



FIFTH ITEM ON THE AGENDA

The minimum wage: Catalyst for social dialogue or economic policy instrument

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Introduction

1. At first glance it seems all too easy simply to define the minimum wage as the wage floor applying to all wage earners to ensure that they receive at least a minimum of protection when it comes to their pay. This, indeed, is what is stipulated in the first Articles of Conventions Nos. 26 and 131. In reality, things are a lot more complicated, as may be seen by the amazing variety of legislative texts and practices existing in this area. Here, we need to distinguish between two stages involved in the process of fixing minimum wages. The first is related to the actual procedures: the parties concerned, the extent to which they participate in determining the minimum wage itself, the categories of workers covered, etc. The second stage has to do with the decision reached: the factors taken into account and the levels at which minimum wages are fixed.
2. The range of possible procedures is endless, depending upon the number of parties involved in the wage-fixing process and the characteristics of the work and employee in question (the kind of activity, where it is carried out, the worker's qualifications). But there is one basic issue that is common to those many and varied procedures and that is collective bargaining; or rather the "choice" that is made between state intervention and collective bargaining. The latter is always a factor in the minimum wage fixing process; through attempts to make up for its absence or to curtail, establish or develop it. In many cases, the minimum wage is a starting point, from which, once it has been established, the collective bargaining process branches out to cover other aspects of working conditions.
3. The minimum wage is determined in the light of a wide range of criteria that vary according to the country or period in time. The reason for this is that each of these criteria are linked to different objectives. In one country the minimum wage may be perceived as a way of ensuring a decent standard of living; in this case, the criterion of purchasing power will take precedence over other considerations. However, the fight against inflation may well be a priority in another country – or might become so in the same country at a later date. Here, it is the inflation rate that will be the main factor. Yet again, there is an aspect common to all these different situations: the minimum wage is an economic and social policy instrument which makes it possible to achieve varied objectives, from income distribution to economic competitiveness. In each country it is adjusted in a myriad of ways, reflecting national characteristics and models – a process that is not devoid of contradictions.

The minimum wage and collective bargaining

4. Minimum wage fixing procedures vary from governmental statutory decisions to negotiation of wages through joint agreements. In the Lao People's Democratic Republic and Nigeria, it is the Government that sets the minimum wage whilst, in Greece, it is fixed through an agreement between the social partners. In Poland, a tripartite commission establishes the minimum wage. Nevertheless, in most cases, it is the government that decides, usually after consultation or bargaining with trade union and employers' organizations.
5. At the same time, these methods fall within a range stretching from the setting of a single minimum rate, to the fixing of wages covering a large section of the wage hierarchy used in companies. Spain has a single rate, India 1,230 rates. No universal system exists.
6. From the outset, minimum wage fixing has been intrinsically linked to the level of development of collective bargaining and the role of the state in wage policy. Indeed,

wages have always been the number-one concern for wage earners. More often than not, in the absence of a structured collective organization, requests for pay increases have led to disputes and strikes. To make up for the lack of collective bargaining that would have provided the means to settle disagreements amicably, governments have often had to intervene directly to resolve wage disputes. With time, in certain states, collective bargaining has gradually been developed to such an extent that, in the end, it has been capable of dealing with wage disputes. In other countries, the state has continued to play the major role in wage setting.

7. New Zealand is thus held to be the first country to have implemented a modern system to regulate minimum wages with the principal aim of avoiding labour disputes. This system was introduced at the end of the nineteenth century. Much later on, in 1957 in Uganda, the colonial authority at the time published a report recommending an increase in the minimum wage, which had been frozen for around ten years, on the grounds that the absence of an appropriate wage-fixing system could lead to unrest and strikes.¹ It is also very revealing that the first example of state intervention regarding minimum wages in European countries, at the beginning of the last century, was an attempt to protect domestic workers. Indeed, the fact that this group was fragmented and covered very many distinctive relationships made it extremely difficult for its members to have even a minimum organization enabling them to defend their rights through collective bargaining. Other categories of workers were supposedly able to organize themselves to defend their interests through collective bargaining. In the United Kingdom, wage councils were therefore set up for these very reasons in the sectors where organization was at its weakest. In others, the social partners fixed wages through collective bargaining. This clearly shows that minimum wage systems are closely linked to the ability – or lack of it – of collective bargaining to deal with wage fixing. From the outset, therefore, state regulation and intervention, on the one hand, and collective bargaining, on the other, have, on this issue, been interchangeable; the context is the determining factor.
8. This relationship between minimum wage fixing, state intervention and the development of collective bargaining is still present in countries which have recently moved to introduce such systems. The system in Lesotho is under the control of the Government, which fixes wages for 21 manual occupations. Taking into account the details involved, this is not just a straightforward minimum wage system; it is much more a regulation of actual wage policies. Nowadays, trade unions disapprove this type of rigid mechanism that does not take into account the ability of companies and sectors to pay. Trade unions now feel strong enough to replace this system with true sectoral collective bargaining. Should this trend continue, the minimum wage will have served as a catalyst in the development of collective bargaining. Once established, negotiation procedures might deal with wider issues than wages (working time, working environment, etc.).
9. One basic conclusion may be drawn from this analysis: historically, the minimum wage is an issue that more often than not has triggered the development of collective bargaining. But that does not mean that the passage has always been smooth and that there have been no exceptions to the rule. For instance, British trade unions were long opposed to the establishment of a minimum wage.² Today, within the German trade union movement there is a vigorous ongoing debate between supporters and opponents of the minimum wage. The latter have put forward a very practical concern: wage earners guaranteed a

¹ J. Weeks: “Wage policy and the colonial legacy: A comparative study”, in *The Journal of Modern African Studies* (London, 1971), Vol. 9, Issue 3, pp. 361-387.

² The TUC came round to the idea of a minimum wage in 1985, followed by the Labour Party in 1986. See: D. Metcalf: “The British national minimum wage”, in *British Journal of Industrial Relations* (London, 1999), Vol. 37, No. 2, pp. 171-201.

minimum wage will have less reason to join a trade union to defend their interests. The basic problem lies in the definition of the aim of having a minimum wage: fixing a wage floor or regulating the entire wage-fixing process. The political will of the actors concerned and their efforts to organize are linked to this problem.

10. Experience has shown that, when social dialogue merely deals with the fixing of a minimum wage at the national level, considerable pressure is exercised at this level, leading to demands for increases that may seem excessive. This is so because it is the only forum in which trade unions can show clearly what they are doing to defend the workers. Minimum wage fixing therefore becomes a serious source of conflict. Adjusting bargaining levels to the stated objectives reduces the social pressure involved in minimum wage fixing. Associating this process with sectoral or enterprise-level negotiations that set out to establish wage levels adapted to their economic situation as well as their internal job market, means that possibilities and constraints can be better taken into account, thus introducing increased objectivity and rationality into social dialogue.
11. A statutory minimum wage fixing system, once it has been set up, can still carry out functions other than those that fall under collective bargaining. This is especially true when it comes to issues within the field of economic policy, be they employment, inflation or income redistribution. The system acquires another dimension which explains, if not justifies, why the state wishes to retain control over it rather than placing it back in the hands of collective bargaining, once established. That is what this document seeks to explore.

The minimum wage and poverty

12. The main aim of the minimum wage is to protect the lowest wage earners in order to guarantee them a decent standard of living. This aim represents what is both laudable and ambiguous about the minimum wage. On the plus side, it is an instrument used in the defence of the poorest wage earners. It is, however, ambiguous because of this very virtue, in that it is often seen as the perfect instrument in the fight against poverty in general, a role that it cannot possibly fulfil on its own.
13. The principle of the minimum wage has been, from the very beginning, that it is an income unconnected with the act of production; it is a sum owed to the worker and essentially linked to the status of wage earner. The earliest methods of minimum wage fixing clearly demonstrate this approach. Whether or not an enterprise can pay or the wage earner's output is sufficient is irrelevant; the minimum wage is primarily concerned with how much the worker needs to live on – and not only the worker but his or her family. No reference is made to the worker's contribution to the enterprise in terms of production; what counts is whether a worker can provide for himself and his family. When the minimum wage was first introduced, in the industrialized countries, wage earner productivity was not even an issue. Wages were so low that workers were not properly paid no matter how much they produced. Of course, things are very different nowadays in a number of countries. Could the minimum wage now be used as a tool in the fight against poverty?
14. This debate was echoed recently with the implementation of minimum wage legislation in the United Kingdom. The terms of reference of the Low Pay Commission, responsible for setting up the system, carefully avoided any mention of acceptable minimum living conditions, in other words, making the minimum wage an instrument to combat poverty.³

³ W. Brown: "The operation of the Low Pay Commission", in *Employee Relations* (Bradford, W. Yorks), Vol. 24, Issue 6, pp. 595-605.

Without going into the details of the underlying tax reasons, the basic position was that attempts to combat poverty called for other instruments. The minimum wage was only one component in a battery of measures forming a coherent policy in the fight against poverty amongst workers. This is also the position adopted in Recommendation No. 135. There should be no contradiction between the level of the minimum wage and the system that provides the subsidies enabling the most destitute to live, be they wage earners or not. This viewpoint is shared by numerous observers who, for example, advocate the use of negative taxation as a basic measure in the fight against poverty, rather than the minimum wage.⁴

15. A common criticism levelled against the minimum wage as an anti-poverty instrument is that it only benefits wage earners and, furthermore, only those working in the formal sector, provided it is applied. Of course this is a particularly serious restriction in developing countries but, all too often, the level of restriction has been exaggerated. The wage paid a formal sector worker goes towards ensuring, in part, the survival of an extended family, whatever the country's level of development. What is more, the minimum wage has an impact on wages in the informal sector in that it provides a benchmark. It has been demonstrated that an increase in the minimum wage has led to a rise in wages in the informal sector. This has been the case in certain Latin American middle-income countries, such as Brazil, Mexico, Argentina and Uruguay, where the minimum wage was relatively low during the 1980s, at between 20 and 25 per cent of the average wage. In those countries, almost all workers in the formal economy received wages that were higher than the minimum wage whilst many workers in the informal sector received the *exact* minimum wage. Many saw their wages go up with each readjustment of the minimum wage, including during periods of low inflation.⁵ Finally, the minimum wage is a powerful means of increasing the wages of individuals at the bottom of the pay scale. For example, when the minimum wage was raised by 13 per cent in 1990 in the United States, workers whose wages were lower than the new rate, received, on average, a 10 per cent increase.⁶
16. The fact that, in many countries, certain social benefits are linked to the level of and variations in the minimum wage is often overlooked. Most commonly, the relationship is with retirement benefit and disability payments. It is less often linked to unemployment and maternity benefits. In many West African, North African and Latin American countries, a fixed percentage of the minimum wage (between 60 and 100 per cent) makes up the minimum retirement benefit of beneficiaries. In the Netherlands, the threshold for unemployment benefits, as well as that for disability payments, is 70 per cent of the minimum wage.
17. In this way, the minimum wage is being used as a "social floor". For example, the adjustment of retirement benefits with each increase in the minimum wage should in principle, in such a system, maintain the purchasing power of the very poorest pensioners. In addition, society as a whole is able to benefit from the progress brought about by economic development and the fruits of growth when minimum wage adjustments are linked accordingly.
18. When the minimum wage has this basic role, it is both fair (the most vulnerable pensioners need a guarantee that the purchasing power of their retirement benefits will not be eroded)

⁴ R. Burkhauser and A. Finegan: "The economics of minimum wage legislation revisited", in *Cato Journal* (Washington, DC, 1993), Vol. 13, No. 1, pp. 123-129.

⁵ M. Neri, G. Gonzaga and J.M. Camargo: "Salário mínimo, 'efeito-farol' e pobreza", in *Revista de economia política*, (Sao Paulo, 2001), Vol. 21, No. 2, pp. 78-90.

⁶ D. Card and A.B. Krueger: *Myth and measurement. The new economics of the minimum wage* (Princeton University Press, Princeton, NJ, 1995).

and straightforward (a single instrument adjusts an entire section of the social protection system); however, there is clearly a risk that any rise in the minimum wage may lead to a huge increase in social security costs – and a certain lack of flexibility ensues. An interesting case in point is Brazil. Since the mid-90s, the minimum wage in this country has risen in real terms and the Government increased it by 8.33 per cent in May 2004, i.e. at a rate higher than that of inflation. But this policy change did not satisfy the trade unions because, in terms of purchasing power, as the minimum wage had lost ground after years of increases at rates which did not keep up with rises in the cost of living, this latest increase could not make up the difference. The Government's basic objection to a massive increase in the minimum wage lay in its link to numerous social security benefits. Such a move would have threatened the stability of the public budget.

19. In conclusion, it is fair to say that the minimum wage plays, or can play, a role in the fight against poverty. Looking at things from this angle, an assessment of earnings of workers paid the minimum wage should be one of the criteria for judging the success or failure of this policy – alongside its impact on employment, for example. Nonetheless, for this to be meaningful, the minimum wage must be a part of an overall policy and it should have a limited number of realistic aims that do not contradict one another. The current tendency is to use the minimum wage in a number of roles, both in the social and economic field. Indeed the minimum wage is frequently used in the social field to fight against wage inequality and discrimination.

The minimum wage and wage inequality

20. The minimum wage may be used to promote pay equity by levelling out differences in wages – particularly to reduce the gap between the average wage of men and women. There are two ideas involved here: first, the minimum wage introduces the same pay threshold for both sexes which immediately cuts down on discrimination; and second, those wage earners at the bottom of the pay scale, the majority of whom are usually women, benefit from the minimum wage.
21. This was the case in the United Kingdom where 70 per cent of women benefited from the minimum wage when it was introduced, together with its consequent adjustment over the 1999-2000 period. At the same time, average full-time hourly earnings for women increased from 81 to 82 per cent of average male hourly earnings. A more significant increase was seen for female part-time workers, with their part-time earnings increasing from 81 to 89 per cent of male earnings.⁷
22. However, in Latin America in general, higher minimum wages reduce wage inequality but not necessarily the gender pay gap: female wage earners are not necessarily at the bottom of the pay scale.⁸ It should be noted here that, in a small number of countries, the government seeks to limit the pay gap by using the minimum wage as a “benchmark”, a figure to be referred to when fixing other wages. Such is the case in Algeria, where basic pay rates for state managerial staff or particular categories of civil servants are set at x times the minimum wage – thus, in part, limiting the pay gap.

⁷ Low Pay Commission: *The national minimum wage: Making a difference*, Third report of the Low Pay Commission (London, 2001), Vol. 1, CM 5075; J. Rubery: *Pay equity, minimum wage and equality at work*, Report for the ILO (Geneva, 2002), p. 57.

⁸ D. Grimshaw and M. Miozzo: *Minimum wages and pay equity in Latin America: Identifying the employment and pay equity effects*, DECLARATION Working Paper 12/2003 (Geneva, ILO, 2003).

23. On the other hand, however, a static minimum wage will most often have the opposite effect: a rise in wage inequality. In Brazil, for example, the fall in the actual value of the minimum wage over the 1963-79 period went hand-in-hand with a drop in “blue-collar” workers’ earnings compared to those of “white-collar” workers.⁹ In a similar fashion, in the United States, the drop in the minimum wage between 1970 and 1990 was largely responsible for the increase in the pay gap between native-born wage earners and immigrants.¹⁰
24. The same conclusions can be drawn from studying the body of documents dealing with the effect of the minimum wage on wage inequality in Member States of the OECD.¹¹ First, an increase in the minimum wage reduces the wages range and the greater the increase, the narrower the wages range becomes. Second, the rise in the minimum wage reduces both the gender pay gap, and the pay gap between adult and younger workers. The latter trend can be explained by the concentration of young people and women at the bottom of the wage scale.
25. Governmental use of the minimum wage within the context of structural adjustment policies can, involuntarily, have an undesirable effect on wage discrimination or poverty. This is particularly true of anti-inflationary policies.

The minimum wage, inflation and public deficits

26. The change in the cost of living is the criterion most often present in legislation on the minimum wage and the one that is most often compulsory. In general, the legislator’s initial concern, when introducing such a factor, has been to maintain the minimum wage’s purchasing power. But this relationship works in two ways. An increase in the minimum wage protects the lowest paid wage earners from inflation but it also runs the risk of accelerating the inflationary spiral by having an impact on wage costs and putting pressure on overall demand due to its effect on wages and public deficits. This whole issue needs to be handled with the utmost care. In theory, there should be no link between the minimum wage and the wage hierarchy, given that the minimum wage only affects the worst-off wage earners. In practice, however, an increase in the minimum wage would have an effect on real wages across the board, as – and this is a fundamental and universal aspect of the minimum wage – it is considered to be a benchmark from the point of view of wages, whether this is deliberate or not.
27. There are as many examples demonstrating this benchmark role, as there are countries with a minimum wage. Until 1994, the Republic of Korea adjusted its minimum wage in January. Wage negotiations within the private sector also take place at the beginning of the year. The social partners saw the rise in the minimum wage as a point of reference, which also underpinned wage increases. To avoid such a link, the authorities have altered the date of the increase of the minimum wage, fixing it in September. In doing so, they have

⁹ J.M. Camargo: *Minimum wages in Brazil: Theory, policy and empirical evidence*, Labour management relations series (Geneva, ILO, 1988), No. 67, pp. 55-80.

¹⁰ K. Butcher and J. DiNardo: “The immigrant and native-born wage distributions: Evidence from United States censuses”, in *Industrial and Labor Relations Review* (New York, 2002), Vol. 56, Issue 1, pp. 97-121.

¹¹ Organisation for Economic Co-operation and Development (OECD): *Employment Outlook* (Paris, 1998).

adopted the model provided by the adjustment mechanism used by their Japanese neighbours. This mechanism makes for a role reversal. The minimum wage is only fixed once the “spring offensive” has ended. In other words, the minimum wage is increased according to the rises in real wages, negotiated in the spring within the private sector and thus the relationship is reversed.

28. The impact that the minimum wage can have on wages may explain its role in anti-inflationary policies. The minimum wage can have a direct effect when there is an indexation clause related to the cost-of-living index. In many countries, this formal link has been challenged during periods of high inflation. Such was the case in the 1980s in Europe, when countries like Denmark, Austria, Belgium, Italy and France altered or even dropped minimum wage indexing. In France, although minimum wage increases continue, in part, to be index-linked to inflation, the legislation prohibits any reference to the price index or to minimum wage adjustments during wage negotiations. Of course, this official ban does not stop the social partners from taking both these elements into account implicitly. A rise in the minimum wage can lead to an increased payroll as a result of the increase in low wages and its subsequent dispersion throughout the wage hierarchy.
29. In these circumstances, the use of the minimum wage as a tool to curb inflation and public deficits can take two forms. The first is radical, consisting of keeping the minimum wage at the same level until it is so low that it barely plays any role at all as a benchmark. The second takes increases in the minimum wage as a reference. Either the minimum wage is frozen, as it was in the Netherlands during the 1980s, or it is increased in line with predicted inflation rates rather than recent ones, so as to avoid transferring the pace of inflation from the previous year to the next year. Another possibility is to systematically fix the rise in the minimum wage below the rate of inflation, thus demonstrating the will to curb the growth in wages, as was done in Mexico.
30. These two techniques were extensively used in most Latin American countries faced with two-, three- or sometimes even four-figure inflation rates during the 1980s. What were the results of this policy? One thing is sure: the minimum wage fell in real terms in many Latin American countries over a long period of time. In Mexico, for example, prices rose 260-fold between 1981 and 1995 whilst at the same time the purchasing power of the minimum wage was divided by 2.9. In Brazil, prices rose more than 600 million-fold whilst the purchasing power of the minimum wage fell by over two-thirds between 1985 and 1994.
31. Matters are far less clear when it comes to the effect on inflation. Households, businesses, institutions – in short, all the economic stakeholders – have seen successive increases in the minimum wages as signs that wages are to be upgraded; this is immediately reflected by businesses in their prices, thus fuelling the inflationary spiral.
32. Although the objectives are different, a similar predicament can be observed in the area of employment policy: although its aim is to combat unemployment, its effects on sustainable employment are less clear.

The minimum wage and employment

33. The relationship between minimum wages and employment has been looked into more deeply than any other and is also the most controversial. Admittedly, when employers apply the minimum wage – leaving to one side situations where the minimum wage is so low that it plays no role whatsoever in the wage hierarchy – increases in that wage definitely represent an extra production cost for businesses. This rise may lead employers to replace labour with capital or skilled workers with unskilled workers, who are those

most likely to receive the minimum wage, thus contributing to the growth in unemployment.

- 34.** However, suggesting to trade unions that any increase in the minimum wage must be curbed to avoid increased unemployment is somewhat spurious. It may well come across as an excuse to fix the minimum wage at a level which would make it meaningless. Slovenian trade unions thus refute the argument whereby a minimum wage, even a low one, would run the risk of seriously affecting the country's textiles sector. They note that a number of businesses in this sector are, in any case, certain to fail due to competition from developing countries and that the argument about the textiles sector cannot be continually used to block the fixing of a decent minimum wage. This is similar to the idea put forward by the Low Pay Commission, the body that deals with minimum wage fixing in the United Kingdom, when it notes that the use of low wages as a tool for competitiveness is common amongst companies, especially the smallest companies, where personnel management is particularly poor. The question that then arises is not that of the survival of marginal businesses but of whether successful companies can recover the markets lost by these businesses following the increase in the minimum wage, alongside the workforce consequently made redundant.¹²
- 35.** Nonetheless, the Government of the United Kingdom was keen to ensure that the establishment of a minimum wage should not affect its youth unemployment reduction policy. That is why a reduced rate for young people aged 18 to 22 years was put in place. It should be stressed that only a minority of countries have put lower rates in place for young people. This decision was doubtless justified on grounds of professional experience – but the basic reason was that unemployment was particularly high amongst young workers and it was reasoned that employers would be more likely to recruit them if the cost of taking them on was reduced. We shall put this theory to the test in the following paragraphs.
- 36.** Another link that can be found between minimum wages and employment is at the level of unemployment benefits or minimum income. In China, the minimum wage is fixed at a higher level than unemployment benefits, in order to motivate the unemployed to look for a job.
- 37.** The idea that the minimum wage creates unemployment was very much taken for granted in most industrialized countries until the beginning of the 1990s. More recently, the concept has lost ground following the publication of several studies showing that the minimum wage had little or no negative effect on employment, even having a positive effect. In middle-income developing countries, the perception that the minimum wage creates unemployment is still widespread, even though available studies show that such effects have to be qualified.
- 38.** One reason for this about-turn in economic thinking is that statistical classic analyses based on time series did not take into account certain hypotheses. This meant that the negative impact of the minimum wage was overestimated, as is demonstrated in the following example:

¹² Brown, *op. cit.*

Table 1. The impact of a 10 per cent minimum wage increase on employment amongst young people in the United States, 1954-1979 (in percentages) ¹³

Method	Results
Analysis of classic time series	-0.95
Analysis of time series taking into account the volatility of seasonal employment and respecting the statistical conditions of stationarity	-0.5 (not significant)

- 39.** Bernstein and Schmitt's study uses two different methods, based on identical data covering the same period, to estimate the impact of a minimum wage increase on employment in the United States. The first analysis, based on classic time series, shows that between 1954 and 1979 a 10 per cent minimum wage increase brought down employment amongst young people by almost 1 per cent (statistically significant coefficient). The second analysis, which takes account of the volatility of seasonal employment and respects the conditions of stationarity, shows that, although the effect of the minimum wage on employment among young people in the United States remains negative, it is clearly less marked. In this case, a 10 per cent minimum wage increase only reduces employment by 0.5 per cent, which is not a statistically significant coefficient.
- 40.** In middle-income developing countries, such as Indonesia or Brazil, the studies available show that the negative effect of the minimum salary on employment is just as minimal, and, in some cases, it is positive (see table below).

Table 2. Effect of the minimum wage on employment in certain developing countries

Rama ¹	Indonesia, 1990-95	The doubling of the minimum wage in real terms had a negative but slight effect on employment (-2 per cent). Employment apparently decreased in small enterprises and increased in large ones.
Lemos ²	Brazil, 1982-2000	A 10 per cent increase in the minimum wage was linked to a total employment effect ranging between -0.9 and +1.4 per cent.

¹ M. Rama: *The consequences of doubling the minimum wage: The case of Indonesia*, Policy Research Working Paper No. 1643 (Washington, DC, World Bank, 1996).

² S. Lemos: *A menu of minimum wage variables for evaluating employment effects: Evidence from Brazil*, University College London Working Paper 03-02 (London, 2003).

- 41.** Readjustments of the minimum wage do not, therefore, always have a significant effect on the level of employment. They may, nonetheless, lead to a drop in employment within certain categories of the population and a parallel rise within others. This may be attributed to the fact that the group of low-paid workers affected by changes in the minimum wage is very mixed (students, people with few skills, people waiting to find a better job in certain countries, skilled workers in other countries).
- 42.** The study carried out by Yuen ¹⁴ shows that in Canada, increases in the minimum wage reduce employment amongst those workers at the bottom of the pay scale, whose productivity is low and who have few skills and little chance of finding a better paid job.

¹³ J. Bernstein and J. Schmitt: *Making work pay: The impact of the 1996-97 minimum wage increase* (Economic Policy Institute, Washington, DC, 1998).

¹⁴ T. Yuen: "The effect of minimum wages on youth employment in Canada. A panel study", in *The Journal of Human Resources* (University of Wisconsin, Madison, 2003), Vol. 38, No. 3, pp. 647-672.

However, they give a boost to employment amongst other categories of workers receiving the same wage, such as students or workers temporarily “trapped” in a low paid job but whose skills mean that they have every chance of finding a better job later on.

43. The fact remains that during periods when unemployment levels are high, especially amongst low-skilled workers and young people – two categories often over-represented when it comes to those earning the minimum wage – it is very tempting to play around with the level of the minimum wage in the hope that employment will go up. This means taking the risk of weakening the role that the minimum wage might be able to play in poverty-reduction strategies. Herein lies a contradiction similar to that cited regarding the use of the minimum wage in the fight against inflation.
44. Having said that, proposed minimum wage increases should not be out of proportion with the prevailing economic and social conditions, for fear of producing a negative effect on competitiveness, or more simply, of non-respect of adjustments. In Chile, the adjustment to the minimum wage, which was 17.1 per cent higher than that of productivity between 1998 and 2000, led to a growth in the proportion of workers paid less than the minimum wage and the proportion of workers without written contracts, without affecting unemployment in the short term.¹⁵

Conclusion and recommendations

45. The information collected to date makes it possible to draw some fairly reliable conclusions. First, with its links to certain basic social security benefits, the minimum wage is a good instrument for protecting poor workers, as well as other vulnerable categories. Second, the minimum wage has an effect on the wage hierarchy and can be used to combat discrimination and improve the standard of life of workers at the bottom of the pay scale. Third, during periods of growth, appropriate increases in the minimum wage have no real significant effect on unemployment, and, as for their effect on inflation, this is far from convincing.
46. Given all of this, we believe it advisable to refocus the use of the minimum wage on its primary function, that is to say, the defence of the lowest paid wage earners and the fight against wage inequality.
47. When governments keep minimum wage increases in check in order to curb unemployment or better control inflation – or for other reasons such as the search for competitive wage costs – they run the risk of eventually losing an effective social policy instrument. The same is true if too many social security benefits are automatically linked to minimum wage adjustments. This, for example, is what happened in Uruguay from 1976 onwards, or in the Russian Federation in 1992, when the minimum wage only accounted for 5.6 per cent of the average wage (as opposed to 14 per cent in 1991 and 23.6 per cent in 1989), showing how meaningless it was within the wage hierarchy.¹⁶ It is worth recalling a number of countries where the level of the minimum wage remained unchanged over a period of several years: Côte d’Ivoire between 1982 and 1993 (the purchasing power of the minimum wage fell by three-quarters); El Salvador between 1980 and 1985 (the purchasing power of the minimum wage was halved); and the United States on numerous

¹⁵ R. Infante, A. Marinakis and J. Velasco: *Minimum wage in Chile: An example of the potential and limitations of this policy instrument*, Employment Paper 2003/52, Employment Sector (ILO, Geneva, 2003).

¹⁶ G. Standing and D. Vaughan-Whitehead (eds.): *Minimum wages in Central and Eastern Europe: From protection to destitution* (Central European University Press, Budapest, 1995).

occasions, for example between 1950 and 1955 (-10.1 per cent), and between 1981 and 1989 (-26.7 per cent). Another risk that governments run in allowing the minimum wage to fall in value is that they may be faced with demands that would be difficult to meet.

48. Finally, the use by governments of the minimum wage as a tool for economic policy is closely linked to its use related to collective bargaining. Basic, undeveloped collective bargaining can leave the field open to extending the influence of a statutory minimum wage, increasing the number of rates and categories covered. In turn, the intensive use of the minimum wage by a government with a view to achieving various economic policy objectives will lead it, willingly or not, to reducing the role of collective bargaining in the field of wages in order to better control its development. Conversely, a well-established collective bargaining process will be more likely to have the effect of excluding government intervention or restricting its role to the protection of the most poorly paid wage earners.
49. It is vital to take into account these different relationships when creating or adjusting a minimum wage system. Finally, the desired objectives must be carefully identified, whilst bearing in mind the fact that the protection of the lowest paid wage earners is the primary aim.
50. The Committee is invited to discuss the analysis contained in this document so that its views might be taken into account in technical cooperation programmes, in the promotion of Convention No. 131, in all discussions with other international agencies on matters relating to poverty and in all future research work.

Geneva, 27 September 2004.

Submitted for discussion.