



# **Mutual Learning Programme**

DG Employment, Social Affairs and Inclusion

**Peer Country Comments Paper - Germany**

## **The German minimum wage – owned by the social partners?**

**Peer Review on “Minimum wages – extending coverage  
in an effective manner”**

**Cyprus, 19-20 September 2019**



**EUROPEAN COMMISSION**

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Unit A1 - Employment and social aspects of European semester

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## **1 Introduction**

This paper has been prepared for the Peer Review on "Minimum wages – extending coverage in an effective manner" within the framework of the Mutual Learning Programme. It provides a comparative assessment of the policy example of the host country (Cyprus) and the situation in Germany. For information on the host country example, please refer to the Host Country Discussion Paper (Christofides, 2019).

## **2 Situation in the peer country**

### **2.1 Strong employment growth since 2009**

After an exceptionally long boom phase between 2009 and 2018, the German economy is currently experiencing a cooldown. Because of rising wages and high levels of public investments, domestic demand remains robust; however, the autumn of 2018 brought an extended downturn in the export-oriented German manufacturing industry which reduced the growth rate of GDP in 2019 according to the most recent forecasts to about 0.6 % (see Table 1 in Annex).

Employment has grown from 2009-2018 by nearly 4 million (3 985 000) and – despite the present cooldown – further employment increase by 473 000 persons is expected in 2019. In 2018, the unemployment rate in Germany reached a new low since re-unification between the East and the West in 1990, with just 5.2 % of the active population out of work. It is expected that the unemployment rate will fall below 5.0 % in 2019.

Most of the employment growth between 2009-2018 related to employees (+ 4 267 000) while the number of self-employed decreased (- 282 000). This does not indicate a decline of entrepreneurial spirit in the German working population but rather the reduction of unsustainable micro-businesses with very low earnings. The employment growth was not linked, as in most other EU-Member States, with an increase of the share of atypical workers (part-time with less than 20 hours. per week, temporary and temp agency employed). Between 1990 and 2009 the share of atypical employees continuously grew but is slowly decreasing since then (Figure 1 in Annex).

### **2.2 Concerning high income inequality**

In the past, strong social partnership guaranteed that productivity increases were relatively evenly distributed. This has changed since the late 1990s. The coverage by collective agreements fell from 85 % in the early 1990s to 57 % in West and 44 % in East Germany in 2017 (Figure 2 in Annex). Because of the absence of a statutory minimum wage until 2015, pay at the bottom end of the earnings distribution plunged sharply downwards (Fernández-Macías and Vacas-Soriano, 2013).

In periods of high employment growth, wage inequality normally declines. In Germany, however, due to declining importance of collective bargaining in many of the fast-growing service industries the share of low-wage workers increased to a level far above the EU average (Figure 3). Even the introduction of the minimum wage in 2015 did not significantly reduce this share since the minimum wage was set below the low-wage threshold (2/3 of the median hourly wage) which amounted to EUR 10.22 in 2015.

Particularly concerning is that low-wage jobs serve less as steppingstones towards better paid jobs than in the past. More and more low-wage careers became the norm where employees in the low-wage sector have limited chances of upward mobility (Bundesregierung, 2017). An important reason for the declining earnings mobility is the increasing concentration of low-wage jobs in subcontracting companies which are cut off from the career ladders in core companies and are not covered by a collective agreement.

### 2.3 The introduction of industry specific minimum wages and the statutory minimum wage

In the past, Germany has been numbered among the countries with 'autonomous' wage-setting systems, in which companies or employers' associations and trade unions negotiate pay and many other employment conditions, usually at industry level and without any direct state intervention. The state only intervened directly in the wage-setting process at the initiative of the social partners, when they applied to make collective agreements generally binding (Bosch G., 2018).

Governments of all stripes long resisted any statutory intervention in wages policy, as did the social partners, for fear of losing their positions of power in their core business, namely the negotiation of employment and working conditions (Bosch G., 2018). The growing share of low-wage earners made a policy change inevitable. The resistance to an introduction of a statutory minimum wage (SMW) was, however, very strong because of fears of serious job losses which were supported by numerous model estimations provided by German mainstream economists (for example Bachmann, Bauer, and Kluge, 2008; Müller, K.U. and Steiner, V., 2008; Ragnitz, J. and Thum, M., 2007; Knabe, A., Schöb R. and Thum, M., 2014).

Therefore, two governments (2005-2009 and 2009-2013) tried to strengthen the social partners to negotiate industry specific minimum wages (IMW) themselves. The instrument used for this purpose was the *Arbeitnehmerentendegesetz* of 1996 (Posted Workers Act). It was on the basis of this legislation, itself based on the European Posted Workers Directive, that minimum wages for workers posted from other countries had been agreed, primarily in the construction industry. This legislation, introduced in order to protect national collectively agreed rates of pay against international competition, was diverted, so to speak, from its original purpose since 2007 and used as a 'Reformwerkstatt' (reform workshop, Däubler, 2012, p. 508f). It was developed to an instrument for regulating domestic wage competition in certain industries was developed.

The hopes that the parties to collective bargaining would negotiate acceptable IMWs in all low-wage sectors under their own steam were not fulfilled. Only in industries with a long tradition of national collective agreements and close cooperation between the social partners were IMWs agreed. In the sectors with the most low-wage workers, such as retailing, hotels and restaurants and the meat processing industry, unions were too weak, and the employers and their associations were so fragmented that no IMWs ever materialised (Bosch G., 2018).

In 2010, the German labour ministry had eight IMWs evaluated by research teams from different institutes, with the aim of moving the debate to a more objective level. All studies came to the conclusion that the IMWs, some of which were relatively high, had had no negative employment effects (Möller, 2012; Bosch & Weinkopf, 2012). On the basis of this unambiguous new evidence and the dissemination of the recent research on minimum wages from the USA and the UK (summarized in the meta-analysis of Belman and Wolfson, 2014), the Minister of Labour at that time (Ursula von der Leyen) and subsequently the Chancellor Angela Merkel declared being in favour of minimum wages.

Since the IMWs materialised only in dribs and drabs without reducing the share of low-wage workers in the economy as a whole, the demand for a SMW became a key issue in the next general election campaign. The grand coalition between the liberal-conservative party (CDU/CSU) and the social-democratic party (SPD), in place from 2014 to 2018, therefore agreed to introduce a SMW set at EUR 8.50 per hour. The new *Mindestlohnengesetz* of 2014 (Minimum Wage Act, MiLoG) became part of a legislative package bearing its programmatic title: *Tarifautonomiestärkungsgesetz* (Act on the Strengthening of Free Collective Bargaining). In pursuance of the new act, IMWs can now be agreed in all industries. Additionally, collective agreements can now be declared

generally binding if there is a 'public interest' in maintaining 'collectively agreed standards in the event of adverse economic developments' (translation of the author).

### **3 Opportunities and challenges of the implementation of a statutory minimum wage**

#### **3.1 Main characteristics of the new German statutory minimum wage**

The German SMW covers nearly all employees with few exceptions. Not covered are young people below 18 years, apprentices, long-term-unemployed, internships up to three months, internships which are part of a degree programme and subsidized practical training in companies for young people (MiLoG, 2014, Section 22). At the beginning the SMW was set by the government. The goal was to set the level for full-time workers above the maximum limit of the so called *Pfändungsfreigrenze* (threshold for income exempt from seizure execution). In 2015, this limit amounted to EUR 1080 of the monthly net income. With 160 working hours the monthly gross income of a minimum wage earner in 2015 came to EUR 1 377 of which roughly 20 % are to be paid as contributions to the social insurances.

The government set a single rate of the minimum wage mainly to increase the transparency of the rate, to support self-enforcement and to facilitate controls. There was a debate whether the rates should be differentiated between regions (mainly between East and West Germany) or by age. The main argument against a youth specific minimum wage was that a high share of young people is trained in the German dual system of vocational training. Their training allowances are negotiated by the social partners in collective agreements and not determined by the SMW. The social partners were given the possibility to deviate from the SMW of EUR 8.50 with a generally applicable collective agreement for two years (until the end of 2016). In some industries such agreements were signed, particularly to foster a smooth introduction of the SMW in East Germany. All of these deviating collective agreements have now expired.

Every two years, the *Mindestlohnkommission* (Minimum Wage Commission, MWC) submits a proposed increase to the government, which can then prescribe it by statutory order but cannot alter the proposed amount, unlike in the UK. In addition to this, the MWC is expected to evaluate the minimum wage and present a report to the government every two years. An office was set up in order to facilitate this process. Deviating from the UK model (which was discussed as a model for Germany), the three representatives of each side of the social partnership are nominated by their respective organisations and are not selected as individuals by the government. The two academics on the MWC are proposed by the social partners, but they do not have voting rights, unlike in the UK. The government appoints an independent chairman proposed by the social partners (MiLoG, 2014, Chapter 2). The first in 2014 appointed chairman was Jan Zilius, a former human resource director in different companies of the RWE-Group.

The benchmark for any increase in the minimum wage is the average increase in collectively agreed rates of pay, in order to clarify that the pace for increases in the SMW is set via collective bargaining and not by the State (MiLoG, 2014, Section 9(2)). The MWC has further strengthened the use of average increases in collectively agreed wage rates as a benchmark for increases of the SMW. In an unanimously agreed amendment to its standing orders it was decided that a two-thirds majority vote would be required before any deviations from this formula would be permitted. As a result, the minimum wage has been effectively index-linked. In a deep economic crisis, the MWC could, however, decide to deviate from the index or the State could refuse to implement a proposed increase.

To enforce the SMW, the minimum wage law foresees high fines for non-compliance (MiLoG, 2014, Section 21). The general contractors are liable for the minimum wage of their subcontractors (MiLoG, 2014, Section 13). To facilitate controls, designated industries (construction, hotels and restaurants or the meat production) with substantial



and well-known compliance problems must record the daily working hours of their employees and to retain the records for two years. In addition, this regulation also applies to the so-called *mini-jobbers*, who earn less than EUR 450 per month, in all industries.

In contrast to many other countries, the German SMW is not linked with other social benefits. This is not surprising since the SMW was introduced only recently and distinct procedures for adjusting pensions, unemployment benefits as well as other benefits to inflation and wage increases were already in place.

The first increase in the minimum wage to EUR 8.84, which came into force on 1 January 2017, was decided unanimously in June 2016. In 2018, the MWC decided to change to yearly increases (EUR 9.19 as of 1 January 2019 and EUR 9.35 as of 1 January 2020) to cushion the impact of the minimum wage increases.

Recently an increase of the SMW up to EUR 12 was proposed by the German Minister of Finance, Olaf Scholz, and the Minister of Labour, Hubertus Heil. Their main argument was that the level of the SMW was set too low and that there is the need for a living wage. In principle it is possible that the government increases the SMW by law, but it seems that in the near future there is no majority in the parliament which would support such an intervention.

### **3.2 High impact of the SMW on wages, but still high levels of non-compliance**

With a relative value of 50 % of the Kaitz Index, the German SMW of EUR 8.50 is not particularly high compared to other EU Member States. The Kaitz index is an economic indicator represented by the ratio of the nominal legal minimum wage to the average wage in the respective country. However, the 'bite' of the German SMW was considerably stronger than in most other European countries because of the sharp downward extension of the wage spread. Slightly more than 4 million employees (13.4 %) were paid less than EUR 8.50 per hour in 2014 (Mindestlohnkommission, 2015, p. 39, Bosch G., 2018).

Recent research shows that the new SMW led to significant – even double digit - wage increases in the two lowest deciles (Figure 5). The analysis further shows above average wage increases (4.8 %) between 2014 and 2015 for women (6.8 %), marginal part-timers (9.2 %), unskilled employees (7.2 %), employees in companies with five to nine workers (13.4 %) and foreigners (9.3 %). Lower are the effects of the SMW on monthly wages since the working hours were reduced. The data does not show whether the employees or the employers initiated the reduction of the monthly working hours.

In 2016, around 1.8 million people entitled to the minimum wage were still paid less than EUR 8.50 per hour. The share of non-compliance is particularly high in mini-jobs (43.3 %), among temporary employees (19.2 %) and employees without vocational qualifications (15.6 %) and in firms with fewer than five employees (33.3 %) and firms with between five and nine employees (23.6 %) (Burauel et al., 2017, p. 1120). Evidently, even the above average pay rises for some of these groups of workers were not sufficient to take all workers in these groups above the minimum wage threshold. This shows just how far the German wage structure had come unravelled before the introduction of the minimum wage.

Case studies show that most companies now pay at least EUR 8.50 for the contractual working time. However, additional hours worked beyond the contractual working time are often not recorded and not paid, particularly in very small companies without works councils whose employees have little bargaining power. As already noted, *mini-jobbers* also tend to miss out on paid holidays and sick leave.

Furthermore, the number of inspections has declined. The *Finanzkontrolle Schwarzarbeit* (German Customs Authority's Undeclared Work Enforcement Unit), which is responsible for monitoring compliance with the SMW and also the IMWs, inspected 63 000 companies in 2014. That number fell by more than a third to 40 374 in 2015 and has

increased since then to 53 491 in 2018. Recent research reveals substantial internal organizational problems of the *Finanzkontrolle Schwarzarbeit* which led to high levels of turnover of the skilled staff (Bosch, Hüttenhoff and Weinkopf, 2019).

### 3.3 No negative employment effects of the Statutory Minimum Wage

Many German economists predicted that because of the allegedly too high level of Germany's SMW, industries and regions with high shares of low-wage earners would experience substantial job losses. These predictions did not materialize. Figure 6 even indicates that, surprisingly, the employment growth was even higher in industries with an above average share of low-wage earners than that in better earning industries.

Another study analyzed regional employment levels in Germany from 2011 to 2016. It was found that in regions where wages were low, the SMW was introduced without changes to employment levels. In fact, unemployment fell in many areas with relatively lower wages for a period in 2015. The authors 'suggest the steady levels of employment in Germany's low-wage regions mean workers were being underpaid, as organizational revenues were transferred to workers rather than being retained by their employers through redundancies that would reduce their overall wage bill' (Ahlfeldt, Roth and Seidel, 2018).

The MWC – in their evaluation – also found a compositional impact on employment. In low-wage industries as well as in non-low-wage industries, total employment and the employment of socially insured employees increased while the number of marginal part-time employees (mini-jobbers with a maximum of monthly earnings of EUR 450) decreased (Mindestlohnkommission, 2018, p. 89). It seems that some employers found mini-jobs less attractive after the introduction of the SMW because (1) the minimum wage law requires stricter documentation of the daily working hours of mini-jobbers due to the high levels of non-compliance in this form of work and (2) the implicit limit on hours makes mini-jobs less flexible. With the actual minimum wage of EUR 9.19, the maximum monthly working hours of a *mini-jobber* is 49 hours per month.

### 3.4 Positive impact on collective agreements

When the SMW of EUR 8.50 was introduced, it had a large effect on collective agreements. In the years before 2015, a substantial share of 10 to 15 % of wage earners covered by collective agreements was below that threshold (Figure 7). Trade unions coordinated their collective bargaining across industries and did not sign agreements with wage groups below EUR 8.50 anymore.

When the SMW was implemented in January 2015, there were still around 6 per cent of the collectively agreed wage groups below the threshold of EUR 8.50. They were mostly found in older agreements which had already expired for years and were only valid through the so-called legal *Nachwirkung* (after-effect). In Germany collective agreements do not expire unless they are replaced by a new agreement. In addition to that, a few sectors such as agriculture or the meat industry, used the possibility provided by the *Mindestlohngesetz* (German Minimum Wage Law) (MiLoG, 2014)) to conclude wages below the SMW for a transitional period up to the end of 2016. After 2015, the share of wage groups below EUR 8.50 decreased further down to one percent, which was almost exclusively due to older and expired agreements.

The increases of the SMW triggered collective bargaining. With the first increase of the SMW to EUR 8.84 in January 2017, 5.5 % of all wage groups dropped below the minimum wage level again and the social partners adjusted the collective agreements to the new level of the SMW (Figure 7). The same happened in January 2019, when the second increase of the minimum wage to EUR 9.19 was implemented.

The SMW did not crowd out the IMWs. On the contrary, in 2018, a higher number of industries than in 2009 agreed on an IMW. With basic rates above the SMW, these industries want to be attractive in the labour market. Some industries set a second higher IMW for skilled employees to retain these employees in their industry and to make apprenticeships in the industry attractive. Such ripple effects (Grimshaw and

Bosch, 2010) are also found in some industries without IMW in which the level of the lowest wage group is above the level of the SMW.

#### **4 Questions**

- Why should the starting national minimum wage be EUR 870? Is this wage rate sufficient to bring a single earner above the poverty threshold?
- Can a minimum wage with a single rate for the whole country and all occupations strengthen the self-enforcement of the minimum wage and facilitate the controls by the labour inspectorate?
- Multiple minimum wages are common in many countries. In FR, BE and NL most collective agreements are declared as generally binding which means that, beside the national minimum wage, there exists industry minima. In DE, the national minimum wage is complemented by industry specific minimum wages. Are not multiple minimum wages feasible in Cyprus?
- What should be the role of the social partners and the State in deciding increases in the future national minimum wage?
- Should not there be a minimum wage commission set up, like in the UK or in Germany, which proposes increases of the minimum wage and also evaluates its impact?

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## Annex 1 Summary table

The main points covered by the paper are summarised below.

### Situation in the peer country

- After an exceptionally long boom phase between 2009 and 2018, the German economy is currently experiencing a cooldown.
- Employment has grown from 2009-2018 by nearly 4 million and is expected to grow by 476 000 persons in 2019.
- In 2018, the unemployment rate in Germany reached a new low since re-unification between the East and the West in 1990, with just 5.2 %.
- Due to declining importance of collective bargaining in many of the fast-growing service industries, the share of low-wage workers increased to a level far above the EU average.
- Particularly concerning is that low-wage jobs serve less as steppingstones to better-paid jobs than in the past.

### Opportunities and challenges of the introduction/ implementation of a statutory minimum wage

- The new German minimum wage covers nearly all employees with few exceptions.
- The training allowances of apprentices are negotiated by the social partners and not determined by the minimum wage to protect the dual system of vocational training and keep youth unemployment low.
- The government set a single rate of the minimum wage mainly because this increases the transparency of the rate, supports the self-enforcement and facilitates the controls.
- Every two years, the Minimum Wage Commission submits a proposed increase to the government, which can then implement it by statutory order but cannot alter the proposed amount.
- The benchmark for any increase in the minimum wage is the average increase in collectively agreed rates of pay. As a result, the minimum wage has been virtually index-linked.
- The minimum wage did not have dis-employment effects. Research even indicates that surprisingly the employment growth in industries with above the average shares of low-wage earners was even higher than in the better wage industries.
- Recent research shows that the minimum wage led to significant – even double digit - wage increases in the two lowest deciles of the income distribution.
- There are still high compliance problems especially in micro-firms and the remuneration of temp agency workers and *mini-jobbers*.
- The number of inspections has declined by the third after the introduction of the minimum wage but are recently increasing.
- The minimum wage had a positive impact on collective bargaining and the negotiation of industry specific minimum wages.

### Questions

- Why should the starting national minimum wage be EUR 870? Is this wage rate sufficient to bring a single earner above the poverty threshold?

- Can a minimum wage with a single rate for the whole country and all occupations strengthen the self-enforcement of the minimum wage and facilitate the controls by the labour inspectorate?
- Are not multiple minimum wages feasible in Cyprus?
- What should be the role of the social partners and the State in deciding increases in the future national minimum wage?
- Should not there be a minimum wage commission set up, like in the UK or in Germany, which proposes increases of the minimum wage and also evaluates its impact?

## Annex 2 Example of relevant practice

Name of the practice:	Statutory Minimum Wage
Year of implementation:	1 January 2015
Coordinating authority:	Ministry of Labour
Objectives:	<ul style="list-style-type: none"> <li>• Improvement of working condition</li> <li>• Creation of a level playing field for employers</li> <li>• Strengthening social partnership</li> </ul>
Main activities:	<ul style="list-style-type: none"> <li>• Introduction of a statutory minimum wage of EUR 8.50</li> <li>• High coverage of the statutory minimum wage (only young people under 18 years and long-term unemployment for the first six months of their re-employment are excluded)</li> <li>• High fines for non-compliance and liability of the general contractor for the statutory minimum wage of their subcontractors</li> <li>• Deviations for two years possible only by generally applicable collective agreements</li> <li>• Much stronger role of the social partners in the Minimum Wage Commission than in the UK</li> <li>• Facilitating the extension of collective agreements if there is a 'public interest' in the extension</li> <li>• Possibilities for higher industry specific wages</li> </ul>
Results so far:	<ul style="list-style-type: none"> <li>• High wage increases for the lower two deciles in the income distribution, also for women, foreigners and employees in SMEs</li> <li>• No negative employment effects</li> <li>• Acceptance of the statutory minimum wage by the employers</li> <li>• Positive impact on collective bargaining</li> <li>• Deterrence effect of fines and liability in bigger companies</li> <li>• Still compliance problems especially in mini-firms and for mini-jobs</li> </ul>



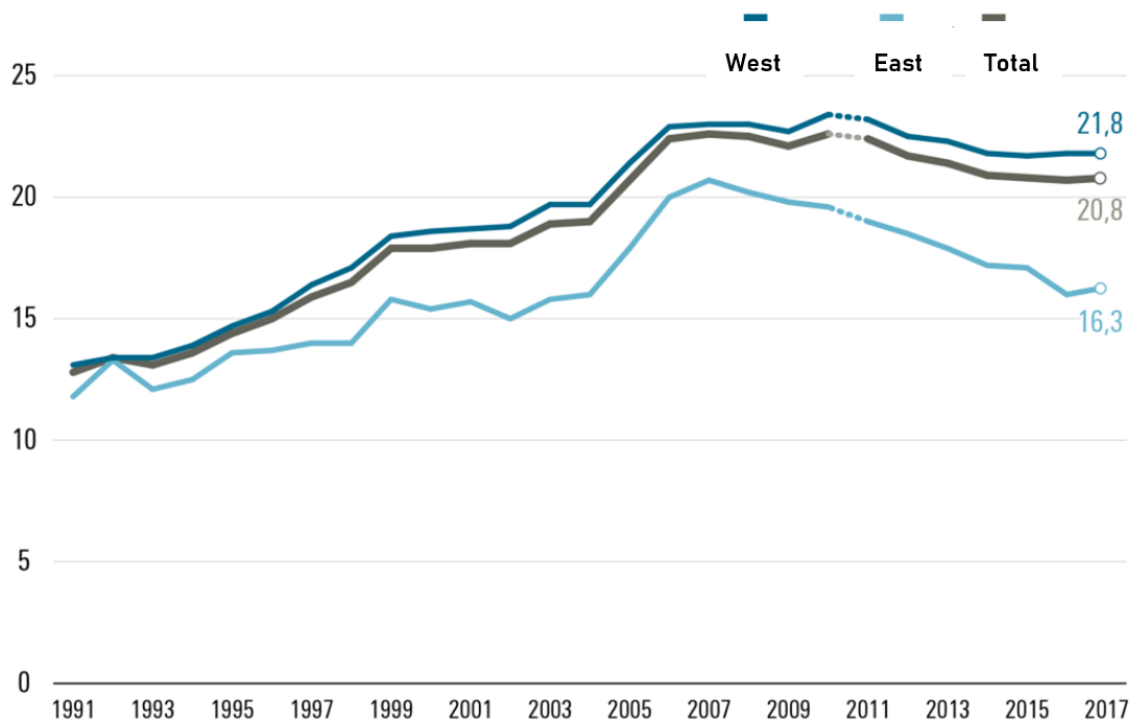
### Annex 3 Data annex

Table 1. Key economic indicators for Germany 2017-2020 (in %, unless otherwise indicated)

	2017	2018	2019	2020
Gross domestic product (GDP), price-adjusted	2.2	1.4	0.6	1.6
Gross domestic product, deflator	1.5	1.9	2.2	2.0
Consumer prices	1.5	1.7	1.4	1.6
Labor productivity (per hour worked)	0.9	-0.0	-0.4	0.7
Employment (1000 persons)	44 269	44 841	45 314	45 607
Unemployment rate	5.7	5.2	4.9	4.8
<i>in relation to nominal GDP</i>				
Public sector net lending	1.0	1.7	1.3	0.9
Gross public debt	63.9	59.9	56.8	54.3
Current account balance	8.0	7.3	7.2	7.0

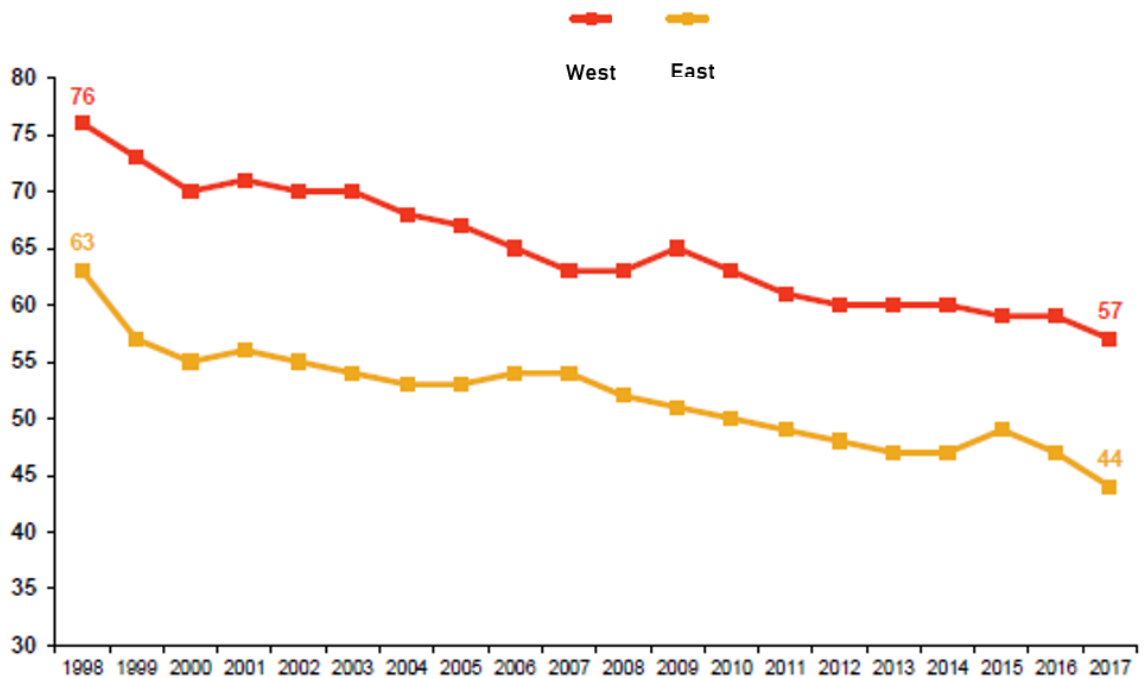
Source: IfW forecast Kiel (<https://www.ifw-kiel.de/topics/economic-outlook/>) accessed 2 August 2019.

Figure 1. Share of atypical employees 1990-2017



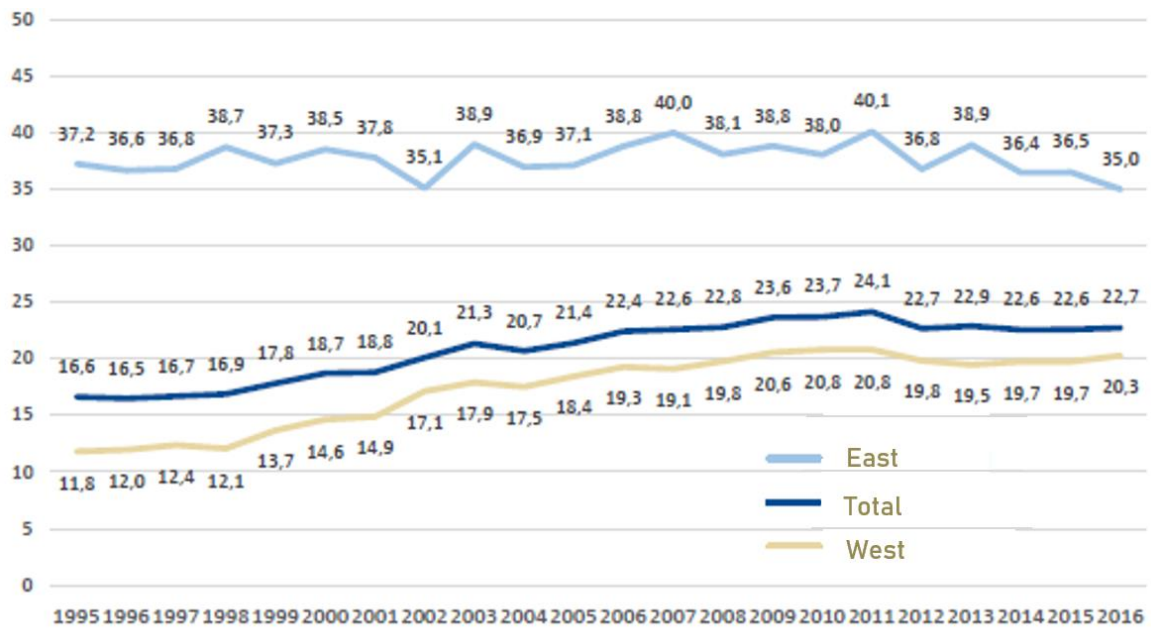
Source: Seils and Baumann, 2019

Figure 2. Coverage by collective agreements 1998-2017 (in % of all employees)



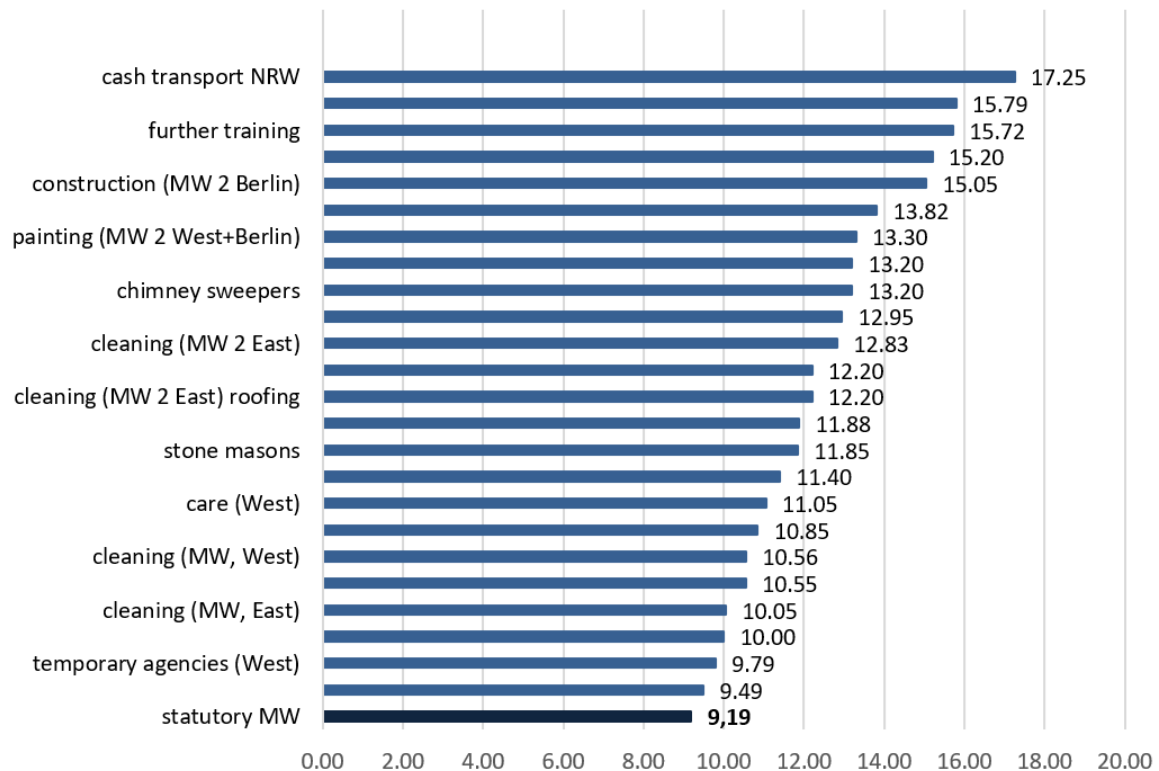
Source: WSI-Tarifarchiv 2019

Figure 3. Share of low-wage earners in Germany 1995-2016 (in % of all employees)



Source: Kalina and Weinkopf, 2018 (SOEP v33.1)

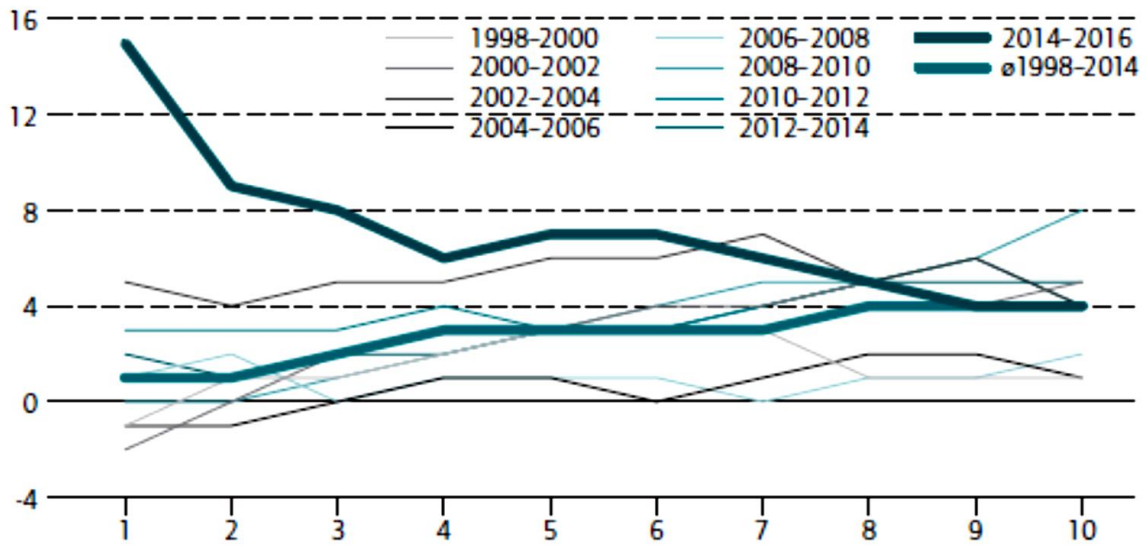
Figure 4. Industry minimum wages and the national minimum wage in EUR per hour (August 2019)



MW 1: Minimum wage for unskilled employees, MW 2 = Minimum wage for skilled employees

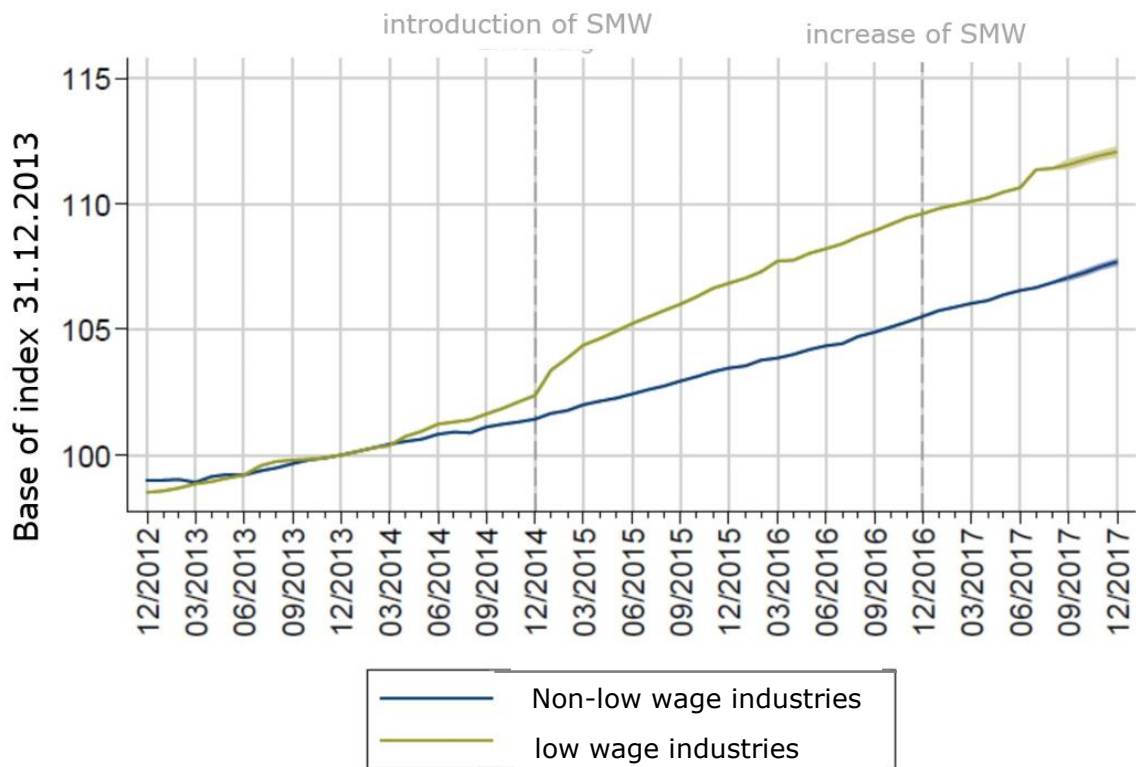
Source: Compiled by the author.

Figure 5. Nominal growth in contractual hourly pay over two years by deciles, Germany, 1998-2014



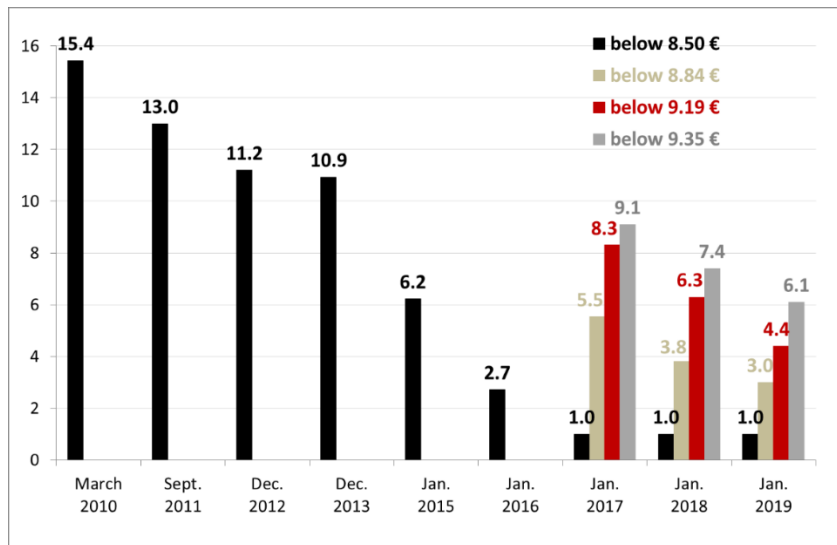
Source: Burauel et al., 2017: 1110.

Figure 6. Employment growth in low-wage and non-low-wage industries 2012-2017  
 seasonal adjusted



Source: vom Berge et al., 2018 p.44

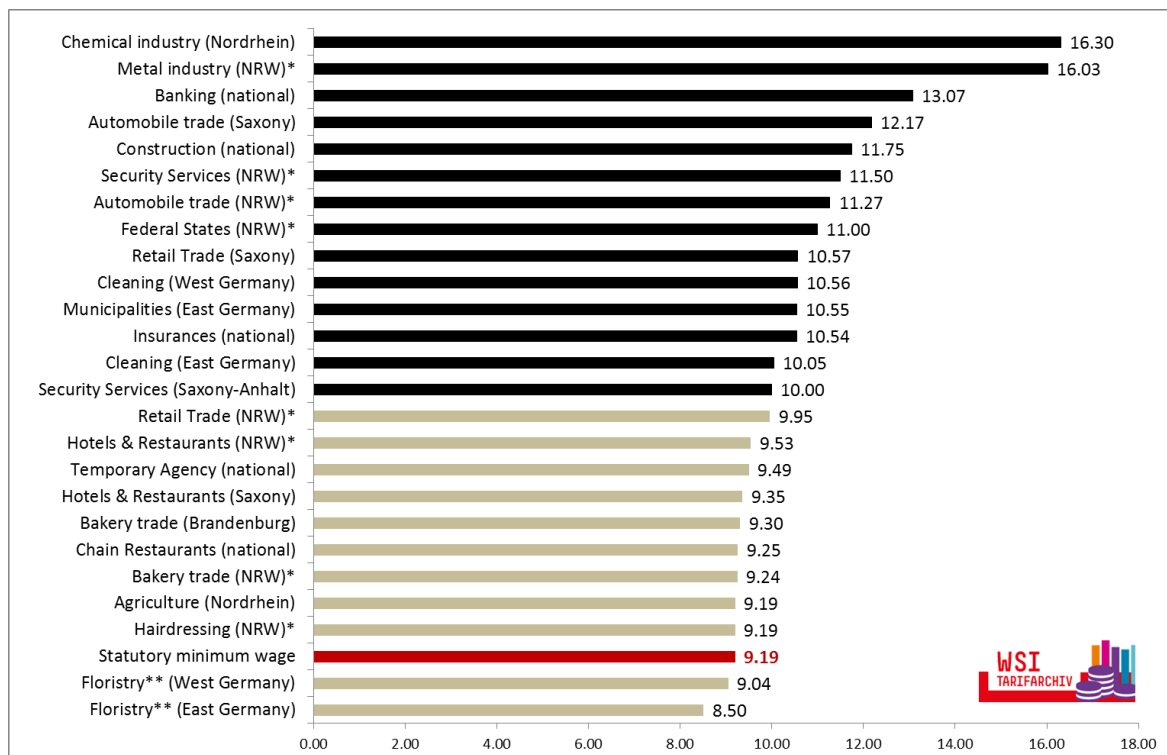
Figure 7. Wage groups in collective agreements below the threshold of the statutory minimum wage in %\*



\* on the basis of around 4 500 collectively agreed wage groups in 40 sectors; including expired agreements which are valid only due to the *Nachwirkung* (after-effect) of old agreements. In Germany collective agreements do not expire unless they are replaced by a new agreement.

Source: Schulten, T. and WSI-Tarifarchiv, 2019

Figure 8. Lowest wage groups in selected German collective agreements in EUR per hour, on 1 January 2019



\* NRW = North Rhine-Westphalia

\*\* Floristry: Agreement in West Germany expired on 31 December 2018 agreement in East Germany expired on 31 December 2016

Source: Schulten, T. and WSI-Tarifarchiv, 2019

