FAIR WORK COMMISSION

ANNUAL WAGE REVIEW 2014

NSW GOVERNMENT SUBMISSION

Contents

Introduction

In its submission to the 2013 Review, the NSW Government urged the Minimum Wage Expert Panel 'to take a cautious approach'[1] when making its decision to adjust minimum wage rates.

Since that time, economic performance has remained soft with price pressures subdued as CPI inflation remains within the Reserve Bank of Australia's 2 to 3 per cent target band. The economy is in a difficult transition where the decline in mining investment has been earlier and greater than expected and the anticipated offsetting pick-up in non-mining business investment has been delayed. These factors have contributed to a particularly soft labour market, with continuing below-trend growth and the most recent unemployment rate at 6 per cent, the highest for over ten years.[2]

In this environment, it is important to support further job creation, suggesting that now is not the time to diminish incentives for the employment of entry-level employees.

Consequently, the NSW Government reiterates the position it took in the 2013 Review and submits that the case for taking a more cautious approach on this occasion is, if anything, more compelling.

The structure of this Submission is as follows.

Part 1 surveys the relevant statutory framework and examines the dimensions of low paid employment, noting recent research undertaken by the Fair Work Commission.

Part 2 provides submissions regarding the relevant statutory objectives, including the performance and competitiveness of the NSW economy.

Part 3 addresses questions regarding productivity and the relative value of the minimum wage foreshadowed by the Expert Panel in its 2013 Decision.

Part 4 concludes this Submission.

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[1] NSW Government Submission Annual Wage Review 2013, p1
[2] ABS 6202.0, Labour Force, Australia, Jan 2014

Part 1 – Statutory framework and award-reliant employment

Statutory Framework

1. In this annual wage review, the Expert Panel is required to review the national minimum wage order and modern award minimum wages.[3] The Panel must then make a national minimum wage order, and may make one or more determinations varying modern awards to set, vary or revoke modern award minimum wages.[4]

2. In addition, the Panel must set special national minimum wages for all award/agreement free employees who are junior employees, employees to whom training arrangements apply, and employees with a disability, as well as setting the casual loading for award/agreement free employees.[5]

3. The NSW Government submits that, in arriving at its decision, the Panel must balance economic, social and industrial considerations, as relevantly provided for in the *Fair Work Act 2009* (Cth).

4. The relevant provisions are the Minimum Wages Objective and the Modern Awards Objective, which are as follows:

> **Minimum Wages Objective**
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>
> What is the minimum wages objective?
>
> (1) The FWC must establish and maintain a safety net of fair minimum wages, taking into account:
>
> (a) the performance and competitiveness of the national economy, including productivity, business competitiveness and viability, inflation and employment growth; and
>
> (b) promoting social inclusion through increased workforce participation; and
>
> (c) relative living standards and the needs of the low paid; and
>
> (d) the principle of equal remuneration for work of equal or comparable value; and
>
> (e) providing a comprehensive range of fair minimum wages to junior employees, employees to whom training arrangements apply and employees with a disability.

[3] Fair Work Act 2009 s285(1)
[4] Fair Work Act 2009 s285(2)
[5] Fair Work Act 2009 s294

Modern Awards Objective

134 The modern awards objective

What is the modern awards objective?

(1) The FWC must ensure that modern awards, together with the National Employment Standards, provide a fair and relevant minimum safety net of terms and conditions, taking into account:

(a) relative living standards and the needs of the low paid; and

(b) the need to encourage collective bargaining; and

(c) the need to promote social inclusion through increased workforce participation; and

(d) the need to promote flexible modern work practices and the efficient and productive performance of work; and

(e) the principle of equal remuneration for work of equal or comparable value; and

(f) the likely impact of any exercise of modern award powers on business, including on productivity, employment costs and the regulatory burden; and

(g) the need to ensure a simple, easy to understand, stable and sustainable modern award system for Australia that avoids unnecessary overlap of modern awards; and

(h) the likely impact of any exercise of modern award powers on employment growth, inflation and the sustainability, performance and competitiveness of the national economy.

5. In addition, consideration is to be given to the Objects of the Act, as relevant.[6]

6. In practical terms, this means that the following key objectives need to be balanced by the Panel:

- Ensuring a wage outcome is not detrimental to strong and sustainable economic performance;
- Ensuring and maintaining a fair and relevant safety net of minimum wages which meets the needs of award-reliant employees and employers; and
- Maintaining incentives to bargain.

Dimensions of award-reliant employment

7. Recent research[7] commissioned by the Panel[8] has provided fresh insight into the nature and extent of award-reliant employees and employers on a national level.

[6] Fair Work Act 2009 ss3(a), (b), (f), (g)
[7] Fair Work Commission Research Report 6/2013 Award Reliance
[8] See Annual Wage Review 2009-10 Decision [2010] FWAFB 4000 (3 June 2010),para [428]

8. The key findings of that Report are:

> The project determined that 25 per cent of organisations were award-reliant. Award reliance was found to be high among larger organisations. A higher proportion of large organisations and medium organisations were award-reliant (both 44 per cent) than small organisations (32 per cent) and micro organisations (18 per cent). The industries that had a relatively high proportion of award-reliant organisations were accommodation and food services (64 per cent) and retail trade (44 per cent). Organisations in regional/rural locations were more likely to be award-reliant than organisations in metropolitan locations.
>
> While it was estimated that 25 per cent of organisations were award-reliant, more than half of all organisations (52 per cent) reported using awards in some way to set pay or guide pay decisions for at least one of the employees in their organisation, i.e. award-based. More than one-quarter (27 per cent) of all organisations used 'over-award' pay-setting arrangements, i.e. where the organisation was not paying any of their employees at exactly the applicable rate specified in an award, but an award was used, in some way, by the organisation to guide the pay-setting decision for at least one of their employees.
>
> The chapter also discusses the degree of award reliance within organisations. This is determined by the proportion of award-reliant employees in the organisation. It was found that in 50 per cent of award-reliant organisations, more than three-quarters of employees were award-reliant. The proportion of organisations with more than three-quarters of employees award-reliant was highest in transport, postal and warehousing; public administration and safety; and accommodation and food services. Over half of micro organisations (59 per cent) and organisations in regional/rural locations (57 per cent) also had more than three-quarters of employees award-reliant.[9]

9. The Report sets out the distribution of pay-setting arrangements in the States and Territories as follows:

	Percentage of workforce by pay setting arrangement			
	Award Reliant	Enterprise Agreement	Other	Total
New South Wales	**21**	**18**	**61**	**100**
Victoria	18	23	59	100
Queensland	19	24	57	100
Western Australia	11	26	63	100
South Australia	22	25	53	100
Tasmania	28	26	46	100
Northern Territory	7	27	67	100
Australian Capital Territory	18	19	64	100
All states and territories	**19**	**22**	**59**	**100**

Table adapted from Table 4.9 at p60 of Research Report 6/2013, Award reliance, Sally Wright and John Buchanan, Workplace Research Centre, University of Sydney Business School, December 2013

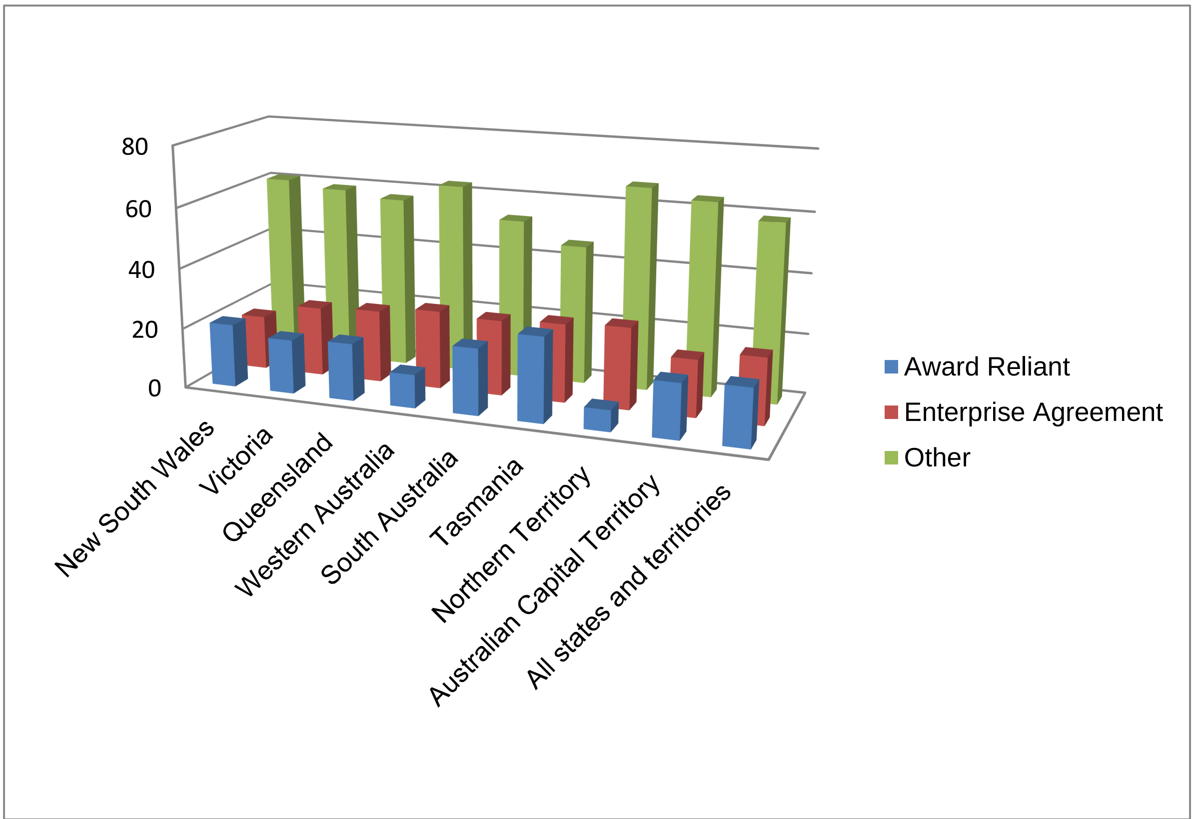
10. The previous table and the following graph indicate that:

- When compared to the national figure, a slightly higher percentage of the NSW workforce is paid at exactly the award rate.

[9] FWC Research Report 6/2013 p32

- NSW employees' participation in collective bargaining through the formal enterprise agreement framework is the lowest of all the States and Territories.
- NSW has a slightly above-average percentage of its workforce on over-award and individual arrangements. This group also includes those employees who have their pay established with reference to an award.

Percentage of workforce by pay setting arrangement – States and Territories



11. The NSW figures for the proportion of award-reliant employees appear to be broadly consistent with that in the established source for such data, the ABS Employee Earnings and Hours survey (ABS EEH Cat No 6306.0, May 2012). Differences in the other data categories appear to relate to differences in the scope of each survey and the definitions of the other data categories.[10]

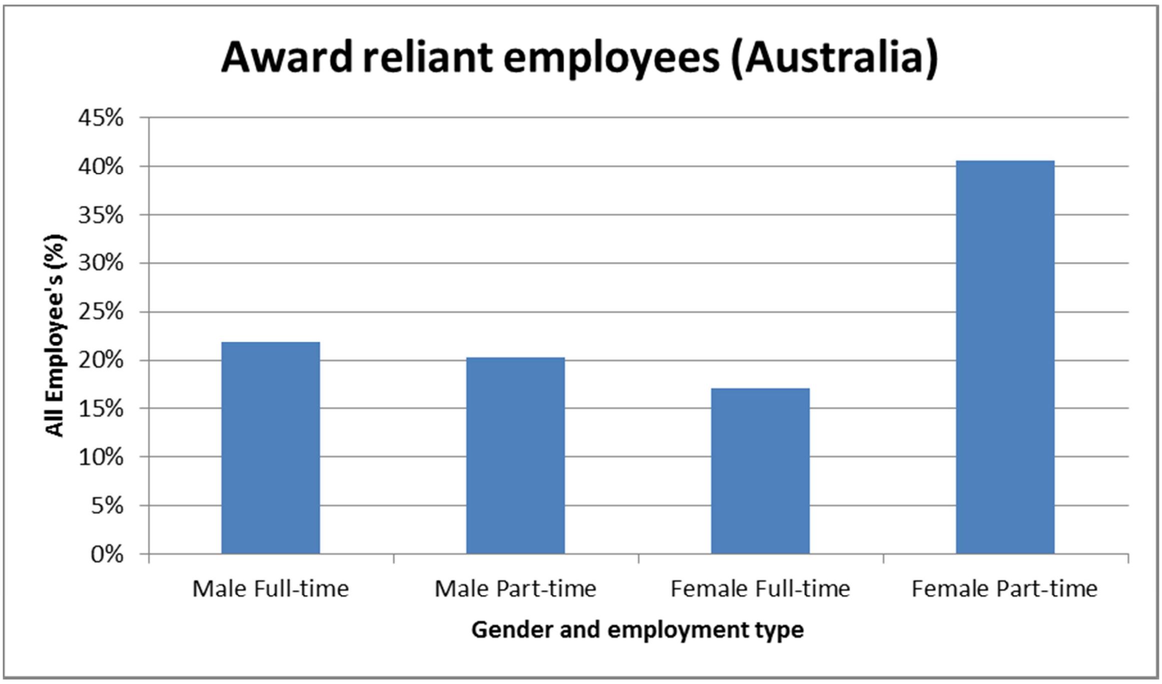
12. In particular, EEH indicates that NSW is the state with the highest numbers of award-reliant employees and the fourth highest on a proportionate basis.[11]

[10] See FWC Research Report 6/2013 Appendix G pp210- 212
[11] ABS Employee Earnings and Hours, May 2012, Cat No 6306.0

13. According to the most recent ABS data, approximately 3.16 million employees in NSW are within the national industrial relations system.[12] Of these, approximately 17 per cent, or 537,600, of all NSW employees are award-reliant and will therefore be directly affected by this wage review.

14. The graphic below sets out the breakdown of employees who are award-reliant by gender and employment status across Australia.

Award-Reliant Employees Australia



ABS, Employee Earnings and Hours, May 2012 Cat. No.6306.0

15. Female employees comprise a high proportion of the total number of award-reliant employees, representing close to 58 per cent. Of note is the number of part-time female employees, representing over 40 per cent of the number of award-reliant employees who will benefit from an increase to minimum wage rates contained within modern awards.[13]

16. Male employees represent over 42 per cent of the total, while part-time male employees make up just over 20 per cent of the total number of award-reliant employees.[14]

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[12] ABS, Labour Force Status, Jan 2014, Cat. No.6202.0
[13] ABS, Employee Earnings and Hours, May 2012, Cat.No.6306.0
[14] Ibid

Superannuation

17. The *Superannuation Guarantee (Administration) Amendment Act 2012* increases the superannuation guarantee rate from 9 per cent to 12 per cent by 0.25 percentage points from 1 July 2013 and 1 July 2014, followed by increases of 0.5 percentage points on 1 July each year until it reaches 12 per cent on 1 July 2019.

18. The NSW Government submits that, in line with its Wages Policy, any increase to the superannuation guarantee rate is an employee-related cost that is included within an employee's remuneration.

19. In last year's review, many parties urged the Commission to take into account the increase in the superannuation guarantee rate when determining the level of wage increases. While the Commission rejected proposals for a "direct, quantifiable, trade-off" the Commission did have regard to the superannuation guarantee rate increase when determining the level of adjustment.[15]

20. While the Australian Government has indicated an intention to defer increases to the superannuation guarantee rate, no change has yet been made to superannuation legislation to give force to that proposal. Consequently, the Commission should consider the scheduled 0.25 percentage point increase in the superannuation guarantee rate on 1 July 2014 when determining any adjustment to award wages and the minimum wage order.

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[15] Annual Wage Review 2012-13 [2013]FWCFB400, at para [359]

Part 2 – Submissions Addressing the Statutory Objectives

The Performance and competitiveness of the NSW economy (s284(1)(a))

21. In the 2013-14 State Budget (released in June 2013), the economic forecasts remained broadly unchanged (from the 2012-13 Half-Yearly Review) with real economic growth expected to return to a trend rate of 2¾ per cent for both 2013-14 and 2014-15. This reflected expected strong growth in public investment, dwelling investment and non-rural commodity exports, as well as solid household income and consumption growth.

22. Employment growth was revised up marginally to 1¼ per cent for 2013-14 and 2014-15, supported by domestic demand growth returning to trend, and solid interstate and international export demand.

23. Given that New South Wales has a diversified industry structure, the State was expected to face a less difficult transition away from mining investment (and related activity), which had dominated the national economy over the past few years. Low interest rates were expected to underpin the abovementioned growth in consumption, dwelling investment, and a gradual improvement in non-mining-related business investment. Also, a modest depreciation of the Australian dollar, an improving global economy, and ongoing demand from resource-intensive states, were expected to assist in this transition.

24. By the time of the 2013-14 Half-Yearly Review, (HYR, December 2013), the global economic outlook had weakened, affecting both national and NSW economic prospects.

25. Nevertheless, global growth is still expected to improve, with the International Monetary Fund (IMF) upgrading their outlook in January (compared to October) to 3.7 per cent in 2014 and 3.9 per cent in 2015. This improvement largely reflects a recovery in advanced economies.

26. The outlook for the national economy was also revised down in the 2013-14 HYR to below trend growth for 2013-14 and 2014-15. This reflected slower global growth weighing on export growth, mining investment falling more quickly than previously expected and a delay in the anticipated pick up in non-mining business investment. Ongoing declines in the terms of trade, and softer employment and wages growth are expected to slow business and household income growth.

27. Relative to the HYR, the outlook for the national economy has improved, reflecting, in part, a more positive external environment and better than expected Gross Domestic Product (GDP) growth in the December quarter. While mining investment has continued to fall faster than expected, indicators around the transition to other growth drivers (such as retail sales, building approvals and confidence) have generally firmed.

28. GDP rose by 0.8 per cent in the December quarter 2013 to be up 2.8 per cent through the year (driven mostly by improved household consumption and underlying public demand growth).

29. The Reserve Bank of Australia (RBA) in its February Statement on Monetary Policy left their 2013-14 GDP growth forecast unchanged at 2½ per cent and revised up 2014-15 growth from 2½ per cent to 2¾ per cent.

30. At the HYR, NSW Gross State Product (GSP) growth was forecast to strengthen, but remain slightly below trend at 2½ per cent in both 2013-14 and 2014-15, broadly in line with the national average. This is a quarter of a percentage point lower for both years compared to Budget, reflecting downward revisions to global and national growth, and the expectation of a more gradual transition to non-mining investment growth.

31. The 2013-14 HYR forecasts by NSW Treasury for major aggregates are[a]:

	2012-13	2013-14		2014-15		2015-16 and 2016-17	
	Outcome	Budget Forecast	Revised Forecast	Budget Forecast	Revised Forecast	Budget Projection	Revised Projection
Real State Final Demand	1.7	3	2¼	3	2¼		
Real Gross State Product	1.8	2¾	2½	2¾	2½	2¾	2¾
Employment	1.7	1¼	1	1¼	1¼	1¼	1¼
Unemployment Rate (b)	5.2	5½	6	5½	6¼		
Sydney CPI(c)	2.6	2	2½	2½	2	2½	2¾
- through the year to June quarter(c)	2.6	2½	2¾	2½	2		
Wage Price Index	3.1	3¼	2¾	3½	3	3½	3½
Nominal Gross State Product	2.9	5¼	3¼	5¼	4		

(a) Per cent change, year average, unless otherwise indicated

(b) Year average, per cent

(c) 2013-14 and 2014-15 forecasts include a ¼ percentage point impact from the increase in tobacco excise; 2014-15 forecasts include a ¾ percentage point impact from the abolition of the carbon tax

World Economy

32. The global economy has improved through the second half of 2013 with a pick-up in world trade. However, growth remains somewhat uneven between regions and risks remain to the downside. In January, the IMF revised up its global growth forecast for 2014 by 0.1 of a percentage point to 3.7 per cent and left its 2015 forecast unchanged at 3.9 per cent. Global growth drivers come largely from the moderate recovery underway in advanced economies.

33. Risks to financial stability continue as corporate leverage rises with corresponding increases in foreign currency exposures. The IMF's concern is that if interest rates increase more than expected then asset valuations could be pressured, including those in emerging market economies. Volatility in capital flows for emerging market economies is also a concern.

34. Notwithstanding downside risks, growth in the advanced economies is expected to improve in 2014 relative to 2013, albeit staying low. US economic growth has been improving consistently through 2013, estimated at 1.9 per cent by the IMF. Their forecast for US growth in 2014 is now 0.2 per cent higher at 2.8 per cent driven by domestic demand and the deferral of some fiscal tightening until 2015.

35. Despite growth turning positive recently, the Euro Area's outlook remains weak, with deflation concerns emerging and significant structural reforms still required. The IMF cites easier credit conditions in the United Kingdom which have increased confidence, with growth to be slightly higher than expected over the next two years. Ongoing effective structural reform is needed in Japan to sustain longer-term growth with the increase in consumption tax offsetting the temporary fiscal stimulus in the near term.

36. The IMF's recent growth forecasts for emerging economies are 5.1 per cent in 2014, rising to 5.4 per cent in 2015. China grew strongly through 2013 at 7.7 per cent and is expected to remain around its 7½ per cent official target for 2014 and 2015 as the economy transitions towards more consumption-led growth.

37. Major trading partner growth is expected to pick up to be slightly above average in 2014 and to remain stronger than overall global growth.

Australian Economy

38. In the 2013-14 HYR, the national economic outlook was revised down compared to Budget time, with below trend growth forecast for 2013-14 and 2014-15. This reflected slower global growth weighing on trade and confidence, mining investment falling more than previously expected and a delay in the anticipated pick-up in non-mining business investment. Ongoing declines in the terms of trade, and softer employment and wages growth are expected to slow business and household income growth.

39. The unexpectedly higher growth in GDP of 0.8 per cent in the December quarter, after a 0.6 per cent increase in the previous quarter, has been consumption led and masks the underlying weaknesses in other sectors of the economy, particularly business investment which fell 3.6 per cent.

40. A number of positive factors should provide some support during 2014.

    a) While still relatively high, the exchange rate has fallen considerably from recent highs, and is expected to depreciate further over the forecast period, in line with the declining terms of trade. However, risks remain that the Australian dollar may stay higher than what would normally be expected from a declining terms of trade, as has been the recent experience. If the exchange rate falls, it will provide some relief to exporters and import competing industries. Commodity exports will also increase as mining transitions from investment to production.

    b) The impact of historically low interest rates is still working through the economy. Dwelling investment has been revised upwards since Budget and is on a strengthening trajectory. Although household consumption growth was higher than expected in the December quarter, it is likely to grow at a below trend rate over the next few years due to modest household income growth. Expected slower wages growth may constrain any pick-up in consumption from rising asset prices which generally bolster household wealth and consumer confidence.

41. Public final demand (consumption and investment) should make modest contributions to growth in 2013-14. Public demand growth has been revised up for 2013-14 compared to Budget time mainly due to State-level capital spending. However, the 2014-15 forecast has been reduced due to fiscal consolidation, especially by the Commonwealth.

New South Wales Economy

42. Following growth of 1.8 per cent in 2012-13, NSW growth was forecast in the HYR to strengthen, but remain slightly below trend at 2½ per cent in both 2013-14 and 2014-15, broadly in line with the national average. This is a quarter of a percentage point lower for both years compared to Budget time, reflecting downward revisions to global and national growth, with a more gradual transition to non-mining investment growth now expected. The projections for 2015-16 and 2016-17 are based on a return to trend growth by that time.

43. The weaker economic outlook reflects an earlier than expected peak in mining investment, and softer consumption growth resulting from weaker employment and wages growth. As a consequence, demand and capacity utilisation is forecast to be lower than expected resulting in a delay to the anticipated pick-up in non-mining investment.

44. Weaker domestic economic activity should lead to some abatement in domestic price pressures. Compared to Budget, a larger decline in the terms of trade over the two years to 2014-15 is now expected as more mining output comes to market and major trading partner growth remains moderate. Additionally, the softer labour market has seen wage forecasts revised lower. Nominal GSP growth forecasts have also been revised lower relative to Budget, from 5¼ per cent to 3¼ per cent in 2013-14 and from 5¼ per cent to 4 per cent in 2014-15.

45. Underpinning growth however, are: expected positive contributions from net exports as imports weaken due to lower demand growth and exports strengthen; solid public final demand growth driven mostly by State government capital spending; a strengthening in dwelling investment as interest rates remain at historical lows; and improving asset prices supporting consumer spending.

46. NSW SFD grew by 0.6 per cent in the December quarter to be up 2.5 per cent through the year. SFD was forecast in the HYR to pick up but remain a little below its trend growth rate of 3 per cent over the forecast period.

47. As at HYR, weaker activity was expected to result in slower employment growth than was forecast at Budget time, resulting in unemployment rates of 6 per cent in 2013-14 and 6¼ per cent in 2014-15, compared to Budget time estimates of 5½ per cent for both years.

48. A number of factors put NSW in a relatively strong position as the national economy transitions from mining investment-led growth to other growth sources. These include an initial lower reliance on mining and a more diversified industry structure. Historically low interest rates, an exchange rate declining in line with the terms of trade and strong housing fundamentals will provide growth impetus. Nevertheless, downside risks to the outlook remain, in particular the timing and extent of the non-mining recovery, together with the recent experience of the exchange rate remaining higher than suggested by fundamental drivers.

Household consumption

49. Household consumption growth has been revised down compared with Budget. Modest employment and wages growth will see below-trend income growth over the next two years, impacting on consumption in the short term. However, rising asset prices should further bolster household wealth and confidence, so that consumption is expected to gather pace between 2013-14 and 2014-15, albeit remaining below trend.

Dwelling investment

50. All housing indicators (building approvals, house prices, lending data) suggest a strengthening housing market. In particular, building approvals have surged in recent months and, accordingly, dwelling investment activity has been revised up since Budget. Rising prices, solid population growth, low interest rates, State government initiatives and pent up demand are likely to provide support for the housing sector over the next two years.

Business investment

51. Underlying business investment growth (i.e. excluding second-hand asset sales) has been revised down since Budget time as mining investment fades and the pick-up in non-mining investment occurs at a slower pace than initially expected. Some positive signs in non-residential building investment are emerging, though, especially in retail and office space.

Public final demand

52. Public demand (consumption and investment) is expected to contribute modestly to growth over the next two years, with Commonwealth Government fiscal consolidation offset by strong growth in NSW Government capital spending. The outlook is modestly stronger than at Budget time.

Net Exports

53. The outlook for net exports of goods and services has strengthened since Budget time. Export growth should rise due to a weakening exchange rate, in line with a falling terms of trade. Weaker than expected private consumption and investment should result in slower growth in imports.

Labour Market

54. Employment grew strongly at 1.5 per cent in 2012-13 but in early 2014 it slowed considerably to almost zero in through the year terms. Leading indicators suggest sluggish employment growth through the remainder of 2013-14. A tentative recovery is expected through 2014-15, although slower economic growth means employment is forecast to rise only modestly.

55. Consistent with national forecasts, the unemployment rate was forecast to drift higher over the next twelve months and average 6¼ per cent over 2014-15.

Inflation

56. In its February Statement of Monetary Policy, the RBA revised short term inflation forecasts upwards. This reflects a "combination of the lower exchange rate and the higher-than-expected December quarter CPI outcome, which have more than offset the effect of the softer outlook for wage growth".[16]

57. The RBA observed that the "various measures of underlying inflation suggest that the quarterly pace picked up to between ¾ and 1 per cent in the quarter – around ¼ percentage point higher than the assessment of underlying inflation a quarter ago. In year-ended terms, the pace of underlying inflation increased to be a touch above 2½ per cent".[17]

58. The proposed abolition of carbon pricing should detract from the headline CPI in 2014-15, resulting in a lower outcome than forecast at Budget time.

Wages

59. The wages growth outlook is also weaker than at Budget time, consistent with recent Wage Price Index movements. Below trend employment growth implies lower wages growth of around 2¾ per cent in 2013-14 and 3 per cent in 2014-15.

Promoting Social Inclusion (s284(1)(b))

60. In its 2013 Review, the Panel observed that:

> For the purpose of conducting an annual wage review, s.284(1)(b) provides that the Panel must take into account promoting social inclusion through increased workforce participation. We accept that our consideration of social inclusion in the context of s.284(1)(b) is limited to increased workforce participation. On that basis it is obtaining employment which is the focus of s.284(1)(b). This involves a consideration of the increased incentives that higher minimum wages can provide to those not in employment to seek paid work, balanced against potential impacts on the demand for low-paid workers and hence the supply of low-paid jobs, from large increases in minimum wages.[18]

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[16] Statement of Monetary Policy, RBA 7 February 2014.
[17] Ibid.
[18] Annual Wage Review 2012-13 [2013]FWCFB400, para [39]

61. In the NSW Government's submission, the best way to promote social inclusion through increased workforce participation and to respond to the relative living standards and needs of the low paid is to ensure that disadvantaged and low skilled job seekers are able to participate fully in the labour market.

62. The NSW Government is committed to pursuing a range of strategies to restore the strength of the State economy, particularly in relation to job creation. Most recently, this includes changes to payroll tax arrangements to provide an additional rebate to businesses that employ workers who have recently lost their jobs through large-scale restructures.[19]

63. Clearly, the rate at which the National Minimum Wage and minimum award rates of pay are set will have a significant bearing on the success of these strategies.

64. It is therefore the view of the NSW Government that the maintenance of a safety net of fair minimum wages must reflect general economic conditions and be balanced against access to employment opportunities and the needs of business.

65. In the 2013 Review, the Panel also observed that:

> Data on the dynamics of labour market mobility show that low-paid employment is an important entry point into the workforce and a stepping stone to higher paid work, however, for some individuals for whom low pay can be highly persistent, increases in minimum wages are particularly important in maintaining living standards.[20]

66. Consequently, when determining any changes to minimum wage rates, the Panel should take into account Australia's soft labour market conditions and forecast below-trend growth.

67. In this regard, it is noted that the participation rate has recently been falling, both at the national aggregate level, as well as in most individual States and Territories.[21]

68. According to a recent report from the Commonwealth Bank[22], there has been a noticeable decrease in the participation rate of 'younger' persons in recent years. The participation rate of persons entering the labour market (15-19 and to a lesser extent, 20-24) has trended lower over the past five years, falling most sharply in the past two years. The report attributes this decline to cyclical factors, such as 'younger' persons adapting their decisions about work and tertiary education around changes in labour market conditions.

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[19] Payroll Tax Rebate Scheme (Jobs Action Plan) Amendment (Fresh Start Support) Bill 2014 introduced 6 March 2014
[20] Annual Wage Review 2012-13 [2013]FWCFB400, at para [462]
[21] See FWC – Statistical Report – Annual Wage Review 2013-14, Chart 6.2
[22] Aird, Gareth, (31 October 2013), 'The participation rate is falling – why?' *Global Markets Research*, Commonwealth Bank of Australia

69. The report also points out that most workers in the 15-19 cohort are employed in industries such as retail trade, where consumer spending has been soft, which may have limited job opportunities in these industries.

70. To encourage a higher participation rate from this cohort of workers (particularly those from a low skills base), it is important that adjustments to minimum wages do not prevent them from entering the labour market or price them out of it.

71. Until recently, the aggregate participation rate for the 55+ cohort was trending higher due to improved healthcare and the shift towards less manual labour. This occurred despite the general increase in the share of the population over 65. However, the Commonwealth Bank report suggests that this structural lift in the participation rate of ‘older’ cohorts has been exhausted. It attributes this, in part, to the fact that some ‘older’ workers delayed retirement and stayed in the workforce longer than they originally intended as a result of the GFC. These workers are now exiting the labour force, resulting in the overall participation rate for 60-64 year olds drifting lower.[23]

72. The participation rate of those of ‘prime working age’, the 25-54 cohort, is the least volatile, as most people within this age group have finished tertiary education and are not retired or approaching retirement. Over the last year, the participation rate has fallen marginally for this group, which the report attributes to the cyclical factor of a relatively small number of discouraged workers leaving the workforce due to a soft labour market.[24]

73. Notwithstanding these falls in the participation rate, NSW job performance has been good, with almost 110,000 new jobs created since the Government came into office in March 2011.[25]

74. Minimum wage jobs provide employment for low skilled workers, function as an important stepping-stone for new entrants into the labour market, particularly young people, and provide opportunities to develop employability skills that facilitate progression to higher paying jobs.

75. The NSW Government submits that the best way of promoting increased workforce participation is to ensure that the level at which minimum wages are set is appropriately balanced with the continuing provision of employment opportunities.

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[23] Ibid
[24] Ibid
[25] NSW Government, 3 Years of Achievements – Overview brochure

76. In addition, the NSW Government submits that the Panel should have regard to the role which the tax-transfer system could play in relation to the maintenance of an effective safety net for the low paid. The NSW Government particularly notes and endorses the observations of the Panel in the 2013 Decision where it provided:

> …that increases in minimum wages are a blunt instrument for addressing the needs of the low paid…..The tax-transfer system can provide more targeted assistance to low-income households and is a more efficient means of addressing poverty.[26]

77. Any decision to set minimum wages must appropriately take into account the role played by the tax-transfer system in supporting the living standards of low paid workers.

78. Minimum wages must not act as an impediment to affected workers securing and maintaining employment, or regaining employment once out of the workforce. Nor should a minimum floor be set such that it raises costs to a level that hinders an enterprise's competitiveness.

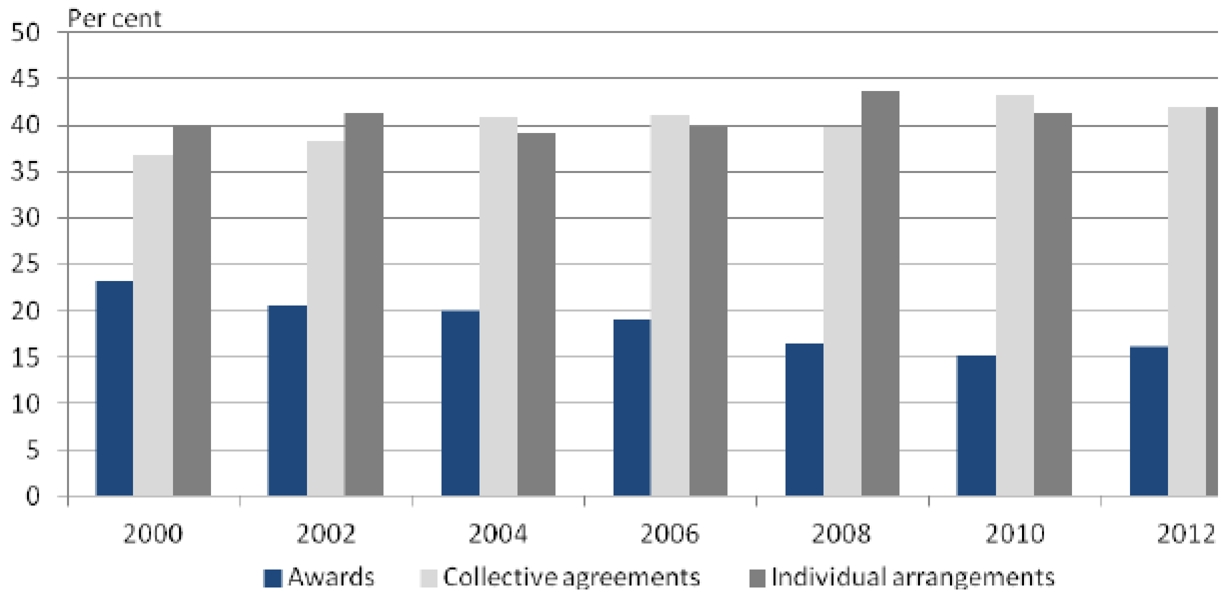
Encouraging Collective Bargaining (Modern Awards Objective s134(1)(b))

79. In the 2013 Review decision, the Panel observed that:

> The current evidence indicates that the level of increases in minimum award wages which have occurred over the last decade are compatible with the continuing encouragement of enterprise bargaining.[27]

80. As noted in that Review, the number of employees who have their pay set by awards has steadily declined over the last decade or more, as per the following graph.

[26] Annual Wage Review 2012-13 [2013]FWCFB 400, at para [57]
[27] Annual Wage Review 2012-13 [2013]FWCFB 400, at para [477]



[Annual Wage Review 2012-13 [2013]FWCFB 400, Chart 8.1]

81. Further, it would appear that differences between award/national minimum wage outcomes on the one hand and bargained outcomes on the other remain significant. The September 2013 Quarter Release of the DEEWR Trends in Federal Enterprise Bargaining data series indicates an average annual increase of 3.5 per cent in wage outcomes across all industries. This compares with a 2.6 per cent increase to the rates of pay determined at the 2013 Review.

82. However, recent research has considered the effect of Annual Wage Review decisions on incentives to bargain in some detail, and concluded that:

> The direct impact of AWR decisions was perceived to be limited at the work sites studied. However, analyses of enterprise agreements revealed some prima facie associations with AWR decisions. Further, the workplace cases in general, and the relativities analysis in particular, revealed that minimum wages themselves (awards) can shape the wage determination process and wage outcomes. All of these findings are consistent with and help to better understand findings from the related 2012–13 study of award reliance. If the AWR increases examined are conceived as being part of an ongoing evolution of the award system, then their impact could be seen to be significant, primarily because such increases are an integral part of a labour standards regime that conditions workplace behaviour and shapes wage outcomes. This appears to be especially the case in those parts of the labour market paying below median wages.[28]

83. The more recent research therefore appears to paint a more complex picture, and suggests that minimum award wage decisions made by the Panel may have an indirect impact upon wage outcomes in the bargaining stream.

84. It is critical that a sustainable safety net of minimum wages is one that supports enterprise bargaining at NSW workplaces. In particular, the Panel should set minimum wages at a level that maintains incentives for enterprise bargaining that rewards flexible and productive work practices.

[28] FWC Research Report 7/2013 pxii, footnotes omitted

85. The NSW Government submits that any unnecessary increase to minimum wages that does not reflect productivity improvements may limit the capacity of businesses to absorb such increases and consequently have a deleterious impact on employment growth.

Part 3 – Submissions Regarding Productivity and the Relative Value of the Minimum Wage

86. In the 2013 Decision, the Panel observed that:

> We appreciate that a gap exists between increases in modern award wages and productivity growth over the past decade which is a relevant consideration in fixing minimum wage rates. However, we are not confident that the forces behind that phenomenon, or the effect on factor shares in the event of a reversal of the divergence between consumer and producer prices in the future, have been adequately explored nor have the implications for minimum wage fixation been clearly identified. However, we have considered recent movements in productivity and the relative living standards of the low-paid in adjusting minimum wages in the current review. We do not propose, on the information currently before us, to draw conclusions about that gap for the purpose of our current determination. In the 2013–14 annual wage review, we will invite further submissions on the implications of the fall in the labour share of national income over the last decade for minimum wage fixation within the statutory parameters applying to the review.[29]

87. This part of the NSW Government's submission aims to address the productivity issues referred to by the Panel.

<u>Australian Productivity Performance</u>

88. National labour productivity grew by 2 per cent in the year to 2012-13.[30]

89. Labour productivity performance by industry for the year to 2012-13 is presented in the following table.

Table: Labour Productivity growth rates by industry[31]

Industry	Growth rate 2011-12	Growth rate 2012-13
Agriculture, Forestry and Fishing	11%	-1%
Mining	-12%	3%
Manufacturing	2%	0%
Electricity, Gas, Water and Waste Services	-4%	6%
Construction	6%	1%
Wholesale Trade	8%	0%
Retail Trade	3%	2%
Accommodation and Food Services	4%	-2%
Transport, Postal and Warehousing	6%	1%
Information, Media and Telecommunications	-3%	-4%
Financial and Insurance Services	-3%	8%
Rental, Hiring and Real Estate Services	1%	6%
Professional, Scientific and Technical Services	1%	0%
Administrative and Support Services	-3%	7%
Arts and Recreation Services	3%	0%
Other Services	5%	-4%

[29] Annual Wage Review 2012-13 [2013]FWCFB 400, at para [167]
[30] Australian Bureau of Statistics [ABS] Estimates of Industry Multifactor Productivity, 2012-13. Cat 5206.0.55.002
[31] ABS, Estimates of Industry Multifactor Productivity, 2012-13. Cat 5206.0.55.002

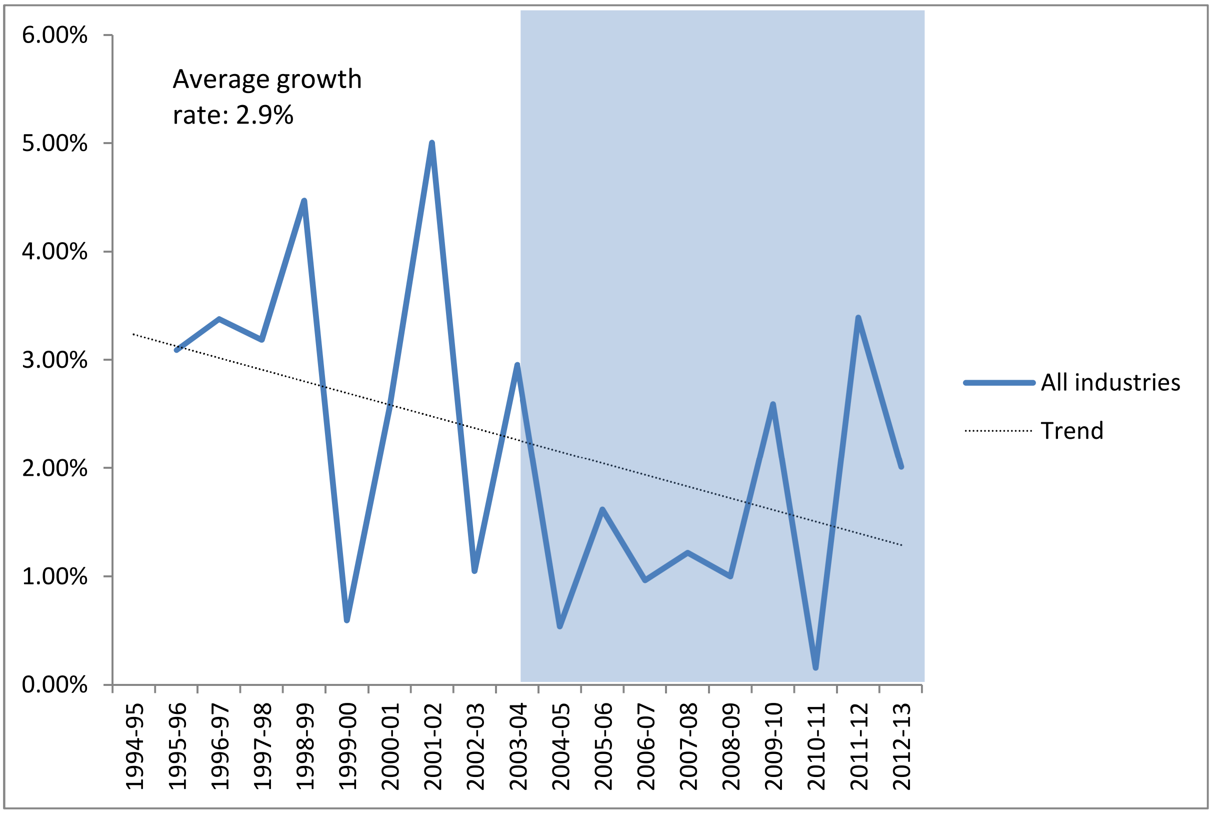
90. Most industries had growth in labour productivity over the year to 2012-13. Notably, electricity, gas and water services (6 per cent), finance and insurance services (8 per cent), rental hiring and real estate services (6 per cent) and administrative and support services (7 per cent) had growth rates well above the all market sector average of 2 per cent.

91. Agriculture, forestry and fishing (-1 per cent), accommodation and food services (-2 per cent), and information, media and telecommunications (-4 per cent) saw labour productivity declines over the period.

92. However, comparison of the results for 2012-13, to the results in 2011-12 show the inherent volatility of the labour productivity series – in seven of the sectors the growth rate changes sign over the two measurement periods.

93. The following chart shows the growth rate of labour productivity for the sixteen market sector industries between 1994-95 and 2012-13.

Chart: Labour Productivity performance: 16 market sector industries[32]



94. Key observations from this data series are:

- Labour productivity grew by around 2 per cent over the year to 2012-13.
- National labour productivity in the period from 1994-95 to 2003-04 grew by an average of 2.9 per cent.

[32] ABS Estimates of Industry Multifactor Productivity, 2012-13. Cat 5206.0.55.002

- From 2004-05 to 2012-13 labour productivity has grown by an average of 1.4 per cent.

- The labour productivity series is extremely volatile. At the national level, labour productivity for 2011-12 was 2.9 per cent. However in 2010-11, labour productivity grew by only 0.2 per cent.

- Given the volatility inherent in the labour productivity series, single year samples are likely to be insufficient to use as the basis for stable wages policy.

95. Trends by industry are presented in the following table.

Table: Labour Productivity growth rates by industry

	1994-95 to 2012-13	1994-95 to 2003-04	2004-05 to 2012-13
	5%	8%	3%
	-2%	1%	-5%
	2%	3%	1%
	-1%	2%	-4%
	2%	2%	2%
	4%	6%	2%
	3%	3%	2%
	1%	2%	0%
	2%	3%	2%
	3%	4%	2%
	3%	4%	3%
	0%	0%	1%
	1%	2%	0%
	1%	1%	1%
	1%	2%	0%
	2%	3%	0%

96. In the majority of industries, labour productivity growth in the second part of the period (2004-05 to 2012-13) is significantly lower than in the period from 1994-95 to 2003-04.

97. In some sectors, namely the mining and electricity, gas and water sectors there has been a prolonged period of labour productivity decline since 2004-05. These sectors have been characterised by a rapid period of capital accumulation.

International comparisons

98. The following table presents average labour productivity growth from a selection of OECD countries from 2000 to 2012.[33]

Table: Labour Productivity growth rates comparison[34]

Country	Average 2000 to 2012 (%)
Australia	1.4%
Canada	0.8%
New Zealand	1.2%
Norway	0.6%
Russian Federation	3.9%
United Kingdom	1.1%
United States	1.9%
OECD Total	1.5%
G7	1.4%

99. Key points:

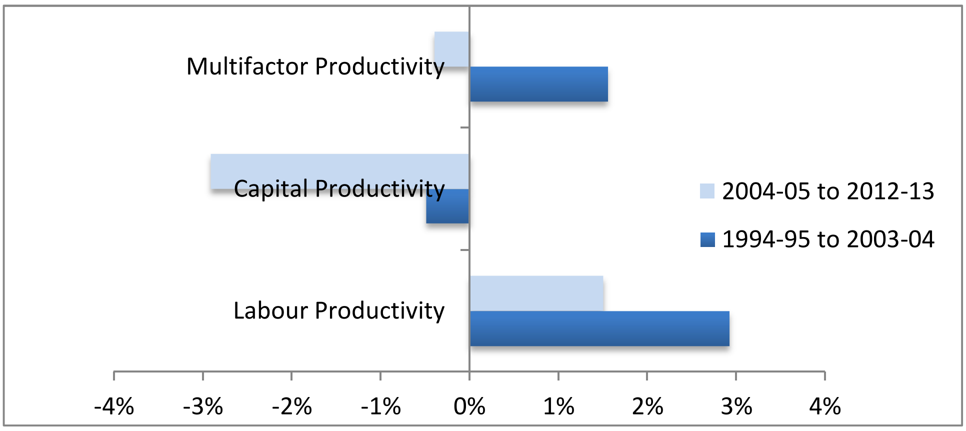
- It is notable over the period that labour productivity performance was in a relatively narrow band.
- The Russian Federation is a notable outlier at 3.9 per cent average productivity growth, however the Russian Federation underwent significant structural change over this period.
- Norway (0.6 per cent) and Canada (0.8 per cent) were the lower performing countries for labour productivity growth, which is notable due to their relative dependence on natural resources.

Comparisons to Capital Productivity and Multifactor Productivity (MFG) Growth

100. The following chart presents a comparison between labour productivity, capital productivity and MFP growth over the period from 1994-95 to 2012-13.

[33] The selection includes resource intensive economies where available.
[34] Organisation for Economic Cooperation and Development [OECD] *Productivity Statistics, oecd.org, accessed 10 February 2014.*

Chart: Labour productivity, capital productivity, and MFG performance: Sixteen market sector industries



101. It is notable that capital productivity has been in continuous decline over the period while labour productivity has grown strongly. These factors have more to do with shifts in the capital labour ratio in the economy than with actual productivity change.

102. MFP grew strongly in the period to 2003-04, but growth has declined since 2004-05.

<u>Labour productivity measures</u>

103. Labour productivity measures the quantity of output per hour worked. It is generally calculated by dividing value added by hours worked (or gross output by hours worked). However, it should be noted that the value added or gross output of the economy is driven by both labour and capital, so labour productivity will be driven by both the use of labour and capital.

104. Measures of labour productivity are driven by a combination of two measures – one is growth in MFP and the other is a change in the ratio of labour and capital used in the production process.

105. Capital deepening, or an increase in the capital intensity of production will result in more output being produced per unit of labour. This means that capital deepening would drive an increase in labour productivity. In a situation where MFP growth for an industry is zero, but the industry experiences capital deepening, we would see positive labour productivity growth.

<u>Effects of commodity prices, terms of trade</u>

106. High commodity prices, and the increase in the terms of trade have no direct impact on labour productivity (or MFP) growth as these use volumes, rather than values of outputs and inputs.

107. However, the indirect impact of high commodity prices has been rapid expansion (particularly in capital usage) in industries that benefit from these higher commodity prices (largely mining). Capital deepening, with a less than proportionate impact on outputs, will cause MFP declines in these industries.[35] As Australia moves to the export stage of the mining boom, it would be expected that MFP will begin to recover in these industries.

108. While not as obviously affected by terms of trade shocks, other industries which have seen significant capital investment over the past decade have experienced a similar outcome, notably electricity, gas and water.[36]

Wage and profit shares of income growth

109. Labour income grew more rapidly in the 2000s than in the 1990s, through stronger growth in both wages and employment. However the labour share of income fell by more than four percentage points over the 2000s because capital income growth accelerated even more. That is, the labour share has fallen as a result of the rapid growth in capital income over the 2000s rather than poor wage performance.[37]

110. The growth in the capital income share was driven largely by the rapid capital accumulation during the investment phase of the mining boom. This rapid capital accumulation resulted in an economy that was more capital intensive (with a correspondingly higher capital share) than before the mining boom.

111. The terms of trade have begun to decline, and are anticipated to fall further. Accordingly, there should be some automatic reversion towards trend shares of labour and capital income. However, the economy is now significantly more capital intensive and the share of labour income should not be expected to return to its pre-mining boom level.

112. Attempts to artificially grow labour income to recover 'lost' income share through aggressive wages policy (for example) would likely have adverse consequences for employment and inflation and for industries already facing adjustment pressures. This issue is more pertinent where an industry is relatively labour intensive – notably tourism, which has high award coverage and is heavily trade exposed.

Implications For Minimum Wage Fixation

113. In the NSW Government's submission, labour productivity is an incomplete measure that should not be used as a guide to assess the appropriateness of minimum wage adjustments.

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[35] Productivity Commission (2009) *Australia's Productivity Performance.* Submission to the House of Representative Standing Committee on economics. September 2009.
[36] Parham, Dean (2013) *Labour's share of growth in income and prosperity,* Productivity Commission Visiting Research Paper, September 2013.
[37] Ibid.

114. Labour productivity is largely driven by factors that are not entirely related to productivity, namely capital deepening. Two industries, mining and electricity, water and gas have undergone rapid capital deepening in the past decade and this has driven much of the growth in labour productivity over that time.

115. Capital deepening is driven by other factors including changes to the terms of trade, commodity prices, and policy decisions, which fluctuate wildly over the business cycle. This leads to a measure that is inherently volatile.

116. Consequently, it is submitted that labour productivity should not be used to guide minimum wage decisions due to its inherent volatility, and its tenuous link to actual productivity.

Part 4 – Conclusion

117. The NSW Government submits that, in arriving at its decision, the Panel should give particular weight to the following three concerns.

118. Firstly, the NSW Government believes that as many people as possible should be afforded the opportunity to obtain employment in the workforce. Many award reliant jobs, particularly for the young and low skilled, can be used as a stepping-stone to provide opportunities for individuals to develop their skills and progress to higher paid jobs in the future. It is therefore essential that minimum wages are not set at a level that has a detrimental impact upon the capacity of business to absorb such increases which in turn may cost employment opportunities.

119. Secondly, it must be noted that economic conditions and the medium-term outlook remain uncertain. Economic growth continues to be below trend and appears likely to remain so in the short term. Labour market performance has been unsuccessful in containing unemployment edging to 6 per cent, and forecasts indicate only modest improvement in the short term. Unemployment has increased as a result of a period of below trend growth which is not yet over.

120. Thirdly, recent research provided to the Commission indicates that the effects of minimum wage adjustments may not be confined to award-reliant employees, but may extend to a significant proportion of the workforce, with uncertain effects on incentives to bargain.

121. In the NSW Government's submission, these concerns should compel the Panel to take a cautious approach to any adjustment to minimum wages in the current Review.