



Setting Australia's Minimum Wages in 2007 and Beyond:
Building a new Australian economic institution

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I would like to start by thanking the School of Economics at the University of Queensland for inviting me to deliver the 17th Colin Clark Memorial Lecture.

I commenced my formal training as an economist at this University, graduating with an Honours degree from what was then the Department of Economics in 1977.

So it is a special privilege to return to Brisbane today and to follow in the footsteps of so many great economists, both Australian and international, who have delivered the Colin Clark lecture.

I never had the pleasure of meeting Colin Clark, having departed for southern ports before he returned to take up his honorary position in the Department.

But no economist, properly trained, could be unaware of his seminal work and towering reputation as an applied economist.

I think it was Heinz Arndt who described Clark as having, "one of the most fertile minds in twentieth century applied economics". High praise indeed.

In preparing for today's lecture I came across a couple of Clark quotations that appealed to me.

Clark said in a letter to Keynes in 1938: "I am having an excellent time in Australia where economics ranks next after cricket as a topic of public interest". ⁽¹⁾

I'm not sure whether this still holds true today or indeed whether Dr Clark was gently ribbing Lord Keynes in the best Australian tradition. But while interest rates might possibly qualify as a high-ranking topic of public interest, I doubt that even they could trump cricket as a national obsession!

Clark also noted in 1941 that: "Queensland is a predominantly rural and small enterprise economy, with a very equalitarian distribution of income and property, very generous social services, compulsory Trade Unionism, and all matters of wages hours and working conditions judicially controlled by the Arbitration court, which now has such prestige that both sides always accept its decision." ⁽²⁾

As a former Queenslander myself, I must say I don't recognise my home state in that description—certainly not today, when things are so dramatically different, especially here in Brisbane, than they were when I left 30 years ago.

The Queensland economy is no longer so rural or small enterprise, trade unionism is no longer compulsory and the federal wage-setting role of the Arbitration court is now performed by the agency I have the privilege to chair.

But, on the other hand, some things haven't changed so much.

Australia still boasts a very robust social safety net and despite all the commentary about the Australian Fair Pay Commission's wage-setting powers, I am pleased to say that our decisions are accepted, even if people don't always agree with them.

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This brings me to the subject of my address today – *Setting Australia's Minimum Wages in 2007 and beyond*.

I have subtitled my address – *Building a new Australian Economic Institution* – because, as you will be aware, the Australian Fair Pay Commission is almost brand new.

In fact, the Commission was established only as recently as March last year.

Since then the Commission has:

- announced two minimum wage decisions;
- implemented a more comprehensive minimum wage safety net system for people with disabilities; and



- introduced new pay arrangements for the real estate sector.

In September this year, the Commission will:

- look into the role of pay and classification scales in the Australian workplace;
- commence a review of junior and trainee wages; and
- consider how we might go about rationalising nearly 4,000 awards and 105,000 pay scales.

So you can see it has been a busy start for the Commission.

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I am often asked why I accepted the role of Chair of this new and somewhat controversial institution.

A colleague put it quite starkly: 'Why on earth did you put your head into a mangle like that?!'

It is above all else an opportunity to serve one's country in a significant capacity and I am honoured and privileged to be given this responsibility.

But I also recognise that, in my working life as an economist, I will probably only get one chance to build a new economic institution from the ground up.

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I mentioned earlier that the Australian Fair Pay Commission replaces the wage-setting role previously performed by the Australian Industrial Relations Commission.

Like its predecessors, the Fair Pay Commission still sets and adjusts minimum wages in the federal sphere but we do so with a quite different legislative remit.

For the first time, those who are affected by minimum wage decisions—workers, their employers and the unemployed—can have a direct say in what minimum wages should be.

We have moved from an adversarial system to a consultative one, supplemented by independent research and analysis.



A new institution for setting minimum wages with a fresh approach is suited to our changing times.

The legislative charge to the Australian Fair Pay Commission is, 'to promote the economic prosperity of the people of Australia'. This places the Commission among a small number of public agencies with responsibility for implementing national economic policy.

Another of these bodies, the Reserve Bank of Australia, sets the cash interest rate to promote national economic prosperity, among other objectives.

Like the Reserve Bank, the Australian Fair Pay Commission has only one economic lever to pull. In our case, it is the level of minimum wages.

Obviously, there's a good deal more to economic prosperity than the level of minimum wages—or the level of interest rates, for that matter.

But, like interest rates, minimum wages influence important decisions in our economy and can affect employment conditions (especially for the low paid), the rate of inflation and ultimately the competitiveness of the Australian economy.

Workforce participation is one of the key drivers of our future economic prosperity. As our population ages, Australia's future economic growth and living standards will depend upon an adequate supply of labour.

Minimum wages can affect labour supply as well as labour demand. In other words, minimum wages, including classification minimum wages, can affect a worker's decision to take up employment as well as an employer's decision to offer it.

The Australian Fair Pay Commission's focus, first and foremost, is on jobs.

Pricing workers out of the labour market does not promote Australia's economic prosperity and will significantly reduce the capacity of the lowest paid and most vulnerable Australians to share in that prosperity.

While having a job is widely recognised as a guard against poverty and disadvantage, it is just one component of the social safety net.

An effective social safety net requires, in addition to decent minimum wages, targeted assistance provided through the income tax and social security systems.



Earlier this month, I was pleased to be able to meet three low-paid workers from the United States who were brought to Australia by the ACTU to discuss life on minimum wages.

Their stories were compelling and in certain respects troubling.

But they also highlighted the very profound differences between our system and that in the United States.

Life on low wages is always challenging, regardless of the country or the context, but in Australia an extensive social safety net exists, including universal health care, parental payments, and unemployment benefits.

And of course our minimum wages are significantly higher. In fact, they have been and remain among the highest in the developed world.

Setting minimum wages at appropriate levels affects *both* the potential for economic prosperity *and* people's capacity to share in rising community living standards.

Placing minimum wage-setting among the other instruments of economic policy establishes the context within which the Australian Fair Pay Commission operates.

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Colin Clark was an applied economist who devoted his working life to developing statistical measures of economic activity.

I am often asked, usually by journalists, to reveal the formula that underpins the Fair Pay Commission's decision making.

Let me state unequivocally that there is no formula and there can be no formula.

Setting minimum wages is very much a question of balancing a range of often competing priorities, without the Commission being able to influence all or any of them directly.

Ultimately, the Commission must weigh up a mix of factors that influence not only an individual's decision to seek or remain in work but also the employer's decision to take on or shed workers.



This requires an informed judgement based on an amalgam of available data and research, and a reading of the prevailing social and economic conditions.

This need for judgement is reflected in the make-up of the Commission. As you may be aware, the Commission comprises five individuals who each bring different backgrounds, skills and interests to the table.

Aside from myself, there is Professor Judith Sloan who is a labour economist and a Commissioner at the Productivity Commission.

There's also Hugh Armstrong, who has retired now, but rose to be national president of the Australian Services Union, and is a lifelong trade unionist.

There is Patrick McClure who was, until recently, CEO of Mission Australia for 10 years and who brings a welfare perspective to the Commission.

And there's Mike O'Hagan, who is a successful small businessman here in Queensland. Mike owns MiniMovers, a business that is active in both Queensland and Victoria.

As a non-judicial authority, the Australian Fair Pay Commission can inform itself independently on questions of fact or interpretation which arise in its deliberations. This knowledge adds to the information brought before the Commission through submissions and consultations.

The Commission is committed to monitoring the results of its decisions. We expect to learn from experience.

We have developed two research projects that identify relevant existing data and how these might be used to monitor wage decisions in light of the Commission's legislative wage-setting parameters.

Our monitoring strategy allows us to analyse the impact of our decisions at an aggregate as well as an industry, regional and (in some cases) workplace level. It provides us with tools to identify emerging trends in employment and wages.

Independent research undertaken or commissioned by the wage-setting authority is a completely new feature of our system. A judicial or arbitral body is precluded from considering evidence apart from that brought before it by parties to a dispute.



The Commission places great importance on the use of research to inform its decision making.

We have established an expert stakeholder committee to advise us on the appropriate direction and approach for our research. The committee includes representatives from peak employer and employee organisations, community groups, and governments (including the states).

We are committed to evidence-based decision making and will continue to undertake and commission research from independent experts to inform our decisions. All of the commissioned research is published on our website.

Through our research program, we are building a bank of knowledge on the Australian labour market and the minimum wage. The steady accumulation of evidence and analysis will allow the Commission's decisions to be better informed as our work progresses.

This year we have commissioned research into the economic and social circumstances of young Australians aged 15 to 20 in anticipation of the Commission's enquiry into junior wages later in the year.

In addition to research, the Commission each year undertakes one of the most extensive community and stakeholder consultation programs in Australia.

Submissions to our second minimum wage review closed in April this year. We received 73 responses from employee and employer organisations, community groups, state and federal governments, academics, individuals and businesses.

Everyone has the opportunity to make written submissions to the Commission, and all submissions are posted on our website (unless confidentiality is requested).

Through our national submissions campaign, we sent information to some 7,000 community locations around the country, including local libraries, Councils and job network providers, to inform people of our work and to encourage their participation in the submissions process.

For the 2007 wage review, we developed an online submission form and trialed internet-based discussion groups, through national bulletin boards. We found this to be an especially effective way to access young people.



We also provide information in the major community languages to inform the public of our work and how we operate.

Since our establishment last year, the Commission has met with more than 200 stakeholder organisations representing the views of employers, employees, community groups and governments.

This year we met with key stakeholders to discuss their submissions to the 2007 wage review and to seek their feedback on the impact of our 2006 decision.

Commissioners visit various sites around the country, meeting with people and talking with them about employment and training issues.

We have established a Business Consultative Group to hear about the impact of our first decision on small to medium-size employers in metropolitan and regional Victoria. The Commission plans to run similar sessions in other states in future.

No Australian is precluded from having a say about federal minimum wages.

Talking to people about their circumstances and hearing at first hand how minimum wages affect their lives is an enlightening and grounding experience.

We have travelled across Australia to talk about our role and the wage-setting process. Last year we held community meetings in metropolitan and regional centres from Albany to Traralgon, from Launceston to Rockhampton, and encouraged people to talk directly with the Commission. We will continue this valuable work in 2007 and beyond.

During February and March this year, we held 24 focus group discussions to hear directly the views of those most affected by our decisions—the low paid, the unemployed and employers of the low paid. We also spoke to juniors, indigenous Australians and people from culturally and linguistically diverse backgrounds.

One striking theme that emerges from the focus groups is that low-paid workers are not a homogenous group. Low wages are earned by people across a very broad spectrum of our society.

How a single 18-year-old student living at home and working casually feels about life on low wages is generally quite different from a person who is self-



supporting, perhaps with dependant children, and for whom low wages are the sole source of income.

Some people work in low-wage employment because they lack the skills or training to move into higher-paid positions. For others, life on low wages, while financially challenging, is a choice they make, given other priorities in their lives.

We found different views across the regions. People living in areas brimming with employment opportunities have quite high wage-bargaining power and employment flexibility, whereas those in struggling locations may not.

We learned that many unemployed people feel that low wages do not provide enough incentive for them to seek work due to the impact on their benefits and in some cases on their lifestyle. But we also found that, for a range of social and psychological reasons, the majority preferred employment to the alternative. This is especially true if they can see a pathway through low-paid work to a steady job paying good wages.

Research, consultations, and submissions—these are the hallmarks of the new approach to minimum wage setting. In an increasingly complex and fast-changing world, the Commission needs input from every quarter to be fully informed about what's happening on the ground.

People are having their say about minimum wages ... and the Commission is listening.

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Further evidence of the Commission's desire to inform itself is a recent visit by the noted American labour economist, Professor David Neumark of the University of California at Irvine.

David Neumark, in collaboration with Bill Wascher, co-authored a landmark review of more than 90 research articles written over the past 15 years analysing the employment effects of minimum wages.

The Commission organised a forum to engage our stakeholders, including employer groups, trade unions, welfare organisations and government officials in discussion of Professor Neumark's work.

Broadening our collective knowledge of the economics of minimum wages is a priority for the Fair Pay Commission.



But the relationship between minimum wages and labour demand, which is the primary focus of the Neumark and Wascher survey, is not all there is to be said about the setting of minimum wages.

Professor Neumark himself observed that increases in minimum wages very probably cost jobs, at least relative to what otherwise would have been the case.

But he went on to point out that the disemployment effects of minimum wage increases may nevertheless be outweighed, in terms of their social benefit, by the effects on the living standards of low-paid workers who keep their jobs.

This balancing of social benefits and social costs in assessing the impact of minimum wage movements is very much consistent with the approach taken by the Australian Fair Pay Commission.

The Commission hopes to conduct similar seminars with labour market or employment experts in the future to continue to inform itself of current research.

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In its May budget, the federal Government allocated \$5 million to the Commission over three years to create and publish new Pay Scales.

These Pay Scales will establish legally-binding instruments that provide employers and employees with a clear understanding of minimum rates of pay across the many different pay classifications.

The Commission has been meeting with key stakeholder organisations—including the ACTU, ACCI, the Ai Group, and the Australian Government—to determine the most effective and efficient way to tackle this project.

An agreed process for creating new Pay Scales and a priority list have been developed by the Commission in consultation with its Pay Scale Stakeholder Reference Group.

The first Pay Scales to be created cover a cross-section of industry sectors and large numbers of Pay Scale-reliant workers.

The Commission expects to begin publishing new Pay Scales by October this year, although it is anticipated that the drafting of some more complex Pay



Scales will require extensive consultation and therefore take longer to complete.

We anticipate that having created the priority Pay Scales, many substantive issues of definition and scope will be resolved allowing the whole process to gather momentum.

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A related but different challenge is the rationalisation of Pay Scales. The Commission has benefited from a comprehensive report on this topic written by Matthew O'Callaghan. This report is published on the Commission's website.

There is no hiding the fact that rationalising the Pay Scales is a complex and demanding task. Consider for a moment what is involved. There are around 4,000 separate Pay Scales and about 105,000 different classifications or pay points within these scales.

Admittedly, many classifications are simply redundant—but the fact remains that we have inherited from the old award system a complex and confusing array of Pay Scales.

What principles should guide the Commission in rationalising Pay Scales? How important are these scales in securing economic prosperity for the Australian people? What role should rationalised Pay Scales play in a modern, flexible labour market?

We need to get this right.

We need to get the facts; find out what the issues and options are; involve stakeholders in a meaningful dialogue; and reach a decision that is fair, balanced and reasoned.

In September this year, we will publish an Issues Paper outlining the challenges involved in Pay Scale rationalisation and seek feedback from interested parties.

The Commission has decided to incorporate the planned review of junior wages (as well as wages for trainees and apprentices) within the broader Pay Scale rationalisation process.



Given that many Pay Scales contain provisions relating to payment arrangements for juniors, trainees and apprentices, it makes sense for the Commission to conduct the various reviews concurrently.

Given the complexity and importance of the task, we will be looking for cooperation among parties who have been historical adversaries in such matters. This will be a test of the Commission's collaborative approach.

The Commission is determined to make the most of this opportunity to reconsider Australia's framework of classification wages. It places us in the foreground of a national economic debate.

Submissions to the review of Australian Pay and Classification Scales in the Australian workplace will close on Friday, 14 December 2007, while those to the review of junior and training wages will close on Friday, 29 February 2008.

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Now a few words about the future ...

How will I know whether or not I have succeeded as the Commission's inaugural Chair when my term concludes in around three years' time?

The first marker of success is that the Commission will be seen by the Australian community to be focussed on and responsive to the needs of unemployed and low-paid Australians. It will be seen as approachable and accessible in the way it goes about its business.

Having established this as a primary aim, I do not underestimate the challenge of creating an environment in which Australians feel comfortable about approaching the Commission and communicating with it.

It is too easy to assume that our audience is educated and at ease with formal processes. We must continue to explore ways of capturing the views of those most affected by our decisions, regardless of their education, background and resources.

I would hope that the Commission is respected and recognised both in Australia and internationally for the quality of its work.

I would want the Commission to be seen as a leading authority on minimum wages and labour markets in Australia, a centre of excellence which attracts



high quality staff and is renowned for the quality of its research, both commissioned and in-house.

Our work will be informed by a range of social and economic research and consultative processes that provide the Commission with knowledge of what is actually happening at both enterprise and individual level, and across states and regions.

I would like to have established effective working relationships with our many stakeholders and have entrenched a collaborative and non-adversarial approach to minimum wage setting. I would also hope that we have earned a reputation for independence in our thinking and in our decision-making.

In sum, I would hope that the Commission will enjoy the respect and standing of an expert, independent economic agency like the Reserve Bank of Australia.

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Setting minimum wages is a singularly important task that goes to the heart of the kind of economy and society we want for Australia.

Choosing the right level for minimum wages influences our chances for enjoying economic prosperity and engaging as many of our citizens as possible in that prosperity.

In many respects, a society is to be judged by the way it treats its least advantaged citizens. I would like to think that the Australian Fair Pay Commission is contributing towards a fair go for all members of our community but most especially unemployed and low-paid Australians.

We will do this if we keep our eyes fixed on the goal of promoting economic prosperity—in other words, setting minimum wages at levels which encourage employment and participation in the workforce while contributing towards a fair and realistic safety net for the low paid.

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Colin Clark wrote in 1940: “There is room for two or three economic theorists in each generation, not more. Only [people] men (sic) of transcendental powers of reasoning can be candidates for these positions. The rest of us should be economic scientists, content steadily to lay stone on stone in building the structure of organised knowledge”.⁽³⁾



He described his work as a, “careful systematisation of all observed facts, the framing of hypotheses from these facts, prediction of fresh conclusions on the basis of these hypotheses, and the testing of these conclusions against further observed facts”.

This aptly describes the approach I am seeking to entrench at the Australian Fair Pay Commission. Laying the foundations of a new economic institution, one with a new focus and legislative framework, requires patient attention to Clark’s “careful systemisation of all observed facts”, as well as his call for constant testing of conclusions against those facts.

Clark was a consummate applied economist. If the Commission holds to the principles he espoused, I have every confidence that we will achieve the objectives laid down for us by the Australian Parliament.

ENDS



NOTES

- (1) Markwell, D.J., "Keynes and Australia", A paper presented at a seminar at the Reserve Bank of Australia, p. 43, 18 September 1985
- (2) Maddison, A., "Macromeasurement Before and After Colin Clark"
http://www.ggdc.net/maddison/articles/colin_clark.pdf, p. 11
- (3) Maddison, p. 15

