

# Prices and Incomes and Labour Market Policies

# 17

## Multiple Choice Answers

1	A	6	D	11	B	16	B
2	D	7	B	12	B	17	C
3	D	8	D	13	B	18	C
4	C	9	C	14	C	19	B
5	D	10	B	15	C	20	A

## Short Answer Questions

### Question 1

- a) Enterprise bargaining refers to negotiations between employers and employees (or their representatives) about pay and working conditions within an individual firm.
- b) Collective enterprise bargaining involves a group of employees, often represented by a union, directly negotiating with the management of a firm to set the pay and working conditions within the firm. Collective bargaining may offer employees greater bargaining power as a group for higher pay and working conditions.
- c) The minimum wage is set by a government body. Currently the Australian Fair Pay Commission sets the minimum wage after conducting its own economic research and hearing submissions from groups in the economy. After 2010 the federal minimum wage will be set by a body to be known as Fair Work Australia.
- d) Enterprise bargaining involves direct negotiations between employers and employees to set pay and working conditions within a firm. The introduction of enterprise bargaining in the early 1990s involved a decentralisation of wage determination, away from a central government body and towards the individual firm. Enterprise bargaining advantages firms and the economy in general because it promotes higher levels of productivity. When workers are reliant on enterprise bargaining to obtain a wage increase, they will be forced to demonstrate increases in productivity. This either provides an incentive for workers to improve productivity, or forces less productive workers to improve productivity or risk losing their wage increase. Employees under enterprise bargaining have a more flexible way to obtain higher wages since employees will have a greater opportunity to earn higher wages by increasing productivity. However, enterprise bargaining is often determined by bargaining power and not productivity. Occupations with relatively low skill levels and low demand across the economy may find it difficult to obtain significant wage increases. Also, occupations which are experiencing a shortage of skilled labour would have higher bargaining power because of the fact that the firm cannot find other workers in the labour market. Finally, individual enterprise bargaining has the potential to shift bargaining power to the firm, as individuals are not often properly trained in negotiation, which is a vital skill needed in enterprise bargaining.

**Question 2**

- a) Decentralisation involves moving wage determination decisions away from a central government authority to the level of the individual firm or the individual employee. This means that rather than one wage decision for an industry or the economy, wage decisions are made throughout the economy which better reflect the conditions within individual firms.
- b) Decentralisation should result in lower levels of inflation. A centralised wage fixing system often awards pay increases based on firms' capacity to pay. If firms have not experienced increases in productivity or sales, they will be forced to pass on this increased cost in the form of higher prices. Additionally, centralised wage fixing provides no incentive for workers to improve productivity, which means that wage increases often become highly inflationary. Under a decentralised wage system, wages become linked to improvements in productivity, which means that wage increases do not need to be passed on in the form of higher prices since the firm will have experienced an increase in its output with the same number of inputs.
- c) Wage indexation involves tying centralised wage increases to increases in the inflation rate. Under this system, if inflation increases, the government automatically increases wages across the economy. Since there has been no improvement in productivity, firms are forced to pass on the increase in costs in the form of higher prices. This raises cost push inflation, which will in turn lead to another increase in wages. This situation is known as a wage price spiral, and leads to persistent high rates of inflation as well as high inflationary expectations.
- d) The Australian industrial relations system has undergone a process of decentralisation over the past decade. The introduction of collective enterprise bargaining and then individual enterprise bargaining has improved the level of productivity in the economy. Enterprise bargaining provides incentives for workers to improve their productivity, since workers have the opportunity to earn higher wages by improving productivity. Individual enterprise negotiation in particular allows individual workers to improve productivity over and above other employees at the firm in return for higher wages. Also, workers who are less productive will be forced to either increase productivity or accept a lower wage increase. Recently, the Rudd Government has announced changes to the industrial relations system (known as to *Fair Work Australia*) to strengthen the role of the award and remove formal individual enterprise bargaining. This means that individual bargaining no longer has the ability to force less productive workers to improve productivity in order to obtain a wage increase. However, workers will still have the opportunity to obtain higher wages by improving productivity through a common law contract. As a result of the introduction of enterprise bargaining, productivity levels increased from averages of 2 per cent per year in the 1980s to 3 per cent per year over the 1990s and parts of the 2000s.

**Question 3**

- a) An award is an instrument regulating pay and working conditions across an industry, set by a government body. After 2010, modern awards will contain the 10 National Employment Standards provisions and 10 industry-specific provisions.
- b) Awards form the safety net of the industrial relations system. For those not covered by enterprise agreements, they provide the minimum pay and working conditions which workers are entitled to, consisting of the 10 National Employment Standards, which cover 10 minimum standards common to the economy as a whole, and 10 industry-specific standards to provide flexibility between industries. Awards also form a safety net for enterprise agreements by forming the yardstick by which the agreements are measured. If an enterprise agreement goes below an award condition, the employee must be compensated elsewhere in the enterprise agreement in order to pass the 'no disadvantage' test, or after 2010, the 'Better Off Overall' test.
- c) The re-introduction of the 'no-disadvantage' test with the introduction of the *Transition to Forward with Fairness*, and its replacement with the 'Better Off Overall' test after 2010 should improve the distribution of income, as it ensures that the ability for employees to reduce wages will be limited to the safety net of the award. Also, the elimination of formal individual enterprise bargaining will shift the focus of the formal industrial relations system to collective bargaining. Since workers in lower skilled industries tend to have stronger collective bargaining power than they have as individuals, this should ensure higher wage increases for lower skilled workers, at a faster rate than under individual bargaining where the bargaining power of an individual may be much lower than the employer.

- d)** Labour market programs can be used to reduce the natural rate of unemployment, which tends to be unaffected by changes to macroeconomic policy. The government may implement a labour skills training program for the unemployed to help those people will skills that are no longer in demand in the economy retrain and gain skills that are demanded in emerging sectors of the economy. The policy of *Skilling Australia for the Future* involves an independent body – Skills Australia – selecting the areas in which retraining vouchers will be offered so as to ease skills shortages elsewhere in the economy. The *Job Services Australia* agency (formerly the *Job Network*) aims to improve the availability of information in the labour market, which should reduce the time taken for workers to switch between jobs, reducing frictional unemployment. *Job Services Australia* also subsumes the ‘Work for the Dole’ program, which provides a disincentive for people to remain voluntarily unemployed, and also a minimum level of skills and work experience to help increase their prospects of employment. Finally, the government can use labour market policy to increase the flexibility of labour, and to increase incentives for workers to increase productivity by tying wage increases more closely to productivity. This would increase the attractiveness of labour relative to capital, providing a long-run incentive for firms to use labour in preference to capital, reducing unemployment.