

28th January 2015

Workplace Relations Inquiry
Productivity Commission
GPO Box 1428
CANBERRA CITY 2601

Submission to the Productivity Commission's Inquiry on Workplace Relations and Penalty Rates of Pay

Dear Sir

I worked as an economist at the Industry Commission between 1985 and 1995 on several enquiries. I also was involved in the Commission's economic analysis of the Hawke/Keating program of tariff reductions. I understood that the Industry Commission was focussed on micro-economic issues such as industry assistance, and I assume that its successor, the Productivity Commission is similarly focussed. I would assume that an issue such as wage levels had a large and important macro-economic component; so I wonder if the Productivity commission (especially if it still has a micro focus) is the right body to undertake an inquiry into this issue.

First of all, what exactly is the government intending when it states it wants to abolish penalty rates? Does it intend simply to reduce overall wages? Or will it compensate workers with an increased flat wage rate? When leave loading was abolished in the public service, we received a pay increase to compensate - this has been the accepted norm when 'one-off' payments such as leave loadings are abolished.

Obviously a reduction in take-home pay will result in an overall reduced level of buying power throughout the economy leading inevitably to a lower level of consumption, and, in the absence of compensatory fiscal stimulation on the part of government, a slowing economy. The government and business leaders are pushing the line that wage costs are preventing them from hiring workers, as it is 'too expensive'. Much anecdotal evidence is offered to support this (a student is desperate for work and who can only work on Sundays but the employer is forced to but can't afford to pay double time.) Employers undertake to employ more staff if wage rates are reduced and this line is a favourite of the government as well. However, employers are unable to quantify the extra staff they intend to hire. And businesses constantly seek to reduce costs, but in order to increase profits, not specifically to employ more staff. Can business guarantee that the money saved will not simply mean greater profits, with no benefit to employment?

Of course, reducing overall wages (if that is what the government intends), will have far reaching social and welfare issues. The government constantly uses for its examples, cafes, restaurants, shops etc. But many of the most important employees in Australia, nurses, child and aged care workers, emergency workers, receive relatively low pay, and depend on penalty rates to 'make ends meet'. On the one hand, it would be unconscionable to reduce the wages of such valued and crucial employees, and, on a more 'practical' level, many such workers, being highly trained, may find their skills transferable to better paying occupations. Hospitals and care facilities already have difficulty attracting and holding staff; a reduction in

their pay will only exacerbate the situation. Overall, if such a policy is implemented, more unskilled employees will be forced into homelessness and poverty, and be more reliant on welfare, (thus increasing welfare costs), and charity organisations, already under stress, will be inundated with claims for assistance. Does the government plan to budget for increased welfare payments and assistance to charities such as Red Cross, St Vincent de Paul and the Salvation Army for the extra demand placed upon them? If so, this represents a direct transfer from the government budget to the benefit of private business.

The demand for labour is a derived demand and wage rates are a small component in employers' decision to hire or to fire. Labour is an input (albeit, usually the most costly one) to the manufacturing process, and the most important driver of employment is consumer demand for the final product (as is the demand for all inputs). In addition, wages are in the unique position (unlike other inputs to production) of being *both* a cost to business and *also* the main source of consumer spending. Both these functions of wages in the economy must be taken into account; to reduce wages as a cost is also to reduce the ability to consume.

During one of the many occasions this issue has been raised, in a televised discussion, they asked a small business owner how it affected him. He said plainly what he considered to be an obvious fact, as indeed it is, that his staffing levels depended entirely on how much business he was doing, and had little or nothing to do with wage rates.

It is a paradox of capitalism that every employer seeks to pay his own staff as little as possible, (to minimise his costs) and at the same time, would like all other employers to pay their staff generously (so they have money to buy his products). Obviously this is an impossible situation. It is a classic case of 'the fallacy of composition'; the man at the back of a footie crowd stands on a box he can see better; but if everyone does this the advantage is lost; if an unemployed person works extra hard to find a job, he'll probably succeed, but this can never be the answer to widespread unemployment when employers aren't hiring.

I would have thought that the aim of any government would be to make Australia a high wage economy. All economies that are considered 'advanced' have high average rates of pay. Indeed, the measure of the wealth of an economy is the average income per head of population. It has always been an accepted strategy in advanced economies, and indeed, is what makes them 'advanced' is that in response to ever increasing wages, employers continually invest in labour saving, increasingly advanced, technologies. Of course, this depends crucially on a universal education system and well-funded scientific research institutions.

Another argument in favour of paying low skilled employees a decent wage is that such employees pay little tax and save virtually nothing; almost all of every extra dollar they earn is spent, their marginal propensity to consume is very high. This means that the multiplier effect of a dollar received by a low paid worker is a much more than for a dollar given to a higher paid worker. Conversely, for any given increase in overall economic activity, it is less costly to the government to raise the income of the lower paid or welfare recipients than it is to raise the incomes of middle class workers. Of course, it works in reverse too; a reduction in the wages of the lower paid has more serious consequences for the economy than a wage cut for other employees.

It seems that the answer to everyone's problem is for there to be an effective central wage fixing body, such as Australia has at present, with its decisions on wages rigorously enforced.

There is much anecdotal evidence of small businesses, especially restaurants, car detailers, manicurists, and suppliers of other personal services, brazenly flouting the minimum wage laws. My son once worked for a car detailer and his boss had never heard of the minimum wage, nor that a recent case had increased it, and was totally unaware of having to pay his staff what they set down. Nor did he.

It must be to the advantage of every business that an independent body such as a minimum wage commission set a standard wage for low paid workers. In exchange for paying his own staff a set wage, every employer gets the advantage of every other worker in the economy receiving a reasonable pay packet; money to spend on the products or services of his business. Far from opposing minimum wage increases, employers should applaud them, accept them and indeed, be at the forefront of steps to police businesses that flout it. A minimum wage commission setting a wage rate acts in the manner of a government sanctioned cartel; if everybody adheres to its rules, everyone benefits, if one flouts the rules, he gains a short term advantage, but if all flout the rules, everybody loses; the fallacy of composition in reverse.

I can summarise these arguments with three statements:

First: it is both unethical and economically irresponsible to reduce rates of pay for the same work. Reducing the overall level of wages also results in a reduction of employees ability to consume, leading to downward pressures on the economy.

Second: the poor and the lower paid are powerful drivers of economic activity. Due to their low rate of tax payments and savings, they have a higher marginal propensity to consume, and hence a higher multiplier effect on the economy. Conversely, a reduction in their income has a greater depressing effect on economic activity.

Third: The path to increased wealth is not to reduce incomes (seen as merely a 'cost' to business), but to reduce costs by continual investment in innovative technology in response to increasing wage levels.

I hope that in your deliberations you will take into account not only the micro economic issues on individual businesses but the implications of a reduced level of wages, and indeed, the resulting reduced general standard of living, for the wider economy. I look forward to your report.

Yours sincerely

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