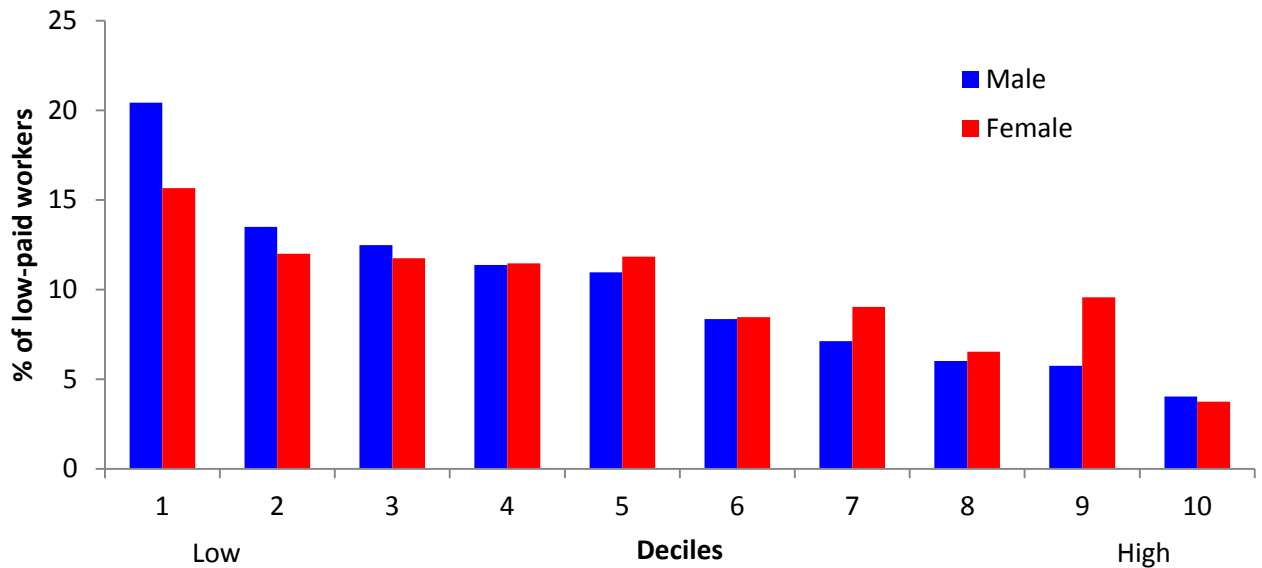
Table 2.1: Earnings of low-paid workers' partners, 2014

Partner 2	Partner 1 – Low-paid employee (%)		
	Full-time	Part-time	Total
Less than \$25,000	8.5	6.7	15.2
\$25,000 ~ \$50,000	18.7	8.1	26.9
\$50,000 ~ \$75,000	8.5	9.5	18.0
\$75,000 ~ \$100,000	1.2	5.2	6.5
More than \$100,000	3.9	11.4	15.3
Not employed	9.6	8.6	18.2
Total	50.5	49.6	100

Source: *HILDA Survey*, release 14 (December 2015), wave 14.

61. Low-paid partnered women in particular tend to have a partner with higher earnings. Around 25.2 per cent of low-paid partnered women have a partner earning more than \$100,000 per annum. This in part contributes to low-paid women being slightly more evenly spread across the household income distribution than men. As shown in Chart 2.5, 27.7 per cent of low-paid women were in the bottom two income deciles, compared to 33.9 per cent of men. Around 13.3 per cent of women are in the top two income deciles compared to 9.8 per cent of men.

Chart 2.5: Distribution of low-paid employees, by equivalised household disposable income and gender, employee households only, 2014



Source: HILDA Survey, release 14 (December 2015), wave 14.

2.3 Conclusion

- 62. The vast majority of workers impacted by the Panel’s decision are paid more than the national minimum wage and are not defined as low-paid employees.
- 63. Low-paid workers are scattered across the entire household income distribution. Nearly half of low-paid workers are in the top 50 per cent of household income.
- 64. Given these factors, seeking to improve the relative living standards of low-paid workers by raising minimum and award classification wages is not a particularly well-directed approach.

3 Economic Environment

Key Points

- The Australian economy is continuing to transition from strong resource investment-led growth to broader-based drivers of economic activity.
- The transition is being supported by historically low interest rates, the fall in the Australian dollar and lower oil prices.
- Wage flexibility is helping to support employment during this transition period. The Wage Price Index grew by 2.2 per cent through the year to the December quarter 2015 and wage growth is forecast to remain moderate.
- The global economy is expected to improve modestly, but downside risks to the outlook are elevated.

3.1 Introduction

65. The outlook as presented in the *2015-16 Mid-Year Economic and Fiscal Outlook* (MYEFO) is for a gradual improvement in real GDP growth.
66. Exports and dwelling investment have been growing strongly, while consumption has been supported by strong growth in employment, low interest rates and lower petrol and electricity prices. The depreciation of the Australian dollar is improving the prospects for trade-exposed sectors of the economy. Services exports grew by 7.6 per cent in 2014-15.
67. Wage flexibility is an important adjustment mechanism in the economy and is facilitating the current economic transition. In making its decision the Panel should have regard to the role of wage flexibility to support the economy during the continued transition to broad-based sources of growth.

3.2 International Outlook

68. Global economic growth is expected to improve modestly, but at a slower rate than expected at the previous Budget. Growth remains uneven, with the recovery in advanced economies being patchy. Growth in the US is forecast to be the strongest amongst the major advanced economies, while the recovery in the Euro area is expected to remain relatively subdued and Japan continues to face significant structural challenges.
69. Growth in China is expected to continue to moderate as the economy transitions. China's shift from investment-led growth to a greater reliance on consumption and services has implications for regional and global activity, while also presenting opportunities for Australian businesses.
70. Australia's major trading partner growth is expected to continue to exceed world growth at 4 per cent in 2015, 2016 and 2017. This reflects the relative strength of East Asian economies and the importance of this region as a destination for Australia's exports.
71. Risks to the global outlook are elevated, with significant transitions underway. China's shift towards a greater reliance on consumption and services has implications for global activity and commodity prices, while decisions around the normalisation of monetary

policy in the US from near-zero interest rates have the potential to contribute to financial market volatility.

3.3 Domestic Outlook

72. The outlook for real GDP growth was revised down in the 2015-16 MYEFO relative to the previous Budget. The economy is forecast to grow by 2½ per cent in 2015-16 and 2¾ per cent in 2016-17.
73. The transition from resource investment-led growth towards broader-based drivers of economic activity is underway, supported by historically low interest rates, the fall in the Australian dollar and lower oil prices. Employment growth has strengthened recently as the economy transitions to more labour intensive sectors such as services and has been supported by moderate wage growth. Business investment intentions currently remain subdued, but conditions conducive to stronger business investment are in place.

3.4 Business conditions

74. Business investment fell by 6.3 per cent in 2014-15 due to the decline in investment in the resources sector. Non-mining business investment grew modestly in 2014-15.
75. The outlook for business investment is more subdued than forecast at Budget as the transition towards broader-based growth is materialising at a slower pace than previously anticipated. The Australian Bureau of Statistics' Capital Expenditure Survey indicates weak investment intentions, though the National Australia Bank business survey has more firms intending to increase than decrease investment in the 12 months from the December quarter 2015.
76. Business investment is forecast to fall by 9½ per cent in 2015-16 and 4 per cent in 2016-17 as the decline in resource investment is only slightly offset by modest average growth in non-mining business investment.
77. However, conditions for investment continue to remain favourable with low borrowing costs leaving firms well placed to increase investment. There has been a sustained lift in non-mining business conditions since February 2015. Confidence and conditions have held up quite well in light of recent declines in equity markets and oil prices.
78. Key commodity prices have fallen significantly over the past year, reflecting both increasing supply and slowing demand growth. At the time of the 2015-16 MYEFO, both oil and iron ore spot prices had fallen by over a third since Budget in US dollar terms, while thermal coal and metallurgical coal spot prices had fallen by around 15 per cent and 10 per cent respectively. However over the course of the March 2016 quarter the price of iron ore returned to around Budget levels.
79. Despite reaching 12 year lows in December 2015, oil prices are now slightly higher than at the 2015-16 MYEFO. While the drop in oil prices is benefiting many parts of the Australian economy, it has a negative impact on Liquefied Natural Gas (LNG) prices. As LNG export prices are typically linked to oil prices through long-term contracts, the large fall in the price of oil has resulted in lower LNG prices than forecast at Budget. With major Australian LNG projects coming on stream in the next few years, the lower oil price assumption is leading to lower forecast export values from these projects.

80. Falls in commodity prices continue to weigh on the terms of trade, with a fall of 10½ per cent forecast in 2015-16 and a further fall of 2¼ per cent forecast in 2016-17.

3.4.1 Consumption

81. Household consumption grew by 2.5 per cent in 2014-15, supported by strong growth in employment and lower petrol and electricity prices. Buoyant conditions in the housing market are also likely to have provided support for household consumption, contributing to an increase in household wealth and underpinning spending on household furnishings.
82. A strengthening labour market and a further modest decline in the household saving ratio are expected to support solid growth in household consumption, albeit at a slower rate than expected at the previous Budget. Household consumption is forecast to grow by 2¾ per cent in 2015-16 and 3 per cent in 2016-17.

3.4.2 Employment

83. The transition in the economy from capital intensive mining to labour intensive services sectors is evident in the strength and composition of employment growth. Over the past year, employment growth has been significantly above its long-run average, driven by the fast-growing household and business services sectors.
84. Employment growth was robust in 2015, with through-the-year growth in employment peaking at 2.9 per cent in November 2015. This was the highest rate of growth recorded since June 2008. Employment is forecast to grow by 2 per cent through the year to the June quarter of 2016 and by 1¾ per cent through the year to the June quarter of 2017. Consistent with lower forecast growth in real GDP and in line with slower population growth, expected employment growth in 2016-17 is lower than forecast at Budget.
85. The unemployment rate is expected to have peaked at a lower level than previously forecast, to be around 6 per cent in the June quarters of 2016 and 2017.
86. The February 2016 participation rate of 64.9 per cent shows that those previously outside the labour market have responded to improving job opportunities, particularly women, who have increased their participation rate over the last year. The overall participation rate is forecast to be 65 per cent in the June quarters of 2016 and 2017.

3.4.3 Wages

87. Wage growth remains moderate, which continues to help the economy in its adjustment to broader-based growth.
88. Wage growth, as measured by the Wage Price Index, was 2.2 per cent through the year to the December quarter of 2015, the lowest published growth rate since 1998 and below the Panel's 2015 decision of 2.5 per cent.
89. Wage growth has been moderate in both public and private sectors. There was an increase of 2.0 per cent for the private sector and 2.6 per cent for the public sector through the year to the December quarter 2015.
90. Of the four most award-reliant industries, the strongest wage growth was recorded in Retail trade, (up by 2.5 per cent through the year), followed by Accommodation and food services and Other services (both up by 2.2 per cent through the year).

91. Wage growth is forecast to be 2½ per cent through the year to the June quarter 2016 and 2¾ per cent through the year to the June quarter 2017. The forecast for low wage growth should be factored into the Panel's decision – otherwise the cost of low skilled labour and award-reliant workers will increase relative to other workers.
92. As outlined in the previous chapter, the Panel's decision impacts 122 modern awards, incorporating over 2,000 adult rates of pay and around 1.9 million Australians, the majority of whom are not low-paid.

3.4.4 Inflation

93. Recent inflation outcomes have been subdued reflecting moderate wage growth, a fall in petrol prices and also a fall in the price of telecommunications equipment and services.
94. The headline Consumer Price Index (CPI) rose by 1.7 per cent through the year to the December quarter 2015 following 1.5 per cent growth through the year to the September quarter 2015. Underlying inflation, as measured by the trimmed mean of the CPI, was within the Reserve Bank of Australia's target band at 2.1 per cent through the year to December quarter 2015.
95. Headline CPI inflation is forecast to be 2 per cent through the year to the June quarter 2016 and 2¾ per cent through the year to June quarter 2017. The subdued outlook for inflation reflects moderate wage growth in combination with lower oil prices, notwithstanding the inflationary effects of the fall in the Australian dollar.

3.4.5 Productivity

96. In the 5-year period to 2014-15, (labour) productivity in the whole economy grew by 1.5 per cent, while productivity in the (16-industry) market sector grew by 2.1 per cent. Over this period, productivity in the award-reliant Retail and Accommodation and food services sectors grew by 1.7 per cent and 1.0 per cent respectively, below market sector growth.
97. In 2014-15, productivity in the whole economy grew by 0.9 per cent in 2014-15, while market sector productivity grew by 1.3 per cent. In the Retail and Accommodation and food services sectors, productivity was also lower than market sector productivity (0.1 per cent and 0.9 per cent respectively).
98. Through the year to the December quarter 2015, seasonally adjusted productivity decreased by 0.4 per cent in the whole economy and increased by 0.9 per cent in the market sector. However, caution should be exercised in interpreting short-run productivity movements as data are volatile and subject to revision. Average growth rates over a number of years can smooth out short-term volatility and provide a more meaningful measure of underlying trends.

3.5 Conclusion

99. The transition from strong resource investment-led growth to broader-based drivers of economic activity is underway in the Australian economy. It has been supported by historically low interest rates, a lower Australian dollar and lower oil prices.

100. Consistent with this outlook, the forecast for unemployment is expected to be around 6 per cent in 2016. Recent moderate wage growth reflects the spare capacity in the labour market and wage flexibility will continue to be an important adjustment mechanism during the economy's transition.

4 Labour market developments

Key Points

- ABS data suggest that labour market conditions have improved over the last year, with the pace of employment growth strengthening and the unemployment rate declining over the period.
- Long-term unemployment as a proportion of the total unemployment pool stood at 23.2 per cent in February 2016, above the 16.0 per cent recorded prior to the onset of the Global Financial Crisis in September 2008. Young people comprised 26.7 per cent of total long-term unemployment in February 2016, above the 22.6 per cent in September 2008.
- Despite the strengthening pace of employment growth over the last year, the unemployment rate is currently forecast to remain around 6 per cent.

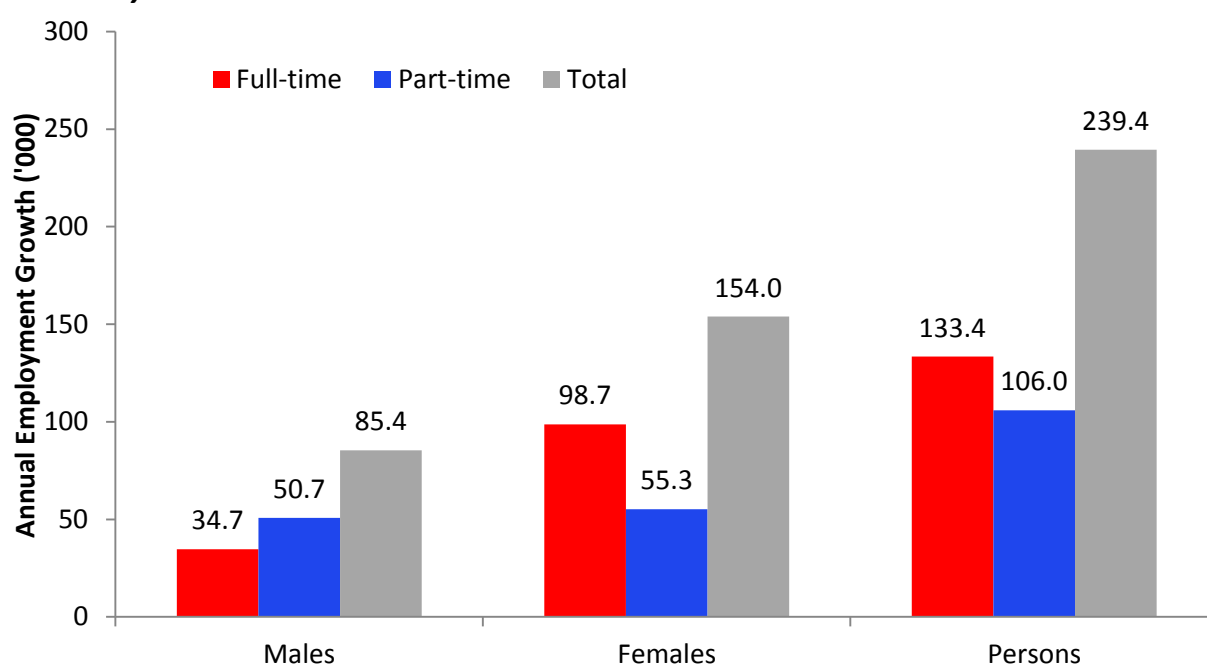
4.1 Broad labour market conditions

101. Underlying labour market conditions are one of the factors to which the Panel must have regard when making its decision about the national minimum wage and award classification wages, as the decision may impact on employers plan to hire more staff. This chapter outlines the most recent developments.
102. ABS data suggest that the Australian labour market has improved over the last 12 months, with the level of employment increasing by 239,400 (or 2.1 per cent) over the year to February 2016, above the decade average rate of 1.8 per cent.
103. The unemployment rate has declined over the period, from 6.3 per cent in February 2015 to 5.8 per cent in February 2016. That said, the unemployment rate remains above the troughs recorded in the last decade.
104. A number of groups, including youth, long-term unemployed people, Indigenous, low-skilled people and those located in specific economically weak regions, continue to experience weaker outcomes in the labour market than the national average.
105. Labour market conditions vary across Australian industries and regions, with some performing strongly, while others have been more subdued. For instance, against the backdrop of below-trend global growth and ongoing competitive pressures, employment in Manufacturing deteriorated considerably over the last year, adding to the decline over the last decade. By contrast, employment has grown more substantially over the last year than on average over the last decade in a range of service industries, such as Health Care and Social Assistance, Financial and Insurance Services and Administrative and Support Services.
106. Despite some recent improvements in the Australian labour market, the 2015-16 MYEFO forecasts are for employment to increase by 2 per cent in 2015-16, before easing to 1¾ per cent in 2016-17. The unemployment rate is expected to be 6 per cent in the June quarter 2016 and remain at that level in the June quarter 2017.

4.2 Employment

107. The level of employment has increased by 239,400 (or 2.1 per cent) over the year to stand at 11,884,000 in February 2016, above the annual average growth rate of 1.8 per cent over the last decade (ABS 2016c).
108. Full-time employment has risen by 133,400 (or 1.7 per cent) over the last 12 months to 8,192,600 in February 2016, while part-time employment increased by 106,000 (or 3.0 per cent) to 3,691,500.
109. Female employment growth (up by 154,000 or 2.9 per cent) outpaced male employment growth (up by 85,400 or 1.4 per cent) over the year to February 2016.

Chart 4.1: Change in full-time, part-time and total employment ('000s) by sex, February 2015 to February 2016



Source: ABS 2016c, *Labour Force, Australia, February 2016*, Cat. No. 6202.0, seasonally adjusted data.

110. Based on ABS trend data, employment increased in 14 of 19 industries over the year to February 2016. The largest employment increases were recorded in Health Care and Social Assistance (up by 82,800 or 5.8 per cent), Retail Trade (up by 68,300 or 5.6 per cent) and Financial and Insurance Services (up by 39,200 or 9.7 per cent).
111. By contrast, a number of industries have experienced declines in employment over the year to February 2016, with the largest recorded in Manufacturing (down by 45,500 or 5.0 per cent), followed by Wholesale Trade (down by 21,300 or 5.4 per cent) and Other Services¹⁴ (down by 10,700, or 2.2 per cent).

¹⁴ Other Services includes a broad range of personal services, religious, civic, professional and other interest group services, selected repair and maintenance, and private households employing staff. Services provided include hair, beauty, diet and weight management, death care, religious events promotion and administration and repair and maintenance of equipment and machinery.

4.2.1 Employment growth in award-reliant industries

112. Over the year to February 2016, employment increased in two of the four most award-reliant industries. Retail Trade recorded the second largest gain of all industries (up by 68,300 or 5.6 per cent) and Administrative and Support Services the fifth largest increase (up by 36,400 or 9.3 per cent). Employment declined in Accommodation and Food Services (down by 3,600 or 0.4 per cent) and Other Services (down by 10,700 or 2.2 per cent).

Table 4.1: Employment growth by industry, February 2006 to February 2016

Industry	Change in employment	
	('000)	(%)
Health Care and Social Assistance	480.8	46.7
Professional, Scientific and Technical Services	302.8	42.2
Construction	197.5	22.9
Education and Training	176.5	23.6
Accommodation and Food Services	161.2	24.5
Retail Trade	135.4	11.7
Transport, Postal and Warehousing	131.0	26.3
Public Administration and Safety	129.5	21.1
Mining	99.5	76.2
Administrative and Support Services	78.3	22.4
Financial and Insurance Services	71.2	19.1
Arts and Recreation Services	53.7	30.5
Other Services	51.1	12.4
Electricity, Gas, Water and Waste Services	33.9	32.1
Rental, Hiring and Real Estate Services	32.0	16.7
Wholesale Trade	0.8	0.2
Information Media and Telecommunications	-18.1	-7.7
Agriculture, Forestry and Fishing	-28.8	-8.4
Manufacturing	-156.4	-15.4
Total	1,920.1	19.2

Source: ABS 2015g, *Labour Force, Australia, Detailed, Quarterly, February 2016*, Cat. No. 6291.0.55.003, trend data. Bold italics signify the four most award-reliant industries.

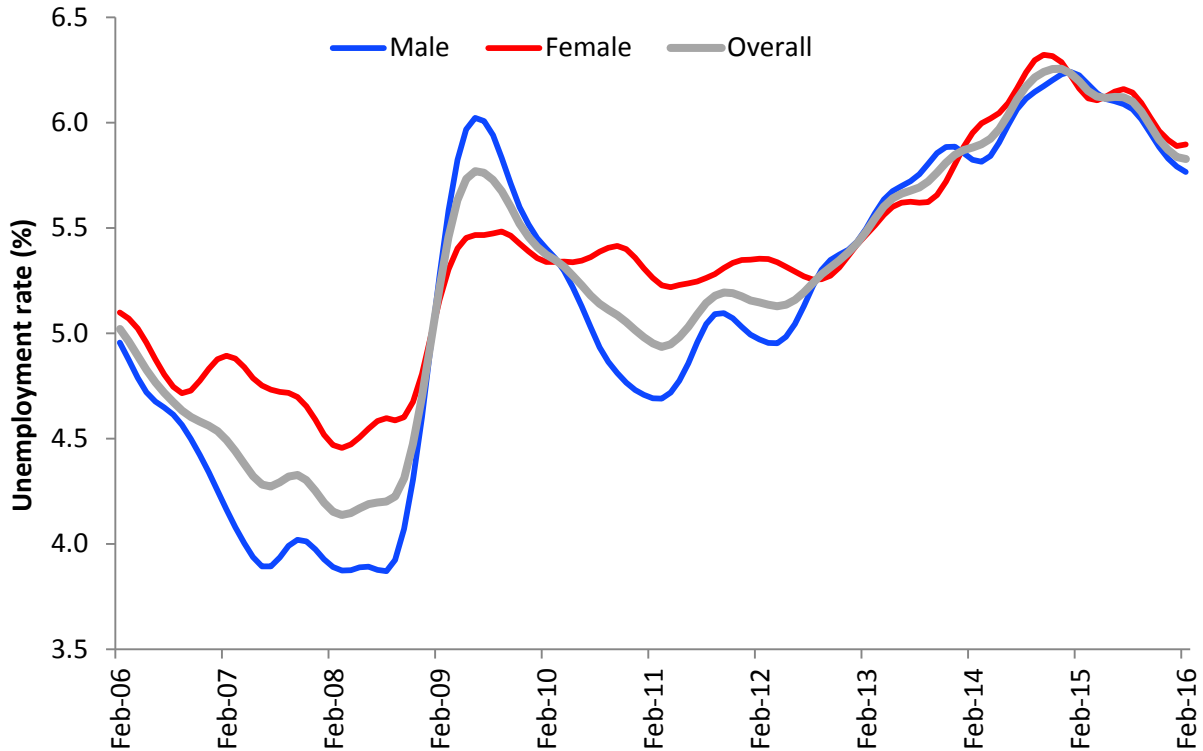
113. Over the past decade, of the most award-reliant industries both Accommodation and Food Services and Administrative and Support Services exceeded the average employment growth rate recorded across all industries (recording growth rates of 24.5 per cent and 22.4 per cent, respectively compared with the 19.2 per cent average, see Table 4.1). Other Services (up by 12.4 per cent) and Retail Trade (11.7 per cent) recorded below average growth rates.

4.3 Unemployment

114. The level of unemployment in Australia has decreased by 45,900 (or 5.9 per cent) over the year, to stand at 732,600 in February 2016. Male unemployment fell by 35,600 (or 8.4 per cent) over the period, while female unemployment also declined, by 10,300 (or 2.9 per cent) (ABS 2016c).

115. The unemployment rate stood at 5.8 per cent in February 2016, below the 6.3 per cent recorded in February 2015 (see Chart 4.2), although it remains above the troughs recorded in the last decade.

Chart 4.2: Unemployment rates by sex, February 2006 to February 2016



Source: ABS 2016c, *Labour Force, Australia, February 2016*, Cat. No. 6202.0, trend data.

4.3.1 Underemployment

116. While the level of underemployment has decreased by 3,000 (or 0.3 per cent) over the year, to stand at 1,058,900 in February 2016, it remains higher than the troughs recorded in the last decade.
117. In considering the issue of underemployment, it is important to note that underemployed workers already have a foothold in the jobs market and many can use this as a 'stepping stone' to achieving their desired hours of employment.
118. The fall in underemployment over the last year has been driven by a decline in female underemployment, down by 8,600 (or 1.4 per cent) to 609,800 in February 2016, while male underemployment has risen, by 5,600 (or 1.3 per cent), to 449,100.
119. The overall underemployment rate¹⁵ has fallen by 0.2 percentage points over the year, to 8.4 per cent in February 2016, although it remains above the 5.9 per cent recorded in August 2008. The female underemployment rate has also declined, from 10.8 per cent in

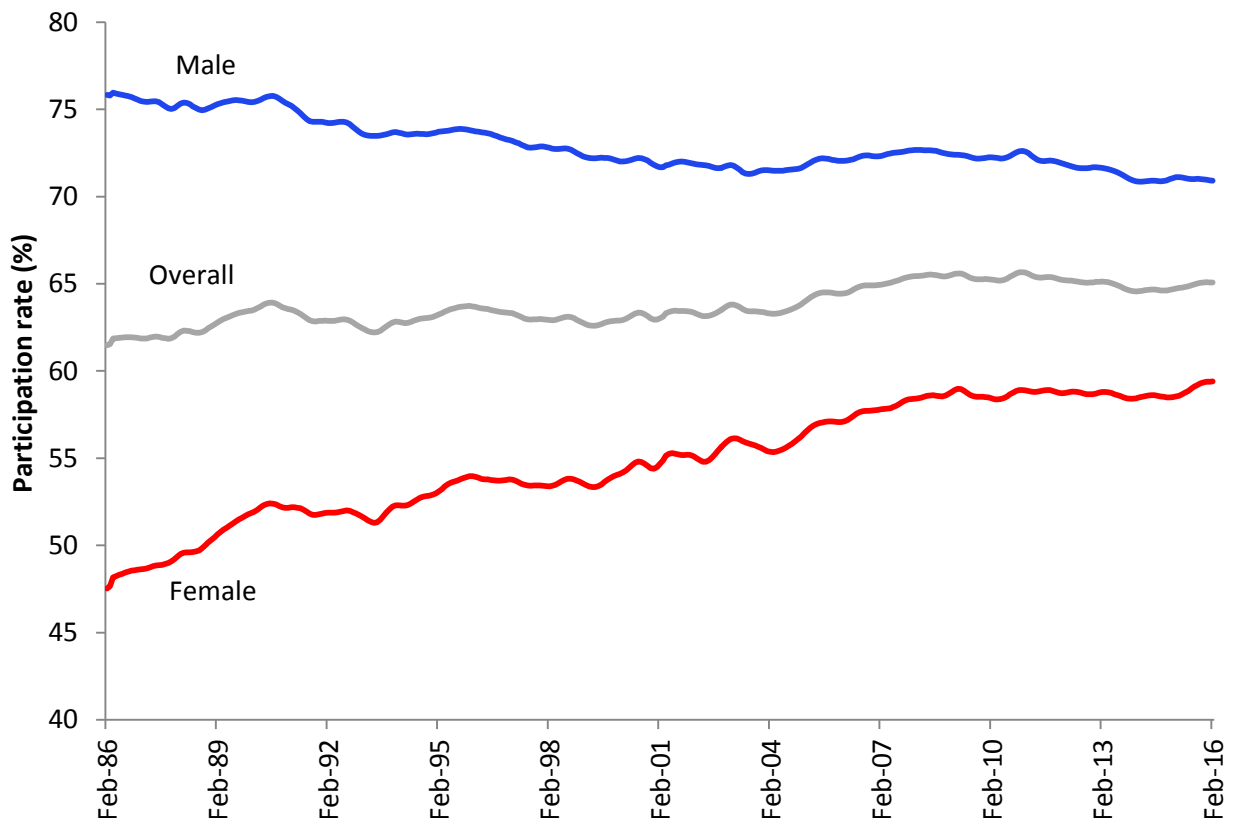
¹⁵ The underemployment rate refers to the number of underemployed workers expressed as a percentage of the labour force.

February 2015 to 10.4 per cent in February 2016, while the male underemployment rate was steady, at 6.6 per cent.

4.4 Participation rate

120. Despite increasing recently, from 64.8 per cent in February 2015 to 64.9 per cent in February 2016, Australia’s national participation rate remains well below the record high of 65.8 per cent recorded in November 2010.
121. A number of factors are likely to have influenced movements in the participation rate over recent years. First, the retirement of the first tranche of the baby boomer cohort, which began in 2011, placed downward pressure on the participation rate, as significant numbers started leaving the labour force. Second, at least part of the decline in the participation rate, up until the last year or so, had been due to the ‘discouraged worker’ effect, as weaker labour market conditions (until recently) had resulted in some people giving up searching for work or even choosing not to enter the labour market. These effects have been partially offset by higher participation rates in the 55-64 year old and 65 years and over cohorts. This is broadly consistent with Treasury analysis on the decomposition of total participation rates into trend and cyclical components (see paragraph 127).
122. With respect to a gender breakdown, the male participation rate has declined from 71.3 per cent in February 2015 to 70.7 per cent in February 2016. The female participation rate has risen, from 58.6 per cent in February 2015 to 59.2 per cent in February 2016 (ABS 2016c).

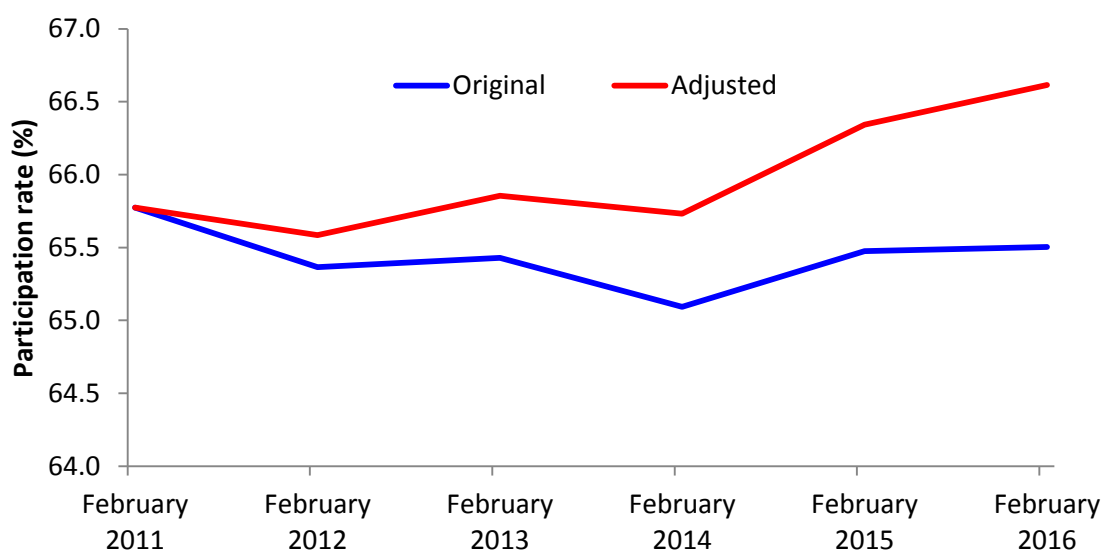
Chart 4.3: Participation rates by sex, February 1986 to February 2016



Source: ABS 2016c, *Labour Force, Australia, February 2016*, Cat. No. 6202.0, trend data.

123. In terms of an age breakdown, the largest increase in participation over the last year was recorded for persons aged 55-64, up by 1.5 percentage points, to 65.5 per cent in February 2016. The participation rate for persons aged 45-54 has also risen, from 82.4 per cent in February 2015 to 83.2 per cent in February 2016. The increase in the participation rate for persons aged 55-64 years will, to some extent, be affected by those who are ageing (and moving into the older age cohort) having a higher participation rate.
124. It is likely in the coming years that the participation rate will be dampened as the ageing of the baby boomer cohort within the workforce begins to outweigh the positive impact of increased mature age and female participation.
125. Indeed, analysis by the Department of Employment shows that while the overall participation rate (in original terms)¹⁶ has declined from 65.8 to 65.5 per cent over five years to February 2016, this process has been driven entirely by the ageing of the population, partially offset by increasing age-specific participation rates.
126. Chart 4.4 shows that if there had been no change in the age distribution of the population since February 2011, then the participation rate in February 2016 would have been over a percentage point higher (66.6 as opposed to 65.5 per cent). Since the actual participation rate has only fallen slightly over the past five years, increases in age-specific participation rates have offset the effects of population ageing by nearly a full percentage point.

Chart 4.4: Age-adjusted participation rates, February 2011 to February 2016



Source: Department of Employment calculations from ABS 2016d, *Labour Force, Australia, Detailed-Electronic Delivery, February 2016*, Cat. No. 6291.0.55.001.

127. This analysis presented in Chart 4.4 broadly aligns with Treasury analysis over a three-year time horizon. This analysis indicates the ageing of the population has been offset by long term increases in female participation, delayed retirement and short-term cyclical factors. Quarterly data indicates that over the three years to December quarter

¹⁶ Data in paragraphs 125-126 and Chart 4.4 are in original terms and are not seasonally adjusted. This is because the ABS does not publish seasonally adjusted labour force participation rates by age group.

2015, the effect of ageing subtracted 0.66 percentage points reflecting the rising share of older age groups which exhibit lower participation rates while the effect of rising participation rates within cohorts (particularly among females and the older age groups) contributed 0.43 percentage points to the participation rate over this time. Cyclical factors are estimated to have contributed around 0.33 percentage points to the participation rate due to the encouraged worker effect.

4.5 Key groups in the labour market

128. A number of groups (including long-term unemployed people and youth) continue to experience weaker outcomes in the labour market. Members of these groups are more likely to seek employment in low-paid jobs and are therefore likely to be more adversely affected by any slowing in the economy or below-trend employment growth. They also tend to possess characteristics (for example, less experience, greater time out of the labour market, lower skill levels) that may predispose them to labour market disadvantage.

4.5.1 Long-term unemployed people

129. The level of long-term unemployment¹⁷ has fallen over the year to February 2016, by 14,100 (or 7.7 per cent), to 169,700. That said, long-term unemployment remains 92,300 (or 119.4 per cent) higher than the level recorded prior to the onset of the Global Financial Crisis in September 2008.
130. Over the year to February 2016, there was a fall in female long-term unemployment, which declined by 10,900 (or 13.7 per cent) over the period, while male long-term unemployment has also decreased, by 3,200 (or 3.0 per cent) over the period.
131. The level of very long-term unemployment¹⁸ has also declined over the year to February 2016, by 3,600 (or 4.1 per cent), to 84,400, although it remains 44,300 (or 110.7 per cent) above the level recorded in September 2008.
132. Female very long-term unemployment has fallen over the year to February 2016, by 2,900 (or 7.6 per cent), while male very long-term unemployment has also decreased over the period, by 800 (or 1.5 per cent).
133. The incidence of long-term unemployment (the proportion of the unemployed population who are long-term unemployed) stood at 23.2 per cent in February 2016, down from 23.6 per cent in February 2015, although it remains above the 16.0 per cent recorded in September 2008.
134. A high level of long-term unemployment is of concern, as people who have been unemployed for a significant length of time, on average, face greater difficulty finding subsequent work due to skill depreciation, the discouraged worker effect and marginalisation from the labour market.

¹⁷ The level of long-term unemployment refers to the number of people who have been unemployed for 52 weeks or longer.

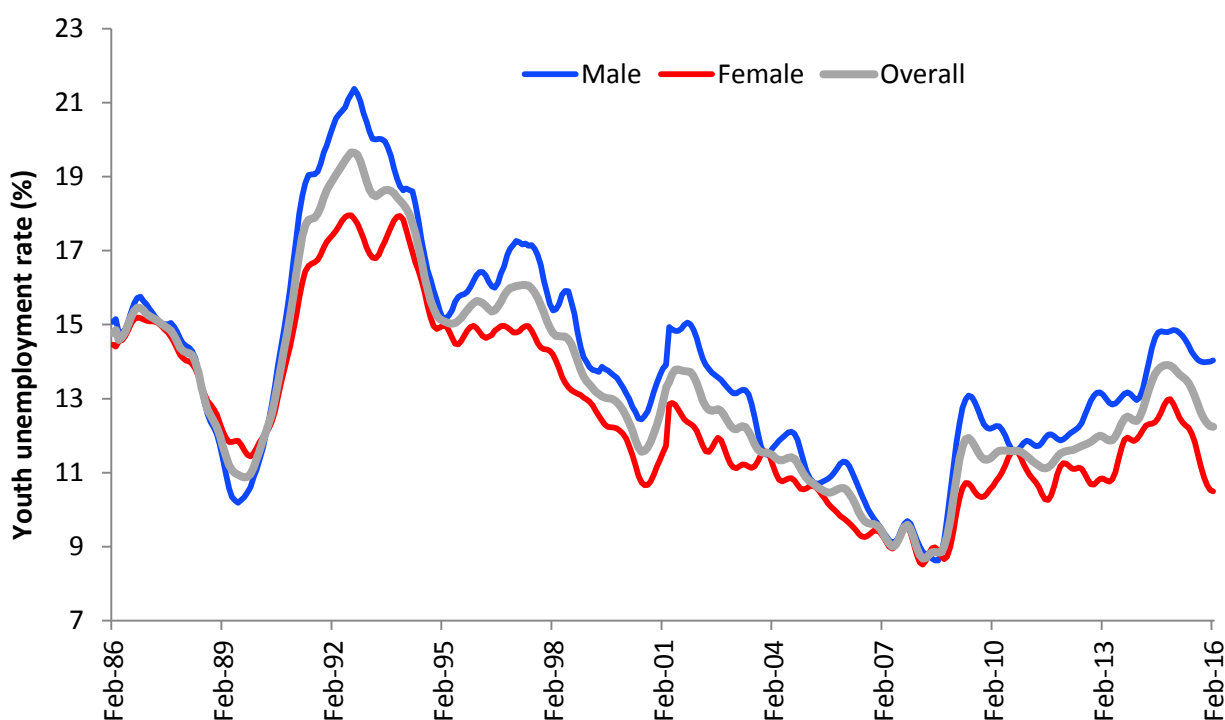
¹⁸ The level of very long-term unemployment refers to the number of people who have been unemployed for 104 weeks or longer.

135. A longer duration of unemployment is also associated with a degrading of human capital and a 'scarring' effect, whereby the long-term unemployed believe their own re-employment prospects are poor.
136. In addition, a sectoral shock (a process whereby one industry shrinks while another expands), or technological change following a downturn, can result in a greater mismatch between the job vacancies available and the skill level of unemployed persons who could fill them, resulting in fewer exits from long-term unemployment.
137. Older job seekers are more likely to remain unemployed for a longer period of time than those in younger cohorts. For instance, in February 2016, 38.3 per cent of unemployed persons aged 55 and over were long-term unemployed, above the 23.2 per cent recorded for all persons.

4.5.2 Youth

138. Labour market conditions for youth (persons aged 15-24 years) have improved over the last year, with employment increasing by 37,700 (or 2.1 per cent) over the year to February 2016. Against this backdrop, the youth unemployment rate decreased from 13.9 per cent in February 2015 to 12.2 per cent in February 2016. That said, the youth unemployment rate remains above the 8.8 per cent recorded at the onset of the Global Financial Crisis in September 2008 and more than double the rate recorded for all persons (ABS 2016c).

Chart 4.5: Youth (15-24 years) unemployment rates by sex, February 1986 to February 2016

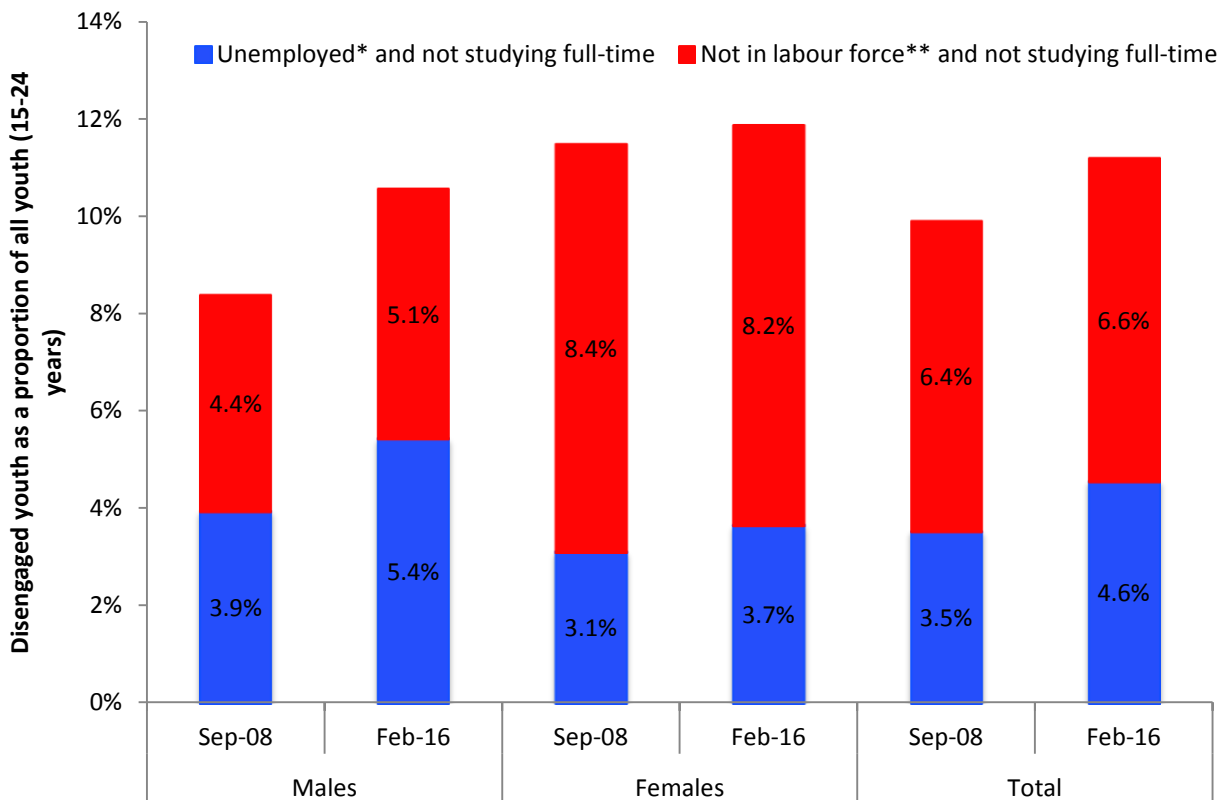


Source: ABS 2016c, *Labour Force, Australia, February 2016*, Cat. No. 6202.0, trend data.

139. Young people are remaining unemployed for longer periods than they were at the onset of the Global Financial Crisis, with the average duration of unemployment for 15-24 year olds increasing from 18 weeks in September 2008 to 30 weeks in February 2016, its equal highest level since February 1999.

140. Long-term unemployment for young people has also increased substantially since September 2008, up by 31,100 to stand at 47,000 in February 2016. Young people now account for 26.7 per cent of the long-term unemployed cohort, above the 22.6 per cent recorded at the onset of the Global Financial Crisis in September 2008.
141. While most youth are either engaged in some form of work or full-time education, 11.2 per cent were not in work and not attending full-time education (and are commonly referred to as disengaged youth) in February 2016, up from 9.9 per cent in September 2008. While a proportion of this group may, for various reasons, be voluntarily outside the labour market (for instance, taking a gap year), many are at risk of ultimately failing to make a successful transition to employment.
142. The increase in youth disengagement has been driven, entirely, by the 20-24 year old cohort, with the proportion of 20-24 year olds who are disengaged rising from 11.9 per cent in September 2008 to 15.0 per cent in February 2016. By contrast, the proportion of 15-19 year olds who are disengaged has declined from 7.8 per cent in September 2008 to 7.0 per cent in February 2016, reflecting the considerable policy changes enacted in various States surrounding compulsory school retention rates.

Chart 4.6: Disengaged youth by sex, September 2008 to February 2016



Source: ABS 2016d, *Labour Force, Australia, Detailed – Electronic Delivery, February 2016*, Cat No. 6291.0.55.001, data are 12-month averages of original estimates.

*Unemployed refers to persons who were not employed during the reference week, and:

- **had actively** looked for full-time or part-time **work** at any time in the four weeks up to the end of the reference week and were available for work in the reference week; or
- were waiting to start a new job within four weeks from the end of the reference week and could have started in the reference week if the job had been available then.

**Not in the Labour Force refers to people who are neither employed nor unemployed.

143. As illustrated in Chart 4.6, disengaged young males are fairly evenly split between those who are not in full-time education and are unemployed, and those who are not in full-time education and are not in the labour force. On the other hand, disengaged young women are primarily not in full-time education and are not in the labour force. Some of these young women will be caring for children.

4.5.3 Indigenous unemployment rates

144. Significant disparity continues to exist between Indigenous and non-Indigenous labour market outcomes.¹⁹ For instance, in 2012-13 (latest available Indigenous data from the *National Aboriginal and Torres Strait Islander Health Survey, 2012-13*, ABS Cat. No. 4727.0.55.006), the unemployment rate for Indigenous persons stood at 20.9 per cent, almost five times the rate recorded for non-Indigenous persons (of 4.2 per cent). The disparity between labour market outcomes for Indigenous and non-Indigenous Australians is likely to be influenced by a number of characteristics such as low educational attainment levels and being located in more remote areas.

4.6 Labour market conditions by skill level

145. Low-skilled workers are more likely to be on the minimum wage or award-reliant than higher skilled workers, making an examination of labour market developments by skill level important.
146. Over the 10 years to February 2016, employment growth has been dominated by the higher Skill levels, with Skill levels 1, 2 and 3²⁰ accounting for 67.5 per cent of employment growth.
147. Consistent with these trends, the share of employment comprised by Skill level 5 has decreased, from 19.2 per cent in February 2006 to 17.2 per cent in February 2016, whereas the employment share accounted for by Skill level 1 occupations has grown from 28.6 per cent to 31.3 per cent over the same period.

¹⁹ Please note all data in this section refer to the working age population (persons aged 15-64 years).

²⁰ The ABS classifies occupations according to five skill levels commensurate with a qualification(s) as follows: Skill level 1: Bachelor degree or higher qualification; Skill level 2: Advanced Diploma or Diploma; Skill level 3: Certificate IV or III (the Certificate III requirement for this skill level includes at least two years on-the-job training); Skill level 4: Certificate II or III; and Skill level 5: Certificate I or secondary education. In some cases relevant work experience may be a substitute for formal qualifications, or relevant work experience and/or on-the-job training may be required in addition to formal qualifications.

Table 4.2: Change in employment by Skill level, one and 10 years to February 2016

Skill Level Occupations	Current employment (February 2016)	Change in employment year to February 2016		Change in employment 10 years to February 2016	
	(000s)	(000s)	(%)	(000s)	(%)
Skill Level 1 (highest)	3,726.8	101.6	2.8	868.1	30.4
Skill Level 2	1,359.4	49.7	3.8	295.5	27.8
Skill Level 3	1,730.9	8.1	0.5	128.1	8.0
Skill Level 4	3,047.4	54.0	1.8	496.0	19.4
Skill Level 5 (lowest)	2,049.9	42.6	2.1	125.8	6.5
All Occupations	11,904.7	275.5	2.4	1,920.1	19.2

Source: ABS 2015g, *Labour Force, Australia, Detailed, Quarterly, February 2016*, Cat. No. 6291.0.55.003, Department of Employment trend data.

148. Over the year to February 2016, employment in Skill levels 1 and Skill level 2 occupations grew at faster rates (2.8 per cent and 3.8 per cent respectively) than employment in other, lower Skill level occupations. The other, lower Skill level occupations recorded below average growth, the lowest growth rate being for Skill level 3 occupations (0.5 per cent) (see Table 4.2).
149. With respect to low-skilled employment, it is worth noting that Department of Employment data show that the average number of applicants per low-skilled job vacancy²¹ has increased from 10 in 2011 to 15 in 2015, indicating increasing competition for low-skilled, low-paid and entry level jobs.

4.7 Regional labour markets

150. Historically, Capital Cities have recorded a lower unemployment rate (and a higher participation rate) than the Rest of State areas.
151. Significant disparity in labour market performance exists between regions within Australia, with some regions recording a deterioration in labour market conditions over the last year, while other regions have performed more strongly.
152. The level of employment has risen in both Capital Cities and Rest of State areas over the year to February 2016. In the Capital Cities, employment has increased by 210,900 (or 2.7 per cent), while in the Rest of States areas, employment has risen by 63,400 (or 1.7 per cent) over the period²² (ABS 2016d).
153. The unemployment rate in the Capital Cities remains below the rate for the Rest of State areas. In Capital Cities, the unemployment rate has declined over the year, from 6.2 per cent in February 2015 to 5.9 per cent in February 2016, while the unemployment rate has also decreased in the Rest of State areas, from 7.0 per cent in February 2015 to 6.4 per cent in February 2016. Further, the participation rate in Capital Cities stood at

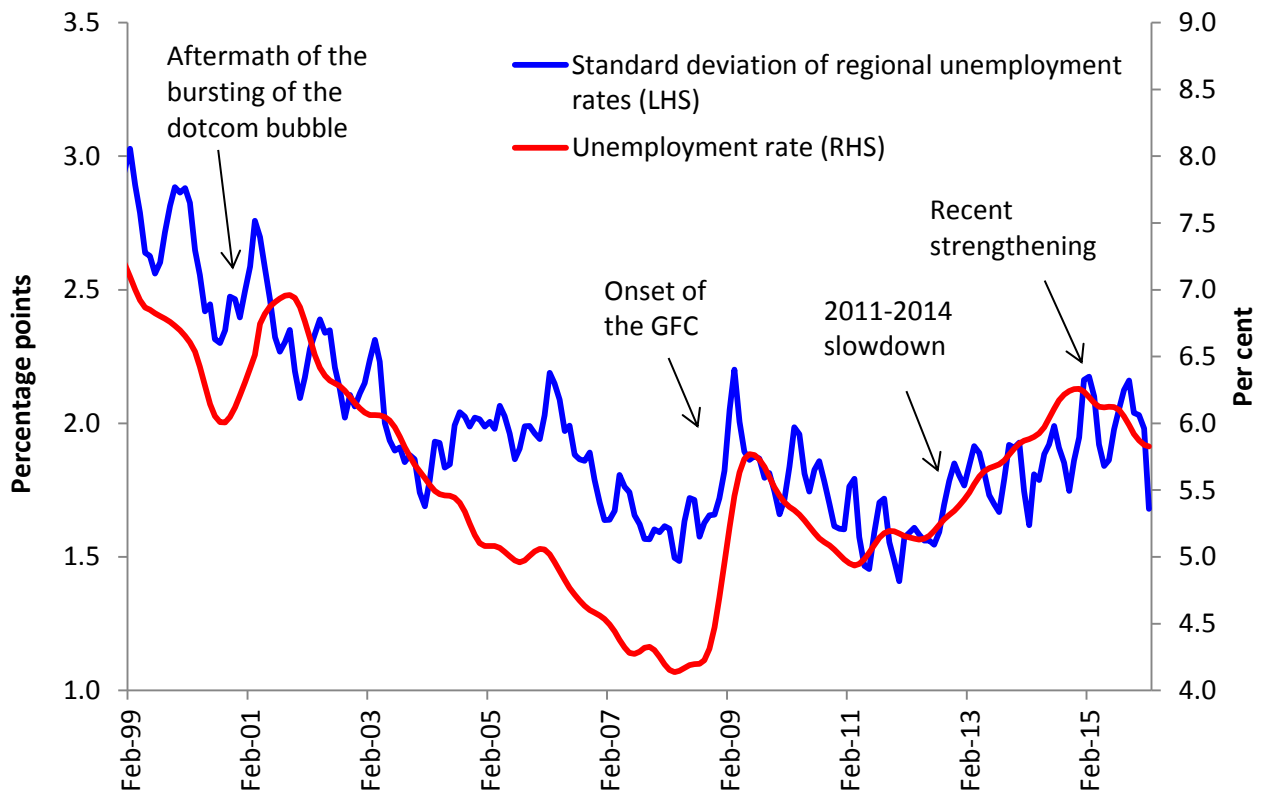
²¹ Refers to vacancies advertised on the internet or in the newspaper.

²² Figures are three-month averages of *original* estimates.

66.8 per cent, above the rate recorded in the Rest of State areas, of 62.1 per cent in February 2016.

154. More broadly, differences in regional labour market performance can be ascribed to a number of factors, such as a region's access to higher education, its industry base, transport networks and infrastructure, its degree of natural amenity, population size and growth, its accessibility to more dynamic labour markets and the skill level of its labour force.

Chart 4.7: The unemployment rate and standard deviation in the regional unemployment rate, February 1999 to February 2016



Source: ABS 2016d, *Labour Force, Australia, Detailed – Electronic Delivery, February 2016*, Cat No. 6291.0.55.001, data are 3-month averages of *original* estimates. The national unemployment rate is sourced from ABS 2016c, *Labour Force, Australia, February 2016*, Cat. No. 6202.0, trend data.

155. Chart 4.7 presents regional disparity (as measured by the standard deviation of regional unemployment rates) and the trend unemployment rate, back to February 1999. The chart clearly shows the strong relationship between the unemployment rate and the level of regional disparity, with both trending down during the late 1990s and 2000s, other than during temporary periods of labour market softness, until 2008.
156. Following the Global Financial Crisis, regional disparity increased steadily, from 1.63 percentage points²³ in September 2008, to a peak of 2.20 percentage points in March

²³ The standard deviation of regional unemployment rates is a measure that is used to quantify the amount of variation in unemployment rates at the Statistical Area 4 (SA4) level. A standard deviation close to zero indicates that the data points tend

2009. The level of regional disparity declined during the recovery in 2010-11, falling to a low of 1.41 percentage points in December 2011. Over the subdued labour market conditions recorded from 2011 to 2014, regional disparity, while increasing in volatility, trended upwards, to 2.16 percentage points in October 2015. Since then, however, against the background of improved labour market conditions, regional disparity has decreased, to stand at 1.68 percentage points²⁴ in February 2016.

157. If the recent strengthening in labour market conditions were to be sustained, it is likely that regional disparity may continue to narrow somewhat in the period ahead.

4.7.1 Labour market conditions by State

158. Labour market conditions have varied across the States and Territories over the year to February 2016. For instance, strong employment growth was recorded in New South Wales (3.9 per cent), Queensland (2.2 per cent) and Victoria (1.9 per cent). By contrast, the level of employment declined in Tasmania (down by 1.4 per cent) the Northern Territory (1.2 per cent) and Western Australia (1.0 per cent) over the year. South Australia (1.1 per cent) and the Australian Capital Territory (1.3 per cent) recorded relatively weak employment growth over the period.
159. The New South Wales labour market has continued to improve. On the other hand, labour market conditions in Tasmania have weakened over the 12 months to February 2016, and the Western Australian labour market has also recorded soft results over the last year. Going forward, employment growth in Western Australia is expected to remain subdued as the State's Mining sector continues to transition from its investment phase to a less labour intensive production phase.

4.8 Conclusion

160. In considering its decision, the Panel should take into account that, despite some improvement in the Australian labour market over the last year, conditions remain uneven as the economy continues to slowly transition from mining investment-led growth, to more broadly-based domestic growth. Of particular concern is that certain groups, including youth and the long-term unemployed, continue to experience weaker outcomes in the labour market, as do some regions. Going forward, the unemployment rate is currently forecast to remain around 6 per cent. In this context the Panel should make a decision that is likely to support the creation of new jobs.

to be very close to the mean, while a high standard deviation indicates that the data points are spread out over a wider range of values.

²⁴ A standard deviation of 1.68 percentage points means that given the average regional unemployment rate stood at 6.1 per cent in February 2016, at least 75 per cent of regions recorded an unemployment rate between 2.77 per cent and 9.49 per cent (as 75 per cent of all regions will fall within two standard deviations of the average).

5 Small Business

Key Points

- The economic environment for small business continues to be challenging, although there are tentative signs of improvement. As a result of these challenging conditions, small businesses remain cautious in taking on new employees.
- Key business surveys show that small businesses are finding conditions more difficult than larger businesses.
- Small businesses are significant employers, employing around 44 per cent of non-financial private sector employees and 38 per cent of employees on award classification wages.
- Small businesses are likely to be particularly impacted by changes in minimum and award classification wages. Small businesses more commonly rely on awards rather than negotiating enterprise or individual-level agreements.
- In making its decision, the Panel should carefully consider the affordability of the changes for small businesses to ensure their ongoing viability and growth, which will in turn support employment.

5.1 Introduction

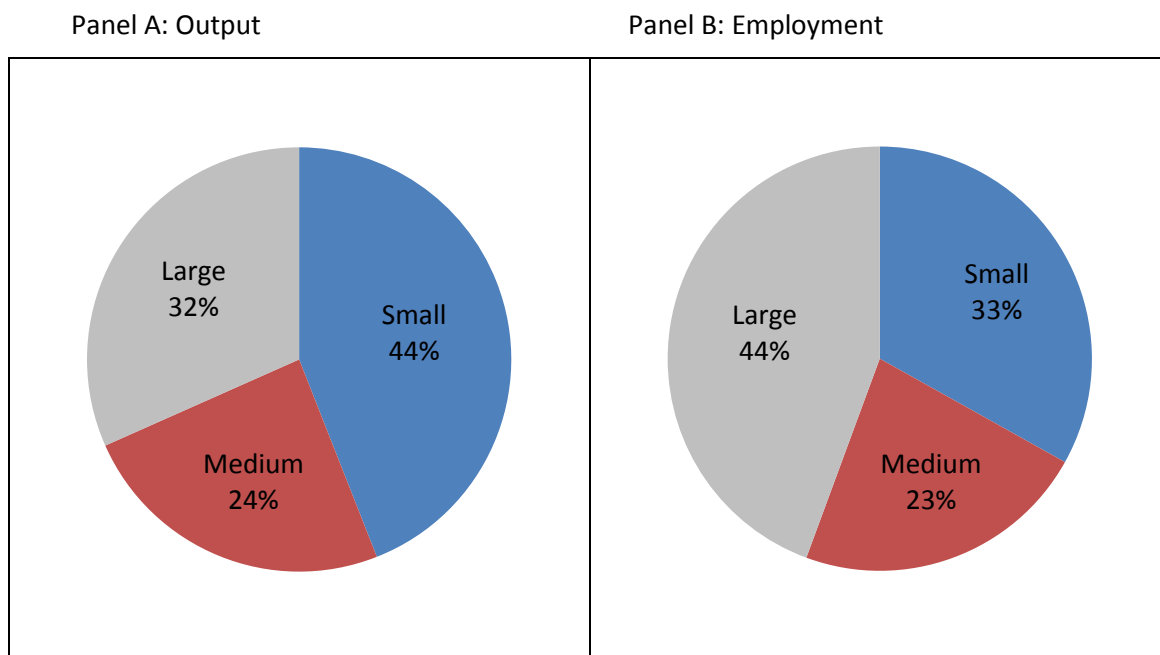
161. Section 3(g) of the *Fair Work Act 2009* outlines that the objects of the Act are to be met through an acknowledgement of the special circumstances of small and medium-sized businesses. Accordingly, decisions on the national minimum wage and modern award classification pay rates need to take into account the circumstances of small and medium businesses.
162. The Panel in its 2014 Annual Wage Review decision noted that aside from the general object of the Act, consideration of the circumstances of small businesses is necessary given their significance to the Australian economy. Most employers are small businesses, and award reliance is relatively high in small businesses compared to businesses generally.
163. The Australian Government agrees with the Panel's assessment on the important role played by small businesses in the Australian economy, through its contribution to economic growth and employment. When making its decision, the Panel should carefully consider the unique features of small businesses and help provide a supportive environment to ensure their viability and growth.
164. The Panel noted in last year's decision that:
- “There is no evidence to suggest that the economic conditions for small businesses have diverged materially from those of businesses generally within the industries in which they operate, as reflected in aggregate and sectoral economic data”* (Fair Work Commission 2015b, Paragraph 257).
165. This small business chapter has been included to provide additional information to help inform the Panel on small business developments, in particular to present the evidence that small businesses are finding conditions more difficult than larger businesses.

5.2 Small businesses in Australia

5.2.1 Importance of small businesses in Australia

166. Small businesses are a significant part of the Australian economy and make an important contribution to output and employment. They are diverse, operate in all sectors of the economy, have varying levels of employment, and conduct business under different legal structures.
167. There were 2,066,523 actively trading small businesses in Australia as at June 2015, accounting for 97 per cent of all businesses (ABS 2016b).²⁵ Of these small businesses, 781,908 (or 38 per cent) were employing small businesses.
168. As at 30 June 2014, small businesses contributed around 33 per cent of non-financial private (i.e. excluding general government, the Financial and insurance industries) sector value added and employed around 4.7 million Australians, or 44 per cent of non-financial private sector employment in Australia (Chart 5.1).

Chart 5.1: Small business share of non-financial private sector



Source: ABS 2015a, *Australian Industry, 2013-14*, Cat. No. 8155.0.

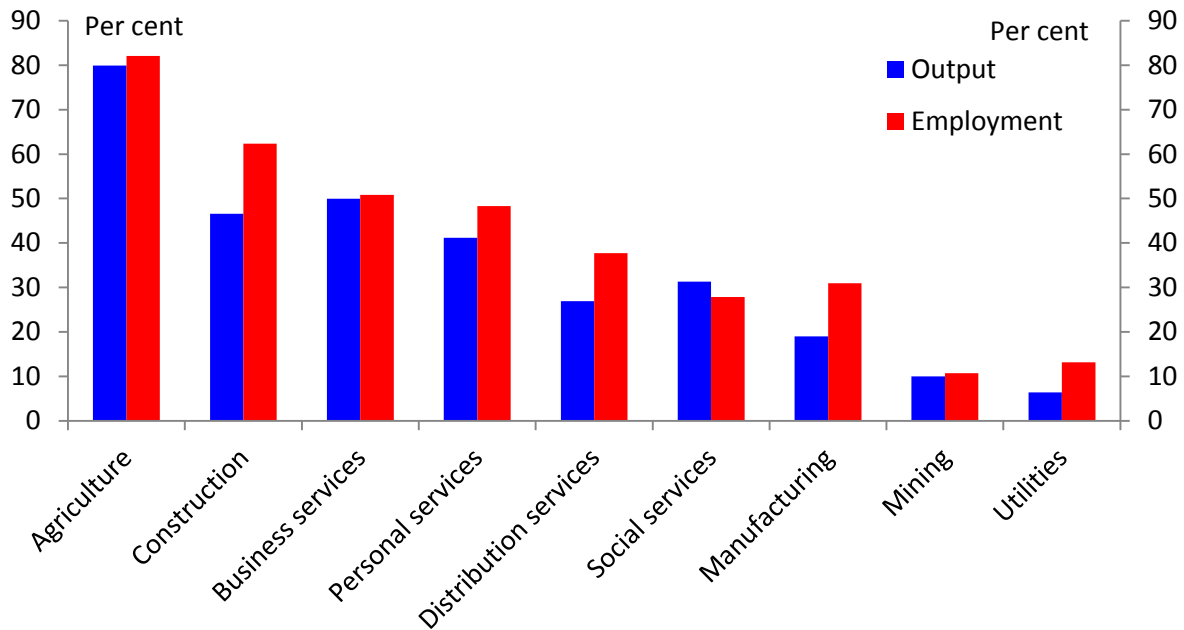
Note: Measures non-financial private sector output (Industry Value Added) and employment (number of individuals employed). These data excludes the general government, Financial and insurance industries.

169. Small businesses operate in every sector of the Australian economy, although their contribution to output and employment varies between sectors (see Chart 5.2). Small businesses are particularly prevalent in the Agriculture, Construction and Services

²⁵ For the purpose of this submission, small businesses are defined as a business employing 0 to 19 employees. This is consistent with the definition used by the ABS, Sensis and the Australian Chamber of Commerce and Industry for the purpose of business surveys. We note that small businesses are defined as a business employing 0 to 14 employees for the purposes of the *Fair Work Act 2009*.

industries. They are less prevalent in industries such as Mining, Manufacturing and utilities.

Chart 5.2: Small business share of private sector output and employment within each industry



Source: ABS 2015a, *Australian Industry, 2013-14*, Cat. No. 8155.0.

Note: Distribution services includes Wholesale trade, Retail trade, Transport, postal and warehousing, and Information media and telecommunications. Business services includes Rental, hiring and real estate services, Professional, scientific and technical services, and Administrative and support services. Social services includes Public administration and safety, Education and training, and Health care and social assistance. Personal services includes Accommodation and food services, Arts and recreation services, and Other services.

170. Small businesses contribute to a greater proportion of employment compared to output in almost every industry which suggests that small businesses may be more labour intensive (that is, on average they have lower labour productivity) than larger businesses within the same industry.
171. As a share of annual turnover, labour costs also comprise a significant component of total expense for small businesses. As at June 2014, for small employing businesses across all industries, labour costs account for around 16 per cent of total expenses (ABS 2015a).²⁶ Across sectors, they can range from as high as 39 per cent in Administrative and support services to as low as 6 per cent in the Mining sector.

5.2.2 Award coverage

172. Small businesses are more award-reliant than large businesses.
173. According to the latest *Employee Earnings and Hours* data (ABS 2015e), small businesses alone account for around 38 per cent of total employees on award classification wages.

²⁶ The ratio is slightly higher for medium and large businesses. This possibly reflects an under-bias for small businesses, where small business owners choose to take out returns in the form of equity and dividends rather than wages and salary.

Further, around 32 per cent of employees in a small business are paid award classification wages compared to 11 per cent of employees in larger businesses (with 100 or more employees).

174. When considering award coverage by sector, the Accommodation and food services sector (43 per cent of total employees across all methods of setting pay), the Administrative and support services (37 per cent), the Retail trade sector (29 per cent) and the Health care and social assistance sector (22 per cent) account for 62 per cent of all award employees (ABS 2015e). These four sectors are heavily comprised of small business, as a proportion of total businesses: 92 per cent, 95 per cent, 95 per cent and 97 per cent respectively (ABS 2016b).

5.3 Characteristics of small businesses

175. There are certain characteristics of small businesses that make them particularly sensitive to the challenging economic conditions that Australia is experiencing – they are generally less diversified in their product offerings and customers, less equipped to deal with soft demand and have less flexibility in terms of meeting workplace operational requirements.
176. This sensitivity is reflected in the survival rate of firms in the small business sector, which is lower than that for larger businesses. According to the ABS (2016b), only 68 per cent of micro-sized businesses (1-4 employees) that were operating in June 2011, were still operating as at June 2015 (for businesses employing 5-19 this figure is 77 per cent). In contrast, the survival rate for medium and large businesses is above 80 per cent.
177. Small businesses are more concentrated in their local area of operation. In 2014, 83 per cent of small businesses sold goods or services in their local area compared to 77 per cent of large businesses. In addition, only 7 per cent of small businesses had an overseas market compared with 34 per cent for large businesses (ABS 2015h).

5.4 Developments in the small business sector

5.4.1 Overview

178. Small businesses have experienced a long period of weak trading conditions. Consistent with these conditions, employers remain cautious in taking on additional labour.
179. At an industry level, for small and medium enterprises (SMEs), the latest survey results suggest conditions are particularly challenging in the Retail sector. This sector has a relatively high proportion of award-reliant employees compared to other industries.
180. When combined with the difficulties faced by small businesses in passing on higher costs to consumers in the current economic environment, higher labour costs could present a major constraint.

5.4.2 Use of survey data

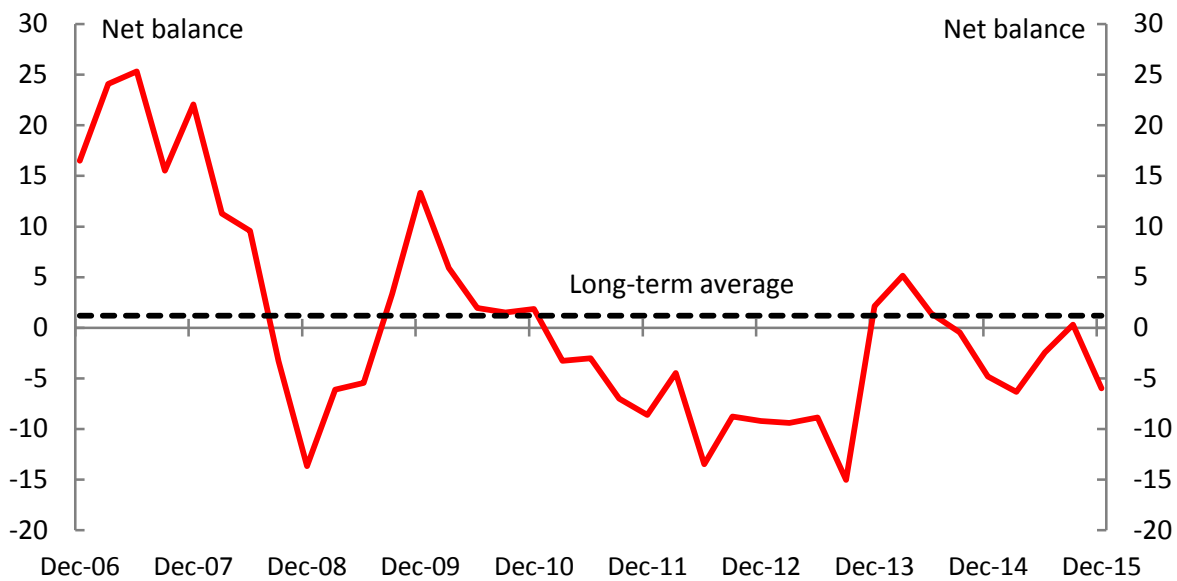
181. In its previous 2013-14 decision, the Panel expressed reservations about the reliability of the data from survey measures for the purpose of providing a representative picture at either an industry or an economy-wide level (Fair Work Commission 2014, Paragraph 226).

182. While official data from the ABS are preferable, small business data are often released with a significant lag, limiting their usefulness for this assessment. In these circumstances, survey measures provide a valuable alternative source of information. Those surveys commonly used and available include those published by the Australian Chamber of Commerce and Industry (ACCI), National Australia Bank and Sensis. These three large-scale surveys have samples ranging from around 600 to over 2600 respondents.
183. To obtain a robust inference, the Government examines a range of survey measures rather than one single measure.
184. The Reserve Bank of Australia (Park 2011; Alymer and Gill 2003) has concluded that while it is important to interpret the survey information with care, business surveys provide useful information about current and future economic activity, and also provide information on parts of the economy that is not readily available. The studies also note that in many instances, the survey data provide more timely information than official data.
185. The Reserve Bank of Australia (Park 2011) found that the information provided by the main business surveys closely track official data. The study reported a high correlation between survey measures of current business conditions (for either a multiple survey average or the National Australia Bank Quarterly Business Survey) and output growth (defined as the official ABS measure of nominal domestic demand).
186. The same Reserve Bank of Australia study suggests that the information content for survey measures on employment were even more significant. There is a high correlation between surveyed hiring intentions and official measures of trend quarterly employment growth. Furthermore, survey measures have also been found to be useful in informing forecasts of employment growth.

5.4.3 Business conditions for small businesses

187. Business conditions remain challenging despite some tentative signs of improvement.
188. The National Australian Bank SME survey (December quarter 2015) shows that the proportion of small businesses that experienced a worsening in business conditions over the December quarter outweighed the proportion of those that experienced an improvement. This result reverses the modest improvement that was seen over the previous two quarters.

Chart 5.3: NAB Business Conditions – Small Business



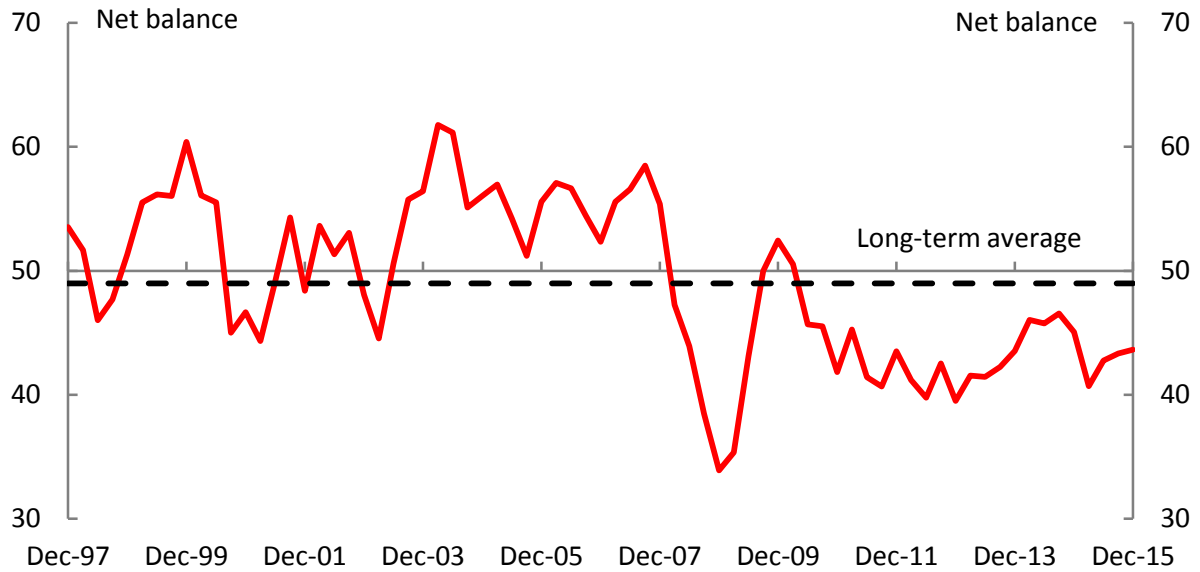
Note: Small business is defined here as the small tier SMEs (annual turnover of \$2-3 million) in the NAB survey. This is at the upper end of the general definition of small business for taxation purposes (\$2 million turnover). The long-term average is the average since June 2006.

Source: *NAB Quarterly SME Survey*, December Quarter 2015, seasonally adjusted data series.

189. The challenging conditions faced by small businesses are confirmed by the ACCI Small Business survey. This survey shows that actual business conditions continue to be difficult for small business and below average, with the proportion of small businesses experiencing a worsening in conditions outweighing those that have experienced an improvement (a negative net balance below 50 for ACCI survey).²⁷

²⁷ The ACCI responses are reported in net balance terms, with statistics represented using an index. An index level of 50 indicates that there is an exact balance between those who responded that the variable is growing and those who replied that the variable had declined. Thus, any level below 50 can generally be interpreted as meaning that the variable is falling and, conversely, a reading above 50 indicates the variable is increasing. Similarly, the NAB survey responses are reported using a net balance index, with an index reading of zero indicating an exact balance.

Chart 5.4: ACCI Business Conditions – Small Business

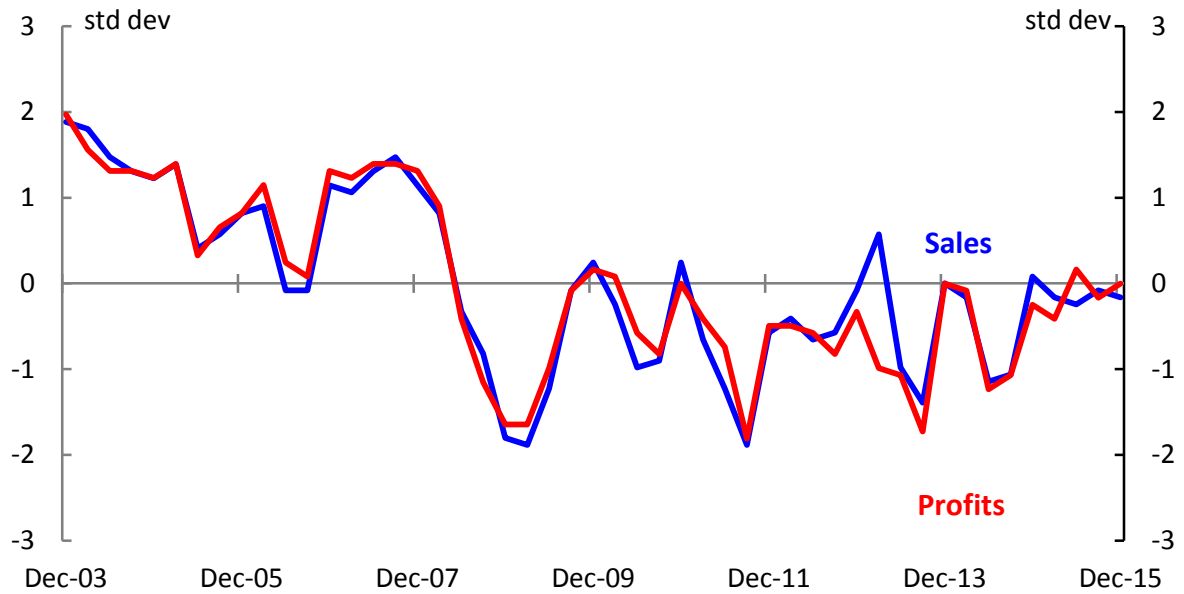


Source: ACCI Small Business Survey, December Quarter 2015.

Note: Small business size based on respondents with 1-19 employees. The long-term average is the average since December 1996.

190. The Sensis Business Index December quarter 2015 survey reports on sales and profitability. While the Sensis survey suggests that small business conditions may be better than that indicated by the NAB and ACCI surveys, it shows small business conditions remain modest.

Chart 5.5: Sensis Small Business Conditions for Sales and Profits

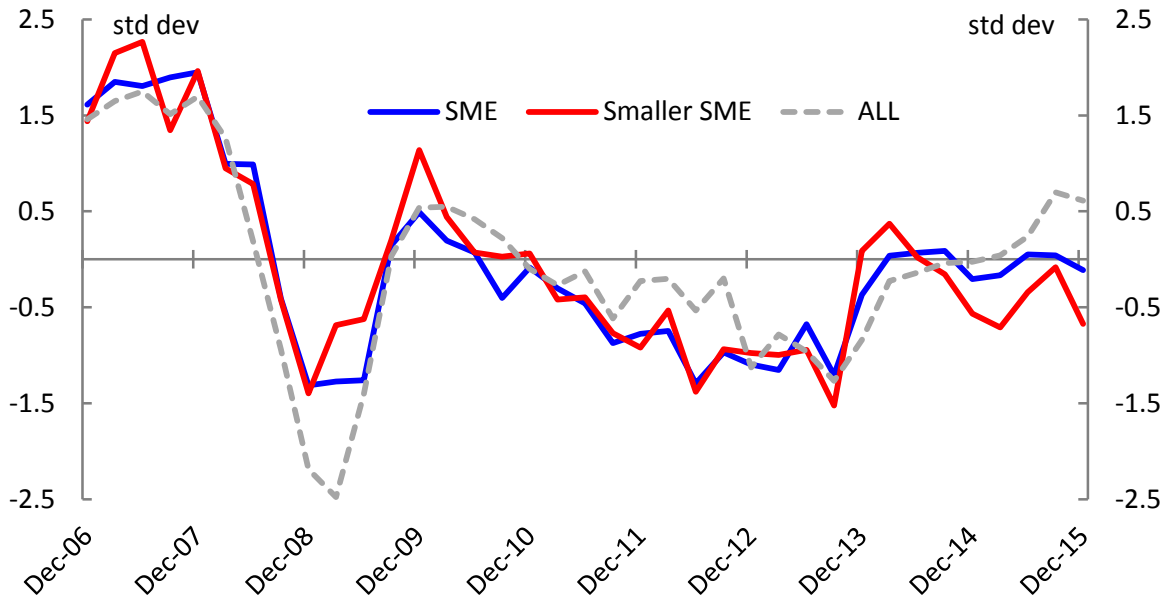


Source: Sensis Business Index, December Quarter 2015.

Note: Standard deviation from average since December 2003.

191. The NAB surveys also point to a divergence between the economic conditions of small and large businesses. As Chart 5.6 shows, business conditions for all businesses in general are above their long-term average, while conditions for small business remain below average. This is consistent with small businesses being more sensitive to uncertainty and challenging economic conditions.²⁸

Chart 5.6: Business Conditions Quarterly Business Survey and SME



Source: NAB Quarterly Business Survey and Quarterly SME Survey, December Quarter 2015, seasonally adjusted data series.

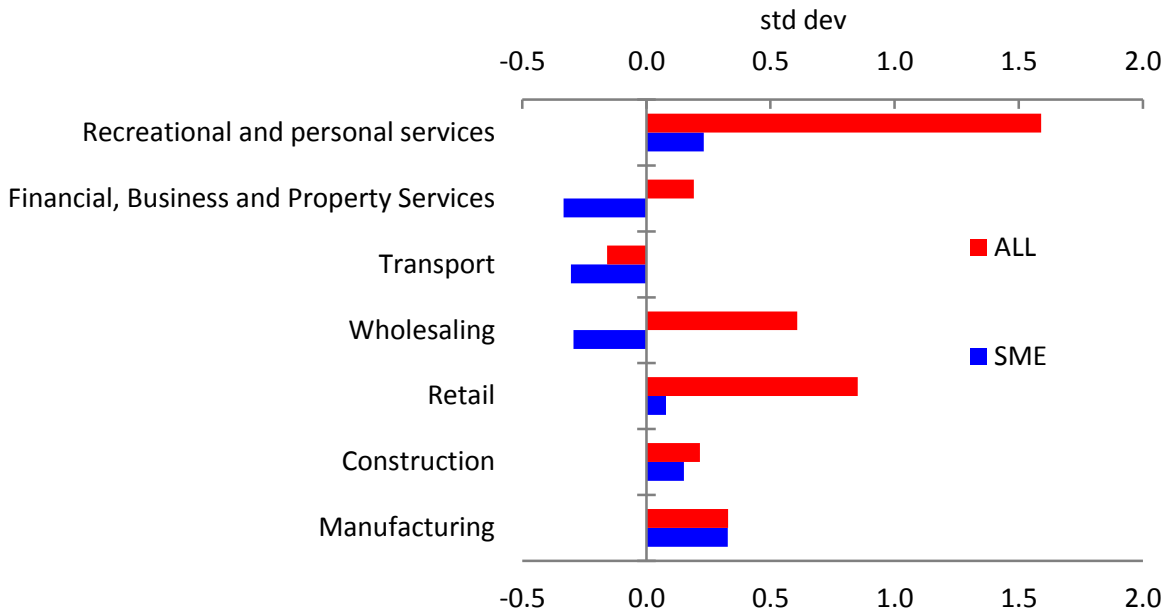
Note: Standard deviation from average since June 2006.

192. In addition, the NAB Quarterly ASX 300 Business Survey for the September quarter 2015 (which covers 80 firms across the ASX top 300 businesses) shows that the difference in business conditions faced by large and small business was at its widest margin since the survey began.

193. Chart 5.7 shows that business conditions are much better for larger business compared to smaller businesses for the more award-reliant industry of Retail and Recreational and personal services.

²⁸ Sensis does not report business conditions, nor does it provide a small and large business split for sales or profits.

Chart 5.7: Industry Business Conditions Quarterly Business Survey and SME

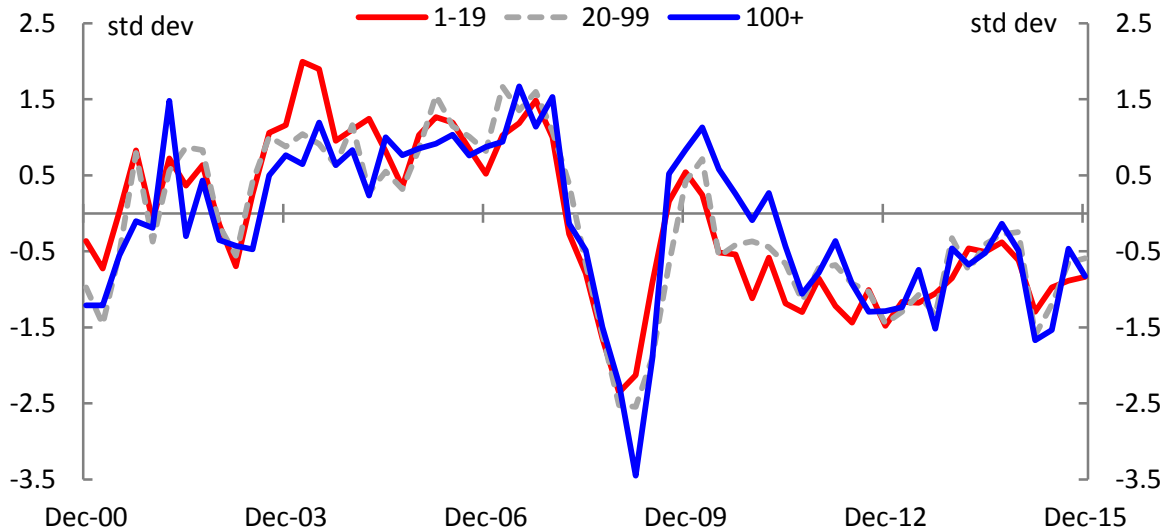


Source: NAB Quarterly Business Survey and NAB Quarterly SME Survey, December Quarter 2015, seasonally adjusted data series.

Note: Standard deviation from average since June 2006.

194. While the ACCI Business survey does not find a sharp divergence in business conditions for small and large business, it does show that conditions are difficult across all businesses.

Chart 5.8: ACCI Business Conditions Index by firm size



Source: ACCI Business Expectation Survey, December Quarter 2015.

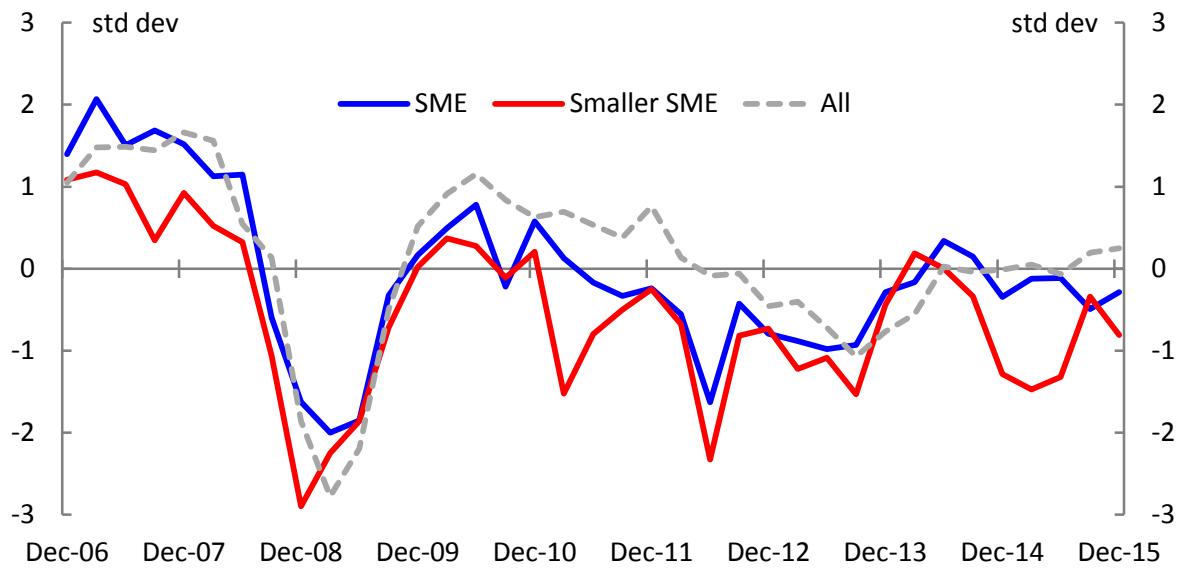
Note: Standard deviation from average since December 1996. Firm size based on employee numbers – small (1-19), medium (20-99) and large (+100).

5.4.4 Labour market

195. Small business employment remains subdued.

196. The NAB Business surveys indicate that small businesses remain cautious in their employment decisions, with more smaller SME’s reducing the size of their workforce compared to those that have reported an increase. For larger businesses, the employment situation is better than for small businesses.

Chart 5.9: NAB Employment Index by firm size

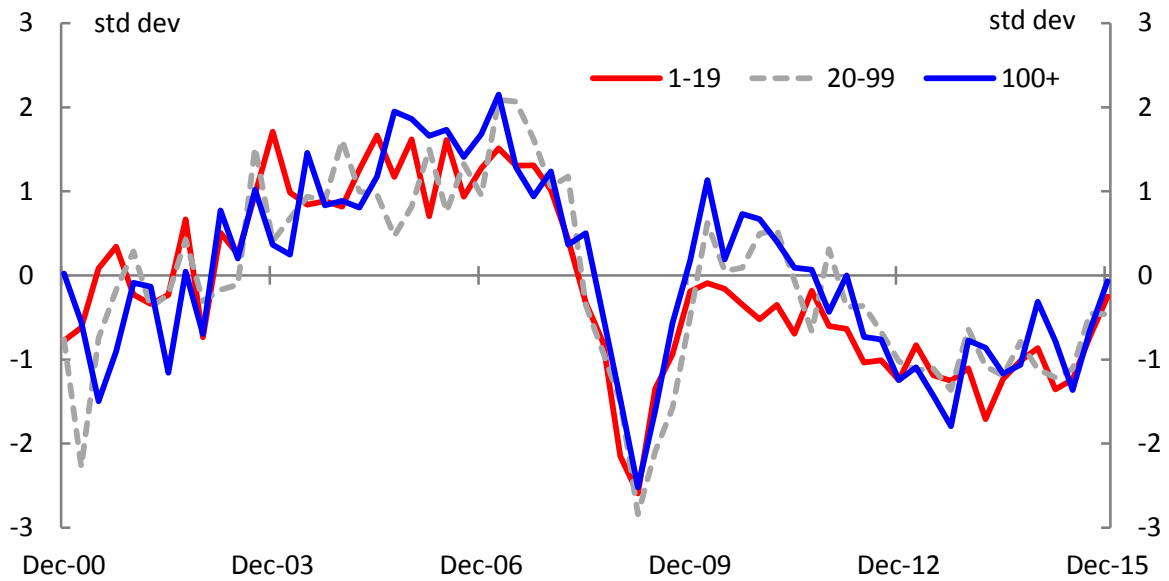


Source: NAB Quarterly Business Survey and NAB Quarterly SME Survey, December Quarter 2015, seasonally adjusted data series.

Note: Standard deviation from average since June 2006.

197. The ACCI Small Business Survey provides further confirmation that small business employment remains subdued although, there are tentative signs of improvement, with employment outcomes approaching the long-term average. Unlike NAB however, it shows employment remains subdued across all businesses.

Chart 5.10: ACCI Employment Index by firm size

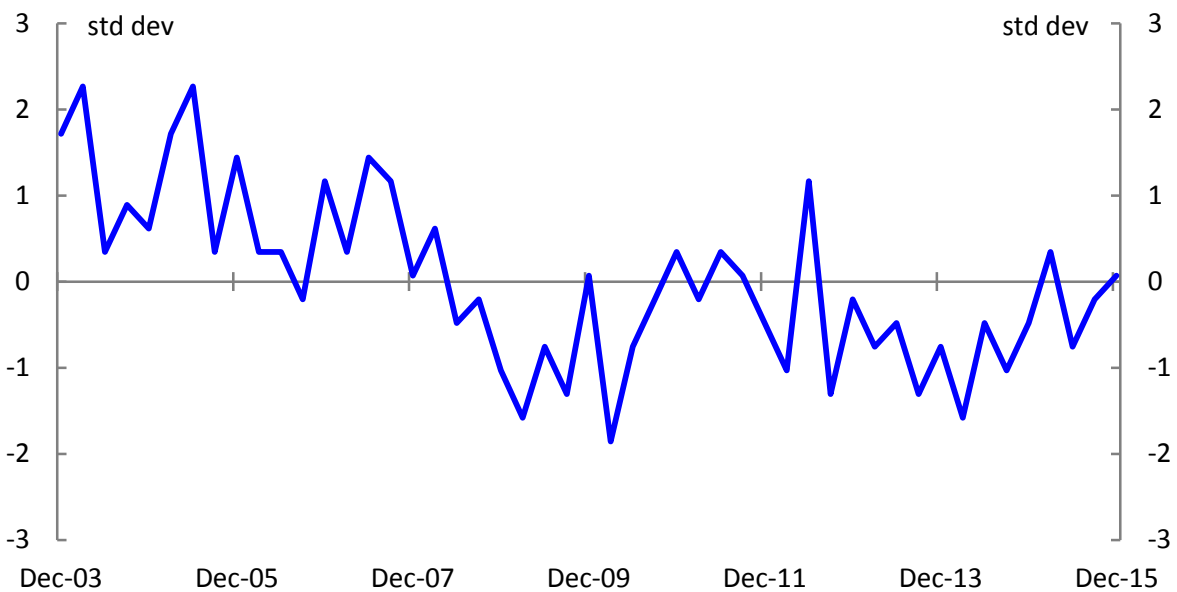


Source: ACCI Business Expectation Survey, December Quarter 2015.

Note: Standard deviation from average since December 1996.

198. The Sensis December Quarter 2015 Business Index also shows a persistent and subdued situation for employing, although there are tentative signs of improvement with responses on actual employment outcomes returning towards the long-term average (see Chart 5.11). Lack of work and sales was by far the most cited as the main barrier to taking on new employees (49 per cent of respondents). Expectations for the year ahead are positive with a net balance of +11 in the December quarter 2015, but are below the long-term average and there has been a noticeable downward shift from previous years (+13 in December 2014 and +19 in December 2013). The net balance reflects the difference between the proportion of respondents that expect an increase in their workforce over the next 12 months and the proportion that expect a decrease.

Chart 5.11: Sensis Actual Employment Index



Source: Sensis Business Index, December Quarter 2015.

Note: Standard deviation from average since December 2003.

5.5 Conclusion

199. The business environment for small businesses continues to be challenging. As a result, small businesses remain cautious about taking on new employees.
200. Proportionately large changes in minimum and award classification wages will particularly affect small businesses compared to larger businesses as they are more likely to be award-reliant.

6 Productivity, labour costs and wage-setting

Key Points

- Productivity growth in recent years, while encouraging, should not be interpreted as a direct signal of the affordability of wage increases for award-reliant employees over the short term.
- The scope for higher wages without impacts on inflation or employment is limited at present due to relatively weak economic conditions.
- Measures of productivity growth over short time periods can be volatile, cyclical and subject to measurement error.
- Enterprise bargaining provides a direct avenue for firms and workers to negotiate wage increases which are consistent with their particular circumstances.

6.1 Productivity growth and wages growth

201. Over the long run, real income growth and improved living standards are largely dependent on productivity growth, and real wages growth and productivity growth tend to move together. However, there are often short-run deviations which reflect labour market and economic conditions.
202. The high terms of trade arising during the resources boom resulted in rising real incomes, despite slower labour productivity growth. Strong growth in the purchasing power of Australian employees between 2003 and 2011 was driven by the high prices of resource exports.
203. The situation has now changed, with the terms of trade declining substantially, and labour market conditions softening. As a result, Australia has experienced slower income growth, despite improving labour productivity growth.
204. In this environment, researchers at the Reserve Bank of Australia have emphasised that amongst other measures *“high productivity growth and real wage restraint would also support Australia’s competitiveness”* (Atkin, Caputo, Robinson and Wang 2014). When economic growth improves, stronger labour market conditions should result in higher wages growth.

6.2 Trends in labour productivity growth

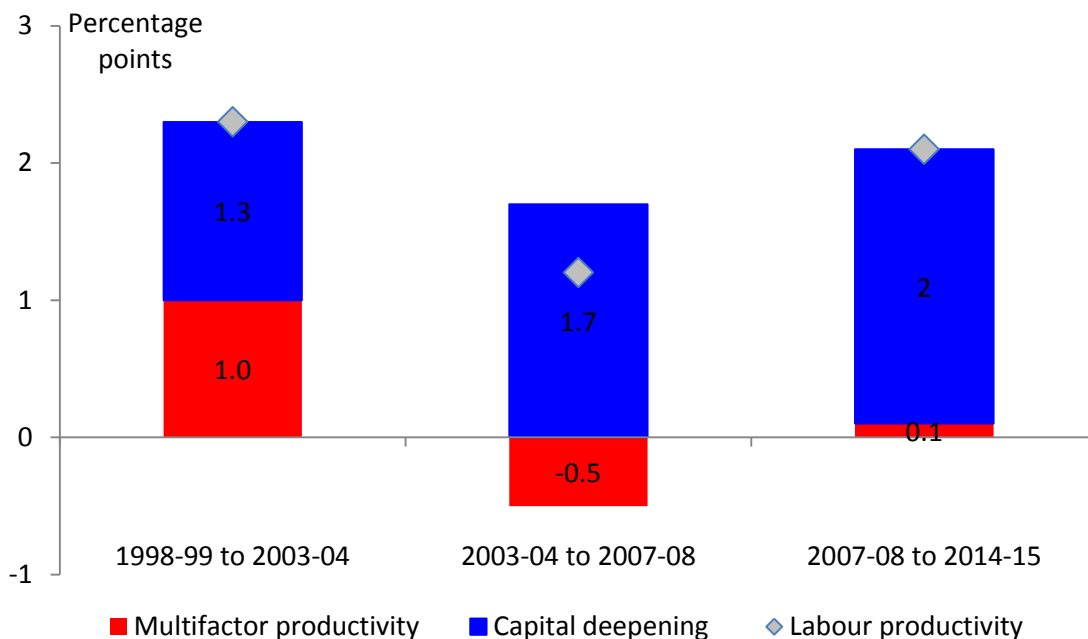
6.2.1 National labour productivity

205. Productivity growth slowed in the mid-to-late 2000s relative to the very strong productivity growth seen through the 1990s. This slowdown has been linked to a number of industry-specific factors, including significant investment in the Mining and utilities industries and the impact of drought on the Agriculture industry (Productivity Commission 2009).
206. For example, during the mining boom there was rapid investment in mining infrastructure, without an immediate rise in production, leading to lower measured productivity growth in the industry. The Productivity Commission estimated that between

2000-01 and 2006-07, lags in production accounted for around one-third of the decline in mining multifactor productivity growth (Topp, Soames, Parham and Bloch 2008). Capital investment during the mining boom is likely to have resulted in a short-term drag on overall productivity growth, despite contributing positively to national income.

207. Productivity data can be volatile, and the most recent data is frequently subject to revision. The latest annual data show that over the past five years labour productivity in the market sector has grown at an average annual rate of 2.1 per cent, higher than the 1.6 per cent over the five years prior (ABS 2015c). This is still below the record productivity growth rate seen through the late 1990s.
208. Labour productivity in the market sector rose by 1.6 per cent, in trend terms, through the year to the December quarter 2015. This followed growth of 0.7 per cent through the year to the December quarter 2014 and 2.4 per cent to the December quarter 2013 (ABS 2016a). This compares to the ten year average through to the December quarter 2015 of 1.8 per cent.
209. Chart 6.1 decomposes labour productivity over growth cycles into its two components:
- Capital deepening, which is a measure of the change in the amount of capital per unit of labour
 - Multifactor productivity, which measures the efficiency of use of labour and capital inputs in producing output

Chart 6.1: Contributions to labour productivity growth in the market sector



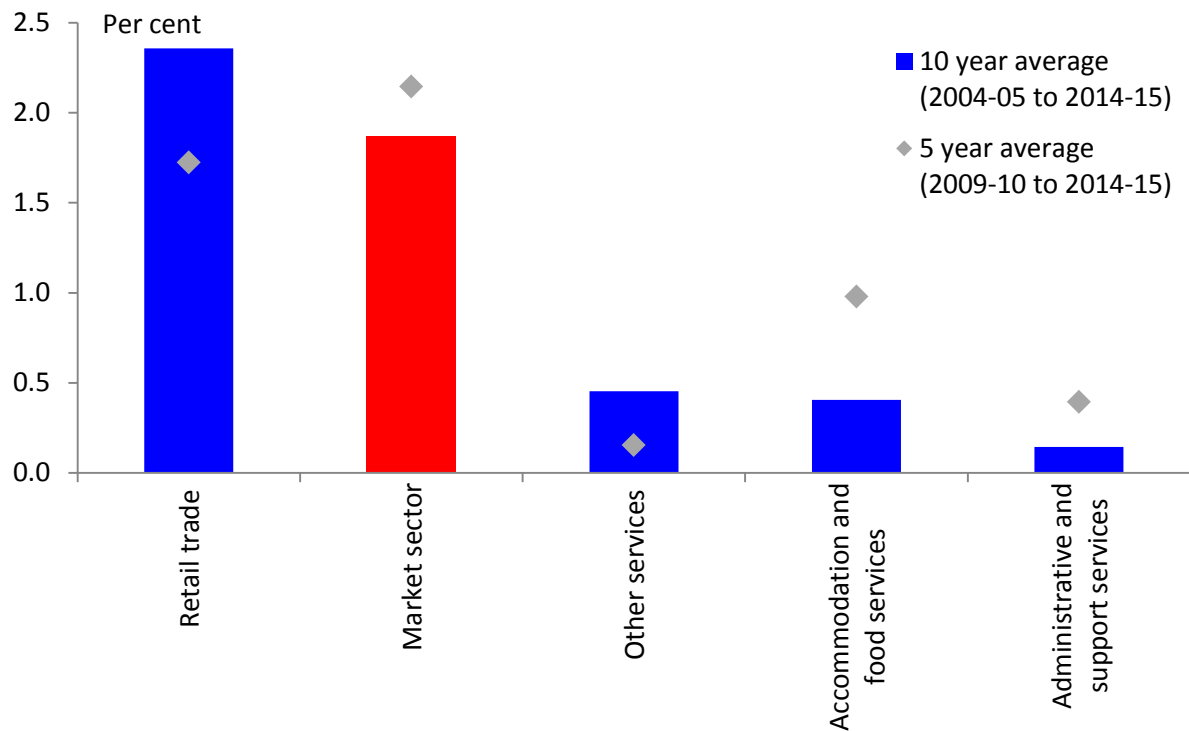
Source: ABS 2015c, *Australian System of National Accounts, 2014-15*, Cat. No. 5204.0. Department of Employment calculations.

Note: Data in original terms. 2007-08 to 2014-15 is not a complete productivity cycle according to the standard ABS definition and may be affected by rates of capacity utilisation.

6.2.2 Industry labour productivity

210. Labour productivity growth at the industry level varies considerably. This is a reflection of specific conditions in each industry, as well as a range of data measurement issues. For example, some recent fluctuations in Mining industry productivity may reflect misclassification of Construction employees as Mining employees during the mining boom. In general, industry level productivity data should be used with caution.
211. Moreover, in general, industry productivity growth rates are more highly correlated with prices growth than with wages growth (Lowe 1995). That is to say, industries with higher productivity growth tend to have lower rates of consumer price inflation, and vice versa. Wages growth at the industry level is likely to respond to the supply and demand for labour in that industry, which will be influenced both by productivity growth within that industry and productivity growth in other industries, as well as changing consumer tastes and preferences and a range of other factors such as broad economic conditions.
212. Nonetheless, the Panel should take into consideration that over the past decade, labour productivity growth in three of the four most award-reliant industries has generally been below the national market sector average of 1.9 per cent per year through to 2014-15 (see Chart 6.2). For example, Other services (0.5 per cent), Accommodation and food services (0.4 per cent), and Administrative and support services (0.1 per cent) had some of the lowest rates of labour productivity growth. Retail trade (2.4 per cent) recorded above average labour productivity growth over this period (ABS 2015c). Other relatively award-reliant industries such as Arts and recreation and Rental, hiring and real estate services have also recorded below average productivity growth over the last 10 years (although Rental, hiring and real estate has performed better over the last 5 years). Furthermore, the Health care and social assistance sector, which employs 15 per cent of award-reliant employees, also recorded below average productivity growth rates (0.6 per cent) over this period.

Chart 6.2: Average annual labour productivity growth by industry, ten and five year averages

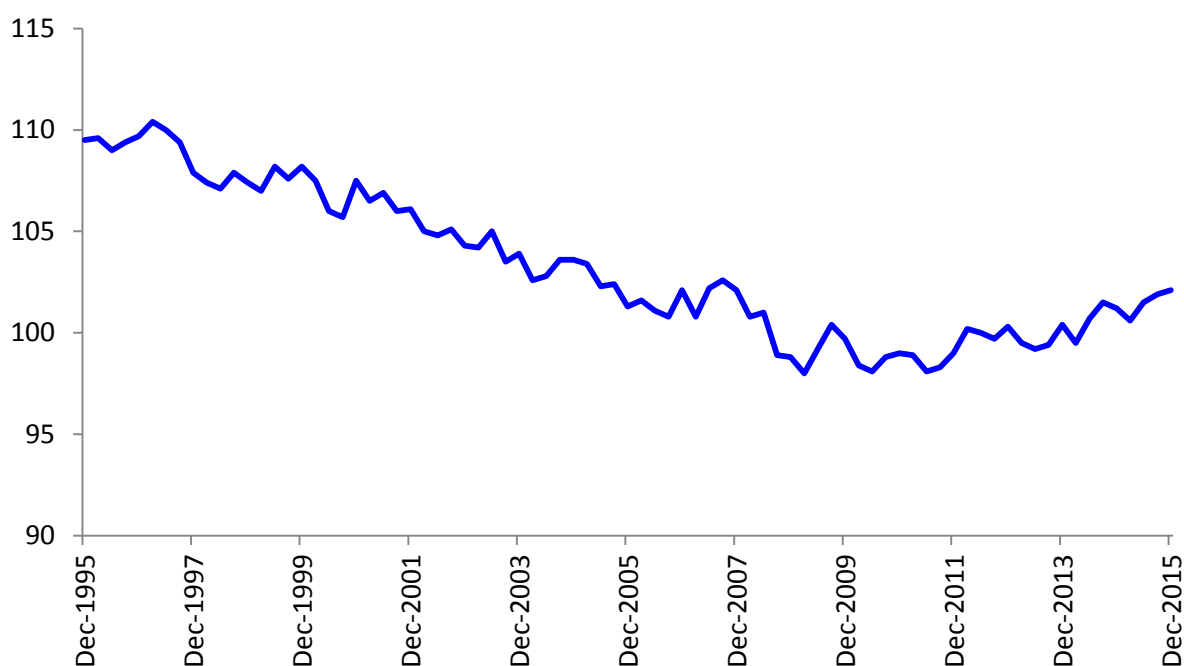


Source: ABS 2015c, *Australian System of National Accounts, 2014-15*, Cat. No. 5204.0
 Note: Industry data in original terms.

6.2.3 Real unit labour costs

213. Over the last twenty years Australia’s real unit labour costs²⁹ have declined by 0.3 per cent per year on average. After a large decline (2.9 per cent) around the time of the Global Financial Crisis in 2008-09, real non-farm unit labour costs have fluctuated over the past six years, with no clear trend discernible in the data (see Chart 6.3).
214. Increases in minimum and award classification wages that are greater than the growth in productivity and output prices in award-reliant industries would increase real unit labour costs in those industries, potentially putting pressure on prices and employment growth.

²⁹ Real unit labour costs are real labour costs per unit of output.

Chart 6.3: Real unit labour costs, December 1995 to December 2015

Source: ABS 2016a, *Australian National Accounts, Dec 2015, Cat. No. 5206.0*

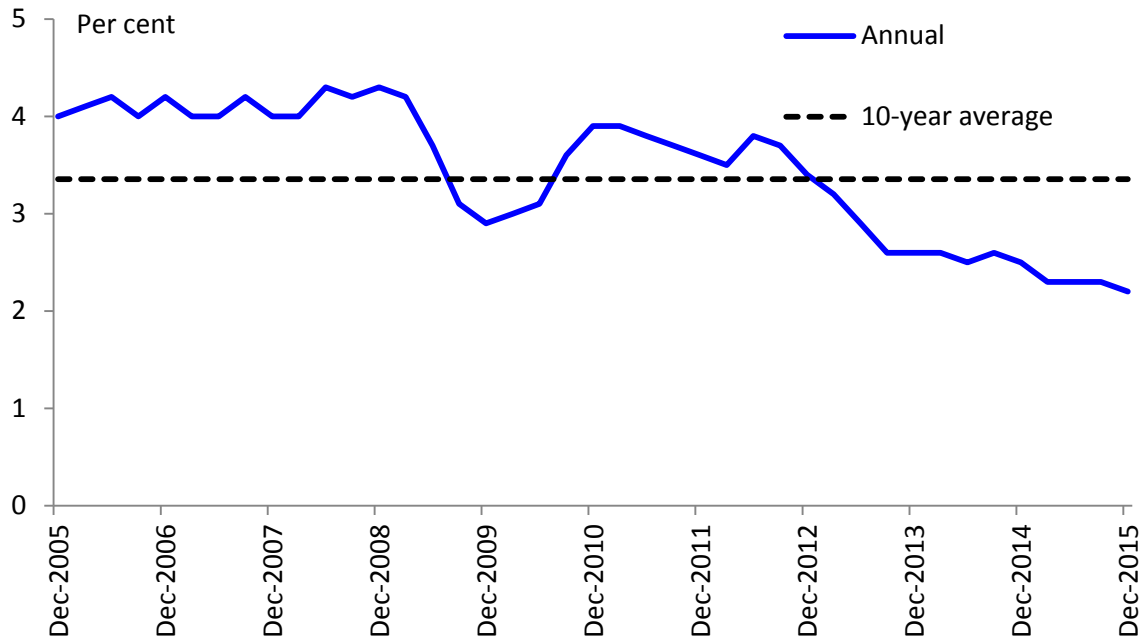
Note: Data are for the non-farm sector. Data in seasonally adjusted terms.

6.3 The relationship between productivity, wages and prices

215. Increases in productivity will result in some combination of higher wages for workers, lower prices for consumers, and higher profits for business. Historically, higher incomes from productivity growth have a strong tendency to flow through to real wage growth. This can occur either through higher nominal wage growth, or falling prices due to higher productivity, which will also result in higher real wages (since workers are also consumers).
216. As detailed in Section 6.2.1, since the period of slower productivity growth through the 2000s, labour productivity growth has, in more recent times, increased by comparison. Just as there is not necessarily an immediate decline in real wages growth when labour productivity growth is low, there has not been an acceleration of real wages growth in line with the recent increase in labour productivity growth.
217. As discussed in Chapter 3, and illustrated in Chart 6.4, economy-wide wages growth has been moderate.³⁰ Wages are currently growing at 2.2 per cent a year. This is more than a percentage point below the ten year average of 3.4 per cent per annum.

³⁰ Please note that the Wage Price Index uses a different measure of wages than the wage measure used to calculate real unit labour costs in Chart 6.3. Further, real unit labour costs are deflated using the GDP implicit price deflator.

Chart 6.4: Growth in wages, December 2005 to December 2015



Source: ABS 2016e, *Wage Price Index, Dec 2015, Cat. No. 6345.0*;

Note: Data for the Wage Price Index is in seasonally adjusted terms.

218. The Reserve Bank of Australia (2015) has identified a number of factors that are likely to have contributed to the restrained growth in wages.

“Below-average growth in economic activity has translated into subdued growth in labour demand, which has resulted in an increase in spare capacity in the labour market. At the same time, expectations for consumer price inflation have moderated to be below average. The decline in the terms of trade and falls in mining investment appear to have played a particularly important role, weighing on economic activity and placing pressure on firms to contain costs.”

219. This suggests that subdued labour market and economic conditions are weighing on wages growth. A common way of passing on wage increases is through higher prices. However, it is harder for firms to pass on higher prices in tougher economic environments. Various studies find that on average consumer demand is more sensitive to price increases during economic downturns (Gordon *et al.* 2013, Heerde *et al.* 2013). This is particularly the case for goods that comprise a higher proportion of consumers’ budgets (Gordon *et al.* 2013).

6.4 Promoting productivity growth through bargaining

220. Enterprise bargaining provides a direct avenue for firms and workers to negotiate productivity offsets for wage increases. Data from the ABS (2015e) *Employee Earnings and Hours* show that between 2010 and 2014, there was a decline in enterprise bargaining coverage, while award-reliance increased.

221. The Government considers that the minimum wage and award classification wages should act as a safety net for workers, noting that enterprise bargaining provides an

opportunity for workers and businesses to agree on workplace measures that best suit their needs and reflect changes in firm-level productivity.

222. Former Prime Minister Paul Keating (1993) said that the workplace relations framework should place its:

“...primary emphasis on bargaining at the workplace level within a framework of minimum standards provided by arbitral tribunals. It is a model under which...awards and...(centralised) wage increases would be there only as a safety net”.

223. A number of studies have looked at a range of workplace level evidence on productivity and bargaining. These include case studies, firm-level data and survey data. These are broadly supportive of a link between productivity and bargaining.

224. The Fair Work Act Review Panel (2012) report, *Towards more productive and equitable workplaces: an evaluation of the Fair Work legislation*, also supported this conclusion.

“It is widely, though certainly not universally, agreed among analysts that these economic reforms...including the transition to enterprise bargaining...removed impediments to more efficient production. These reforms may account for a significant part of the upswing in productivity through the 1990s”.

225. In making its decision, the Panel should have regard to object 3(f) of the Act and consider how its consideration of the safety net of a minimum wage and the comprehensive system of award classification wages can encourage enterprise bargaining, and consequently, additional productivity.

6.5 Conclusion

226. The Panel should be cautious in interpreting recent labour productivity growth as a signal of the appropriateness of minimum and award classification wage increases.
227. The Panel should consider productivity in the context of broader economic and labour market conditions and also consider other indicators such as inflation, employment growth and wages growth.
228. Wage increases that are not supported through productivity gains may have flow-on impacts on employment and inflation. This is particularly the case in a subdued economic environment.
229. The Panel’s decision should encourage enterprise bargaining, which provides a way for firms and workers to negotiate for wage increases consistent with the economic conditions facing the enterprise.

7 Employment Impacts

Key Points

- The Panel's decision should support employment growth. Employment is clearly beneficial to workers, their families and the communities in which they live. Low-paid jobs are often an entry point to the workforce and can act as stepping stones to higher paid work.
- The economic literature on the impacts of minimum wages on employment is complex and contested. However, there is broad agreement among economists that excessive increases to the minimum wage are likely to reduce employment growth. Economic research tends to suggest that any impact on employment growth will be greater during times of economic slowdown and among certain groups, such as young people.
- Given the benefits of work, it is important that the level of the minimum wage provides incentives for potential employees to look for and accept work. Government modelling shows that the minimum and award wage system currently provide sufficient financial incentives to work, across a range of household types.

7.1 The importance of low-paid work

230. Jobs provide benefits to individuals, their families and communities. Jobs can boost incomes, skills, and self-confidence and provide an opportunity for social engagement. People out of work tend to have poorer health and lower levels of wellbeing compared to those in work.
231. Low-paid jobs are important. They often act as an entry point into the workforce, through which people can build skills and experience to gain higher paid work in the future. Compared to people looking for work, people in low-paid jobs have a higher level of wellbeing and lower levels of financial stress.
232. Given these benefits of work, efforts must be made to ensure that everyone with the capacity to work has the opportunity to do so. The Panel's decision should recognise the importance of employment and make a decision that supports employment growth. It is particularly important that job opportunities are available for at risk groups, including low-skilled people, long-term unemployed people and young Australians.

7.1.1 Low-paid work transitions

233. Low-paid jobs offer an important entry point to the workforce. Around one-third (26.7 per cent) of people who enter the workforce do so by taking a low-paid job.³¹ Low-paid jobs are a particularly important pathway for some groups of workers. For example, 34.3 per cent of workers aged under 25 enter the workforce through low-paid work. Those with Year 12 qualifications or below (30.9 per cent) are also likely to enter the workforce through a low-paid job.

³¹ Refer to Chapter 2 and Appendix A for a definition of low-paid.

234. Low-paid employment is often temporary, with most low-paid workers exiting low-pay within two years. Table 7.1 shows that 67.1 per cent of people who entered low-paid work left within a year and a further 17.6 per cent left in the subsequent year.

Table 7.1: Duration in low-paid employment, per cent

Duration	Less than 1 year	1 to 2 years	2 to 5 years	More than 5 years
Proportion	67.1	17.6	13.1	2.1

Source: *HILDA Survey*, release 14 (December 2015), pooled waves 1 to 14.

Note: Data is based on flows into low-paid work, not the number of people in low-paid work at a point in time. Numbers are mutually exclusive.

235. Workers leaving low-paid jobs generally move into higher paid employment. Table 7.2 shows that of those workers leaving low-paid work within one year, 76.2 per cent left for higher pay, 17.1 per cent left the labour force, and 6.8 per cent became unemployed. The results are similar for workers leaving low-paid work after one to two years. For this group, 77.3 per cent left for a higher paid job, 15.9 per cent left the labour force and 6.7 per cent became unemployed. Of those workers leaving a low-paid job after two to five years, 81.0 per cent left for a higher paid job, 12.0 per cent left the labour force and 7.0 per cent became unemployed.

Table 7.2: Destination on leaving low-paid employment, per cent

Duration in low-paid employment	Higher paid work	Left the labour force	Unemployment
Less than 1 year	76.2	17.1	6.8
1 to 2 years	77.3	15.9	6.7
2 to 5 years	81.0	12.0	7.0

Source: *HILDA Survey*, release 14 (December 2015), pooled waves 1 to 14.

Note: Those remaining in low pay for 5 years or more are not shown due to a small sample size.

236. Furthermore, those people leaving low-paid work for higher paid work were often receiving significant increases in wages. The median increase in hourly wages for those moving from low-paid to higher paid jobs was 56 per cent.³²

237. Given that low-paid work is temporary for a majority of low-paid workers and serves as a pathway to higher paid work, increasing the national minimum wage and award classification wages is not an efficient way to raise the living standards of low-paid workers. It is important that the Panel's decision supports job growth and preserves job opportunities, particularly entry level job opportunities.

7.1.2 Satisfaction with low-paid work

238. It is important that low-paid work provides people with the capacity to meet their needs. Government analysis from the *HILDA Survey* shows that low-paid workers are generally more satisfied and have lower levels of financial stress than unemployed people and in some aspects they are just as satisfied as higher-paid workers.

³² *HILDA Survey*, release 13 (December 2014), pooled waves 1 to 13.

239. Respondents were asked to rank their satisfaction from 0 (totally dissatisfied) to 10 (totally satisfied). In 2014, low-paid employees (7.87) were on average more satisfied with their lives than unemployed people (7.39), and had a similar level of satisfaction to higher-paid employees (7.90) (see Table 7.3). Low-paid workers (7.52) were slightly less satisfied with their job satisfaction compared to higher-paid workers (7.64). Low-paid workers (7.05) were slightly less satisfied with their employment opportunities compared to higher-paid employees (7.34), but significantly more satisfied than unemployed people (4.65). Low-paid workers were less satisfied (6.22) with their financial situation³³ than employees who were higher-paid (6.74), but significantly more satisfied than people who were unemployed (4.67).

Table 7.3: Average satisfaction of low-paid workers (Score 0-10)

	Unemployed people	Low-paid employees	Higher paid employees
General life	7.39	7.87	7.90
Overall job	N/A	7.52	7.64
Employment opportunity	4.65	7.05	7.34
Financial situation	4.67	6.22	6.74

Source: *HILDA Survey*, release 14 (December 2015), wave 14.

Note: Respondents ranked their satisfaction from 0 (totally dissatisfied) to 10 (totally satisfied).

240. Low-paid workers were not only more satisfied with their financial situation than unemployed people, but on average they experienced lower levels of financial stress. In 2014, 39.0 per cent of unemployed people had at least one type of financial stress³⁴ compared to 26.6 per cent of low-paid employees and 17.9 per cent of employees who were higher-paid (see Table 7.4). Unemployed people were also more likely to experience multiple financial stress indicators. For example, 10.5 per cent of unemployed people experienced four or more financial stress indicators compared to 4.4 per cent of low-paid employees and 1.7 per cent of employees who were higher-paid.

Table 7.4: Percentage of people who reported financial stress, 2014

Number of financial stress indicators	Unemployed people (%)	Low-paid employees (%)	Higher-paid employees (%)
None	61.0	73.4	82.1
One	14.3	11.9	9.4
Two or three	14.2	10.3	6.8
Four or more	10.5	4.4	1.7

Source: *HILDA Survey*, release 14 (December 2015), wave 14.

³³ Financial satisfaction includes satisfaction with individual earnings, household income, wealth, access to savings and expenditure requirements.

³⁴ Employees are considered to have experienced some financial stress if they answered yes to at least one of seven financial stress indicators. The list of the seven financial stress indicators are: Could not pay electricity, gas or telephone bills on time; Could not pay the mortgage or rent on time; Pawned or sold something; Went without meals; Was unable to heat home; Asked for financial help from friends or family; Asked for help from welfare/community organisation.

7.2 Minimum wages and employment growth

7.2.1 Minimum wages and economic theory

241. Given the benefits of work and the consequences of unemployment, it is important that the level of the minimum wage supports employment growth. Minimum wages can affect employment growth through their impact on the supply and demand of labour.
242. Classical economic theory suggests that higher minimum wages will reduce employment growth. The theory suggests that when faced with an increase in labour costs and the resulting loss in profitability, businesses will respond by increasing prices for goods and services or by reducing employment. This may occur through a reduction in the hours worked by existing staff and/or a reduction in the numbers of jobs. Minimum wage increases also provide stronger incentives for people out of work to look for and accept work and for people in work to increase their hours. Under the classical approach, the net effect of an increase in the minimum wage is a reduction in jobs growth and an increase in unemployment and underemployment.
243. Alternate theories do provide some circumstances in which employment may not be impacted or could even increase as a result of increases to the minimum wage (for a summary see Productivity Commission 2015b and Bray 2013).

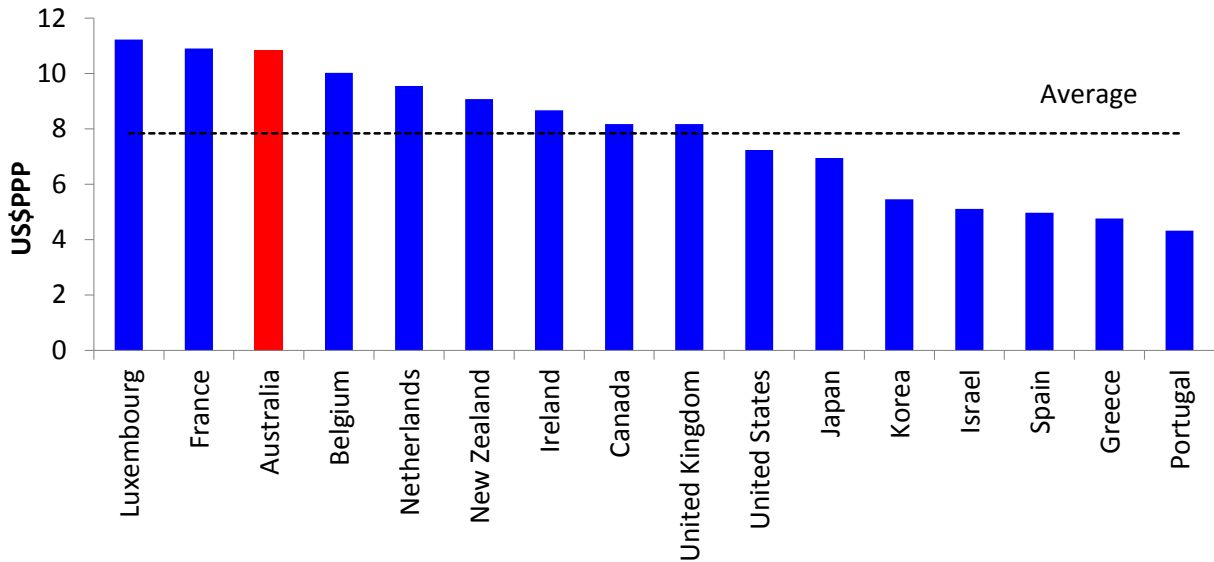
7.2.2 Empirical evidence

244. There is a substantial body of international research on the impacts of minimum wages on employment. The literature is complex and there is competing evidence on the size and direction of the impact. Some researchers (see Neumark and Wascher 2008) have found that minimum wage increases reduce employment, while others (see Card and Krueger 1995) have shown that employment gains are possible in some circumstances.
245. There is difficulty undertaking research in this area and this contributes to the divergent results. For example, results may depend on the data source, the time period analysed, the cohort of analysis, the research techniques used and how confounding factors are controlled for, such as changes in economic growth and underlying structural trends. There is further difficulty in applying the findings found in one circumstance to another, as the findings are likely to be influenced by factors such as the economy, institutional arrangements and coverage of the minimum wage.
246. Most of the international research has been conducted in the United States. Compared to other developed economies, and particularly the United States, Australia's minimum wage system is very different. Around one-fifth of Australians have their pay set by an award and the national minimum wage is generally higher than in other developed countries. In 2015, Australia's national minimum wage was the third highest in the OECD in purchasing power parity terms (see Chart 7.1) and Australia's minimum wage bite³⁵ was considerably higher than the bite in the United States (see Chart 7.2). An international comparison of Australia's national minimum wage with other countries does

³⁵ The minimum wage bite measures the adult minimum wage as a proportion of median earnings.

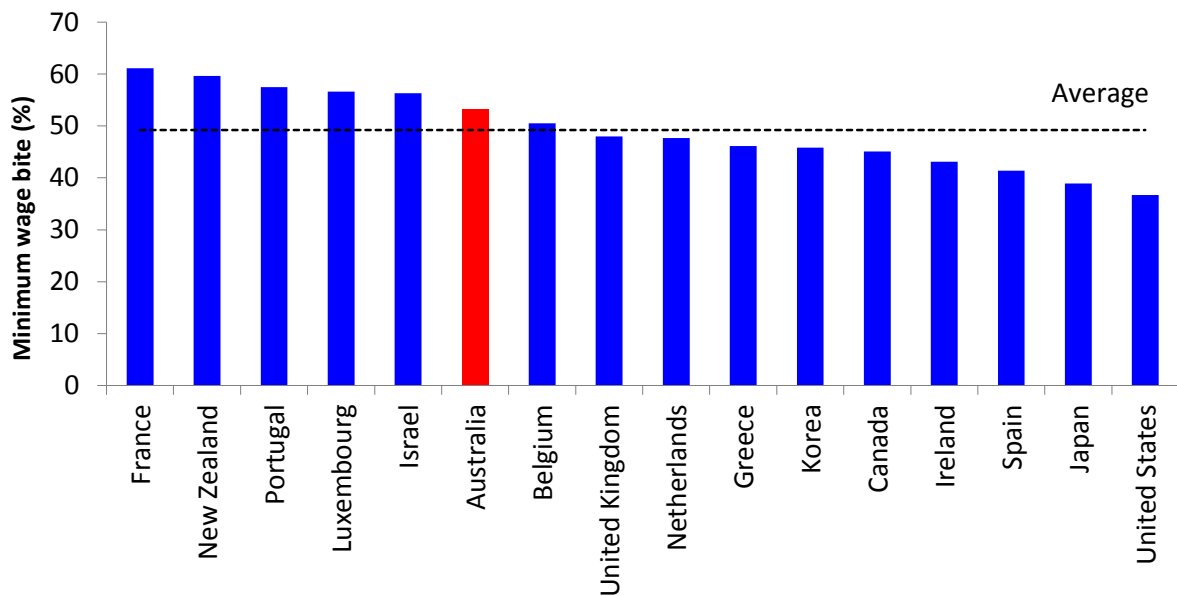
not take into account Australia’s unique award system. In 2014, the median full-time award-reliant worker earned 56.2 per cent more than the national minimum wage (refer to Chapter 2). Therefore, it is necessary to be cautious in applying findings from international research to Australia.

Chart 7.1: Minimum wage among comparable OECD countries, purchasing price parity terms, 2015



Source: *OECD Stat Extracts*, stats.oecd.org, extracted March 2016.

Chart 7.2: Minimum wage bite among comparable OECD countries, 2014



Source: *OECD Stat Extracts*, stats.oecd.org, extracted March 2016.

247. There have been relatively few Australian studies on the employment impacts of minimum wage increases. The studies that do exist tend to find a negative impact of minimum wage increases (see Leigh 2003, 2004a, 2004b). However, we must be cautious

in interpreting these results because these studies are often dated or have data and/or methodological issues.

248. More recently the Productivity Commission (2016) undertook economic modelling of the impact of minimum wages on employment, finding that a one per cent reduction in the growth of award wages for five years from 2017-18 would increase the number of aggregate full-time equivalent jobs by around 150,000 by 2024-25.³⁶ This modelling is based on a hypothetical scenario and results may differ under different sets of assumptions.
249. Despite the mixed results in the empirical literature and the different views held by economists, there is stronger evidence to support the following:
- Studies have tended to show that minimum wage increases have a greater negative impact on the employment of young people (see Boockmann 2010, Neumark and Wascher 2008).
 - Studies have tended to show that changes to minimum wages have larger impacts on employment when the economy is in a recession or a prolonged economic slowdown (see Addison et al. 2013, Dickens et al. 2012).
 - Economists generally acknowledge that if set too high, or if increases are too large, the minimum wage will have disemployment effects. For example, even Card and Krueger (1995) whose research has shown positive employment impacts of minimum wage increases have stated that *“at sufficiently high levels of the minimum wage, the predicted employment losses of the standard model will be borne out”*.
250. These areas are particularly relevant to the Panel’s considerations. The Panel has an important role in promoting job growth for young people at a time when youth unemployment is high. Furthermore, the Panel should be aware that it is more likely that increases in the minimum wage will have a negative employment impact in the current period of higher unemployment and slower economic growth. In addition, while one wage decision may not seemingly have a large effect on employment, noting the consensus view that a sufficiently high minimum wage will have an impact, over the long-term the cumulative impact of multiple decisions will be greater.
251. The Panel should be aware of the risk that increases in minimum wages can impact jobs and the hours worked by existing employees. Underemployment is an important issue, particularly when noting that for many households low income is not just a result of low hourly pay but also a result of lower working hours (refer to Chapter 2).
252. In making its decision, the Panel should be mindful of the evidence on the employment impacts of minimum wages. The Panel’s decision should note the risk of increasing minimum wages given that excessive increases, and increases beyond a certain level, are likely to have a negative impact on employment growth.

³⁶ The Productivity Commission notes that some of the increased demand for employment may be absorbed through existing employees working more hours.

7.2.3 Minimum wages and incentives to work

253. The level of the minimum wage can influence people's decisions to look for and accept work. It is important that the minimum wage is set at a level that encourages people who are out of work to enter work in order to enjoy the benefits that work can provide to individuals and communities. The level of the national minimum wage currently provides sufficient financial incentives to work across a wide range of household types. Accordingly, modern award wages, which are often substantially higher than the national minimum wage, provide even greater incentives to work.
254. The Government has modelled the interaction between the tax-transfer system and the national minimum wage for a broad range of hypothetical single and second earner households.³⁷ The modelling shows that all of the household types modelled were substantially better off when an unemployed member of the household gained a job at the national minimum wage. Some examples are provided below, with detailed tables in Appendix C.
255. A single adult household, without children, would increase their disposable income by \$324 per week (120 per cent) by moving from unemployment and into a full-time job paying the national minimum wage. Even by taking a part-time job³⁸ at the national minimum wage, disposable income would increase by \$142 per week (52 per cent).
256. An unemployed couple without children would be \$240 per week (49 per cent) better off if one unemployed member of the household found a full-time job at the national minimum wage. A couple without children with one adult already in full-time employment at the national minimum wage would be \$460 per week (63 per cent) better off if the second member of the household moved from unemployment into full-time minimum wage work.
257. Households with children are also better off when an unemployed adult gains a job at the national minimum wage, even after paying for any necessary childcare costs. For example, a couple with a three year old child, with one member of the couple in a full-time job at the national minimum wage would be \$171 per week (19 per cent) better off if the second member of the couple also found a full-time national minimum wage job. If the second member of the household took a part-time job at the national minimum wage the household would increase their disposable income by \$60 per week (7 per cent).

7.3 Conclusion

258. The Panel should be conscious of the benefits of work and the negative impacts of unemployment on the individual and community. Low-paid jobs provide an important

³⁷ The analysis considered the potential impact of earnings from a job at the national minimum wage on combined household income, after income support (Newstart Allowance or Parenting Payment), other transfer payments (such as Family Tax Benefits and Rent Assistance), other earnings (if other members of the household were already receiving earned income from employment), childcare costs and taxation. The assumptions used in the analysis are detailed in Appendix B.

³⁸ Working 15 hours per week at the national minimum wage.

entry point into the workforce, particularly for at risk groups such as young people, the low-skilled and the long-term unemployed.

259. Economists generally agree that minimum wage increases will cost jobs when increases to the minimum wage are excessive or when the minimum wage is set too high. It is important that the Panel is mindful of the impact of successive minimum wage increases on employment, noting that the long-term cumulative impacts of minimum wage increases are likely to be greater than the impact of one decision.
260. Economists tend to agree that any negative impacts will be larger for certain cohorts, including young people, and during times of weaker economic conditions. The Panel should be aware of the risk that their decision may reduce employment growth and make a decision that supports jobs growth and protects job opportunities for all Australians, and particularly for young Australians, the low-skilled and those who are long-term unemployed.

8 Household Incomes and Inequality

Key Points

- The minimum wage and the earnings of the low-paid have grown in real terms, although not as quickly as average or higher earnings.
- Household income inequality is a more useful measure than individual earnings inequality for assessing differences in living standards. In Australia, it has risen modestly, but remains well below the levels seen in the US and UK.
- Minimum wage increases have a limited and uncertain effect on income inequality.
- The minimum wage is not the best instrument to address the gender pay gap.
- The tax-transfer system provides substantial redistribution to low-income households and families with children, including minimum wage earners.

8.1 Earnings inequality and income inequality

261. Since the national minimum wage was introduced in 1997, it has increased on average by 3.4 per cent a year in nominal terms and 0.7 per cent a year in real terms. This is less than growth in median full-time earnings, which averaged 4.4 per cent a year in nominal terms and 1.5 per cent a year in real terms to 2014 (ABS 2015d).
262. Therefore, the minimum wage bite (the ratio between the minimum wage and median earnings) has declined from 62 per cent in 1997 to 53 per cent in 2014. This is still above average for comparable OECD countries (see Chart 7.2). Most of the decline occurred in the late 1990s and the mid 2000s, with the early 2000s and the period since 2008 exhibiting relative stability.
263. This picture is mirrored in the wider earnings distribution. Table 8.1 presents the real weekly earnings of full-time adult employees between 1994 and 2014 for various points in the earnings distribution. It shows that real earnings have grown at all levels, more rapidly in the second decade than the first. However, growth rates were highest amongst the higher-paid. According to the OECD (2011), earnings inequality increased in most OECD countries between the mid-1980s and mid-2000s. The increase observed in Australia is consistent with the international trend.

Table 8.1: Growth in full-time real weekly earnings, 1994 to 2014

% growth:	1994 to 2004	2004 to 2014
10th percentile	6.3	12.9
50th percentile (median)	11.1	19.0
90th percentile	17.9	27.1

Source: ABS 2015e, *Employee Earnings and Hours*, Cat. No. 6306.0, published and unpublished data.

Note: 1994 to 2004 growth is for ordinary time earnings and 2004 to 2014 is for total cash earnings.

264. Disposable income is a more comprehensive measure of living standards. It is measured at the household rather than the individual level, to take account of sharing between family members, and is adjusted for household size ('equivalised'). It takes account of the number of people in jobs within a household, investment income, direct taxes, and transfer payments, not just the earnings of those in jobs.

Table 8.2: Growth in equivalised real household disposable income, 1994-95 to 2013-14

% growth:	1994-95 to 2003-04	2003-04 to 2013-14
10th percentile	20.0	28.1
50th percentile (median)	24.0	28.5
90th percentile	23.2	34.5

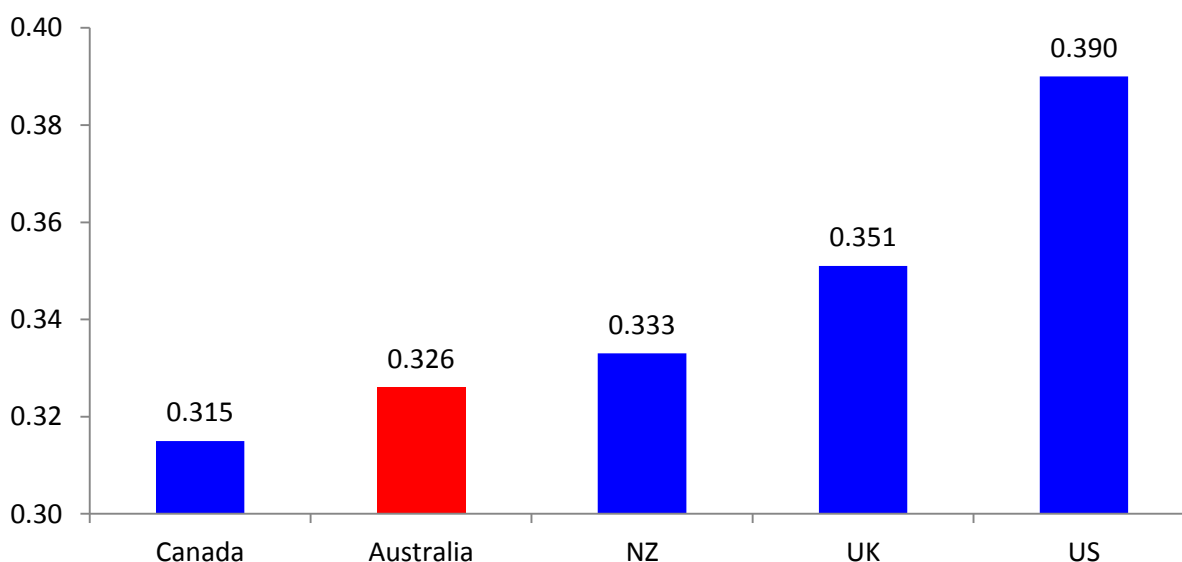
Source: ABS 2015f, *Household Income and Wealth, Australia, 2013-14*, Cat. No. 6523.0.

Note: Estimates for 2007–08 onwards are not directly comparable with previous estimates due to improvements in income measurement. Estimates for 2003–04 and 2005–06 have been recompiled to reflect the new measures of income, however not all components introduced in 2007–08 are available earlier.

265. Table 8.2 shows gains in household disposable income have been more evenly spread than gains in individual earnings. For the first decade, growth for the median household slightly exceeded growth for the (high-income) 90th percentile, while for the second decade, growth for the (low-income) 10th percentile was almost equal to growth at the median. Changes in ABS methods may have exaggerated the acceleration in high income growth during the second decade.³⁹

266. The Gini coefficient, a commonly used measure of inequality, has remained fairly stable from 2007-08 to 2013-14 (ABS 2015f). It has risen over the last two decades, although due to the changes in ABS methods mentioned above, the rise between 2003-04 and 2007-08 has probably been exaggerated.

267. As shown in Chart 8.1, Australia's level of income inequality after taxes and transfers remains well below levels in the UK and US. Piketty (2014) notes that "*the upper centile's [top 1%] share in the United States increased...about three times as much as in Australia*".

Chart 8.1: Gini coefficients, international comparison, 2012

Source: *OECD Stat Extracts*, stats.oecd.org, extracted March 2016.

Notes: Canadian data for 2011.

³⁹ Improvements in the Survey of Income and Housing, including a new definition of income, had a greater impact at the top of the income distribution (ABS 2013a, Fact Sheet 5). Income growth also appears to be higher than earnings growth generally, because of more rapid growth in employment and investment income, and changes to the tax-transfer system.

8.2 The minimum wage and inequality

268. Rises in the minimum wage probably reduce earnings inequality, to some extent. Neumark and Wascher (2008, p.p. 138-9) find that they create a spike at the lower end of the wage distribution, and possibly encourage wage rises above the legal minimum ('spillover effects'). However, they argue that the shift in demand away from less-educated workers has been a more important driver of earnings inequality. More recently, Autor, Manning and Smith (2014) come to similar conclusions, but suggest that the apparent spillover effects may be the result of measurement error.
269. The effect on income inequality is more ambiguous, given that minimum wage workers are found across the household income distribution (Chapter 2), and that minimum wage increases may reduce employment (Chapter 7). The more minimum wage workers are in higher-income households, and the greater the disemployment effect of a minimum wage rise, the less effective the minimum wage will be in reducing household income inequality.
270. Findings from US studies, in particular, should be approached with caution. Not only is the Australian national minimum wage higher, and our welfare system different, but the national minimum wage is a part of Australia's comprehensive system of modern awards and the 2,000 plus minimum award classification wages within it. The award wage system operates in relation to workers higher in the income distribution (noting also, that only a small proportion of award-reliant employees receive the national minimum wage; the remainder are paid the often much higher award classification wages).
271. For Australia, Leigh (2007) concluded, based on simulations, that:
- "... it appears unlikely that raising the minimum wage will significantly lower family income inequality".*
272. The Productivity Commission (2015a) extended Leigh's approach to include the effects of the tax-transfer system. They found that, assuming no reduction in employment, the dollar benefits of a minimum wage increase are largest for middle-income households, although in percentage terms, or if only working households are considered, low-income households benefit more. If the employment impacts are large enough, the Productivity Commission finds that they negate the benefits of higher wages across all income levels. (These studies both rely on assumptions about the employment effects of minimum wages, rather than estimating them.⁴⁰ They also only consider changes in the national minimum wage, and not award classification wages.)
273. Government modelling finds that, even assuming no change in hours worked, minimum wage increases are not fully reflected in disposable income. This is a result of having a highly progressive and targeted tax-transfer system. Table 8.3 shows the change in disposable income for various household types following the 2015 minimum wage increase. Full-time workers without children retained the greatest fraction of the minimum wage increase after taxes and transfers, since they receive no transfer

⁴⁰ They both assume that a 1 per cent increase in the minimum wage will reduce employment by between 0 and 1 per cent.

payments and therefore face no means tests. Part-time workers and workers with children kept less, since they are affected by the means tests on payments such as Newstart and Family Tax Benefit. Childless couples with one full-time worker and an unemployed partner are the worst off of the modelled households, retaining only 16 per cent of the minimum wage increase.

Table 8.3: Effect of 2015 minimum wage increase on household disposable incomes

Household type	Wage increase (\$pw)	Increase in household disposable income (\$pw)	Percentage of wage increase retained (%)
Single, no children			
Full-time NMW	16.00	12.64	79.0
Part-time NMW	6.30	2.52	40.0
Student on part-time NMW	6.30	2.82	44.8
Single parent			
Full-time NMW, child aged 3	16.00	5.13	32.1
Full-time NMW, child aged 9	16.00	7.77	48.6
Part-time NMW, child aged 3	6.30	3.78	60.0
Part-time NMW, child aged 9	6.30	3.78	60.0
Single income couples (partner on Newstart Allowance)			
Full-time NMW, no children	16.00	2.53	15.8
Full-time NMW, child aged 3	16.00	4.44	27.8
Full-time NMW, children aged 3 and 9	16.00	4.46	27.9
Dual income couples			
Both full-time NMW, no children	32.00	25.28	79.0
One full-time and one part-time NMW, no children	22.30	5.56	24.9
One full-time and one part-time NMW, child aged 3	22.30	6.07	27.2
One full-time and one part-time NMW, children aged 3 and 9	22.30	6.08	27.3

Source: Government modelling.

Note: Figures are based on tax and benefit rates applicable on 1 July 2015. Part-time hours are assumed to be 15 hours per week.

8.3 Gender inequality

274. In November 2015, the national gender pay gap was 17.3 per cent (Workplace Gender Equality Agency 2016). This is the difference between women's and men's average weekly full-time earnings, expressed as a percentage of men's earnings.⁴¹

⁴¹ This figure is based on ABS average weekly ordinary time earnings. Men work longer hours than women on average. The gender pay gap in hourly terms was 13.6 per cent in May 2014 (ABS 2015e). This figure covers non-managerial employees, both full-time and part-time.

275. The gender pay gap is mostly driven by higher-paid workers. Recent research for the Fair Work Commission shows little evidence of an hourly gender pay gap for workers on awards. Rozenbes and Farmakis-Gamboni (2015) find no statistically significant gender pay gap for award-reliant employees, but a gap of 14.7 per cent for employees on other industrial arrangements. Broadway and Wilkins (2015) find that award-reliant men and women are equally likely to be low-paid, although under other methods of setting pay, women are more likely to be low-paid.
276. In general, the Panel's decision is a blunt tool for addressing the complex factors underlying gender pay inequality. While the gender pay gap is smallest among lower paid and award-reliant workers, these are precisely the workers most likely to be affected by the Panel's decision. They are also the workers most at risk if there is any reduction in hours worked or employment as a result (see Chapter 7).
277. The Government has committed to the G20 goal to reduce the gap between male and female labour force participation rates (for people aged 15-64 years) by 25 per cent by 2025.
278. For Australia, this could be achieved through lifting the female participation rate by three percentage points. Boosting women's workforce participation requires a range of strategies including accessible, affordable and flexible child care, supporting women out of the workplace to become job-ready, and supporting small business to generate more jobs. This is an additional reason to be cautious about any measures which may jeopardise female employment (Chapter 5).
279. Analysis by the Grattan Institute has shown that raising women's participation could increase the size of the Australian economy by around \$25 billion a year (Daley et al 2013).

8.4 Taxes and transfers

280. The tax-transfer system plays a large role in equalising the distribution of income among Australian households. The distribution of private income is quite unequal, with the top fifth of households receiving 14.5 times as much as the bottom fifth. After direct (mainly income) taxes and transfer payments, however, this ratio drops to 5.6. When in-kind transfers (mainly Education and Health services) are added, it drops again to only 3.5.⁴²
281. Minimum wage workers, including some full-time workers, benefit from the system. Transfer payments are roughly a third of disposable income for full-time minimum wage workers in single-income households with children (see Table 8.4).

⁴² Government calculations from ABS (2015b). Income is per household (not adjusted for household size).

Table 8.4: Transfer payments to full-time NMW households with children, 1 January 2016

Household type	(\$pw)	(% of disposable income)
Single		
Child aged 3	345.84	37.0
Child aged 9	230.04	27.7
Children aged 3 & 9	464.59	44.2
Single income couple (partner on Newstart)		
Child aged 3	314.92	34.2
Child aged 9	299.74	33.1
Children aged 3 & 9	428.75	41.4
Dual income couples (both on NMW)		
Child aged 3	43.47	3.5
Child aged 9	51.74	4.2
Children aged 3 & 9	153.07	11.4

Source: Government modelling.

282. The system helps compensate for the costs of raising children. Table 8.5 shows that while equivalised (adjusted for household size) earnings are much lower in households with children, equivalised disposable income is actually higher in some minimum wage households with children than in households with equal earnings but without children. This is true even when childcare costs are taken into account.

Table 8.5: Equivalised income for full-time NMW workers with children, 1 January 2016

Household type	<u>Earned income</u>			<u>Disposable income, adjusted for childcare costs</u>		
	Earnings (\$pw)	Equivalised earnings (\$pw)	(% of single, no children)	Income (\$pw)	Equivalised income (\$pw)	(% of single, no children)
Single person – working full-time at the NMW						
No children	656.90	656.90	100.0	594.01	594.01	100.0
Child aged 3	656.90	505.31	76.9	818.38	629.52	106.0
Child aged 9	656.90	505.31	76.9	804.35	618.73	104.2
Children aged 3 & 9	656.90	410.56	62.5	915.62	572.26	96.3
Dual income couples – both partners working full-time at the NMW						
Child aged 3	1313.80	729.89	111.1	1091.84	606.58	102.1
Child aged 9	1313.80	729.89	111.1	1208.64	671.47	113.0
Children aged 3 & 9	1313.80	625.62	95.2	1183.61	563.62	94.9
Single income couples – P1 working full-time at the NMW, P2 on Parenting Payment/Newstart						
Child aged 3	656.90	364.94	55.6	920.76	511.53	86.1
Child aged 9	656.90	364.94	55.6	905.58	503.10	84.7
Children aged 3 & 9	656.90	312.81	47.6	1035.89	493.28	83.0

Source: Government modelling.

Note: It is assumed that the single income couples incur no childcare costs, since the non-working partner will look after the children.

283. The tax-transfer system has also assisted real income growth in minimum wage households. The Government has modelled the percentage change in real disposable income for a number of hypothetical households over the five years from 2011 to 2016.

As shown in Table 8.6, even if the national minimum wage had remained constant in real terms, most minimum wage households' disposable incomes would have improved in real terms due to changes in the tax-transfer system. Further, the real increase in the national minimum wage only increased household incomes by a marginal amount, as measured by the difference between the first two columns (shown in the third column).

Table 8.6: Changes in real disposable household income, 2011 to 2016

Household type	Total change (%)	Tax-transfer contribution (%)	Net impact of real NMW increases (%)
Single, no children			
Full-time NMW	1.7	-0.9	2.6
Part-time NMW	5.9	5.1	0.7
Student on part-time NMW	18.2	17.0	1.2
Single parent			
Full-time NMW, child aged 3	2.9	2.3	0.7
Part-time NMW, child aged 3	5.3	4.6	0.6
Full-time NMW, child aged 9	9.2	8.0	1.2
Part-time NMW, child aged 9	11.4	10.6	0.8
Single income couples			
Full-time NMW, no children	-0.4	-0.8	0.4
Full-time NMW, child aged 3	2.1	1.5	0.6
Full-time, children aged 3 and 9	2.9	2.3	0.6
Dual income couples			
Both full-time NMW, no children	1.7	-0.9	2.6
One full-time and one part-time NMW, no children	3.0	2.2	0.8
One full-time and one part-time NMW, child aged 3	2.5	1.8	0.8
One full-time and one part-time NMW, children aged 3 and 9	3.2	2.5	0.7

Source: Government modelling.

Notes: Based on NMW and tax-transfer system of 1 January each year. The first column shows the percentage change in real disposable income given the actual changes in the national minimum wage and tax-transfer system. The second column shows the contribution of the tax-transfer system, by assuming that the minimum wage had grown in line with the CPI, while the third shows the contribution of real NMW increases (the difference between the first two). They may not sum exactly due to rounding.

8.5 Conclusion

284. Household income inequality in Australia has only risen modestly, and remains well below US levels. Furthermore, the tax-transfer system is the primary means of redistributing income in Australia. It can provide better targeted and more effective assistance to maintain living standards, including the living standards of the employed, than increases in the national minimum wage and award classification wages.

285. The Panel's decision on the minimum wage and award classification wages is not particularly well suited to addressing the complex factors underlying gender inequality in the labour market, since the gender pay gap is much larger among high-paid workers, and increasing the minimum wage raises wages for both men and women.

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Appendices

Appendix A: Low-paid and national minimum wage workers – definitions and data

286. In defining low-paid employees, data was used from the ABS's survey of *Employee Earnings and Hours* (EEH) as well as the *Household Income and Labour Dynamics in Australia* (HILDA) Survey.
287. Different variables are available in these data sets. Also slightly different low-paid thresholds are used due to differences in the median wage and timing of the surveys. However, the low-paid definition is consistently two thirds of median earnings.

A.1 Defining low-paid employees using HILDA

288. Low-paid adult employees have been defined as employees aged 21 or older earning less than two-thirds of the median employee hourly earnings. Accordingly, adult employees with hourly earnings below \$18.42 have been classified as low-paid. To identify low-paid junior employees, the low-pay threshold derived from adult employees has been adjusted as detailed below.^{43,44}
289. In order to calculate the number of low-paid employees using the HILDA Survey the following approach has been taken:
- limited the population to employees aged 15 years and over with positive hours of work and earnings
 - calculated hourly earnings for employees in their main job
 - deflated the earnings of casuals by 1.25 to reflect the casual loading
 - calculated the median earnings of adult employees (i.e. aged 21 years and over) at (\$27.63) and set the threshold for low-pay at two thirds of this amount (\$18.42)
 - adult employees with an hourly wage below \$18.42 have been classified as low-paid
 - low-pay thresholds for employees aged under 21 have been adjusted by the relevant junior minimum wage rate (from the National Minimum Wage Order) which is a percentage of the adult national minimum wage.⁴⁵ Table A.1 contains all low-pay thresholds used for juniors.

⁴³ The Government's analysis is not limited to adult low-paid employees, but also includes low-paid workers aged under 21 years. This is because younger employees are one of the main groups affected by Annual Wage Review decisions.

⁴⁴ The Government has adjusted the low-paid threshold for juniors because junior minimum wages are lower than adult minimum wages. This type of approach is not unique and has been taken in various academic reviews.

⁴⁵ Junior minimum wage rates (as a proportion of adult minimum wage rates) vary considerably across awards. The junior-adult minimum wage relativities in the National Minimum Wage Order are based on the Miscellaneous Award 2010.

Table A.1: Low-pay thresholds, by age

	Percentage of NMW (%)	Low-paid threshold (\$)
Adult (21 years and over)	100.0	18.42
20 year old	97.7	18.00
19 year old	82.5	15.20
18 year old	68.3	12.58
17 year old	57.8	10.65
16 year old	47.3	8.71
15 year old	36.8	6.78

Note: Junior minimum wage rates refer to the National Minimum Wage Order.

Example: The low-paid threshold for 15 year olds was set at \$6.78 which is the adult threshold of \$18.42 multiplied by 36.8 per cent (the special national minimum wage for 15 year olds is 36.8 per cent of the national minimum wage). Fifteen year olds paid less than \$6.78 per hour have been classified as low-paid.

A.2 Defining low-paid employees using EEH

290. Low-paid employees have been defined as employees earning less than two-thirds of the median employee hourly earnings. Accordingly, employees with hourly earnings below \$18.67 have been classified as low-paid.

291. In order to calculate the number of low-paid employees using the EEH Survey the following approach has been taken:

- limited the population to employees aged 15 years and over with positive hours of work and earnings
- limited the population to non-managerial employees as managers have not normally reported on hours worked
- calculated hourly ordinary time cash earnings for all non-managerial employees
- deflated the earnings of casuals by 1.25 to reflect the casual loading
- calculated the median hourly wage (\$28.00 per hour) and two thirds of this amount (\$18.67 per hour)
- employees with an hourly wage below \$18.67 are classified as low-paid
- no adjustment has been made to the low-pay thresholds for juniors because the EEH Survey has not traditionally reported on the age of respondents.

A.3 Defining national minimum wage employees using EEH

292. National minimum employees have been defined as adult employees who are paid less than \$16.50 per hour. This excludes workers paid junior, apprentice and disability rates of pay.

293. In order to calculate the number of national minimum wage adult employees using the EEH Survey the following approach has been taken:

- limiting the population to non-managerial employees as managers have not normally reported on hours worked
- calculating hourly ordinary time cash earnings for all non-managerial employees
- deflating the earnings of casuals by 1.25 to reflect the casual loading

- the national minimum wage at May 2014 was \$16.37. Employees paid at or below \$16.50 per hour in May 2014 are considered to be paid the national minimum wage rate (this uses an upper error band of 13 cents).

A.4 Characteristics of low-paid workers

Table A.2: Detailed characteristics of low-paid workers

	% of low-paid employees	% of higher-paid employees	% of all employees	% of employees who are low-paid
Gender				
Male	43.7	51.9	50.4	15.7
Female	56.3	48.2	49.6	20.5
Age				
Age 15-24	43.2	11.8	17.5	44.7
Age 25-34	18.5	25.4	24.1	13.9
Age 35-44	15.1	24.2	22.5	12.1
Age 45-54	11.6	22.1	20.2	10.4
Age 55-64	8.7	14.3	13.3	11.8
Age 65+	2.9	2.3	2.4	21.4
Marital status				
Single	63.5	35.8	40.8	28.1
Partnered	36.5	64.2	59.2	11.2
Age of youngest resident child				
No child	72.1	52.3	55.8	23.3
0-5 years	9.3	16.6	15.3	11.0
6-11 years	6.7	10.1	9.5	12.9
12-17 years	5.2	9.7	8.9	10.5
18 years or more	6.7	11.3	10.5	11.6
Location				
Major city	68.0	71.6	71.0	17.3
Inner regional Australia	23.0	19.1	19.8	20.9
Outer regional Australia	8.4	7.9	8.0	19.0
Remote/very remote Australia	0.7	1.4	1.2	9.8
Long term health condition				
Present	18.3	13.6	14.4	22.8
Not present	81.7	86.3	85.5	17.3
Highest education attainment				
Degree or post Graduate	14.2	37.0	32.9	7.8
Certificate 3-4/Diploma	28.7	33.6	32.7	15.9
Year 12	28.8	15.1	17.6	29.6
Year 11 or below ^(c)	28.3	14.3	16.8	30.5
Years of work experience				
Less than 2 years	23.2	5.4	8.6	48.4
2-5 years	21.4	8.5	10.8	35.7
More than 5 years	55.4	86.1	80.6	12.4
Hours				
Full-time	42.9	71.8	66.6	11.6
Part-time	57.1	28.2	33.4	30.8
Contract type				
Casual	61.7	17.0	25.1	44.5
Permanent	38.3	0.83.0	74.9	9.2

	% of low-paid employees	% of higher-paid employees	% of all employees	% of employees who are low-paid
Business size				
Small (1-19 employees)	54.4	30.5	34.8	28.1
Medium (20-199 employees)	39.0	42.2	41.6	16.8
Large (200 plus employees)	6.7	27.4	23.6	5.1
Occupation				
Managers	3.9	13.1	11.4	6.1
Professionals	6.4	28.7	24.7	4.7
Technicians & trades workers	11.6	11.9	11.9	17.6
Community & personal service	20.4	10.5	12.3	29.9
Clerical & administrative workers	12.3	15.6	15.0	14.9
Sales workers	19.3	7.1	9.3	37.7
Machinery operators & drivers	6.9	6.4	6.5	19.4
Labourers	19.3	6.7	9.0	38.9
Industry				
Agriculture, forestry & fishing	3.3	1.0	1.4	41.5
Mining	0.4	2.5	2.1	3.4
Manufacturing	6.8	8.8	8.5	14.6
Electricity, gas, water & waste services	0.2	1.4	1.1	3.5
Construction	6.1	6.1	6.1	18.1
Wholesale trade	2.5	3.8	3.5	12.8
Retail trade	18.7	8.9	10.7	31.8
Accommodation & food services	18.6	4.0	6.7	50.5
Transport, postal & warehousing	4.7	5.1	5.0	16.9
Information media & telecommunications	0.8	1.8	1.6	9.0
Financial & insurance services	0.8	4.8	4.1	3.5
Rental, hiring & real estate services	2.0	1.3	1.4	25.4
Professional, scientific & technical services	4.5	7.2	6.7	12.0
Administrative & support services	3.9	2.3	2.6	27.0
Public administration & safety	1.4	7.8	6.6	3.8
Education & training	5.5	12.0	10.8	9.2
Health care & social assistance	11.8	16.7	15.8	13.5
Arts & recreation services	2.9	1.6	1.8	28.8
Other services	5.3	3.0	3.4	27.8

Source: *HILDA Survey*, release 14 (December 2015), wave 14.

How to read: The first column of data shows the percentage of low-paid people with each characteristic. For example, using the gender data, the table shows that 43.7 per cent of low-paid workers are male. The last column shows the percentage of workers of a particular characteristic that are low-paid. For example, 15.7 per cent of male workers are low-paid.

Note: (a) Income support payments include Government Pensions, Parenting Payments and Allowances (b) Total public transfers include income support payments, non-income support payments (including Family Tax Benefit A and Family Tax Benefit B) and payments not elsewhere classified. (c) Includes certificate 1-2.

Appendix B: Modelling assumptions

B.1 Tax-transfer assumptions

- (i) All tax rates and transfers are as at 1 January 2016.
- (ii) Families are assumed to have no private health insurance.
- (iii) Modelling includes Telephone Allowance where relevant.
- (iv) Modelling assumes the maximum rate of Rent Assistance where it is stated that the household is renting.
- (v) Families are assumed to not live in public housing or face shared care arrangements.
- (vi) People are assumed to be born after 1952 and hence partnered couples are assumed to not receive the Dependent Spouse Tax Offset.
- (vii) Any lump sum payments are spread evenly over the period.

B.2 Childcare assumptions

- (i) Hours of usage assumptions are listed in Table B.1. These are based on the hours of work of the second earner in a couple household.⁴⁶ Where only one member of a couple household works, it is assumed that the household does not require child care.
- (ii) Families are in receipt of the Child Care Benefit and Child Care Rebate only.⁴⁷
- (iii) Long day care costs \$8.81 per hour and after school care costs \$6.89 per hour. This is based on average child care fees for the September quarter 2014, indexed to the Consumer Price Index for childcare up to the September quarter 2015.⁴⁸

Table B.1: Child care usage assumptions

Child age	Care type	Hours required per week	
		Full-time	Part-time
0-4 years	Long Day Care	50	20
5-12 years	Outside School Hours Care (a)	15	6

Note: (a) Usage for school aged children is based on care requirements during the school term. It is expected that care requirements will differ over the school holiday period. Children aged 5-12 years are presumed to only attend the after school session of Outside School Hours Care.

⁴⁶ Basing child care usage on hours of work is a method also used elsewhere in the literature (e.g. Immervoll and Barber 2006).

⁴⁷ Some families may also receive Jobs Education Training and Child Care Fee Assistance when they transition from unemployment to minimum wage work. However, this is only available for a constrained time period and has been excluded from our analysis as it does not provide an indication of the 'typical' assistance available to minimum wage earners.

⁴⁸ This was the latest available data when the modelling was done. Increases in the December quarter are generally small. Child care fees vary between providers and this will affect individual experiences.

Appendix C: Modelling results

Table C.1: One unemployed member of the household accepts a job paying the NMW (\$17.29 p/hour)

Household Type	Income / payments before finding a job	Transfer payments after finding job	Tax & Medicare (deduction)	Disposable income after finding job	Improvement in financial position	Transfer payments as a proportion of disposable income
	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	(% increase) (\$ pw)	(%)
<i>Single without children –FT job at \$656.90 p/week</i>						
Adult - NSA	\$270.35	\$0.00	\$62.89	\$594.01	119.7% \$323.66	0.0%
Adult renter - NSA	\$335.05	\$0.00	\$62.89	\$594.01	77.3% \$258.96	0.0%
<i>Single without children –PT job at \$253.05 p/week</i>						
Adult - NSA	\$270.35	\$152.84	\$0.17	\$412.02	52.4% \$141.67	37.1%
Adult renter – NSA	\$335.05	\$217.54	\$0.17	\$476.72	42.3% \$141.67	45.6%
Student – YA – away from home	\$224.35	\$202.93	\$5.27	\$457.01	103.7% \$232.66	44.4%
Student – YA – lives with parents	\$149.15	\$127.72	\$0.00	\$387.08	159.5% \$237.93	33.0%

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NSA – Newstart Allowance
 YA – Youth Allowance
 PPP – Parenting Payment Partnered
 PPS – Parenting Payment Single

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Household Type	Income / payments before finding a job	Transfer payments after finding job	Tax & Medicare (deduction)	Disposable income after finding job	Improvement in financial position	Transfer payments as a proportion of disposable income
	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	(% increase) (\$ pw)	(%)
<i>Couple – both unemployed, one finds a FT job at \$656.90 p/week</i>						
No children - NSA	\$487.58	\$128.05	\$57.28	\$727.67	49.2% \$240.09	17.6%
With 1 child aged 3 years - PPP	\$651.36	\$314.92	\$51.05	\$920.76	41.4% \$269.40	34.2%
With 1 child aged 9 years – NSA	\$636.18	\$299.74	\$51.05	\$905.58	42.3% \$269.40	33.1%
With 2 children aged 3 and 9 years – PPP	\$765.19	\$428.75	\$49.75	\$1035.89	35.4% \$270.70	41.4%
<i>Couple – both unemployed, one finds a PT job at \$259.35 p/week</i>						
No children - NSA	\$487.58	\$370.07	\$0.00	\$629.42	29.1% \$141.84	58.8%
With 1 child aged 3 years - PPP	\$651.36	\$533.85	\$0.00	\$793.20	21.8% \$141.84	67.3%
With 1 child aged 9 years – NSA	\$636.18	\$518.67	\$0.00	\$778.02	22.3% \$141.84	66.7%
With 2 children aged 3 and 9 years – PPP	\$765.19	\$647.68	\$0.00	\$907.03	18.5% \$141.84	71.4%

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Household Type	Income / payments before finding a job	Transfer payments after finding job	Tax & Medicare (deduction)	No Child Care			With Child Care		
				Disposable income after finding job	Improvement in financial position	Transfer payments as a proportion of disposable income	Net child care costs	Disposable income after finding job	Improvement in financial position
	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	(% increase) (\$ pw)	(%)	Amount (\$ pw)	Amount (\$ pw)	(% increase) (\$ pw)
<i>Lone parent –FT job at \$656.90 p/week</i>									
With 1 child aged 3 years –PPS	\$571.28	\$345.84	\$68.37	\$934.38	63.6% \$363.10	37.0%	\$116.00	\$818.38	43.3% \$247.10
With 1 child aged 9 years – NSA	\$472.40	\$230.04	\$57.50	\$829.44	75.6% \$357.04	27.7%	\$25.09	\$804.35	70.3% \$331.95
With 2 children aged 3 and 9 years – PPS	\$685.11	\$464.59	\$70.65	\$1050.84	53.4% \$365.73	44.2%	\$135.23	\$915.62	33.6% \$230.51
<i>Lone parent –PT job at \$259.35 p/week</i>									
With 1 child aged 3 years – PPS	\$571.28	\$504.86	\$0.00	\$764.21	33.8% \$192.93	66.1%	\$42.23	\$721.98	26.4% \$150.70
With 1 child aged 9 years – NSA	\$472.40	\$389.06	\$0.00	\$648.41	37.3% \$176.01	60.0%	\$10.03	\$638.38	35.1% \$165.98
With 2 children aged 3 and 9 years – PPS	\$685.11	\$623.61	\$0.00	\$882.96	28.9% \$197.85	70.6%	\$49.73	\$833.23	21.6% \$148.12

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Household Type	Income / payments before finding a job	Transfer payments after finding job	Tax & Medicare (deduction)	No Child Care			With Child Care		
				Disposable income after finding job	Improvement in financial position	Transfer payments as a proportion of disposable income	Net child care costs	Disposable income after finding job	Improvement in financial position
	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	Amount (\$ pw)	(% increase) (\$ pw)	(%)	Amount (\$ pw)	Amount (\$ pw)	(% increase) (\$ pw)
<i>Couple – one employed FT on the NMW, the other finds a FT job at \$650.90 p/week</i>									
No children - NSA	\$727.67	\$0.00	\$125.78	\$1188.02	63.3% \$460.35	0.0%	Not applicable		
With 1 child aged 3 years - PPP	\$920.76	\$43.47	\$125.78	\$1231.49	33.7% \$310.73	3.5%	\$139.64	\$1091.84	18.6% \$171.10
With 1 child aged 9 years – NSA	\$905.58	\$51.74	\$125.78	\$1239.76	36.9% \$334.18	4.2%	\$31.12	\$1208.64	33.5% \$303.10
With 2 children aged 3 and 9 years – PPP	\$1035.89	\$153.07	\$125.78	\$1341.09	29.5% \$305.20	11.4%	\$157.47	\$1183.61	14.3% 147.72
<i>Couple – one employed FT on the NMW, the other finds a PT job at \$259.35 p/week</i>									
No children - NSA	\$727.67	\$10.54	\$62.89	\$863.90	18.7% \$136.23	1.2%	Not applicable		
With 1 child aged 3 years - PPP	\$920.76	\$169.12	\$62.40	\$1022.97	11.1% \$102.21	16.5%	\$42.23	\$980.74	6.5% \$60.0
With 1 child aged 9 years – NSA	\$905.58	\$153.94	\$62.40	1007.79	11.3% \$102.21	15.3%	\$10.03	\$997.75	10.2% \$92.20
With 2 children aged 3 and 9 years – PPP	\$1035.89	\$282.95	\$56.17	\$1143.02	10.3% 107.13	24.8%	\$49.73	\$1093.29	5.5% 57.40