

Why have a minimum wage?

Steve Maharey

The minimum wage is again the focus of debate. As unemployment rises and young workers in particular end up on an unemployment benefit, some commentators have argued that the minimum wage is to blame.

If only the minimum wage were lower, so the argument goes, employers would be able to offer jobs. But the rise in the minimum wage has pushed the price of labour to a point where they simply cannot take the risk.

This may be true. Equally, it may not be true. The fact is that no one really knows if the minimum wage is contributing to current high levels of unemployment or not.

In general terms the research we have available to us from around the world suggests that the minimum wage, set at a level that matches the state of the labour market, will not cost jobs. And therein lies the test – matches the state of the labour market. In New Zealand, the minimum wage is set after information has been gathered by the Department of Labour and tendered to Ministers. On the basis of the evidence presented Ministers agree on the rate. Given that the current Government is very sensitive to the needs of employers, it can be assumed that the last three minimum wages were set with an eye to what seemed “reasonable”.

So it is perhaps safe to conclude that despite the lack of empirical evidence about the impact of the minimum wage on current levels of unemployment, we can be assured that every care has been taken to ensure labour is not being priced out of the reach of employers.

Yet the arguments continue, so it may be useful to set out why we have a minimum wage at all.

The first reason is that it is one of the main ways of dealing with inequality. In societies like ours where income inequality is a major issue, the minimum wage is an attempt to ensure those at the bottom end of the scale have at least enough money to live on. The results of inequality are well known and documented so it seems sensible for any society that can afford to do so to have a minimum wage.

It follows, and this is the second reason, that workers should not be expected to work for very low wages. This is nothing more than exploitation and a society that has any sense of fairness should not allow this to happen.

Third, wages should be set at as level that does not require the Government to provide subsidies. In all developed nations, Governments do offer a range of financial supports to workers, particularly those with families, but there has to be a limit. Without a minimum wage it would be all too tempting for at least some employers to take advantage of what the Government offers. A fair days pay for a fair days work should be the starting point for wages policy.

Fourth, low pay is often a result of undervaluing what a worker can do or the skills they have on offer. Young workers are often paid less simply because they are young even if their contribution is the same as older workers. Care workers are often paid very low wages even though they are commonly referred to as “saints” doing a job few want to do. The assumption is that they have few skills worthy of higher pay. These situations are often simply unjust and should not be allowed.

Fourth, low pay is not a good economic strategy. When times are good, low pay leads to high turnover and a weak commitment to training. It also encourages what is known as a “race to the bottom” strategy. In other words, success becomes dependent on who can pay the least to their workers not on quality, productivity, design, marketing, value-add, skill and the other elements of a desirable economy. Certainly for an economy like New Zealand’s it makes no sense at all to try and compete on the basis of low wages. There are too many other economies already in this space who do it so much better.

Of course none of these arguments can tell us exactly what level the minimum wage should be set at. And it is true that if it is set too high jobs may well be placed at risk. So the trick is to be clear about what can be afforded – which is the purpose of the Department of Labour gathering evidence and cautious decisions made by Ministers.

Appropriately set, the evidence suggests that jobs will not be at risk. Indeed, evidence shows that a minimum wage can assist employers to create jobs because a wage floor means that they can focus on growing their business rather than trying to compete by holding costs down.

Appropriately set, the minimum wage will marginalise exploitation while encouraging employers to invest and rely less of the taxpayers to subsidise them.

There is, finally, a sense that the minimum wage provides a clear signal of what it takes to be able to afford to participate fully in our society. At a time when people on low wages are being asked to endure a recession caused by people on very high salaries, a minimum wage makes it clear that the principle of fairness has not been abandoned. It also lets people on high salaries know just how large their pay packets are compared to people at the “bottom of the heap”.

End

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