

In Confidence

Office of the Minister for Workplace Relations and Safety

Chair, Cabinet Economic Development Committee

Minimum Wage Review 2018

Proposal

1. This paper seeks Cabinet agreement to:
 - 1.1. increase the adult minimum wage from \$16.50 to \$17.70 per hour from 1 April 2019;
 - 1.2. increase the starting-out and training minimum wages from \$13.20 to \$14.16 per hour from 1 April 2019 (the Minimum Wage Act 1983 requires that these rates are set at no less than 80 per cent of the adult minimum wage); and
 - 1.3. set indicative rates for the adult minimum wage of \$18.90 per hour for 2020 and \$20 per hour for 2021, subject to confirmation in each year's annual review.

Executive Summary

2. The adult minimum wage is currently \$16.50 per hour, and the starting-out and training minimum wages are currently \$13.20. The adult minimum wage is being paid to approximately 71,500 workers.
3. In light of the Government's commitment to increase the minimum wage to \$20 by 2021, I seek Cabinet's agreement to increase the adult minimum wage to \$17.70 (and the starting-out and training minimum wages to \$14.16) from 1 April 2019, because:
 - 3.1. \$17.70 represents an even approach to increasing the minimum wage to \$20 by 2021 and provides the best foundation to meet the Government's commitment;
 - 3.2. up to 209,200 workers will receive an increase to the new minimum wage;
 - 3.3. no increase or a small increase would erode the real incomes of the lowest paid workers compared to wage growth and inflation;
 - 3.4. it will have a moderate restraint of 8,000 fewer individuals in employment than there would have been if the minimum wage had not increased. This compares to forecast employment growth of 56,900 in 2019;
 - 3.5. the unemployment rate has fallen significantly within the context of the 1 April 2018 increase to the minimum wage of 75 cents and wide publication of the increase to \$20 by 2021.

4. Many employers and workers that the Ministry of Business, Innovation and Employment (MBIE) engaged with raised the importance of certainty about the pathway to raise the minimum wage to \$20 by 2021. To provide greater certainty to employers and workers, I seek Cabinet's agreement to publish indicative rates for the adult minimum wage for 2020 and 2021, subject to confirmation in each year's annual review. I recommend that the indicative rate for the adult minimum wage is \$18.90 for 2020 and \$20 for 2021, in line with the even approach to achieving the Government's commitment.

Background

5. The adult minimum wage is currently \$16.50, and the starting-out and training minimum wages are currently \$13.20. As Minister for Workplace Relations and Safety, I have a statutory obligation to review the minimum wage by 31 December 2018 each year under section 5 of the Minimum Wage Act 1983 (the Act).
6. In line with recent reviews, the review considered the following factors in the analysis of options for the minimum wage:
 - 6.1. inflation, using the Consumer Price Index as the indicator;
 - 6.2. wage growth, using median wage as the indicator;
 - 6.3. restraint on employment; and
 - 6.4. other relevant factors, such as the impact on sectors, including the state sector.
7. For the 2018 review, the Government's coalition agreement to increase the minimum wage to \$20 by 2021 is a key focus, in addition to the following factors which I directed be considered in the review:
 - 7.1. living costs and financial needs of workers and their families;
 - 7.2. the actual incomes of workers and households after tax and social transfers;
 - 7.3. relativity of the minimum wage to welfare benefits and the average and median wages;
 - 7.4. distributional impacts of any minimum wage change;
 - 7.5. the impact of any minimum wage change on poverty;
 - 7.6. the Government's goals for the economy; and
 - 7.7. the impacts on different types of employers, including small, medium and large businesses, export and import-reliant businesses, and other employers such as charities.
8. The minimum wage normally increases every year after the completion of the annual review. The following table shows the annual changes to the minimum wage and compares it with the annual increase in the median wage.

Date of new minimum wage	Adult minimum wage	% change	Median wage (June each year)	% change	Minimum wage as % of the median wage
April 2007	\$11.25	9.8%	\$18.00	5.9%	63%
April 2008	\$12.00	6.7%	\$18.56	3.1%	65%
April 2009	\$12.50	4.2%	\$19.51	5.1%	64%
April 2010	\$12.75	2.0%	\$19.95	2.3%	64%
April 2011	\$13.00	2.0%	\$20.02	0.4%	65%
April 2012	\$13.50	3.8%	\$20.78	3.8%	65%
April 2013	\$13.75	1.9%	\$21.48	3.4%	64%
April 2014	\$14.25	3.6%	\$21.92	2.0%	65%
April 2015	\$14.75	3.5%	\$22.68	3.5%	65%
April 2016	\$15.25	3.4%	\$23.22	2.4%	66%
April 2017	\$15.75	3.3%	\$24.00	3.4%	66%
April 2018	\$16.50	4.8%	\$25.00	2.9%	66%
April 2019	\$17.70	7.3%			

Setting the minimum wage to \$17.70 on 1 April 2019

9. In general, minimum wage increases can have the following impacts:
- 9.1. *Increased earnings for minimum wage workers*, although net household income is also affected by other government interventions, such as taxation and abatements for those receiving income support and tax credits.
 - 9.2. *Increased labour costs for employers*, especially for sectors that employ a large number of minimum wage workers such as hospitality and retail which employ 22,800 and 17,900 minimum wage workers respectively, as well as flow-on costs from increasing the wages of other workers earning close to the minimum wage to maintain their wage relativity to the minimum wage.
 - 9.3. *Inflation pressure* if employers pass on all or part of their increased labour costs through increased prices.
 - 9.4. *Employment impacts*, including lower job growth and reduced hours. The extent of these effects will depend on the size of the wage increase and the economic and labour market context in which it occurs. Evidence indicates that under certain conditions minimum wage increases may have negligible or marginally positive employment effects for some groups. Employment effects are most likely to impact some demographic groups such as youth, Māori and women.
 - 9.5. *Changed fiscal costs for government* through both direct wage costs (employees paid at or near the minimum wage) and indirect costs due to government expenditure on programmes that are affected by the minimum wage. Further discussion is included under the Financial Implications section.

10. MBIE has assessed a number of minimum wage options to analyse the impact of the different increases. A summary of this assessment is in Annex 1.
11. I have considered MBIE's analysis of the options and seek Cabinet's agreement to increase the adult minimum wage to \$17.70, and the starting-out and training wages to \$14.16 (the Act requires that these rates are set at no less 80 per cent of the adult minimum wage). MBIE's analysis shows that an increase to \$17.70 is preferred because:
 - 11.1. it represents an even approach to increasing the minimum wage to \$20 by 2021 and provides the best foundation to meet the Government's commitment. Front- and back-loaded approaches involve larger increases in some years and are associated with greater risks and levels of uncertainty;
 - 11.2. up to 209,200 workers will receive an increase to the new minimum wage. Many of those earning above the new minimum wage can also expect an increase over time as relative wages between different roles are addressed, and new entrants to employment can expect to start employment at a higher wage than if this increased did not occur. This represents an increase in hourly wages and overall income for many workers;
 - 11.3. no increase or a small increase would erode the real incomes of the lowest paid workers compared to wage growth and inflation;
 - 11.4. \$17.70 restrains employment less than higher increases. MBIE estimates that 8,000 fewer individuals (low estimates indicate this number could be 5,000, while high estimates suggest a figure of 9,000) would be in employment than there would have been if the minimum wage had not increased. This compares to forecast employment growth of 56,900 in 2019; and
 - 11.5. the unemployment rate has fallen significantly and the labour market has tightened. The unemployment rate is the lowest it has been since June 2008. This tightening labour market has occurred since the 1 April 2018 increase to the minimum wage of 75 cents, and while the increase to \$20 by 2021 has been widely publicised.

MBIE's minimum wage model has been updated

12. Following recent analysis, the model MBIE uses to predict the impacts of minimum wage increases has been updated. More specifically:
 - 12.1. the elasticities used in the model to estimate the impact of minimum wage changes on employment have been updated
 - 12.2. the new model uses improved calculations and more recent employment data
 - 12.3. some technical issues with the earlier model have been addressed.
13. When compared to the earlier model, the updated model produces different estimated employment effects, at both an aggregate and subgroup level. For example, the earlier model, if used for this year's review, would predict an employment impact of -5,500 for an increase to \$17.70, compared to the updated model's prediction of -8,000. These differences are the result of the changes listed above, as well as the group of employees

considered. The earlier model primarily focused on the groups most at risk of employment impacts (16-17 year olds, 18-19 year olds, females, Māori and Pacific peoples), whereas the updated model considers all employees aged between 16 and 64.¹

14. The minimum wage review presents the updated model's results. However, for transparency, the results of the previous model are also included so that a comparison can be made with the modelling and results of previous minimum wage reviews.

Future increases to the minimum wage

15. An issue raised almost universally during MBIE's consultation with employers and workers was a desire for certainty regarding the commitment to raise the minimum wage to \$20 by 2021. There is strong support for government publishing either indicative or actual minimum wage increases in advance until the \$20 goal is reached.
16. I seek Cabinet's agreement to publish indicative rates for the adult minimum wage for 2020 and 2021, subject to confirmation in each year's annual review. This will provide greater certainty for employers, so that they can build reserves, plan for upcoming labour cost increases, and more accurately set prices for future goods and services (important in the tourism and exporting sectors). For workers, indicative rates can provide greater certainty in terms of future income. In addition, both employers and workers felt it would be useful in allowing collective bargaining to proceed in an informed manner, rather than parties trying to predict what the minimum wage could be in the future years covered by an agreement.
17. The statutory obligation to review the minimum wage each year by 31 December will remain, but the 2019 and 2020 reviews could be streamlined to primarily consider whether the indicative rate is appropriate when considering the current economic context. This approach provides greater certainty for employers and workers, but allows room to amend the indicative rate if needed. For example, the indicative rates could be amended if there is a significant change in the economic outlook, projected employment levels, or evidence that a previous minimum wage increase had different than expected impacts on some groups or sectors.
18. I recommend that the indicative rate for the adult minimum wage is \$18.90 for 2020 and \$20 for 2021, in line with the even approach to achieving the Government's commitment.

Year	Minimum wage	Increase
2019	\$17.70 (+\$1.20)	7.27%
2020	\$18.90 (+\$1.20)	6.78%
2021	\$20 (+\$1.10)	5.82%

Consultation

19. Consultation was undertaken with BusinessNZ and the New Zealand Council of Trade Unions, as has been the case in recent reviews of the minimum wage. MBIE also consulted with more employer and worker representatives for the 2018 review. Although

¹ The updated model has three iterations for predicting employment impacts ('groups most affected', '16-64 year olds', 'minimum wage bite'), which provide a range of estimates. In order to provide an actual figure within this range, the '16-64 year olds' figure is used, as MBIE judges it to be the best estimate of the impacts.

there were different views on how the Government could best reach its commitment, the majority of stakeholders were comfortable with an approach that spread the increases evenly over the next three years.

20. The Treasury, State Service Commission, Accident Compensation Corporation, Department of Prime Minister and Cabinet (Child Poverty Unit and Policy Advisory Group), the Reserve Bank of New Zealand, Te Puni Kōkiri, Inland Revenue, Oranga Tamariki, the Ministries of Health, Education, Social Development and Justice, and the Ministries for Pacific People and Women have been consulted in this review.

20.1. The Ministry of Education advises that increasing the adult minimum wage rate to \$17.70 will impact a number of employees in the education sector, particularly those in non-teaching roles whose salary costs are met from Boards of Trustees operational funding or other Board-raised funds. This will create a cost pressure for impacted Boards, and without increased funding, there is a risk that Boards will manage the cost pressure by reducing employees' hours of work which is likely to impact services provided to students.

Financial Implications

21. The Ministries of Education, Health and Social Development, Oranga Tamariki and Accident Compensation Corporation have provided an estimate of how their costs would be affected by an increase to the minimum wage. For these agencies, total annual costs directly related to the proposed minimum wage increase to \$17.70 per hour are estimated to be approximately \$93.1 million per year. A large proportion of the increased total annual cost will be borne by the health sector [REDACTED]

Withheld consistent with the Official Information Act 1982

22. As well as affecting wage costs, there may be other fiscal impacts. For example, social assistance costs through benefit payments may rise if an increase in the minimum wage results in a higher level of unemployment. However, it is also likely that the fiscal costs to government could be largely offset by an increase in the goods and services tax received due to more people having disposable income, and a reduction in the amount of social transfers due to abatements on government support. However, given the amount of variables and behavioural assumptions involved, these impacts cannot be accurately assessed and quantified.
23. Furthermore, some other government programmes are adjusted based on labour market wage statistics (for example, parental leave payment rates are adjusted annually based on changes in average ordinary time hourly earnings). The large changes to the minimum wage proposed over the next three years may have an impact on these programmes.

Legislative Implications

24. Minimum wages are set through an Order in Council made under section 4, 4A and 4B of the Act. To give effect to a change of the minimum wage, a new Order in Council needs to be made by the Governor-General, on the recommendation of the Minister for Workplace Relations and Safety. The new order to increase the minimum wage to \$17.70 will come into force on 1 April 2019.

25. I intend to bring a paper to the Cabinet Legislation Committee in early 2019 to give effect to the minimum wage increase agreed by Cabinet.

Impact Analysis

26. The Regulatory Impact Analysis requirements apply to the proposal in this paper and a Regulatory Impact Statement (RIS) has been prepared and is attached.
27. A joint Quality Assurance Panel with representatives from the MBIE and the Treasury reviewed the Regulatory Impact Assessment (RIA) "Increasing the Minimum Wage" prepared by the MBIE and considers that the information and analysis summarised in the RIA meets the Quality Assurance criteria.
28. The reviewers commented: "The RIA is clear and concise. The impacts of the proposed change and key constraints on the analysis are well set out. The proposal has been well consulted. We note that the analysis supports an increase in the minimum wage to \$17.70, as a foundation to meet the Government's commitment to an increase to \$20 by 2021. The impacts of the proposed change in this RIA will need to be closely monitored to feed into the future reviews".

Human Rights

29. I recommend that the starting-out and training minimum wages continue to be set at 80 per cent of the adult minimum wage. As these minimum wages make a distinction on the basis of age, namely those aged 16 to 19 years, or their employment status, it continues to raise an issue of discrimination under section 19(1) of the New Zealand Bill of Rights Act 1990 (BORA).
30. However, this discrimination appears to be justified in terms of section 5 of the BORA. There can be negative long-term economic and social effects associated with young people being out of work, especially if they remain unemployed for a significant period of time. Providing the ability to pay young, unskilled, and in-training workers a lower wage than the adult minimum wage is one way to get young people into work and work-based training. This encourages employers to take a chance on a young person, and provide opportunities for 16 to 19 year olds to engage in training in their chosen occupation. Young people can earn money, gain skills and get work experience. It mitigates some effects of long-term unemployment by assisting young people into work before they move into a cycle of welfare dependency.

Gender Implications

31. Women tend to be overrepresented in a number of demographic characteristics associated with the minimum wage, including working part-time and working in the hospitality and retail sectors. MBIE estimates that 60 per cent of minimum wage earners aged 16-64 are women, compared to 50 per cent of all wage earners. A minimum wage increase to \$17.70 is likely to reduce the proportion of women that are minimum wage earners.²

² MBIE's modelling estimates that 60% of minimum wage earners are women, but this would reduce to 58% with increasing the minimum wage to \$17.70.

Publicity

32. I intend to make a media statement about the decision on the minimum wage for 2019 following Cabinet decisions. I also intend to communicate the Government's indicative rates for the minimum wage for 2020 and 2021, following the approach set out in paragraph 18.

Proactive Release

33. I intend to proactively release this Cabinet paper, the RIS, and relevant briefings on the MBIE website, subject to any appropriate withholding of information that would be justified under the Official Information Act 1982.

Recommendations

34. The Minister for Workplace Relations and Safety recommends that the Cabinet Economic Development Committee:
1. **note** that the Ministry of Business, Innovation and Employment had the Government's coalition agreement to increase the minimum wage to \$20 by 2021 as a key focus in this year's annual review
 2. **agree** that the adult minimum wage be increased from \$16.50 per hour to \$17.70 per hour from 1 April 2019
 3. **agree** to maintain the starting-out and training minimum wages at 80 per cent of the adult minimum wage, which will mean that these each increase to \$14.16 per hour from 1 April 2019
 4. **invite** the Minister for Workplace Relations and Safety to issue drafting instructions to the Parliamentary Counsel Office to give effect to these recommendations through an Order in Council
 5. **agree** to publish indicative rates for the adult minimum wage for 2020 and 2021, subject to confirmation in each year's annual review
 6. **agree** for the indicative rates for the adult minimum wage to be \$18.90 for 2020 and \$20 for 2021, in line with the Government's coalition agreement
 7. **note** that these change to the minimum wages and the indicative rates will be announced before the end of 2018

Authorised for lodgement

Hon Iain Lees-Galloway

Minister for Workplace Relations and Safety

Annex 1: Summary of impacts of minimum wage options

Minimum wage rate impact measures	Option 1	Option 2	Option 3	Option 4	Option 5	Option 6	Option 7
Adult minimum wage (hourly rate)	\$16.50	\$17.00	\$17.50	\$17.70	\$18.00	\$18.50	\$20.55
Adult minimum wage (gross weekly income) ³	\$660	\$680	\$700	\$708	\$720	\$740	\$822
Percentage increase	N/C	3.03%	6.06%	7.27%	9.09%	12.12%	24.55%
Relativity to median wage ⁴	66%	68%	70%	70.8%	72%	74%	82.2%
Relativity to Job Seeker support ⁵	274.3%	282.6%	290.9%	294.2%	299.3%	307.6%	341.6%
Number of people directly impacted (rounded up to nearest 100)	71,500	106,500	177,500	209,200	225,600	294,300	525,300
Estimated restraint on employment ⁶	N/C	-500	-6,000	-8,000	-11,500	-17,000	-39,000
Estimated economy-wide increase in wages (\$m, annual)	N/C	57	171	231	330	551	1,956
Estimated inflationary impact/GDP (percentage points)	N/C	N/C	N/C	0.1%	0.1%	0.1%	0.5%
Additional annual costs to the government (\$m) ⁷	N/C	\$30.6	\$74.9	\$93.1	\$160	\$357	\$1,174

³ This is calculated on a 40 hour week basis.

⁴ The median hourly earnings are \$25.00 per hour (Labour Market Statistics (Income), June 2018).

⁵ For a single adult, aged 25 or over, receiving \$240.60 (gross) per week.

⁶ The employment effects for '16-64 year olds' are represented.

⁷ This is a high level estimate based on the additional costs to the Ministries of Health, Social Development and Education, Oranga Tamariki and Accident Compensation Corporation. It does not include potential transfer savings.