

National Minimum Wage

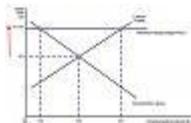
What is the national minimum wage and why do we have it?

The National Minimum Wage refers to the *legal minimum hourly rate of pay* an employer pays its workers. Rates differ from country to country and it also depends on the age of the worker e.g. the current **UK rate** for ages 21 and over, (as of 2013) is £6.31.

The minimum wage is a floor wage which **protects workers in low-paid occupations** such as shop assistants, cleaners and laundries. It is a form of government intervention.

Explanation of the National Minimum Wage diagram:

So what is the effect of a national minimum wage?! If it is **set above the market equilibrium wage** (the wage rate that produces neither an excess of demand of workers or excess of supply of workers) in a labour market then it could cause **unemployment**, which is shown by the diagram and an explanation provided below:



From looking at the diagram, we know that **W1Q2 is the market equilibrium wage (where demand and supply meet)**, and has **increased** to the **national minimum wage rate which is Wmin**. So how exactly does the NMW cause unemployment if it is set above the market equilibrium wage?

Diagram shows that **demand for labour has decreased** from **0Q2 to 0Q3** (follow the dotted lines to help you). Diagram also shows that **supply of labour extended** from **0Q2 to 0Q1**, **meaning there is excess supply of labour which is Q3Q1** (x axis shows employment of labour).

So, if the demand for workers has decreased and there is an excess supply of workers, it evidently means that the minimum wage has caused unemployment, which is what the NMW diagram is all about!

Advantages of increasing NMW:

- A **reduction in exploitation of labour and poverty**.
- A **reduction in wage inequality between men and women**. Women tend to be disproportionately represented in low-paid occupations and so benefit most from an increase in NMW.
- Incentive to take on low-paid work means there is a reduction in voluntary unemployment.
- **Labour productivity increases** because **workers are more satisfied with their jobs**. Firms may also increase training of workers in order to increase productivity and so justify paying the higher wage.
- To keep up with an increase in the cost of living due to inflation.

Disadvantages of increasing the NMW (evaluation):

- Can be **increases in unemployment** because firms may find that it is **too expensive to employ workers** (more costs for the firm). Therefore, workers may be replaced with **capital** (machinery) e.g. self checkout tills in supermarkets.
- An increase in inflationary pressure as **firms pass on the extra wage costs to consumers in the form of higher prices for their products.**
- It is an **ineffective way of reducing poverty since many poor people don't work** e.g. the unemployed, sick and elderly. Similarly, many people who benefit from the NMW may not be from poor households e.g. students and second wage earners.
- An increase in red tape or bureaucracy for firms leading to higher costs and less flexibility in the labour market - representation of government failure?
- **Elasticity:** A **wage-inelastic demand for labour** will lead to only a few job losses. It means **workers are hard to replace in the production process** e.g. cleaners. Whereas a **wage-elastic demand for labour** will lead to a large proportion of job losses because **workers are easier to replace in the production process** e.g. supermarket cashiers replaced by self checkout tills.