Coversheet: Increasing the minimum wage

Advising agencies	*Ministry of Business, Innovation and Employment*
Decision sought	*Increasing the Minimum Wage*
Proposing Ministers	*Minister for Workplace Relations and Safety*

Summary: Problem and Proposed Approach

Problem Definition **What problem or opportunity does this proposal seek to address? Why is Government intervention required?**
This proposal seeks to increase the adult minimum wage to $17.70 from 1 April 2019 in order to make progress on the Coalition Agreement commitment to increase the minimum wage to $20 by 1 April 2021.

Proposed Approach **How will Government intervention work to bring about the desired change? How is this the best option?**
Increasing the minimum wage to $17.70 represents a steady, predictable and lower risk 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, which include larger increases in some years, are associated with greater risks and levels of uncertainty.

Section B: Summary Impacts: Benefits and costs

Who are the main expected beneficiaries and what is the nature of the expected benefit?
Up to 209,200 workers (those currently earning up to $17.70) will receive an increase up to the new minimum wage. Many of those earning above the new minimum wage can also expect an increase over time as relative wage rates between different roles are addressed, and new entrants to employment can expect to start employment at a higher wage rate than if this increase did not occur. This represents an increase in hourly wages and overall income for many workers. The minimum wage provides a wage floor for workers, to ensure that they receive an adequate wage for their employment. One of the Government's objectives is to lift the wages of low-paid workers, and increasing the minimum wage is one part of this policy objective. Increasing the overall income for low wage earners may result in more people having disposable income, which could then lead to an increase in consumption levels. This could have some benefits for domestic businesses.

Minimum wage increases may also have a small impact on poverty rates, particularly for households without children. This is because these households are more likely to be on the lowest wages and receive less government-provided income support to supplement their income.

Where do the costs fall?
The costs of any minimum wage increase fall initially to employers who will experience an economy-wide labour cost increase (of approximately $231 million in this case). The increased cost of labour may then be passed on to customers through rising prices of goods and services, as employers seek to maintain a profit. However, for many businesses and sectors, workers on the minimum wage represent a small fraction of total labour costs so will not significantly impact overall operation costs. Increasing the minimum wage is expected to create some inflationary pressure, and MBIE's minimum wage model suggests a small impact (0.1%). Increasing the adult minimum wage to $17.70 is expected to have an annual fiscal cost of $93.1 million to government. Although increases to the minimum wage are predicted to increase costs for government, it is likely that they would also impact on the tax and transfers system and other social policy programmes.

What are the likely risks and unintended impacts, how significant are they and how will they be minimised or mitigated?
Any increase to the minimum wage has the potential to affect employment levels as the rising cost of labour may mean that employers choose to substitute labour for capital, or for higher-wage/higher-skill labour. MBIE's model predicts a possible negative employment effect (disemployment) of 8,000 (low estimate of 5,000 and a high estimate of 9,000), compared to forecast employment growth of 56,900 in 2019[1]. Evidence indicates that minimum wage increases are more likely to impact certain demographic groups, such as young people, Māori, and low-skilled workers. Increasing the minimum wage may also have a 'ripple effect' due to wages above the minimum wage also increasing faster than expected income growth. This has the potential to have a larger impact on employment, and the economy-wide wage bill. The extent to which this might occur is not possible to quantify.

Identify any significant incompatibility with the Government's 'Expectations for the design of regulatory systems'.
None.

Section C: Evidence certainty and quality assurance

Agency rating of evidence certainty?
The minimum wage model used by MBIE has a relatively high level of confidence. It was reviewed and updated in 2018 to better predict the impact of minimum wage changes, particularly the impact on employment. More specifically, the elasticities used in the model to estimate the impact of minimum wage changes on employment have been updated.

[1] This indicates that employment impacts may be partially absorbed by wider employment growth. However, the two figures are not directly comparable as the time periods they cover are not fully aligned.

The new model uses improved calculations and more recent employment data, as well as addressing some technical issues with the earlier model. The model does not provide estimates on the flow-on economic impacts. Due to a lack of adequate data, MBIE is only able to estimate the direct impacts of minimum wage changes. The model is also based on a number of assumptions about how a single change to the minimum wage will impact the labour market and wider economy. The impacts of a series of successive minimum wage changes are not captured in MBIE's minimum wage model, or the review. This is largely because there is little international or domestic evidence of the impact of these types of successive increases signalled well ahead and across multiples years. MBIE's model predicts the impact of a single change as a one-off event, which is consistent with the Minimum Wage Act and the requirement that the minimum wage is reviewed annually. International evidence of the impacts of minimum wage changes – particularly any impacts on employment – is by its nature context-specific and based on local labour market and economic conditions at that time. As such, there is always some uncertainty in predictions and how a specific minimum wage change will impact the New Zealand economy. This uncertainty increases as the size of the minimum wage change being modelled increases. Most historic minimum wage changes, both domestically and internationally, are relatively modest (eg most increases are lower than 5%). Therefore, modelling of larger increases is inherently more uncertain.

To be completed by quality assurers:

Quality Assurance Reviewing Agency:
The Treasury and Ministry for Business, Innovation and Employment
Quality Assurance Assessment:
A joint Quality Assurance Panel with representatives from the Ministry of Business, Innovation and Employment and the Treasury have reviewed the Regulatory Impact Assessment (RIA) "Increasing the Minimum Wage" prepared by the Ministry of Business, Innovation and Employment and considers that the information and analysis summarised in the RIA meets the Quality Assurance criteria.
Reviewer Comments and Recommendations:
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.

Impact Statement: Increasing the minimum wage

Section 1: General information

Purpose
The Ministry of Business, Innovation and Employment is solely responsible for the analysis and advice set out in this Regulatory Impact Statement, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing final decisions to raise the minimum wage to $17.70 to be taken by or on behalf of Cabinet.
Key Limitations or Constraints on Analysis
• This year's review occurs within the context of the Coalition Agreement commitment between the New Zealand Labour Party and New Zealand First Party to 'progressively increase the Minimum Wage to $20 per hour by 2020, with the final increase to take effect in April 2021'. • MBIE is only able to estimate the direct impacts of minimum wage changes. We do not have adequate data to assess any flow-on effects of any increase in the minimum wage rate. While MBIE's model provides estimates based on publically available figures from Stats NZ, the direct impacts or the degree of those impacts of changes to the minimum wage are difficult to assess. • The extent to which the minimum wage has an employment effect, particularly for larger increases, is heavily debated in economic literature. There is no clear consensus, and the results of empirical studies are subject to economic and labour market contexts. • The economic literature indicates that minimum wage increases can result in fewer hours worked for some employees. MBIE's minimum wage model is not able to provide estimates on the impact of hours worked for employees at an aggregate level. • There is little evidence of the specific uptake of the starting-out wage and training minimum wage, but the evidence that does exist suggests that relatively few workers are paid the training wage, while some young people are paid the starting-out wage. Recent survey data suggest that 5 per cent of employers use the starting-out wage, and less than one per cent of employers use the training minimum wage. These figures are unlikely to accurately represent the number of employees that are paid less than $16.50 (in 2018) using these other minimum wages. For example, some of the employers using the training minimum wage are likely to be industry training organisations and have many employees earning the training minimum wage.
Responsible Manager (signature and date):

Gerard Clark Employment Standards Policy Labour and Immigration Policy Ministry of Business, Innovation and Employment

Section 2: Problem definition and objectives

2.1 What is the context within which action is proposed?

The Minimum Wage Act 1983 sets the hourly minimum wage rates, and requires the responsible Minister to review the rates by 31 December each year. The responsible Minister is the Minister for Workplace Relations and Safety.

There are currently three minimum wage rates:

- the adult minimum wage rate at $16.50 per hour
- the starting-out minimum wage rate at $13.20 per hour
- the training minimum wage rate at $13.20 per hour

The adult minimum wage is paid to an estimated 71,500 employees. Some sectors and demographics are more likely than others to be paid the minimum wage. The table below provides a summary of who is paid the minimum wage currently (at $16.50) based on MBIE's modelled data and survey data from the Labour Market Statistics (Income – June 2018).

Table 1: Demographics of workers paid $16.50 per hour

Demographic	% of minimum wage earners			% of total wage earners
	16-24 year olds	25-64 year olds	16-64 year olds	16-64 year olds
Aged 16-24 years	100%	0%	61%	17%
Female	56%	67%	60%	50%
European/Pakeha	59%	42%	52%	62%
Māori	17%	17%	17%	14%
Pacific	4%	6%	5%	6%
Part-time	72%	46%	62%	18%
Studying	36%	9%	26%	12%
Total	**43,900**	**27,600**	**71,500**	**2,044,000**

Table 1 shows that workers aged 16 to 24 make up 61% of minimum wage earners (this same demographic make up 17% of all wage earners). Table 1 shows that young people, Māori and women are disproportionately paid the minimum wage than other groups.

This year's review takes place in an economic climate marked by positive growth. Gross Domestic Product (GDP) growth in June 2018 was 2.8 per cent and this level of growth is expected to persist in the near term averaging 3 per cent over the next five years. Although increasing uncertainty (trade tensions, low business confidence and low consumer spending) present risk to the economy, the labour market has been tightening. In Stats NZ's Labour Market Statistics September 2018, the unemployment rate fell to 3.9 per cent, the lowest since June 2008 (when it was 3.8 per cent). Employment increased by 2.8 per cent to 2,663,000. This is a positive sign for the labour market as the number of new jobs in the market is larger than the number of people entering the labour market.

2.2 What regulatory system, or systems, are already in place?

The minimum wage sets a price floor for all employees, below which employers are not allowed to set or pay wages.

This assists employees that do not have the bargaining power to negotiate wage increases, ensures that workers are paid an appropriate wage in compensation for their time working, and prevents businesses from 'undercutting' their competition by paying less for their labour. Reviewing the minimum wage is one way to ensure that it maintains relativity to inflation and/or wage growth, so that minimum wage workers' real earnings are not eroded over time if they continue to earn the minimum wage.

The Minister responsible for the minimum wage (the Minister for Workplace Relations and Safety) is required to review the minimum wage each year by 31 December, although the criteria for the review are not specified in legislation.

2.3 What is the policy problem or opportunity?

It is the government's priority to improve the well-being and living standards of all New Zealanders through productive, sustainable and inclusive economic growth. To help achieve this goal, the Government has committed to increasing the minimum wage to $20 per hour by 2021.

There are strong rationales for having a minimum wage, and for making changes to it. These include protecting real incomes for minimum wage earners (for example, using CPI as an indicator), maintaining relativity to median or average earnings, and lifting the incomes of low-income households. In addition, some employees do not have the bargaining power or capability to negotiate wage increases that reflect the value of their work. These workers would likely receive no annual increase, or an increase lower than inflation, in the absence of an annually reviewed minimum wage. This would mean that workers would receive lower pay over time for the same work, and may increase income inequality.

MBIE's analysis for this proposal does not include examining the underlying rationale of the minimum wage, but the minimum wage is a well-established and accepted feature of New Zealand employment law.

Employers and employees have expectations of the minimum wage increasing in light of the Government's commitment to increase the minimum wage to $20 by 2021. The proposal to increase the minimum wage to $17.70, which is approximately a third of the way to $20, provides the best foundation to meet the Government's commitment. Front- and back-loaded approaches, which include larger increases in some years, are associated with higher risks and levels of uncertainty.

2.4 Are there any constraints on the scope for decision making?

This year's review occurs within the context of the Coalition Agreement commitment between the New Zealand Labour Party and New Zealand First Party to 'progressively increase the Minimum Wage to $20 per hour by 2020, with the final increase to take effect in April 2021'. The purpose of this impact statement is to provide an assessment and analysis of options to progress towards this objective, as well as contextualising any impacts with comparisons to other minimum wage rates.

2.5 What do stakeholders think?
Consultation was carried out with BusinessNZ and the New Zealand Council of Trade Unions (NZCTU). BusinessNZ suggests the minimum wage should be set as a percentage of the median wage, with the percentage determined by a review, and limited by inflation as measured by CPI. The NZCTU proposed an increase to $20.99 (preferred step for 1 April 2019), $18.26 (suggested alternative step for 1 April 2019) or $17.75 (suggested approach to the $20 target). MBIE also consulted with other employer and worker representatives. Although there were different views on how Government could best reach its commitment to set the rate at $20 by 2021, the majority of stakeholders expected an approach that spread the increases evenly (rather than a small increase this year followed by progressively larger increases the following two years, or a large increase this year followed by progressively smaller increases the following two years) and are comfortable that if the Government is to meet its commitment, then an even spread over the years is an acceptable way to meet it. Employers and employees reported more interest in having the pathway to reach the $20 rate by 2021 signalled clearly by the Government, than which pathway was followed. Many employers stated that businesses (eg tour operators, hoteliers) often need to set prices well in advance and knowledge of future minimum wage increases, particularly when they are larger than usual, is crucial to ensuring these prices are set appropriately. It also allows businesses to build up reserves, ensure they can manage increased labour costs and better plan when making any adjustments to address gender wage disparities. For employees, the increased certainty in minimum wage increases is anticipated to also provide greater certainty for low wage earners in terms of future income. Both groups 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. A number of agencies were also consulted to gain information about their estimated costs for increases to the minimum wage. The agencies that provided detailed costs information were the Ministries of Health, Social Development, and Education, Oranga Tamariki and Accident Compensation Corporation. Their costs are included in MBIE's assessment of minimum wage options. The Treasury, Accident Compensation Corporation, Department of the Prime Minister and Cabinet (Policy Advisory Group and Child Poverty Unit), Inland Revenue, Ministry of Justice, Ministry for Pacific Peoples, Ministry for Women, Te Puni Kōkiri, the Reserve Bank of New Zealand and the State Services Commission have also been consulted in this review.

Section 3: Options identification

3.1 What options are available to address the problem?

A range of options were developed to analyse and model the impacts of increasing the minimum wage. MBIE's model can assess the impact of 5 cent increases to the minimum wage. However, to focus consultation and analysis of options, only some have been selected for consideration:

- $16.50 (status quo)
- $17.00
- $17.50
- $17.70 (approximately a third of the way to $20)
- $18.00
- $18.50
- $20.55 (proposed by Living Wage Aotearoa as a 'living wage')

Setting the starting-out wage and training minimum wage
The Minimum Wage Order 2019, which will set the adult minimum wage, will also set the starting-out wage and training minimum wage. These wage rates are available to some workers who meet appropriate criteria.

The *Minimum Wage Act 1983* requires these other minimum wages to be no less than 80 per cent of the adult minimum wage, which means that they would be set at $14.16 per hour. MBIE has not considered other options for the starting-out wage and training minimum wage because:

- a differential between these rates and the adult minimum wage rates supports the transition of youth into employment
- employers expect these minimum wages to be 80 per cent of the adult minimum wage
- maintaining the training minimum wage rate at 80 per cent of the adult minimum wage is necessary to achieve the policy objective of incentivising employers to take on and support trainees. Legislation does not allow a rate lower than 80 per cent and anything substantially higher than 80 per cent would create a lowered incentive for employers to take on trainees
- it is important that the starting-out and training minimum wages are the same, as they are used interchangeably in some cases.

3.2 What criteria, in addition to monetary costs and benefits, have been used to assess the likely impacts of the options under consideration?

The criteria used to assess the impacts of the proposed minimum wage are consistent with MBIE's assessments in previous reviews of the minimum wage. The criteria here include those prescribed by Cabinet in 2012 (CAB Min (12) 41/5B) and other additional factors, and are used here to indicate likely impacts or trade-offs, rather than for directly comparing options. An overview of MBIE's analysis of each criterion is provided in the following section.

The criteria used in the minimum wage review include:

- relativity to median and average wages
- number impacted
- restraint on employment
- economy-wide wage increase

- inflationary impact
- costs to government
- increasing the minimum wage to $20 by 2021
- impact on workers
- impact on employers
- impact on poverty

3.3 What other options have been ruled out of scope, or not considered, and why?

Options greater than $20.55 have not be considered. This is because the Government's commitment is to reach $20 by 2021 and increases larger than $20.55 are unlikely to be adopted due to the significant employment and inflation impacts.

Options less than the status quo have not been considered as it is not general practice for the review to result in a reduction in the minimum wage.

Section 4: Impact Analysis

Marginal impact: How does each of the options identified at section 3.1 compare with the counterfactual, under each of the criteria set out in section 3.2?

Table 2: 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)[2]	$660	$680	$700	**$708**	$720	$740	$822
Percentage increase	N/C	3.03%	6.06%	**7.27%**	9.09%	12.12%	24.55%
Relativity to median wage[3]	66%	68%	70%	**70.8%**	72%	74%	82.2%
Relativity to Job Seeker support[4]	274.3%	282.6%	290.9%	**294.2%**	299.3%	307.6%	341.6%
Number of people directly impacted (rounded up to nearest 100)	71,500	106,500	177,500	**209,200**	225,600	294,300	525,300
Estimated restraint on employment[5]	N/C	-500	-6,000	**-8,000**	-11,500	-17,000	-39,000
Estimated economy-wide increase in wages ($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)[6]	N/C	$30.6	$74.9	**$93.1**	$160	$357	$1,174

2 This is calculated on a 40 hour week basis.

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

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

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

6 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.

Analysis of criteria and objectives
This section outlines MBIE’s assessment of how the Government’s preferred option of $17.70 per hour meets each of the criteria described in section 3.2. MBIE has modelled all of the options to show the impact of each option against the criteria. However, due to the coalition agreement to increase the minimum wage to $20 by 2021, the other options have not been core to our analysis and so MBIE has focused on the option of $17.70. **Relativity to median and average wages** MBIE has assessed the relativity of minimum wage options to both median and average wages. The median wage is currently $25.00 per hour (New Zealand Income Survey, June 2018) and the average wage is $31.34 per hour (Labour Market Statistics, September 2018). If these same rates were used to assess an increase to $17.70 on 1 April 2019, the proposed minimum wage would lift relativity from 66 per cent to 70.8 per cent of the median wage and from 52.6 per cent to 56.5 per cent of the average wage – which would be an historic high. However, the exact relativity of the minimum wage to the median and average wages could change by the time a new minimum wage is introduced on 1 April 2019. **Number impacted** MBIE’s model estimates the number of people who are likely to be paid each option for the minimum wage. The number impacted provides an estimate of the number of employees which will receive a pay increase, and is also related to employment impacts. A minimum wage of $17.70 will apply to an estimated 209,200 workers – many of whom will receive an increased wage as they are paid between the current minimum wage of $16.50 and the proposed minimum wage of $17.70. The number of predicted impacted workers is larger than in previous years (164,100 in 2017, 119,500 in 2016). **Restraint on employment** MBIE’s model makes an estimate for the impact on employment due to the increased minimum wage (the number of individuals not in employment than would have been if the minimum wage had not increased). This is based on historic elasticities for various groups of minimum wage earners. Restraint on employment can be due to labour-capital substitution (where employers swap low-wage labour for capital investment), or labour-labour substitution (where employers hire higher-wage workers due to better return on the cost of labour), or through marginal firms exiting the market because of higher costs. Restraint on employment is a mandated criterion. The estimated restraint on employment for a minimum wage of $17.70 is 8,000 (low estimate of 5,000 and high estimate of 9,000), compared to forecast employment growth of 56,900 in 2019. MBIE judges the 8,000 figure to be the best predictor of employment factors, when considering all iterations of the model and the international literature. This is a net figure, and includes both positive and negative effects for different groups. MBIE’s approach to the minimum wage in previous years has been to recommend options based on minimising negative employment effects as much as possible. The unemployment rate has fallen significantly and the labour market has been tightening. The unemployment rate is the lowest it has been since June 2008, when it was 3.8 per cent.

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. Given recent and forecast job growth, MBIE expects that the possible employment effect of the Government's preferred wage will be at least partially absorbed.

Economy-wide wage increase
MBIE's model provides an estimate of the total increased cost of labour across the entire economy. It does not include any ripple effect for workers whose wages above the minimum wage are increased for reasons of relativity, as these are due to individual decisions made by employers. Wage growth is a mandated criterion.

The estimated economy-wide impact of $231m is greater than previous years' estimates for the option that was chosen ($129m in 2017, $65m in 2016, and $75m in 2015). This is in line with the fact that a large number of people are expected to be affected by the new minimum wage.

While this raises the concern of wage compression at the bottom of the wage scale, previous reviews have not shown this to occur in a significant way. In general, the number of people estimated to be earning a new minimum wage is higher than the actual number earning the minimum wage by the time of the next year's review. For example, in the 2017 review, 164,100 people were expected to be earning the new minimum wage of $16.50. This year's model, however, estimated only 71,500 people are actually earning $16.50. This is not because the model is incorrect, but because the structure of the labour market changes between each review of the minimum wage, and is captured in the June Labour Market Statistics (Income) survey.

It is expected that, in line with previous findings, the number of minimum wage earners will not be as high as predicted when the next minimum wage review occurs. However, as this year's proposed increase is larger than in recent years and will impact more workers, it is possible that the number will not reduce as much as in previous years.

Inflationary impact
MBIE's model estimates the possible impact on general price inflation an increased minimum wage might have. Inflation is a mandated criterion.

MBIE's model estimates that there will be a minor direct inflationary impact (0.1%) to the consumer price index of increasing the minimum wage to $17.70. The model does not assess wage inflation, and there is uncertainty around the impact that wage inflation might have on consumer price inflation. MBIE also acknowledges that there is a risk that significant ripple effects to wages above the minimum wage could lead to much greater wage inflationary pressure, which could have flow-on impacts to general price inflation and interest rates. Expectations for wage growth due to the Government's signalled increase to $20 by 2021 may also have an effect, but the extent to which this might occur is not possible to quantify.

Costs to government
The costs to government of an increased minimum wage are estimated based on modelled costs for a number of agencies and ministries at each minimum wage option. MBIE received costings from the Ministry of Health, the Ministry of Education, the Ministry of Social Development, Oranga Tamariki and Accident Compensation Corporation.

The estimated additional costs to government (based on agencies' costings) are higher than in 2017, largely due to a larger proposed rate ($1.20 vs. 75c). This year, a $1.20 increase is estimated to cost government $93.1 million annually.

Although increases to the minimum wage are predicted to increase costs for government, it is likely that they would also impact on the tax and transfers system and other social policy programmes. While many of these are not able to be quantified, examples include:

- a minimum wage increase is likely to lead to expenditure savings as a result of lower entitlements being paid out due to abatement of welfare benefits and other social assistance (eg Working for Families Tax Credits)
- the number of people required to make student loan repayments could increase, as well as the rate they are required to repay them
- the amount of KiwiSaver contributions made could increase, which could increase expenditure if it results in more people receiving their full member tax credit entitlement
- it is expected that PAYE tax revenue paid by employees would increase, but Inland Revenue advises this is likely to be more than offset by a decrease in tax paid by their employers (as wages are deductible from employer revenue)
- an increase may lead to more people having disposal income, which could result in the collection of more GST due an increase in consumption levels.

Increasing the minimum wage to $20 by 2021
A key focus of this year's review has been how different options may impact on the Government's ability to meet their commitment to increase the minimum wage to $20 by 2021.

$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. Front- and back-loaded approaches, which include larger increases in some years, are associated with higher risks and levels of uncertainty. MBIE's modelling indicates that as the increase in any year gets larger, the constraint on employment growth increases at a disproportionately higher rate.

Impact on workers
MBIE has considered the impacts of minimum wage increases on workers. Workers who are female, Māori, Pacific peoples, part-time employees, without formal qualifications, or working in the retail and hospitality industries are more likely to be paid at the minimum wage rate. These workers are therefore generally more likely to benefit from any increase to the minimum wage rate. However, they may also be the first to experience any negative impacts that could result from a change to the minimum wage (for example, reduced hours offered or substitution of some groups of workers for others).

The table below shows the demographics of minimum wage earners if the minimum wage is increased to $17.70. This looks broadly similar to those in previous years.

Table 3: Demographics of wage earners at $17.70

Demographic	% of minimum wage earners			% of total wage earners
	16-24 year olds	25-64 year olds	16-64 year olds	16-64 year olds
Aged 16-24 years	100%	0%	50%	17%
Female	51%	64%	58%	50%
European/Pakeha	57%	45%	51%	62%
Māori	19%	17%	18%	14%
Pacific	7%	9%	8%	6%
Part-time	59%	36%	47%	18%
Studying	34%	9%	22%	12%
Total	104,900	104,300	209,200	2,044,000

Wages are often only part of the income of low income workers. There are a range of government interventions and initiatives aimed at protecting employment and increasing incomes. These interventions encompass labour market policies, the social assistance system, the taxation system, and education and training policies.

Tables 4 and 5 set out the anticipated increase in weekly income for two family types if the minimum wage is $17.70.

Table 4: A couple working a combined 60 hours per week at $17.70 per hour with two dependent children living in various regions across New Zealand

Minimum wage		Auckland	Ashburton	Whakatane
$17.70 (+7.27% from current minimum wage)	Combined household net earnings	$46,753.39	$46,753.39	$46,753.39
	Government transfers after abatements	$21,506.00	$14,964.40	$13,966.00
	Total annual household earnings	$68,259.39	$61,717.79	$60,719.39
	Per cent increase in annual earnings from current minimum wage	**1.74%**	**1.93%**	**1.96%**

Table 5: A solo parent working 40 hours per week at $17.70 per hour with two dependent children living in various regions across New Zealand

Minimum wage		Auckland	Ashburton	Whakatane
$17.70 (+7.27% from current minimum wage)	Combined household net earnings	$31,278.26	$31,278.26	$31,278.26
	Government transfers after abatements	$28,303.00	$22,198.20	$20,763.00
	Total annual household earnings	$59,281.26	$53,476.46	$52,041.26
	Per cent increase in annual earnings from current minimum wage	**3.18%**	**3.56%**	**3.66%**

Impact on employers

The impact of a minimum wage increase on each sector depends on the number of employees earning the minimum wage and close to it in those sectors. In New Zealand (and in many countries), employers in the hospitality, manufacturing, and retail sectors are more likely to have staff paid at, or close to, the minimum wage than employers in the professional/technical services, and health industries.

The table below shows the sectors employing minimum wage workers at $17.70. This looks broadly similar to those in previous years.

Table 5: Minimum wage workers by sector at $17.70

Sector	Workers		Working Hours	Their Earnings
	% of total workers	Number	% of total hours	% of total earnings
Agriculture	11.3	8,900	10.8	7.8
Mining	0	0	0	0
Manufacturing	7.7	16,800	7.1	4.2
Utilities	2.9	600	3	1.4
Construction	6.2	10,200	5.3	3.1
Wholesale	6.3	5,900	4.9	2.5
Retail	27.4	54,100	21.5	15.7
Hospitality	37.6	46,200	30.8	25.6
Transport and Storage	7.2	6,300	6.7	3.8
Information and Telecommunications	4.5	1,800	4.3	2
Finance	0.3	200	0.2	0.1
Real Estate	11.9	3,600	12	6.1
Professional Services	2.5	4,200	1.5	0.7
Administrative Services	21.1	12,200	17.1	10.6
Public Administration	2.7	3,800	2.2	1
Education	5	10,300	4	2.2
Health	4.9	11,500	3.6	2
Arts and Recreation	11.3	3,800	8.2	4.8
Other Services	10.9	7,100	9.2	5.9
Total	10.2	209,200	7.9	4.4

Both the number, and proportion, of workers earning the minimum wage, or close to it, is relevant in determining the impact of a minimum wage increase in that region. At the minimum wage rate of $17.70, Wellington would have a higher proportion of its workers earning the minimum wage than other regions, making up 13.9 per cent of all workers in Wellington.

Table 6: Minimum wage earners by region at $17.70

Region	Number (%)
Northland	5,900 (10.2%)
Auckland	67,400 (9.6%)
Waikato	20,000 (9.2%)
Bay of Plenty	16,300 (10.8%)
Gisborne/ Hawke's Bay	11,100 (13.3%)
Taranaki	4,900 (12.6%)
Manawatu-Wanganui	13,200 (10%)
Wellington	20,300 (13.9%)
Nelson/Tasman/Marlborough/ West Coast	10,300 (8.7%)
Canterbury	25,900 (14%)
Otago	8,200 (9.9%)
Southland	5,800 (8.1%)

Impact on poverty

Analysis conducted by the Child Poverty Unit and Ministry of Social Development indicates that minimum wage increases on their own will have a relatively limited impact on measured income poverty for those with children. This conclusion relies on households fully receiving their in-work entitlements and available evidence suggests there are take-up issues with both the Accommodation Supplement and the Minimum Family Tax Credit.

Nevertheless, this analysis, combined with the relatively small proportion of households with children on the lowest wages, indicates that the impacts of minimum wage increases on child poverty rates should be relatively limited. Minimum wage increases are more likely to have an impact on poverty rates for households without children. This is because they are more likely to be on the lowest wages and receive less government-provided income support to supplement their income (such as through the MFTC, which results in the withdrawal of Government assistance).

It is more difficult to assess the impact of the minimum wage on material hardship, particularly as material hardship is seen across the household income distribution, and levels of material hardship are influenced by a much broader range of factors, other than income.

Section 5: Conclusions

5.1 What option, or combination of options, is likely best to address the problem, meet the policy objectives and deliver the highest net benefits?
MBIE's analysis of the Government's proposed minimum wage is that there are both positive benefits for workers of increased incomes, as well as potential negative impacts (such as restraint on employment or the risk of increased inflationary pressure). The increase of $1.20 (to $17.70) represents a steady, predictable and lower risk 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, which include larger increases in some years, are associated with higher risks and levels of uncertainty. In light of the commitment, many employers and workers already expect a larger-than- usual increase. The labour market and economic context is currently well placed to support this increase with relatively minor impacts. The unemployment rate (3.9 per cent) is the lowest it has been since June 2008, when it was 3.8 per cent. The tightening of the 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. This increase will have positive impacts for low-paid workers by increasing their income. Up to 209,200 workers (those currently earning up to $17.70) will receive an increase up to the new minimum wage. Many of those earning above the new minimum wage can also expect an increase over time as relative wage rates between different roles are addressed, and new entrants to employment can expect to start employment at a higher wage rate than if this increase did not occur. This represents an increase in hourly wages and overall income for many workers. A minimum wage of $17.70 will result in historically high relativities to the median and average wages. The estimated restraint on employment for this minimum wage is 8,000, compared to forecast employment growth of 56,900 in 2019. This is higher than last year's estimated restraint of 3,000; however, the larger increase also benefits significantly more workers (209,200 compared to 164,100 last year). This indicates that minimum wage workers will be better off through increased incomes, compared to relatively minor negative employment effects. Further, the current strong labour market is expected to be able to absorb some of this impact. The minimum wage model identifies a small direct inflationary impact (0.1%) of increasing the minimum wage to $17.70, although MBIE acknowledges that there is the risk of greater inflationary pressure on wages due to a ripple effect for wages above the minimum wage. There is also the possibility that minimum wage increases could lead to compression of wages at the lower end of the wage distribution. In the past this has been a concern raised, but there has been little evidence of this occurring. Previous reviews of the minimum wage estimate relatively similar numbers of people earning the minimum wage each year. However, as this year's proposed increase is larger than in recent years and will impact more workers, it is possible that the number of minimum wage earners could increase more than in previous years.

The estimated additional cost to government (based on agencies' costings) is similar to some previous reviews.

5.3 What other impacts is this approach likely to have?
Given the publicity surrounding the Government's commitment to increase the minimum wage to $20 by 2021, and policies such as paying the living wage to core government workers, there is the possibility that workers and unions will have higher than usual wage expectations for wages above the minimum wage. This could make the impact on wage inflation greater and, as explained above, there is uncertainty over the extent to which wage inflation might have an impact on general price inflation (CPI). Likewise, signalling of future increases will allow businesses to prepare for future minimum wages, but may trigger some of the effects that would be expected of a larger increase before the new minimum wages are adopted. For example, businesses may start to make decisions about investing in staff and capital based on their expectations of higher minimum wages in the coming years. It is not possible to quantify or estimate the extent to which this may occur. Increasing the minimum wage will, for many households, interface with in-work tax credits. Workers in low-income households whose incomes are currently supplemented by tax credits may not receive the full benefit of the wage increase due to abatement of their tax credits if their total income is over the abatement threshold. This will have an offsetting effect for fiscal impacts to Government, although the extent of this cannot be quantified.

5.4 Is the preferred option compatible with the Government's 'Expectations for the design of regulatory systems'?
Yes.

Section 6: Implementation and operation

6.1 How will the new arrangements work in practice?
Any increase to the minimum wage is made by Order in Council under the *Minimum Wage Act 1983*. The new minimum wage (and training minimum wage and starting-out wage) traditionally take effect the following 1 April. This convention provides the greatest certainty for employers and businesses and, importantly, aligns with the tax year. Publicity and media statements will be used to communicate the increase in a way to ensure clear messaging. Once implemented, all employers will be required to pay their workers at least the adult minimum wage (or the applicable training wage or starting-out wage). Failure to provide this minimum pay would mean that the employer is in breach of the *Minimum Wage Act,* and liable for penalties and recovery of wages.

6.2 What are the implementation risks?
Increasing the minimum wage is straightforward, and requires no significant process or procedural change. Effective communication and signalling is required. Increased minimum wages also present the risk that some employers may attempt not to comply and avoid paying the minimum wage. Likewise, employers may make decisions about their business practice in order to avoid the increased minimum wage for employees, such as increasing the use of contracted workers.

Section 7: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?
Monitoring the effects of the minimum wage increase is done by analysing a range of labour market and economic statistics that are collected and regularly published by Stat's NZ. As MBIE has ongoing responsibilities to support the Minister to review the minimum wage annually, the monitoring of the minimum wage increase will be built into future assessments of any potential increase.

7.2 When and how will the new arrangements be reviewed?
The minimum wage is required to be reviewed each year. Given the Government's intention for the minimum wage to increase to $20 by 2021, the longer-term impacts of the minimum wage (especially regarding potential employment effects) will be of interest to MBIE, will continue to be monitored, and will feed into future reviews of the minimum wage.