



Global Wage Debates

Politics or Economics?

Edited by Gregory Randolph and Knut Panknin

September 2015



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FOREWORD

Six years into the worst global economic crisis since the Great Depression, recovery continues to be sluggish and uneven across the globe. Policymakers are focused on reviving economic growth and job creation, but it is sustained and decent wage growth that would be a true sign of success.

Good wages are as economically wise as they are socially just. Wage increases – especially at the bottom – help reduce inequality, which is now widely acknowledged as harmful to economic growth. They fuel consumption that boosts aggregate demand. New research shows that when multiple countries pursue wage moderation to boost their competitiveness at the same time, the result is depressed demand, increased inequality and stunted growth.

Successful wage regimes must include a minimum wage that serves as a floor to ensure that all workers can afford to meet their basic needs. They must also provide compensation ladders, established through sound industrial relations and collective bargaining, in which wage growth is aligned with productivity and prices. Finally, they must have measures to ensure equal pay for equal work.

Wages are central to the JustJobs Network's engagement with policymakers, business leaders, and civil society to help define a new kind of economic growth – one that puts people first, recognizes the value of work and fosters the creation of just and equitable societies.

The balance between equality and efficiency has been a pervasive theme in economics, brought front and center through Arthur Okun's forceful arguments forty years ago. The present volume pulls together international experts – from the United States and Brazil to Indonesia and India – to reexamine the politics and economics of this balance through the lens of wages.

By drawing on specific examples of wage mechanisms at play, it highlights what has worked and what has not. I expect the volume you hold in your hands to play an important role in furthering dialogue and policymaking around wages, jobs and economic growth.



Sabina Dewan
President & Executive Director
JustJobs Network

INTRODUCTION

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INTRODUCTION

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The dual imperative

From advanced economies like the United States and Germany to emerging markets like Indonesia and South Africa, policy debates are increasingly focused on how to tackle growing income inequality. Wages are at the heart of the question of how to create more equitable economic growth. Policymakers, employers, and workers are all engaged in a complex tug-of-war to determine the best way for wage levels to meet the needs of families, societies and economies.

Boosting wages is not only a social imperative – a prerequisite for giving more people more opportunity and mobility. It is also an economic imperative. Anemic aggregate demand is part of the reason the post-crisis recovery has been so sluggish. A rise in wage levels across the globe can benefit the private sector as well as workers and governments. To assume that there is a trade-off

between high wages and competitiveness does a disservice to all three.

In particular contexts and circumstances – some of which this volume will explore – high wages *do* come at the cost of efficiency and growth. But it is more often the case that higher wages strengthen economies. In short, giving people – women and men – more and equal opportunity through higher wages also gives businesses new consumers, allowing them to grow and thrive.

The subject of debate and research should not be whether high wages are good or bad, but rather which pathways to better wages are the most viable and sustainable. The authors of this volume share evidence from their respective countries to add value to this conversation.

Anemic aggregate demand is part of the reason the post-crisis recovery has been so sluggish. A rise in wage levels across the globe can benefit the private sector as well as workers and governments.

The growing importance of wages

Wage debates have taken center stage partly because wage labor is an increasingly important source of income for workers throughout the world.¹ Economies across the globe are witnessing two transitions: one within agriculture – from smallholder to commercial farms – and one from employment in agriculture to employment in industry and services. Both transitions mean that an increasing number of workers are dependent on wage labor to meet theirs and their families' basic needs and fulfill their aspirations.

Wage labor is important not only for basic economic survival but also as a pathway out of poverty.² However, “escaping poverty” cannot be conflated with “joining the middle class.” Recent research shows that the notion of a “global” middle class – consisting of households across both industrialized and emerging economies – is more aspiration than reality. Only 13 percent of the world’s middle class lives outside advanced economies – and this figure changed little between 2001 and 2011.³

Wage labor is important not only for basic economic survival but also as a pathway out of poverty. However, “escaping poverty” cannot be conflated with “joining the middle class.”

The majority of the world’s population, 56 percent, is low-income – earning between two and 10 U.S. dollars per day.⁴ This population overlaps significantly with the workers who are transitioning from non-wage subsistence agriculture to working as wage laborers. A demographic of 3.4 billion people, they may not be considered poor in official statistics, but they are a single medical emergency or bad harvest away from falling back into poverty. They need higher wages and stronger safety nets to make the exit from poverty permanent.

In other words, a global effort to boost wages would ensure that those who have transitioned out of poverty continue to experience economic mobility. It would also ensure that the investors and private sector players who have staked their hopes for growth on a global middle class see their positive projections pan out.

The five themes of this volume

1. Politics – rather than social or economic concerns – often drive statutory wage setting.

The debate over statutory minimum wages is usually framed as a compromise between social concerns – workers' welfare – and economic concerns – competitiveness and the needs of business. But oftentimes, neither is the primary concern motivating governments. Instead, political expediency – the need for governments to appease certain constituencies or to win favor with their own internal factions – determines how and the level at which minimum wages are set.

Minimum wage legislation generally outlines a highly rational approach to wage setting – weighing the needs of different stakeholders and taking into account objective criteria like cost of living and economic growth. Yet governments are inclined to flout those approaches in favor of short-term political interest.

One way of tackling this unhealthy politicization of wage setting is to introduce a more rigid formula, as Brazil did by linking minimum wage growth to economic growth and inflation. As the chapter on Brazil will explore, however, this inflexible formula comes with its own perils.

2. Where minimum wages are supplanting collective bargaining, it is to the detriment of both workers and employers.

In a healthy industrial relations system, a statutory minimum wage acts as an absolute compensation floor; it is intended to protect the most vulnerable workers and new hires. As a complement, collective bargaining should help create a compensation ladder that extends far higher than the statutory minimum.

Yet in many countries – particularly in labor-intensive sectors like garments – advocating for a higher minimum wage has become the only instrument workers have to improve their remuneration.

The consequences here are crucial – for both employers and employees. When minimum wage is the only vehicle through which workers can demand higher compensation, employers lose the ability to design a compensation structure that is correlated with experience, skill, and productivity levels. The wage scale gets compressed, with average wage hovering close to the statutory minimum.

In other words, the minimum starts to act like a maximum. With little opportunity for upward mobility, employees lose the incentive to sharpen their skills or become more productive. Both workers and businesses lose.

3. Wage increases and productivity gains must be aligned.

In some contexts, despite growing labor productivity, wages remain stagnant. When productivity gains do not feed back into fair compensation for workers, inequality grows.

The reverse – increasing wages with minimal productivity growth – can also endanger workers' livelihoods. Wage hikes unaccompanied by gains in worker productivity are unsustainable.

Companies compelled to pay higher wages can only offset those costs if the relationship between wage growth and productivity growth stays relatively stable in the long run; otherwise they will eventually be forced to reduce production and lay off workers. This risk runs especially high when wage hikes are steep and rapid.

For this reason, governments must devote equal attention to investing in their workforces through skill development and improvements in health services and education – all of which impact workers' productivity. Moreover, policymakers should seek to implement minimum wage

increases gradually, so that employers have the time to make productivity-enhancing investments in their workers.

4. Decentralized wage setting enables higher local minimums, but may exacerbate regional disparities.

In many countries, both national and local governments have the authority to set minimum wages. In other contexts, national governments have completely devolved this responsibility to provincial and state governments.

This sort of decentralization can come with clear benefits. Localities where the cost of living is especially high can set wages consistent with what workers need to meet their basic needs. In the United States, for instance, where the national government is gridlocked on the subject of minimum wage, 29 out of 50 states have set a wage floor higher than the national minimum wage.

But decentralization of wage setting can also be problematic. For one, it can enhance regional inequalities. In China for example, coastal cities have raised their minimum wages much faster than the less developed inland districts. As a result, the per capita income gap between regions has grown. Brazil, by contrast, has managed to reduce inequality between regions by instituting a national minimum wage.

5. Tight labor markets help raise wages, but may not address wage inequality.

When labor markets “tighten” – in other words, when the demand for labor rises faster than the supply – one result is a boost to wages. Employers must offer better incentives to compete for workers. This is true for individual sectors as well as entire economies. On the other hand, a “slack” labor market depresses wages. In other words, job creation is itself a strategy for promoting wage growth.

However, upward pressure on wages does not necessarily address another social and economic concern – inequality. A “tightening” labor market pulls up wages across the board, but it does not necessarily tackle wage disparities. For example, it does not cause a convergence between the wages of men and women. Therefore, while job creation itself can work as a strategy to boost wages, it cannot alone empower workers who are marginalized in the labor market or address persistent pay gaps that result from structural inequality.

The structure of this volume

Impact of wage policies

Chapters one through four of this volume are empirical examinations of different wage policies across the world. Chapter one analyzes Brazil’s dynamic minimum wage policy – where a national wage floor is mandated by law to grow proportionate to the rate of inflation and Gross Domestic Product (GDP) growth. It illustrates the policy’s positive impact on wage inequality while also exploring its connection to Brazil’s current economic woes.

Chapter two takes up minimum wage policies in the United States, looking at the impact of local and state-level statutory wage floors that are growing in importance as the real value of the national minimum declines. The authors of chapter three explicate the nuances of minimum wage setting in China, looking at how the steady increases in China’s local wage floors have impacted women, migrant workers and other marginalized groups. Finally, chapter four presents the mixed outcomes of minimum wage policies in South Africa.

Collective bargaining and minimum wages

Chapters five through seven all deal with the nexus of collective bargaining and minimum wages. Chapter five examines how the proliferation of unions in Reformation Era Indonesia – along with the decentralization of governing authority – has shifted the political dynamic in minimum wage setting. Chapter six describes the turbulent journey of the German labor movement in arriving at unified support for a nationwide minimum wage, exploring unions' concern that a minimum wage might erode the strength of collective bargaining.

Chapter seven shines a spotlight on the industry where the most heated wage debates are taking place – the garment sector. It examines key wage developments across five major garment exporters – Bangladesh, Cambodia, Myanmar, Pakistan and Vietnam – and describes the evolving role of trade unions in wage setting processes.

Wages in agriculture and the informal economy

Chapter eight looks at persistent pay gaps between men and women in India's agricultural sector, asking why men's out-migration from farm-based work into jobs in industry and services has not translated into fairer wage outcomes for women in agriculture. A special feature following chapter eight highlights an innovative skills training program in India aimed at boosting the incomes of informal construction workers.

Proposing and assessing new wage strategies

The final two chapters of this volume map new frontiers in the global debate on wages. Chapter nine examines the emerging idea of a European Union-wide minimum wage. Chapter ten outlines a strategy that major private sector players are deploying to promote fair compensation and commit to paying more than just the statutory minimum.

Endnotes

¹ Bernd Mueller and Man-Kwun Chan. 2015. Wage Labor, Agriculture-Based Economies, and Pathways out of Poverty: Taking Stock of the Evidence. (Washington DC: USAID). Accessed on August 15, 2015. <https://www.microlinks.org/library/wage-labor-agriculture-based-economies-and-pathways-out-poverty-taking-stock-evidence>

² *ibid.*

³ Rakesh Kochhar. 2015. A Global Middle Class Is More Promise than Reality. (Washington DC: Pew Research Center). Accessed on August 15, 2015. <http://www.pew-global.org/2015/07/08/a-global-middle-class-is-more-promise-than-reality/>

⁴ *ibid.*

MINIMUM WAGE IN BRAZIL

A useful policy tool to reduce wage inequality?

Alexandre de Freitas Barbosa, Maria Cristina Cacciamali, Gerry Rodgers and Fabio Tatei

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Canada

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The project received financial support from IDRC.



BRAZIL



5.9

Unemployment Rate



52.7

GINI



66.4

Wage and salaried
workers, total (% of
total employed)



13557

GDP per person
employed
(constant 1990 PPP \$)

MINIMUM WAGE IN BRAZIL

A useful policy tool to reduce wage inequality?

Alexandre de Freitas Barbosa, Maria Cristina Cacciamali, Gerry Rodgers and Fabio Tatei

Introduction

What role did a rising minimum wage play in reducing wage inequality in Brazil in the first decade of the 21st century? Is it reasonable to expect that the policy of tying minimum wage to economic growth will continue to act as a key driver of inequality reduction in the near future?

In order to answer these questions, this chapter is structured as follows: The first part presents the broad macroeconomic situation, with a focus on productivity and labor market outcomes, pointing out the main features of the Brazilian growth modelⁱ as well as its main challenges.

The second part looks at how the country's active minimum wage policy fueled the rise in the real value of Brazil's minimum wage over time. This section further discusses the importance of this policy for different types of wage workers –

registered and non-registered, urban and rural – and the changing relationship between minimum wage and average wages.ⁱⁱ

Third, the chapter shows how income inequality decreased across sectors, regions and social groups – including sex, race/color and levels of education. The authors use the Theil indexⁱⁱⁱ to look at the reduction in inequality across these different variables, while also examining how the average wage ratios between non-registered and registered wage earners changed.

Finally, the last section discusses how trends in wage inequality are likely to evolve in the near future, especially considering that Brazil has been confronting an economic downturn over the last two years.

i One could also use the term “growth regime.” This concept, borrowed from the French school of regulation theory, was developed for a comparative analysis between Brazil and India. See CEBRAP/IHD. 2015a. Growth regimes, labour markets and inequality in Brazil and India: parallel experiences in historical perspective, mimeo.

ii The ratio of minimum wage to average wage is known as the Kaitz index.

iii The Theil index measures inequality. Like the Gini coefficient, an index of 0 indicates perfect equality (everyone earns the exact same), while an index of 1 indicates perfect inequality (one person has all the income).

The Brazilian growth model, labor productivity and the labor market

In the 2000s, Brazil experienced a virtuous cycle of economic growth that involved a decline in poverty and the reduction of income inequality. These trends, unprecedented in Brazilian history, were the result of several factors, such as high levels of GDP growth, the expansion of formal employment, a steady increase in the real minimum wage, and the expansion of income transfer programs.

This virtuous cycle was interrupted by the 2008 global financial crisis. Brazil reacted fast with counter-cyclical policies – such rising public loans, fiscal incentives and public expenditures both in investments and social transfers.¹ As a result, Brazil managed to shield its economy from some of the most severe effects of the crisis, and GDP growth jumped to 7.6 percent in 2010. But in the years following, growth slowed to around 2 percent per year. In 2014 the economy was stagnant and the country is bracing for a recession in 2015 (**Figure 1**). Rising unemployment, destruction of formal jobs and falling wages plague Brazil's labor market today.

The investment rate has fluctuated much less. Even during the high-growth years it rose only from 16.8 percent in 2000 to 19.5 percent in 2010, and

it then declined due to the international financial crisis and the short-term effect of the counter-cyclical policies. This is key to understanding the low productivity growth of the past decade. Low investment meant that Brazil neither moved toward higher productivity sectors nor was able to create new productive capacity to go beyond domestic demand as a source of growth.

Some factors already present in the high-growth first decade of the 21st century have come to threaten the sustainability of growth in the current decade. The most important factor is the low rate of productivity growth in a period of relatively high GDP growth. This is partly related to the poor performance of the investment rate and partly to the fact that manufacturing goods from abroad flooded the domestic market, even before the financial crisis. Partly driven by Brazil's overvalued currency, imports from the United States, the EU and China rose, discouraging domestic production and its modernization.

Domestic and foreign demand boosted Brazilian economic growth in the 2000s. Growing demand for commodities, particularly from China, drove an increase in both the prices and volume of Brazil's exports of primary products. This generated a

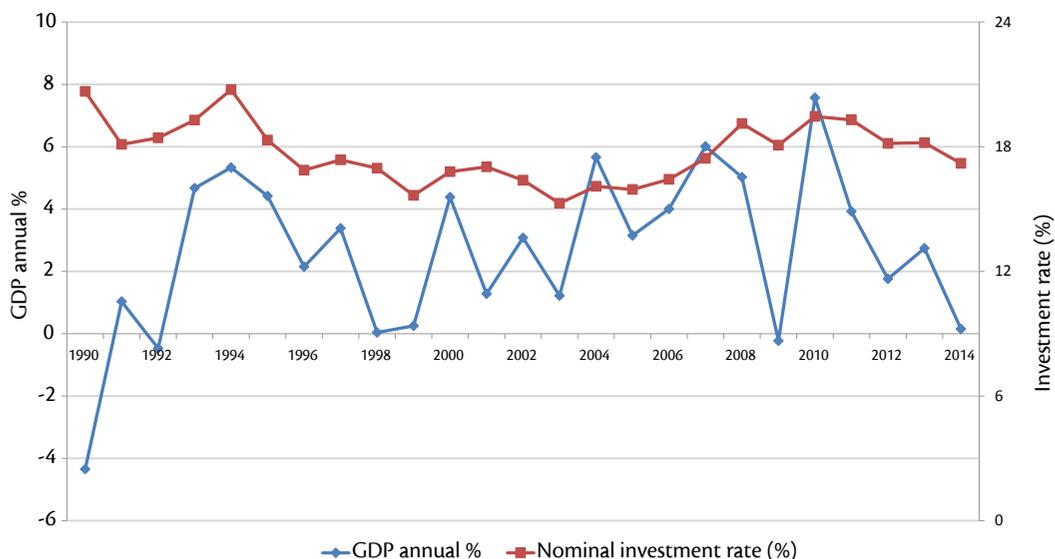
Some factors already present in the high-growth first decade of the 21st century have come to threaten the sustainability of growth in the current decade.

trade surplus and a growth in foreign exchange reserves, paving the way for lower interest rates and for key policies – such as the active minimum wage policy, social transfers, rising public bank loans and investments in infrastructure – that fueled an expansion of domestic demand.²

The 2000s saw a rise in the labor force participation rate and the formalization of employment and labor income, while the unemployment rate

continued to decline – from 12.4 percent in 2003 to 6.7 percent in 2010, considering major metropolitan areas. The growth of the Brazilian domestic market, the vigorous expansion of employment and wages, the real increase in the minimum wage – faster than average wages – and the expansion of cash transfer programs led to a decrease in inequality never before seen in Brazilian contemporary history.

Figure 1
GDP growth and investment rate.
Brazil (1990-2014)



Source: System of National Accounts ref.2000 / IBGE.

Breaking down the reduction in inequality by income source shows that the growth in labor income drove more than half of the fall in household income inequality in the 2000s. Growth in pensions contributed 21 percent to the fall in inequality, social benefits 6 percent,³ and cash transfer programs 12 percent. Along with labor income, both pensions and social benefits are linked to minimum wage; BPC, Brazil's social benefits program, is offered to elderly and disabled people who earn less than one quarter of the minimum wage. The percentage of the population living in extreme poverty fell from 17 percent in 1990 to 5 percent at the end of the 2000s.⁴

However, the growth cycle experienced in the 2000s was not accompanied by growing labor productivity.⁵ It is possible for output to grow even if productivity growth is low simply due to the increased deployment of labor, which can be driven by increasing employment and labor force participation rates as well as demographic growth of the working-age population. This is what happened in Brazil in the high-growth decade.

The growth of the Brazilian domestic market, the vigorous expansion of employment and wages, the real increase in the minimum wage and the expansion of cash transfer programs led to a decrease in inequality never before seen in Brazilian contemporary history.

In the 1990s, GDP per capita and labor productivity grew together, whereas from the year 2000 a divergence began (**Figure 2**). In the period up to 2000, more than 90 percent of output growth was driven by labor productivity growth. In the 2001-2009 period, however, little more than half per capita GDP growth was explained by productivity gains.⁶ GDP growth with low levels of productivity growth is unsustainable in the long run. Employment rates and the size of the working-age population eventually reach a peak, at which point productivity gains are needed to drive economic growth and higher wages.

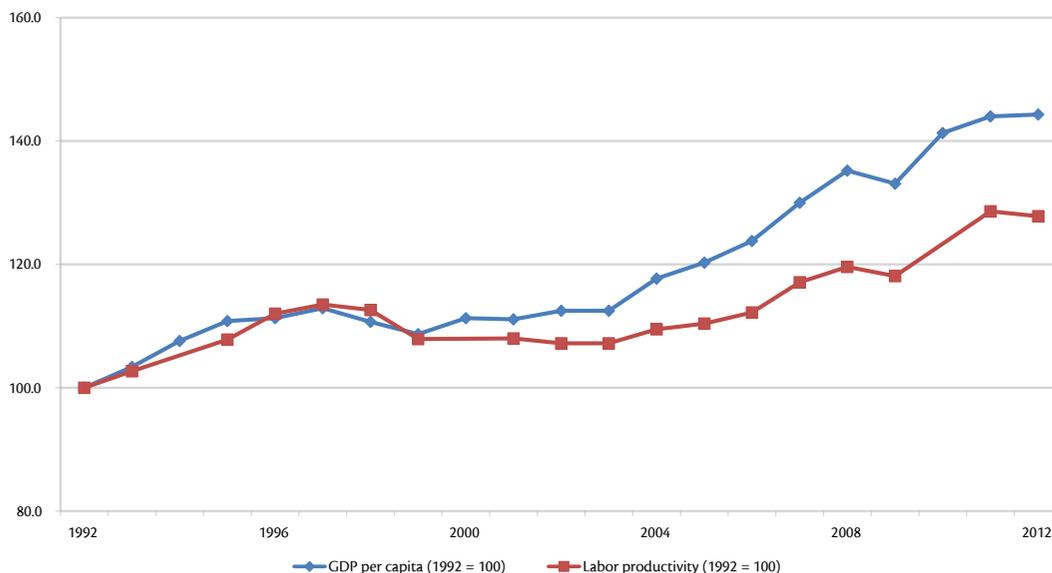
From 2001 to 2012 aggregate labor productivity grew by only 1.5 percent per year, but there were large variations between economic sectors. Productivity growth was high in agriculture, utilities and financial services, but it fell in manufacturing (**Figure 3**). The sectors with the highest increases in productivity growth saw less significant increases in employment. Moreover, their productivity gains had little influence on aggregate productivity growth. It was the sectors with sluggish growth in productivity –

especially construction and the services sector – that experienced the largest expansion of employment (**Figure 4**). This is a different picture compared with how industrialized countries developed.⁷

Therefore, once the economy experienced a downturn and investments were postponed,

labor market performance faltered. So did gains in minimum and average wages, which had underpinned the fall of inequality in the previous decade. However, since labor income and employment are generally lagging indicators, these trends remained positive until 2014, but since then Brazil has witnessed a reversal.

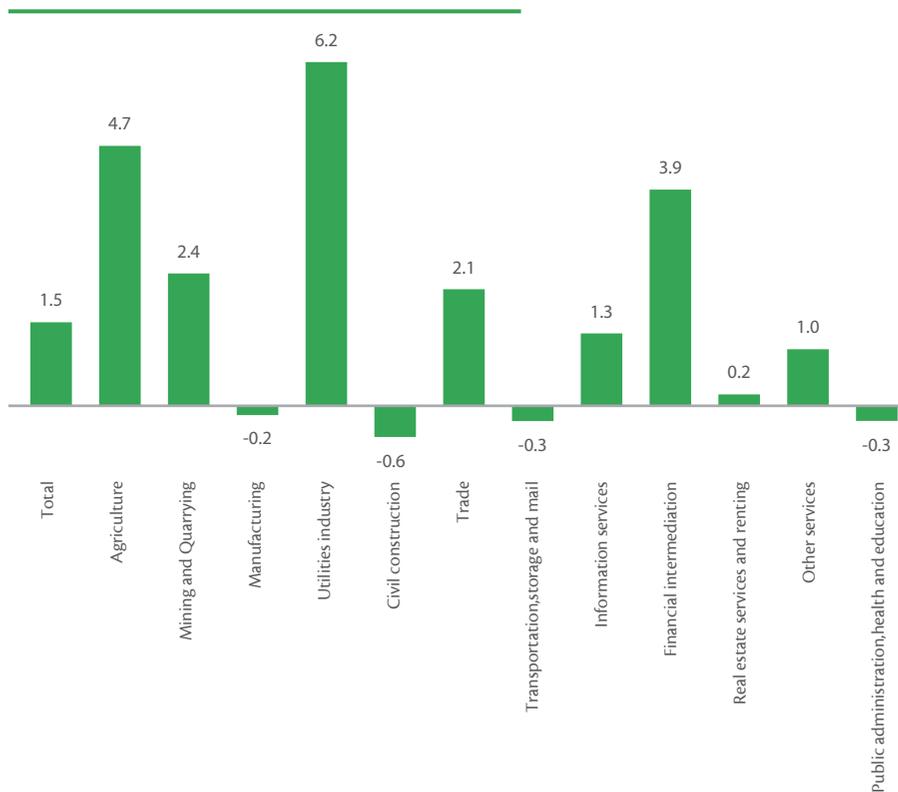
Figure 2
GDP per capita and labor productivity.
Brazil (1992-2012)



Source: IPEA, IBGE/SCN 2000 and IBGE/PNAD.

Figure 3

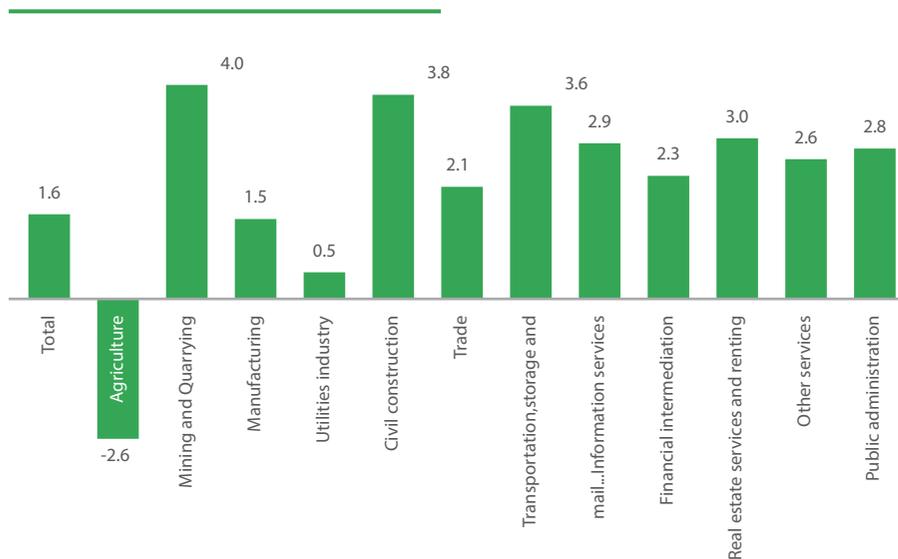
**Growth in labor productivity by industry (%).
Brazil (2001-2012)**



Source: G.C. Squeff and F. De Negri. 2014. Produtividade do trabalho e mudança estrutural no Brasil nos anos 2000.
In: De Negri, F.; Cavalcante, L. R. Produtividade no Brasil: desempenho e determinantes. (Brasília: ABDI / IPEA.)

Figure 4

Growth of occupied workers by sector (%). Brazil (2002-2012)



Source: G.C. Squeff and F. De Negri. 2014. Produtividade do trabalho e mudança estrutural no Brasil nos anos 2000. In: De Negri, F.; Cavalcante, L. R. Produtividade no Brasil: desempenho e determinantes. (Brasília: ABDI / IPEA.)

The role of the minimum wage in Brazil

Figure 5 depicts the long-term evolution of the real minimum wage. After an increase in its real value in the late 1950s, the country witnessed a downward trend between 1964 and 1994. A sharp recovery started in 1994 and was especially pronounced after 2005.

From 2005 to 2012 the minimum wage was one of the most crucial policies in ensuring a strong positive relationship between economic growth, income redistribution and social inclusion.⁸

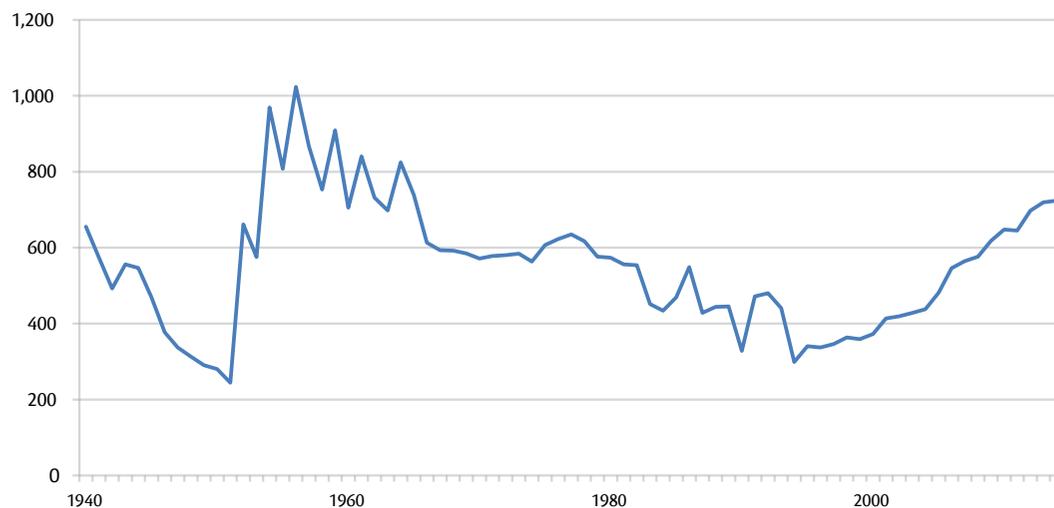
At present, the 1988 Federal Constitution guarantees a nationally unified minimum wage.

The current rules for setting the minimum wage were established in 2011.^{iv} The law stipulates that the percentage increase in minimum wage must equal the rate of inflation (National Consumer Price Index, or INPC) during the previous 12 months plus the real rate of GDP growth 2 years prior.^v For instance, with a GDP growth rate of just over one percent in 2012 and an inflation rate of just under six percent in 2013, minimum wage in 2014 rose 6.8 percent (GDP growth + inflation growth = minimum wage growth).

This formula establishes a predictable policy tool for the pro-cyclical increase of the minimum wage, which not only compensates for inflationary losses, but also reflects output growth. Prior to becoming law, it had been an official but non-legislated policy since 2005. Earlier this year, the National Congress approved its continuation for the next four years.

Due to the policy of tying the minimum wage to rising GDP in the 2000s, its value became closer

Figure 5
Trend in the National Minimum Wage, Brazil, 1940-2014 (in constant 2014 Brazilian Reals)



Source: IPEA

^{iv} Law No. 12,382, of February 25, 2011

^v The minimum wage regulation can be expressed in the following formula: $\Delta \text{minwage}_t = \Delta \text{INPC}_{t-1} + \Delta \text{GDPT}_{t-2}$, ($t=2012, 2013, 2014$)

to the average wage. The minimum wage was equivalent to 46 percent of the average wage in 2013, compared with 30 percent in 1999.

When we break down wages by type of employment – registered and non-registered^{vi} – the same pattern can be observed for both types of wage earners (Figure 6). However, for informal (i.e. non-registered) employees, the minimum wage is much closer to the average wage, especially in rural areas, since average wages for these workers are much lower than in formal employment. Given that the ratio of minimum wage to average wage is difficult to compare between employment groups, it is best to analyze how this ratio changes within each group over time.

Mirroring the formalization process that the Brazilian labor market underwent in the 2000s, the minimum wage became more important for informal employees. However, in 2013, 35 percent of unregistered wage workers still earned below

the minimum wage, with the figure reaching 44 percent among domestic workers (Figure 7). On the other hand, almost no registered workers in the private sector (only 1.4 percent) earned wages below the minimum as of 2013. And far more formal jobs were created in the 2000s as compared to informal jobs, due in part to more effective oversight by the Ministry of Labor and the growing power of unions.

From 2005 to 2012 the minimum wage was one of the most crucial policies in ensuring a strong positive relationship between economic growth, income redistribution and social inclusion.

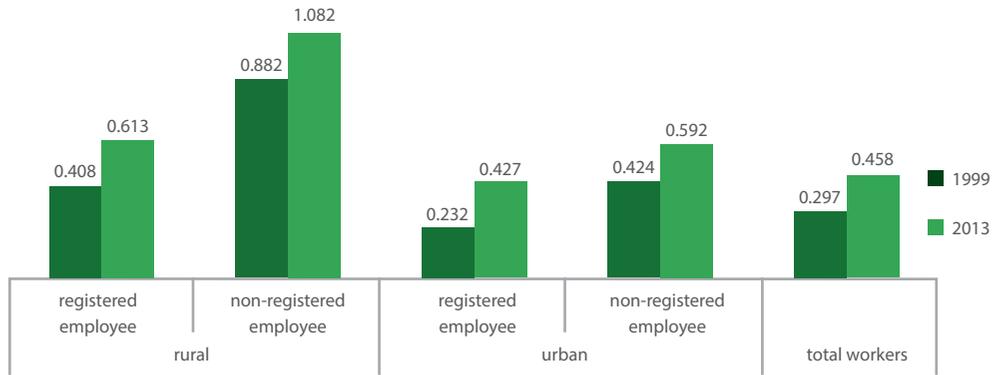
Enforcement of the minimum wage in Brazil is actively promoted by the Labor Justice system, which reviews complaints filed for non-compliance with rules

set forth in the labor code, imposing fines on noncompliant employers and ordering payment of compensation to workers. In parallel, union leaders have played an important role in public administration and in shaping public opinion, increasing the influence of unions on decisions relating to labor rights.⁹

^{vi} In Brazil, registered wage earners have direct access to labor rights. The non-registered have access only indirectly in case they appeal to the Labor Courts, as the Constitution states these rights should be applied to all wage earners. Sometimes, in the literature, non-registered wage workers are referred to as informal workers.

Figure 6

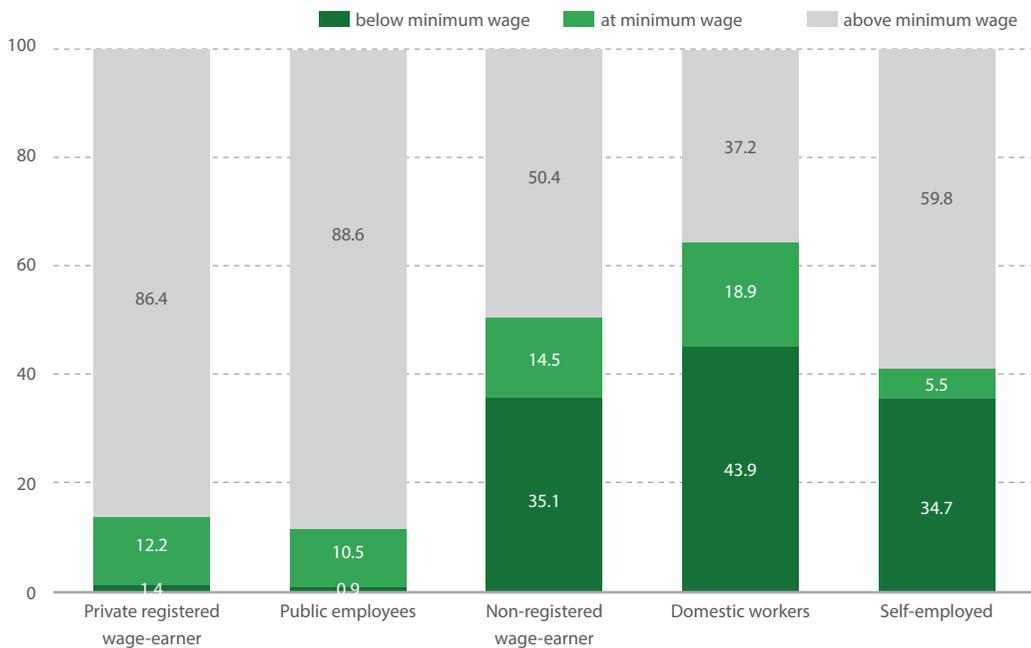
**Ratio of minimum to average wages.
Brazil, 1999-2013.**



Source: Prepared by the authors based on PNAD microdata.

Figure 7

**Occupied workers by minimum wage levels
and work status (in %). Brazil, 2013**



Source: Prepared by the authors based on PNAD microdata.

Wage inequality in Brazil

The rising minimum wage, in the context of job creation and increasing formalization of wage work, brought about a convergence of wage levels between and within economic sectors, regions and social groups.

The changes were most dramatic between 2001 and 2011, even though the trend can be traced back to 1995, when the purchasing power of the minimum wage started to increase.

To understand the role of characteristics like gender, race, region and education level, the researchers use a Theil index, enabling an analysis of the extent to which inequality is driven by these variables.^{vii} The analysis shows that during the first decade of the century in Brazil, social and geographic factors became less important as determinants of inequality.^{viii,ix} For example, wage inequality between men and women and between those with low and high levels of education became less important in explaining overall inequality.

Figure 8, which shows inequality trends for wages, labor incomes and per capita household income,

demonstrates that declining wage inequality was the main factor driving overall reductions in income inequality, as the fall in inequality was greater for wages than for labor income (which includes self-employed incomes) and per capita household income (which includes pensions, social assistance benefits and cash transfers).

This means that Brazil's minimum wage policy played a more central role in reducing inequality than the country's income transfer programs during the first decade of the century, even though this varies from region to region and from urban to rural areas.

Moreover, while the growth in registered jobs propelled the downward trend in wage inequality – as the minimum wage is almost fully enforced among registered workers – the minimum wage came to function as a standard for unregistered wage earners, too. This is demonstrated by the even faster decline of wage inequality among unregistered wage earners in the period 2005–2011 (**Figure 9**). In a booming labor market,

^{vii} A Theil index enables one to calculate the “within group inequality” as compared to “between group inequality.”

^{viii} CEBRAP/IHD. 2015b. *Patterns of income inequality in Brazil: recent evolution*, mimeo.

^{ix} CEBRAP/IHD. 2014a. *Labour market inequality in Brazil and India: concepts and methods*. Working Paper Series, N. 4. (Cebrap –IHD: São Paulo and New Delhi).

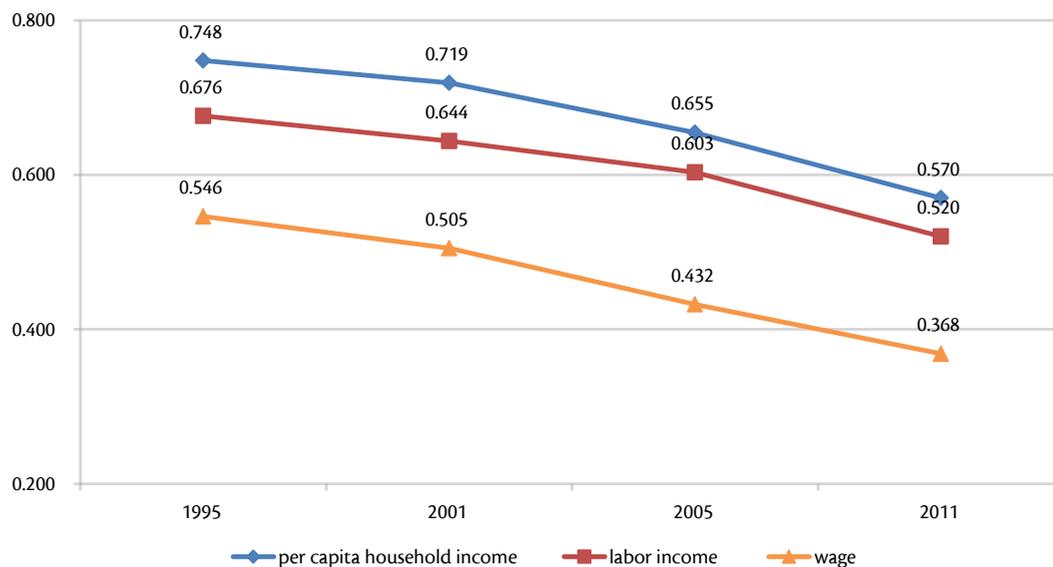
compounded by high turnover rates, paying the minimum wage has become almost a requirement in order to recruit less skilled but specialized workers, even when they are not registered.

but also with increasing wage levels. The active minimum wage policy is a key driver of this trend since it functions increasingly as a benchmark for employers, even in low-productivity sectors.

Contrary to the assumption that a higher minimum wage brings about a shrinking of the formal sector and an expansion of the low-wage informal sector, Brazil witnessed employment and wages rise in the formal economy. The informal economy saw much slower employment growth,

Another important feature of the wage pattern is increasing convergence between economic sectors and regions. Though the gap is still wide, this is remarkable in a country where heterogeneity across sectors and regions has been extreme throughout history, especially

Figure 8
Theil indexes for different types of income.
Brazil, 1995 to 2001



Source: Prepared by the authors based on PNAD microdata.

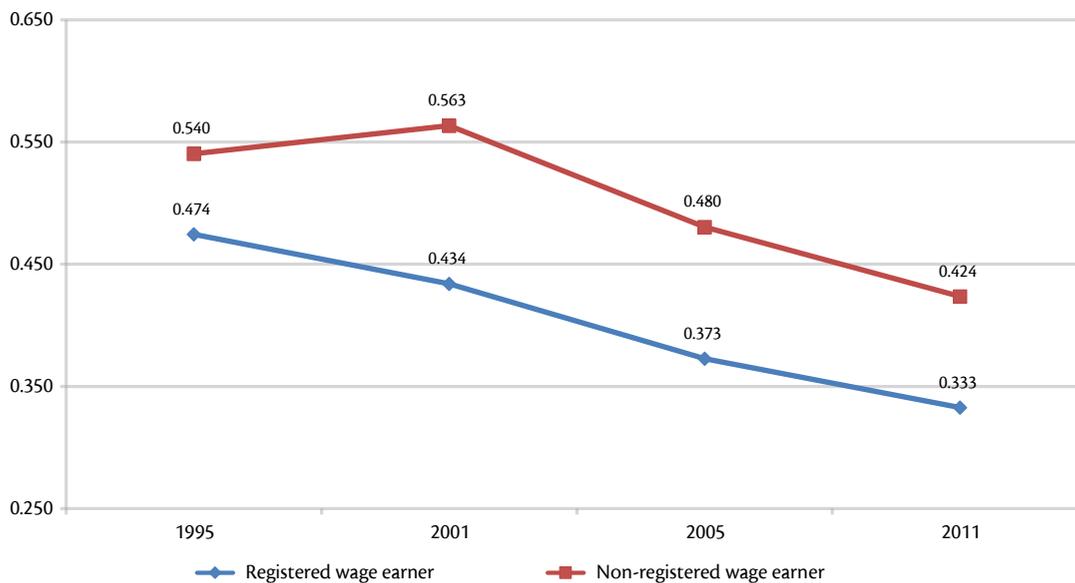
during the industrialization process from 1930 to 1980.¹⁰

Wage inequality has fallen in all sectors and most rapidly for construction and services, sectors that not only generated more jobs but also increased the share of registered wage earners in the years since 2000. In these sectors, average wages are not much above minimum wages, so a rise in the minimum tends to reduce sector-wise wage inequality.

In manufacturing, by contrast, most workers are paid far above the minimum wage, and the wage scale is much wider. The fall in wage inequality therefore was less. In agriculture, an altogether different trend can be observed: wage inequality is already low, and minimum wage is less often paid due to informality, so the rising minimum wage had little impact in terms of inequality reduction (Figure 10).

Figure 9

Theil indexes for registered and nonregistered wage earners. Brazil, 1995 to 2011



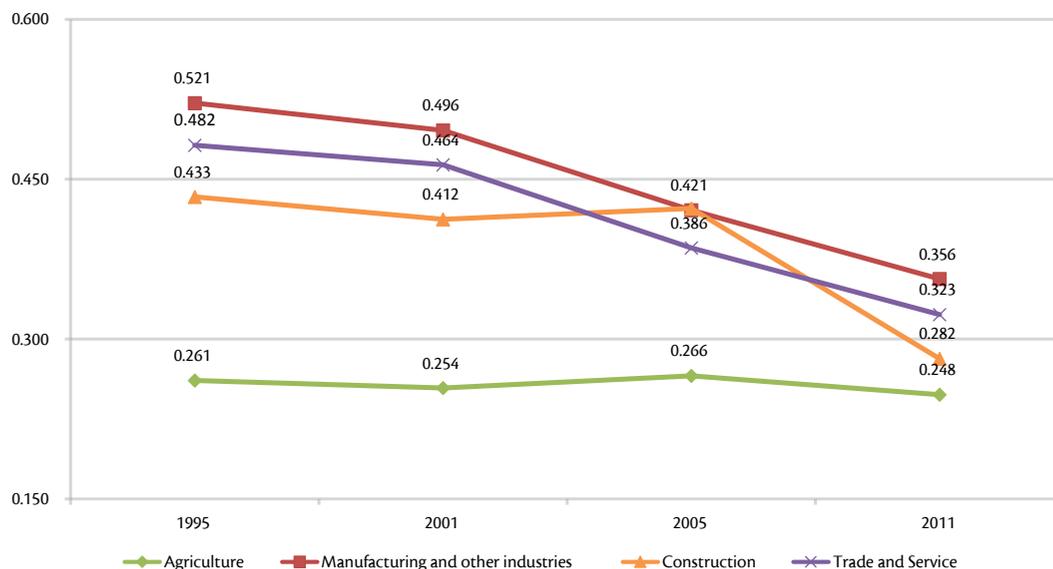
Source: Prepared by the authors based on PNAD microdata.

Another point, not shown in the figure, is that the gap between the wages of informal and formal employees (unregistered and registered) narrowed in all sectors. The same is true of the gap between average wages in lower-paying and lower-productivity sectors (agriculture, construction, trade and services) and average wages in manufacturing.

Wage inequality has fallen in all sectors and most rapidly for construction and services.

In terms of the regional differences, there was a remarkable shift. As **Figure 11** shows, the Northeast region, with the lowest GDP per capita in the country, saw the largest decline in inequality during the period 2001-2001. On the other hand, in the Southeast, the most developed region with a much higher GDP per capita, the reduction in inequality was less dramatic. While the Northeast was the most unequal region in

Figure 10
Theil indexes for wage earners by economic sectors. Brazil, 1995 to 2001



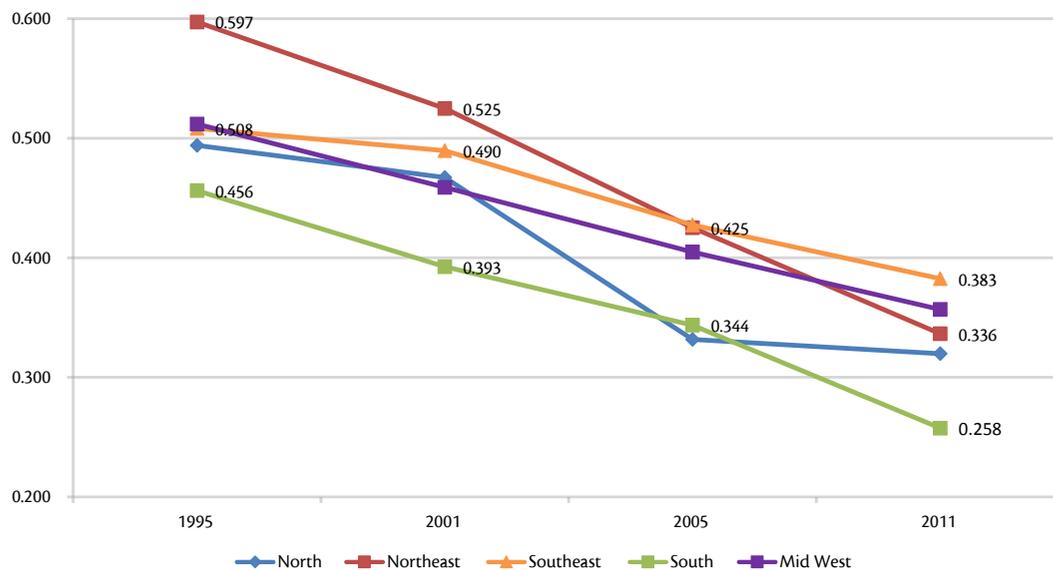
Source: Prepared by the authors based on PNAD microdata.

1995, the Southeast had taken over that spot by the end of the first decade of this century.

These data should be looked at with some caution. Self-employed workers are not considered, nor is the rural subsistence economy, both with a large percentage of the workforce in the poorest regions. The higher wage inequality for the most sophisticated regional economy of the country, the Southeast, reflects the concentration of higher

productivity activities (in manufacturing, services but also agriculture), which allows for a wider wage scale. Thus, the opposite trend – that is, a faster decrease of inequality for the richest region and a slower one for the poorest – is observed if we consider labor income (which includes all types of workers) or family per capita income^x. Furthermore, the gap between the wages in the Northeast and wages in the Southeast, even though narrowing, was still significant as of 2011,

Figure 11
Theil indexes for wage earners by regions. Brazil, 1995 to 2011



Source: Prepared by the authors based on PNAD microdata.

^x CEBRAP/IHD. 2014b. *Accumulation regimes, labour market and inequality: the Brazilian experience in the long-term*, mimeo.

with the average worker in the former earning only 60 percent of the average in the latter.

It is also worth mentioning that wage inequality fell most significantly among almost all disadvantaged groups – especially non-whites and the less educated – and also among women (**Table 1**). The minimum wage is responsible for this change as these groups have more wage earners receiving around the minimum wage. The growth of jobs was more concentrated at both ends of the wage scale for women as compared to men. At the same time, the female to male wage ratio, at over 0.8, was much higher than that between non-whites and whites, even

though the latter increased from 0.55 to 0.66 in the concerned period.

Considering education, wage premiums have fallen for all schooling levels, which is related both to the influence of the minimum wage and to an abundance of workers with secondary and tertiary education in a context in which productivity has remained stagnant. The wages of illiterate wage earners were 10 times lower than those for workers with college education in 2001, but fell to 4.2 times lower in 2011. The change is staggering even considering the fact that the size of the first group dropped sharply while the size of the second grew dramatically.

Table 1
“Within-Group” inequality, and ratio of average wages. Brazil (2001/2011)

	Theil Index 2001	Theil Index 2011	% ▲Theil Index 2001-2011	Wages Ratio 2001	Wages Ratio 2011	ratios
male	0.529	0.378	-28.6	0.855	0.834	female / male
female	0.451	0.388	-22.9			
whites	0.514	0.41	-20.3	0.552	0.659	non-whites / whites
non-whites	0.351	0.251	-28.5			
Without instruction	0.218	0.194	-10.8			
Incomplete Primary Ed	0.233	0.156	-32.9			
Complete Primary	0.258	0.166	-35.5	0.798	0.912	incomplete/complete primary/secondary
Secondary	0.337	0.229	-32	0.659	0.751	secondary / tertiary
Tertiary	0.403	0.404	0.1	0.329	0.387	

Source: Prepared by the authors based on PNAD microdata.

Conclusion and policy implications

Brazil, in the first decade of the 21st century, is a prime example of how an active minimum wage policy can lead to inequality reduction in the labor market. It is true that the gap between wages and productivity was high at the beginning of this period and that the macroeconomic conditions also aided the policy's success.

However, one of the main weaknesses of the growth regime was the stagnation of labor productivity. Job creation was concentrated in sectors with productivity that was low or not rising, impeding the sustainability of economic growth, job creation and inequality reduction.

This leads to the conclusion that for the downward trend in inequality to continue, an active minimum wage policy will not suffice. The same is true for an increase in social transfers.

These policy tools may prevent the emergence of a new growth model that fosters inequality – the type that characterized the Brazilian economy for most of the 20th century. But they need to be complemented with policies that address other economic and social woes. Resuming robust economic growth requires overcoming stagnant productivity – a pattern that may lead to a less positive performance in terms of job creation than was experienced in the last decade.

In this context, collective bargaining, higher investment in social policies – such as health, training, education, housing and basic infrastructure – and tax reform must become central elements of a new strategy to reduce inequality and improve the living conditions of the workers at the bottom of the social pyramid.

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STATE AND LOCAL GOVERNMENTS LEAD THE WAY

*Examining the impact of subnational minimum wage increases
in the United States*

Jacqueline Odum, CAP

Center for American Progress (CAP)

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UNITED STATES



7.4

Unemployment Rate



41.1

GINI



93.2

Wage and salaried
workers, total (% of
total employed)



68374

GDP per person
employed
(constant 1990 PPP \$)

STATE AND LOCAL GOVERNMENTS LEAD THE WAY

Examining the impact of subnational minimum wage increases in the United States

Jacqueline Odum, CAP

Introduction

America's working class families have witnessed a daunting trend over the last 30 years – one marked by wage stagnation and rising costs. Worker productivity rose by nearly 65 percent, yet American workers saw their wages remain stagnant in real terms, and in some cases, even decline.¹ At the same time, the costs of key components to middle class security – such as childcare, higher education, health care, housing, and retirement – have risen, diminishing the prospect of the American dream.² This tension between rising costs and wage stagnation is the defining issue of our time. It affects all households, but is a particularly acute concern for low-wage workers, since rising costs are swallowing an increasingly large share of their household income.

Today, 29 states and the District of Columbia have minimum wages above the federal minimum wage. In 2015 alone, 20 states raised their minimum wages, lifting the pay of over 3.1 million workers.

As this chapter will demonstrate, part of the reason for stagnating wages is the declining value of the federal, or national, minimum wage. Because the federal minimum wage has not kept up with inflation, it is worth far less today than in the late 1960s.³ Moreover, research shows that the declining value of the federal minimum wage continues to contribute to the trend of rising income inequality.⁴ Raising the federal minimum wage is a simple and practical policy approach that lawmakers can take to lift wages for workers and combat rising inequality. While the vast majority of Americans support this approach,⁵ gridlock on the issue in Congress, the American national legislature, has made federal action almost inconceivable. Amid this inaction,

however, states and localities have taken it upon themselves to implement wage floors above the federal standard.¹

Today, 29 states and the District of Columbia have minimum wages above the federal minimum wage.⁶ In 2015 alone, 20 states raised their minimum wages, lifting the pay of over 3.1 million workers. The District of Columbia's

minimum wage is the highest, at US\$ 10.50 per hour. Moreover, 10 states have their minimum wage indexed annually to adjust for inflation, and another five states and the District of Columbia plan to follow suit.⁷ Cities and counties, too, have begun to set their own minimum wage floors through local ordinances and ballot initiatives. (See **Table 1.**)

Table 1

States with Minimum Wage Floors Above the Federal Standard (US\$)

United States	\$7.25	Illinois	\$8.25	New Mexico	\$7.50
Alaska	\$8.75	Maine	\$7.50	New York	\$8.75
Arizona	\$8.05	Maryland	\$8.25	Ohio*	\$8.10/\$7.25
Arkansas	\$7.50	Massachusetts	\$9.00	Oregon	\$9.25
California	\$9.00	Michigan	\$8.15	Rhode Island	\$9.00
Colorado	\$8.23	Minnesota*	\$8.00/\$6.50	South Dakota	\$8.50
Connecticut	\$9.15	Missouri	\$7.65	Vermont	\$9.15
Delaware	\$8.25	Montana*	\$8.05/\$4.00	Washington	\$9.47
D.C.	\$10.50	Nebraska	\$8.00	West Virginia	\$8.00
Florida	\$8.05	Nevada*	\$8.25/\$7.25		
Hawaii	\$7.75	New Jersey	\$8.38		

* These states differentiate between wage floors on the basis of size of employer and employment benefits offered.

Source: National Conference of State Legislatures, "State Minimum Wages: 2015 Minimum Wage by State," available at <http://www.ncsl.org/research/labor-and-employment/state-minimum-wage-chart.aspx#1> (last accessed July 2015).

Unlike in other countries, the authority to set minimum wages falls with national, state and local authorities. The federal minimum wage acts as an absolute floor, but states are empowered to pass higher minimum wages, and localities can legislate them above the state level if they so choose.

These state and local measures have become an important wage-lifting tool for policymakers. They offer a glimmer of hope for low-wage workers, especially for those residing in areas with a higher cost of living. As minimum wage increases continue to pick up steam on the state and local level, the economic effects of such laws remain highly contentious among both advocates and opponents. This chapter will examine the economic effects of minimum wage increases

and provide new analysis while drawing upon existing literature to assess the following:

1. How inadequate minimum wage levels have historically contributed to rising income inequality
2. The impact minimum wage increases have on employment levels
3. The effect that minimum wage increases have on businesses and labor costs

Impact on rising income inequality

For nearly thirty years after World War II, America's working class experienced a period of growing wealth. From 1948 to the mid-1970s, positive trends in hourly compensation mirrored those in growing worker productivity. In the late 1970s, however, these two trends began to diverge as labor productivity growth began to outpace wage growth. The Economic Policy Institute estimates that from 1979 to 2013, worker productivity grew by 64.9 percent.⁸ During that same time period, however, hourly compensation of production and nonsupervisory workers, who make up

approximately 80 percent of the private sector workforce, grew by a meager 8.2 percent in real terms.⁹

These trends illustrate unprecedented levels of wage stagnation. It should come as no surprise

Erosion of the federal minimum wage is one major reason poor households are witnessing the stagnation or even decline of their incomes.

that wage stagnation combined with rising productivity contributes to rising income inequality, which includes other non-wage forms of income. Since 1979, income inequality has risen dramatically. Analysis from the Congressional

Budget Office shows that, from 1979 to 2007,

Figure 1
Real minimum wage in 2014 dollars



Source: Author's calculations based on Bureau of Labor Statistics' Consumer Price Index.

inflation-adjusted after-tax income for the top 1 percent of households increased at a rate of 275 percent. In comparison, inflation-adjusted after-tax income increased at a rate of nearly 40 percent for the middle quintile and at a rate of only 18 percent for the bottom 20 percent of households.¹⁰ In other words, while inflation-adjusted income for those at the top of the distribution increased nearly threefold, the vast majority of Americans barely saw their incomes grow.

This growing unevenness in the nation's distribution of income is particularly alarming

for low-wage workers, as they often lack access to other non-wage forms of income – such as employer-sponsored healthcare benefits, pensions and capital gains. In fact, wage-related income accounts for the vast majority of total income for those at or near the bottom of the income distribution.¹¹ Thus, slow hourly wage growth is the major contributing factor to the trend of slow total income growth for the poorest households.¹²

Erosion of the federal minimum wage is one major reason poor households are witnessing the stagnation or even decline of their incomes.

Since 1968, there have been a total 15 legislated increases in the federal minimum wage. Today, the federal minimum wage stands at US\$ 7.25 an hour.¹³ However, the federal minimum wage has not kept up with inflation, and therefore, has declined in real terms.

Had the federal minimum wage kept up with inflation since 1968, it would stand at \$10.88 in 2014 dollars.¹⁴

Research shows that this decline in the real value of the federal minimum wage continues to contribute to the rise in inequality. One way experts measure inequality is by looking at the gap between the median wage and the average wage of those at the bottom 10 percent of the wage distribution – the so-called 50-10 wage gap. According to the Economic Policy Institute, the declining real value of the federal minimum wage between 1979 and 2009 explains more than half (57 percent) of the expansion of the 50-10 wage gap during that time period.¹⁵ Interestingly, the erosion of the federal minimum wage explains almost two-thirds (65.5 percent) of the 50-10 wage gap expansion among female workers but only a tenth (11.3 percent) of the expansion for male workers.¹⁶ This is due, in part, to the fact that two-thirds of minimum wage workers are women, so the erosion in its value

While an increase in the federal minimum wage would help reverse the trend of rising inequality, it should also be noted that minimum wages are generally not enough to lift families out of poverty.

has a greater effect on inequality where female workers are concerned.¹⁷

Within the context of wage inequality, it is important to note that minimum wage increases

are not just vehicles for lifting wages for the lowest paid workers. Studies show that minimum wage increases also boost wages for workers that earn slightly above the minimum wage.¹⁸ This ripple effect reduces wage inequality at the lower end of the wage distribution, shrinking the 50-10 wage gap. The positive impact

would be felt particularly by women, but also other vulnerable populations that are more likely to be in low-wage work, such as single-parent households and communities of color. In fact, racial minorities represent almost half of potential beneficiaries.¹⁹

While an increase in the federal minimum wage would help reverse the trend of rising inequality, it should also be noted that minimum wages are generally not enough to lift families out of poverty. This is confirmed by the persistence of poverty in states that provide a minimum wage above the federal standard. Many state-level wage floors fall short of providing living wages

for workers that live in comparatively higher-cost cities. For example, the current minimum wage in California is US\$ 9.00 an hour. Hence, today, a full-time, minimum-wage worker in the city of Los Angeles, California makes about \$18,720 annually. According to the Massachusetts Institute of Technology's Living Wage Calculator, a family of three – that is, two parents and one child – in Los Angeles needs US\$ 58,281 annually to meet minimum standards of living.²⁰ Thus, the combined salaries of two full-time, minimum-wage workers with one child in Los Angeles falls short by over US\$ 20,000.²¹ Cities, Los Angeles included, are beginning

The analysis generates no clear evidence that minimum wage hikes increase unemployment levels during periods of already high unemployment.

to address wage stagnation through local ordinances and ballot initiatives that lift the local minimum wage. In 1993, the District of Columbia became the first city to raise its minimum wage, and since then 15 cities have followed suit. Over the last two years alone, 14 cities and four counties have implemented local minimum wage laws of their own.²² Los Angeles is the most recent example in this series of local policy initiatives. In May 2015, city residents backed a ballot measure that will raise the local minimum wage to US\$ 15 over the course of five to six years, depending on the size of the employer.²³

Impact on employment

The effect of minimum wage increases on employment is the subject of a highly contentious debate. Opponents of minimum wage increases often claim that raising the minimum wage increases labor costs, placing a burden on employers that either constrains new job growth or, worse, results in lay-offs. However, a growing body of credible economic research has shown that these claims are unfounded, and that

minimum wage increases have no discernible effect on employment levels.²⁴

Previous analysis by the Center for American Progress Action Fund (CAPAF) examined the employment effect of minimum wage increases during periods of high unemployment.²⁵ Lester, Madland and Odum found that, between 1987 and 2012, the majority of states that experienced

a minimum wage increase during a time of high unemployment saw a decrease in their unemployment rate over the following year.²⁶ This chapter's analysis replicates the approach used by Lester and his colleagues. The updated analysis includes every effective minimum wage increase for each state and the District of Columbia from 1987 through 2013 at times when the state's (or District's) unemployment rate was at or above 7 percent.ⁱⁱ It then examines changes in the unemployment rate over the year following the effective minimum wage increase.

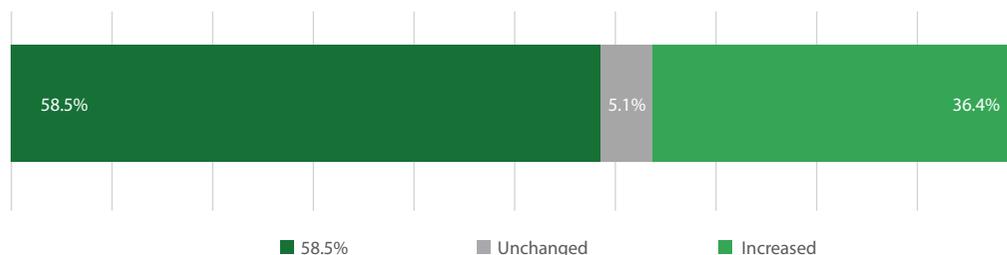
unemployment levels during periods of already high unemployment. Between 1987 and 2013, there were a total of 118 instances in which certain states and the District of Columbia experienced a minimum wage increase in the context of high unemployment. In 69 of these cases, the unemployment rate decreased one year after the effective hike, and in 6 other cases, the unemployment rate remained unchanged. In contrast, the unemployment rate increased for 43 cases. In other words, when the minimum wage was increased during a period of high unemployment, unemployment rates either decreased or remained unchanged 63.6 percent of the time.

This updated analysis is consistent with previous findings. The analysis generates no clear evidence that minimum wage hikes increase

Figure 2

Unemployment dropped following a majority of minimum-wage increases

From 1987 through 2013, states raised the minimum wage 118 times when the unemployment rate was at or above 7 percent. Unemployment fell after 58.5 percent of these increases and remained unchanged after 5.1 percent of them.



Source: Authors' analysis of the Bureau of Labor Statistics' Local Area Unemployment Statistics data. Monthly data were averaged to produce quarterly figures.

ii The authors' baseline of 7 percent is based, in part, on the Congressional Budget Office's estimate of the short-term natural rate of unemployment, which peaked at 6 percent in 2012.

Another CAPAF report examined the employment effect of citywide minimum wage hikes.²⁷ Using a similar approach to that above, the report included every citywide minimum wage increase between 1993, when the first local increase was implemented, and 2013, the last year after which impact can be examined. Because city minimum wage increases are a relatively new trend, only a small number of cities were included in the analysis.ⁱⁱⁱ The results showed that in 64 percent of the local minimum wage hikes, local unemployment rates either decreased or remained unchanged.²⁸

While we acknowledge that these basic state-and-city-level comparisons do not illustrate causation, these findings offer additional support for a growing consensus among researchers that minimum wage increases have no discernible effect on employment levels.

Rigorous academic studies on state-level minimum-wage hikes support this notion. The latest state-level studies are regarded as some of the most methodologically accurate to date.

After controlling for various heterogeneities in employment trends, the authors found that the minimum wage increases had no discernible effect on employment levels.

Unlike older studies, they use quasi-experimental research designs that control for various regional and heterogeneous trends along U.S. Census Bureau divisions.²⁹ A study published by the Center for Labor Research and Education at the University of California, Berkeley, for example, examined the employment effects for minimum wage increases at state borders.

The authors of the study specifically analyzed employment levels of restaurants and other low-wage industries in bordering counties across state lines that had different minimum wage floors. After controlling for various heterogeneities in employment trends, the authors found that the minimum wage increases had no discernible effect on employment levels.³⁰

Because citywide minimum wage laws are relatively new, little research exists to measure the full economic effects of local minimum wage increases. However, the literature that does exist offers insightful analysis that supports the general hypothesis championed by proponents.

iii While the state-level analysis controls for periods of high unemployment – unemployment at or above 7 percent – the city-level analysis differs. It does not control for periods of high unemployment because city-level minimum-wage increases are a relatively new trend, and the impact could only be measured in a small number of cities. Controlling for periods of high unemployment in the city-level analysis would have narrowed the number of cases down to a number too small for measurement.

Of the existing city-focused studies, the most rigorous is a paper commissioned by the Institute for Research on Labor and Employment at Cornell University where researchers measured a variety of economic outcomes following San Francisco's 2004 minimum wage increase.³¹ The authors found that the city's minimum wage increase had no discernible effect on employment levels in San Francisco. Their analysis on the law's regional employment effects also suggests that the local increase did not negatively affect employment levels in neighboring counties with different minimum wages.³²

Further, meta-studies reflect a consensus among economists with respect to the general effect

minimum wage increases have on employment levels. A meta-study is essentially a "study of studies" that uses statistical methods to compare the results of a large number of separate studies. In a meta-analysis conducted by the Center for Economic and Policy Research (CEPR), economists reviewed the results of the most recent wave of minimum wage studies dating back to the year 2000.³³ The meta-analysis revealed that the majority of existing modern literature showed that minimum wage increases have little to no effect on employment.³⁴ These findings, coupled with similar meta-studies, signal a growing consensus view among experts that clash with that of minimum wage opponents.

Impact on businesses and labor costs

A common misconception among opponents of minimum wage increases is that they hurt employers. This view is often based on a flawed assumption about the relationship between the minimum wage and labor costs, or the sum of all wages paid to employees. Opponents argue that increases in the minimum wage drive up labor costs, which negatively affect other aspects of business operations, such as costs of goods and services, productivity levels, and hiring and firing decisions. Research, however, dispels this

view, suggesting that increases in labor costs for employers are often absorbed by adaptations in the production process.

Historically, increases in labor costs associated with minimum wage hikes have been minimal. For example, of the 10 federally legislated minimum wage hikes since 1989, average increases in labor costs ranged anywhere between a low of 5.3 percent and a high of 9.4 percent.³⁵ Research suggests that businesses often absorb these

costs through changes in other aspects of production known as “channels of adjustment.”³⁶ These channels include changes in prices, profits, wage compression, the number of hours worked, turnover, worker productivity and performance standards.³⁷

Empirical research on how these channels of adjustment absorb the higher labor costs is generally inconclusive or else suggests only small effects. The strongest evidence, however, shows that some of the most important channels for offsetting labor costs actually improve the well being of a firm’s workers.³⁸ Higher wages boost employee morale and reduce absenteeism, thereby increasing levels of worker productivity.³⁹ In the same way, minimum wage increases can also help to reduce turnover, and with that, costs to the employer associated with recruitment and training.⁴⁰

Moreover, the macroeconomic impact of raising the minimum wage can also benefit businesses. In 2013, the Federal Reserve Bank of Chicago estimated that an increase of US\$ 1.75 per hour

in the federal minimum wage would result in a real GDP increase of 0.3 percent in the short term without any negative effects in the long run.⁴¹ This is because an increase in wages boosts consumer spending. Poorer households tend to spend more of their income than wealthier households, so rebalancing the income distribution has positive effects for aggregate demand.

Taken together, these findings suggest that employers and workers respond to minimum wage increases through several channels of

Higher wages boost employee morale and reduce absenteeism, thereby increasing levels of worker productivity. In the same way, minimum wage increases can also help to reduce turnover, and with that, costs to the employer associated with recruitment and training.

adjustment, thereby minimizing potential negative economic effects. Contrary to popular rhetoric, minimum wage increases are not likely to invoke mass layoffs and substantial price increases within the business community. In fact, the price effect is minimal, with an

increase of no more than 0.4 percent to overall prices for a federal minimum wage increase of 10 percent.⁴² Rather, both employers and workers are likely to respond to minimum wage increases through a series of changes that will alter the workplace in ways that benefit business owners, working families, and communities as a whole.

Conclusion

Rising costs and wage stagnation have stymied progress in the American economy. Contrary to popular rhetoric, the bulk of empirical evidence suggests that minimum wage increases have positive effects for the economy as whole. This policy measure has the ability to combat rising inequality with little to no effect on employment levels or business costs.

State and local lawmakers recognize that minimum wage increases are an effective policy tool for lifting wages and strengthening the economy. Already, 29 U.S. states, or a *majority*, have adopted this policy approach, and in recent years, a growing number of cities and counties have implemented increases of their own. These state and local legislative trends are indicative of a growing need to also raise the federal minimum wage floor. Economic opportunities should not simply be determined by one's place of residence.

As is, the current federal floor stands as a barrier to achieving the American dream. It keeps workers trapped in low-wage work that offers poverty-level wages and an increasing reliance on government transfer programs.

The federal minimum wage floor was meant to allow workers to meet the minimum standards of living; however, in the United States, the federal floor has failed to meet that standard. As is, the current federal floor stands as a barrier to achieving the American dream. It keeps workers trapped in work that offers poverty-level wages

and creates an increasing reliance on government transfer programs. Raising this floor would lift the take home pay for millions of workers at or near the bottom of the income distribution.⁴³ It would give working families a fair chance to secure a middle-class standard of living. Setting a higher federal minimum wage is a simple

and practical policy approach to addressing some of the economic disparities of our time.

Endnotes

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THE IMPACTS OF MINIMUM WAGE POLICY IN CHINA

Mixed results for women, youth and migrants

Li Shi and Carl Lin

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CHINA



4.6

Unemployment Rate



37.0

GINI



15250

GDP per person
employed
(constant 1990 PPP \$)

THE IMPACTS OF MINIMUM WAGE POLICY IN CHINA

Mixed results for women, youth and migrants

Li Shi and Carl Lin

Introduction

Since China enacted its first minimum wage law in 1994, the magnitude and frequency of changes in the minimum wage have been substantial, both over time and across jurisdictions. The impact of the minimum wage and its controversial nature has sparked heated debate in China, highlighting the importance of rigorous research to inform evidence-based policymaking.

This chapter summarizes the impacts of the minimum wage policy in China on various aspects of the labor market: overall wages, employment, gender and income inequalities, and regional disparities. The authors pay special attention to

the 1.68 million rural-urban migrant workers in China, focusing on the wage and employment impacts they experience as a result of minimum wage policies.

Minimum wage policy should focus on its initial intended purpose – ensuring that workers receive remuneration at a particular threshold to provide for their basic needs. Beyond that, the minimum wage should not be used as the primary tool to accomplish other political and economic goals.

The chapter's findings show that since 2004, nominal minimum wages in China have increased substantially, at an average of 11 percent per year, leading to positive effects on wages and decreases in gender wage differentials and income inequality. On the other hand, the rising minimum wage has resulted in job

losses for young adults, women, and low-skilled workers.

For migrant workers, the minimum wage has only small negative impacts on migrants' employment in the east and central regions of the country and no effect in the west. In addition, this research finds that employers have increased the monthly working hours of migrant workers. Offsetting the costs of a higher minimum wage by increasing the number of working hours means that employers do not have to layoff migrant workers.

Taken together, this research shows that the minimum wage policy in China has resulted

in both positive and negative effects. As such, policymakers are confronted with a tradeoff. The authors propose, however, that in its application by policymakers, minimum wage policy should focus on its initial intended purpose – ensuring that workers receive remuneration at a particular threshold to provide for their basic needs. Beyond that, the minimum wage should not be used as the primary tool to accomplish other political and economic goals, such as increasing average wages or promoting social development.ⁱ

The politics of minimum wage setting in China

China is in the midst of a transition from a planned economy to a market economy. As a result, the country faces economic and social problems that impede its long-term sustainable development. Moreover, the social instability resulting from widening income inequality, corruption, and social exclusion has become a major concern for the Chinese government. To respond to these challenges, both central and local governments are placing new emphasis on inclusive growth, introducing a number of new policies and regulations. Especially in recent

years, the government has actively intervened in the labor market – increasing job-training opportunities for unskilled workers and migrant workers, more strictly implementing new labor contracts, ensuring job stability, and expanding coverage of social insurance programs.

Raising the minimum wage has been one of the Chinese governments' most important labor market interventions. Since adopting the "New Minimum Wage Regulation" in 2004, the nominal minimum wage has increased significantly,

i In China, there already are, for example, macroeconomic policy and social security/assistance measures such as unemployment insurance, medical care, and urban minimal living assurance systems that seek to improve the functioning of the labor market and reduce poverty.

with average growth of 11 percent per year nationally. The process is largely driven by political competition between local governments at the city and provincial levels in response to the central government's appeal to raise the wage share of national income, as outlined in the 12th Five-Year Plan.ⁱⁱ The plan specifies the mean minimum-to-average wage ratio should reach 0.4 by 2015. As of 2009, the ratio was 0.29.ⁱⁱⁱ

Since China's political system is highly centralized and hierarchical, the way in which the minimum wage is determined can be quite different from developed and other

developing countries. Local governments are eager to win the central government's support in the form of infrastructure development, fiscal transfers, bank loans, and land use. Moreover, promotions of local officials at provincial and city levels are determined by the central government.^{iv} By raising the minimum wage, local governments signal their determination to address issues such as income inequality that could otherwise threaten political stability.

In past decades, local governments had kept minimum wages low because they worried that high wages would

Raising the minimum wage has been one of the Chinese governments' most important labor market interventions. Since adopting the "New Minimum Wage Regulation" in 2004, the nominal minimum wage has increased significantly, with average growth of 11 percent per year nationally.

ii In the last ten years, the Chinese central government has gradually changed its development goals from emphasis on economic growth to social development. The government is also less concerned with production incentives and more focused on equitable distribution. This implies that wage growth and wage equality could become new indicators for the central government to evaluate and monitor the performance of local economic and social developments and efforts of local officials.

iii Urban Household Surveys (2004-2009).

iv Given the political system in China, the local governments have strong incentives to meet the desires of the central government since the promotion of local officials is decided by the central government. (See: Y Chen, H Li and L-A Zhou. 2005. Relative performance evaluation and the turnover of provincial leaders in China. Economics Letters 88, 421-425). The relevant studies indicate that the political status of a province is positively correlated with the provincial economic ranking in China, when the central government sets up economic growth as a priority. (See: E Maskin, Y Qian, C-G Xu. 2000. Incentives, scale economies and organizational form. Review of Economic Studies 67, 359-378). Li and Zhou present evidence on the link between political turnover of top provincial leaders and provincial economic performance, which is interpreted as the central government's method for controlling local officials. (See: H Li, L-A Zhou. 2005. Political turnover and economic performance: The incentive role of personnel control in china. J Public Econ 89, 1743-1762.)

cause jobs to shift to districts with cheaper labor costs, exacerbating already high levels of unemployment in particular regions. Once China's labor market began to thrive, concerns over unemployment diminished and local governments began raising wages substantially and consistently. They calculated that any disemployment resulting from wage increases would likely affect migrant workers. As migrant workers are not eligible for unemployment benefits, any increase in migrant worker unemployment would not drive up fiscal spending. Given this dynamic, local governments in coastal cities, which host the most migrant workers, enacted the most significant wage increases.

The Chinese minimum wage policy has been regarded as the solution not only to protect workers with a wage floor, but to increase the income of the poor and reduce inequality.^v But very limited empirical research has studied the consequences of the minimum wage policy in China. This chapter seeks to answer the following questions:

1. What are the wage and employment effects of China's minimum wage?
2. How are minimum wages set at city and provincial levels in China?
3. What are the impacts of minimum wages on wage distribution, the gender wage gap, and income inequality?

A brief history of minimum wage legislation in China

Prior to 1994, China had no minimum wage law. China issued the first national minimum wage regulations in 1993, and in July 1994, these regulations were written into China's new labor law.

The 1994 legislation required that all employers pay wages no less than the local minimum wage. Further, all provincial, autonomous regions, and municipal governments were required to set the minimum wage according to six principles:

v The political competition among local governments would speed up the rise of the minimum wage. As a matter of fact, this would presumably hasten labor migration to coastal areas, leading to greater imbalances. Moreover, this competition process is hypothesized to be harmful to the economic growth in the western region and lead to widening regional economic disparity in China.

- the cost of basic living expenses of workers;
- the average number of dependents workers support;
- local average wages;
- the level of labor productivity;
- the level of local employment; and
- the level of economic development.

These conditions provided considerable flexibility for provinces in setting minimum wages; the economic development principle gave them the flexibility to limit the minimum wage to attract foreign investment.¹ High minimum wages would mean higher operational costs, which could reduce China's attractiveness to foreign investors looking to invest in Chinese businesses.

In the early 2000s, sluggish growth in minimum wages, along with growing concerns for uninsured workers, led the government to introduce new minimum wage regulations. The

new law, announced in January 2004, extended coverage to all employees in state-owned and private enterprises, own-account workers, and private, non-enterprise (non-profit) units.^{vi} In particular, the new law established two types of minimum wages: a monthly minimum wage applied to full-time workers and an hourly minimum wage applied to part-time employees.

Moreover, the minimum wage standards are set and adjusted jointly by the local government, trade union confederation, and enterprise confederation of each province. The draft is then submitted to the Ministry of Labor and Social Security for review, and the Ministry asks for opinions from the All China Federation of Trade Unions (ACFTU) and the China Enterprise Confederation. The ACFTU, however, is a government body, which means that the authority to set minimum wages ultimately rests within the Ministry.

According to the new regulation, local governments must renew their minimum wage

According to the new regulation, local governments must renew their minimum wage standards at least once every two years, and compared to the previous legislation, penalties for violations quintupled – from a maximum of 100 percent to a maximum of 500 percent of the owed wages.

vi Private non-enterprise units are equivalent to NGOs as defined by the Chinese government.

Figure 1
Provinces and Regions in China



standards at least once every two years, and compared to the previous legislation, penalties for violations quintupled – from a maximum of 100 percent to a maximum of 500 percent of

the owed wages. Moreover, employers could no longer include extra allowances such as overtime pay or food and travel subsidies as part of an employee’s wage to meet the minimum standard.

How does the minimum wage affect earnings and employment?

Fang and Lin found that minimum wage changes in China led to significant negative effects on employment in the eastern and central regions

(see **Figure 1**), and caused disemployment for young adults and low-skilled workers, particularly workers who at the time of a minimum wage

increase were receiving a wage between the old and new minimum wage.² They also show that minimum wages in the provinces with vigorous enforcement did increase average wages, but

this simultaneously had an adverse effect on employment. This trade-off between an increase in the minimum wage and job protection has been extensively discussed in the literature.

Gender and minimum wages in urban China

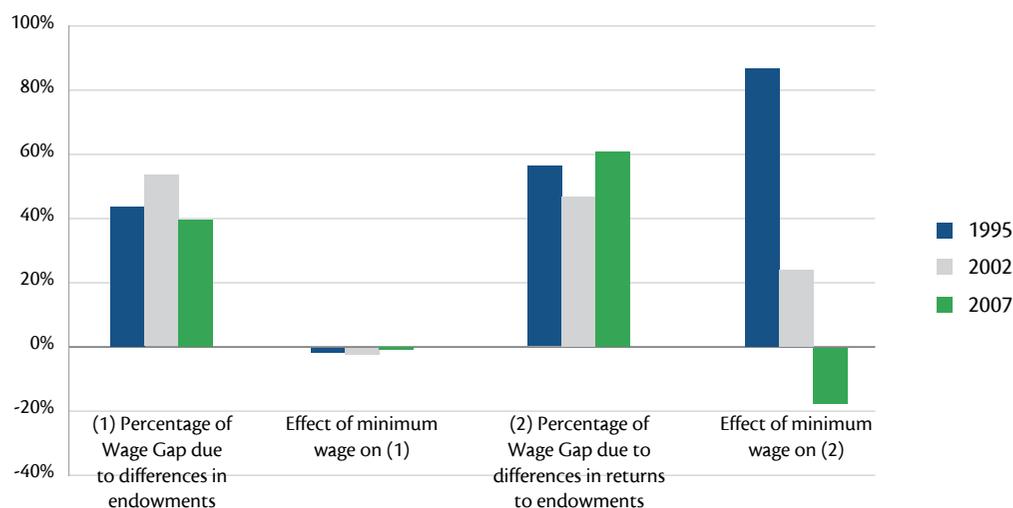
In urban China, the gender wage gap was small when there was a planned economy. But as the country began to transition to a market economy, especially after the 1990s, when state-owned enterprises (SOEs) were reformed further, the gender wage gap gradually expanded. The implementation of a minimum wage system generally contributes to an increase in wages for all low-income groups. Therefore, if a higher proportion of female workers are paid below the minimum wage level, then the implementation of a minimum wage system should narrow the gender wage gap. Ma and Li provide evidence that minimum wages do have an impact on the gender wage differentials in urban China, based on data from the China Household Income Project Surveys of 1995, 2002 and 2007.³

The authors of the study provide three major findings. First, they do not find a spike in the percentage of workers at the minimum wage as the statutory wage floors are increased, a phenomenon seen in some countries such as the United States. Second, in 1995, 2002 and 2007, the proportion of female workers earning wages below the minimum wage was higher than that of men. Third, minimum wage levels have different impacts on male and female workers' wages.^{vii} For example, in 1995 a minimum wage increase of 100 yuan (US\$ 15.6) raised males' average wages by 3.2 yuan (US\$ 0.50) and females' average wages by 2.7 yuan (US\$ 0.42).^{viii} But at the low end of the wage distribution (the 1st and 3rd percentiles), the rise in the minimum wage level has a slightly larger impact on females' average wages.

vii Ma and Li show that in 1995, the gender gap between the average wage and the minimum wage level (between males and females) is -8.0 yuan (US\$ 1.25). In 2002 and 2007, however, the gaps are 8.9 yuan (US\$ 1.4) and 22.1 yuan (US\$ 3.5), respectively. In other words, the difference between females' wages and the minimum wage standard was larger compared to those of males in 1995; in 2002 and 2007, the difference was smaller for females than for males. (See: X Ma, S Li. 2014. Impact of minimum wage on gender wage differentials in urban china, China Institute for Income Distribution Working Paper No.16.)

viii The numbers for male and female are 3.5 yuan (US\$ 0.55) and 2.8 yuan (US\$ 0.44) in 2002 and 3.4 yuan (US\$ 0.53) and 2.4 yuan (US\$ 0.38) in 2007.

Figure 2
Contribution of the Minimum Wage on Reducing Gender Wage Gaps in China



Ma and Li show that the gender wage gap is the largest in regions with high minimum wage levels, and smallest in regions with “middle” minimum wage levels.^{ix} According to their research, increasing minimum wage levels reduces the wage gap between men and women for incomes above the sixth percentile in the wage distribution. This illustrates the “sticky floor phenomenon” – a wage gap between female

workers and their male counterparts even for jobs that require relatively few skills and little education.

The study also shows that endowments – for example, land, skills, and time – lead to a gender wage gap directly, because men receive a higher set of endowments than women. There is also a gap in terms of return on endowments; in other

^{ix} According to Table 1 in Ma and Li, middle and high minimum wage levels are 165-175 yuan (US\$ 25.8- US\$ 27.4) and over 175 yuan (US\$ 27.4) in 1995, 285-330 yuan (US\$ 44.6-51.6) and over 330 yuan (US\$ 51.6) in 2002 and 510-615 yuan (US\$ 79.8 – 96.2) and over 615 yuan (US\$ 96.2) in 2007, respectively. (See: X Ma, S Li. 2014. Impact of minimum wage on gender wage differentials in urban china, China Institute for Income Distribution Working Paper No.16).

words, even if men and women had the same set of endowments, men would earn more. The study finds that the gender pay gap is due even more to the latter than the former.

Both the effect of endowments and the effect of the returns to endowments are affected by changes to the minimum wage. Changing the minimum

wage impacts returns to endowments more than it affects the distribution of endowments themselves. The fourth column in **Figure 2** shows the effect of the minimum wage on the gender wage gap via the returns to endowments. The implication is that raising the minimum wage is a more effective tool for narrowing the gender pay gap than directly providing women endowments.

Table 1
Decomposition of Earnings Inequality and Contributions of the Minimum Wage, 2004-2009

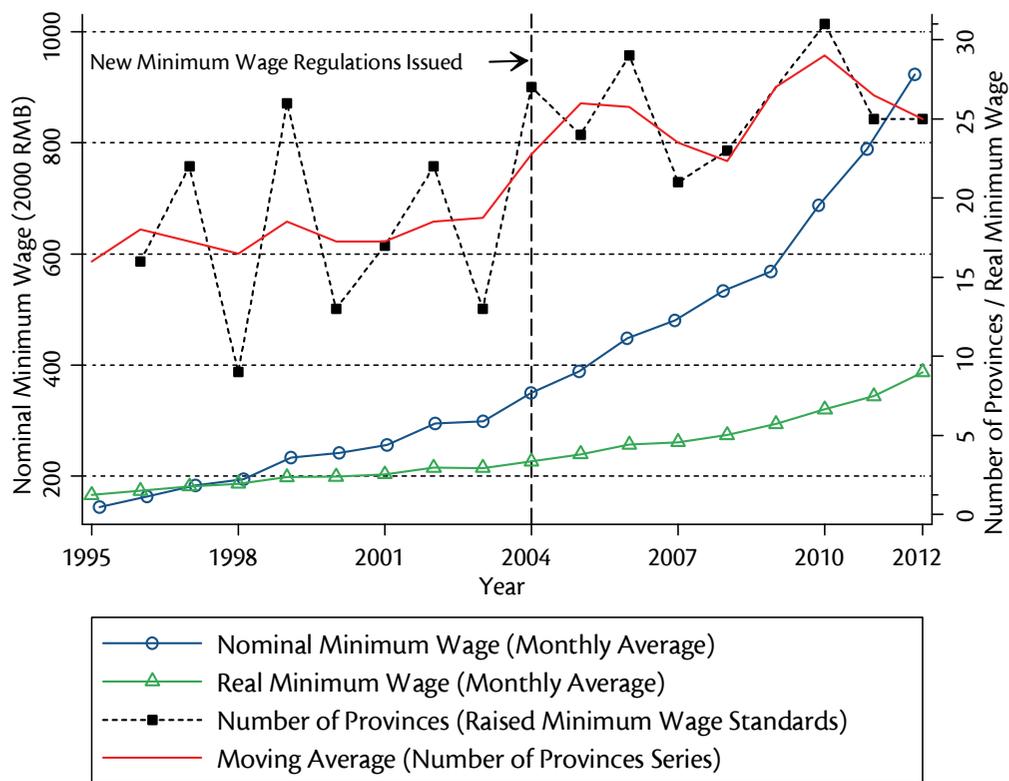
For wage earners at the lower end of the distribution, changes to the minimum wage have the effect of reducing inequality. Labor market characteristics, meanwhile, have caused inequality to increase.

Earnings inequality measure	Total change between 2004 and 2009	Due to	
		(1) Changes in minimum wage	(2) Changes in labor market characteristics
Gap between 50th percentile and 10th percentile of wage earners	.058*** (.007)	-.092*** (.012)	.150*** (.013)
Gap between 50th percentile and 25th percentile of wage earners	.031*** (.006)	-.044*** (.010)	.076*** (.010)
Gap between 75th percentile and 50th percentile of wage earners	.046*** (.005)	.043 (.032)	.003 (.012)
Gap between 90th percentile and 50th percentile of wage earners	.019*** (.006)	-.003 (.026)	.022 (.025)
Gap between 90th percentile and 10th percentile of wage earners	.077*** (.008)	-.095*** (.033)	.171*** (.032)
Gini coefficient	.004*** (.002)	-.050*** (.013)	.055*** (.012)
Variance of log earnings	.022*** (.002)	-.069*** (.013)	.091*** (.013)

*** denotes a high degree of statistical significance (p-value of 0.99)

Note: The table is drawn from Lin and Yun (2015). All numbers are in log points. Bootstrapped standard errors with 100 repetitions are given in parentheses. Earnings gaps, Gini coefficients and variances are calculated at individual level.

Figure 3
Minimum Wages in China, 1995–2012



Note: Nominal wages have been adjusted for inflation and are expressed in 2000 yuan (RMB).

Minimum wages and inequality in urban china

Lin and Yun used a large set of city-level data, containing relevant information on the minimum wage combined with a longitudinal household survey of 16 representative provinces, to estimate the effect of minimum wage changes in China over the period 2004-2009 across different income groups.⁴ Compared to previous studies using provincial-level data and reporting mixed results, their study shows that minimum wage changes significantly help reduce the earnings gap at the bottom end of the earnings distribution – between the 10th percentile and the median wage. As one would expect, minimum wage changes did not have an effect on other parts of the wage distribution – for instance, the gap between the median wage and the 90th percentile. Their analysis also suggests that minimum wage reduces earnings inequality measured, for example, by the Gini index.

Lin and Yun's findings are consistent with recent studies for other countries, reporting that the minimum wage plays an essential role in lowering wage inequality. Both the U.S. and Mexico, for example, have seen a declining real minimum

wage and rising inequality, and empirical evidence shows that the declining minimum wage accounts for a substantial part of the growth in inequality in both countries over the past three decades.⁵ In contrast, China has experienced both a rapid increase in the minimum wage *and* rapidly increasing income and earnings inequalities in the past 10 years.

Lin and Yun's findings that minimum wage increases have beneficial effects on the earnings distribution – by reducing the earnings gap particularly at the bottom end of the wage distribution – have both regional relevance and general implications in the context of the minimum wage literature. They break down the rise in inequality to show that minimum wage mitigated that increase.

For example, from 2004 to 2009 the earnings inequality between the 10th percentile and the median wage grew, but by far less than it would have without minimum wage.^x In other words, the increase in income inequality that China has witnessed would have been more severe if not for the growth in minimum wages.

By offsetting the costs of a higher minimum wage by increasing the number of working hours, employers do not see the need to layoff workers.

^x The earnings inequality between the median and 10th percentile workers (p50-p10) grows by 0.058 log point from 2004 to 2009. By decomposing this gap, they find that labor market characteristics increase the gap by 0.150 log point, whereas the minimum wage significantly decreases the gap (-0.092 log point) during this period.

Minimum wages and migrant workers

The minimum wage in China has received increased attention because of growing income inequality and the vulnerable position of low-wage migrant workers who are flooding into cities. The national minimum wage in China has more than doubled over a brief period: from 474 yuan (US\$ 74) in 2004 to 1072 yuan (US\$ 167.37) in 2011. In advanced economies, most low-wage workers are paid by the hour and regulations prevail on legal working hours. In China, by contrast, most low-wage migrant workers are paid by the month, and minimum wage legislation does not specify the number of working hours. As such, employers may extend employees' working hours to compensate for increased costs. This unintended consequence of the minimum wage legislation is of particular importance for migrant workers who may receive less legal protection and may be more affected by minimum wage legislation than other workers.

Most low-wage migrant workers are paid by the month, and minimum wage legislation does not specify the number of working hours. As such, employers may extend employees' working hours to compensate for increased costs.

Yang and Gunderson used a large migrant household survey dataset and municipal data to investigate the impact of increases of minimum wages on migrant workers' wages, employment and working hours.⁶ The results indicate that the minimum wage has only small negative impacts on migrants' employment, with the largest negative effects for rural female workers and for workers in east and central China. But because employers increase the hours worked by migrant workers in each month to offset some of the cost increases due to higher monthly minimum wages, the amount workers actually earn per hour does not increase. This adjustment in part explains the absence of adverse employment effects that are commonly found in the minimum wage literature on China. By offsetting the costs of a higher minimum wage by increasing the number of working hours, employers do not see the need to layoff workers.

Conclusions

The minimum wage has been regarded as an important element of social protection policy in many countries around the world. Increasing the minimum wage is intended to raise wages for millions of low-income workers and enhance their well-being. Yet existing literature from mostly industrialized countries provides no consensus on whether the minimum wage is an effective policy tool. Studying the effects of the minimum wage is even more complicated in developing countries such as China than it is in industrialized countries because of large informal sectors in urban areas, large pools of surplus labor in rural areas, and difficulties in ensuring compliance with minimum wage legislation. Since China instituted its first minimum wage law in 1994, the magnitude and frequency of changes in the minimum wage have been substantial, both over time and across jurisdictions.

China is a large developing country that is transitioning to a market economy, with an abundance of workers in low-paid occupations that are affected by changes in the minimum wage. Although its experience with minimum wages is new, the findings of this chapter's authors offer general implications for other transition and developing economies. Most

importantly, this research on China shows that when the minimum wage increases rapidly – an 11 percent per year growth rate since 2004 – the effects are significant. China's experience illustrates that rapid increases in minimum wages have led to an increase in average wages and a reduction in the gender wage gap and income inequality. However, the fast rising minimum wage has resulted in job losses for young adults, women, and low-skilled workers.

This research highlights the importance of rigorous research to inform evidence-based policymaking. Despite the fact that the minimum wage policy is popular and welcome by most policymakers and workers around the world, the debate in academia has gone on for decades, and no consensus about its effects have emerged. Minimum wage policy should focus on its initial intended purpose – ensuring that workers receive remuneration at a particular threshold to provide for their basic needs. Beyond that, the minimum wage should not be used as the primary tool to accomplish other political and economic goals, such as increasing average wages or promoting social development; there are other more effective policy tools to achieve these broader goals.

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THE MISUNDERSTOOD MINIMUM WAGE

A case study of South Africa

Aalia Cassim, Ben Jourdan and Kavisha Pillay, Development Policy Research Unit

Development Policy Research Unit (DPRU)

The Development Policy Research Unit (DPRU) has been actively engaged in policy-relevant socio-economic research since 1990, establishing itself as one of South Africa's premier research institutions in the fields of labor markets, poverty and inequality. The DPRU is a University-recognized research unit located within the School of Economics at the University of Cape Town. Through the application of economic and statistical techniques, DPRU's aim is to produce academically credible and rigorous policy analysis.



SOUTH AFRICA



24.9

Unemployment Rate



65.0

GINI



84.5

Wage and salaried
workers, total (% of
total employed)



14659

GDP per person
employed
(constant 1990 PPP \$)

THE MISUNDERSTOOD MINIMUM WAGE

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Introduction

After independence from colonization, many countries within Africa introduced some form of minimum wage legislation. According to the ILO,¹ 37 out of the 55 African countries had a minimum wage policy framework by 2008. However, very few of these countries have tested the economic and labor impacts of such legislation.

Studies conducted in various other developed and developing countries on the impact of minimum wages have produced mixed results and spurred a debate that stretches as far back as 1913.² On the one hand, classical economic theory claims that if mandated wages are higher than what the equilibrium of supply and demand for labor would require, the result

will be adverse effects on employment, hours worked, and non-wage benefits.³ On the other side of the debate is the argument that with an increase in minimum wages comes a reduction in poverty and inequality and increased demand for goods and services, fueling economic growth.⁴ Overall, the results produced from these studies on this matter depend on the country context, methodology used, and, in some cases, perceived bias of their authors.¹

Several studies have measured the effects of minimum wages on employment, wage levels, hours of work and contractual obligations in South Africa. In addition, researchers have examined the institutions mandated to set and

i For example, Card and Kruger's (1994) seminal paper *Minimum Wages and Employment: A Case Study of the Fast Food Industry in New Jersey and Pennsylvania* claimed increases in wages did not lead to disemployment effects. However, this paper spurred several response papers from Neumark and Wascher (1995, 2000) which claimed to use the same data set but found disemployment effects. See: D. Neumark and W. Wascher. 1995. *The Effect of New Jersey's Minimum Wage Increase on Fast-Food Employment: A Re-Evaluation Using Payroll Records*. Cambridge: National Bureau of Economic Research, Working Paper 5224; D. Neumark and W. Wascher. 2000. *Minimum Wages and Employment: A Case Study of the Fast-Food Industry in New Jersey and Pennsylvania: Comment*. *American Economic Review*, vol. 90, 5:1362-1396

enforce minimum wages within the country along with levels of compliance with minimum wage legislation. While some sectors such as agriculture appear to be significantly impacted by minimum wage increases, other sectors have witnessed little or no adverse effects. In some of these studies, employers have adapted to minimum wage laws by reducing employees' hours of work rather than laying them off. Importantly, these studies show that, for workers, the benefit of increased wages outweighed the loss in hours worked.

Overall, much is misunderstood about minimum wages within South Africa. Workers' unions within the country lobby for doubling or even tripling the current minimum wages and claim that no adverse effects to employment or the economy

Workers' unions within the country lobby for doubling or even tripling the current minimum wages and claim that no adverse effects to employment or the economy would result. Some employers' organizations believe that minimum wages should be abolished completely, and that the free market should set wages.

would result. Some employers' organisations believe that minimum wages should be abolished completely, and that the free market should set wages. These two policy stances represent opposite ends of a spectrum of opinions in South Africa. Yet they share common characteristics: they are unrealistic and would both be detrimental to the economy and social well-being of the country's poor population. This chapter seeks to provide clarity on the topic of minimum wage legislation by contextualizing the debate and detailing sector-specific empirical evidence of minimum wage legislation's impact in South Africa given the country's unique historical, social and economic context. It then outlines policy recommendations based on the core concerns around minimum wages in the country.

Background: The minimum wage policy framework in South Africa

The major legislative frameworks that govern labor relations in South Africa today are the Labour Relations Act of 1995 and the Basic Conditions of Employment Act of 1997, which outline the country's two major wage-setting systems:

- Collective bargaining through bargaining councilsⁱⁱ
- Sectoral Determination (SDs) that are published by the Ministry of Labour and set minimum wages for sectors/areas

The Labour Relations Act (1995) created a voluntary system that promoted centralized bargaining while extending collective bargaining rights to almost all employees. It established private sector bargaining councils as well as public service bargaining councils for civil servants. The Basic Conditions of Employment Act of 1997 sets a minimum floor of rights for all employed individuals in the South African labor market and allows for the Minister of Labour to create SDs that dictate the conditions of employment, including minimum wages, for vulnerable workers in a specific sector.

However, the bargaining council framework, through which some sectoral wages are determined in South Africa, faces some of the same challenges as its predecessor law in terms of its effectiveness and ability to represent and cover a wide spectrum of workers and businesses, enforce compliance, and manage the tradeoff between employer and employee interests.ⁱⁱⁱ Currently, there are 47 bargaining councils in South Africa spanning from the clothing industry to civil engineering.

Sectoral Determinations, first introduced in 1999 with the contract cleaning sector, cover a range of sectors including wholesale and retail, domestic workers, farm workers and private security, amongst others.⁵ In total, there are currently 124 different wage schedules legislated through SDs that apply across various sectors, areas and occupations. Compared to other BRICS and African countries, this is a high number of minimum wage rates, contributing to the wage system's complexity and making it difficult to enforce (See **Table 1** below).

*ii Bargaining councils can be understood as institutionalized collective bargaining structures established by one or more registered trade unions together with one or more registered employer organizations for a specific area and sector in the economy. They are statutory in the sense that they apply to and are officially recognized by the registrar of labor relations. Participation in a bargaining council is voluntary and the parties negotiate wages, conditions of employment, and social benefit funds. See: S. Godfrey, J. Maree, D. Du Toit, & Theron, J. (2010). *Collective Bargaining in South Africa: Past, present, and future?* Claremont: Juta & Co, Ltd.*

*iii Benjamin, Borat, & Cheadle (2010) also note rigidities in the labor market are also due to the inefficient judiciary system. While the Commission for Conciliation, Mediation and Arbitration (CCMA) has been proven to efficiently resolve labour disputes, Labour Courts in South Africa have created substantial labor market hysteresis. See: P. Benjamin, H. Borat and H. Cheadle. 2010. The cost of "doing business" and labour regulation: The case of South Africa. *International Labour Review*, 149: 73–91.*

Table 1

Minimum Wage Schedules in Select African and Emerging Economies

Country	Number of Wage Schedules
Brazil	1
Russia	1
Uganda	1
Mali	1
Ghana	1
Malawi	1
Nigeria	2
Botswana	10
Zambia	10
Tanzania	29
China	31
Namibia	32
India	45
Kenya	55
Ethiopia (public sector)	57
South Africa	124

Source: Various Labour Departments of Respective Countries and ILO TRAVAIL Database.

The impact of sectoral minimum wages in South Africa

The number of empirical studies focused on the impact of minimum wages in South Africa is relatively small compared to the number

conducted in developed countries. Only seven sectors have been studied, and no economy-wide impact studies exist. What the sector-

specific studies show is that minimum wages have had varying effects on employment, hours worked, and wages. These studies also demonstrate a relationship between compliance and enforcement of already established minimum wages and the impact of new minimum wage legislation in South Africa.

In the domestic workers sector, Hertz found that employment decreased and working hours were reduced after the introduction of a sectoral minimum wage for domestic workers over the period 2001 to 2004.⁶

Average wages within the sector, however, did increase as a result of the minimum wage. This is in contrast to more recent work by Dinkelman & Ranchhod⁷ and Borat, Kanbur & Mayet,⁸ which found no clear evidence of disemployment effects. Borat, Kanbur & Mayet did find that hours worked were reduced, but that increases in the minimum wage outweighed this effect in terms of workers' overall income.⁹ In other words, even if their working hours were reduced, workers were still earning more due to the rise in the hourly wage. In addition to the domestic workers sector, Borat, Kanbur & Mayet also examined the

retail, private security, forestry, and taxi sectors. The authors found no disemployment effects in these sectors and showed that real hourly wages

increased for all sectors as a result of the legislation, except for the forestry and taxi sectors.¹⁰

In agriculture, Borat, Kanbur & Stanwix found significant negative employment effects as a result of the introduction of minimum wages in the sector.¹¹ Additionally, average wages and the incidence of a written contract increased substantially. Garbers

found that an increase in agricultural minimum wages in 2003 was accompanied by job losses of approximately 16 percent, of which 7.5 percent was directly attributable to higher unskilled labor costs resulting from a higher wage floor.¹² Conradie surveyed 190 wine and table grape farmers in the Western Cape and found that a 10 percent increase in the minimum wage had led to between 3 and 6 percent of workers being let go.¹³ Murray & van Walbeek surveyed 103 farmers in Natal and found no large disemployment effects. However, they estimate that workers' hours were reduced by between 22 percent

It appears that employment in the agricultural sector was most negatively affected by the introduction of minimum wages in 2003 – replaced mainly by mechanization and casual labor. The result of introducing minimum wages in other sectors seems to be mixed but with no major negative impacts.

and 40 percent.¹⁴ Sparrow et al¹⁵ found that an increase in labor costs motivated employers to replace farmworkers with machinery and casual laborers.^{iv}

Overall, from the literature examined above, it appears that regular employment in the agricultural sector was most negatively affected by the introduction of minimum wages in 2003 – replaced mainly by mechanization and casual labor. The result of introducing minimum wages in other sectors seems to be mixed but with no major negative impacts. However, where negative effects have been identified, marginalized

populations – such as women, youth and low-skilled workers – seem to be most affected. For example, the impact of the 50 percent increase in agricultural minimum wages in 2013 has not yet been analyzed empirically, but there is some anecdotal evidence to suggest that employment in the Western Cape has been affected, and that employment losses have been concentrated among women.^v

A minimum wage, however, will only have an impact in the event that it is enforced and therefore compliance plays a key role in determining the outcome of minimum wage policies.

Compliance and enforcement: A difficult balance

South Africa, like many other developing countries, witnesses high rates of minimum wage non-compliance. Concerns over the economic effects of minimum wage laws – understandably prominent in the context of active labor market policies – have largely overshadowed the discussion of compliance and enforcement. Internationally, the research in this area is nascent and in many cases the data are inadequate to understand enforcement practices and the

various elements that influence compliance. However, papers by Borat et al,¹⁶ Rani et al¹⁷ and Almeida et al¹⁸ provide clear evidence that many workers covered by minimum wage legislation around the world still earn wages below the legal minimum. These studies have found that factors such as levels of unemployment, firm size, informality, intensity of inspection, and the steepness of fines for non-compliance all influence compliance rates.

iv Farmworkers in this context are full-time, formally employed workers in the sector. Casual laborers are part-time and informally employed – i.e. no contract or working conditions established, typically paid below the legislated minimum wage, v This information comes from interviews with DoL officials and private correspondence with Ruth Hall at PLAAS.

Table 2

Maximum Permissible Fines for Violation (Schedule 2 of the BCEA, 1997 as amended 2014)

No previous violation	R 300 (US\$ 22.74) per employee
No previous violation in respect to the same provision of the Act	R 600 (US\$ 45.50) per employee
A previous violation the same year or two violations in respect to the same provision during the past 3 years	R 900 (US\$ 68.22) per employee
3 previous violations of the same provision within 3 years	R 1200 (US\$ 90.96) per employee
4 previous violations of the same provision within 3 years	R 1500 (US\$ 113.70) per employee

Source: Basic Conditions of Employment Act, 1997

This section presents updated data on the level and depth of non-compliance in South Africa for each of the SDs – meaning the percentage of workers who are underpaid and the degree to which they are underpaid, respectively. It then provides a brief overview of the enforcement procedures in South Africa at present.

Minimum wage regulations in South Africa are currently enforced by labor inspectors who conduct workplace inspections and serve employers with penalties for violations of stipulated employment conditions listed within SDs. Information on the penalties for non-compliance with the minimum wage law reveals that while repeat offenses and

greater levels of underpayment attract larger penalties, overall the fines are small compared to the degree to which employers underpay their workers (see **Table 2**).

The evidence suggests that compliance levels are generally low across the developing world and that more rigorous enforcement measures are needed to ensure that firms, as well as households, do not underpay their employees.

What then do levels of compliance look like in South Africa? **Table 3** uses the violation index to report the levels and depth of non-compliance for each covered sector. The index allows us to calculate the overall level of non-compliance, which is simply the percentage of workers who earn below the minimum wage that applies to them. It also allows us to go beyond this to calculate the depth of this non-compliance, which measures how far below the minimum wage these workers earn, on average.

Table 3

Level and Depth of Minimum Wage Violation by Sector, 2013

Worker Category	Percentage of Workers Earning Below the Minimum Wage	Average Degree to Which Workers are Earning Subminimum Wages
Agriculture	0.65	0.26
Forestry	0.75	0.33
Domestic Workers	0.40	0.14
Private Security	0.65	0.28
Wholesale and Retail	0.47	0.24
Taxi	0.38	0.18
Hospitality	0.37	0.16
Contract Cleaners	0.56	0.24
Average	0.53	0.23

Source: Labour Market Dynamics Survey, 2013. Statistics South Africa, own calculations

The numbers are striking, but it must be noted that a high degree of wage dispersion among minimum wages in a sector can cause overestimation. Because there are multiple minimum wages within a sector, the calculation presented here is based on the average wage rate for the sector. Survey data shows the actual number of workers earning below that average sectoral wage rate. In a sector like Wholesale and Retail or Private Security – where there are several and disparate fixed minimum wages, and the higher wage grades pull up the average minimum wage – the percentage of workers earning below their stipulated wage may be overestimated.

On average, 53 percent of workers covered by an SD report earning wages below the legislated minimum, and among those earning subminimum wages the average distance from the minimum wage is 23 percent (i.e. if a stipulated minimum wage is R 100 (US\$ 7.58) per hour, a worker is earning R 77 (US\$ 5.84) per hour, on average). This average, though, masks large intra-sectoral differences in compliance rates. The highest rates of non-compliance are found in the forestry sector where approximately 75 percent of workers earn below the minimum wage, while in the hospitality sector this figure falls to 37 percent. The depth of non-compliance also differs

significantly by sector and is smallest among domestic workers and highest among workers in private security.

Concerning government policy on enforcement, it is evident that if minimum wages are not effectively enforced, the intended policy benefits will largely be restricted to a small proportion of low-paid workers in the public sector. The evidence suggests that compliance levels are generally low across the developing world and that more rigorous enforcement measures are needed to ensure that firms, as well as households, do not underpay their employees.¹⁹

South Africa is not unique in this regard. Two fundamental issues face policymakers on minimum wage: First, the level at which minimum wage should be set, and second, the degree to which it is enforced. Setting the minimum wage should balance potential wage gains against the

risks of adverse effects on employment, while also taking account of the extent to which wage laws can be enforced. Evidence shows that minimum wages in developing countries tend to be set fairly high relative to the median wage, and that they are often set above the median wage for unskilled labor. Andalón and Pagés,²⁰ for example, find that minimum wages in Kenya are set high relative to the median wage (above 70 per cent of the median wage in salaried employment) and thus non-compliance levels in the country are also high. South Africa's experience is similar.

While a number of African countries implemented minimum wage legislation many decades ago, the impact of minimum wages on key labor market variables is not well understood, in part as a result of non-compliance.

The observation that higher relative minimum wages are generally correlated with higher levels of non-compliance, together with the fact that these two variables constantly interact with each other, should be factored into decision-making around a minimum wage policy.

Recommendations for policymakers

South African research on minimum wages presents a number of key findings that are useful for policymakers in developing countries.

- The large number of wage schedules in South Africa has made it one of the most complex wage systems in Africa. Simplification of these schedules by having fewer minimum wages should be considered so that managing them is less resource-intensive and enforcement is easier.
- Specific consideration should be given to the agricultural sector when assessing wage adjustments within the country. Evidence shows that this sector is most vulnerable to adverse effects from wage increases.
- The level of the minimum wage plays a significant role in determining employment effects. Despite negligible effects found in some sectors from small minimum wage increases, substantial increases in minimum wages will likely have large negative impacts, as shown in South Africa's agricultural sector.
- Compliance and enforcement are critical for minimum wages to have an impact on

poverty and inequality. However, the fact is that institutional capacity to enforce minimum wage legislation is low, and increases in minimum wages actually increase the rate of noncompliance. Minimum wage policies, therefore, must be complemented with stronger social protections.

While a number of African countries implemented minimum wage legislation many decades ago, the impact of minimum wages on key labor market variables is not well understood, in part as a result of non-compliance. If anything, the research presented here suggests that the impact of minimum wage legislation cannot be easily predicted and will differ depending on a range of factors, which could include the level of the minimum wage relative to average wages, the size of the minimum wage increase, the sector under consideration, the timing of the wage changes, the level of worker productivity, the enforcement regime, and the extent of compliance. This calls for empirical research in the region to guide policymakers such that legislation plays a key role in lowering levels of poverty and inequality.

Endnotes

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THE MINIMUM WAGE DEBATE IN DECENTRALIZED INDONESIA

The power of unions and local government

Indrasari Tjandraningsih, AKATIGA - Social Analysis Center

AKATIGA - Social Analysis Center

AKATIGA is a non-profit research institute that was founded in 1991, by a group of social science researchers at Institut Teknologi Bandung and Bogor Agricultural University. Through various activities, AKATIGA helps the marginalized in expanding their access to resources and policy-making processes, especially in areas such as labor, small business, agriculture, community development, budgetary policy, and public services. AKATIGA provides input and recommendations based on the results of research to drive policy change. The process is done through advocacy and strengthening networks of marginalized groups, civil society, government, the media, and international institutions.



INDONESIA



6.3

Unemployment Rate



38.1

GINI



36.5

Wage and salaried
workers, total (% of
total employed)



11461

GDP per person
employed
(constant 1990 PPP \$)

THE MINIMUM WAGE DEBATE IN DECENTRALIZED INDONESIA

The power of unions and local government

Indrasari Tjandraningsih, AKATIGA - Social Analysis Center

Introduction

The fall of the New Order under President Suharto in 1998 ended authoritarian rule and marked the beginning of a democratic era in Indonesia. In the political context of Reformation Era Indonesia, the debate over minimum wages has been influenced to a significant degree by changes in labor policy and the move toward decentralization. Since 2000, the minimum wage increased significantly as a direct result of the rise of the labor movement and the impact of a new governance structure based on regional autonomy. During the last six years (2007-2013), the real average minimum wage among the provinces increased by 61.8 percent, with the highest single annual increase being 31.5 percent in 2013.

By shifting authority over labor affairs to local governments, this new governance structure has resulted in greater politicization of the wage-setting process.

Freedom of association in Indonesia ended the era of a single nationwide and government-controlled trade union. During the New Order, the government curbed collective bargaining in three important ways: (1) It subsumed all worker representation under one organization; (2) it limited the mandate of that singular organization to social and economic activities, circumscribing the ability to bargain collectively; and (3) it ensured control over the national union by placing its own party members in leadership positions.¹

After the fall of Suharto, the newly established freedom of association prompted a proliferation

of unions and almost instantly strengthened the power of workers' organizations vis-à-vis local and central governments. Since the year 2000, several government plans to revise labor regulations that – from the unions' point of view – had the potential to reduce workers' rights, were thrown out because of strong opposition from workers.

Workers' bargaining position also grew stronger within the process of minimum wage setting, as trade unions were afforded greater representation on wage councils. The expansion of unions' power is related not only to freedom of association, but also to regional autonomy policies introduced at the time. By shifting authority over labor affairs to local governments, this new governance structure has resulted in greater politicization of the wage-setting process.

This chapter discusses the political economy of minimum wage setting that has developed in Indonesia and seeks to examine the changing role of workers, employers, and local governments. First, the chapter explains the differences between New Order-era minimum wage setting and the regulations of the current Reformation Era. It then explains how these reforms, along with the newfound freedom of association, have transformed the political economy of the minimum wage-setting process.

The next section explores empirically how much minimum wages have actually increased. After a brief discussion of enforcement and compliance, the chapter concludes with policy recommendations toward improving Indonesia's wage-setting mechanisms.

Minimum wage setting in Indonesia's political regimes

Three factors distinguish the minimum wage policies of the New Order period (pre-1998) and the Reformation period (post-1998): the mechanics of determining minimum wages; the level of trade union involvement; and the role of local governments. In the New Order era, minimum wage setting was carried out

by national and regional wage councils that consisted of government, employer and union representatives. The latter two, however, were appointed by the government.

In the New Order, the minimum wage applied to workers with less than 12 months of employment,

– with compensation rising afterwards based on experience and on the company’s wage structure – and the minimum wage review process took place every two years. The minimum wage setting was executed by the Minister of Labor, assisted by the national wage research council, based on a proposal by the local government and local wage council.¹

There were six factors determining minimum wages as stated in the same regulation:

- Minimum needs for decent living, or KHL (Kebutuhan Hidup Layak), determined through market surveys administered by regional wage councils;
- Consumer Price Index;
- The potential impact on companies’ profitability;
- Local and regional average wages;
- Labor market conditions;

- Provincial level of economic development.

The minimum wage setting process was very simple and efficient in the New Order era. There was no objection to the minimum wage, largely

because there were neither redress mechanisms nor workers’ organizations. Even in the context of the Asian financial crisis of 1998, when the government decided not to increase the minimum wage, there was no labor unrest.²

In the political arena, the issue of minimum wages has become a vehicle for picking up workers’ votes in local elections. In some cases, local candidates have – in an effort to rally last-minute support from workers – intervened in the minimum wage setting process by violating its procedures and regulations.

Soon after the fall of Suharto, new minimum wage regulations were introduced, transferring

authority over minimum wage setting to the local government, i.e. the governor, mayor or district head. Under the new laws, the local district head (or mayor in cities) proposes the minimum wage to the governor, based on the recommendation of a local wage council.

The local wage council now has a more balanced composition of members, including government officials, trade unions and employers’ associations.

¹ As stated in the Minister of Labor’s regulation no 1/1999 on Minimum Wage. Another feature of the minimum wage law stipulated that the basic wage must make up at least 75 percent of total earnings (benefits can make up the other 25 percent).

Figure 1

Provincial minimum wage setting process



In addition to the provincial and local minimum wage, the new regulation also sets the sectoral minimum wages. The process is depicted in **Figure 1**.

Beyond mere representation on these councils, the power of trade unions to influence wage council proposals grew significantly as compared to representatives of government and employers, as the following paragraph will explain.

Another fundamental change is that the review of the minimum wage now happens once a year, doubling the frequency at which unions can exercise their power.³ The variables used in

determining the minimum wage are equivalent to the previous regulations. However, a new ministerial decree in 2005 expanded the number of items included in "minimum needs for decent living" (KHL), adding education, health, transportation, recreation and savings.

Another post-1998 change in the minimum wage setting is the right of employers to apply for temporary suspension of payment of minimum wages with the approval of the union, as stated in an article in the Employment Law of 2003. This particular article is contrary to the general applicability of the minimum wage, which is compulsory.⁴

Minimum wage setting in the Reformation Era: The power of unions and local governments

After Suharto stepped down, Indonesia's first Reformation Era presidential administration –

under B. J. Habibie – set up a plan reforming employment law with the aim of promoting the

freedom of association. The new regulations attempted to create a modern system of industrial relations that would guarantee collective bargaining rights.⁵ The government also ratified ILO Convention no. 87, Freedom of Association and Protection of the Right to Organize, and a new law on trade union rights was enacted.

The immediate result of these policies was the mushrooming of workers' organizations. The latest data from 2013 show that there are six confederations, 92 federations, 11,852 company-based unions, and 170 state-owned enterprise unions – with a total membership base of 3,414,455 workers.⁶ This still represents only 3 percent of Indonesia's workforce,⁷ but the proliferation of voices in the collective bargaining landscape has significant implications for the ways in which minimum wage setting functions.

Due largely to the reforms discussed above – along with the newfound freedom of association – the political economy of minimum wage setting has undergone a dramatic transformation in the Reformation Era. Nearly every stage of the process has become a political battleground between trade unions, the government, and employers.

Minimum wage setting has become a very dynamic process because unions now have the political capital to get actively involved in the process.⁸ Moreover, regional autonomy created

a more complex minimum wage setting process at the local level, especially in industrial zones. This growth in complexity has created additional opportunities for intervention by unions.

Minimum wages act as the core issue that unites competing unions and mobilizes hundreds of thousands of workers across the country. For each of the last 10 years, unions have leveraged the annual minimum wage setting process to flex their muscle, placing tremendous pressure on the central and local governments to set higher wages. In Jakarta and the most important industrial areas throughout Indonesia, the minimum wage fixing process is always marked by street protests and the mass mobilization of union members, who aim to influence the sessions on minimum wage setting in the local wage council.

In the political arena, the issue of minimum wages has become a vehicle for picking up workers' votes in local elections. In some cases, local candidates have – in an effort to rally last-minute support from workers – intervened in the minimum wage setting process by violating its procedures and regulations.

In 2012, for instance, a district-level incumbent made large minimum wage increases a central campaign promise.⁹ In the same year, Joko "Jokowi" Widodo – the current president of Indonesia – approved a 40 percent increase in

the minimum wage of Jakarta while serving as governor, igniting protests from employers. In other cases, local governments have tried to counter major union-led protests with steep increases in the minimum wage. This kind of action is seen by many as undermining the role of the wage council and violating the minimum wage setting procedure. Technically, however, the local head is granted this right based on the minimum wage law.

Unions see the KHL – or basic needs index – as another way to influence the process. They advocate for additional components

and for increasing the allocations for existing components, arguing that workers are entitled to better quality goods as well. For example, unions have proposed changing certain household needs, such as suggesting that the allocation for cookware should cover the cost of a gas stove rather than an oil burner. These proposals become the subject of debate between unions and employers. In 2012, a ministerial decree increased the number of items in the KHL basket from 46 to 60 items based on the results of a study on living wages,¹⁰ though the change did not meaningfully alter the KHL calculation.

Table 1

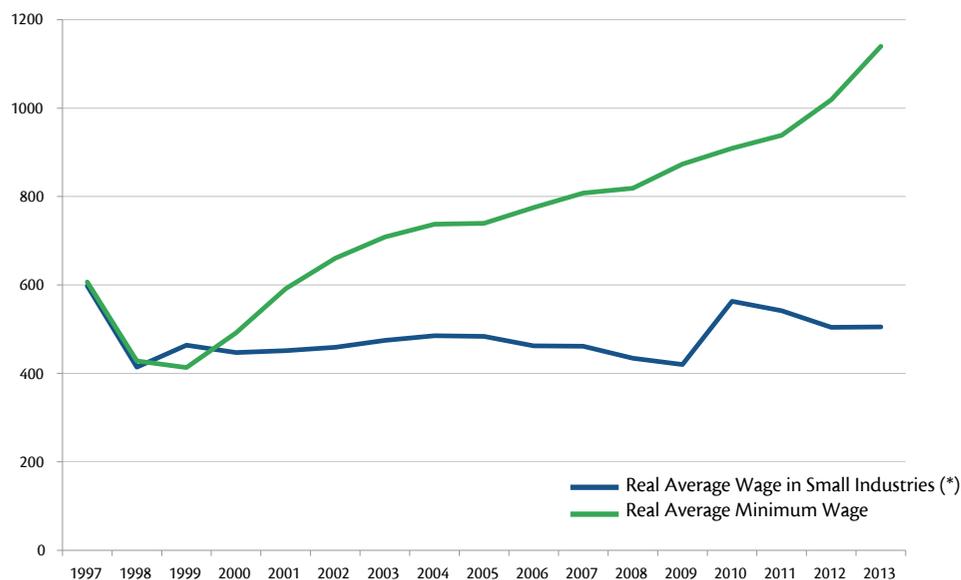
Monthly Minimum Wage 2015 – Comparison of West Java and Central Java Districts

West Java		Central Java	
District / City	Minimum Wage	District / City	Minimum Wage
Bandung	Rp 2.001.195 (US \$150)	Semarang	Rp 1.419.000 (US \$107)
Purwakarta	Rp 2.600.000 (US \$195)	Pekalongan	Rp 1.271.000 (US \$95)
Karawang	Rp 2.957.450 (US \$222)	Boyolali	Rp 1.197.800 (US \$90)
Bekasi	Rp 2.840.000 (US \$ 213)	Sukoharjo	Rp 1.223.000 (US \$92)
Bogor	Rp 2.590.000 (US \$195)	Karanganyar	Rp 1.226.000 (US \$92)

Source: Daftar UMP-UMK 2015 Seluruh Indonesia. Accessed on August 15, 2015.

Figure 2

Average Minimum Wage vs. Average Wage in Informal Small Industry Sector (1997-2013) (expressed in adjusted 2010 currency)



* A small industry/enterprise is defined to have between 5 and 19 employees.

Source: Daftar UMP-UMK 2015 Seluruh Indonesia. Accessed on August 15, 2015.

West Java, the heart of the labor movement and where the country's most important industrial areas are located, has witnessed significant increases in minimum wages. One consequence of the increases is the growing number of factory relocations into Central Java,¹¹ which has much

lower minimum wages – about half, on average – and a weaker labor movement. **Table 1** shows a comparison of minimum wages in some important industrial cities and districts of West Java and Central Java.

How much have minimum wages increased?

The result of this new dynamic of minimum wage negotiations means that the national average minimum wage has risen much faster than average wages in other parts of the economy.

Figure 2 compares the national average minimum wage to the average wage in informal small enterprises over the Reformation period.

The graph shows two important trends: First, it demonstrates that the difference between the minimum wage and wages levels that firms would “naturally” set has grown. This could have adverse impacts on employment, hours worked, and non-wage benefits. Second, the graph illustrates the increasing wage polarization between those who work in Indonesia’s formal economy, earning

minimum wages, and those who work in the informal economy, where most small enterprises are located. This could be one reason for growing inequality in the country.

Moreover, the gap between minimum wages and wages in small, informal economy industries

is widening. This means that, in theory, one barrier to formalization faced by small business – the requirement to pay workers in accordance with minimum wage standards – has grown significantly. Interestingly, Indonesia is in fact not witnessing greater levels of informality.

Increasing wage polarization between those who work in Indonesia’s formal economy, earning minimum wages, and those who work in the informal economy, could be one reason for growing inequality in the country.

In 2015, 52 percent of the country’s workers were in the informal economy, compared to nearly 66 percent in 2011.¹²

Compliance and the private sector's stance on wage developments

Employers claim the minimum wage increases have eroded Indonesia's competitiveness, soured the investment climate, and made foreign investors reluctant to come to Indonesia.¹³ This claim is rejected by unions and has become a central point of debate surrounding the minimum wage issue. Trade unions see the significant increases in the minimum wage as the end of an era of undervalued, cheap labor in Indonesia.

Businesses object most strongly to sharp increases in the minimum wage that bypass procedures for wage setting. Some employers, through industrial associations, have taken legal action against government decisions.¹⁴ Anecdotal evidence shows that other employers have shut down their factories, while many simply do not comply with the government's edicts.

A stronger industrial relations system, where unions and employers negotiate employment terms bilaterally, would also reduce the political pressure that currently weighs down the minimum wage setting process.

The level of compliance with minimum wage regulation is highly dependent on the characteristics of the company and on the effectiveness of local law enforcement. The minimum wage regulation says that only workers with less than 12 months of employment at the firm are supposed to be compensated at the minimum wage, with compensation rising afterwards based on experience and the wage structure of the company. In reality, workers with more than a one-year tenure are commonly paid the minimum wage.¹⁵ Another violation is delay in payment. Suspension of wage payments is only allowed with union and government approval, but companies sometimes take this measure unilaterally without the necessary permission.

Conclusions and policy recommendations

Since minimum wages are politically highly contentious between unions and employers, the government must play the role of a mediator. The current environment for minimum wage setting is the result of Reformation Era policies, and both unions and employers feel that the central government is in a weak position when it comes to wage policy.

First of all, local government leaders need to play a more productive role in setting the minimum wage according to the norms laid out in official policy. They have to respect unions' considerations but cannot ignore other factors, such as the business environment. Currently, government leaders prefer to avoid confrontation with unions by bowing to their demands, even if that means bypassing the established procedures for minimum wage setting, which are designed to take into account the needs of all stakeholders.

Another reason why minimum wage has become the focus of such intense political debate is because it is one of the only redress mechanisms available to workers. Whereas minimum wage was intended as a basic wage for only those workers with less than a one-year tenure at their company, it now functions as a kind of welfare policy, with other forms of collective bargaining playing a minimal role, if any role at all. A stronger industrial relations system, where unions and employers

negotiate employment terms bilaterally, would also reduce the political pressure that currently weighs down the minimum wage setting process.

To establish a more coherent and productive minimum wage setting process that is less disruptive and politicized, several steps must be taken:

1. **Reinforce the definition of the minimum wage as a safety net for workers with less than a year tenure, rather than a replacement for collective bargaining.** The government should require that companies paying a high proportion of their workers at minimum wage levels, including more experienced employees, submit to a review of their compensation structures.
2. **Maintain minimum wage setting procedures under the existing regulations.** Local governments should resist the path of political expediency and follow existing procedures for minimum wage setting, rather than issuing pre-election edicts to solicit workers' votes. This kind of unpredictable policy environment will ultimately detract from their districts' competitiveness.
3. **Revitalize and strengthen the role and authority of local wage councils.** Local governments should, first of all, respect the authority of local wage councils and

only override their recommendations in extraordinary circumstances. Second, the government has a role to play in strengthening these wage councils to ensure they reflect appropriate, equal representation of unions and employers, and that they adequately follow established procedures for recommending local minimum wages.

4. **Review the decentralized minimum wage setting policy.** The central government should undertake a review

of the decentralized wage-setting policy to determine whether it is still the most effective method. Just as minimum wage setting has become a union-dominated process in parts of the country where the labor movement is strong, it is also possible that minimum wages are too low in less industrialized regions where workers are not mobilized and the political economy favors employers.

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THE BUMPY ROAD TO A NATIONAL MINIMUM WAGE IN GERMANY

Toward revitalizing collective bargaining

Claudia Weinkopf, German Institute for Work, Skills and Training

Friedrich-Ebert-Stiftung (FES)

FES is the oldest non-profit German political foundation. Its mission is to promote and strengthen democracy through political education, dialogue, and international cooperation. FES stands for social democratic values and supports the labor movement. As the largest global center-left “think and do tank” with more than 100 offices worldwide, the work of FES intersects with politics, the economy, the trade union movement, civil society, and science. By providing more than 2,700 scholarships annually to students from socially and economically disadvantaged families, FES makes an important contribution to promoting equal opportunities in facilitating access to education.

Claudia Weinkopf contributed this chapter for FES.



GERMANY



5.3

Unemployment Rate



30.6

GINI



88.8

Wage and salaried
workers, total (% of
total employed)



43243

GDP per person
employed
(constant 1990 PPP \$)

THE BUMPY ROAD TO A NATIONAL MINIMUM WAGE IN GERMANY

Toward revitalizing collective bargaining

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Introduction

In January 2015 – for the first time in its history and after more than ten years of heated debate

– Germany introduced a national minimum wage of € 8.50 (US\$ 9.32) per hour. Up to this point, pay had been negotiated exclusively through collective bargaining between unions and employers, and the state had not intervened directly in the wage-setting process.

As this chapter will demonstrate, a key driver behind the introduction of the minimum wage was the erosion of the German collective bargaining system that began in the mid-1990s.

The rapid increase in low-paid work and the sharp downward extension of the wage scale went virtually unnoticed for almost a decade, since all the actors – including trade unions – balked at the idea that the traditional German model of negotiating wages through collective bargaining was no longer future-proof and in need of reform.

A key driver behind the introduction of the minimum wage was the erosion of the German collective bargaining system that began in the mid-1990s.

It was not until the ‘Hartz Acts’ of 2003 further expanded the low-wage sector in Germany, which was already excessively large by European standards,¹ that it became clear that trade unions in many industries no longer had the bargaining

power to set effective wage floors. Consequently, debates on minimum wage went beyond expert circles and it became a national policy issue.

Between 2005 and 2013, trade unions attempted to establish collectively agreed minimum wages at industry level – which would have rendered a national minimum wage unnecessary. These initiatives failed because the employers' associations in the largest low-wage sectors – for example, retail and hospitality – were unable or unwilling to negotiate these agreements with the trade unions.

Nevertheless, the idea behind industry-specific minimum wages – namely to strengthen the role of collective bargaining – also lies behind the new minimum wage legislation. It became part of a broader legislative package – “Act on the Strengthening of Free Collective Bargaining” – whose aim, in addition to introducing the minimum wage, was to increase the number of workers covered by collective bargaining agreements and facilitate the process of making industry-wide agreements on minimum wage legally binding.

The erosion of collective bargaining agreements

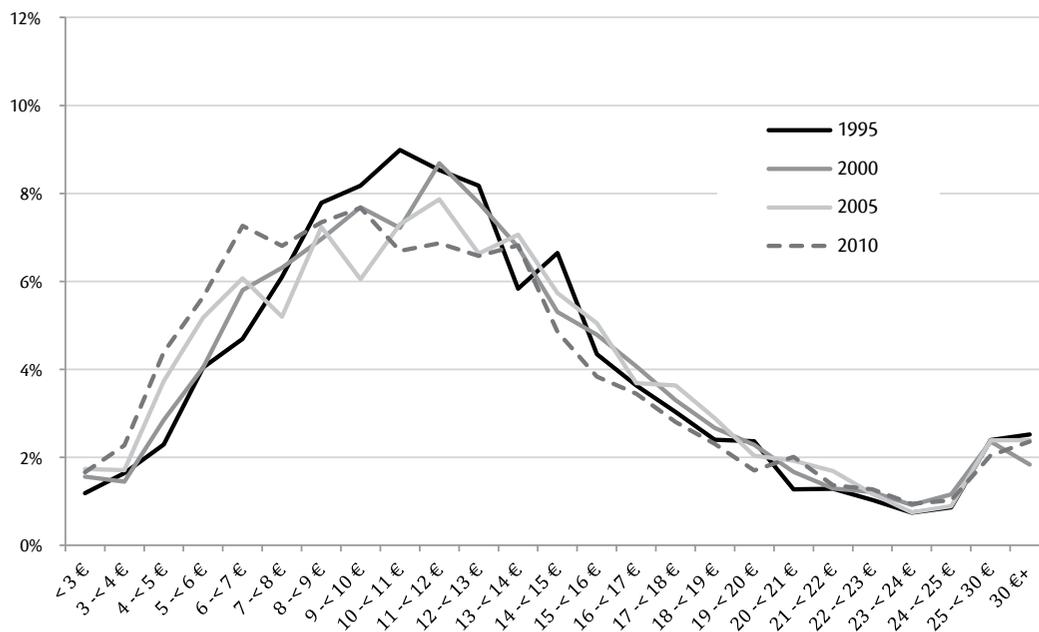
Germany was traditionally included among countries with ‘autonomous’ wage-setting systems² – meaning that companies or employers' associations and trade unions negotiated pay and many other employment conditions at the industry level and without any direct state intervention. The state intervened directly in the wage-setting process only at the request of unions and employers, specifically when they applied to make collective

The percentage of workers covered by collective agreements steadily declined. By 2013, it had fallen to just 60 percent in West Germany and 48 percent in East Germany.

agreements binding, though this was rare. Until German reunification, the percentage of workers covered by collective bargaining agreements stood at 85 percent.³ Because these agreements were negotiated at an industry level, and most companies belonged to an employers' association, this rate of coverage was several times higher than trade union density. Even companies not bound by collective agreements tended to use the collectively agreed pay rates as benchmarks.

Figure 1

Distribution of hourly wages (inflation-adjusted), all employees (students, pupils and pensioners included), Germany, 1995, 2000, 2005, 2010



Source: : Own calculations based on GSOEP.

For this reason there remained, by European standards, a relatively low share of employeesⁱ earning low wages.⁴

From the mid-1990s onwards, however, employers' compliance with collective agreements began

ⁱ Estimated at around 14 percent, depending on the choice of data sets.

to crumble. This process of erosion began in East Germany, where several developments coincided. After the sudden shock caused by the deindustrialization of East Germany's economy – mainly due to low productivity combined with the sudden introduction of the West German currency

– and the ensuing rapid rise in unemployment, many companies saw an opportunity to set wages unilaterally without negotiating with the trade unions. Moreover, most of East Germany's companies, which were new at the time, faced low productivity and were opposed to paying workers in accordance with West Germany's collective agreements. Certain sections of the employers' camp were openly preaching the benefits of withdrawing from collective agreements, and even companies not adhering the wage standards of those agreements were granted access to the employers' associations. It became evident that the trade unions in many industries did not have the power to enforce compliance with collective agreements on their own.

The percentage of workers covered by collective agreements steadily declined. By 2013, it had fallen to just 60 percent in West Germany and 48 percent in East Germany.⁵ This development was further supported by new corporate strategies

The considerable decline in coverage of collective agreements has allowed the low-wage sector to grow since 1995 to a level that is above average by European standards.

and the opening up of many public services (postal services, railways, urban transport, etc.) to private providers that were not bound by collective agreements. The wide pay differential

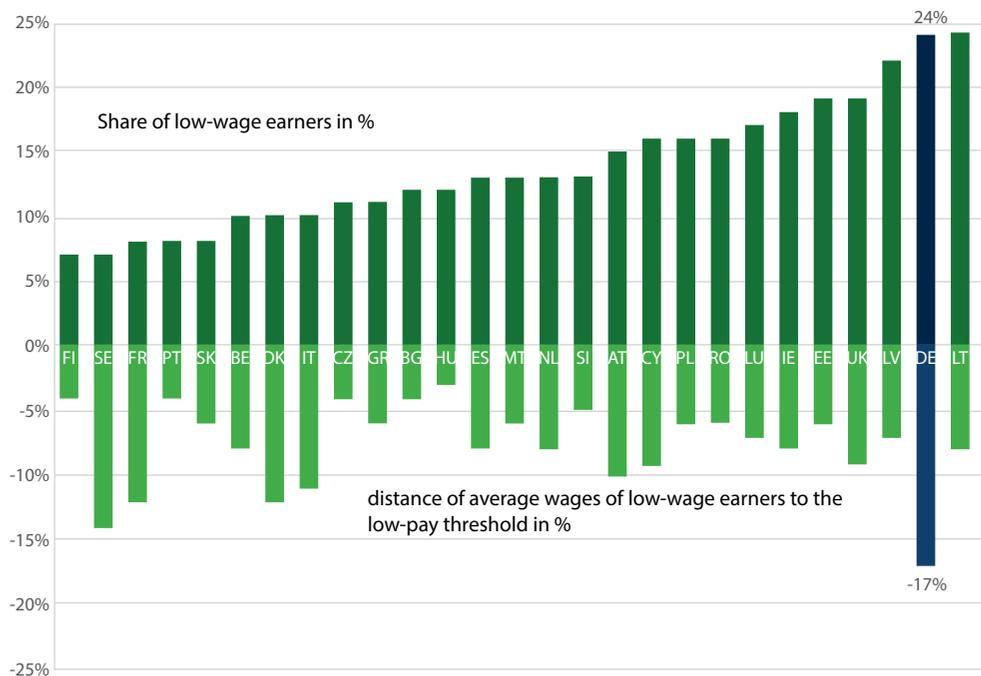
between industries and companies of different sizes, which results from the fact that smaller companies are less likely to be party to collective agreements, became a strong incentive to outsource activities in order to cut labor costs, including wages.

The 'Hartz' labor market reforms, implemented in 2003 and 2004, further changed the landscape for collective bargaining. Several changes to the relatively generous German safety net increased the downward pressure on wages. For example, the new regulations replaced income-related unemployment assistance with a standard flat payment plus an additional rent subsidy. In other words, the long-term unemployed now face dwindling assistance. Moreover, temporary agency work and so-called 'mini-jobs'ⁱⁱ were deregulated; this form of temporary and marginal

ii Mini-jobs are part-time jobs with monthly earnings of up to € 450 (US\$ 493.4) per month. Employees do not have to pay income tax or social security contributions, which make mini-jobs particularly popular for wives who prefer to work part-time. This is related to the progressive joint taxation for married couples in Germany that provides the highest tax savings if there is only one single earner (plus an additional mini-job). Although there is no legal limit as to how many hours a month people may be employed for €450 (previous limits were abolished by the new legislation) most of these jobs are marginal and part-time (up to 15 hours per week). They are widespread in private households and in the private service industries.

Figure 2

Share of low-wage workers and distance between their average wages and the low-pay threshold (less than 60% of the median wage) in the EU in 2010



Source: Enrique Fernández-Macías and Carlos Vacas-Soriano. 2013. A coordinated EU minimum wage policy? (Dublin: Eurofound), own presentation.

part-time employment with very low hourly pay has increased substantially in recent years.

The considerable decline in coverage of collective agreements has allowed the low-wage sector to

grow since 1995 to a level that is above averageⁱⁱⁱ by European standards.⁶ Furthermore, because of the absence of a statutory minimum wage, pay at the bottom end of the earnings distribution has plunged, so that the average pay gap between

ⁱⁱⁱ According to this comparison for 2010, Germany had one of the highest incidences of low wages across Europe (22 percent compared to 17 percent on average). The lowest low pay incidences were 2.5 percent in Sweden and 5.9 percent in Finland.

low-wage workers and the low-wage threshold – defined as 60 percent of the national hourly

median wage^{iv} – is greater in Germany than in any other European country (**Figure 2**).

The minimum wage and German trade unions: From disagreement to unity

The German wage-setting system, once relatively homogeneous and inclusive, is now very heterogeneous and exclusive, reflected in considerable differences in collective bargaining coverage and in the share of low-wage workers between industries. In public administration only 3.8 percent of workers are low-wage, whereas the figure stands at 64 percent in hospitality. Up until 2006, these considerable differences were an obstacle to forming consensus within the trade union movement to officially campaign for the introduction of a statutory minimum wage.

The trailblazers were the Food, Beverages and Catering Union and ver.di, the largest German service-sector union. Both recognized at an early stage that the chances of negotiating acceptable rates of pay within the existing collective bargaining system had grown slim. In other industries, such as the metalworking and chemical industries, the traditional autonomous

wage-setting system was still functioning well. In these sectors, the lowest collectively agreed rates of pay were significantly higher than any minimum wage proposal. These trade unions feared, therefore, that a statutory minimum wage would empower employers to move away from higher collectively agreed rates, discouraging workers in firms not bound by collective agreements from joining a union.

But manufacturing unions eventually realized that the outsourcing of activities to temporary work agencies or subcontractors not bound by collective agreements meant that the low-wage sector was exerting increasing pressure on their collectively agreed rates and, moreover, was eating away at their membership, too. After a debate within the trade union movement that lasted several years and was initially very heated, the German Trade Union Confederation decided at its national congress in May 2006 to campaign

iv The definition for the low-wage threshold depends on the source. While Eurostat uses 60 percent of the median hourly wage, the OECD uses two-thirds of the median wage as its threshold, and individual countries often set their own benchmarks.

for a statutory minimum wage. However, it was not until sometime after this decision that representatives of the two largest manufacturing

unions publicly expressed support for the trade unions' demand of a minimum wage floor.

The minimum wage and the German government: From resistance to acceptance

At the political level, there was strong resistance to minimum wages in the late 1990s.^v The coalition between the Social Democratic Party (SPD) and the Green Party under Chancellor Gerhard Schröder believed that high levels of unemployment at that time were driven by the low level of wage differentiation in Germany, which they regarded as a barrier to improving the employment opportunities of low-skilled workers. Cutting support for the unemployed and deregulating temporary agency work and mini-jobs through the Hartz Acts, which came into force in 2003, sought to push pay at the lower end of the wage distribution further downwards based on the notion that employment would expand.

The considerable decline in coverage of collective agreements has allowed the low-wage sector to grow since 1995 to a level that is above average by European standards.

Since the main group affected by this was SPD voters, who consequently turned away from the party in increasing numbers, the SPD's platform in the 2005 general election campaign included a pledge to introduce a statutory minimum wage. In the context of falling wages, the general population – including conservative voters – had grown increasingly supportive of a statutory minimum wage. The conservative parties in Germany allied with the SPD in the so-called 'grand coalition' (2005-2009) did not agree on a statutory minimum wage, but instead agreed to introduce additional collectively agreed minimum wages for industries where employer associations and unions jointly demanded them.

^v One exception is the construction industry, where a sector-specific minimum wage was introduced in 1997 mainly in order to ensure that posted construction workers from other countries could not be paid below the collectively agreed minimum wage

However, hopes that unions and employers would negotiate acceptable minimum wages in all low-wage sectors were not fulfilled. Only in industries with a long tradition of national collective agreements and close cooperation between the social partners (e.g. the construction industry and related trades) could these conditions be met. Consequently, these industries were among the first in which industry-wide minimum wages were established in late 1990s and early 2000s.^{vi} Other industries – for example, cleaning and industrial laundries – were dominated by regional collective bargaining or even had competing collective agreements, narrowing the prospect of reaching a mutual agreement on an industry-wide minimum wage.

The conservative-liberal coalition government in power from 2009 to 2013 refused to include the introduction of a national minimum wage in its coalition agreement. Even industry-specific minimum wages were controversial within the

coalition and as a result, decisions on declaring agreements binding were delayed a number of times. The German business world and many economists issued almost apocalyptic warnings of the dramatic job losses that would inevitably accompany the introduction of a statutory minimum wage. The estimates of the numbers of jobs that would be lost ranged from 100,000 to 4 million and were prominently published in the press over the years.⁷

In 2011, the industry minimum wages in eight German industries were evaluated by different research institutes. They came to the conclusion that the industry-level minimum wages, some of which were relatively high, had no negative employment effects.⁸ On the basis of this new evidence, the labor minister and the Chancellor declared their support for expanding minimum wages at the industry level.

However, industry-specific minimum wages could not reduce the share of low-wage workers

In 2011, the industry minimum wages in eight German industries were evaluated by different research institutes. They came to the conclusion that the industry-level minimum wages, some of which were relatively high, had no negative employment effects.

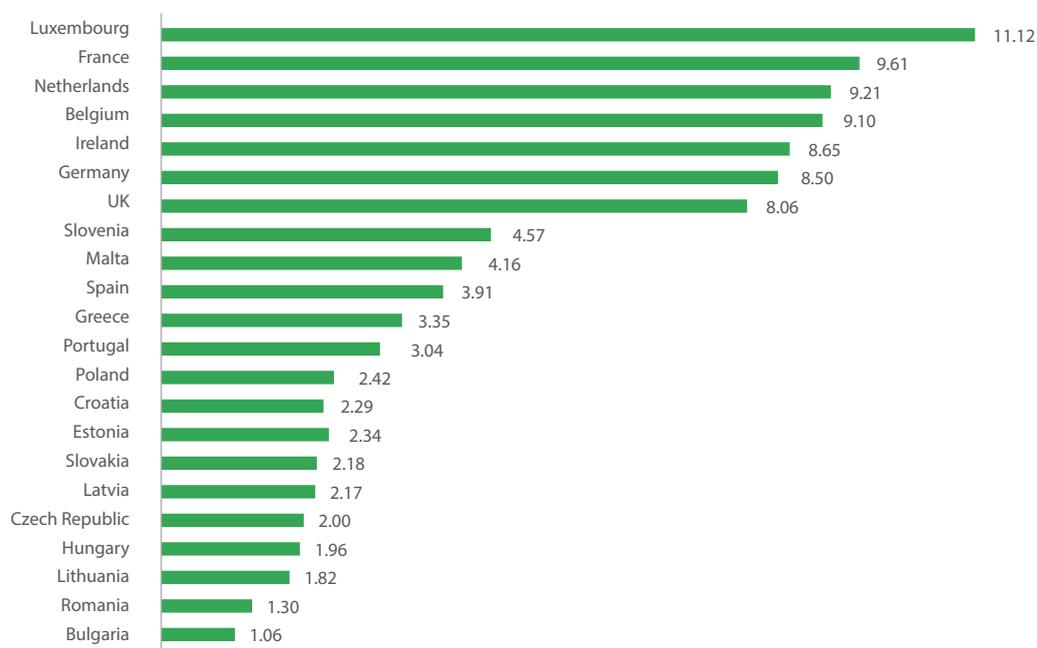
^{vi} Minimum wages for roofers and electricians were introduced in 1997 and for painting and varnishing in 2003.

in the economy as a whole. In the sectors with the highest share of low-wage workers, such as retailing, hospitality or the meat processing industry, union density and coverage by collective agreements were low and employers and their associations were so fragmented or at odds with each other that no minimum wage agreements ever materialized. This situation

was further compounded by the Confederation of German Employers' Associations (BDA). Their representatives on the national collective bargaining committee – which decides on the enforceability of collective agreements – repeatedly overturned agreements that had been reached at industry level because the agreed minimum wages were too high in their opinion.

Figure 3a

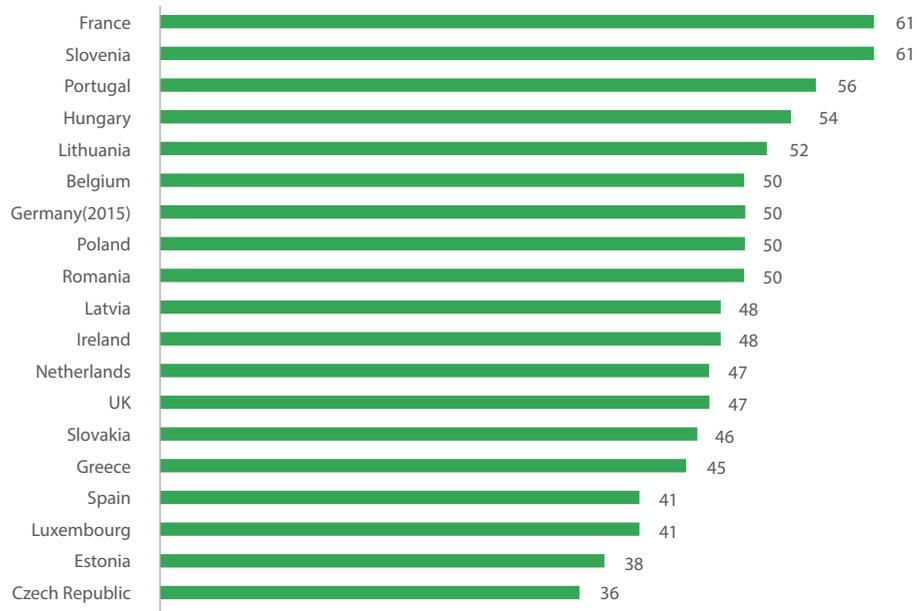
Hourly minimum wages in Europe, 2015 (€)



Source: Thorsten Schulten. 2015. WSI-Mindestlohnbericht 2015 – Ende der Lohnzurückhaltung? In: WSI-Mitteilungen 68 (2): 133-140.

Figure 3b

Hourly minimum wages in % of full-time median wages, 2013



Source: Thorsten Schulten. 2015. WSI-Mindestlohnbericht 2015 – Ende der Lohnzurückhaltung? In: WSI-Mitteilungen 68 (2): 133-140.

In 2013, the demand for a statutory minimum wage became a key issue in the general election, principally as a result of pressure from the unions. The SPD was willing to enter into another coalition government with the conservative parties only under the condition that a statutory minimum wage of € 8.50 per hour be introduced (**Figures**

3a and 3b), together with the re-regulation of temporary agency work and a strengthening of free collective bargaining. These demands were largely met, but in exchange the SPD had to accept the restrictive German fiscal policy approach favored by the conservatives under Chancellor Angela Merkel.

The design of the German minimum wage

Trade unions sought to influence the design of the minimum wage to ensure that increases in the minimum wage were decided by unions and employers – not simply state-sanctioned – and that the introduction of the minimum wage was closely linked to collective bargaining. Since the conservatives and the employers' associations were also interested in maintaining their involvement in the minimum wage-setting process, the unions achieved most of their objectives. The new Minimum Wage Act became part of a more extensive legislative package, 'Act on the Strengthening of Free Collective Bargaining'. In pursuance of the new act, industry-level minimum wages can now be agreed upon in all industries. Additionally, for an industry-wide minimum wage to go into effect, there is no longer a stipulation that at least 50 percent of the industry's workers are covered by collective agreements.

There are a few groups for whom the new minimum wage of € 8.50 per hour does not apply: trainees; the long-term unemployed for the first six months after their return to employment;

vii In 2017, all industries are obliged to have a minimum wage of at least € 8.50 (while the statutory minimum wage will be increased for the first time in January 2017).

employees under the age of 18; and – in response to pressure from the press – for newspaper deliverers until 2017. Furthermore, deviations from the minimum wage are permissible up to the end of 2016, if they are part of national collective agreements.^{vii}

The Minimum Wage Act calls for the establishment of a minimum wage commission that is tasked

The new minimum wage will impact a large segment of the labor force. As of 2012, some 6.6 million employees (19.2 percent of the workforce) were paid less than € 8.50 per hour in 2012.

with determining the wage level in the future. It consists of an independent chair, a total of six representatives from unions and employers' associations, and two academic members without voting rights. Importantly, the

law stipulates that increases in wage levels in national collective bargaining agreements serve as the benchmark for any increase in the national minimum wage. This enforces the idea that it is collective bargaining that sets the pace for future increases in the minimum wage.

The regulations on compliance with minimum wage standards are another important part of the Minimum Wage Act. In certain industries with high incidence of illegal practices – such

as construction, meat processing, or catering – working hours with start and finish times have to be recorded and the records kept for two years. This also applies to ‘mini-jobs,’ which were frequently paid below € 8.50 per hour in the past.

The new minimum wage will impact a large segment of the labor force. As of 2012, some 6.6 million employees (19.2 percent of the workforce) were paid less than € 8.50 per hour in 2012.⁹ One peculiarity of the German low-wage sector is that, although low-skilled workers are likely to be on low pay, they represent only a minority of those entitled to the minimum wage. More than three quarters of the workers earning less than € 8.50 per hour in Germany have a vocational qualification or even a university degree. It can be ascertained, therefore, that many Germans earning low wages are paid significantly below their productivity level. Since many of the workers whose wages will rise as a result of the new law are skilled, productive workers, firms in Germany are likely to absorb the cost of a rise in wages

more easily than they would otherwise through increasing efficiency.

A second peculiarity is the considerable difference in pay between East and West Germany. The minimum wage will have a particularly strong effect in East Germany, where wages are still significantly lower than in West Germany even 25 years after reunification. Several experts had even recommended a temporarily lower minimum wage rate for the East. However, politicians preferred to take into account the particular situation in East Germany by freezing the minimum wage until the end of 2016 and permitting deviations in collective agreements. In some sectors, like temporary agency work, meat processing, and agriculture, transitional rates with lower minimum wages were negotiated, particularly in East Germany. Trade unions supported such agreements only in order to revitalize collective bargaining, and on the condition that the € 8.50 threshold was exceeded before the end of 2016.

Current debates on implementation and outlook

The biggest political issue following the adoption of the new minimum wage law is its monitoring. Employers' associations are up in arms against the obligation to record working times for mini-jobbers and in industries with high incidence of illegal practices, which they have described as a 'bureaucratic nightmare'. Technically, such an obligation existed previously. Unlike in the UK, several German employers' associations and conservative politicians have not yet made their peace with the minimum wage. They would prefer a 'minimum wage-light' and are doing what they can to torpedo its implementation.

In view of the fact that the German wage-setting system has been significantly eroded over the years, the introduction of a statutory minimum wage can be regarded as one of the greatest social reforms of the post-war

period. The German minimum wage will lead to significant wage rises in the bottom two deciles of the earnings distribution and a narrowing of the gender pay gap in Germany,^{viii} since women are more likely than men to earn low wages.¹⁰ The risk to jobs tends to be low, the minimum wage is frozen until 2017 and certain sectors have been allowed transitional arrangements. Moreover,

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as three quarters of low-wage workers in Germany have qualifications, firms have opportunities to increase their efficiency. Whether the new legislative package will, as intended, lead to a revitalization of collective bargaining

and have a ripple effect on workers closer to the middle of the wage scale is yet to be seen.

^{viii} The reduction of the gender pay gap is estimated at 2.5 percentage points.

Endnotes

¹ For 2005, the low-pay incidence in Germany was at 22 percent (similar to the United Kingdom with 21.7 percent and 25 percent in the United States) while the related figures for the Netherlands (17.6 percent), France (11.1 percent) and particularly Denmark (8.5 percent) were much lower. See: Wiemer Salverda and Ken Mayhew. 2009. Capitalist economies and wage inequality. In: *Oxford Review of Economic Policy* 25 (1): 126-154.

² Jelle Visser. 2009. The quality of industrial relations and the Lisbon Strategy. In: *European Commission: Industrial Relations 2008*. 45-72. (Luxembourg: European Commission)

³ Jelle Visser. 2015. Institutional Characteristics of Trade Unions, Wage Setting, State Intervention and Social Pacts (ICTWSS): An international database. (Amsterdam: Amsterdam Institute for Advanced Labour Studies).

⁴ OECD. 1996. *Employment Outlook*. (Paris: OECD)

⁵ Peter Ellguth and Susanne Kohaut. 2014. Tarifbindung und betriebliche Interessenvertretung: Ergebnisse aus dem IAB-Betriebspanel 2013. In: *WSI-Mitteilungen* 67 (4): 286-295.

⁶ Eusebio Bezzina. 2012. In 2010, 17% of employees in the EU were low-wage earners. In: *Statistics in Focus* 48/2012. (Eurostat).

⁷ Two examples: Knabe, Andreas, Ronnie Schöb and Marcel Thum. 2014. *Der flächendeckende Mindestlohn*. Discussion Paper No. 2014/4 (Berlin: Sachverständigenrat) estimated a loss of 911,000 jobs (340,000 full-time equivalents). The German Council of Economic Experts (Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung. 2013. *Gegen eine rückwärtsgerandte Wirtschaftspolitik*. Jahresgutachten 2013/14) did not provide precise numbers but emphasized the high risk of severe negative effects of the statutory minimum wage on employment.

⁸ Joachim Möller. 2012. Minimum wages in German industries – what does the evidence tell us so far? In: *Journal for Labour Market Research* 45 (3-4): 187-199; Gerhard Bosch and Claudia Weinkopf. 2012. *Wirkungen der Mindestlohnregelungen in acht Branchen*. Expertise im Auftrag der Friedrich-Ebert-Stiftung WISO Diskurs. (Bonn: Friedrich-Ebert-Stiftung).

⁹ Thorsten Kalina and Claudia Weinkopf. 2014. *Niedriglohnbeschäftigung 2012 und was ein gesetzlicher Mindestlohn von 8,50 € verändern könnte*. IAQ-Report 2014-02. (Duisburg: Universität Duisburg-Essen).

¹⁰ Christina Boll, Hendrik Hüning, Julia Leppin and Johannes Puckelwald. 2015. *Potenzielle Auswirkungen des Mindestlohnes auf den Gender Pay Gap in Deutschland – eine Simulationsstudie*. (Hamburg: HWWI).

MINIMUM AS MAXIMUM?

Wage policies in the garment industries of select Asian countries

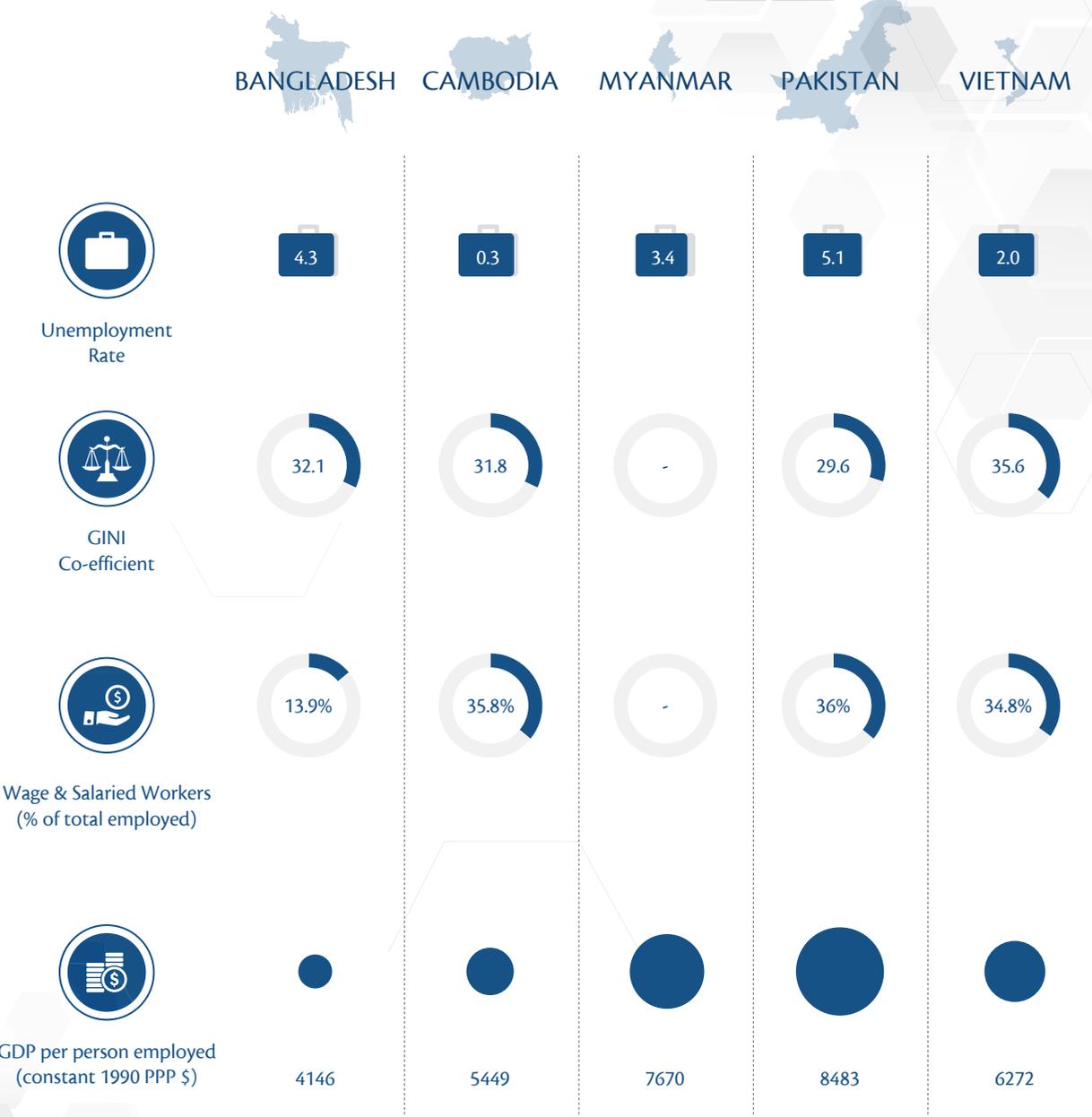
Friedrich-Ebert-Stiftung (FES) - Regional Programme in Asia

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The Friedrich-Ebert-Stiftung (FES) is the oldest non-profit German political foundation. Its mission is to promote and strengthen democracy through political education, dialogue, and international cooperation. FES stands for social democratic values and supports the labor movement. As the largest global center-left “think and do tank” with more than 100 offices worldwide, the work of FES intersects with politics, the economy, the trade union movement, civil society, and science. By providing more than 2,700 scholarships annually to students from socially and economically disadvantaged families, FES makes an important contribution to promoting equal opportunities in facilitating access to education.

The Regional Programme in Asia fosters inclusive and participatory processes where freedom, justice and solidarity are core elements of peace and security, political and socio-economic policy advancements in the Asia-Pacific region.

WAGE AND EMPLOYMENT INDICATORS



Note: Figures are from the most recent year when data were available.

MINIMUM AS MAXIMUM?

Wage policies in the garment industries of select Asian countries

Julia Mueller and Lukas Bauer (Editors)ⁱ, FES - Regional Programme in Asia

Introduction

Historically, industrial and economic development in many countries began with a focus on labor-intensive industries like garments and textiles.

ⁱⁱ Following this strategy, Asia has become the world's low-cost production hub. Developing countries like Bangladesh, Cambodia, Myanmar, and Vietnam try to emulate the successes of their Asian peers (Korea, Taiwan, Japan and more recently China) by taking advantage of cheap labor costs and a growing workforce. Economic

development in these countries has become highly dependent on their respective garment industries.

Suppliers cannot influence the prices of raw materials, energy, and transport; in contrast, labor costs are relatively easy to manipulate, making them an important production factor in global competition. In most of the countries examined in this chapter, garment industry workers are

i This article is co-authored by several representatives of Friedrich-Ebert-Stiftung (FES): Julia Mueller and Lukas Bauer (FES Singapore), Henrik Maihack and Shadhan Kumar Das (FES Bangladesh), Konstantin Baerwaldt and Myo Myo Myint (FES Myanmar), Philipp Kauppert and Abdul Qadir (FES Pakistan) as well as Erwin Schweisshelm and Mai Ha Thu (FES Vietnam).

ii There is no universal definition to distinguish between garment and textile industry. This chapter refers to "garment, which is also called wearing apparel and clothing [so called Ready Made Garments as] the main final product of the textile industry. Though the industry does have other final products, [...] their amount in terms of both consumption and production, are far smaller than the garment, in terms of both quantity and value. Broadly, the textile industry includes the entire production process for final products from fibers [...]. In the narrow sense, the textile industry contains only spinning, weaving, and knitting, namely the process that make thread/yarn and fabrics from fibers." Fukahiro, Fukunishi; Yamagata, Tatsufumi. 2014. Introduction: The Dynamism of the Garment Industry in Low-Income Countries. In: Takahiro Fukunishi et al. (IDE-JETRO). 2014. The Garment Industry in Low-Income Countries. An Entry Point of Industrialization, p. 4-5.

covered by sectoral, national and/or provincial minimum wages. They range from US\$ 67 per month in Bangladesh to US\$ 128 in Cambodia and US\$ 101 to 146 in Vietnam. Myanmar is currently in the process of setting sectoral minimum wages, including one for the garment sector.

Wages in the apparel industries remain below a living wage – despite major increases in recent years. A living wage is the minimum income necessary for workers to meet their and their families' basic needs – including nutrition, housing, health care, education, clothing, transport and savings for retirement and life risks.¹ In addition, working conditions and occupational standards in factories are frequently substandard. The 2013 collapse of the Rana Plaza factory in Bangladesh has increased international scrutiny of precarious working conditions and low wages in the Asian garment industry. Consumers especially have become more aware of workers' grievances, leading to increased public pressure on international clothing brands. These brands have therefore signaled their willingness to

improve cooperation with trade unions for better working conditions and higher wages.

But has the situation changed in recent years?

Do workers now receive a larger share of growing profits and is the paradigm of the global garment industry leading to shared prosperity? If yes, what are the driving forces behind wage adjustments? How significant are collective bargaining agreements? And has there been a trade-off between wage hikes and competitiveness?

This chapter analyses and contextualizes the wage developments in the garment industry in five Asian countries: Bangladesh, Cambodia, Myanmar, Pakistan, and Vietnam. In addition, it evaluates their national mechanisms and dynamics of wage formation and identifies common trends and challenges the industries face as well as country-specific characteristics.

Suppliers cannot influence the prices of raw materials, energy, and transport; in contrast, labor costs are relatively easy to manipulate, making them an important production factor in global competition.



1. Bangladesh

Henrik Maihack and Shadhan Kumar Das

Fast Growth with Low Wages

Bangladesh's low labor costs have made the country the second biggest garment exporter after China.² Accounting for 81 percent of Bangladesh's total exports³ and for 14 percent of its GDP,⁴ the garment sector is of crucial importance to Bangladesh's economy. More than 4 million workers are employed in more than 4,000 mainly locally owned factories across the

country.⁵ Producing almost exclusively readymade garments (RMG), the sector continued to grow in 2014 with exports worth US\$ 25.4 billion,⁶ down slightly to 9 percent growth from the five-year average of 12 percent.⁷ It provides much needed jobs for a growing labor force.ⁱⁱⁱ

However, the Rana Plaza building collapse in 2013 that killed 1,137 people and injured more than

iii For an overview of developments in export value, export shares, as well as employment trends in the sector see: Bangladesh Garment Manufacturers and Exporters Association. 2015. Trade Information. Accessed July 31, 2015. http://www.bgmea.com.bd/home/pages/tradeinformation#.VbsUI_nli8A.

2,500 workers⁸ tragically demonstrated the risks and exploitative working conditions in many of the country's factories. In the aftermath of Rana Plaza, renewed global attention has been brought to the poor enforcement of safety and social standards as well as the low wages in Bangladesh's RMG industry. Even after a 77 percent hike in the sector-wide monthly minimum wage for RMG workers, from 3,000 Taka to 5,300 Taka (US\$ 38 to 67) for the lowest and 13,000 Taka (US\$ 164) for the highest of seven pay grades, Bangladesh's RMG workers continue to earn the lowest minimum wage among RMG workers in Asia.⁹

Wage formation – No Regular Wage Setting Mechanism

The minimum wage for the RMG sector is determined by negotiations through the Minimum Wages Board (MWB), formed under the legal framework of the Bangladeshi Labour Act.^{iv} The MWB includes representatives from the government, business owners, trade unions and independent experts, all of whom are

Negotiations at the Minimum Wage Board and collective bargaining on the factory level continue to be hampered by organizational weakness and conflicts among trade unions in Bangladesh as well as a political economy that heavily favors factory owners.

nominated by the government. Upon receiving a recommendation from the MWB, the government sets the final minimum wage. So far, the MWB has only been convened five times (in 1983, 1994, 2006, 2010 and in 2013)¹⁰ to revise the minimum wage in the RMG sector and always on an ad hoc basis, as there are no regular (annual or biannual) meetings of the MWB.

Negotiations at the MWB and collective bargaining on the factory level continue to be hampered by organizational weakness and conflicts among trade unions in Bangladesh as well as a political economy that heavily favors factory owners. So far, workers are organized in trade unions in only 10 percent of the factories, and only 5 percent of the overall RMG workforce. This makes it difficult for labor representatives to influence industry-wide decisions.¹¹ A positive sign is an increase in trade union registrations (around 300 new registrations in 2014 and 2015) in the aftermath of the Rana Plaza collapse. However, given the highly fragmented union landscape, the extent to which a large number

iv Chapter 11 (sections 138-149) of the Bangladesh Labour Act 2006 deals with Minimum Wages Board.

of newly registered unions will improve workers' bargaining power remains to be seen.

Wage development – Wages Increased but Remained Low

In 2013, shortly after the Rana Plaza building collapse and in the context of growing international pressure, the government formed a new six-member MWB for the RMG sector to revise the previous minimum wage of 3,000 Taka. Subsequently, the trade union delegate on the MWB demanded a minimum wage of 8,000 Taka.¹² Employers on the MWB set off protests with an initial offer of just 4,500 Taka, leading to the temporary closure of 250 garment factories. The MWB finally recommended 5,300 Taka (US\$ 67) for the lowest salary grade (of seven occupational grades), which was consequently set by the government as the new minimum wage for the sector starting December 1, 2013.

Despite this 77 percent increase, an annual inflation rate of more than 6 percent over the last decade and an even higher inflation rate for food and rent close to RMG factories mean that the

new minimum wage is still too low. The current Labour Act, however, states that the cost and standard of living of workers should be taken into consideration while recommending a minimum wage for a sector. Prominent experts from the Center for Policy Dialogue (CPD), one of the leading think tanks in Bangladesh, have argued that the current minimum wage also does not correspond to the actual productivity of workers. CPD recommends a minimum wage of at least 8,200 Taka (US\$104) for an entry-level worker.¹³ The new minimum wage falls even further short of the 25,687 Taka (US\$ 325) that the Asia Floor Wage Alliance calculates to be a living wage for

Some factory owners have avoided paying the higher minimum wage by including holiday bonuses and overtime compensation in the basic wage payments. Others have categorized more workers in the lower pay grades.

a Bangladeshi RMG worker and her or his family.¹⁴

The implementation of the new minimum wage has been sluggish and has prompted further criticism. Some factory owners have avoided paying the higher minimum wage by including holiday bonuses and overtime compensation in the basic wage payments. Others have categorized more workers in the lower pay grades. More workers, and for longer periods of time, are now declared “apprentices” – not one of the seven grades covered by minimum

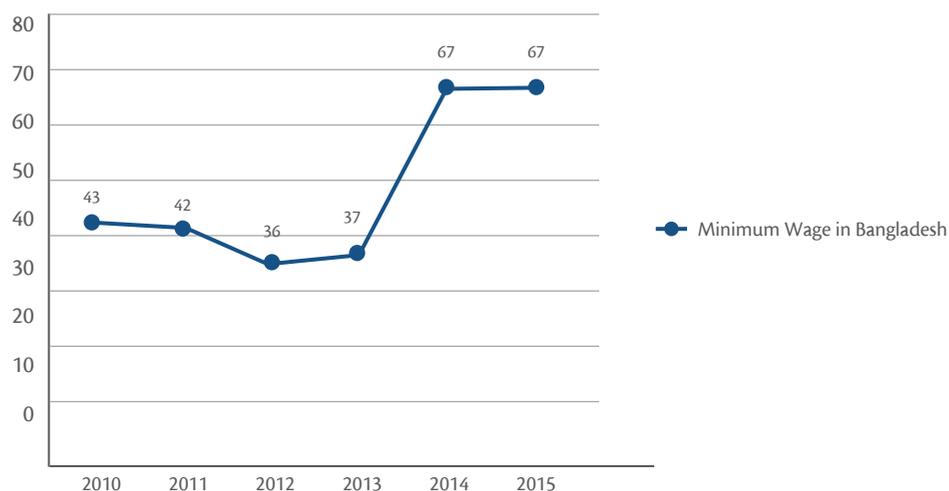
wage – so that factory owners can pay less than the minimum wage. In addition, female workers face persistent discrimination. First, wages for male workers are 42.5 percent higher than wages for women across all pay grades,¹⁵ and second, men are also much more likely to get promoted.

A Call for Fair Social Dialogue

A political economy tilted towards the interests of unified factory owners, international clothing brands unwilling to pay their suppliers more for RMG products, and a low density of trade union

membership has kept the minimum wage for Bangladesh's RMG sector lower than that of any other country in Asia. As a result, the willingness among international brands to pay suppliers more and readiness among factory owners to share this increased margin with their workers are crucial preconditions for ensuring RMG workers receive a living wage. For this to happen, the development of a democratic, strong and unified trade union movement in Bangladesh with solidarity from the international trade union movement is essential.

Figure 1
**Real Minimum Wage in Bangladesh
2010 - 2015 (US\$)**



Note: The authors calculate the real value of the minimum wage, adjusting for inflation, at the level of BDT 3,000 (2010-2013) and then BDT 5,300 (2014-2015).



2. Cambodia

Julia Mueller and Lukas Bauer

Industrial Growth and Industrial Unrest

Cambodia's political opening and the transformation to an open market economy in the early 1990s resulted in significant economic restructuring and integration in regional and global trade. Even though its share of the global garment market is still relatively small, the fast-growing garment industry – in addition to agriculture and tourism – has played a crucial role in Cambodia's economic development. Garment

exports increased on average 16 percent annually between 2000 and 2014, thereby growing more than twice as much as the overall GDP (7 percent).^{16,17} The sector accounts for 16 percent of the country's GDP¹⁸ and over 80 of exports¹⁹, benefiting from preferential customs and trade tariffs like the EU's "Everything but Arms" initiative.^v

Around 600 factories, largely owned by foreign investors, employ an estimated 650,000

v As part of the EU Generalized System of Preference (GSP), the "Everything but Arms" initiative started in 2001. It allows duty- and quota-free imports from Least Developed Countries (LDCs) - including Cambodia - for most products (except arms and munitions), including garments, into the EU. UNCTAD. 2011. The 'Everything But Arms' initiative. Accessed July 31, 2015. http://www.unctad.info/en/Infocomm/Agricultural_Products/Banana/Economic-policies/The-Agreement-Everything-But-Arms/.

workers.²⁰ Today the trade union movement in Cambodia is characterized by fragmentation and competition along political lines with more than 3,000 unions and several dozens of federations and confederations. While the garment sector has a unionization rate of about 40 percent,^{vi} unions' influence and bargaining power is limited, partly due to the lack of unity among them and corruption.

Still, over the past years, several trade unions have put extensive pressure on the government, employers and international brands to increase the minimum wage and to improve working conditions in the industry. After a violent crackdown on demonstrating workers in January 2014,^{vii} and the temporary suspension of the freedom of assembly, the government agreed to increase the sectoral minimum wage by 28 percent.^{viii}

Today the trade union movement in Cambodia is characterized by fragmentation and competition along political lines with more than 3,000 unions and several dozens of federations and confederations.

Wage formation – Wage Setting Rather than Negotiation

The Labour Code of 1997 guarantees a minimum wage “without distinction among professions or jobs”²¹. In reality a minimum wage only exists for the garment sector. It is determined by the Ministry of Labour and Vocational Training after consultation with the Labour Advisory Committee (LAC) which is composed of representatives from government (14), employers (7), and employees (7). Usually, the tripartite consultations end when unity among the workers' representatives breaks apart, with some unions offering to support the government.²² In 2014, the LAC was reformed in an important way: It now meets annually in the second half of the year to review the current minimum wage. Prior to that it was convened irregularly.²³

vi However, many trade unions are dominated or influenced by the employers. The cross-sector unionisation rate amounts only 7.7 percent.
vii The violent interruption of a peaceful demonstration by the military police led to five dead, several injured, and the arrest and detention of 23 workers, the UN Special Rapporteur on the situation of human rights in Cambodia, Surya P. Subedi reported to the UN Human Rights Council, www.ohchr.com.

viii Based on eight hours per day or 48 hours a week (six days a week).

The outcome of the minimum wage negotiations is crucial for workers' salaries as there are no sector-wide collective bargaining agreements (CBAs) and firm level CBAs rarely go beyond the benefits and compensations set in the minimum wage proclamation ("Prakas").^{ix} As a result, the projected average income of garment workers in 2015 (US\$ 147 to 157)²⁴ hardly exceeds the monthly minimum wage of US\$ 128. Its composition also shows that, on average, workers may not be receiving overtime compensation of at least US\$ 1.00 per hour, the legal stipulation.^x

Wage development – Economic or Political Necessity

The Cambodian government and the Garment Manufacturers Association in Cambodia (GMAC) seek to keep wages low, arguing that this will attract more foreign direct investment (FDI) and

create additional jobs.²⁵ At the same time, they raise the specter that steep rises in the minimum wage might cause fashion brands to shift to countries with lower wage costs.

But over the last five years – in response to a shifting political context and growing international

Over the last five years – in response to a shifting political context and growing international pressure – garment workers in Cambodia have witnessed the doubling of their minimum, after more than a decade of relatively stagnant wage growth.

pressure – garment workers in Cambodia have witnessed the doubling of their minimum, after more than a decade of relatively stagnant wage growth. The sharp rise from US\$ 80 (2011) to US\$ 128

(2014) must be understood as compensation for missing wage adjustments over the past few years when the minimum had not been increased despite high inflation rates and a tremendous hike in living costs.

The political context is largely responsible for forcing a shift in minimum wage policy. The main opposition party, Cambodia National Rescue Party

ix "Between 2008 and 2010, around 15 high quality agreements were reached that appear to be working well, and around 30 'high quality' agreements are currently active. [...] However, many [of the 405 CBAs registered CBAs with the ministry by 2012] were negotiated by non-recognised bargaining agents such as shop-stewards, which raises doubts over their quality." Most CBAs in Cambodia covering only single issues (e.g. food allowances); however, the number of more comprehensive CBAs are on the rise. Cf. ILO. Decent Work Country Programme Cambodia (2011-2015), p.24; accessed June 10, 2015.

x Monthly minimum wage of US\$ 128 breakdown to hourly rate of US\$ 0,66 based on 8 hours a day and 48 hours a week with the factor 1.5. See: WageIndicator Network. 2015. Labour Law Overtime Compensation. Accessed June 8, 2015. <http://www.prake.org/home/labour-law/compensation>.

(CNRP), grew its vote share significantly in the July 2013 general elections, especially among young workers in garment factories. In the aftermath of the elections, the CNRP contested the official result, stating that the party was “robbed of crucial votes that would have put them in front,”²⁶ and boycotted the Parliament. During numerous demonstrations the CNRP supported workers’ demands for a major increase in the minimum wage. In January 2014, the government not only forcefully dissolved strikes; it also removed opposition protest camps in “Freedom Park,” a public square in the center of Phnom Penh. The political stalemate ceased in July 2014 when the CNRP ended its boycott and the parties agreed on a joint reform agenda²⁷ and on further engagements based on a “culture of dialogue.”²⁸ By the end of 2014, the ministry announced the 28 percent increase of the minimum wage to US\$ 128 and social partners agreed on annual negotiations of the minimum wage.

While the adjustments of the minimum wage represent a promising development, wages are still far too low to enable a decent living for the workers and their families.

xi Letters from international brands to Keat Chhon, Permanent Deputy Prime Minister dated September 18, 2014 and from November 10, 2014. Accessed April 23, 2015. http://www.industrial-union.org/sites/default/files/uploads/documents/Cambodia/letter_to_dpm_cambodian_government_september_2014.pdf; http://www.fairlabor.org/sites/default/files/letter_from_global_brands_on_wages_in_cambodia_nov_2014.pdf.

xii The full study remains unpublished, though its main points have become public. *The Cambodian Daily*. February 12, 2014. *Labor Ministry Ignored Its Own Research on Minimum Wage*. Accessed May 28, 2015. <https://www.cambodiadaily.com/archives/labor-ministry-ignored-its-own-research-on-minimum-wage-51977/>.

xiii 275 PPP\$ converted to Cambodian Riel (rate 1,562.92, based on World Bank 2013), own calculation; The Asia Floor Wage Alliance calculated EUR 285.83 as the Cambodian minimum wage in 2014.

Aside from domestic forces at play, a total of 17 international brands argued in a statement in 2014 that they “supported workers’ right to a fair wage” and called for “an inclusive and consistently applied national collective bargaining process” in letters to the Cambodian government.^{xi}

While the adjustments of the minimum wage represent a promising development, wages are still far too low to enable a decent living for the workers and their families. A study^{xii} commissioned by the Ministry of Labor and Vocational Training found that the minimum wage must range between US\$ 157 and 177 a month to cover workers’ basic needs.²⁹ The Asia Floor Wage Alliance calls for a much higher number of US\$ 278.14^{xiii} per month.

From the Streets to the Negotiating Table

The Cambodian garment industry was at one point seen as a potential role model for the global

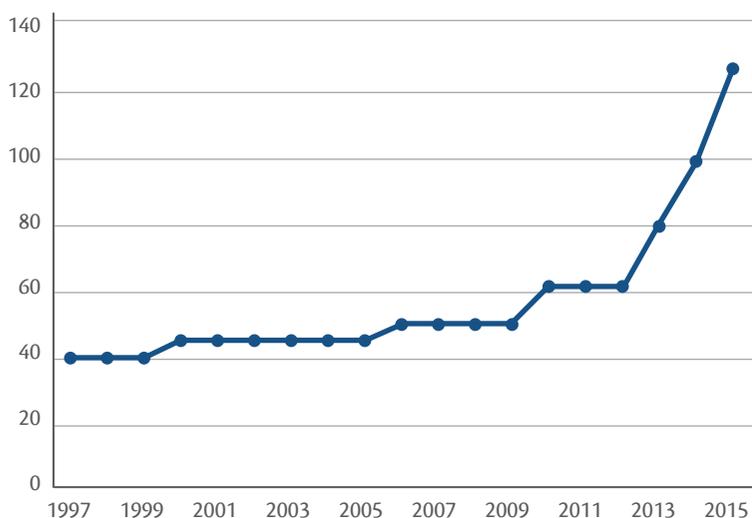
garment industry, with comprehensive factory monitoring and strong worker protections.^{xiv} However, working conditions in Cambodia still remain poor, not only in terms of occupational health and safety but also in terms of forced and inadequately compensated overtime, discrimination against pregnant workers, short-term contracts and unpaid bonuses.³⁰

For the past years, increases in the minimum wage were mainly dependent on political circumstances

rather than the result of a democratic social dialogue. While the establishment of an annual minimum wage review is a positive sign, it is crucial that the Cambodian trade unions stay united. Fair and effective collective bargaining on the factory level needs to be an additional step to ensure that workers and their families can afford a decent living from the wages earned. The current minimum wage of US\$128 for the first time exceeds the national poverty line of US\$ 120 in 2014.³¹

Figure 2

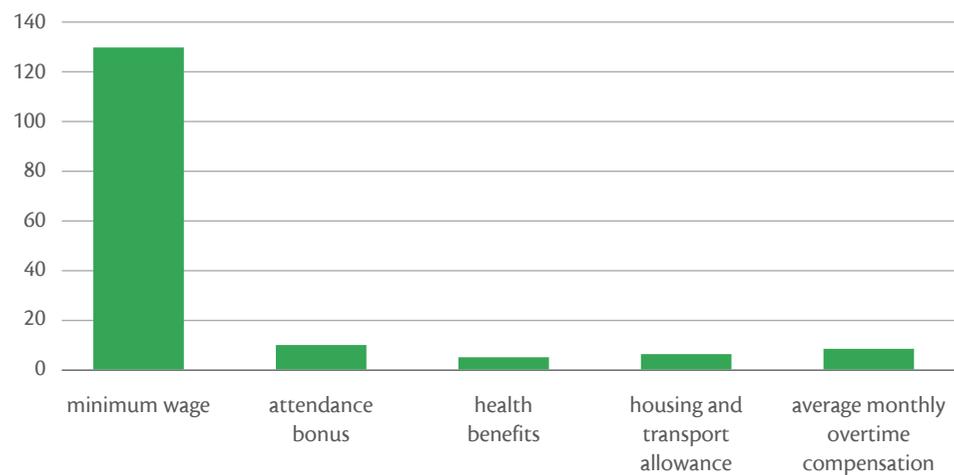
Minimum Wage in Cambodian Garment Sector 1997-2015 (US\$)



Source: Cambodian Ministry of Labour and Vocational Training (MoLVT) and Ministry of Commerce (MoC)

xiv In 2001, the ILO “Better Factories Cambodia Programme” (BFC) was launched as a result of a trade agreement between Cambodia and the US. It was established aiming at improving the working conditions in exchange for better access to the US market. BFC monitors and reports on the compliance with international and national labour standards in the more than 500 participating exporting factories. For further information: <http://betterfactories.org>.

Figure 3
**Average income composition among
Cambodian garment workers (US\$)**



Source: Wageindicator. 2014. Minimum Wage for the Garment and Shoe Industry in Cambodia w.e.f October 1, 2010



3. Myanmar

Konstantin Baerwaldt and Myo Myo Myint

An Industry on the Rise

Garments are virtually the only manufactured exports of Myanmar. The turning point for the garment sector came around 1989 when – after more than 25 years of Burmese socialist rule – the new government decided to end its isolationist economic policies and open its economy to the international market. The share of garments in total exports increased from 2.5 percent in 1990 to 39 percent in 2000. The industry has been, and is still concentrated on cutting, making and packing (CMP) processes. At its earlier peak in 2000, it was estimated that around 400 factories employed about 135,000 workers. However, when

the industry was ready to take off, the military regime's oppressive politics drove the United States and the European Union to boycott "Made in Myanmar" products and impose sanctions. The majority of domestic firms and some foreign firms shut down immediately.³²

After the new civilian government came into power in March 2011, the reinstatement of the EU's Generalized Scheme of Preferences (GSP) program and the lifting of sanctions by the United States allowed Myanmar garments to regain access to these two important markets. As a result, in 2011-12 the total value of garment exports

amounted to US\$ 845.9 million, and in 2012-13 the value grew to US\$ 904 million, contributing to about 9 percent of the value of total exports.^{xv} In 2013-14, garment exports exceeded US\$ 1 billion, amounting to some 10 percent of total exports. The sector's annual growth is approximately 20 percent.^{xvi} According to the Myanmar Garment Manufacturers Association (MGMA), there are currently about 300 to 400 factories employing 200,000 to 250,000 workers – nearly double the number at the earlier peak in 2000.³³

National-level Minimum Wage Policy – Waiting for the Announcement

Currently, there are no minimum wage standards for the private sector in Myanmar. As soon as the

Labor Organization Law (2011)^{xvii} and Settlement of Labor Disputes Law (2012)^{xviii} were enacted, the workers from the garment sector used their newly obtained rights to demand wage increases.

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With the number of strikes growing, a monthly minimum wage of Myanmar Kyat 56,700 (US\$ 65) was temporarily established in the industrial zones. Due to enforcement problems, however, the Ministry of Labor, Employment and Social Security soon

drafted a bill to create a mechanism for setting a national minimum wage.

The Minimum Wages Law was enacted in March 2013, replacing the 1949 Minimum Wage Act.^{xix} To set the minimum wage, a national minimum wage committee under the office of the President was

xv Roughly 40 percent of Myanmar's exports are petroleum and gas. Total exports data for Myanmar are obtained from the World Bank Group, Myanmar Economic Monitor, 2013. Garment export data are obtained from UN Comtrade.

xvi Figure is based on an estimate only as there is no exact data available. The annual export growth rate of the garment sector fluctuates. Its export grew in average by 21 percent between 2010 and 2011 and 53 percent between 2011 and 2012. Latest reliable data were not available.

xvii The Labor Organization Law sets the legal framework for the founding and operation of trade unions on the company, city, regional and national level.

xviii The Settlement of Labor Disputes Law stipulates rules and regulations to solve labour disputes by means of negotiation, mediation and legal action.

xix The Minimum Wage Act from 1949 was never fully implemented and was limited to milling, cigars- and cheroot rolling industries and parts of the public sector. Additionally, in contrast to ongoing discussions on the introduction of locally specified minimum wages, the old act did not foresee the introduction of different minimum wage levels for different regions.

formed in September 2013, with representatives from employer and employee organizations, responsible government departments as well as independent experts. The government considers the recommendations of the committee, but they are not legally binding.

Since then, the Ministry of Labor, Employment and Social Security, together with the International

Labour Organization and the local research organization Myanmar Development and Resource Institute (MDRI) have been conducting surveys to determine an appropriate minimum wage. On June 29,

2015, the National Minimum Wage Committee proposed a daily minimum wage of Kyat 3,600 (US\$ 2.90) per eight-hour workday. The garment manufacturers criticized the proposal as too high. Finally, after months of protest and dispute, the government confirmed a daily minimum wage of 3,600 Kyat (US\$ 2.90) on August 18, 2015. A monthly minimum wage is yet to be proposed.³⁴

Minimum Wage Policy in the Garment Sector – A Very Low Basic Wage

In the absence of a minimum wage for the garment sector, salaries of the workers are composed of a relatively low basic wage of around US\$ 25 to 30 per month supplemented by overtime payments, regular attendance bonuses, production bonuses or targets, living allowances and transportation

allowances. Although wages in the garment sector have increased from time to time, this has been offset by increasing inflation and the rising cost of living and consumer goods, particularly in Yangon, the country's largest city.^{xx} Including

overtime compensation and other allowances, the actual average income ranges from about US\$ 80 to US\$ 110. Basic wages vary slightly from one factory to another. As basic wages are not sufficient to meet living costs, overtime is necessary for almost all factory workers in the garment sector. In general terms, the basic wage component is only about 35 to 40 percent of the total wage.

Although wages in the garment sector have increased from time to time, this has been offset by increasing inflation and the rising cost of living and consumer goods, particularly in Yangon, the country's largest city.

xx The inflation rate averaged 5.12 percent from 2010 to 2014. The rate decreased to 2.8 percent in 2011 and 2012, but increased to 5.7 and 7.06 percent in 2013 and 2014 respectively. Central Statistics Organization, World Bank and Trading Economics. Accessed April 28, 2015. <http://www.tradingeconomics.com/myanmar/indicators>.

There is no legally binding collective bargaining agreement for minimum wages at the industry level so far, with all collective bargaining agreements negotiated at the plant or firm level. This is in large part due to the fragmented nature of the trade union movement.

The industry is currently facing an increasing number of strikes mainly caused by two grievances: low wages and excessive overtime. A total of 85 labor unions with roughly 13,000 members had been formed as of December 2014 at the factory level in the garment industry – a unionization rate of less than 1 percent. However, membership is on the rise.³⁵

The Need for a Wage Reform Mechanism

The Myanmar garment sector still has relatively low labor costs, but faces increasing demand

for higher wages by workers. At the same time, importing countries and buyers are paying more attention to comply with social standards and protection. Labor unions, employers as well as government bodies are playing an important

While the importance of setting a minimum wage is widely recognized by all stakeholders, the current unpredictable economic and political situation in combination with a highly volatile labor market undermines efforts to create an institutionalized, effective and efficient wage determination mechanism in Myanmar.

role in establishing a wage reform mechanism. The cooperation of international organizations may also have an impact on minimum wage policies. While the importance of setting a minimum wage is widely recognized by all stakeholders, the current unpredictable economic and political situation in combination with a highly volatile

labor market undermines efforts to create an institutionalized, effective and efficient wage determination mechanism in Myanmar.



4. Pakistan

Philipp Kauppert and Abdul Qadir

Pakistan's Garment Industry as Part of a Larger Textile Industry

Textile and garment industries have a long history in Pakistan and have provided important employment and business opportunities. According to the All Pakistan's Textile Mills Association (APTMA), there are 452 textile units, 90 percent of which are located in the provinces of Punjab (65 percent) and Sindh (25 percent).³⁶ Garment manufacturing is an important but minor sub-sector of the overall textile industry, which is comprised of cotton yarn, cotton fabric

and clothes, and textile made-ups (knitwear, home textiles and readymade garments). Textile products make up 54 percent of all exports, and clothing contributes around one third of this figure.^{xxi}

Textile production has remained stagnant over the last decade, while the value-added garment sector including Ready Made Garments (RMG) has only grown marginally. By international comparison, the export industries have lost ground in competitiveness against other

xxi Due to the lack of specific data on garments the section on Pakistan will mainly refer to the textile sector in a broader sense (cf. definition in footnote II). Wherever possible, garment specific data is supplied; however comparability of the data will be limited.

developing economies in South and Southeast Asia. The reasons for this development include the difficult security situation, high costs of energy generation due to frequent power cuts, low rates of both public and private investment, and the lack of a comprehensive industrial policy.

The textile industry, including garments, provides employment for around 5 million workers (40 percent of the industrial labor force) in Pakistan, accounting for 8 percent of GDP and nearly

25 percent of all value-added products. Pakistan's textile value chain consists of 10 sub-sectors, from cotton picking all the way to finished garments. The garments manufacturing segment generates the highest employment within the textile value chain.³⁷ In 2014, its share of EU and U.S. apparel markets was 2.8 percent and 2.2 percent, respectively. Over 75 percent of the industry is comprised of small-and medium-sized units.^{xxii,38}

In September 2012, a fire in the garment factory in "Baldia Town" in the area of Karachi killed 258 workers. This tragic incident has led to controversial

By international comparison, the export industries have lost ground in competitiveness against other developing economies in South and Southeast Asia.

debates about insufficient occupational health and safety measures at the factory level but also generally ineffective labor market regulations. The Generalized Scheme of Preferences (GSP) Plus – a conditional trade agreement between Pakistan and the European Union that came into effect in

2014 – provides incentives for more effective implementation of social standards. In this context, trade unions can play a crucial role in holding employers accountable for compliance with the legal framework. But the labor

movement, comprised of around 8,000 registered unions and 1.2 million members (2.5 percent unionization across all sectors; no data available for garment sector) is still weak and faces many internal and external challenges: fragmentation and flagrant violations of workers' constitutional and statutory rights and their freedom to organize and collectively bargain.

Wage formation – Politics of Provincial Minimum Wage Setting

Based on the 18th Amendment to the Constitution in 2010, minimum wages at the provincial level are

xxii According to Pakistan's classification system, small and medium enterprises include units or firms with up to 250 employees, fixed capital PKR 25 million (about US\$ 245,000) and annual sales of less than PKR 250 million (about US\$ 245 million). (See: http://www.smeda.org/index.php?option=com_fsf&view=faq&catid=3&faqid=48)

xxiii The Constitutional Amendments devolved many federal subjects including labour to four provinces, thus creating separate federal and provincial territorial labour jurisdictions in the country.

determined by Provincial Minimum Wages Boards (MWB).^{xxiii} In June 2015, the central government announced a new minimum wage of PKR 13,000 (US\$ 130) for employees in the public sector, and it is expected that most provinces will also adopt this minimum.

The MWBs are tripartite provincial bodies, composed of government officials, workers' representatives, and employers' representatives all nominated by the provincial government.

Criteria for minimum wage fixing are inflation, cost of living and economic growth indicators. The minimum wages are announced at the time of budget speeches to the federal and provincial legislatures, leading to competition among ruling parties to set higher minimum wages than their rivals in other jurisdictions.

Unionized sectors or plants have experienced higher wages due to statutory regulations that require a regular collective bargaining process every two years. Large-scale textile processing units that are capital-intensive have a relatively higher level of unionization and collective

bargaining, while labor-intensive garment units, with few exceptions, are mostly unorganized. As such, minimum wages are the only wage-setting mechanism for most of the workforce.

Wage Development – Poor Wages, even poorer for Female Workers

In nominal terms, applicable monthly minimum wages grew from PKR 7,000 (US\$ 82) in 2010 to PKR 13,000 (US\$ 128) in 2015 while the growth in real wages in the same period was 21 percent.^{xxiv}

Rather than acting as a basic wage floor for the most vulnerable workers, the minimum wage is the only recourse for workers in the garment sector and other industries seeking higher wages – supplanting collective bargaining.

The remaining problem is poor implementation and enforcement of existing labor laws, including the statutory minimum wages. More than 73 percent of the non-agricultural workers (which are not subject to labor laws) work in informal conditions and therefore lack the basic legal coverage. Even in the

formal economy, labor inspections are either ineffective or absent altogether. Wage figures in the official surveys are available only at the industry level, but according to the ILO,³⁹ the wages applicable in the garment sector range from US\$ 85 to 95 in 2013-14, which is closely comparable to applicable minimum wages.

^{xxiv} Based on Consumer Price Index 2009 to 2010 as reported in: Ministry of Finance of Pakistan. 2014/15. Pakistan Economics Survey (PSE) 2013-14, 2014-15. Accessed June 9, 2015. http://www.finance.gov.pk/survey_1314.html.

Rather than acting as a basic wage floor for the most vulnerable workers, the minimum wage is the only recourse for workers in the garment sector and other industries seeking higher wages – supplanting collective bargaining. It is especially discouraging that minimum wages have become the only form of wage protection for most workers, since even these standards are poorly enforced.

While female participation in Pakistan's labor market has been growing in recent years, it still lags behind in a regional comparison. This is also true in the garment sector. As of 2009, only 20 percent of garment sector workers were women, dramatically lower than in other South and Southeast Asian countries where over 80 percent of the garment industry workforce is female. Only 47 percent of companies provide maternity leave to their staff.⁴⁰ Across the economy, those women who are able to find formal employment generally receive lower pay than their male counterparts. On average, women earn 38.5 percent less than men in Pakistan.

Majority of Garment Workers Paid Below the Minimum Wage

Smooth political transition since the end of Musharraf's military regime in 2008 has positively influenced the statutory minimum wage growth, despite minimal economic growth in the country. The era of military rule saw the opposite trend. With spiraling price inflation since 2007-8 the pressure from workers and voters inevitably influenced decision makers to adjust minimum wages on an annual basis. On the other hand, business and enterprise owners who are often political figures continue to violate laws in connivance with the administration, and hence implementation remains weak.

The textile and garment sector in Pakistan is the largest industrial employer, yet workers' organization is minimal. In the absence of effective labor market regulations, the presence of representative trade unions is key to ensuring compliance with labor laws as well as promoting more decent and fair social standards in domestic and global value chains.

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Table 1

Pakistan Structure of Exports (Textile sectors) (US\$ million)

	2013-14	2014-15	% change
Total	20,979.10	19,921.50	-5
Textile Manufactures	11,420.10	11,281.60	-1.2
Non-Manufactured Textiles			
Raw Cotton	196.1	144.7	-26.2
Cotton Yarn	1,715.80	1,587.10	-7.5
Cotton Cloth	2,345.80	2,088.10	-11
Knitwear	1,839.20	1,981.90	7.8
Value-added textiles			
Bedwear	1,767.30	1,747.40	-1.1
Towels	629.9	650.1	3.2
Readymade Garments	1,577.90	1,722.10	9.1
Made-up articles	542.1	542.6	0.1
Other Textile Manufactures	806	817.7	1.4

Note: Figures are for July-April of the years indicated.

Source: Pakistan Economic Survey 2014-15



5. Vietnam

Erwin Schweishelm and Mai Ha Thu

Trans-Pacific Partnership Expected to Foster Growth

Vietnam has one of the fastest growing economies in Asia, and the textile and garment industry plays an important role.

The country's textile and garment exports increased 19 percent in 2014 to approximately US\$ 24 billion, accounting for 14 percent of GDP and 13.6 percent of the total export value⁴¹. In 2015, the export volume is expected to increase by another 20 percent⁴²,

Due to rising labor costs in China and the tragic accidents in Bangladesh, many investors are considering Vietnam as an alternative.

bolstered partly by declining prices of oil and raw material. Moreover, the ongoing negotiations on a Free Trade Agreement with the EU and the Trans Pacific Partnership Agreement (TPP)

may give Vietnam an additional competitive edge. Projections suggest Vietnam may soon overtake Bangladesh as the second-largest producer, reaching 11 percent of the global export volume by 2024.⁴³ Due to rising labor costs in China and the tragic accidents in Bangladesh,

many investors are considering Vietnam as an alternative.

There are more than 5,000 companies and an estimated 2.5 million people employed in the sector,^{xxv} a large majority of which is female. The Vietnam Textile and Garment Union (VTGU) was founded in 2007 and is part of the Vietnam General Confederation of Labor (VGCL). Its 123,000 members constitute only about 5 percent of workers in the industry. However, there are also enterprise-level unions that are directly affiliated with the umbrella organization VGCL.

Wage Formation and Development at National Level – On the Way to a Living Wage

A minimum wage is defined in the 2012 Labor Code as the lowest rate paid to the employees who perform the simplest work in normal working conditions. The code stipulates that the wage must ensure basic living needs of the employees and their families.

In 2013, the National Wage Council (NWC) was established in accordance with the new Labour Code that had come into effect earlier that year. The NWC consists of representatives of employers' associations, the VGCL as the sole representative of employees, and the Ministry of Labor, Invalid and Social Affairs. The tripartite council gives

representatives of trade unions and employers a direct stake in minimum wage negotiations and recommendations, significantly strengthening the minimum wage setting mechanism in Vietnam.

Minimum wages in Vietnam are set for four regions, from least developed rural areas to large cities, including Hanoi and Ho Chi Minh City. In recent years – even prior to the establishment of the NWC – minimum wages have increased substantially, often by more than 10 percent per year. The last increase took effect on January 1, 2015, bringing the minimum up to US\$ 100 in rural areas and US\$ 145 in large urban centers – an average increase of almost 15 percent across the four regions.

However, the regional minimum wages, proposed by the NWC and adopted by the government have not yet met the level of a living wage. Both the government and the trade unions calculate the living wage in large cities at about US\$ 190 to 200. The target was to raise the minimum up to a living wage by 2015, but this goal has been postponed until 2017.

Collective bargaining and enterprise-level dialogue are important mechanisms in the wage setting process. In Vietnam, these forms

xxv In factories that participate in the ILO project Better Work Vietnam, covering around 200,000 workers, 80 percent are women. Policy Brief: Gender Equality at the Workplace Baseline Findings from Better Work Vietnam. Accessed June 9, 2015. <http://betterwork.org/global/wp-content/uploads/Vietnam-Research-Brief-V4.pdf>.

of dialogue and negotiation are still limited in quantity and quality, resulting occasionally in “wild-cat strikes”.^{xxvi} Although industry-wide collective bargaining is made possible by the 2012 Labor Code, the vast majority of collective bargaining agreements (CBAs) are only concluded at the enterprise level.

Wage formation and development in the textile and garment industry – towards sectoral collective bargaining

According to the information provided by trade unions, the sector’s average income is about US\$ 200 to 300 per month, including meal allowances, transportation, work uniforms and work equipment or gifts on special occasions and overtime payments. A usual workweek for garment workers has 55 to 60 hours.

Collective bargaining and enterprise-level dialogue are important mechanisms in the wage setting process and develop sound industrial relations. In Vietnam, these forms of dialogue and negotiation are still limited in quantity and quality.

The textile and garment industry (the vast majority of products are readymade garments) is one of only two industries in Vietnam that has successfully negotiated CBAs beyond the level of individual enterprises. The latest textile and garment industry’s CBA stipulates that the sector’s minimum wages must be at least 3 percent higher than the regional minimum wage.

xxvi Strikes which are not led by trade unions and thus considered illegal in Vietnam.

Since the minimum wage is the basis to calculate social insurance and other allowances, its increase results in higher allowances as well. However, wages differ based on company, region, overtime hours and sources of investment.

Despite its achievement in concluding CBAs, the textile and garment industry still recorded the highest strike rate among all industries in recent years. In 2014, 36.5 percent of strikes in 2014 were in textile and garment companies.⁴⁵ In most cases, workers’ demands and complaints were salary-

related – concerned with wage increases, unpaid or deferred wages, allowances, pay scale, payroll, overtime payments, or bonuses. As mentioned above, the VGTU represents only 5 percent of the garment and textile workers in Vietnam, and this low rate of unionization in the industry might partly explain the paradox.

Impact and Conclusion – why productivity matters

Wage development relies mainly on mandatory increases by the government and not on a proper mechanism of dialogue and negotiation between employers and workers. This is not sustainable, since it is often accompanied by a

faster rise of living costs that mostly eliminates any improvement in workers' real income. Consequently, high turnover rates and wild-cat strikes continue to reflect workers' frustration and have negative impacts on productivity and competitiveness at both the enterprise and national level.

Being at the bottom of the supply chain, garment workers in Vietnam work hard to support themselves and their families.

On the other hand, if wage developments at the national level and in the textile and garment industry in Vietnam are not aligned with productivity growth, the country will face the risk of losing its competitiveness in

the global market. Being at the bottom of the supply chain, garment workers in Vietnam work hard to support themselves and their families and cannot be entirely responsible for this

productivity conundrum, which must be solved from a different end. As Vietnam is integrating more deeply into the regional and global economy, Vietnamese policy makers will face

ever greater challenges to balance the country's economic competitiveness with its goal of ensuring fair wages for workers.

Table 2

Minimum wage developments in Vietnam (2010-2015) (in Vietnamese dong)

	Region I		Region II		Region III		Region IV		Average increase in %
	In absolute number	Increase in %							
2010*	980,000		880,000		8,10,000		730,000		
	1,340,000		1,190,000		1,040,000		1,000,000		
2011	1,350,000	0.7%	1,200,000	0.8%	1,050,000	1.0%	830,000	-17.0%	-2.50%
2012	2,000,000	48.1%	1,780,000	48.3%	1,550,000	47.6%	1,400,000	68.7%	52.35%
2013	2,350,000	17.5%	2,100,000	18.0%	1,800,000	16.1%	1,650,000	17.9%	17.39%
2014	2,700,000	14.9%	2,400,000	14.3%	2,100,000	16.7%	1,900,000	15.2%	15.20%
2015	3,100,000	14.8%	2,750,000	14.6%	2,400,000	14.3%	2,150,000	13.2%	14.29%

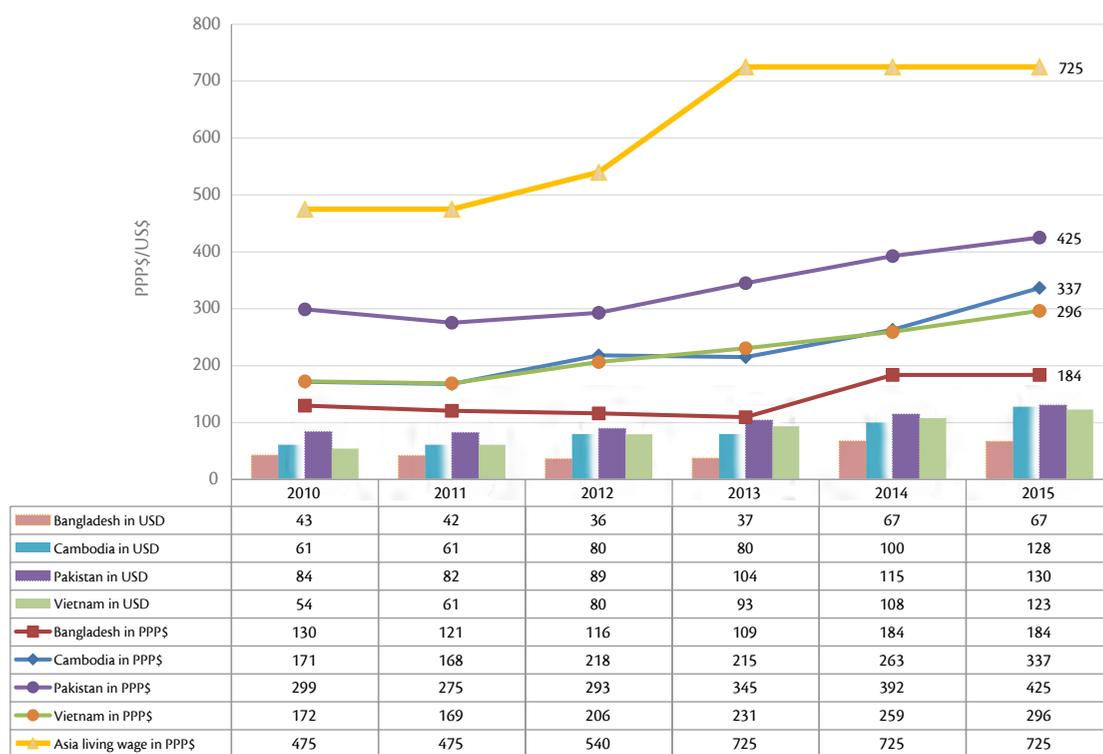
* There are two figures because at that time minimum wages were lower for local enterprises than for enterprises funded through foreign investment.

Source: Minister of Ministry of Labour, Invalids and Social Affairs (MOLISA)

Note: Regions I-IV denote areas with differing levels of development and urbanization, with Region I being the most industrialized and Region IV being the most rural.

Figure 4

Wage development from 2010-2015 in Bangladesh, Cambodia, Pakistan and Vietnam (in US\$ and PPP\$)

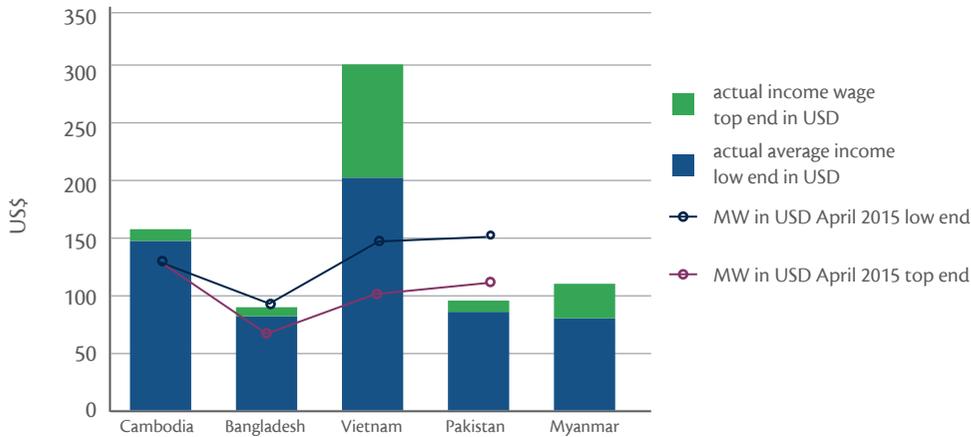


Note: PPP\$ conversion rate to local currency based on World Bank data.

Source: Ashim Roy. Asia Floor Wage Alliance.; Vietnam Union of Textile and Garment Workers, VGTU; Cambodia Ministry of Labor and Vocational Training; Bangladesh Gazette published on November, 2013 on Minimum Wage Board; own calculations.

Figure 5

Actual income wage composition in relation to minimum wage among garment workers

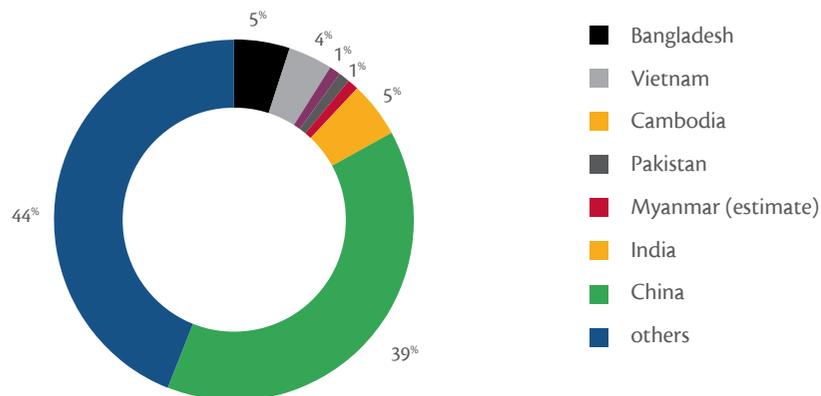


Note: Even though the Pakistan provincial minimum wages ranging from US\$ 110 to US\$ 150 the actual average wage of garment workers fall below.

Source: Ashim Roy. Asia Floor Wage Alliance.; Vietnam Union of Textile and Garment Workers, VGTU; Cambodia Ministry of Labor and Vocational Training; Bangladesh Gazette published on November, 2013 on Minimum Wage Board; own calculations.

Figure 6

Percentage of world market export



Source: WTO, Standard Chartered Research

KEY TRENDS AND POLICY IMPLICATIONS

Julia Mueller and Lukas Bauer

The comparability of wage development and formation across all five countries is challenging due to the complex and different minimum wage structures as well as a lack of data for some countries. However, a number of key trends can be extrapolated, which apply to all or most of the countries examined. These trends also serve as the basis for recommendations toward sustainable wage formation and development of the garment sectors in Bangladesh, Cambodia, Myanmar, Pakistan and Vietnam.

Steep Minimum Wages Hikes: The Need for a Regular Minimum Wage Review

The significant increases in minimum wages over the past five years need to be partly understood as compensation of previous wage freezes and real income losses for workers in the garment sector over the years prior. It is a positive sign that in all the countries examined, the wage increases have been the result of a tripartite wage committee. But the convening of these dialogues, especially in Bangladesh and Cambodia, happened mainly

due to pressure from striking workers and buyers responding to consumers' call for decent wages – not due to a regular and effective wage setting mechanism.

While the reform and/or creation of tripartite minimum wage bodies is a step towards more constructive social dialogue, they need to be further strengthened in order to function in a fully democratic and transparent manner.

While the reform and/or creation of tripartite minimum wage bodies is a step towards more constructive social dialogue, they need to be further strengthened in order to function in a fully democratic and transparent manner. Hence, a regular (annual or biannual) review based on statistical evidence

is crucial to pave the way toward living wages in the garment sector and, at the same time, make wage increases more predictable for producers and buyers.

Minimum Wage as a Substitute for Collective Bargaining: The Need for Constructive Social Dialogue

In Bangladesh and Cambodia the average income hardly exceeds the minimum wage. In Pakistan, it even falls short. This demonstrates that the results of minimum wage negotiations have become

de-facto sectoral collective pay agreements and therefore the main mechanism for wage setting.

Firm-level collective bargaining agreements – if existent – are weak in quality and rarely go beyond the wage standards guaranteed by the minimum wage orders. Sectoral collective bargaining agreements are – with the exception of Vietnam – completely absent.

Minimum wage is meant to set a wage floor, not act as the only wage-setting mechanism. In the countries examined, collective bargaining

mechanisms need to be set up or further strengthened. It is the task of the governments

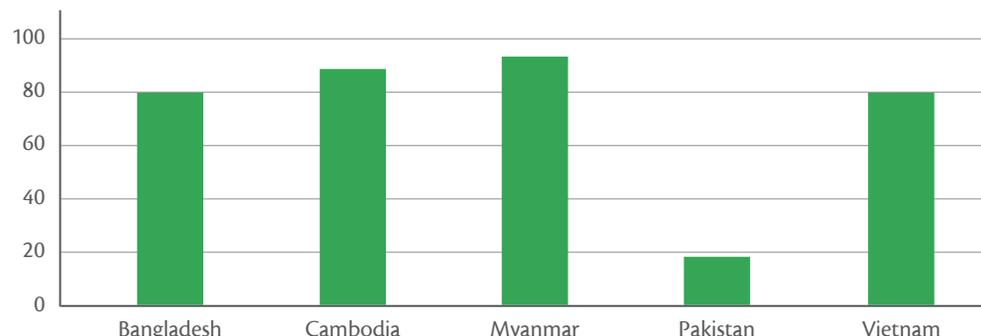
to create an enabling environment for collective bargaining at both the factory and the sectoral level, in line with ILO Convention 98 on the Right to Organize and Collective Bargaining.⁴⁶ But it is also essential that wage

development does not rely only on mandatory increases by the government -- minimum wage, but includes a proper bilateral bargaining process between workers and employers -- collective bargaining.

It is the task of the governments to create an enabling environment for collective bargaining at both the factory and the sectoral level, in line with ILO Convention 98 on the Right to Organize and Collective Bargaining.

Figure 7

Percentage of women workers in the garment industry (%)



Source: Bangladesh: BFMEA (2015); Cambodia: GMAC (2015); Myanmar: own estimates; Pakistan: Ehsan-ul-Haque (2009); Vietnam: Better Work Vietnam (2015).

Weak bargaining power: The need for strong and unified trade unions

A main reason for low wages and weak or non-existent collective bargaining agreements is the weak bargaining power of the trade unions in most of the countries examined. The lack of influence relates to external as well as internal factors. As regular reports of the ITUC Survey of Violations of Trade Unions Rights show, basic trade union

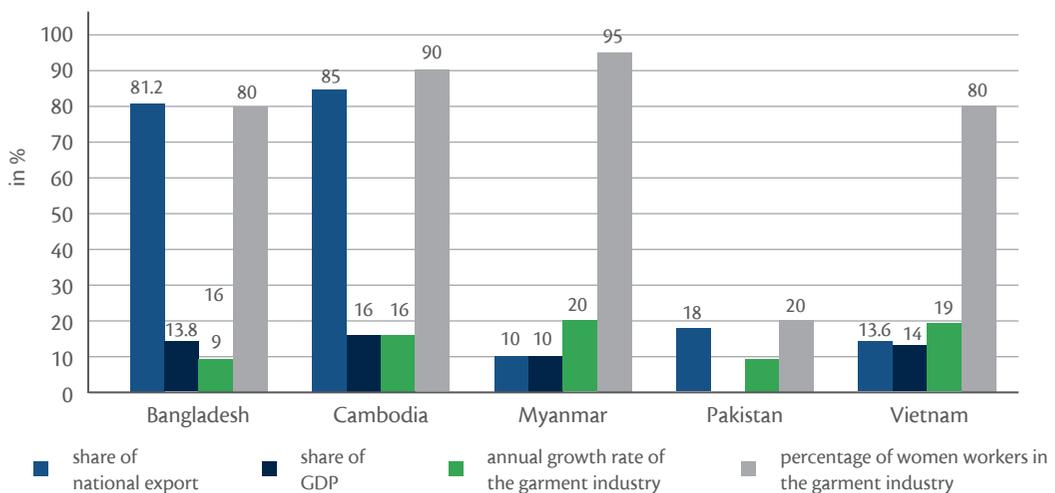
rights like freedom of association are not fully respected in all the countries.⁴⁷ In some cases, rights are even severely violated – for example, when strikes are forcefully dissolved.

The scattered movement with extremely low unionization rates impedes a joint, professional struggle for better working conditions and decent pay – at both the national and the factory level.

But for most of these countries, the weak bargaining power also points to challenges within the labor movement. With the exception of Vietnam, the union landscape is highly fragmented and lacks unity while the employers

are mostly organized in a single association.

Figure 8
Significance of the garment industry for the local economy in select Asian countries (2014)



Note: Figures are based on multiple sources. Citations are included in the body of the text.

The scattered movement with extremely low unionization rates impedes a joint, professional struggle for better working conditions and decent pay – at both the national and the factory level.

As recent research shows, strong and united unions are decisive for better working conditions and decent pay.⁴⁸ Wages are substantially higher in factories with a united work force. Therefore, unions in the countries examined

need to further professionalize their work, act in unity towards employers and governments and attract more members in order to increase their bargaining power in minimum wage committees, in factories, and at the industry level.

A feminised sector: The need to end all forms of exploitation and wage discrimination

With the exception of Pakistan, the garment sector employs a remarkably high proportion of female workers (80 to 95 percent). Most are rather young, with a low level of education, originally from rural areas and migrating to cities to earn a living for their generally poor families.⁴⁹ While it is a positive development that the employment in the formal garment industry can be a “route out of poverty”⁵⁰ and a chance for women to enter the labour market, the industry also takes advantage of poor women striving for a better

life. In the garment industry, women are paid less, less likely to be promoted, and often denied any form of maternity protection and effective

protection against sexual harassment or other forms of exploitation in the workplace.

Governments need to enforce ILO Core Convention 111, which prohibits any form of discrimination – including wage discrimination –

based on a worker’s gender and ensure a work environment without any forms of exploitation. Unions also need to reform and strive for more proportionate representation. While the majority of union leaders are men, the majority of their members are women. Moreover, any long-term strategy to end women’s exploitation must rely on improving their access to education and creating employment that goes beyond low-skilled and low-paying jobs.

High dependency on the garment industry: The need for long-term investments and skills development

With the exception of Vietnam and Pakistan, the economies examined here are overly dependent on the garment industry and lack diversification in their manufacturing sector. At the moment, there are few signs of change. This makes these

The abundance of industrial workers in one sector also has an adverse impact on wages, whereas a diversified manufacturing sector results in a tighter labor market and more bargaining power for workers.

countries highly vulnerable to adverse economic shocks. Whereas wage increases in China's garment industry went along with investments in skills development, labor productivity, and modern production methods,⁵¹ the industries in most countries examined in this chapter mainly focus on short-term profits. However, in order to ensure long-term profits in the garment industry, investments in safety, labor standards and higher wages are imperative.⁵² An over-abundance of industrial workers in one sector has an adverse impact on wages, whereas a diversified manufacturing sector results in a tighter labor market and more bargaining power for workers.

To create more sustainable and robust prospects for growth and development, these countries need to concentrate on moving up the value chain. The focus on low-end garments can only kick-start the development of a manufacturing sector. Such an industrial policy must be accompanied by investments in skill development – which increases productivity, enabling higher wages without sacrificing competitiveness.

Conclusion: A trade-off between minimum wage increases and competitiveness?

Overall, in the countries examined labour costs are still relatively low – especially compared to other garment producing countries in the region like China, Malaysia and Thailand.^{xxvii} According to the global manufacturing union IndustriALL, a typical pair of jeans made in Bangladesh is sold for US\$ 30 to US\$50 at retail stores, whereas the worker who sews them receives about US\$ 0.10.⁵³

There is still substantial space – especially in Bangladesh, Cambodia and Myanmar, to increase minimum wages without losing competitiveness on the global garment market. The constant growth of the garment industries in the countries examined and the likelihood of continued expansion proves that significant hikes in minimum wages have not discouraged buyers from sourcing from these countries.

Although the industry is historically built on low wages, they are not the only factor that drive sourcing decisions of international buyers. Thanks to increased awareness among consumers, fashion brands are increasingly prioritizing stable industrial relations, productivity, reliability of supply and decent working conditions.⁵⁴

xxvii Monthly minimum wages in the garment sector in China range between US\$ 156 and US\$ 266, in Malaysia between US\$ 244 and US\$ 275. In Thailand it is set at US\$ 237. ILO Regional Office for Asia and the Pacific. December 2014. Wages in Asia and the Pacific: Dynamic but uneven progress. Accessed July 1, 2015. http://www.ilo.org/wcmsp5/groups/public/---asia/---ro-bangkok/---sro-bangkok/documents/publication/wcms_325219.pdf, p. 3.

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CLOSING THE GENDER WAGE GAP IN INDIAN AGRICULTURE

Recognizing women's contributions through equal wages

Sabina Dewan, JustJobs Network

JustJobs Network

JustJobs Network (JJN) is a private, nonpartisan organization finding evidence-based solutions to one of the most pressing challenges of our time: How to create more and better jobs worldwide. JJN produces empirical research on good job creation, focusing its work on the critical knowledge gaps in the global employment landscape.



INDIA



3.6

Unemployment Rate



33.6

GINI



18.1

Wage and salaried
workers, total (% of
total employed)



9200

GDP per person
employed
(constant 1990 PPP \$)

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Introduction

From raising families to weeding and harvesting, women in rural India balance the demands of their domestic lives with agricultural work. Notwithstanding their importance, women's contributions are grossly undervalued—especially relative to men in the sector.

Female agricultural workers in India are relegated to the least desirable farm activities. They are denied access to critical tools, such as technology, information and training, constraining their productivity and undermining the sector's economic performance. Women are often deprived of benefits such as days off. Most notably, they receive lower wages than men for the same work.¹

Underpinned by deep-seated patriarchy, these conditions reflect a lack of women's

empowerment, that adversely affecting everything from their family's health outcomes to the educational attainment of their children.

The undervaluing of the contributions of women in the agricultural sector has ramifications beyond the family. Research on microfinance and the impact of public cash transfers confirms that when low-income women are given more resources, they tend to spend them in better ways than do men – on necessary expenditures like medical services, health and nutrition needs, and school fees. Such expenditures benefit their families, enhance the productive capacity of the future workforce, and generate aggregate demand that ultimately advances the economy.²

Underpinned by deep-seated patriarchy, these conditions reflect a lack of women's empowerment, that adversely affecting everything from their family's health outcomes to the educational attainment of their children.

Realizing the promise of India as an emerging market economy entails recognizing the burden of work and responsibility on women in agriculture, removing the obstacles that constrain their productivity, and adequately compensating women in the sector toward ultimately closing the gender pay gap.

This chapter provides an overview of the wage differentials between men and women in India's agriculture sector and explores explanations for why female work continues to be undervalued. It ends by proposing concrete policy measures to help close the gender wage gap in Indian agriculture.

Women in agriculture

Agriculture's value-added as a share of India's Gross Domestic Product (GDP) was 17 percent in 2014, down 11 percentage points from two decades earlier.³ The share of those in agriculture as a percentage of the total employed workforce also declined, from 60 percent in 1994 to 47 percent in 2012, marking a tremendous structural shift in the Indian economy – a consequence of government reforms undertaken in the early 1990s. Nevertheless, with almost half of employed persons continuing to work in agriculture, the sector remains extremely important to India's labor market.

Six out of every 10 employed women work in the sector where the wages are the lowest.

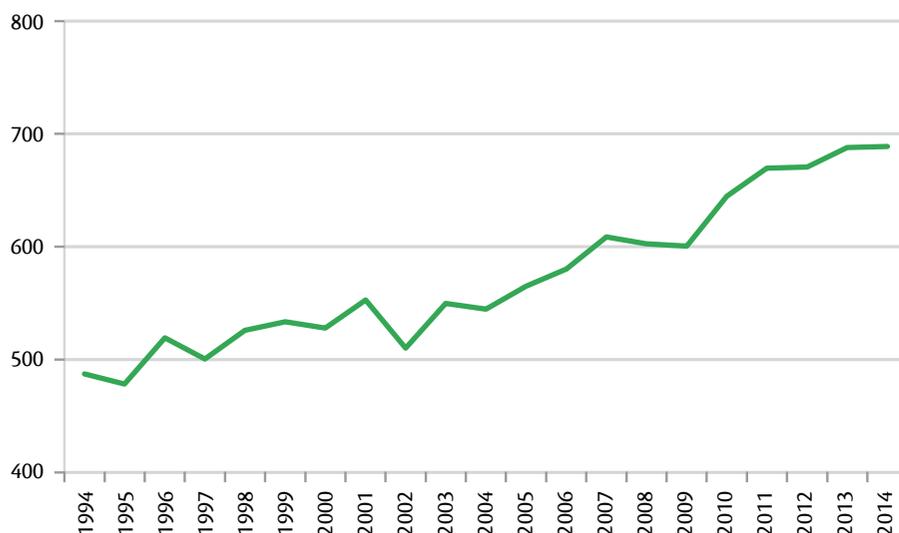
Agriculture value-added per worker (in constant 2005 US\$) increased from US\$ 487 in 1994 to US\$ 689 in 2014 (see **Figure 1**). But the decline in agriculture's value-added as a share of GDP, coupled with the high share of employment in the sector,⁴ reflects the fact that agriculture is still labor-intensive and low-productivity relative to other parts of the economy.

Of the three economic sectors – agriculture, industry, and services – agriculture therefore has the lowest wages.

Agriculture constitutes the largest share of female employment. Six out of every 10 employed

Figure 1

Agriculture value added per worker Constant 2005 (US\$)



Source: World Bank. World Development Indicators.

women work in the sector where the wages are the lowest.ⁱ (see **Figure 2**)

While the share of both women and men employed in agriculture fell between 1994 and 2012, it has fallen at a faster rate for men than for women because men are more likely to access better job opportunities in other sectors. The compound annual growth rate (CAGR)

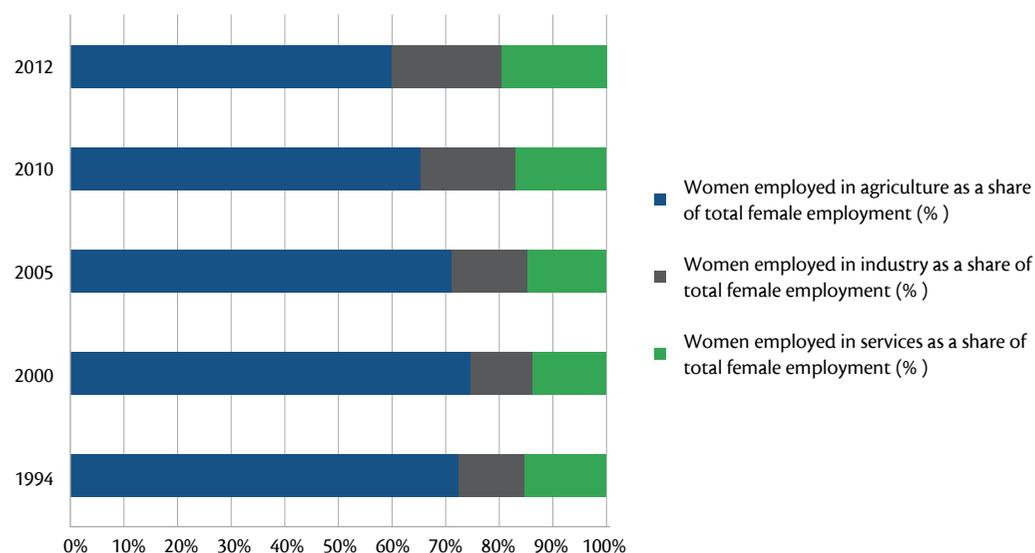
calculated for female agriculture employment as a percentage of female employment was -1.05 during this time period. The CAGR for male agriculture employment as a percentage of male employment was -1.42. Overall, the CAGR for employment in agriculture, male and female workers put together, stood at about -1.36 percent.ⁱⁱ

ⁱ 21 percent of employed women worked in industry and 19 percent in services in 2012. By contrast, 43 percent of all employed men worked in agriculture, 26 percent in industry, and 31 percent in services. (Source: World Bank. World Development Indicators.)

ⁱⁱ Since there are more men in total employment than women, and since the proportion of men has increased over the time period examined in this chapter, the growth rate for total employment is heavily weighted toward male employment.

Figure 2

Sectoral Composition of Female Employment



Source: World Bank. World Development Indicators.

At the same time, female employment in the industrial sector as a share of total employment in the sector declined from 22 percent in 1994 to 20 percent in 2012. Female employment in services as a proportion of total services employment also declined from 18 percent to 17 percent. Male employment in these sectors rose accordingly – corroborating the fact that men tend to have greater access to better opportunities in other sectors than women do.

This out-migration of men has led to conjecture on the feminization of agriculture in India. Yet examination of the data over the last couple of decades suggests that agriculture continues to be a male-dominated sector. In the Indian experience, agriculture's share of female employment has declined, as has the number of female agricultural workers as a fraction of total agricultural workers. This is driven by the decline in female labor force participation (LFP).ⁱⁱⁱ LFP

iii There is a significant amount of literature exploring the reasons behind the decline in India's female labor force participation. One reason is that women are staying in education longer. Another is that as economies move from low-income to lower-middle and upper-middle-income status, women who once worked out of necessity drop out of the labor force, sometimes working in the care economy that is not captured in labor market statistics (See: JustJobs Network and Fafo Institute for Applied International Studies. 2014. JustJobs Index.).

India relative to other countries

It is useful to compare India's experience to that of other emerging economies. Between 1990 and 2008 in Brazil, while female employment in agriculture as percentage of total female agriculture fell by 0.1 percent, those for males fell by 1.7 percent and total decrease for agricultural employment was 1.5 percent. This shows that agricultural share of male employment has decreased much more rapidly than that for women in Brazil as well.

The experience in Vietnam corresponds to India's as well; the percentage of employed men working in agriculture fell more rapidly than for women between 1996 and 2012. However, Indonesia witnessed the opposite trend during the same time period: the share of employed women working in agriculture fell by 2.7 percent, while for men the share fell by just 2.5 percent.

CAGR Brazil, Indonesia, Vietnam

Country	CAGR %, male agricultural employment as % of total male employment	CAGR %, female agricultural employment as % of total female employment	CAGR %, agricultural employment as % of total employment
Brazil	-1.7	-0.1	-1.5
Indonesia	-2.5	-2.7	-1.8
Vietnam	-2.6	-2.2	-2.4

Source: World Bank. World Development Indicators.

among women went from 37 percent in 1994 to 28 percent in 2012 (see **Figure 3**).⁵

This is significant because studies suggest that – holding other factors such as productivity, seasonal changes, and trade constant – rural wages should rise as rural working populations decline, due to a tighter labor market.⁶ There is a greater demand for workers as the labor force shrinks. Outward migration of men to pursue

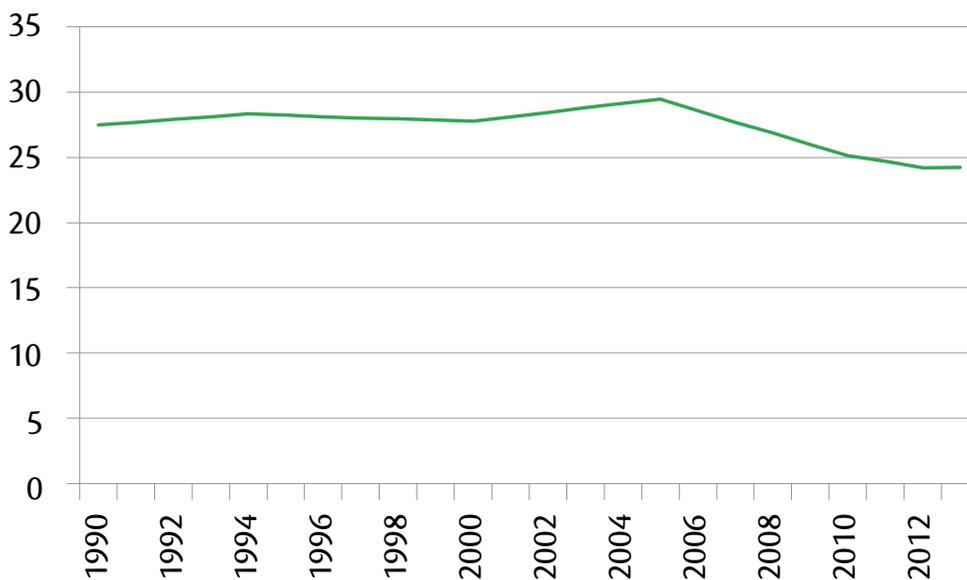
other opportunities and the declining labor force participation of women results in a decrease in labor supply; as such, the remaining workers – men and women – should see their wages go up.

There has in fact been an increase in agricultural wages in India – fuelled by a shrinking labor force along with rises in productivity, and potentially the Mahatma Gandhi National Rural Employment Guarantee Act (NREGA).^{iv} Between 2004 and

iv The Mahatma Gandhi National Rural Employment Guarantee Act is an employment guarantee scheme that provides a hundred days of wage-employment per financial year to rural households in which adult members volunteer to perform unskilled manual work.

Figure 3

Female labor force participation rate India (%)



Source: World Bank. World Development Indicators.

2010, average of wages in selected agricultural occupations grew at a compound annual growth rate of 11 percent.⁷

But an increase in wages across the board do not close the gender wage gap in India's agricultural

sector. Achieving parity in wages requires specific measures to improve wage rates and levels paid to women.

Persistent wage gaps in agriculture

Within agriculture, women's labor is valued less than men's. More women than men are hired as casual laborers with only short-duration contracts as opposed to longer-term, secure waged work. In 2004-2005, 29 percent of female rural workers, compared to 23 percent of male rural workers, were casual laborers.⁸ Casual workers do not have job security; they enjoy fewer rights and protections and have limited economic mobility. Among casual workers, women's wages were estimated to be 69 percent of male wages in 2004-2005.⁹

Women are also relegated to the least desirable tasks in agriculture, such as weeding, that tend to pay less. Men meanwhile participate in ploughing and harvesting. Evidence suggests that women tend to get fewer days off and are rarely paid

government-mandated minimum wages.¹⁰ In 2007, 95 percent of female agricultural wageworkers received less than a minimum wage.¹¹

Beyond this, studies based on time-use surveys suggest that women shoulder a larger burden of tasks and responsibilities than men.¹²

National statistics do not capture the full scale of women's work in agriculture.¹³ Many women are unpaid family workers who work for no remuneration in a relative-owned or -operated enterprise. Women also combine housework with non-crop agricultural activities, such as tending to livestock or processing and storage, that are often unaccounted for in agricultural employment statistics.¹⁴

Why is women's work undervalued?

These facts point to a deep-seated preference for men over women in agricultural employment that fuels the undervaluation of women's work in agriculture. A combination of economic and cultural reasons drive this preference.

A key empirical observation about female wages in development economics is a negative

correlation between fertility and female wages.¹⁵ This observation points to the fact that women's fertility is valued more than their employment.

Rural households value childbearing over women's wage income. Children are seen as insurance for old-age care. In the absence of any elderly care services, particularly in a sector such

as agriculture with a high degree of informality, children act as caretakers. Moreover, children become extra hands for family farm and wage labor activities.

In this context, women's work becomes secondary and undervalued – considered supplementary as opposed to primary income.

Differences in the nutritional levels of workers could be another reason motivating the gender pay gap. If one assumes that nutritional level is an important proxy for a laborer's productivity, and that productivity in part determines market wage, the pervasive female nutritional deficit in India could explain why men's wages remain persistently higher than women's. This is an economic consequence of deep-rooted patriarchy, as women's high malnutrition rates are driven by their "second-class status" within the family.

Table 1 illustrates the difference between the wages that men and women earned in various agricultural occupations between 2006-2010.

The data reveal occupations where the real wage differential has actually increased – unskilled rural laborers being the most important; occupations where the real wage spread has fluctuated over the four years; and the few instances where the real wage spread has narrowed.

The nutritional deficit and the household's preference for women to bear children over participating in wage labor are manifestations of deep-seated cultural norms that discourage female employment. Cultural norms and traditions in India have historically discounted women's economic contributions.

Women have less access to land, credit, technology and market information, inhibiting their upward mobility for work. This also corroborates with the finding that as households improve their economic standing, the preference is for women to stay at home. Research suggests this is one of the reasons behind the declining female workforce participation rate.

National statistics do not capture the full scale of women's work in agriculture. Many women are unpaid family workers who work for no remuneration in a relative-owned or -operated enterprise.

Conclusions and policy recommendations

India's agricultural sector relies on its female workforce. Women shoulder the disproportionate burden of carrying out household work in addition to the least desirable economic activities of the sector, yet their contributions remain undervalued. At the same time, they are denied the tools – skills training, information, and financial agency – to become more productive economic agents. Allowing gender disparities in the conditions of work to persist, especially the gender wage gap, reinforces patriarchal norms, discourages women from working, and perpetuates a loss of valuable productive potential.

But addressing the disparity in agricultural wages of men and women through targeted policies first requires data. Evidence on the complex roles that women play, the agricultural activities they engage in, and their conditions of work – especially wages – has improved. Yet the information is dated and short-term, frequently based on anecdotal rather than nationally representative empirical evidence. More consistent, longer-term and nuanced investigation is required to understand how the gender wage gap reacts to economic, social and political shifts over time.

Beyond this, greater efforts are needed to facilitate the transition of women from casual labor to more regular wage labor¹⁶ which offers better

security, benefits and potential opportunities for mobility. On the one hand this entails reducing the load of housework by providing piped water and electricity, for instance.¹⁷ On the other hand, it involves generating opportunities for regular wage labor that are specific to women's needs and aspirations.

Employment guarantee schemes that pay the minimum wage or better, targeting women during the off-season, can help. Research in rural Tamil Nadu, for example, shows that the National Rural Employment Guarantee Act's fixed, regular and gender-neutral wages have benefited rural women.¹⁸ Audits of NREGA do however suggest that the participation of women in such schemes is also contingent on the provision of ancillary services such as childcare on the worksite.¹⁹

While general enforcement of labor laws is low, it is even worse when it comes to women's working conditions. More stringent efforts must be undertaken to ensure that employers comply with minimum wage laws and other labor protections and entitlements for women.

In addition, national skills development policies must specifically address the training needs of women in the sector. The present draft of the National Policy for Skill Development sets a target of 30 percent participation of women in

Table 1

Real wage differentials in agricultural professions 2007-2010 (INR per day)

	Year	2007	2008	2009	2010
Ploughing	Men	81.8	91.4	102.9	120.9
	Women	42.4	50.0	55.4	70.4
	Difference in nominal wages	39.4	41.4	47.5	50.4
	Difference in real wages	10.1	9.8	10.3	9.4 ↓
Sowing	Men	73.3	79.3	90.0	104.5
	Women	51.4	57.2	65.0	79.5
	Difference in nominal wages	21.9	22.1	25.0	25.1
	Difference in real wages	5.6	5.2	5.4	4.7 ↓
Weeding	Men	65.0	70.1	80.2	92.8
	Women	52.8	58.3	68.0	78.9
	Difference in nominal wages	12.2	11.8	12.1	13.8
	Difference in real wages	3.1	2.8	2.6	2.6 ↓
Transplanting	Men	69.2	73.8	83.3	98.3
	Women	56.4	61.9	71.4	86.7
	Difference in nominal wages	12.7	11.9	11.9	11.6
	Difference in real wages	3.2	2.8	2.6	2.2 ↓
Harvesting	Men	68.5	75.2	87.1	102.8
	Women	55.7	62.3	71.6	85.0
	Difference in nominal wages	12.8	12.9	15.5	17.9
	Difference in real wages	3.3	3.1	3.3	3.3 ↓
Winnowing	Men	66.2	71.1	81.2	96.3
	Women	51.0	56.1	65.1	79.0
	Difference in nominal wages	15.1	15.0	16.2	17.3
	Difference in real wages	3.9	3.5	3.5	3.2 ↓

	Year	2007	2008	2009	2010
Threshing	Men	67.4	73.5	85.1	100.2
	Women	54.4	59.4	67.7	82.1
	Difference in nominal wages	13.0	14.1	17.4	18.1
	Difference in real wages	3.3	3.3	3.8	3.4 ↑
Picking	Men	67.5	72.5	81.1	97.0
	Women	51.1	58.2	66.4	78.9
	Difference in nominal wages	16.4	14.3	14.7	18.0
	Difference in real wages	4.2	3.4	3.2	3.4 ↓
Herdsman	Men	43.5	47.6	53.5	62.2
	Women	34.4	37.8	41.3	46.7
	Difference in nominal wages	9.0	9.9	12.2	15.6
	Difference in real wages	2.3	2.3	2.6	2.9 ↑
Well Digging	Men	99.5	107.0	116.3	140.8
	Women	53.6	58.3	63.5	75.4
	Difference in nominal wages	45.9	48.6	52.8	65.4
	Difference in real wages	11.7	11.5	11.4	12.2 ↑
Cane Crushing	Men	72.5	77.9	87.3	98.4
	Women	47.1	54.9	61.2	75.5
	Difference in nominal wages	25.4	23.0	26.0	22.9
	Difference in real wages	6.5	5.4	5.6	4.3 ↓
Unskilled Labour	Men	66.8	73.3	86.4	101.9
	Women	50.0	55.6	65.7	77.7
	Difference in nominal wages	16.8	17.8	20.8	24.2
	Difference in real wages	4.3	4.2	4.5	4.5 ↑

vocational training courses by 2017.²⁰ But the proposed tools to achieve the target – “hostels for women, scholarships, transport, training materials and loans” – are the same as they were for the previous policy, when they proved to have little impact.²¹

The National Skills Development Corporation and the Ministry for Skill Development and Entrepreneurship can provide incentives for female trainees in the agricultural sector, especially in activities that tend to be reserved for men. This should be coupled with incentives for employers to hire women as regular wage laborers and pay them the minimum wage or better, equal to their male counterparts.

Greater efforts are needed to facilitate the transition of women from casual labor to more regular wage labor that offers better security, benefits and potential opportunities for mobility.

Debates over minimum wage as a strategy for stemming growing income inequality are dominating airwaves across the globe. Yet the

wage inequalities that persist between women and men, and have for decades, are given insufficient attention. Taken together, these interventions toward ensuring equal pay for women in agriculture will not only help families, but economies as well. In the long run they will help

change the deep-seated cultural norms that impede social and economic progress in India.

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²¹ *ibid*.

SPOTLIGHT: SAATH

Can a training program boost the wages of construction workers?

Saath is a non-profit organization based in Ahmedabad, India and a member of JustJobs Network. Over the past 26 years, Saath has facilitated participatory community development to improve quality of life for the urban and rural poor. Its one-stop, integrated services have reached over 460,000 individuals in the states of Gujarat and Rajasthan.

The construction sector employs about 44 percent of the informal workforce in India. Informal workers in construction often receive lower wages and poorer treatment at the workplace than their

counterparts in the formal sector. Employment is usually temporary, leading to a volatile work environment. Workers suffer from a lack of basic amenities, little to no compensation for accidents and deaths, unsafe working conditions, and irregular or non-payment of wages.

In 2008, Saath carried out a study on the status of construction workers in Ahmedabad with the American India Foundation. The study covered 625 construction workers. Some of the study's major findings are shown below.

Survey of Construction Workers in Gujarat, India



Workers hired on a daily basis



Workers who found employment through word-of-mouth



Workers who reported they were semi-skilled

vs



Workers reporting themselves as skilled



Average wage of female workers

vs



Average wage of male workers



Workers who work six days per week whenever possible

vs



Workers who work all seven days of the week whenever possible

Following the study, Saath decided to start a Worker Facilitation Centre to connect construction workers to employment opportunities and safeguard workers' rights. The center did not have the envisioned impact because the initial plan lacked an important aspect: assessment and upgrading of workers' skills.

Saath decided to implement a skill-building program in 2011 – called Nirman (Hindi for “Progress”) – focusing on construction workers. Nirman focuses on skill enhancement, better bargaining power and market knowledge, networking with employers and the government, bringing women into non-traditional trades, social security, safety, financial inclusion and improving the overall quality of livelihoods in the construction sector.

The program runs basic courses in carpentry, plumbing, masonry and electrical work. The course has six subjects – technical skills, life skills, entrepreneurial skills, safety, basic numeracy/literacy and financial literacy. Since 2011, Nirman has trained over 1,492 workers (including 183 women) in different trades. After the training, a basic tool kit and a certificate of completion is provided to the trainees. This helps them establish the credibility of their skill levels and obtain better jobs.

Saath helps workers register with the Labour Department in order for them to benefit from various welfare schemes. It has helped over 150 applicants this way, but for fewer than 20 has the

government completed the registration process. Two of these successful workers have received financial assistance from the Department towards their children's education. Saath recently surveyed workers trained through Nirman to gauge the efficacy of the program. Out of the 541 respondents,

- **430** reported that they are now able to find work for at least **25 days a month** compared to 10-15 days before.
- **383** reported that they have been able to **move up one level** in the workplace hierarchy, from helper/labourer to a semi-skilled worker.
- **425** reported that, post training, there has been a **10 percent to 30 percent increase** in their daily income. Some have even started taking up work as contractors.

Shantaben Amrutbhai, a woman mason trained through Nirman, says: “I am now able to balance being a mother, wife and mason. I am more aware of the importance of saving, of safety measures I can take while at work, and have been able to bargain for a 50 rupees [US\$ 0.80] increase in my daily wages along with better work hours.”

Parsottam Parmar, who was trained as an electrician, reported: “I used to work as a guard earning 6,000 Rupees [US\$ 95] per month. After my Nirman training on electricals, I received a certificate and tool kit. I was connected with an electricity company, Torrent Power, and now earn 10,000 rupees per month.”

STATUTORY MINIMUM WAGE REGULATION IN EUROPE

A necessary evil?

Line Eldring and Kristin Alsos, Fafo Institute for Applied International Studies

Fafo Institute for Applied International Studies

Fafo is an independent and multidisciplinary research foundation focusing on social welfare and trade policy, labor and living conditions, public health, migration and integration, and transnational security and development issues. Fafo works within both a domestic Norwegian and a larger international context. Fafo was founded by the Norwegian Confederation of Trade Unions (LO) in 1982 and was reorganised as an independent research foundation in 1993 with contributions from the Norwegian Confederation of Trade Unions, Norwegian Union of Municipal and General Employees and six major Norwegian companies. Fafo has offices in Oslo, Jerusalem and Beijing.

EUROPE



10.5

Unemployment Rate



30.8

GINI



84.3

Wage and salaried
workers, total (% of
total employed)



39335

GDP per person
employed
(constant 1990 PPP \$)

STATUTORY MINIMUM WAGE REGULATION IN EUROPE

A necessary evil?

Line Eldring and Kristin Alsos, Fafo Institute for Applied International Studies

During the last decade, the topic of minimum wage regulation has gained new relevance in Europe. Massive labor mobility from east to west in the wake of the European Union enlargements in 2004 and 2007 have put pressure on existing national regulatory regimes, and the consequences of the financial crisis have had a brutal impact on several European labor markets. These developments have given rise to broad and fundamental questions about how employees can be ensured a decent wage level, and whether new approaches are required.

Both the European Parliament and the European Trade Union Confederation (ETUC) have

The European trade union movement is united in its desire for decent and fair wages, but there is a strong division within the European Trade Union Confederation (ETUC) when it comes to the introduction of a European minimum wage policy.

frequently debated a possible EU-wide minimum wage. The European trade union movement is united in its desire for decent and fair wages, but there is a strong division within the ETUC when

it comes to the introduction of a European minimum wage policy. So far, the Nordic and Italian trade union confederations have strongly rejected this as a way forward. This chapter gives an overview of current minimum-wage setting mechanisms in European countries and looks more specifically at why statutory minimum wage is causing such controversies in some

of the countries that have the strongest trade unions in Europe.¹

¹ The article is based on L. Eldring and K. Alsos. 2012. *European minimum wage: A Nordic Outlook*, and L. Eldring and K. Alsos. 2014. *European minimum wage: A Nordic Outlook – an update*. (Oslo: Fafo).

Regulation of minimum wages in Europe

Regulation of minimum wages in European countries is based on collective agreements and/or national legislation. We can distinguish between three main forms of minimum wages:

Statutory minimum wages: Statutory minimum wages refers to a minimum wage that is either determined by legislation or pursuant to legislation. A statutory minimum wage level defines a wage floor that can go up but not down. Statutory minimum wages are generally guaranteed for all employees of a country, though exceptions are sometimes made for certain groups. The specifics of how the statutory minimum wage level is determined vary from one country to another,¹ but the main point is that the legislature has determined a minimum wage or a procedure for fixing a minimum wage.

Collectively agreed minimum wages: Another form of minimum wage setting is via collective agreements, negotiated between trade unions and employers' organizations. Most often, the collectively agreed minimum wage is higher than a statutory

minimum. However, the collectively agreed minimum wages apply only to the parties to the collective agreement – trade union members and the employers' association. Employers who are party to the agreement may still be obligated by it with regard to unorganized employees in the enterprise, too. The number of employees who end up being paid at the collectively agreed minimum rate and how many will be paid above this floor – as a result of local wage variations – will vary from one sector to another.

Extended minimum wages: Many European countries have mechanisms for expanding the coverage areas for collective agreements by making them generally binding.² Most often, this takes the form of legal extensions of collective agreements, whereby wage rates and other collectively bargained provisions are expanded to cover a greater number of workers. The most common procedure is to apply the provisions not only to the parties of the agreement and their members, but to the entire

While statutory minimum wages are most often determined on social grounds – ensuring workers can fulfill basic standards of living – collectively agreed minimum wages emerge as a result of the bargaining system, the parties' wage policies and their relative bargaining strength.

industry or profession that falls under the scope of the agreement. An enterprise with non-unionized

employees must thereby conform to the extended minimum wage level, even though the employees' opportunities to bargain collectively for local supplements may be nonexistent or far weaker than in organized companies.

While statutory minimum wages are most often determined on social grounds – ensuring workers can fulfill basic standards of living – collectively agreed minimum wages emerge as a result of the bargaining system, the parties' wage policies and their relative bargaining strength.

In countries that have statutory minimum wages, this level will constitute an absolute lower limit to the wages that can legally be paid in an employment relationship. Statutory minimum wages are very common in Europe. They are applied in 23 of the 28 EU countries.ⁱⁱ The statutory rates amount to approximately 30 to 50 percent of the average wage level in the countries concerned. The coverage of collective agreements in European countries varies considerably (see **Table 1**). And this coverage does not necessarily correlate with the unionization rate. For instance, only 8 percent of French workers are members

Table 1

Statutory minimum wages, extensions, coverage of collective agreements and trade union density in the EU (and Iceland, Norway and Switzerland).

Country	Statutory minimum wage	Extensions of CA ⁺ possible	Scope of extension	CA ⁺ coverage (percent)*	Trade union density (percent)*
Austria		X	Low	99	28
Belgium	X	X	High	96	50
Bulgaria	X	X	Not used	18 **	20
Croatia	X	X	Low	60	35
Cyprus	X			52	49 **
Czech Rep.	X	X	High	41 **	17
Denmark				83	69
Estonia	X	X	Low	25	8 **
Finland		X	High	90	69

ii Including Cyprus, which has adopted statutory minimum wages in nine industries.

Country	Statutory minimum wage	Extensions of CA ⁺ possible	Scope of extension	CA ⁺ coverage (percent)*	Trade union density (percent)*
France	X	X	High	90	8 **
Germany	X	X	Low	61	18
Greece	X	(x)	(High)***		25 **
Hungary	X	X	Low	34 **	17 **
Iceland		X	High	99	85
Ireland	X	X	Low	36	42
Italy				85	35
Latvia	X	X	Not used	20 **	15
Lithuania	X	X	Not used	13	10
Luxembourg	X	X	Low	58 **	37 **
Malta	X			55	49 **
Netherlands	X	X	High	84	19
Norway		X	Low	67	52
Poland	X	X	Not used	29	14
Portugal	X	X	(High)***	90	19
Romania	X	X	Low	20 **	33
Slovakia	X	X	Low	35	17
Slovenia	X	X	Low	92	24 **

* Figures are for 2010/11, but are more recent for the Nordic countries, for which the data mostly stems from 2012.

Figures for 2008/09. *The situation in these countries is unstable/changing rapidly.

+ Collective Agreement

Table sources: J. Visser. 2013. ICTWSS Database version 4.0, Aprile (<http://www.uva-aias.net/207/>); T.Aa. Stokke. 2010. Allmenngjøring i Europa. I: T.Aa. Stokke (ed.) Allmenngjøring i Norge og Europa. Fafo-rapport 2010:14; Eldring & Alsos. 2012. T. Aa. Stokke, K. Nergaard and S. Evju. 2013. Det kollektive arbeidslivet. Organisasjoner, cavgtaler og lønnsoppgjør. (Oslo: Universitetsforlaget); S.K. Andersen, J.E. Dølvik and C.L. Ibsen. 2014. De nordiske aftalemødeller i åpne markeder – utfordringer og perspektiver. Fafo-rapport 2014:08; Eurofound. 2011. Extension of collective bargaining agreements in the EU. (Dublin: European Foundation for the Improvement of Living and Working Conditions); OECD Database on trade union density; EirOnline.

Country	Statutory minimum wage	Extensions of CA ⁺ possible	Scope of extension	CA ⁺ coverage (percent)*	Trade union density (percent)*
Spain	X	X	(High)***	73	16
Sweden				88	69
Switzerland		x	Low	49	17
UK	X			31	27

of a trade union, but 90 percent are covered by a collective agreement. This is because, like many other countries, France has applied broad extensions of collective agreements.

1, 2015. Only three countries in this cohort – Italy, Denmark and Sweden – have neither a statutory minimum wage level nor schemes for extension of collective agreements.

The most common practice is to apply both a statutory minimum level and schemes for extension of collective agreements. This pertains to 20ⁱⁱⁱ of the 31 European countries included in **Table 1**.

While Denmark and Sweden have collective agreements as their only mechanism for regulation of minimum wage levels, Finland, Iceland and Norway have the legal instrument to make agreements generally binding.

In its constitution, however, Italy has a provision stating that all employees are entitled to fair wages, which in practice has meant an extension of the wage rates defined in industry-level collective agreements. But recent

A significant development has recently taken place in Germany, where a statutory minimum wage (at € 8.50 / USD 9.30 per hour) was introduced, having taken effect January

court rulings have confirmed the validity of collective agreements that set a lower standard than the rates defined by industry-level

iii In Greece, the opportunity to extend collective agreements has been temporarily suspended because of the financial crisis (EirOnline 2013). In Portugal, extensions are still possible, but an austerity policy has reduced the practice considerably (M.P.C. Lima. 2013. Dramatic decline in collective agreements and worker coverage. EirOnline PT1302029). In Spain, legal amendments in the wake of the crisis have reduced the scope of collective agreements, which in turn have reduced the number of employees entitled to extensions (P.S. Miguel. 2013. One million workers to lose collective agreement protection. EirOnline ES1307011).

bargaining – a development that may weaken this mechanism.³ When it comes to statutory minimum wage, the proposed Jobs Act in Italy entails a possibility for introducing such a scheme, but so far it has not materialized.⁴

The Nordic model is characterized by a high unionization rate and high collective agreement coverage. Within this framework, however,

the countries have chosen different solutions. While Denmark and Sweden have collective agreements as their only mechanism for regulation of minimum wage levels, Finland, Iceland and Norway have the legal instrument to make agreements generally binding. None of the Nordic countries has adopted a statutory minimum wage.

Statutory minimum wages

National minimum wage rates, among those European countries that have set them, vary significantly, even when adjusting for differences in the costs of goods and services.^{iv} As of January 2015, hourly rates vary from € 11.10 (USD 12.69) (Luxemburg) to € 1.00 (USD 1.14) (Bulgaria).

Figure 1 shows the minimum wage in euros for all EU countries that have defined a statutory minimum wage level.

In **Figure 1** one observes that the eastern European countries clearly have the lowest minimum wages – most of them have rates of €

In terms of the ratio of the minimum wage to the median wage, the Nordic countries and Italy – where minimum wage is laid down in collective agreements – have higher relative minimums than countries with universal rates.

3.00 (USD 3.30) or less per hour. Among the western European EU countries, Portugal, Spain and Greece stand out in terms of their low rates, while countries such as France, Luxemburg, the Netherlands,

Belgium and the United Kingdom have far higher ones. Most countries undertake annual

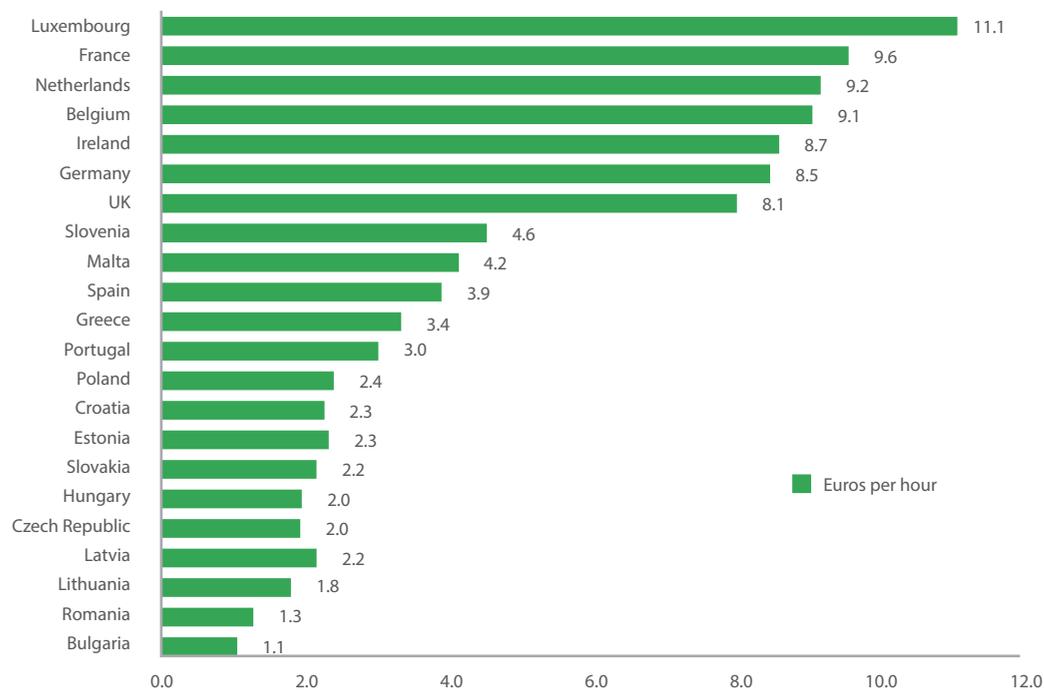
iv The relationship between minimum wages and working hours varies considerably among the countries, in the sense that some countries have defined a minimum pay for overtime, while others have left such issues to be settled in each employment relationship. The same applies to payment for work during inconvenient hours, shift-work supplements etc.

adjustments, although the financial crisis caused many countries to freeze minimum wage levels in 2011 – namely Ireland, Latvia, Lithuania, Portugal, Spain and the Czech Republic. In the last couple of years, most countries have increased their rates at a measured pace.

This overview of nominal minimum wage rates conceals national differences in general levels of prosperity and average wage levels relative to the minimums. Minimum wage levels across diverse economic contexts measured in the same currency provide little information about the value of these minimum wages in the national

Figure 1

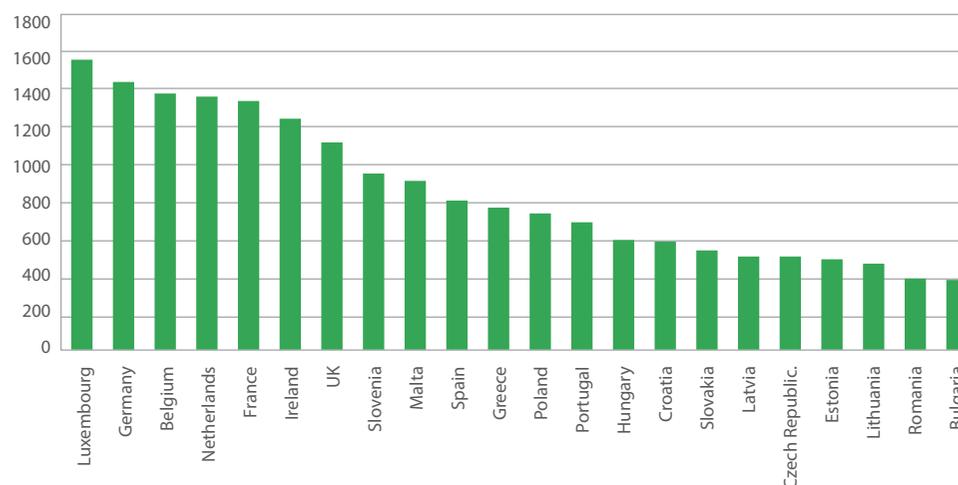
Statutory minimum wage rates in EU countries, in euros, January 2015



Source: WSI-Mindestlohndatenbank 2015

Figure 2

Minimum wages in purchasing power standards in the EU, 2015



Source: Eurostat. 2015.

* Numbers of 1 January (except Croatia July 1, 2008). PPS for 2015 estimated.

context. If price level differences are eliminated, disparities are considerably smaller. One way of measuring this is by expressing minimum wage in purchasing power standards (PPS)^v (Figure 2). Seen in light of purchasing power, the eastern EU countries had in 2013 seen the most positive development.⁵

Another commonly used method to understand the value of the minimum wage rates is to compare

them to national average wages or median wages.

^{vi} In Europe, a low wage is commonly defined as less than 60 percent of the median wage.⁶ Calculations from the Organisation for Economic Co-operation and Development (OECD) of national minimum wage rates as percentages of the national median wage level show that in 2013, the statutory minimum wage rates varied from 36 percent (Czech Republic) to 63 percent (France) of the median wage.⁷ The distinctions

^v Purchasing power parities are used to remove the effect of differences in price levels across countries. Household consumption expenditure in each country is used to convert the monthly minimum wages to an artificial common unit called the purchasing power standard (PPS) (Eurostat 2015 National minimum wages in the EU. Monthly minimum wages in euro varied by 1 to 10 across the EU in January 2015. 35/2015 – February 26, 2015.).

^{vi} This measure is known as the Kaitz Index.

between the various regions of Europe are no longer as marked when these relative measures are applied. In terms of the ratio of the minimum wage to the median wage, the Nordic countries and Italy – where minimum wage is laid down in collective agreements – have higher relative minimums than countries with universal rates.⁸

Effects on employment are a key issue when it comes to statutory minimum wage levels. If the minimum wage is set “too high,”

Advocates for higher compensation see that an EU-wide wage floor could diminish the downward pressure on wages that has resulted from migration. Moreover, it could reduce the regional disparities that drive labor migration.

this may reduce the value of low-paid (and often unskilled) workers in relation to their productivity, and for this reason enterprises may reduce their staffing levels or refrain from hiring new labor. Even though this has become a kind of accepted truth in the European context, studies of the employment effects of minimum wage systems provide few unambiguous answers. Recent international empirical research on minimum wages takes the view that existing minimum wage regimes have minimal if any negative effects on employment.⁹

The case for a European minimum wage

Given that most European countries have already introduced statutory minimum wages, one might ask why some stakeholders are calling for a European minimum wage. This question is particularly confounding since the majority of those countries that do not have a statutory minimum wage do not wish to see one introduced at the European level.

One explanation is that the trade unions in countries with low minimum wage levels want to raise these levels above what can be achieved by way of national bargaining and consultations. Another factor is that some countries have had good experiences with their minimum wage schemes, and would like to see their national policies reinforced at the European level. One example is France, where the Ministry of Finance

recently published an article providing ideas for what the European minimum wage standards should be.¹⁰ Earlier campaigns in Germany on a national minimum wage also spurred the interest in a statutory minimum wage for the EU as a whole, and it remains to be seen whether the introduction of minimum wage in Germany may reduce the pressure for a common European solution.

Beyond these reasons, the reality of labor migration from eastern to western Europe also drives the case for an EU-wide minimum. The eastern enlargement of the EU and the

creation of a single market in 2004 stimulated major changes for many European countries. In increasing numbers, people left countries with low wage levels in the east to take up work in high-income countries in the west, leading to increasing competition for lower-wage jobs in most of the destination countries. This has troubled labor unions in EU member states, as advocacy around higher wages has become more difficult. Advocates for higher compensation see that an EU-wide wage floor could diminish the downward pressure on wages that has resulted from migration. Moreover, it could reduce the regional disparities that drive labor migration.

Is a European minimum wage a possible solution?

The EU's regulation of the labor market has two main elements: First, the regulations for the internal market and second, the "social dimension." The latter is comprised of rules for working environment, equal rights and employees' rights, plus coordination of entitlements to social benefits and cooperation on employment policy, social inclusion, poverty alleviation, social issues and health. Even though the competencies of the EU in the social arena have been considerably strengthened over the course of its history, matters pertaining to wages remain explicitly excluded. According to Article 153, no. 5 of the

treaty, the EU does not have the authority to issue directives or enact other regulations with regard to wage setting. Such regulations would therefore require the unlikely event of member states giving EU institutions increased authority in wage setting, or else would be issued as non-binding recommendations.

Nevertheless, recent years have witnessed a continuous debate in the Parliament on the need for European-level regulations on minimum standards for wages and incomes. And recent developments show that EU institutions do have

the power to shape wage policies across the union, through mechanisms that could ultimately be used to enact EU-wide minimum wage standards.

As shown by Schulten & Müller,¹¹ EU institutions such as the Commission and the European Central Bank have already regularly issued non-binding recommendations on wage policy. Following the 2008 global financial crisis and the European debt crisis that unfolded a couple years later, the institutions have focused on labor costs as

Even though the competencies of the EU in the social arena have been considerably strengthened over the course of its history, matters pertaining to wages remain explicitly excluded.

a central adjustment mechanism for national competitiveness, and thus monitored the development of wages, employee benefits and collective bargaining systems. One could argue that the Commission's recommendations to member states on wage policies in recent years are a kind of European maximum wage policy. Whether this development in the longer term may pave the road for an implementation of a European minimum wage policy remains to be seen.

Nordic resistance toward a European minimum wage policy

While the call for a European minimum wage policy has been welcomed by most trade unions in Europe, Nordic countries in particular have been strongly opposed. This is primarily based on a fear that a minimum wage will weaken the system of collective bargaining in these countries that succeeds in maintaining decent wage levels for the vast majority of workers. Any European measures and campaigns that aim at a statutory

regulation of wages in the member states are met with profound skepticism. Although the Nordic unions have voiced their resistance repeatedly in the ETUC and in several European trade union federations over the last years, they have experienced difficulties in getting their message across.

Strong organizations, high union density, high

collective agreement coverage, well-developed bargaining relations and cooperation between the social partners are core elements of the Nordic labor market model, even though the countries vary in some respects. The collective agreements have a pervasive effect beyond the unionized parts of the labor market, and trade unions maintain that a statutory minimum wage would represent a strong competitor to the collective agreements. It could become acceptable, they believe, for wage rates to follow an EU-wide statutory minimum as opposed to collectively agreed minimum rates, which are inexorably higher. Nevertheless, Nordic countries are considering new wage regulations to cope with labor migration from eastern Europe, which places downward pressure on wages. Denmark and Sweden in particular are increasingly debating the prospect

The collective agreements have a pervasive effect beyond the unionized parts of the labor market, and trade unions maintain that a statutory minimum wage would represent a strong competitor to the collective agreements.

of legal extension of collective agreements. However, it seems far more likely that they will introduce statutory minimum wages. In Norway there is still widespread disagreement regarding the functionality of the current extension scheme, and employers' associations have repeatedly

voiced their view that a statutory minimum wage would represent a better solution.

This contrasts with Germany, where unions eventually came to favor a minimum wage, with employers opposed. The German context also

differs because a statutory minimum wage there is not envisioned as an alternative to collective agreements. On the contrary, Germany's new minimum wage law creates the opportunity for new extensions of collective agreements to ensure that these remain the main basis for wage formation.

Outlook

There are clear signs indicating that the debates on a European minimum wage will continue. In his appointment speech as President of the EU in July 2014, Jean-Claude Juncker stated that

all EU countries ought to introduce a minimum wage or minimum income.¹² Juncker has also made similar statements on earlier occasions. The question is whether his statements signal

that EU institutions want to gain more influence over minimum wage policies in member states. If nothing else, Juncker's speech indicates that the topic of a "European minimum wage" may remain the subject of contentious debate.¹³

The increase in the numbers of working poor and low-wage workers in Europe in the wake of the financial crisis has revived the debate also within the European trade union movement.¹⁴ Most likely the discussions will continue at the coming ETUC congress in Paris in 2015. However, agreement on a common European strategy with regard to minimum wage will likely remain elusive.

In the view of this chapter's authors, the debates so far have suffered from a mutual lack of understanding of the different positions. To a certain extent, the Nordic trade unions have been perceived as egoistic and unwilling to grasp the magnitude of the low-wage problem in Europe. From their perspective, meanwhile, it seems almost impossible to support a policy they fear could threaten their current collectively agreed minimum wage-setting processes. Although the

Nordic unions now recognize that a statutory minimum wage may be a 'necessary evil' in some countries, most of them are still very far from supporting a European minimum wage policy. However, the situation in many EU countries calls for measures that can strengthen the position for those working at the low-income end of the

The only – and difficult - way forward is probably to develop a joint minimum wage policy that is strong enough to have an impact on countries with growing low-wage sectors and weak trade unions, but at the same time flexible enough that opponents are convinced it will not impair their high-functioning collective bargaining systems.

labor market. Such measures would have to accommodate the fact that wages are determined differently in different member states, and that changing these systems could affect ways in which national regulatory mechanisms function. The only – and difficult - way forward is to develop a joint minimum wage policy that is strong enough to

have an impact on countries with growing low-wage sectors and weak trade unions, but at the same time flexible enough that opponents are convinced it will not impair their high-functioning collective bargaining systems. A successful outcome will by all accounts require a measure developed and anchored among all three social partners - government, employers and workers - at both the national and EU level.

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BEYOND MINIMUM WAGES IN CORPORATE CODES OF CONDUCT

Private sector innovation toward realizing fair compensation

Jason Judd and Andrew Korfhage, Fair Labor Association

Fair Labor Association (FLA)

Fair Labor Association (FLA) is a collaborative effort of universities, civil society organizations and socially responsible companies dedicated to protecting workers' rights around the world. FLA is an international organization with a dedicated staff and board, headquartered in Washington, DC, with offices in China, Switzerland and Turkey. FLA places the onus on companies to voluntarily meet internationally recognized labor standards wherever their products are made.

FLA is a guest contributor to this volume.

BEYOND MINIMUM WAGES IN CORPORATE CODES OF CONDUCT

Private sector innovation toward realizing fair compensation

Jason Judd and Andrew Korfhage, Fair Labor Association

Introduction

Around the globe, debates over the minimum wage continue in many countries where global brands buy and make their products.

In Myanmar, the garment employers' association argues for keeping garment workers' wages lower than the other industries, ostensibly to spur investment in the country. In Haiti, workers and companies debate the disparity between the legal minimum daily rate and legal minimum piece rate. And in some countries disagreements over minimum wage levels can be so intense they result in mass demonstrations and—as in Cambodia in 2014—violent suppression of wage protests.

Despite these serious debates, workers find that even when a minimum wage is adopted – or its level increased – they often remain unable to afford a basic standard of living. Minimum wages in many countries are simply too low, or government enforcement is lax.

For this reason, corporate codes of conduct that only commit companies to pay minimum or market wages to their workers have proven—in most key sourcing countries—insufficient in the task of ensuring workers are fairly compensated. To do their share, global brands must commit to a higher standard than just paying minimum wages.

The companies that affiliate with the Fair Labor Association (FLA) and similarly designed initiatives have accepted this higher standard, and in February 2015 the FLA launched its Fair Compensation Work Plan – a strategy for buyers, suppliers, and unions to move companies toward meeting their Code of Conduct obligations on fair compensation, and for the FLA to hold them accountable for measurable progress.

The crisis of poverty wages

When global brands follow business models that continually seek the lowest possible cost of production, pressure on suppliers to lower costs can keep both minimum and actual wages low. Governments likewise play a role in keeping minimum wages low, in countries where the low cost of labor is used as a selling point to invite investment.

The 2014 report “Tailored Wages” produced by the Clean Clothes Campaign, in partnership with the Asia Floor Wage Alliance, demonstrated that few companies are currently implementing a corporate code of conduct that can make up for gaps between legal minimum wages and what workers need to live. The report found that of the 40 apparel brands they surveyed, only half made a commitment in their company code of conduct to pay wages that met workers’ basic needs, and only four were “able to demonstrate clear progress on implementing this.”¹

While this report focused primarily on wages in Asia, a subsequent Clean Clothes Campaign report, published in 2015, found similar conditions in the post-Communist economies

of Eastern Europe.² This report found that the gap between the legal minimum wage and the estimated living wage was even greater in the cheaper labor countries of Europe than in Asia. A May 2014 study by the Solidarity Center found that workers in Haiti earning the minimum piece rate make barely enough money to pay for their meals and transportation.³

Similarly, in 2012 and 2013, as part of its annual factory assessments, the FLA began asking workers whether their wages met their basic needs. Across all countries and all sectors⁴ covered by the FLA, the majority of workers surveyed reported that they were unable to meet their basic needs within a regular workweek at their current wage levels.

Other research finds employers failing to pay their workers even the government-mandated minimum wages they are owed. For example, the

American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) reported in March 2015 that 70 percent of employers in Honduras violate the minimum wage law.⁵ In

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the United States, the Department of Labor found that illegal wage violations in 2014 cost workers more than US\$ 3 million in the Southern California garment industry. And in 2014, the FLA found that in 9 percent of its announced factory visits,⁶ workers were not earning the minimum wage. In an additional 16 percent of factory visits, FLA assessors found instances of miscalculated or unpaid overtime.

In China, the country where the FLA conducted the most assessments by far, assessors found unpaid overtime and non-payment of minimum

FLA assessors found that only slightly more than 10 percent of factories assessed in China were paying full and accurate benefits on all five forms of social insurance – pension, medical, work-related injury, unemployment, and maternity.

wages in 25 and 10 percent of all factories, respectively (See **Table 1**). In both the electronics and apparel sectors of China, assessors found widespread disregard for the legal obligation to provide workers with social insurance and Housing Provident Fund benefits.

FLA assessors found that only slightly more than 10 percent of factories assessed in China were paying full and accurate benefits on all five forms of social insurance – pension, medical, work-related injury, unemployment, and maternity.⁷ (See **Table 2**) Chinese law likewise requires

Table 1
Compensation-Related Violations In FLA Assessments, 2014

Violation	Number Of Violations (Among 129 Assessments)	Percentage	Countries
Failure to maintain accurate payroll records	31	24%	China, India, Pakistan
Maintenance of false payroll records	20	16%	Guatemala, China, India, Indonesia, Mexico, Slovenia, Sri Lanka, Taiwan, Turkey, USA
Unpaid or miscalculated overtime	20	16%	China, India, Indonesia, Pakistan, Turkey
Non-payment of minimum wage	12	9%	China, India, Indonesia, Pakistan

Table 2

Legal Pay Violations In FLA Assessments In China, 2014

Violation	Number Of Findings (Among 129 Assessments)	Percentage
Non-payment of Housing Provident Fund	47	98%
Non-payment of social insurance	42	88%
Non-payment of minimum wage	13	25%
Unpaid or miscalculated overtime	5	10%

employers to pay into the Housing Provident Fund, and assessors found only one of the 48

facilities to be providing contributions correctly.⁸

The FLA's fair compensation work plan

As a first principle, the FLA's plan emphasizes the gravity of legal pay violations in supply chains, comparing them to fire safety or child labor violations that require swift and immediate remediation.

Beyond calling for the remediation of legal pay violations, such as those mentioned above, the Fair Compensation Work Plan prepares affiliated companies for assessments that flag the parts of the supply chain—from individual suppliers to key sourcing countries—where companies need to work with unions, workers, and governments to close the gap between prevailing wages and fair compensation.

The plan begins with a global stock-taking of the landscape for workers' wages in 2015, followed by a period of original FLA research to help brands and suppliers understand best practices for closing the gap between actual earnings and fair compensation. By 2017, the FLA will set out clear goals for member companies to meet in their own detailed plans, focusing first on countries where the gap between pay and fair compensation is the widest.

Companies are expected to demonstrate that their efforts—including revised sourcing strategies and purchasing practices, engagement

with unions, national governments, and more—are progressing towards fair compensation at their supplier facilities. These plans will be subject to revision, and companies will be measured for progress, with those findings published by the FLA. Companies that fail to engage meaningfully

on the issue of fair compensation will be subject to a review of their affiliation status.

The compensation data collected and analyzed by the FLA in its 129 factory assessments in 2015 will be published—within the bounds drawn

Figure 1
Median Monthly Compensation in U.S. Dollars as Compared to Various Wage Standards⁹ (US\$)

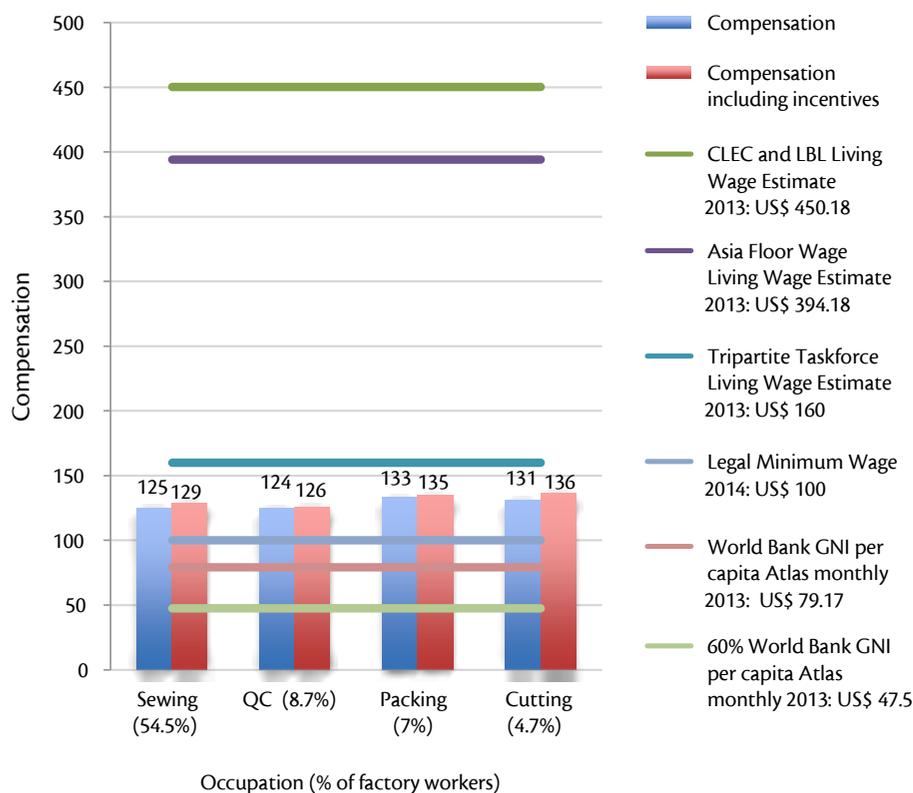
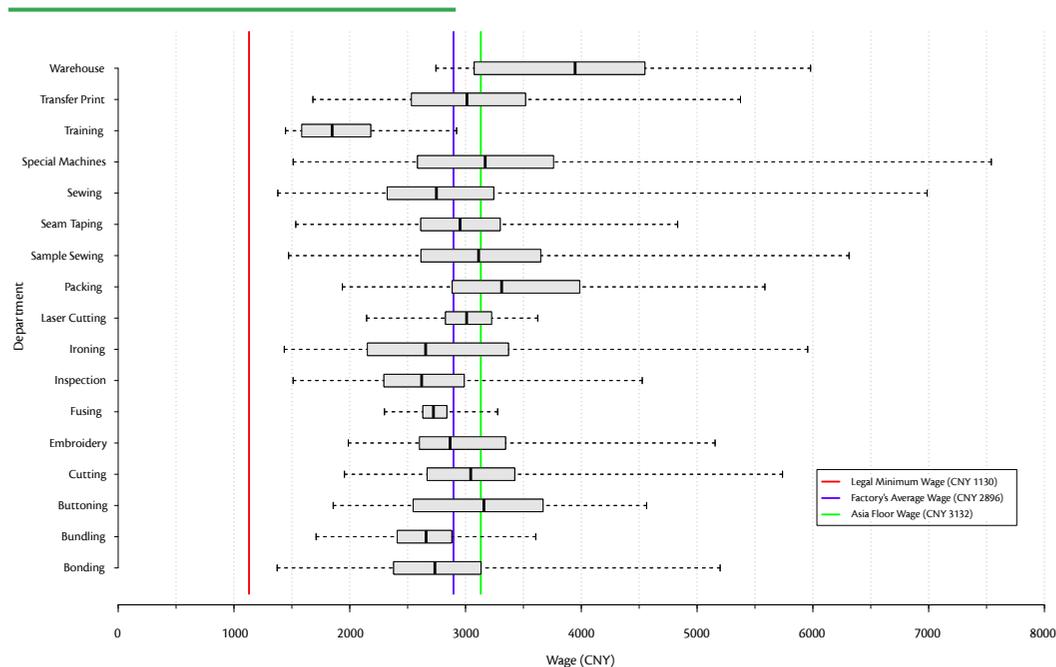


Figure 2
**Wage Data from KTC Limited,
 Garments Manufacturer**



by anti-trust law—in compensation “ladders” showing how factory-level pay stacks up against different benchmarks, including legal minimum wages, poverty line measures, and living wages. **Figure 1** is an example of how the new data will be organized, using Cambodia as an example.

Also in mid-2015, the FLA will pilot the use of mobile phone platforms to collect pay data

directly from workers in key manufacturing areas such as Dhaka and Istanbul. This data and analysis will be published by the FLA and the Cornell University Industrial and Labor Relations School Project on Sustainable Labor Practices in Global Supply Chains.

This systematic data collection and analysis by the FLA and companies, plus data solicited directly

from workers, will help fill critical gaps in the wage landscape. The research will enable the FLA to develop a comprehensive set of benchmarks that FLA affiliates and other stakeholders can use to gauge the gap between wages paid to workers and fair compensation.

Some FLA affiliates are already leading the way. KTC Limited, a Hong Kong-based supplier of technical outerwear with factories in China and Laos, already posts its China wage data publicly, demonstrating how its compensation strategy measures up to objective benchmarks

– the country’s legal minimum wage, the Asia Floor Wage, and the overall average wages at the factory (see **Figure 2**). An early goal of the FLA’s fair compensation work

is to make KTC’s strategy the norm, such that suppliers and buyers have a clear understanding of wage levels in any given facility, whether those

levels need to rise, and—crucially—how buyers, suppliers, and workers together will make it happen.

In May 2016, the FLA plans to publish its first annual compensation report, organizing and disclosing a compilation of compensation data collected by the FLA, its research partners, and its affiliates. This report will be the first of its kind to disclose this data¹⁰ and is designed to drive the

debate over pay from questions of “how much” and “where to focus” to the critical questions of “when” and “how.”

Beyond calling for the remediation of legal pay violations, such as those mentioned above, the Fair Compensation Work Plan prepares affiliated companies for assessments that flag the parts of the supply chain where companies need to work with unions, workers, and governments to close the gap between prevailing wages and fair compensation.

A research agenda for designing fair wage strategies

The FLA Fair Compensation Work Plan anticipates a number of strategies for brands to employ to get to fair compensation for their workers, including: engaging in collective bargaining with unions and workers, engaging national governments on wage policy, adjusting their own purchasing and pricing strategies, and developing cooperative relationships with suppliers¹¹ that share their commitment to fair compensation.

To help affiliates learn about the best strategies for achieving fair compensation for workers, the FLA will conduct a series of research projects that will explore how labor costs are negotiated, shared, or offset in relationships between buyers and suppliers.

Some FLA-affiliated buyers already have experience with specific strategies for working with suppliers to raise wages, such as the Fair Wage process (piloted by Adidas, H&M, and Puma), and the Fair Trade USA model (followed by some Patagonia and prAna suppliers).

The Fair Wage process uses three primary tools for assessing whether wages paid by any given supplier are fair to workers. Two rounds of surveys are conducted, the first for factory management and the second an anonymous survey on wages conducted with a representative sample of workers at the same factory. The two surveys

measure 12 “dimensions” of fair wages, going beyond asking if wages meet the legal minimum, or local prevailing wages, to investigate links between wages and performance, cases of wage discrimination, and other issues.¹² The third phase is customized and includes a site visit to investigate any identified problems and cooperate on solutions with the supplier.

While the fair trade model originated as a way to provide higher prices for the producers of commodities, Fair Trade USA has recently expanded its model into apparel supply chains as well. For apparel, the fair trade model involves adding a supplemental premium onto the brand’s Free on Board (FOB) prices paid to suppliers. The amount of this premium is determined by an assessment of wages in the target factory. A worker-committee chooses to distribute the funds to the workers, or to invest in a community development project.

Because workers and unions in many countries experience routine violations of their organizing rights, a second key research question will examine how companies can best support collective bargaining in the diverse industrial relations systems found in sourcing countries around the world. While explicitly endorsing all forms of bargaining by effective, legitimate unions – at the supplier, sectoral, and national levels – as the

best, simplest, and most sustainable mechanism for achieving fair compensation for workers, the FLA will focus its research on how buyers and suppliers can support sector-level bargaining, to maximize the number of workers covered. As IndustriALL has reported, “company agreements tend to cover only a small percentage of non-unionized workers (7 percent on average), [while] under industry agreements, this rises to over 40 percent.”¹³

Existing research confirms that if companies are to protect workers’ collective bargaining rights, they must focus specifically on this issue, as freedom of association violations are far less likely to be uncovered by factory assessments than other violations.¹⁴ The FLA receives and investigates third-party complaints regarding freedom of association at a far higher rate than these violations are reported through factory assessments. Recent FLA freedom-of-association investigations in Honduras¹⁵ and Turkey¹⁶ have resulted respectively in restoration of wages to workers illegally fired for union association and the resumption of a stalled collective bargaining process.

New FLA research on freedom of association will support the fair compensation work by outlining

new ways that companies can support collective bargaining at the factory, sectoral, and national levels.

Buyers and suppliers investing in new approaches to fair wages may be reluctant to share details of their early efforts, both to preserve their advantages over competitors, and to maintain caution about announcing progress before their approach has been modeled, tested, and scaled up. As companies’ approaches mature, however, the FLA anticipates that the organization will independently study and report on its affiliates’ efforts.

The FLA will focus its research on how buyers and suppliers can support sector-level bargaining to maximize the number of workers covered.

One of the most relevant recent analyses — conducted by the International Labor Organization (ILO) this year and not yet published in full — examines the roles of buyers and suppliers in complying with the 2014 increase in Cambodia’s minimum wage. It plots changes in supplier prices and U.S. retail prices against changes in wages and cost of living for workers in the Cambodian garment sector. Among other questions, the study asks what share of higher labor costs suppliers can meet through productivity gains, and how buyer pricing can impact wage levels and the longer-term viability of Cambodia’s garment industry.

It directly confronts the question of who has to pay when wage levels have to rise, noting that the prices Cambodian factories receive have been “stagnating or declining.” At the same time, the study shows that expected wage increases are “far higher than what can be generated through efficiency gains.” The study concludes that buyers must make up the difference.

To cover the shortfall, and assuming other costs remained the same, the ILO estimates that global brands would need to pay Cambodian factories between 2.4 and 3 percent more, adding about two cents to the production costs of T-shirts that can currently be made for 80 cents and that might retail for about US\$ 10.¹⁷ Similarly, an August 2014 study conducted by Georgetown University found that the Alta Gracia factory in the Dominican Republic – a factory

committed to paying living wages – was able to increase compensation for workers with only very small increases to the cost to produce a shirt.¹⁸ The report found that brands can choose to absorb

these costs, or pass them on to consumers with very small mark-ups, while some amount of the cost will be “off-set by increases in worker productivity and quality control, reduced turnover, fewer marketing costs, and initially lower profits.”

Fair compensation strategies can catalyze innovation among buyers, suppliers, unions, and governments. The

FLA’s work plan expects companies to treat fair compensation as a core business challenge and opportunity that requires the use of their considerable resources and talents, and not merely as a social compliance obligation.

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Fair compensation is a right

The Ruggie Framework, as approved by the UN Human Rights Council, identifies a “state duty to protect against human rights abuses by third parties, including business.” Building off this principle, the FLA framework calls for international brands to actively engage with governments to ensure that wage regulations are in line with the goal that every worker receives a living wage. In November 2014, nine FLA-affiliated brands took a stand in support of legitimate collective bargaining and higher wages in Cambodia.

But the goal of fair wages cannot wait on government action in places where minimum wages are too low. So in the framework’s second

pillar, the “corporate responsibility to respect human rights” comes into play, obligating socially responsible companies to pay fair wages out of respect for their workers’ human rights.

The data collection project that the FLA is now beginning – combined with the data collection efforts of affiliated companies and others examining wages worldwide – will show the private sector where it is obligated to pay higher wages. This process will help drive the next wave of innovation in production, as buyers, suppliers, unions, and governments grapple with strategies to make measurable progress towards fair compensation.

Endnotes

¹ Clean Clothes Campaign. 2014. Are the big brands paying the people who make our clothes enough to live on? Accessed on August 14, 2015. <http://www.cleanclothes.org/livingwage/tailoredwages/tailored-wage-report-pdf>

² Clean Clothes Campaign. 2014. Poverty wages for garment workers in Eastern Europe and Turkey. Accessed on August 14, 2015. <http://www.cleanclothes.org/resources/publications/stitched-up-1>

³ Solidarity Center. 2014. The High Cost Of Low Wages In Haiti. Accessed on August 14, 2015. <http://www.solidaritycenter.org/wp-content/uploads/2014/11/Haiti.Living-Wage-Study-FINAL-updated.3-11-15.pdf>

⁴ The FLA primarily works with apparel and footwear companies. Among its affiliates, the FLA also includes two agricultural companies and an electronics company.

⁵ AFL-CIO. 2015. Trade, Violence and Migration: The Broken Promises to Honduran Workers. Accessed on August 14, 2015. <http://www.aflcio.org/content/download/147761/3770791/file/Honduras.PDF>

⁶ The FLA conducted 129 factory assessments in 2014 in Bangladesh, Cambodia, China, El Salvador, Guatemala, Honduras, India, Indonesia, Jordan, Laos, Malaysia, Mexico, Pakistan, Singapore, Slovenia, Sri Lanka, Taiwan, Thailand, Turkey, the USA, and Vietnam.

⁷ One prominent supplier affiliated with the FLA recently completed a comprehensive revision of its social benefits program to come into full and complete compliance with national law. The FLA's verification report of its progress can be found at: <http://www.fairlabor.org/report/social-benefit-verification-factories-operated-pou-chen>.

⁸ More information on social insurance and Housing Provident Fund requirements can be found at: <http://www.fairlabor.org/report/social-insurance-china> and <http://www.fairlabor.org/report/housing-provident-fund-china>

⁹ Data for Figure 1 are from the following sources:

- Actual 2013-14 compensation is taken from sample of 19 Cambodian apparel manufacturers. Figure 1 above categorizes workers into the largest four occupations.
- CLEC and LBL Living Wage Estimate 2013 (US\$ 450.18): The Community Legal Education Centre (CLEC) – a Cambodian NGO – and Labour Behind the Label (LBL) – a UK-based NGO – calculate living wage based on food consumption and price for a family of three, including one worker and two dependents.
- Asia Floor Wage Living Wage Estimate 2013 (US\$ 394.18): Living wage estimate based on food consumption and price for a family of three including one worker and two dependents (dependent counts as half of the consumption unit) by Asia Floor Wage Alliance, a global coalition of trade unions and workers' and human rights organizations.
- Tripartite Taskforce Living Wage Estimate 2013 (US\$ 160): Living wage estimate based on basic needs expenditure for a worker and his/her family (family size not specified) by a tripartite taskforce comprised of Cambodian government officials, representatives of both the Garment Manufacturers Association in Cambodia (GMAC) and Cambodian trade unions. Information comes from "Crackdown in Cambodia: Workers Seeking Higher Wages Meet Violent Repression" by Worker Rights Consortium, March 24, 2014.
- Legal Minimum Wage 2014: US\$ 100.
- World Bank GNI per capita Atlas monthly 2013 (US\$ 79.17): Original data from World Bank GNI per capita based on the Atlas method (current U.S. dollars) is 950 US dollars per year – or 79.17 per month (<http://data.worldbank.org/indicator/NY.GNP.PCAP.CD>).
- 60% World Bank GNI per capita Atlas 2013 monthly (USD 47.5): 60% of the World Bank GNI per capita Atlas monthly figure. This is a variation on the standard OECD measure for poverty.

¹⁰ This data will be disclosed within the limits allowed by anti-competition law.

¹¹ These relationships will necessarily be within the bounds of anti-trust law.

¹² The 12 dimensions of the Fair Wage process are: (1) Payment of wages (Are wages paid in full and on time?); (2) Living wage (Do wages meet workers' basic needs and provide discretionary income?); (3) Minimum wage (Do wages exceed the local legal minimum?); (4) Prevailing wage (Do wages exceed the local industry standard?); (5) Working hours (Can workers earn fair compensation without excessive working hours?); (6) Pay systems and wage structures (Are holidays and social benefits properly paid? Does piece rate allow workers to earn fair compensation?); (7) Social dialogue and communication (Does the supplier communicate clearly on wages with workers and unions?); (8) Wage disparity (Are there cases of wage discrimination?); (9) Real wages (Do wages keep pace with inflation?); (10) Wage share (Are workers' wages linked to company performance?); (11) Wage costs (Is the share of labor costs within total production cost holding steady or increasing?); (12) Wages, training, and technology (Do wages progress with training and technological improvements?).

¹³ industriall. 2015. Industry bargaining is an essential tool in the fight for living wages. Accessed on August 14, 2015. <http://www.industriall-union.org/special-report-industry-bargaining-is-an-essential-tool-in-the-fight-for-living-wages>

¹⁴ Mark Anner. 2010. Corporate Social Responsibility and International Labor Rights: The Quest for Legitimacy and Control. Accessed on August 14, 2015. https://mitsloan.mit.edu/iwer/pdf/Mark_Anner-IWER_paper_20111101.pdf

¹⁵ Fair Labor Association. 2015. Freedom Of Association Violations At Petralex In Honduras. Accessed on August 14, 2015. <http://www.fairlabor.org/report/freedom-association-violations-petralex-honduras>

¹⁶ Fair Labor Association. 2015. Orma Tekstil Independent Freedom Of Association Investigation. Accessed on August 14, 2015. <http://www.fairlabor.org/report/orma-tekstil-independent-freedom-association-investigation>

¹⁷ UN News Centre. 2015. UN agency calls on global clothing brands to help Cambodian manufacturers absorb wage hike. Accessed on August 14, 2015. <http://www.un.org/apps/news/story.asp?NewsID=49731#VZ52iRNVhBc>

¹⁸ John M. Kline and Edward Soule. 2014. Alta Gracia: Four Years and Counting. Accessed on August 14, 2015. <https://georgetown.app.box.com/s/8jgos0ainsv13civ-o30q>

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