



Issue 01

**Economic and
Social Indicators –
Monitoring Report**

July to December 2007

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Australian Fair Pay Commission

Economic and Social Indicators – Monitoring Report

July to December 2007

Released 25 February 2008

Introduction

This is the first issue of the Australian Fair Pay Commission's *Economic and Social Indicators – Monitoring Report*. It is designed to monitor the outcomes from the Commission's minimum wage-setting decisions and to inform future decisions. The report discusses trends in key indicators, together with changes that have occurred since the Commission was established and developments in the past six months.

The Commission's approach to monitoring has been informed by a range of sources, including research commissioned from the National Institute of Labour Studies and Access Economics regarding strategies for monitoring the impact of minimum wage decisions.¹

There are three main sections to the report, broadly reflecting the factors that the Commission must have regard to in fulfilling its wage-setting function:

1. Macroeconomic developments;
2. Employment of low-paid workers; and
3. The safety net and work incentives.

Overall, the economy has performed better than was expected by most analysts at the time of the Commission's July 2007 decision. The non-farm economy grew by 4.5 per cent in real terms over the year to the September quarter 2007, underpinned by significant growth in investment.

While employment has grown moderately over the past year, at 2.5 per cent, labour force participation has been generally stable at 65 per cent of the working age population, following increases between 2004 and 2006. As a result, the unemployment rate has edged lower in 2007, to 4.3 per cent. A broader measure of labour underutilisation has fallen consistently over the past year, to 7 per cent of total hours worked.²

Differences in labour market performance remain between the states and territories. Most regions experienced good employment growth in 2007, with the strongest growth recorded in Western Australia and Victoria. Unemployment rates were lowest in Western Australia and Queensland, at 3.1 per cent and 3.5 per cent, respectively.

Generally, labour costs have been growing steadily, at around 4 per cent over the year to December 2007. Consumer prices rose by 3 per cent over the year, which is slightly higher than was expected at the time of the Commission's July 2007 decision on minimum wages. The Reserve Bank of Australia's forecast for inflation in the year to June 2008 is now 3½ per cent.

¹ Copies of the reports from the National Institute of Labour Studies and Access Economics can be found at <http://www.fairpay.gov.au/fairpay/Research/Research2007/Research2007.htm>

² Hours lost due to unemployment, underemployment and discouraged participation.

Overall, wages in those industries and occupations with greater sensitivity to minimum wages have grown more slowly than in other segments of the economy in the past year. Employment patterns have been diverse, with strong growth in the Retail trade sector, at 6.4 per cent, and the level of employment in the Accommodation, cafes and restaurants sector unchanged. Job vacancies in most industries continue to be high, compared with the levels recorded over the past five years.

Labour force participation and employment for many demographic groups who tend to have relatively higher numbers of low-skilled or low-paid workers have continued to improve over the past year. There has been a particularly strong improvement in the employment of single parents, due, in part, to changes in work requirements for income support recipients which have been implemented since mid-2006.

Some measures of work incentives have improved over the past year, largely through an easing in the rate at which benefits are reduced as earnings rise and as a result of changes which effectively raised the minimum threshold for the payment of income tax.

The real value of the Federal Minimum Wage and of disposable incomes for low-income households has been broadly steady over the past year. However, these indicators have declined relative to average earnings and, for some household types, relative to the relevant Henderson Poverty Lines.

The Commission's December 2006 increase in minimum wages particularly benefited single people with or without children, whereas there was a lesser effect for couples, due to higher effective marginal tax rates. Subsequently, disposable incomes for all family types rose as a result of the July 2007 income tax cuts and the October 2007 minimum wage increase.

In summary, the Australian economy has continued to demonstrate sound employment and income growth, with the safety net for low-paid workers being maintained in broad terms.

Future issues of the report will continue to analyse trends in the major indicators outlined above and evolve as the Commission furthers its research activities. Such research is ongoing, for example, in respect of patterns of economic performance between industries, labour market transitions of low-paid workers, and the employment outcomes of young people, trainees and apprentices, and people with disabilities.

The Commission welcomes comment on the issues monitored in this report, as input into the 2008 Minimum Wage Review.



Ian R. Harper
Chairman

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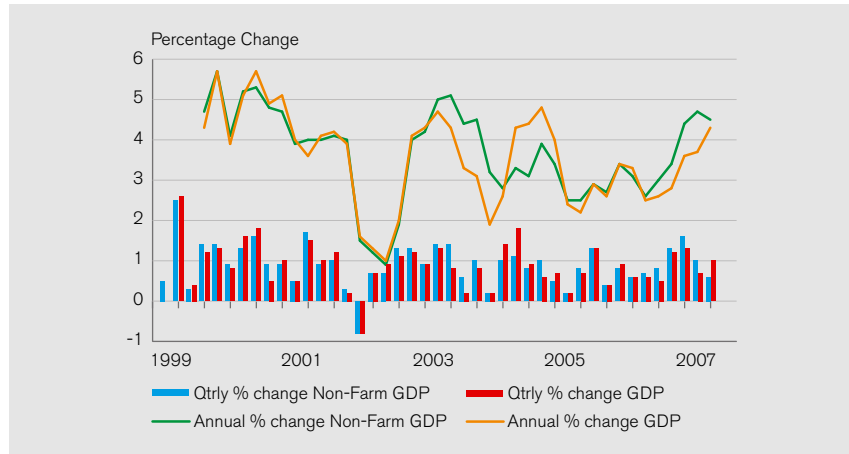
1. Macroeconomic developments

In this section, developments in the macroeconomy are discussed, drawing together broad indicators of economic activity, labour market performance and price inflation.

Economic activity

The economy has continued to grow solidly over the past year (Chart 1). Gross domestic product (GDP) increased by 4.3 per cent in real terms in the year to September 2007, the highest growth rate recorded since mid-2004. The non-farm economy grew by 4.5 per cent over the year, driven by rapid growth in investment. Real farm GDP is around 7 per cent below its level a year ago, although recent data have not been as weak as in previous quarters.

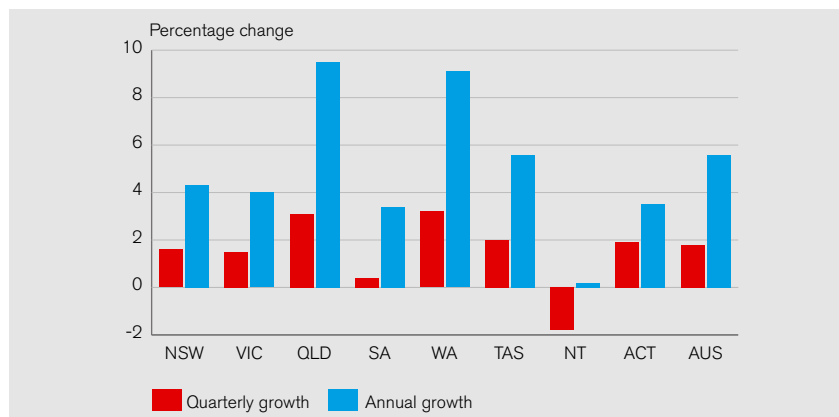
Chart 1: Change in real GDP



Source: ABS, *National Accounts*, September quarter 2007, Catalogue No. 5206.0.

Recent developments across state economies indicate that the resources boom continues to underlie strong growth in final demand in Queensland and Western Australia, largely through investment expenditure, with most states experiencing moderate growth in household consumption (Chart 2).

Chart 2: State final demand



Source: ABS, *National Accounts*, September quarter 2007, Catalogue No. 5206.0.

The labour market

Employment has continued to grow moderately over the past year, at 2.5 per cent, reflecting ongoing economic growth (Table 1 and Chart 3). Most of the employment growth has been in full-time work.

Labour force participation has been generally stable, at 65 per cent of the working age population, following increases between 2004 and 2006. As a result, the unemployment rate has edged lower in 2007, to 4.3 per cent (Chart 4).

Table 1: Key labour market indicators*

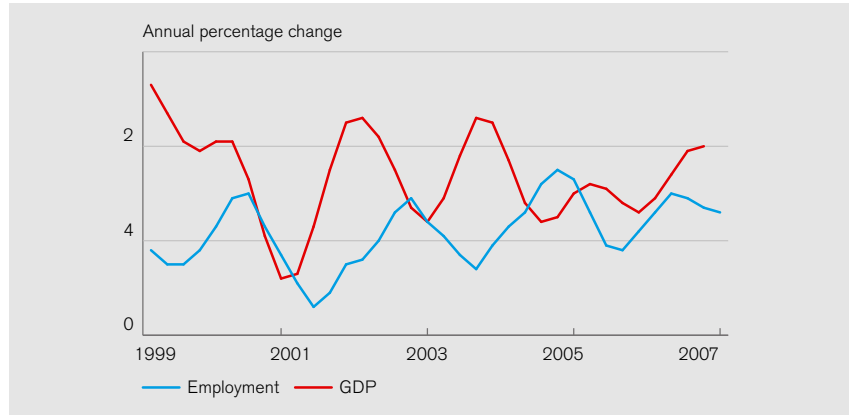
	December 2006	June 2007	December 2007	Semi-annual Change	Annual Change
Employment ('000)	10341	10462	10603	1.3%	2.5%
Full-time ('000)	7388	7493	7599	1.4%	2.9%
Part-time ('000)	2954	2970	3004	1.2%	1.7%
Unemployment ('000)	497	473	474	0.1%	-4.5%
Looking for a full-time job ('000)	354	331	325	-1.8%	-8.2%
Looking for a part-time job ('000)	143	142	149	4.8%	4.4%
Long-term - 1 year or longer ('000)	90.7	65.7	71.4	8.7%	-21.3%
Unemployment rate (%)**	4.6	4.3	4.3	0.0	-0.3
Looking for a full-time job (%)	4.6	4.2	4.1	-0.1	-0.5
Looking for a part-time job (%)	4.6	4.6	4.7	0.2	0.1
Participation Rate (%)**	64.9	65.0	65.2	0.2	0.3
Employment to Population (%)**	62.0	62.2	62.4	0.3	0.4
Labour Force ('000)	10838	10936	11077	1.3%	2.2%

Source: ABS, *Labour Force*, December 2007, Catalogue No. 6202.0; ABS, *Labour Force Detailed*, October 2007, Catalogue No. 6291.0.55.001.

*All data are seasonally adjusted.

**Changes in this row are percentage point changes

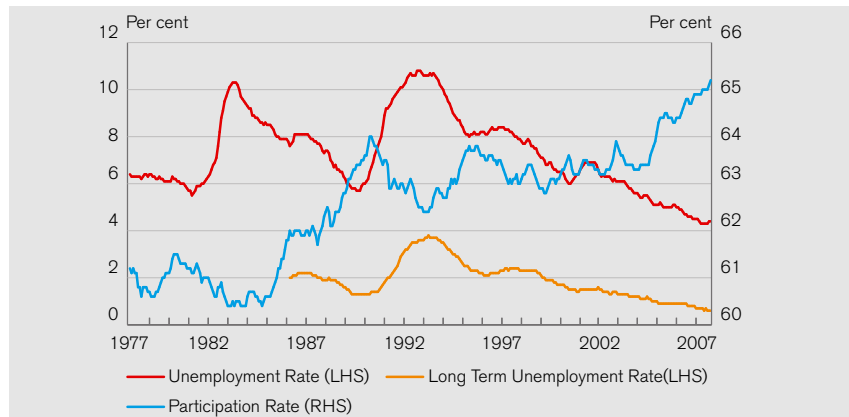
Chart 3: Change in employment and real GDP*



Source: ABS, *National Accounts*, September quarter 2007, Catalogue No. 5206.0; ABS, *Labour Force Spreadsheets*, December 2007, Catalogue No. 6202.0.55.001.

*All data are in trend terms. Employment data calculated as monthly average over quarter.

Chart 4: Unemployment and participation*



Source: ABS, *Labour Force Spreadsheets*, December 2007, Catalogue No. 6202.0.55.001; ABS, *Labour Force Detailed*, December 2007, Catalogue No. 6291.0.55.001.

*Three month moving average of seasonally adjusted data.

Between 2004 and 2006, increases in employment were met by rising labour force participation. This suggests that job prospects and work incentives combined to attract an increasing number of people into the labour force to satisfy demand. However, in the past year, the overall participation rate has been broadly steady at the 65 per cent mark, while the unemployment rate had edged lower.

Some of the state economies have continued the pattern of strong employment growth combined with increasing participation. For instance, employment in Victoria and Western Australia grew by 3.4 and 4.1 per cent, respectively, in 2007, the highest of any states, with participation increasing by around 1 percentage point in each case. Employment growth appears to have been weakest in New South Wales in the first half of 2007, before strengthening in the past six months.

Unemployment rates in all states, at or near their lowest levels in the past thirty years, have continued to fall during 2007. In Western Australia and Queensland, unemployment rates have fallen to 3.1 per cent and 3.5 per cent, respectively.

At a local level, 76 per cent of small labour market areas recorded a fall in their unemployment rate over the year to the September quarter 2007, with 73 per cent recording an unemployment rate of less than 5 per cent.³

There have been significant reductions in long-term unemployment in recent years. Since mid-1993, the long-term unemployment rate has fallen from 3.8 per cent to 0.6 per cent. This suggests that the capacity of the labour market to absorb this group of unemployed people has improved.

Broader measures of labour underutilisation, drawing underemployment and discouraged jobseekers into the calculation, also point to a stronger labour market and tightening labour supply. Indicators of labour underutilisation based on the hours of work lost due to unemployment, underemployment or discouraged status have consistently fallen over the past year (Table 2). Measured underutilisation is now just below the level recorded in the late 1980s, at 7 per cent of hours worked.

Table 2: Hours-based measures of labour underutilisation

Measures	August 2006	May 2007	August 2007	Quarterly Change	Annual Change
Underemployment*	3.0	2.8	2.8	-0.1	-0.2
Underutilisation (excl hidden unemployment)**	6.4	5.9	5.7	-0.1	-0.6
Underutilisation (incl hidden unemployment)**	7.8	7.1	6.9	-0.2	-0.9

Source: Centre of Full Employment and Equity (University of Newcastle), *Labour Market Indicators*, August 2007.

*Underemployment is measured as the ratio of the hours of work lost due to part-time workers not working as many hours as they would like to the total available hours of work in the labour force. The measure cited above does not include part-time workers who preferred more hours of work but did not actively search for it or were unavailable.

**Underutilisation is measured as the ratio of the hours of work lost due to unemployment and underemployment to the total available hours of work in the labour force. Hidden unemployment refers to the hours of work lost due to 'discouraged' workers, who are willing to work and available to start work, but are not actively searching for work because they believe they cannot find a job.

Demand for skilled and unskilled labour remains high. The Australian Bureau of Statistics' (ABS) measure of the job vacancy rate is significantly higher than it was a year ago, and is at its highest level since the 1970s. Around 182,000 job vacancies were recorded in November 2007, 13.7 per cent more than a year ago, with most states and industries reporting relatively high vacancy rates.

Overall, the labour market is expected to remain strong in the months ahead, notwithstanding forecasts of some easing of employment growth and a modest rise in the unemployment rate.

³ Department of Education, Employment and Workplace Relations, *Small Area Labour Markets*, September quarter 2007.

Wages and prices

Most indicators suggest that wages have increased at a slightly higher rate in the second half of 2007, at just above 4 per cent (annualised).

The Wage Price Index (WPI) increased by 1.0 per cent in the September quarter 2007, to be 4.2 per cent higher over the year (Table 3). This is consistent with the annual growth rates recorded since the first half of 2005 (Chart 5).

Average weekly ordinary time earnings and average weekly earnings have been growing more quickly through 2007 than in the previous year, although they remain below the rates of growth recorded in 2005.

The average annualised wage increase from agreements reached in the September quarter 2007 was just under 4 per cent, around the average for 2006-07, but below the average for 2005-06.⁴

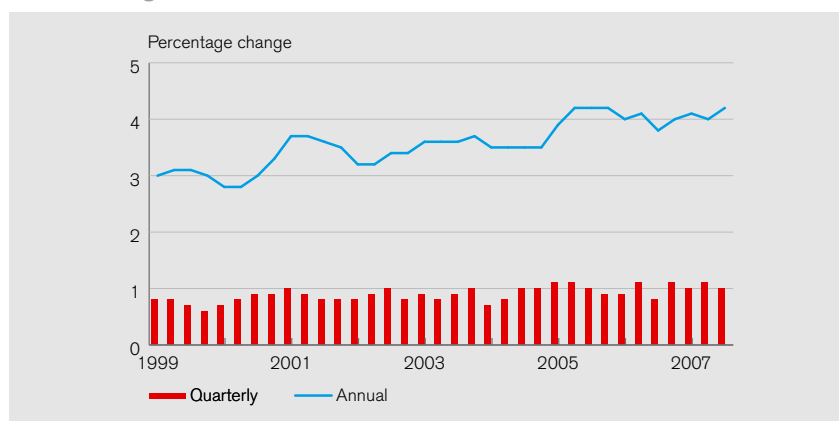
Table 3: Wage measures

Wage measure	Level*	Percentage change from June quarter 2007 to September quarter 2007	Percentage change from September quarter 2006 to September quarter 2007
WPI (Index)		1.0	4.2
Average Weekly Ordinary-Time Earnings for Full-Time Adult Employees (AWOTE)	\$1,102.40	1.0	4.9
Average Weekly Earnings (AWE)	\$873.60	0.6	4.5

Source: ABS, *Labour Price Index*, September quarter 2007, Catalogue No. 6345.0; ABS, *Average Weekly Earnings*, August 2007, Catalogue 6302.0.

*Data are seasonally adjusted estimates. AWOTE and AWE are measured at mid-month of quarter.

Chart 5: Wage Price Index



Source: ABS, *Labour Price Index*, September quarter 2007, Catalogue No. 6345.0

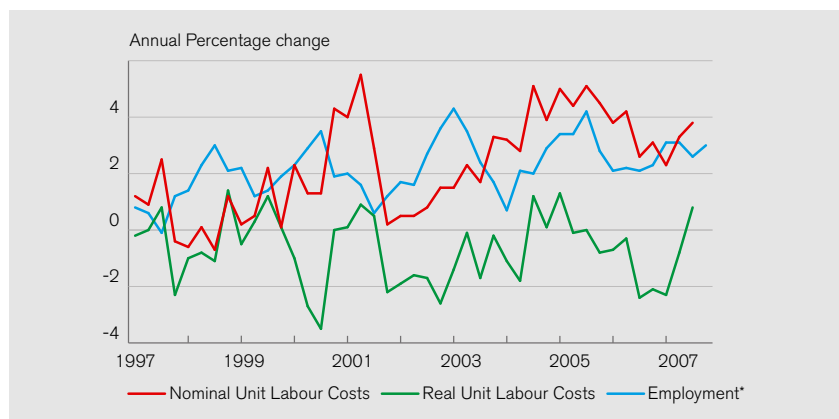
⁴ Department of Education, Employment and Workplace Relations, *Trends in Federal Enterprise Bargaining*, September Quarter 2007.

The relationship between wages, prices and employment is complex, with labour productivity a key element in that relationship. Increased productivity can offset growth in total labour costs, thereby helping to contain any inflationary pressures arising from a buoyant labour market. There is a wide range of productivity estimates, and such estimates, particularly short-term movements, should be treated with care. As a result, productivity trends and the main factors behind those trends are difficult to ascertain at any given point in time.

One aggregate measure of labour productivity – GDP per hour worked – increased by 1.6 per cent over the past year, while another measure – GDP per hour worked in the market sector – increased by 0.8 per cent.⁵ Most measures suggest that recent labour productivity growth remains below the rates achieved during previous productivity cycles.

Unit labour costs represent a further link between productivity, the cost of labour, prices and employment. Estimates of nominal unit labour costs are growing at moderate rates (Chart 6). The real cost of labour to producers has been falling in recent years, making labour more affordable. These changes are also reflected in the general rise in the profit share of national income over the past five years (Chart 7). However, the volatility in the data, including the sharp rise occurring in the most recent quarter, warrants continued monitoring.

Chart 6: Unit labour costs and employment (non-farm)

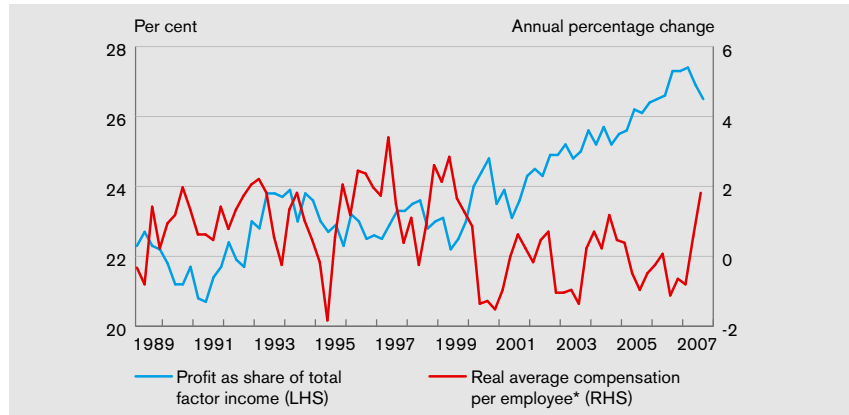


Source: ABS, *National Accounts*, September quarter 2007, Catalogue No. 5206.0; ABS, *Labour Force Detailed, Quarterly*, November 2007, Catalogue No. 6291.0.55.003.

*Sum of all industries except Agriculture, forestry and fishing.

⁵ Australian Bureau of Statistics, *Australian National Accounts: National Income, Expenditure and Product*, ABS Catalogue No. 5206.0, September 2007, p.20

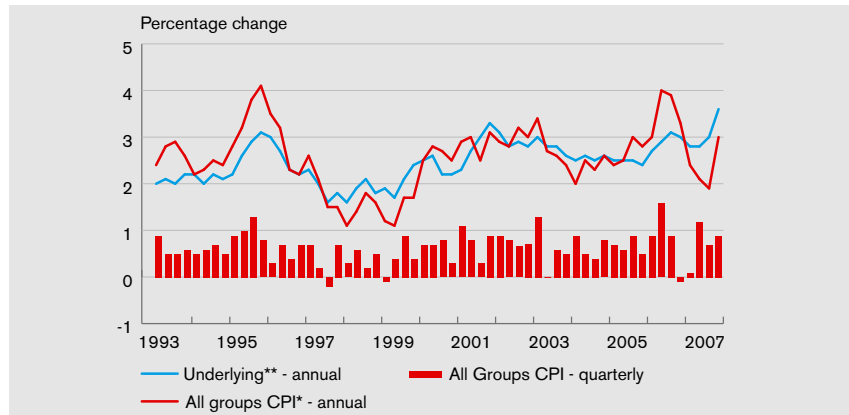
Chart 7: Profit share of national income and real wages



Source: ABS, *National Accounts*, September quarter 2007, Catalogue No. 5206.0.
 *Average compensation per employee adjusted by implicit GDP deflator.

There are several measures of consumer price inflation published by the ABS, each involving a slightly different methodology or scope. The All Groups Consumer Price Index (CPI) increased by 0.9 per cent in the December quarter 2007, to be 3.0 per cent higher over the year (Chart 8). The quarterly data in this series have been volatile over the past year, due to a number of temporary factors. By contrast, the average of the Reserve Bank of Australia's (RBA) underlying inflation measures was 3.6 per cent over the year, registering around 1 per cent per quarter recently.

Chart 8: Consumer price inflation



Source: ABS, *Consumer Price Index*, December quarter 2007, Catalogue No. 6401.0; RBA, *Statement on Monetary Policy*, November 2007.
 *Excluding interest charges prior to the September quarter 1998 and adjusted for the tax changes of 1999-2000.
 **Average of the trimmed mean and weighted median inflation measures.

Domestic economic forecasts

The economic outlook remains steady at this stage. The Australian Government, in its *Mid-Year Economic and Fiscal Outlook 2007-08* (MYEFO), forecast real GDP to grow by 4¼ per cent in 2007-08, before easing to 3½ per cent the following year. Consumption growth is expected to continue, based on strong employment growth, while business investment is expected to grow solidly, adding to the capital stock. However, some concerns were noted in relation to internal risks (from a tightening labour market) and external risks (particularly the health of the US economy).

The MYEFO forecast is for employment to grow by 2¼ per cent in 2007-08 (compared with a forecast of 1½ per cent in the 2007-08 Budget), before moderating in 2008-09 due to a slowing of economic growth and higher growth in labour costs. The participation and unemployment rates are forecast to increase to 65¼ per cent and 4½ per cent, respectively, in 2007-08, due in part to new participation requirements for income support recipients.

Table 5 presents the most recent published Treasury forecasts for economic indicators of significance to the Australian Fair Pay Commission's (Commission's) forthcoming Minimum Wage Review.⁶

Table 5: Domestic economic forecasts

Indicator	2006-07 Outcomes Year average	2007-08 Forecasts Budget Year average	2007-08 Forecasts MYEFO Year average
Gross Domestic Product	3.3	3¾	4¼
Non-farm product	3.9	3½	4
Farm product	-19.2	18	14
Labour Market			
Employment	2.7	1½	2¼
Unemployment rate	4.5	5	4½
Participation rate	64.8	65	65¼
Prices and Wages			
Consumer Price Index	2.9	2½	2¾
Wage Price Index	4	4¼	4¼

Source: Australian Government, *Mid-Year Economic and Fiscal Outlook 2007-08*, released 15th October 2007.

⁶ Note that the Treasury forecasts were released four months prior to the RBA's forecasts contained in its February 2008 *Statement on Monetary Policy*.

Macroeconomic developments

Both the Australian Treasury and the RBA have expressed concern over a tightening labour market and the possible implications for price inflation. The RBA has also noted that:

...the recent pick-up in inflation carries the risk of generating an upward drift in inflation expectations, which could feed back into wage and price-setting behaviour.⁷

In its February 2008 Statement on Monetary Policy, the RBA forecast that inflation, as measured on a year-ended basis, would increase in the near term (reflecting in part the large quarterly increases in the three latest quarters). Underlying inflation was forecast to reach 3¾ per cent in annual terms by June 2008, while CPI inflation was forecast to reach 3½ per cent (Table 4). Both measures were then expected to fall gradually over the next couple of years, to around 3 per cent, reflecting a moderation in demand growth and a gradual easing in capacity pressures.

Table 4: RBA inflation forecasts

	Percentage change over year to quarter						
	Sep 2007	Dec 2007	June 2008	Dec 2008	Jun 2009	Dec 2009	June 2010
Consumer price index	1.9	3.0	3½	3½	3¼	3¼	3
Underlying Inflation*	3.0	3.6	3¾	3½	3¼	3¼	3

Source: ABS, *Consumer Price Index*, December quarter 2007, Catalogue No. 6401.0; RBA, *Statement on Monetary Policy*, February 2008.

*Average of the trimmed mean and weighted median inflation measures.

Conclusion

The macroeconomic evidence suggests that the labour market has continued to improve over the past year. Measures of underlying inflation and wages growth have increased over the same period, a sign that the labour market may be tightening.

⁷ RBA, *Statement on Monetary Policy*, February 2008, p. 56.

2. Employment of low-paid workers

The low-paid segments of the labour market are analysed in this section, with a focus on selected demographic groups, occupations and industries.

Educational attainment

Over the past decade, the average level of educational attainment of the population has increased. People without a post-school qualification made up a smaller percentage of the labour force and working age population in 2007 than they did in 1997, indicating that the pool of low-skilled workers is getting smaller in proportional terms (Table 6).

At the same time, labour market outcomes for those without a post-school qualification have improved in relative terms since the mid-1990s. For example, the unemployment gap between persons without a post-school qualification and persons with a post-school qualification, while still substantial, has closed somewhat since 1997. Similarly, the participation rates and the employment to population ratios for the two groups have shown signs of convergence.

In part, the ability of low-skilled people to gain employment, compared with that of higher-skilled people is influenced by the business cycle. As the labour market continues to tighten, low-skilled people, whether unemployed or not in the labour force, are more likely to be drawn into employment. This trend is also reflected in the steady decline in long-term unemployment (Chart 4).

Table 6: Labour force status of persons with and without a post-school qualification

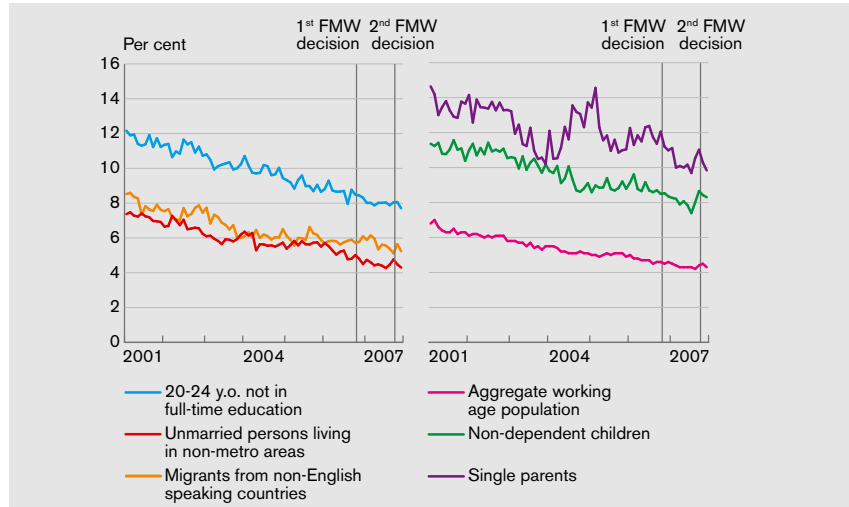
	Percentage with		Percentage without	
	1997	2006	1997	2006
Working-age population	40.4	52.4	59.6	47.6
Not in the Labour Force	22.8	32.7	77.2	67.3
Labour Force	46.5	58.2	53.5	41.8
Unemployment	28.9	38.7	71.1	61.3
Employment	48.2	59.2	51.8	40.8
Employed full-time	52.4	63.6	47.6	36.4
Employed part-time	36.1	48.2	63.9	51.8
Unemployment rate	5.4	3.3	11.6	7.3
Participation rate	85.3	85.9	66.5	68.0
Employment to population ratio	80.7	83.0	58.7	63.0

Source: ABS, *Education and Work*, May 2007, Catalogue No. 6227.0.

Selected demographic groups

In its monitoring strategy, the National Institute of Labour Studies identified five demographic groups that contain a relatively high proportion of low-skilled workers, a proxy for award and Pay Scale reliant workers. In recent years, the unemployment rate has fallen for each of these groups (Charts 9a and b). Participation has also increased, with the exception of non-dependent children (Charts 10a and b). This suggests that both unemployed people and new entrants into the labour force are finding employment.

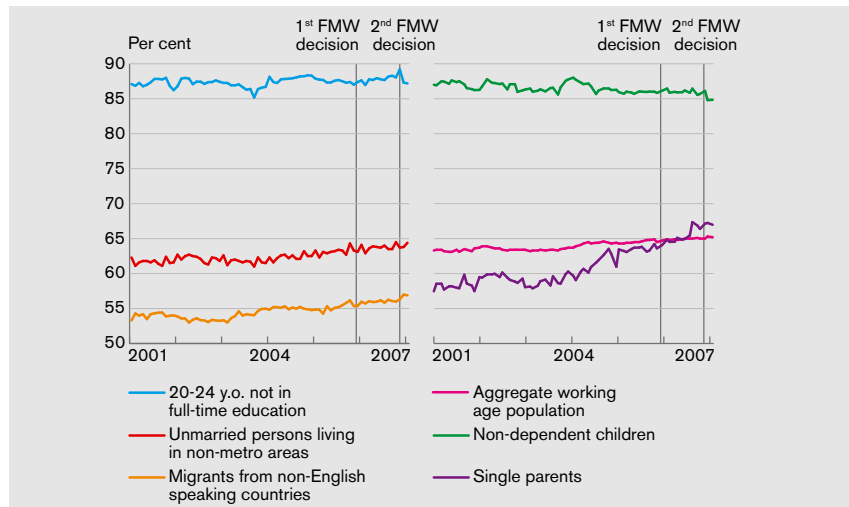
Chart 9: Unemployment rates for selected low-skilled groups*



Source: ABS, *Labour Force Detailed*, September 2007, Catalogue No. 6291.0.55.001.

*All data, except aggregate data, seasonally adjusted by AFPCS.

Chart 10: Participation rates for selected low-skilled groups*



Source: ABS, *Labour Force Detailed*, September 2007, Catalogue No. 6291.0.55.001.

*All data, except aggregate data, seasonally adjusted by AFPCS.

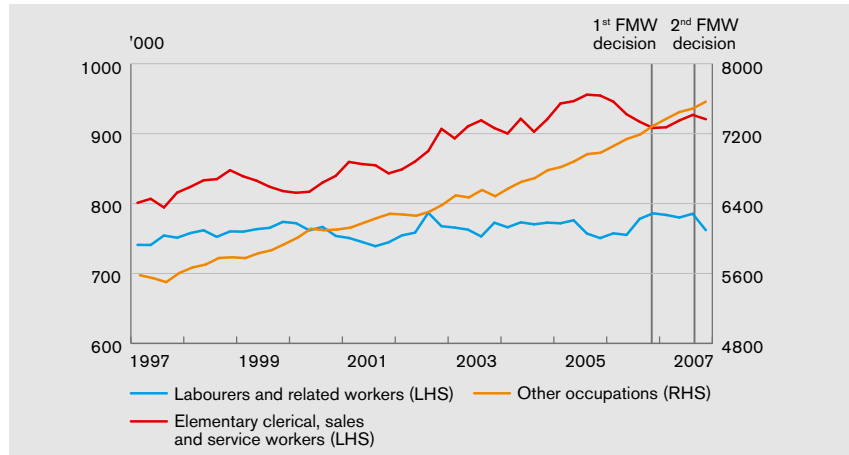
Employment of low-paid workers

Improvements in labour market outcomes for single parents have been most significant. A large increase in participation in mid-2006 was supported by a strong improvement in employment. This trend was not as marked for other labour market groups, suggesting that factors specific to the single-parent population, such as changes to income support work requirements, may have had a significant role.

Low-skilled occupations

While employment outcomes for low-skilled demographic groups have continued to improve, employment in low-skilled occupations has not grown as quickly in recent times as for other occupations. The numbers of employees classified as Elementary clerical, sales and service workers and Labourers and related workers have remained broadly the same since late 2002 (Chart 11). By contrast, the number of employees in other occupations has increased steadily, at an annualised rate of around 3.5 per cent over that period.

Chart 11: Employment in low-skilled occupations*

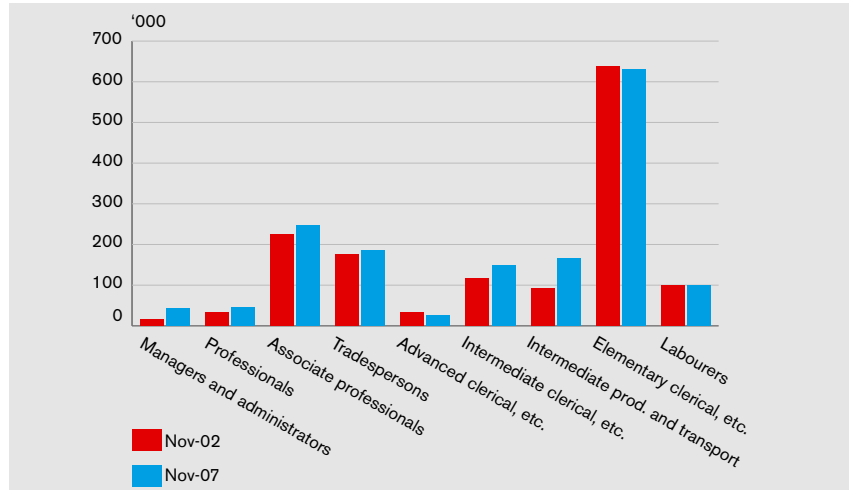


Source: ABS, *Labour Force Detailed*, Quarterly, November 2007, Catalogue No. 6291.0.55.003.
*Data seasonally adjusted by AFPCS.

Employment of low-paid workers

Around 60 per cent of all Elementary clerical, sales and service workers are located in the Retail trade industry. However, most of the employment growth in that industry has been concentrated amongst the medium to high-skilled occupational groups (Chart 12).

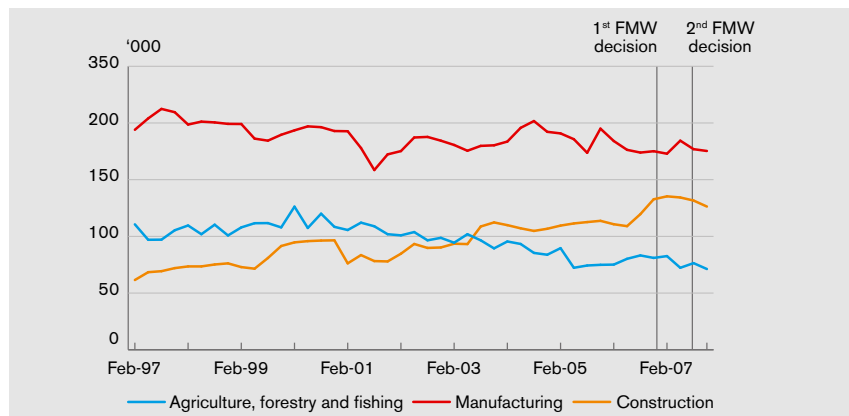
Chart 12: Employment in Retail trade by occupation*



Source: ABS, *Labour Force Detailed*, Quarterly, November 2007, Catalogue No. 6291.0.55.003.

In contrast, labourers and related workers are more evenly distributed across industries than are Elementary clerical, sales and service workers. Over the past decade, the number of Labourers and related workers has fallen in Manufacturing and Agriculture, forestry and fishing (Chart 13), both of which are industries that have experienced a general fall in employment over the period. These falls have been offset by a rise in the number of Labourers and related workers employed in Construction, in line with the strong growth in employment in that industry over the medium term.

Chart 13: Employment of Labourers and related workers by industry*



Source: ABS, *Labour Force Detailed*, Quarterly, November 2007, Catalogue No. 6291.0.55.003.

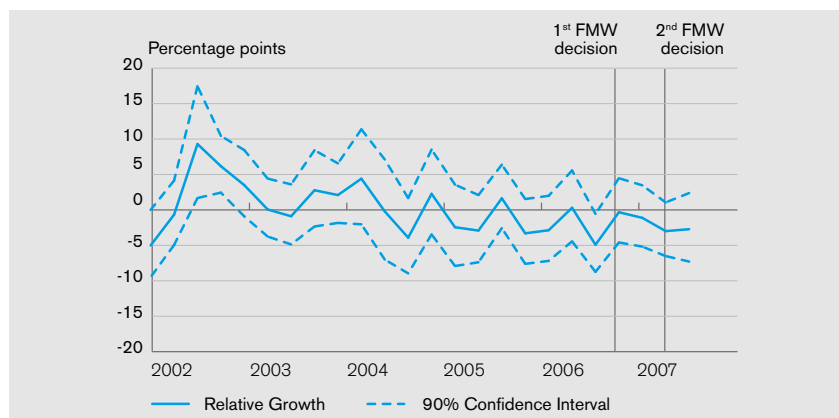
*Data seasonally adjusted by AFPCS.

Employment of low-paid workers

In its recommendations to the Commission on monitoring strategies, Access Economics suggested using a labour demand model to compare the growth in employment in low-paid occupations and high-paid occupations. Given that the wage bill of low-paying sectors tends to be relatively high, on account of the share of labour costs in total costs, an increase in real labour costs may lead to lower employment growth in the more sensitive occupations compared to all others.

The results from this analysis suggest that employment growth in low-skilled occupations has been lower than that for all other occupations in recent years, after industry-specific effects on employment growth are taken into account (Chart 14). However, some caution is needed in the interpretation of the estimates, given the imprecision of the results.

Chart 14: Employment growth in low-skilled occupations relative to other occupations (net of industry effects)^{8*}



*Low-skilled occupations include Elementary clerical, sales and service workers and Labourers and related workers. A negative number means that employment in low-skilled occupations have grown relatively less rapidly than others.

Industries

Four industries – Accommodation, cafes and restaurants, Health and community services, Property and business services, and Retail trade – are estimated to account for around 70 per cent of all Pay Scale reliant employees.

Employment growth in some of these industries has been higher than the average for the economy as a whole, while growth in other relatively Pay Scale reliant industries has been lower (Table 7). Overall, employment growth in Retail trade and Health and community services has been strong recently. The number of people employed in the Accommodation, cafes and restaurants industry grew strongly in 2006-07, before declining in the second half of 2007 (Chart 15).

Generally, employment growth in low-skilled occupations has been slower than in each industry as a whole.

⁸ Confidence intervals are used to indicate the reliability of an estimate. It reflects the range of values within which the estimate can be asserted to lie, at a chosen confidence or probability level, as estimated from the data sample.

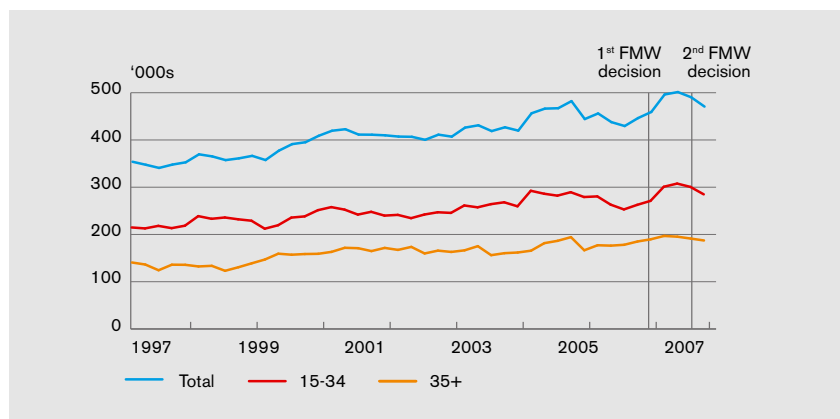
Table 7: Employment growth in Pay Scale reliant industries

Industry	Percentage of total Pay Scale reliant employees across all industries	Annualised growth rates			
		1-year	3-year	5-year	10-year
Accommodation, cafes and restaurants	14.0	0.0	-1.1	1.5	2.1
Low-skilled occupations*		-5.3	-3.7	-0.1	1.3
Health and community services	12.1	3.5	4.0	3.0	3.3
Low-skilled occupations		11.6	3.1	0.2	0.3
Property and business services	21.1	0.7	3.5	3.1	3.5
Low-skilled occupations		-5.6	-1.7	-0.9	1.7
Retail trade	22.2	6.4	2.3	2.2	2.2
Low-skilled occupations		3.1	0.6	-0.2	1.2
All industries	100.0	2.9	2.6	2.4	2.2
Low-skilled occupations		0.9	0.2	0.1	0.5

Source: ABS, *Labour Force Detailed*, Quarterly, November 2007, Catalogue No. 6291.0.55.003; ABS, Unpublished *Employee Earnings and Hours* data.

*Low-skilled occupations include Elementary clerical, sales and service workers and Labourers and related workers.

Chart 15: Employees in Accommodation, cafes and restaurants by age group*



Source: ABS, *Labour Force Detailed*, Quarterly, November 2007, Catalogue No. 6291.0.55.003.

*Data seasonally adjusted by AFPCS.

Predominantly low-skilled industries, such as Retail trade and Accommodation, cafes and restaurants, recorded some of the lowest annual growth rates in total hourly rates of pay over the year to the September quarter 2007, at 3.5 and 3.3 per cent, respectively. However, consistent with favourable labour market conditions, annual wage growth in these industries was high compared with growth over the past decade (Table 8). Similarly, while annual growth rates for wages of low-skilled occupational groups – particularly Elementary, clerical and service workers – were lower than for high-skilled occupations, they were also high relative to the past ten years.

There was a boost to wage growth for low-skilled industries and occupations in the March quarter 2007, the first quarter in which the Commission's Wage-Setting Decision 1/2006 took effect. Data for the period in which the Commission's Wage-Setting Decision 3/2007 came into effect are not expected until early 2008.

Table 8: Wage growth in low-skilled industries and occupations

	Annual percentage growth to September quarter 2007	Annualised percentage growth since September quarter 1997
Industries		
Accommodation, cafes and restaurants	3.3	2.8
Retail trade	3.5	2.9
Occupations		
Elementary clerical, sales and service workers	3.6	3.1
Labourers and related workers	4.2	3.3
Intermediate clerical, sales and service workers	3.9	3.4
All industries/occupations	4.2	3.6
Consumer Price Index	1.9	2.9
Underlying inflation*	3.0	2.6

Source: ABS, *Labour Price Index*, September quarter 2007, Catalogue No. 6345.0; ABS, *Consumer Price Index*, September quarter 2007, Catalogue No. 6401.0; RBA, *Bulletin*, November 2007.

*Underlying inflation refers to average of weighted median and trimmed mean measures.

Similar to the technique proposed for analysing employment growth by occupation, Access Economics suggested that the Commission monitor output in those industries that have a relatively high reliance on low-skilled labour and are, therefore, likely to be most affected by minimum wage decisions. Given that the wage bill for low-paying sectors tends to be relatively high, due to a large share of labour costs in total costs, an increase in real labour costs may lead to lower industry output compared with that in other industries.

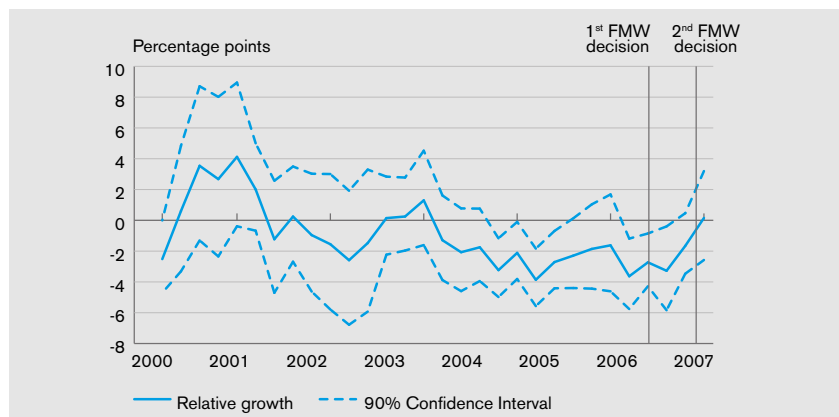
Output in the more sensitive industries appears to have been growing at slightly lower rates than output in other industries since 2003, after controlling for economy-wide shocks common to all industries (Chart 16). However, the relative growth rate of the sensitive industries appears to have improved in late 2007.⁹

Only in 2000 and 2001 did output in the sensitive industries grow at a faster rate than that of other industries, due to a combination of a downturn in Construction and stronger activity in Personal and other services and Property and business services. Since that time, sensitive industries have tended to grow more slowly than the remainder of the economy.

Following the Commission's Wage-Setting Decision 1/2006, economic activity in non-sensitive industries such as Construction and Mining has grown strongly. Nonetheless, recent annual changes in economic activity show a decline in Mining and relatively rapid growth in some of the sensitive industries, with Retail trade, Property and business services, Manufacturing and Personal and other services acting to narrow the gap in output growth rates over the past year.

⁹ Industries most sensitive to minimum wage decisions are identified based on an index number approach that combines AFPC coverage, labour cost and trade exposure into an 'all factor' index. The industries thus identified are Accommodation, cafes and restaurants, Manufacturing, Retail trade, Property and business services, Education, Health and community services, and Personal and other services. These industries account for 60 per cent of total employment in the economy.

Chart 16: Output growth in sensitive industries relative to other industries



Source: ABS, *National Accounts*, September quarter 2007, Catalogue No. 5206.0, AFPCS modelling.

Strong global demand for mineral and energy resources, combined with solid business investment in sensitive industries such as Manufacturing and Property and business services, are expected to continue in 2007-08 and 2008-09.¹⁰

Estimates of productivity growth vary widely between industries and within each industry. For example, annual labour productivity growth in the Retail trade industry increased from 1.7 per cent in 2005-06, to 4.6 per cent in 2006-07, while growth in the Accommodation, cafes and restaurants industry slowed from 7 per cent to -1.6 per cent.¹¹ Although the measurement of industry productivity is undergoing refinement, such estimates illustrate that the patterns of economic performance at an industry level are complex.

Conclusion

Previous trends in low-paid employment have continued over the past year. Education and occupation data suggest that growth in low-skilled employment has been a little weaker in recent years, particularly compared with the solid growth in high-skilled employment. However, participation rates have increased and unemployment rates have decreased for those demographic groups that contain a relatively high proportion of low-skilled workers.

Given the general trends in the labour market, it is difficult to determine whether changes in employment of low-skilled workers have been influenced by adjustments in the minimum wage and Pay Scales. Many factors determine employment for this group of workers, and the lack of detailed data at the workplace level precludes attempts to isolate the effects of minimum wages, for the time being. Nonetheless, there have been some positive trends in employment for low-skilled, Pay Scale reliant workers.

¹⁰ Australian Government, *Mid Year Economic and Fiscal Outlook 2007-08*, Canberra.

¹¹ ABS, *Australian National Accounts, 2006-07*, Catalogue No. 5204.0. Labour productivity is measured as gross value added per hour worked.

3. The safety net and work incentives

The income safety net in Australia comprises not only wages, but also income transfers through the social security system (pensions, benefits and family payments) and a range of tax subsidies. It is not uncommon for households to rely on a combination of these for their disposable income.

Accordingly, the strategy adopted by the Australian Fair Pay Commission (Commission) for monitoring the state of the safety net involves following movements in the real and relative value of wages, together with trends in the real and relative disposable incomes of households in receipt of minimum wages. Commission modelling of household disposable incomes also enables an assessment of trends in the financial incentives for jobless people to take up low-paid employment.

Real and relative values of the Federal Minimum Wage (FMW)

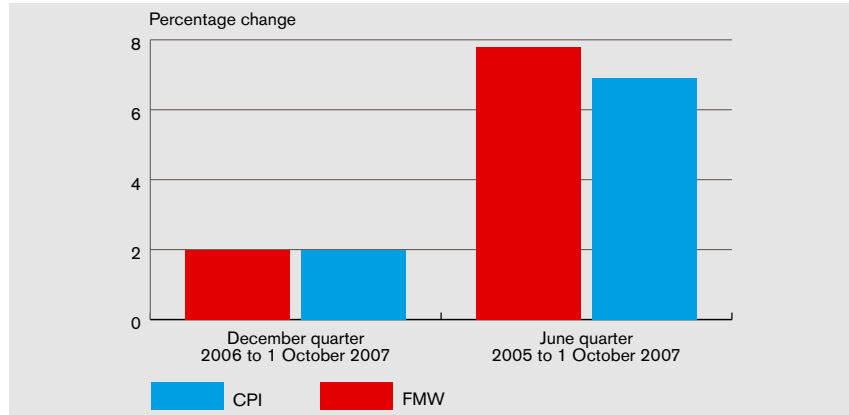
Estimates of the value of minimum wages adjusted for price inflation can reflect the extent of the safety net provided by minimum wages, the strength of work incentives and the incentive to enter into wage bargaining rather than rely on minimum wages.

The FMW increased by 2 per cent on 1 October 2007. This equalled the change in the CPI over the period since the Commission's Wage-Setting Decision 1/2006 (Chart 17).¹² The FMW has increased by 7.8 per cent since the June quarter 2005, a one percentage point increase in real terms.¹³ The real value of the FMW has increased by 10 per cent over the decade from the September quarter 1997 to October 2007, while the real value of some of the higher Pay Scale rates has decreased (Chart 18).

¹² The CPI is measured over the period from the December quarter 2006 to the September quarter 2007. The Commission's first general wage decision took effect on 1 December 2006 and its second general wage decision took effect on 1 October 2007.

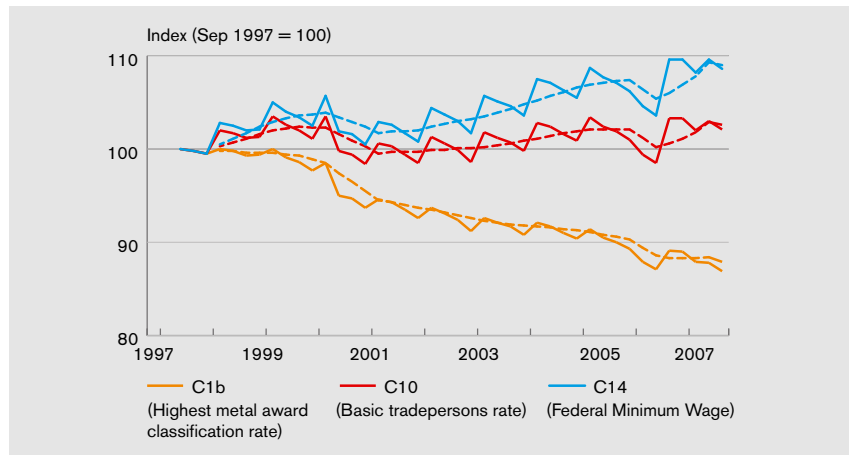
¹³ The CPI is measured over the period from the June quarter 2005 to the September quarter 2007. The Australian Industrial Relations Commission brought down its 2005 Safety Net Review decision on 7 June 2005.

Chart 17: Federal Minimum Wage and the Consumer Price Index*



Source: ABS, *Consumer Price Index*, September quarter 2007, Catalogue No. 6401.0; ABS, *Unpublished Employee Earnings and Hours* data.

Chart 18: Trend in the real value of selected Pay Scale rates*



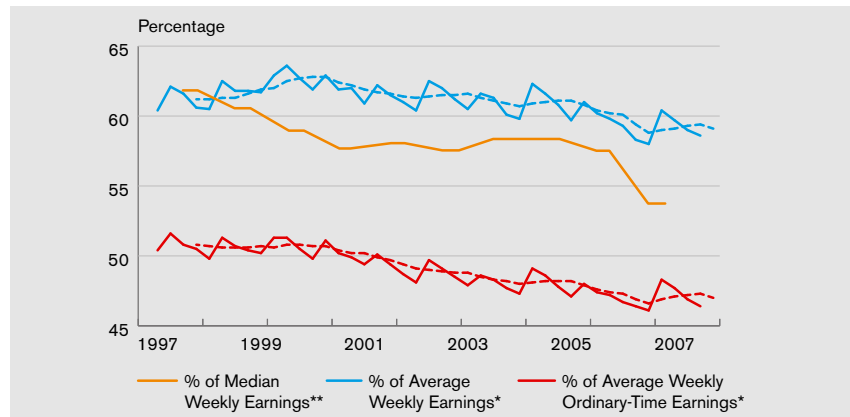
Source: ABS, *Consumer Price Index*, December quarter 2007, Catalogue No. 6401.0; Metal, Engineering and Associated Industries Award 1998.

*Pay Scale rates are measured at end of quarter, except for the September quarter 2007, which measures the Pay Scale rates as of 1 October 2007.

The FMW has declined relative to various measures of average and median earnings over the period since the June quarter 2005, consistent with longer-term trends. As at August 2007, the FMW was 46.4 per cent of average weekly ordinary-time earnings for full-time adult employees (AWOTE), compared with 48 per cent in the June quarter 2005 (Chart 19). Further, the FMW was 58.6 per cent of average weekly earnings for all employees, down from 61 per cent in the June quarter 2005.¹⁴ Although more recent average earnings data are not available, both ratios will have increased following the October 2007 adjustment to the FMW.

¹⁴ The FMW is measured at the end of the quarter, while AWOTE and AWE are measured in the middle of the quarter.

Chart 19: The FMW relative to average and median earnings



Source: ABS, *Average Weekly Earnings*, August 2007, Catalogue No. 6302.0; ABS, *Employee Earnings Benefits and Trade Union Membership*, August 2006, Catalogue No. 6310.0.

*Latest observation is August 2007.
 **Latest observation is August 2006.

Real disposable incomes

The income safety net afforded to low-paid workers is the net result of the interaction of wages, taxes and transfers. At a given level of wages, changes in tax/transfer parameters will affect the value of a person's disposable income and, hence, of the safety net.

Tax-transfer changes since July 2005

Between July 2005 and June 2006, there were no major changes made to the social security or taxation parameters applying to low-paid Australians. Over that period, households receiving a combination of wages and income transfers benefited from small regular indexed increases in those transfers.

From July 2006, the rate at which unemployment benefits and related payments are reduced for earned income was eased.¹⁵ These changes were particularly beneficial to people in substantial part-time work and for couples with one partner in low-paid work.

Tax liabilities of low-paid workers were reduced in both July 2006 and July 2007, through increases in:

- the maximum low income tax offset (LITO) from \$235 to \$600 and then to \$750, raising the effective tax threshold from \$7567 to \$11 000;
- the income threshold for the 30 per cent tax rate from \$21 600 to \$25 000 and then to \$30 000; and
- the dependent spouse tax offset from \$1655 to \$2100 (in July 2007).

¹⁵ For each additional dollar earned between \$142 and \$250 a fortnight, the unemployment benefit is now reduced by 50 cents, compared with 70 cents previously; and for income over \$250 a fortnight, the benefit is reduced by 60 cents for each dollar earned, compared with 70 cents previously. The taper rate applying to a partner's income was also reduced from 70 to 60 per cent for earnings above the partner income free area.

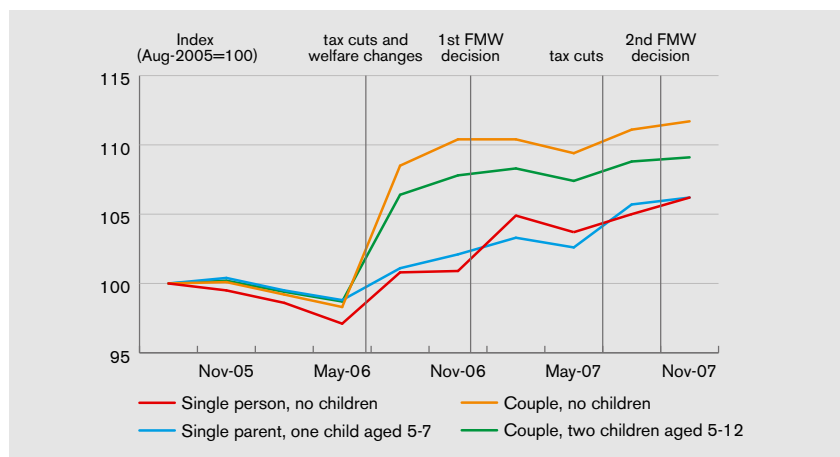
Trends in real disposable incomes of families with one earner on FMW

To monitor the value of the safety net for people earning the FMW, movements over time in the real value of their disposable income may be tracked.¹⁶ For illustrative purposes, four different types of household are considered, all with a single wage earner, who receives the FMW: (i) a single person with no children; (ii) a couple with no children; (iii) a single parent with one child aged 5-7; and (iv) a couple with two children aged 5-12.

Chart 20 indicates trends in real disposable income from August 2005, for these four family types. It shows that, in the period to June 2006, real disposable incomes declined slightly for all family types, in the absence of an increase in the FMW or significant changes to the tax/transfer system.

The July 2006 tax cuts and income support changes lifted real disposable income for all family types. Single people without children also benefited from the December 2006 minimum wage increase, whereas this had a smaller effect for couples and for single parents, due to their higher effective marginal tax rates. Disposable incomes for all family types also rose as a result of the July 2007 tax cuts and the October 2007 minimum wage increase.

Chart 20: Real household disposable income for selected families with one earner on the FMW



Sources: AFPCS modelling; ABS, *Consumer Price Index*, Catalogue No. 6401.0, various.
 Notes: Disposable incomes have been adjusted according to published changes in the CPI.

Overall, single FMW earners (with or without children) had real disposable incomes around 6 per cent higher in November 2007 than in August 2005. For couples with one FMW earner, the corresponding increase ranges from 9 to 11 per cent.

¹⁶ The disposable income figures that form the basis of the following analysis represent quarterly 'snapshots' of the interaction of wages, taxation and income transfers (as at February, May, August and November of each year). Some components of disposable income are derived from weekly amounts (for example, wages and income support payments), others represent the weekly equivalent value of annual amounts (for example, the low income tax offset and some components of family tax benefits). The modelling assumes that all available income transfers (income support payments, family tax benefits) are taken up and that the household is paying sufficient private rent to receive the maximum rate of rent assistance, where applicable.

Relativities with low income benchmarks

Relativities between the disposable incomes of people receiving the FMW and conventional low-income benchmarks may be monitored by comparing the disposable incomes of the four family types identified above, to the relevant Henderson Poverty Lines (HPLs).

Henderson Poverty Lines as indicators of low income

Henderson Poverty Lines first established by the Henderson poverty inquiry in 1973, are based on a benchmark income required to support the basic needs of a family of two adults and two dependent children. Poverty lines for other types of family are derived from the benchmark using a set of equivalence scales specific to the HPLs. While they have no official status, HPLs are commonly used in Australia as an indicator of low income.

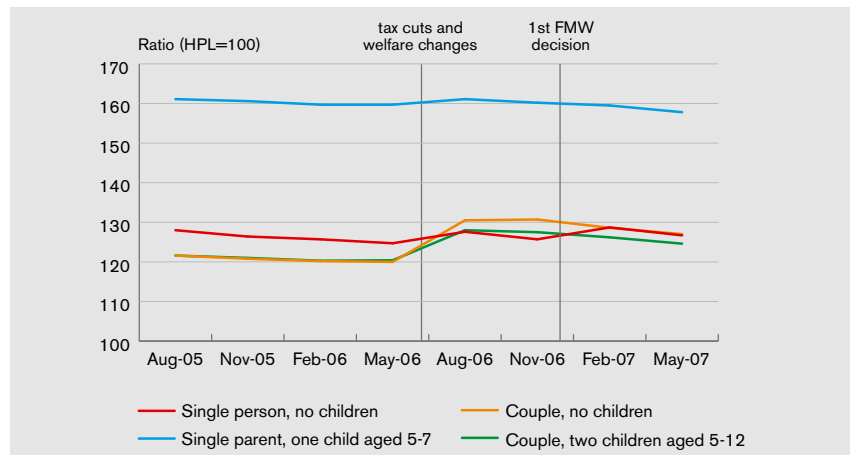
The poverty lines are updated each quarter using an index of per capita household disposable income derived from ABS income and population data. This means that changes in the HPLs can also be regarded as a proxy for movements in average community incomes.

Ratio of disposable incomes for families with one earner on FMW to HPL

As the proportion of households with more than one earner continues to increase, it might have been expected that households containing only one FMW earner would experience some decline in their disposable incomes relative to the HPLs.¹⁷ However, as Chart 21 shows, relativities between FMW-based household disposable incomes and HPLs have remained fairly stable over the period 2005 to 2007. Single people, with or without children, have experienced a slight decline, while couples, due to the changes to income support introduced in July 2006, have experienced a moderate increase.

¹⁷ Although the HPLs also assume a single wage earner, they are indexed to average per capita income, changes in which are affected by the increasing prevalence of families with more than one wage earner.

Chart 21: Household disposable income relative to the relevant Henderson Poverty Line for selected families with one earner on the FMW



Source: AFPCS modelling; Melbourne Institute of Applied Economic and Social Research, *Poverty Lines: Australia*, various.
 Note: Henderson Poverty Lines have not yet been released for the September 2007 and December 2007 Quarters.

Relationship with the overall distribution of household disposable income

Additional information on the relative standard of living of households reliant on the FMW can be obtained by examining their position within the distribution of household disposable income for the Australian population as a whole. However, unlike the quarterly HPLs, updated data on the distribution of household income are available only every two years, with a considerable lag (for example, income distribution data for 2005-06 have only recently been released).

In order to compare the incomes of households of different sizes and composition, nominal incomes are 'equivalised' by dividing the income of a given household with more than one member by an equivalence factor.¹⁸ Table 9 provides information on the nominal and equivalised disposable incomes of each of the four illustrative family types, along with their percentile ranking within the 2005-06 distribution of equivalised household disposable income.¹⁹ It also contains an estimate of percentile rankings following the income support and tax changes in July 2006 and implementation of the Commission's Wage-Setting Decision 1/2006 in December 2006.

¹⁸ While a number of equivalence scales are possible, the ABS uses the 'modified OECD' equivalence scale, which allocates values of 1.0 for the first person aged 15 or over, 0.5 for each additional person aged 15 or over and 0.3 for each child aged under 15. Thus, a couple with two children aged 5-12 has an equivalence factor of 2.1 and a single parent with one child aged 5-7 has an equivalence factor of 1.3.

¹⁹ The percentile ranking is the position that a person occupies on the overall distribution of equivalised household disposable income. A person with a ranking at the 25th percentile has an income higher than 25 per cent of the population and lower than the remaining 75 per cent.

Table 9: Nominal and equivalised weekly household disposable income and estimated percentile ranking for selected families with one earner on the FMW

Family type	December 05			December 06		
	Disposable income	Equivalised disposable income	Percentile ranking	Disposable income	Equivalised disposable income	Estimated percentile ranking
Single person, no children	413.19	413.19	30	450.34	450.34	32
Couple, no children	528.24	352.16	22	602.16	401.44	26
Single parent, one child 5-7	674.66	518.97	44	717.58	551.98	45
Couple, two children 5-12	742.67	353.65	22	829.42	394.96	25

Sources: AFPCS modelling; ABS, 2005-06 *Household Income and Income Distribution, Australia*, Catalogue No. 6523.0; Melbourne Institute of Applied Economic and Social Research, *Poverty Lines, Australia, December Quarter 2006*.

Note: Estimated percentile rankings for December 2006 are derived by inflating 2005-06 equivalent household disposable incomes by the rate of increase in household disposable income per head, but assuming no change in the shape of the income distribution.

Work incentives

Trends in work incentives are monitored by tracking the movement over time of three related indicators of the financial incentive for an unemployed person²⁰ to take up a full-time job at the FMW – the replacement rate, the net financial gain from moving into a job at the FMW, and the proportion of earnings retained after taking account of taxation and reductions in income transfers. These indicators are once again tracked for the four illustrative family types previously identified.

It is worth noting that financial indicators do not capture all the work incentives facing individuals – apart from financial incentives, a person's decision whether to work or not is influenced by other factors such as individual motivation and the preference for non-market activities.

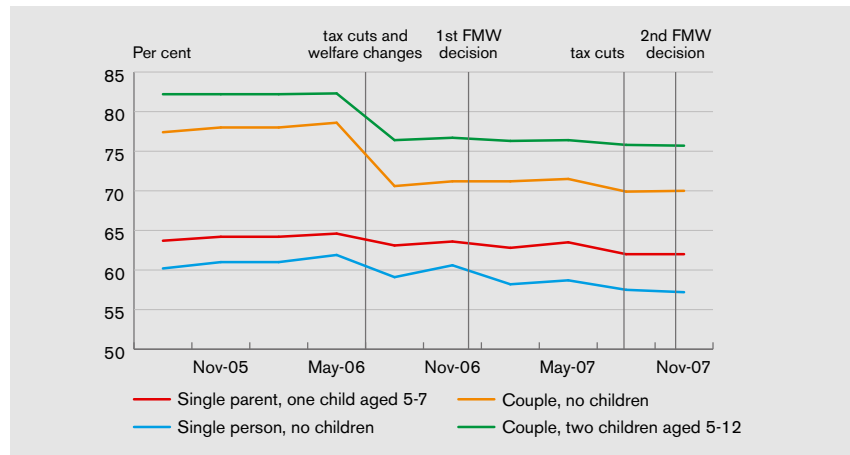
Replacement rates

The replacement rate measures disposable income when out of work and fully reliant on income support, as a proportion of disposable income when earning the FMW. It is a common assumption that people with higher replacement rates have lower financial incentives to work.

Chart 22 measures replacement rates for the four illustrative family types over the period August 2005 to November 2007. It shows that replacement rates tend to increase slightly between wage rises (for example, over the course of 2005-06) due to the regular indexed increases in income support taking place. However, following a peak in mid-2006, replacement rates have since fallen for all family types, due to the combination of tax cuts in July 2006 and 2007 and the July 2006 improvements in income support for working couples.

²⁰ Single parents with a youngest child under the age of eight qualify for the Parenting Payment (single), regardless of their labour force status. Their financial incentive to take up a job at the FMW, therefore, is calculated by reference to that payment, not based on the assumption that they are unemployed and receiving the NewStart Allowance.

Chart 22: Replacement rates for selected families with one earner on the FMW



Source: AFPCS modelling.

Notable among these trends:

- The reduction has been most pronounced for single-income couples without children, for whom the replacement rate has fallen from almost 79 per cent to 70 per cent.
- A single childless person now has a replacement rate about 5 percentage points lower than in May 2006, while the reduction has been more modest for single parents (around 2 percentage points).

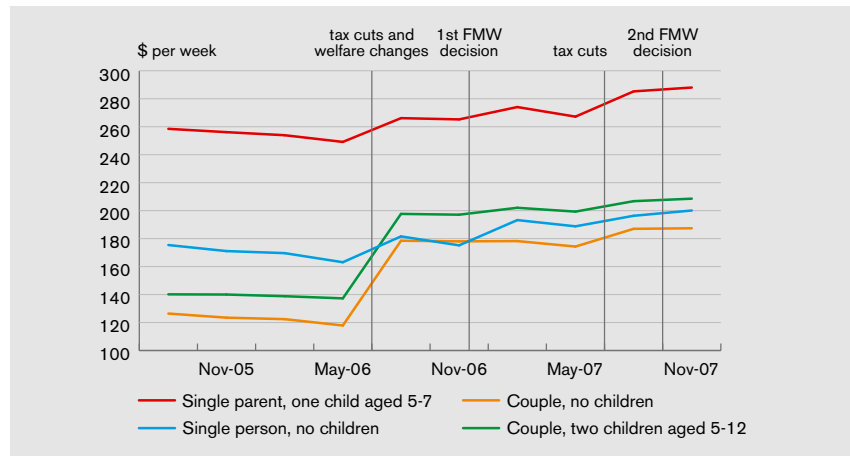
Most of the reductions in replacement rates are due to changes in the tax/transfer system. The December 2006 increase in the FMW had a significant effect only for the single person without children.

Net financial gain from taking up full-time work at the FMW

An alternative, simpler, perspective on the financial incentive to take a full-time job at the FMW is provided by the net absolute financial gain that a person would secure by taking up such a job. This indicator measures the dollar value of the difference between a person or household's disposable income in FMW employment and their disposable income when out of work and receiving income support payments.

Chart 23 illustrates trends in the net financial gain from moving from no work into a job paying the FMW over the period July 2005 to November 2007. The figures represent current (November 2007) values, with earlier figures adjusted for CPI inflation.

Chart 23: Real net financial gain from taking up a full-time job at the FMW for selected families



Source: AFPCS modelling; ABS, *Consumer Price Index, Australia*, Catalogue No. 6401.0, various.
 Note: Figures have been adjusted for CPI changes published by ABS.

Mirroring the trends in replacement rates, all family types have experienced some increase in the net financial gain that they can expect from taking up a job at the FMW. For single people with or without children, the increase has been relatively modest (around \$25 to \$30 a week in real terms), while the net financial gain for couples is around \$60 to \$70 a week higher than in August 2005.

The differences between replacement rates for single people and couples are quite large because the amount of available income transfers both in and out of work varies with family size. By contrast, the differences in net financial returns depend largely on the form of income support available when out of work. The single parent illustrated here gains much more from taking up a job, due to a relatively generous income test, while the other family types experience lower, more similar, gains.²¹ Another contrast with replacement rates is that this indicator of work incentives is more positive for people with children than for people without children.

Net proportion of earnings retained

A third perspective on work incentives is provided by the proportion of a person's earnings that is effectively retained after taking account of taxation liabilities and reductions in income transfers. This is arrived at by dividing the increase in disposable income (net financial gain) by the increase in gross earnings (in this case, the FMW). This indicator is closely related to the Effective Tax Rate (ETR), which measures the proportion of extra earnings effectively lost to taxation and reductions in income transfers.

²¹ Single parents with a youngest child under 8, and those with a youngest child aged 8-15 who were already on payment before 1 July 2006 are eligible for parenting payment (single), which is equivalent to the age pension. By contrast, single childless people, some single parents with older children and couples with and without children are generally eligible for much less generous unemployment benefits or the related parenting payment (partnered).

Table 10 summarises the net proportion of earnings retained by each of the four family types at four different points in time:

- in August 2005, just after the last Safety Net Review decision of the Australian Industrial Relations Commission;
- in August 2006, after the tax/transfer changes that took place in July 2006 and before the Australian Fair Pay Commission's first minimum wage decision;
- in February 2007, after the Australian Fair Pay Commission's first minimum wage decision; and
- in November 2007, after the Australian Fair Pay Commission's latest minimum wage decision.

Table 10: Net proportion (%) of earnings retained on moving into FMW employment

Family type	August 05	August 06	February 07	November 07
Single person, no children	34	37	37	38
Single parent, one child 5-7	50	54	52	55
Couple, no children	24	36	34	36
Couple, two children 5-12	27	40	38	40

Source: AFPCS modelling.

Here also, the biggest boost to the proportion of earnings retained accrued to couples, as a result of the income support changes in July 2006. For single people, the proportion of earnings retained has risen modestly relative to August 2005, largely as a result of tax cuts.

The single parent with one child aged 5-7 consistently retains a larger proportion of earnings than the other family types, due to the more generous treatment of earnings under the pension income test.

Conclusion

The real value of the FMW has increased over the period since the final Safety Net Review decision by the Australian Industrial Relations Commission. Moreover, there has been a sustained increase in the real value of the overall income safety net for minimum-wage workers since mid-2006, due in large part to improvements in the tax/transfer system, but also to the Commission's first two minimum wage decisions.

Single-earner couples on the FMW have improved their disposable income position, relative to both the HPLs and the overall distribution of equivalised household disposable income. The disposable incomes of FMW earners who are single, have broadly maintained their relative value, due to the combination of minimum wage increases and recent tax cuts.

The available evidence indicates that the improvement in the disposable incomes of FMW households have been accompanied by an improvement in the financial incentive for jobless people to take up FMW employment. All of the indicators of work incentives (replacement rates, net financial gain and proportion of earnings retained) show continuing improvement, relative to their levels in 2005-06.



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