Trade Union
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OECD policy brief argues there is room to raise minimum wages

A recent OECD publication ('Minimum wages in times of rising inflation', December 2022) discusses how minimum wages can help shield the most vulnerable, low-income households from high inflation. Alongside negotiations with and between social partners to protect the purchasing power of a large share of workers in the lower and middle range of wage distribution, the OECD policy brief advocates using the minimum wage as one of the tools to help preserve the living standards of low-paid workers.

The brief argues that several countries can go beyond their current minimum wage levels and protect, at least in part, the most vulnerable workers from rising prices. The OECD does not explicitly identify the margins, but the brief contains several data points and arguments that support the idea. This TUAC paper details three margins which would allow several OECD economies to increase their minimum wage.

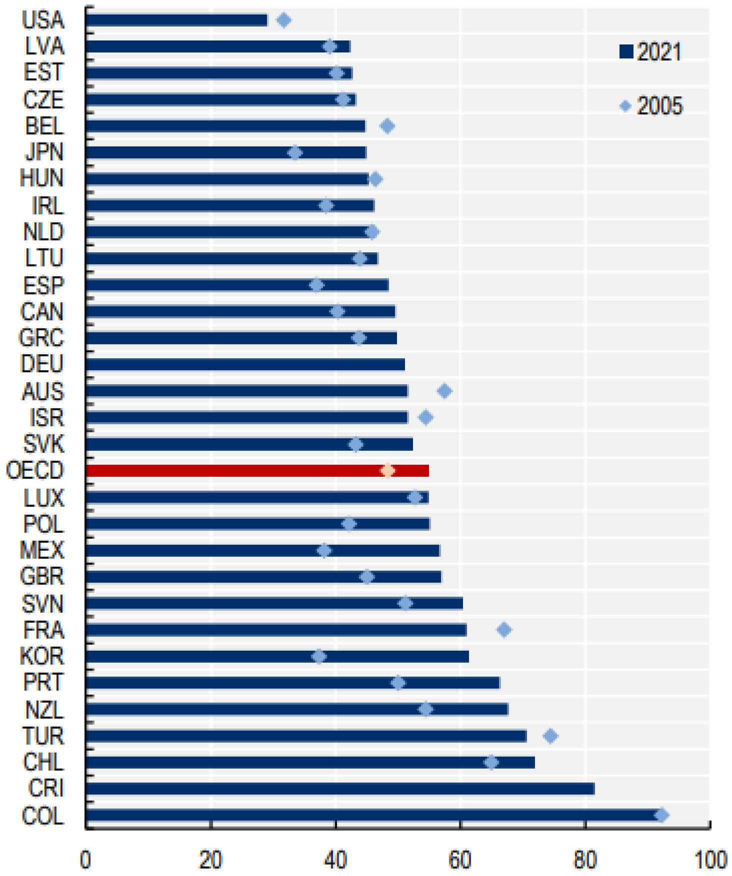
Many countries have below average minimum wage

Expressing minimum wage as a percentage of the median wage (the 'Kaitz index') allows for comparison between countries and suggests the extent to which minimum wages can help ensure an acceptable standard of living. With this indicator, the OECD calculates that of the 30 OECD countries with a statutory minimum wage, the average (unweighted) minimum wage equates to 54% of the median wage, up from 48% in 2005 (see graph I).

A majority of OECD countries (17 out of 30) have a minimum wage below this OECD average. The United States, where the federal minimum wage was last updated in 2008, ranks bottom of the list with a minimum wage no higher than 29% of the median wage. Above the US is a range of primarily European countries (Latvia, Estonia, Czech Republic, Hungary, Belgium, Ireland, Netherlands, Spain) and Japan, where minimum wages range between 40 and 45% of the median wage.

The OECD average of 54% provides a point of reference that shows which countries have a relatively low minimum wage and who could therefore consider raising it to protect minimum wage workers from high inflation.

Graph I: Statutory minimum wages: % of median wage of fulltime workers



Source: OECD Policy Brief

From minimum gross wages to minimum labour costs

The minimum wage ratios described above are based on *gross* wages (the *gross* minimum wage as a percentage of the *gross* median wage). Gross wages do not reflect the total labour cost, as this also includes employer social security contributions.

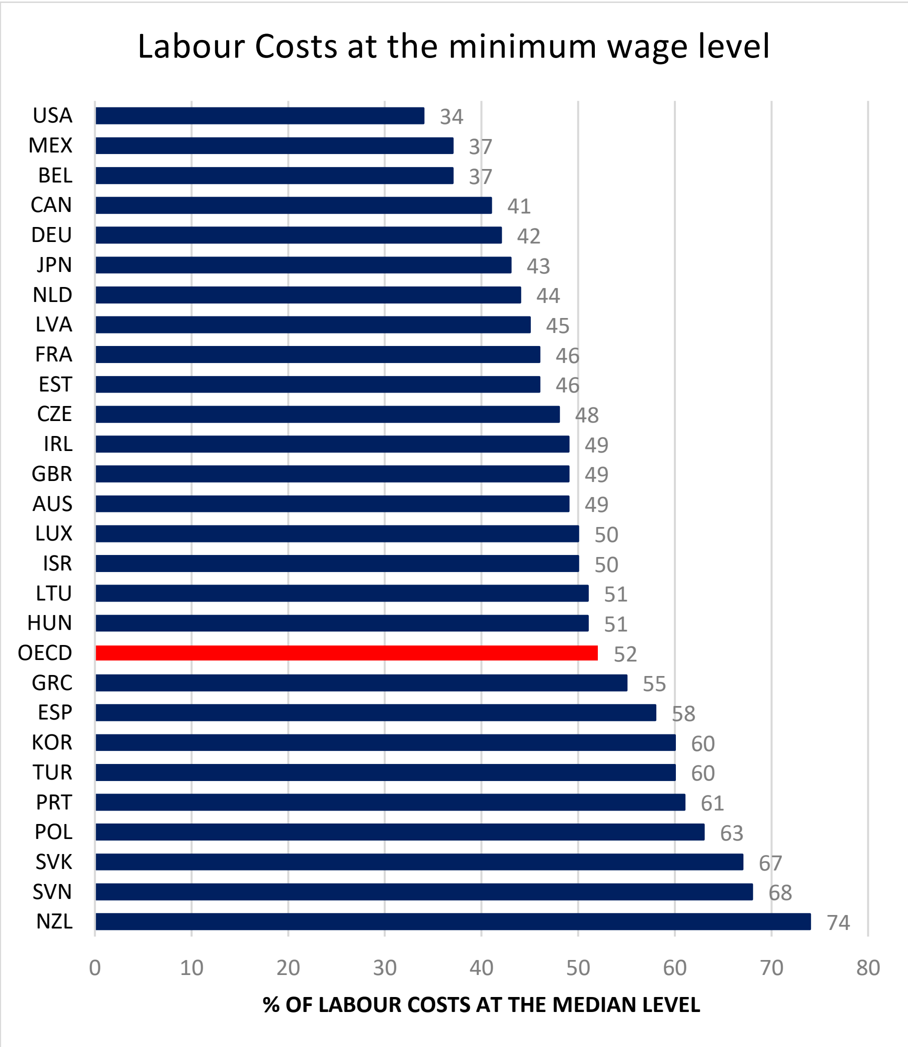
Employer social contributions, however, do not always take the form of a fixed rate to be levied on all wages. In the US and Spain for example, the gross wage upon which employer contributions are calculated is capped. Other countries, such as France and Belgium, give employers large discounts on social security contributions for workers who are paid the minimum wage or close to it.

This indicates that the ratio of the minimum wage to the median wage in terms of total labour cost will be different to that for gross wages.

What happens when the total labour cost of the minimum wage is calculated for countries where employers benefit from reduced social charges for minimum wage workers ? In those instances, the amount that is added to the gross minimum wage in the nominator is proportionally less than the full charge of social contributions added to the gross median wage in the denominator. The discrepancy between the changes in the nominator and denominator results in a minimum labour cost ratio that is below the minimum gross wages ratio.

Using OECD figures on "minimum labour costs' therefore results in a very different picture (Graph II). Several countries where employers, based on the *gross* wage comparison, pay a relative minimum wage much higher than the OECD average now fall in the rankings, ending up below the OECD average. Mexico, for example, tumbles from a *gross* minimum wage of 57% to a minimum *labour cost* of 37%, the second lowest in the OECD. France, by *gross wage* comparison, has one of the highest minimum wage ratios of the OECD (61%) but now joins other European countries in having a modest minimum *labour cost,* around 46% of the median. The UK also experiences a large downward turn in the value of the two indicators (from 57% of the *gross* minimum wage to 49% of the minimum *labour cost*). Meanwhile, Belgium, a country that was already low ranking in terms of *gross* minimum wages (44%) now ends up near the bottom of the table with a (relative) labour cost for minimum wage workers of just 37%. This is only slightly higher than that of the US (34%) and on a par with Mexico.

Graph II: Minimum labour costs as a share of median labour costs



Source: OECD data

This policy of subsidising low wage employers by reducing their social security contributions is aimed at ensuring jobs are available for lower skilled workers. However, it also raises the question of whether the policy does indeed safeguard low paid jobs, or simply supports low wage employers with minimal effect on jobs. With the OECD policy brief claiming that "at the level set in most OECD countries, minimum wage increases (even large ones) have had a positive effect on low incomes but no or limited negative effects on employment", doubts can be raised as to whether compressing social charges for low wages does in fact lead to higher job availability; if higher minimum wages do not cause job cuts, then it is unlikely that lowering the labour cost of minimum wage workers will create jobs.

Since low wage employers in countries with discounted social charges face moderate to very low labour costs for minimum wage workers and given the doubt as to the negative jobs impact of minimum wages, there is room to manoeuvre. Public resources currently going to low wage employers can be shifted to improve the purchasing power of low wage workers themselves. This can be done by raising the gross minimum wage, while keeping discounts on employer social charges at the same level. Alternatively, it can be done by reducing employers' discounts and cutting taxes for low wage earners.

Median wages have lagged productivity growth for several decades

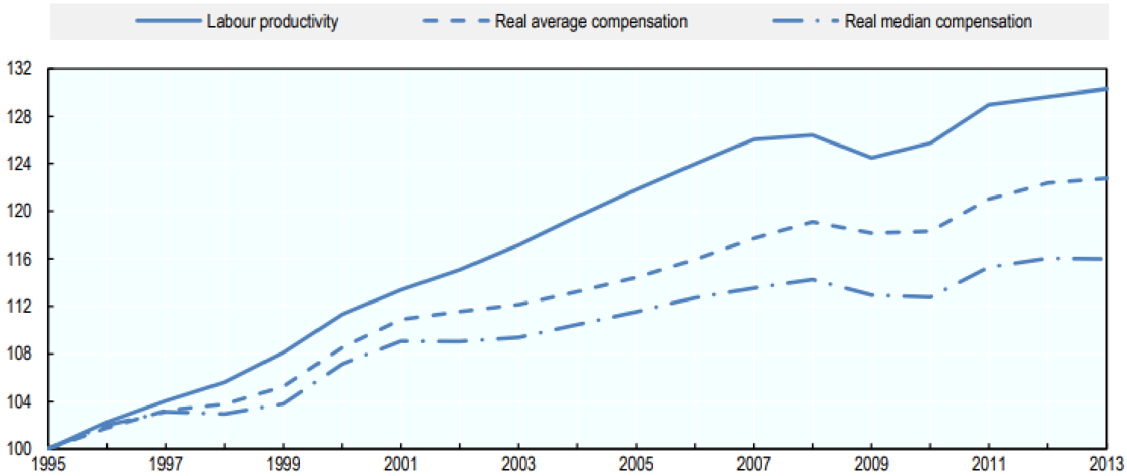
A third margin is indirectly referenced in the OECD policy brief, in its statement that minimum wages across the OECD were raised between 2005 and 2021, "in a context of modest overall wage growth"[1]

Previous OECD work shows that median wage growth has systematically been lagging behind productivity developments in recent decades (graph III).

[1] See page 2 of OECD policy brief

Graph III: Median wages decoupling from labour productivity

Total economy excluding primary, housing and non-market industries, 1995=100



Note: Employment weighted average of 24 countries (two-year moving averages ending in the indicated years). 1995-2013 for Finland, Germany, Japan, Korea, United States; 1995-2012 for France, Italy, Sweden; 1996-2013 for Austria, Belgium; United Kingdom; 1996-2012 for Australia, Spain; 1997-2013 for Czech Republic, Denmark, Hungary; 1997-2012 for Poland; 1996-2010 for Netherlands; 1998-2013 for Norway; 1998-2012 for Canada, New Zealand; 1999-2013 for Ireland; 2002-11 for Israel; 2003-13 for Slovak Republic. All series are deflated by the value added price index excluding the primary, housing and non-market industries. The industries excluded are the following (ISIC rev. 4 classification): (1) Agriculture, Forestry and Fishing (A), (2) Mining and quarrying (B), (3) Real estate activities (L), (4) Public administration and defence, compulsory social security (O), (5) Education (P), (6) Human health and social work activities (Q), (7) Activities of households as employers (T), and (8) Activities of extraterritorial organisations and bodies (U).
Source: OECD (2018[5]), “Decoupling of wages from productivity: What implications for public policies?”, in *OECD Economic Outlook, Volume 2018 Issue 2*, https://doi.org/10.1787/eco_outlook-v2018-2-en.

StatLink http://dx.doi.org/10.1787/888933880964

This decoupling implies that expressing the minimum wage as a percentage of the median wage distorts the comparison between wages and productivity. A minimum wage that is 60% of a median wage, but which has been falling in relative terms compared to productivity growth for several years, can no longer be thought of as still being aligned with 60% of the labour productivity performance that is representative for the country; the true figure is far lower. This in turn casts further doubt on the suggestion that increasing minimum wages, by imposing a wage floor that exceeds some of the productivity levels that labour can deliver, endangers employment.

Policy makers also need to take this factor into account when deciding to increase minimum wages and shield low-income workers from the cost-of-living crisis.

Final remark

Besides the message that there is room for several OECD countries to raise minimum wages amid the cost-of-living crisis, the OECD policy brief also documents the difficulties that minimum wages have in keeping up with soaring inflation. Here however, the OECD policy message is somewhat ambiguous. On one hand, the paper does underline the importance of ensuring regular adjustments of statutory minimum wages. Yet on the other, it refrains from calling for an indexation of minimum wages, despite referencing research from US states which found that indexation (as opposed to discretionary increases) has the benefit of making minimum wage rates more predictable and lowers non-compliance in the payment of minimum wages[2].

[2] See page 8 of OECD policy brief