The Implementation of Minimum Wages in Malaysia: Issues & Challenges

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Introduction

Motivation

- Slow growth of wages relative to labour productivity growth
- New Economic Model: to have growth with inclusiveness, to ensure that the low income people are not left out in reaping the benefits of growth and enjoying better quality of life.

Why?

- Income growth among the top 20% income earners has been strong; however, the income of the bottom 40% was rather stagnant.
- About 33% (3.2 mil) of workers in the private sector are earning < RM700 a month in 2010 and below the poverty line income of RM763 a month (for Peninsular Malaysia in 2009).
- Reduce our dependence on cheap labour.
Definition

- ILO: lowest basic wage guaranteed by law as an attempt to put a floor under the wages of a particular subgroup of the working population, that is, the working poor.

- In Article 7 of the ILO Convention no 131 on minimum wage fixing (1970) and its accompanying recommendation no 135, specify that the minimum wage should not be fixed at a lower rate than one which would ensure the subsistence of the worker and his or her family.

→ Before the implementation of the national minimum wage, Malaysia did not ratify to this convention.
Rationale For A Minimum Wage Policy

- Positive impacts on the welfare of the low income workers
- Increase wages without reducing employment levels
- Reduce reliance on foreign workers
- Improve the circumstances of the working poor and unequal distribution of income
- Reduce low income group in line with high income economy objective
- Promote productivity growth
If implemented correctly, and set at the right level, minimum wages can increase wages without reducing employment levels. Card and Krueger (1993) confirmed that minimum wages can increase employment in New Jersey. Neumark and Wascher (1994) found no compelling evidence to support the view that minimum wages help in poverty alleviation. However, Neumark and Wascher (2000) which used matched CPS surveys, found that over a 1-to-2 year period, minimum wages increase the probability that poor families escape poverty line. Levine (1992) and Raff and Summers (1987) found that minimum wages will increase workers’ productivity. This may be due to increased work effort, multitasking, reduce job turn over and more job training in order to enhance the labour capability. Ransom (1993 and 1962) and Mincer and Leighton (1981) found that minimum wages tend to have adverse impact on employment.
Justification For A National Minimum Wage Policy

Minimise regional biasness

- Productivity may be influenced by sector, location and market.
- To avoid market distortion

Different minimum wage rate in Peninsular Malaysia and Sabah Sarawak.

- Different geographical area would result in different technology and productivity level.

Lack of worker bargaining power

- Regardless of sector and productivity
Dimensions Considered In Implementing The Minimum Wage Policy

- Economic sectors
- Women participation
- Country’s regions
- Informal sector
Objectives Of Minimum Wage Policy

The national wages consultative council outlined the following objectives:

• Ensuring the basic needs of workers and their families are met,
• Providing sufficient social protection to workers,
• Encouraging industry to move up the value chain by investing in higher technology and increase labour productivity, and
• Reducing the nation’s dependence on unskilled foreign labour.
Wages Councils Act 1947 (Act 195)

- Established to fix legal minimum wages for certain occupations or industries as recommended by the commissions of inquiry (COIs)
- Lacked the framework to enforce compliance and continuously review of the minimum wages rates


- Contains provisions on matters relating to the establishment of the NWCC, minimum wage order, investigation and enforcement, offences and penalties and other general matters
Criteria For Setting The Minimum Wage

The common criteria that many countries consider in implementing their minimum wages are:

- Labour productivity
- Wages level
- Competitiveness
- Cost of living
- Consumer price index
- Unemployment
- GDP growth
- Consumer price index
Minimum Wage Formula

The minimum wage formula is specified as follows:

\[
MW_i = \text{Avg} \left( \frac{PLI_i}{\text{Avg workers per household}} + \text{Median wage}_i \right) \times \left[ 1 + \left( \frac{P_i}{100} \right) + \left( \frac{CPI_i}{100} \right) - \left( \frac{UE_i}{100} \right) \right]
\]

where

- \( MW \) = Minimum wage in RM
- \( PLI \) = Poverty Line Income (RM)
- \( P \) = Productivity growth (%)
- \( CPI \) = % change in Consumer Price Index
- \( UE \) = Real Unemployment Rate (%): Actual Unemployment Rate minus Natural Unemployment Rate (4%)
- \( i \) = Region
<table>
<thead>
<tr>
<th>Region</th>
<th>Monthly MW Rate</th>
<th>Hourly MW Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Peninsular Malaysia</td>
<td>RM900</td>
<td>RM4.33</td>
</tr>
<tr>
<td>Sarawak and Sabah*</td>
<td>RM800</td>
<td>RM3.85</td>
</tr>
</tbody>
</table>

* Including Federal Territory of Labuan.
Some Lessons Learned From Other Countries

The design, implementation and adjustment of the minimum wages require good quality data, considerable analytical capacity and time-intensive and evidence-based analysis.

Balance in the bargaining powers of the negotiating parties in the decision-making process.

Impact of the minimum wage depends on the number of workers that it affects and on how easy it is to evade it.

Be aware of other policies that interact with the minimum wage policy.

Computation and coverage of the minimum wage needs to be thorough.

Labour market must be prepared for the implementation of the minimum wage law.
Implementation of the MW

- The Minimum Wage Order 2012 was gazetted on 16 July, 2012
- 1 January, 2013 for employers with >5 workers (about 22% of business establishments), and on 1 July, 2013 for employers employing five and less workers, excluding firms that provide professional services classified under the Malaysian Standard Classification of Occupation (MASCO) like science and engineering, health, teaching, ICT, legal, hospitality, retail and services professionals.
- Those companies that have problems to restructure to implement the minimum wages can apply for deferment before the deadlines given by the Ministry of Human Resources. The organisations that have more than five employees are generally assumed to be in a better position to implement the minimum wages compared to those that employ fewer workers. All establishments are required to restructure their workers pay before the dates of enforcement. The minimum wage rates are to be reviewed every two years as required by the NWCC Act 2011.
Issues and Challenges

- Higher cost of employing foreign workers, led to further deferment for SMEs.
- The objective to reduce reliance on foreign workers – minimal impact.
- Small enterprises find it hard to absorb higher wage costs.
- Possibility of shifting to informal sector.
- Unproductive and incompetent firms may face closure.
- Possible domino effect on higher wage structure.
- Difficulties in absorbing service charges especially in the hotel industry.
- Some employers are taking more time to adjust and comply, and the public sector that uses their services may also take time to revise their contract.
Conclusion

- The concept of implementing the minimum wage needs to be understood in order to appreciate the reasons for implementing the national minimum wages.
- The rationale, objectives, coverage and technical details of its implementation have shown how thorough studies and considerations have been made and carried out before any decision related to it is made.
- The government has also learned from the experience of other countries and initiatives were taken to avoid problems faced by them.
- However, managing the implementation of minimum wage is never an easy task.
- With meticulous preparation for an optimal design of the minimum wage policy, Malaysia is facing its own challenges to ensure that it will be able to achieve the objectives set in the minimum wage policy.
Thank You