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The curious incident of low wages growth

Wages and Policy in the 21st Century

Report No. 1

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Carmichael Centre at the Centre for Future Work

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About the Carmichael Centre

The Carmichael Centre, a project of the Centre for Future Work at The Australia Institute, is named in honour of Laurie Carmichael, the legendary manufacturing unionist who passed away in 2018 at the age of 93.

The Carmichael Centre conducts and published research on themes related to Carmichael's legacy, including:

- industrial relations;
- social policy;
- manufacturing and industry policy;
- vocational education; and
- international labour solidarity.

The Centre sponsors an annual Laurie Carmichael lecture, with a prominent labour or progressive personality speaking on Carmichael's legacy.

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Wages and Policy in the 21st Century: A new series from the Carmichael Centre

This series of reports investigates the paradox of low wages in relatively tight labour markets. It looks at the long-run forces behind the historically peculiar combination of low unemployment existing alongside falling real wages, and covers matters such as declining union and bargaining coverage, and vacancies and mobility in monopsonistic labour markets, using data from the Australian Bureau of Statistics (ABS) and other sources.

It explains the theory and empirics of this, but also includes some boxed case studies to illustrate points along the way. To the surprise of few actors in wage determination, this series will show that the missing ingredient in the classical models of labour markets is the failure to account for power. It draws from insights in labour economics (including theories of monopsony) and industrial relations to show how power needs to be, and can be, incorporated into the analysis of wages and labour markets. It concludes with some possible explanations as to why workers' power has declined, and whether and how this can be remedied.

This report is on low wages growth and power in contemporary labour markets. It is planned that other reports in the series will encompass the following issues:

- monopsony and structural power in wages
- wage norms and wages growth
- vacancies, unemployment and wages
- forms of power and wages
- normalisation of low wage growth

Contents

Summary 6
Introduction 9
Some curious incidents 10
Some policy failures in the 21st century 13
Thinking about labour markets 17
International thinking and rethinking about labour markets 17
What had been the perfectly competitive ideal of labour markets? 19
A realistic perspective on wages 22
Inherent barriers to competition 22
Gender, ethnicity and wages 23
Wage stickiness 24
Power, wages and norms 26
Employer discretion over wage rates 26
Power effects on wage rates 27
The nature of wage norms 29
How has power been influenced over time? 32
Economic and labour market factors and power 32
Public policy and power 34
The effects on wages after a change in policy 38
Evidence from indexes of wage rates 38
Evidence from enterprise agreements 39
Evidence from the national accounts 40
Are gains restricted to union members? 41
Conclusions: power, markets and wages 43

Glossary

Term	Definition
Associational power	Achieving power through joining together with other players to boost your relative importance
Collective bargaining	A group of individuals (usually workers) join into a collective (usually a union) to bargain with an organisation (usually an employer)
Discretion	The power to decide
Downward sloping	As price increases, quantity decreases
Equilibrium	A stable situation in which there is no pressure for either wages or employment to increase or decrease
Heterodox	Not orthodox (i.e. not mainstream)
Institutional power	Power achieved through having rules, procedures or norms that affect power
Labour demand	How many workers are sought by employers (or how many hours of work they seek)
Labour supply	How many workers offer their labour (or how many hours of work they offer)
Market-clearing	A situation occurs in which there is no unmet demand and no unfulfilled supply. At the equilibrium wage, all employers have the labour they want, and no worker is unemployed.
Market power	Power achieved through there being high demand, or low alternative supply, of the services one can supply
Monopsony	A situation in which there is only one or a small number of buyers of labour (employers).
Multi-employer bargaining	Collective bargaining with more than one employer, such that more than one employer will be covered by the agreement
NAIRU	Non-accelerating rate of unemployment: the unemployment rate below which, its adherents believe, inflation will accelerate.
Perfect competition	A situation in which a market has a large number of competitors selling products and a large number of buyers, with perfect information and mobility, such that there are no price makers, only price takers,
Price maker	A party that determines the price for a factor of production (the wage, when the factor of production is labour)
Price taker	A party that cannot influence the price (or wage). The price is instead determined by the market (or the other party)
Structural power	Power achieved through occupying strategic locations for which there are few if any alternatives, thereby making it inherently easier to achieve objectives
Union density	The number of union members divided by the number of people eligible to be union members (usually, the number of employees)
Upward sloping	As price increases, quantity increases
Wage norm	A view common to a group of employers regarding the appropriate wage to pay workers

Summary

After a period of real wage declines during the rapid inflation of the early 2020s, real wages in December 2024 were at the same level as December 2011. In that period, labour productivity (measured by gross value added per hour worked in the market sector) had risen by 15.1%. In other words, none of the gains in labour productivity between 2011 and 2024 went to workers.

The vast majority of wage gains by workers had always been due to factors other than workplace productivity growth — that is, the relative bargaining strengths of the workers and employers.

Many observers appeared to expect the wage spiral of the 1970s would be repeated in 2022-23. This did not happen. There were many fundamental differences between the inflation of the 1970s and the inflation of the 2020s.

There were problems in predicting wages growth and in the conduct of monetary policy after the pandemic. Policymakers misunderstood inflation in the 2020s by focusing on wages, not profits, and failed to adequately incorporate concepts of power, including labour market monopsony, into their understanding of how labour markets work.

Thinking about labour markets

Questioning of the perfect competition model gained impetus with the global financial crisis of 2008. By 2018 the OECD shifted to support multi-employer bargaining. Neoclassical ideas have not suddenly been totally abandoned, but by the 2020s bodies such as the European Central Bank had joined the OECD and IMF in raising questions about the orthodoxy.

While traditional economics has something to offer, it does not tell us how *all* forces affecting labour markets work. In the perfect competition model, firms do not have a choice as to what wage they pay. Full employment is always achieved, unless unions or government interfere. It assumes a large number of buyers and sellers of labour.

Fundamentally, the assumptions behind the model are wrong. Employers have discretion in setting wage offers, and employees can influence wage rates through collective bargaining or political influence. Employers rarely adjust pay in response to skills shortages. They may be able to maximise their profits at a lower wage than any ‘market-clearing’ wage.

Power and wages

Firms’ power to choose a wage may arise from monopsony (there being only one or a small number of buyers of labour). But employer power may also arise from limitations in the collective organisation of labour — including unionisation, bargaining and industrial action.

Power may take many forms. One key aspect of power is the role of wage norms, that may be influenced by several factors related to power. These include: reference points set by institutions such as tribunals; pressure from employer organisations or government agencies; the operation of product markets; employer actions within labour markets; wage stickiness; macroeconomic circumstances; and collective organisation amongst employees and their ability to engage in collective bargaining and action.

How has power been influenced over time?

Analysis of influences on wages suggests there has been a trend decline in worker power and hence in workers' ability to offset employers' power where it is exercised. To understand how low wages growth has been normalised, despite low unemployment, we can consider the various ways that power has been affected, both by changes in the economy and in public policy.

Examination of 16 factors that influence or indicate power in the labour market shows almost all economic and labour market trends in the past half century have reduced workers' power. The only major determinant, that for some time went in the opposite direction, has been a tightening labour market.

Public policy is a key influence on power. Over the first portion of the past decade up until 2022, most major public policy initiatives acted to reduce workers' power, while a number of minor actions increased workers' power. From 2022, by contrast, almost all new federal legislation increased workers' power.

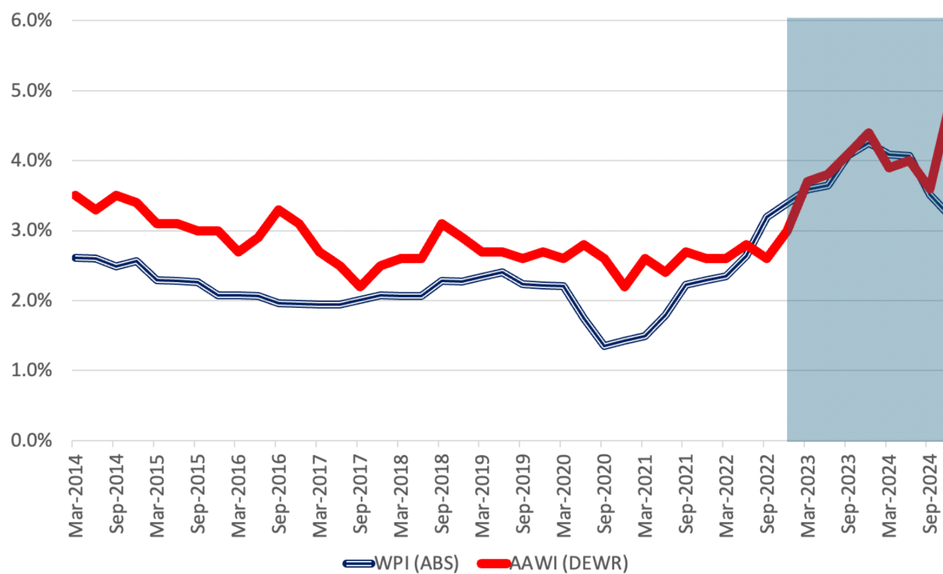
The effects on wages after a change in policy

The policy shift from 2022 appeared to have an impact on wages growth, even though some laws only passed in 2024 and so have not yet had time to influence outcomes. *Nominal* wages grew at a little over 2% per year through most of the period from 2014, falling then recovering in the pandemic. After September 2022, nominal wages grew more quickly, to over 4% per annum through 2023-24. *Real* wages typically grew by between 0 and 1% a year through to 2019, then after a brief increase fell substantially to the end of 2022. There was a recovery in real wages growth after then, through 2024.

Average annualised wage increases (AAWI) under all new enterprise agreements gradually declined from around 3.5% per annum in 2014 to close to 2.5% by 2022. However, in the two years after that, AAWI peaked at 4.8%, and in every quarter after December 2022 it was higher than in every quarter between 2014 and 2022 (Figure 1).

National accounts data on the wages and profit shares of factor incomes show a pattern that is broadly consistent with those shown in the WPI and AAWI series. In March 2014 the wages share was 53.0% of factor income, but by December 2022 it had fallen to just 50.3%. Over the period to December 2024, it rose back to 53.8% of factor income.

Figure 1: Average annualised wage increases (AAWI) under new quantifiable enterprise agreements and the Wage Price Index (WPI).



This refutes any idea that the recent growth in wages is simply a response to a temporary surge in inflation. The increase in wages growth reflects a genuine, recent change in the balance of power, favouring workers and facilitating wages growth. It has occurred in a period when inflation has been falling — from over 7% at the end of 2022, to below 3% at the end of 2024. A shift in power towards workers has led to higher nominal and positive real wages growth and an increasing share of wages in national income, yet it also accompanied a decline in inflation.

The wage gains associated with increased worker power are experienced by union members and non-members. But it is likely the latter do not experience as large an increase as union members.

Conclusions: power, markets and wages

Over the past half century there has been an unambiguous reduction in workers' power. Unlike in the 1970s, workers simply do not have the bargaining power to prevent real wage declines during periods of rapidly rising prices. Nor, consequently, do they play any role in intensifying or sustaining inflationary pressures. In short:

- Australian workers can no longer extract the wage increases that they previously could from wage negotiations, and do not contribute to inflation.
- Influences on power have combined to normalise low wages growth, for both union and non-union workers, even in tight labour markets.
- The one countervailing force in recent times has been public policy which, since 2022, has led to some increases in workers' power.

Introduction

I like to imagine that, if Arthur Conan Doyle were still alive, and had turned his creation, Sherlock Holmes, to solving the economic mysteries of the 21st Century, he would have written this conversation:

> Economist: "Is there any other point to which you would wish to draw my attention?"
> Holmes: "To the curious incident of the wages explosion."
> Economist: "There was no wages explosion."
> Holmes: "That was the curious incident."

This is, of course, a parody of a famous conversation in Conan Doyle's *Silver Blaze,* in which Holmes solves the mystery of a horse's disappearance (and worse) by noting that a guard dog that should have barked when a stranger stole the horse, did not, in fact, bark.[1]

This short story aims to solve the mystery of the Australian labour market in contemporary times.

Until recently, Australia had its tightest labour market for half a century. Firms were screaming for workers. Unemployment was at its lowest since the early 1970s. In earlier times, such circumstances would have seen wages growing rapidly as workers reaped the long-awaited gains from that tight labour market. Low unemployment gave workers lots of options and employers few, so workers had the chance to bargain wages upwards.

Yet this time, the reverse happened. Wages growth was ordinary at best. For a few years we even saw real wages (that is, the value of wages after you adjust for price rises) go down. The wages dog did not bark. It barely whimpered.

To many, the state of affairs represented a new normal in the modern economy. How could that have happened. *Why are low wages normalised even in tight labour markets?*

This report commences that investigation, by interrogating power and low wages in labour markets. It focuses on:

- some policy failures of recent decades;
- the theoretical underpinnings of labour market policy, and how modern thinking has changed on this, rendering the preceding foundations obsolete;

[1] Arthur Conan Doyle (1894) 'The Adventure of Silver Blaze', in *The Memoirs of Sherlock Holmes*, George Newnes, London. The original conversation began with Inspector Gregory, a Scotland Yard detective, asking:
"Is there any other point to which you would wish to draw my attention?"
"To the curious incident of the dog in the night-time."
"The dog did nothing in the night-time."
"That was the curious incident."

- building a more appropriate understanding of how labour markets operate, taking account of what is actually happening in the economy;
- accounting for the importance of power in understanding wage outcomes, and the discretion employers have in setting wages within the bounds set by wage norms and market circumstances; and
- how developments in the economy and in public policy have influenced wage outcomes and, until recently, normalised low wages growth.

SOME CURIOUS INCIDENTS

The traditional economic texts and models showed us that tight labour markets are reflected in higher wages growth, either in nominal terms (without adjusting for price inflation) or in real terms (after adjusting for price inflation), or both. Yet low wages growth has seemingly become normalised. While real wages rose slightly during early 2024, they barely came to a level equivalent to real wage maintenance, with no small part played by the fact that inflation had fallen substantially.

After a period of real wage declines during the rapid inflation of the early 2020s, real wages in December 2024 were at the same level as December 2011. In that period, labour productivity (measured by gross value added per hour worked market sector) had risen by 15.1%. In other words, none of the gains in labour productivity between 2011 and 2024 went to workers. While Treasury analysis had suggested that the pass-through of productivity increases into wages had fallen by 10-20% between 2001/02 and 2014/15,[2] this suggests that, on average over the period, it had disappeared altogether. That said, the Treasury analysis interestingly suggested that, at the workplace level, only 10% of productivity gains were typically passed on to workers anyway,[3] even though *on average* Treasury believed national data suggested a 1:1 relationship between productivity growth and wages growth.[4] So, as it was, the vast majority of wage gains by workers had always been due to factors other than workplace productivity growth — that is, the relative bargaining strengths of the workers and employers.

The inflation spiral of the early 1970s had been the last occasion Australia had a labour market as tight as in the early 2020s. However, that inflation spiral was not repeated during the most recent (post-pandemic) inflationary cycle. In fact, aside from inflation itself, it would be hard to find two periods with such different economic outcomes. Yet many observers appeared to expect that the same relationship, between inflation and the labour market, would hold this time as had held half a century ago. The Reserve Bank of Australia (RBA) acted as if they believed this. They spoke repeatedly of a 'non-inflation accelerating rate of unemployment' (NAIRU) and the need to not have the labour market operating tighter than this, as if that is what would lead to an acceleration of inflation. Successive increases in interest rates partly reflected concerns which were clearly misguided. RBA

[2] Dan Andrews, Nathan Deutscher, Jonathan Hambur and David Hansell (2019) Wage Growth in Australia: Lessons from Longitudinal Microdata, Working Paper 2019-04, Treasury, pp7-10.
[3] 'An unexpected 10% increase in firm productivity leads to a 1% increase in worker wages'. Ibid, p7.
[4] Ibid, p9 and footnote 8. This was consistent with earlier studies, including in other jurisdictions.

interest rate increases later brought to an end the record low unemployment that existed as recently as 2023.

To illustrate the way in which the inflation spiral of the 1970s was not repeated in 2022-23, Box A, below, provides more detail about the similarities and critical differences between the inflation of 1973-74 and that of 2022-23. Low wage growth has been a problem in most industrialised countries in recent years, but from 2013 through 2020 Australia's nominal wage growth was well below the average in the Organisation for Economic Cooperation and Development (OECD), and its real wage growth was less than one-third the OECD average.[5]

[5] Jim Stanford, Fiona Macdonald, and Lily Raynes (2022) Collective Bargaining and Wage Growth in Australia, Centre for Future Work, Canberra, Table 2.

Box A: The inflation surges of the 1970s and the 2020s

Many observers appeared to expect the wage-wage spiral of the 1970s, that began on the last occasion Australia had a labour market as tight as recently, would be repeated in 2022-23. This did not happen. The world of work had changed a lot in the intervening half century.

Union membership had fallen from one half of the Australian workforce in the 1970s to one seventh in the 2020s. In 1974, 6.3 million working days were lost through industrial action. In 2021, it was just 0.1 million working days lost. In 1974-75, real wages *grew* by 10%. Real wages *fell* by more than 3% over 2021-22.

During the inflationary year to June quarter 1974, the profit share went *down* by 4.5 percentage points, and the wages share went up by 2.8 points. During the inflationary year to June 2022, the profit share went *up* by 3.3 percentage points, and the wages share down by 2.5 points.

There were fundamental differences in the causes of inflation in the 1970s and the 2020s. In the 1970s, rising international commodity prices, exaggerated in Australia by the deliberate undervaluation of the Australian dollar, and then the OPEC oil embargo, led to rising prices in Australia. Through union action, workers were able to extract real wage increases out of employers in key sectors, and flow those elsewhere. Unions in different sectors had different views on what relativities between them and other sectors should be. Some unions sought to 'leapfrog' each other, to become the pay pacesetter.[6] The window for this action only lasted briefly. Changes to the wage system made it harder for unions to leapfrog others' wage gains, and eventually saw lower increases awarded to workers, leading to lower growth in labour costs. Higher interest rates and government spending cuts reduced workers' bargaining power. Inflation fell.

In the 2020s, rising commodity prices, driven by pandemic, war and energy shortages, again played a key role at the beginning of the inflationary cycle. This time, though, unions lacked the power to even keep up with prices, let alone leapfrog each other. The changes to wage fixing laws and practice in the 1990s, which made award wages a 'safety net' and shifted determination of wages and conditions to 'enterprise bargaining', put an end to such possibilities being repeated. So even if some powerful unions could achieve high increases through negotiation, there is now no mechanism for such increases to be transmitted elsewhere. As it was, though, the decline in union density and collective bargaining, and the changes in legislative framework, made the negotiation of high wage increases by even the most powerful unions unlikely. Instead, there was strong evidence that Australia, like many other countries, was experiencing "seller's" or "profit-led" inflation.[7]

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[6] Steps summarised in E G Whitlam (1985) *The Whitlam Government 1972-1975*, Viking.

[7] Jim Stanford et al. (2023) Profit-Price Inflation: Theory, International Evidence, and Policy Implications Centre for Future Work, Canberra; Organisation for Economic Cooperation and Development (2023) *Economic Outlook*, 113, No 1, OECD, Paris, pp 26-31; ; European Commission (2023), European Economic Forecast Spring 2023, Institutional Paper 200, Directorate-General for Economic and Financial Affairs, Brussels; Isabella M. Weber and Evan Wasner (2023), Sellers' inflation, profits and conflict: why can large firms hike prices in an emergency?, *Review of Keynesian Economics*, 11(2), Summer, pp. 183–213; Niels-Jakob Hansen, Frederik

SOME POLICY FAILURES IN THE 21ST CENTURY

The labour market has changed since the 1970s, but policy-makers' understandings of how labour markets work have not kept up with those changes. Some public policies have been seriously misguided by this shortfall in understanding.

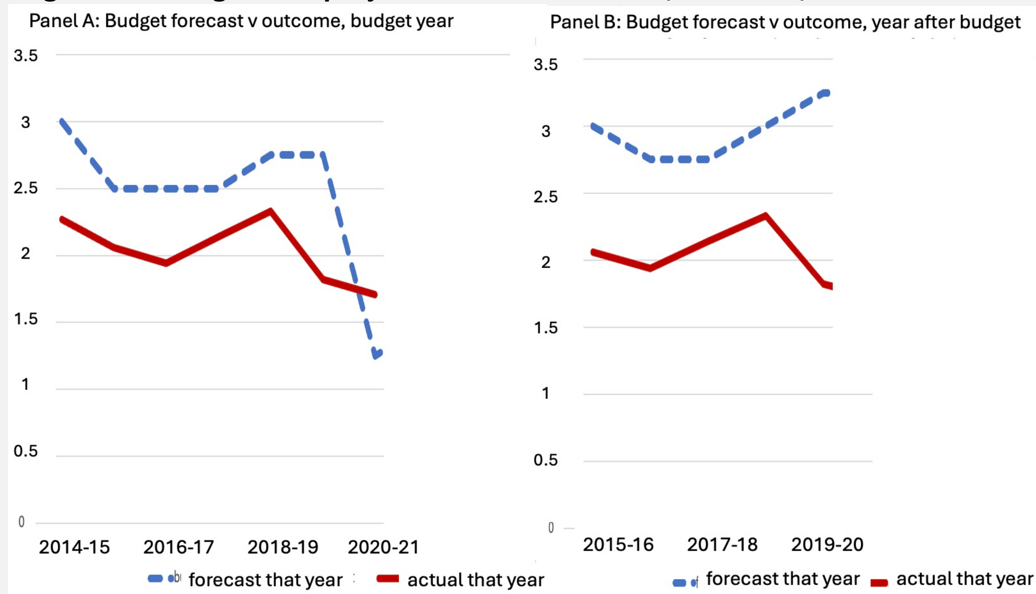
One example is the inability of the Reserve Bank of Australia, through several years preceding the COVID-19 pandemic, to predict the rate of wages growth. As shown in **Box B**, the RBA over-estimated prospective wages growth for six consecutive years, by between 0.5 and 1.0 percentage points (for the 12 months ahead) or more (for the 24 months ahead). These were not trivial shortfalls.

Toscani, and Jing Zhou (2023), Euro Area Inflation after the Pandemic and Energy Shock: Import Prices, Profits and Wages, IMF Working Paper WP/23/131, Washington DC, June; Giuseppe Mastromatteo & Sergio Rossi (2024) 'Sellers' Inflation' and Monetary Policy Interventions: A Critical Analysis, *Review of Political Economy*, 36:4, 1465-1485, DOI: 10.1080/09538259.2024.2354334; Servaas Storm (2023), "Profit inflation is real", *PSL Quarterly Review*, 76 (306):243-259; Paul Donovan, 'What is profit-led inflation?', *UBS Chief Economist's Comment*, 16 March 2023, http://joseluisoreiro.com.br/site/link/332ed4a1c501e1d8970217df6e74fc78101f27a3.pdf ; Michalis Nikiforos, Simon Grothe and Jan David Weber (2024), 'Markups, profit shares, and cost-push-profit-led inflation', *Industrial and Corporate Change,* 33, 342–362 DOI: https://doi.org/10.1093/icc/dtae003; Cucignatto G., Garbellini N., Fora-Alcalde F. (2023), "Profit-led or cost-led inflation? Propagation effects through the EU inter-industry network", *PSL Quarterly Review*, 76 (306):261-276, https://doi.org/10.13133/2037-3643/18215; Claudia Sahm (2023), 'Price-price spirals take us for a spin', Stay-at-home Macro (SAHM), 16 May, https://stayathomemacro.substack.com/p/price-price-spirals-take-us-for-a

Box B: Official failure to predict low wages growth

A persistent issue that governments faced through the 2010s was the failure of the system to generate expected wages growth. Linked to this has been an inability to accurately forecast wages growth and indeed a persistent tendency to over-estimate it. For example, in Australia (as shown in Figure B1), most of the federal Budgets between 2014-15 and the onset of the COVID-19 pandemic overestimated future nominal wages growth, in both the budget year (Panel A) and the year beyond (Panel B). It seemed difficult to accurately model changes in labour market behaviour in the context of changes in wage norms and monopsony, discussed below.

Figure B1: Budget WPI projections and outcomes, Australia, 2014-2020



Source: Budgets. ABS WPI.

It was not a problem restricted to Australia. For example, writing about the British Office of Budget Responsibility's forecasts of earnings growth, Blanchflower and Machin described how 'over time, each forecast has been downgraded from the previous forecast, which then proves to be overly optimistic and is downgraded again at the next forecast'.[8] In 2018, US Federal Reserve Board chair, Jerome Powell[9], described how he 'would have expected that wages would move up a little bit more,' and a former European Central Bank Executive Board member referred to employee compensation growth that had 'remained stubbornly low' despite a tightening labour market.[10] Central bank and government forecasters do not rely solely on economic models. They make subjective adjustments to account for where they think they models might be wrong. Yet still they could not work out what was happening.

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[8] D. Blanchflower and S. Machin (2014). Falling real wages, *CentrePiece*, Spring, 19-21.

[9] J. Powell (2018). 'Interview by Kai Ryssdal, Marketplace'. 12 July. Transcript at https://www.marketplace.org/2018/07/12/economy/powell-transcript/

[10] B. Cœuré (2017). 'Scars or scratches? Hysteresis in the euro area', Speech at the International Center for Monetary and Banking Studies, Geneva, 19 May. https://www.ecb.europa.eu/press/key/date/2017/html/ecb.sp170519.en.html cited in E. Frohm (2021) 'Labour shortages and wage growth'. Working Paper 2576, European Central Bank, Frankfurt, July.

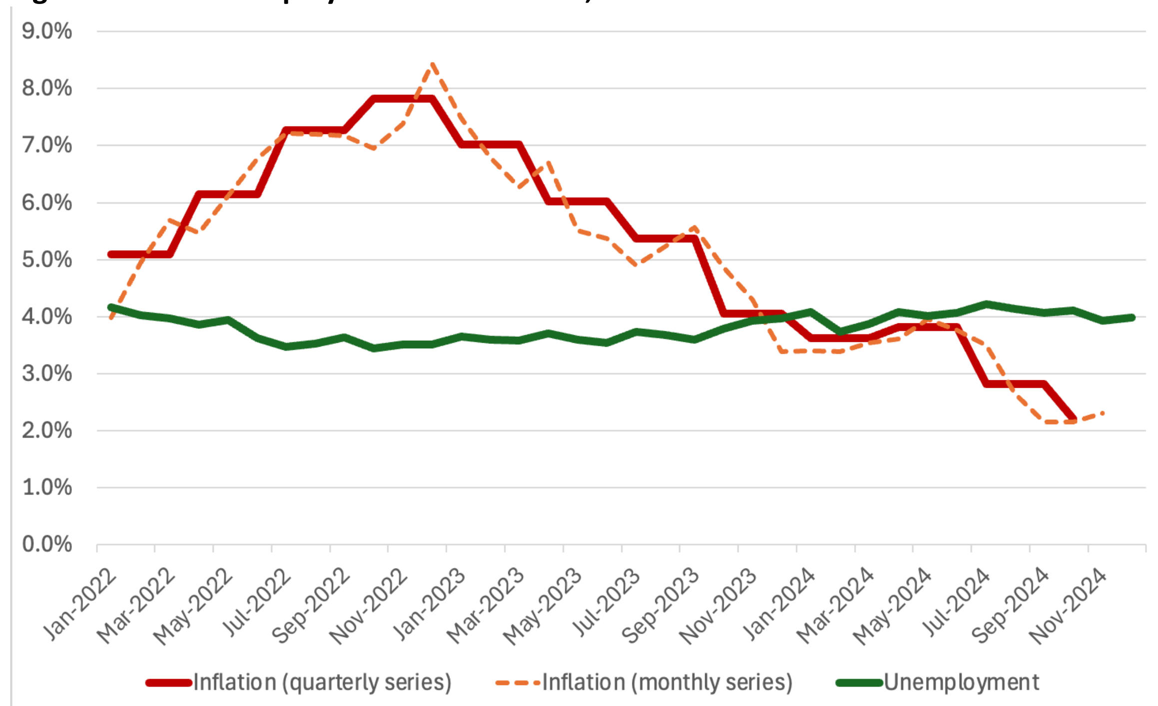
A second, more damaging example is the conduct of monetary policy after the pandemic.

In the context of the pandemic, and especially the Russian war on Ukraine, commodity prices rose. Many firms saw the inflationary environment as an opportunity to raise prices without objection, well beyond the cost increases they faced. Profits increased, in sharp contrast to the 1970s' inflation when they fell. The window for these profit increases in the 2020s was only brief. Firms could not indefinitely increase prices as they would become uncompetitive with smaller players in markets. Profit growth eased, and inflation again fell — not just in Australia, but in most countries.[11]

Central banks `raised interest rates, in the belief that higher interest rates would reduce labour demand, thereby reducing wage increases and in turn reducing inflation. However, this policy act had little impact on supply shortages and so was not, in itself, the cause of slowing inflation. Indeed, contrary to the expectations of central banks, including the RBA, unemployment did not rise initially to the extent expected, or in a time frame consistent with its being responsible for the fall in inflation. For example, in Australia, as Figure 2 shows, inflation started to fall *before* there was any significant rise in unemployment — the opposite of what would have happened if reducing labour demand was what led to the reversal of inflation. By late 2023, inflation was lower than at any time since early 2022, even as unemployment had barely altered from its half-century low,. That said, one of the most notable aspects of the two series was how little unemployment moved at all, despite very large movements in inflation which clearly were not driven by developments in the labour market. For almost all of this period, unemployment was well below the RBA's estimate of the NAIRU. If a NAIRU really existed and did what it said on the box, inflation would have continued to accelerate. Had the Reserve Bank not misunderstood the relationship between labour markets and inflation, including through privileging its belief in the magical NAIRU, interest rates would have been reduced a lot earlier.

[11] Jim Stanford et al. (2023) Profit-Price Inflation, n7 above. See also other references in n7 above.

Figure 2: Unemployment and inflation, 2022-2024



There are two further aspects of this failure of monetary policy. The first is a misunderstanding of dynamics of inflation in the 2020s. It was an interpretation that focused on wages, not profits, and one that has been critiqued in earlier work by numerous researchers around the world, the OECD, the IMF and the ECB.[12] This failure to understand the role of profits explained both why inflation rose and why it fell before unemployment rose. It is not the focus of this paper, though.

The second reason, which was also a reason why wages growth has been frequently underestimated, lies in the failure of policy makers to adequately incorporate concepts of power, including labour market monopsony, into their models of how labour markets work. That is the focus of this series of papers.

[12] See fn 7 above.

Thinking about labour markets

A major part of the problem, about how policy affecting work and rewards is governed, is weakness in the understanding of how labour markets work.

This weakness is not altogether surprising, as a broad consensus about theory in this area emerged nearly half a century ago, and it thereby became self-perpetuating, particularly as its continuation was in the interests of those with the greatest power. (You don't want to talk about power when you're the one who has it.) The facts have thrown up challenges to the perfect competition formulation, and indeed the facts themselves have changed: the world of work is very different now to how it was half a century ago. However, it has not normally been in the interests of those with power to concede the errors of a model that justified their position, so change has been slow.

In this section, we discuss international theorisation about labour markets, and how some key institutions have rethought their position. We then look more specifically at the dominant, perfectly competitive model, its weaknesses, and an alternative, more realistic approach to understanding labour markets. Subsequent sections then look in more detail at the key missing ingredient — power — and an important, poorly canvassed aspect of that ingredient, being wage norms.

INTERNATIONAL THINKING AND RETHINKING ABOUT LABOUR MARKETS[13]

It was in the 1990s that the perfect competition model, not only of labour markets but of product markets and financial markets generally, reached their peak acceptance within international institutions. In labour market policy, probably the pinnacle was the 1994 OECD *Jobs Strategy*, which recommended policies to increase wage flexibility, including moves to reduce non-wage labour costs and decentralise wage bargaining.[14]

A questioning of this model gained substantial impetus with the global financial crisis of 2008, which destroyed the complacency brought about by the 'Great Moderation',[15] a long period of growth uninterrupted by recession. The financial markets — ostensibly the closest thing to a 'perfect market' with access to 'perfect information' — and allied institutions such

[13] More detail on the issues raised in this section can be found in David Peetz, 'Multi-employer bargaining in New Zealand within the rise and fall of labour market neoliberalism', *New Zealand Journal of Employment Relations*, 48(2): 1-19, available in open access at https://ojs.aut.ac.nz/nzjer/forthcoming/view/index, https://doi.org/10.24135/nzjer.v48ix.161, from which this section draws.
[14] Organisation for Economic Cooperation and Development (1994). *The OECD Jobs Study: Facts, Analysis, Strategy*. OCED Publishing Paris.
[15] B. Bernanke (2004). The Great Moderation. The Federal Reserve Board. 20 February, https://www.federalreserve.gov/BOARDDOCS/SPEECHES/2004/20040220/default.htm

as the 'ratings agencies' had not only failed to predict the crisis, they were largely responsible for it happening.[16]

This was not, however, the moment when scepticism first arose. Even by 2004, the OECD was softening its rhetoric, describing the evidence for its own *Jobs Strategy*'s demands for deregulatory policies as 'plausible' but 'fragile'.[17] In 2008, the OECD published its *Growing Unequal* report, in which it warned of rising inequality and its consequences.[18] After the global financial crisis, the OECD's doubts became more overt. In 2009, the OECD concluded that it could find no evidence that structural reform policies to promote flexibility had made labour markets 'less sensitive to severe economic downturns than was the case in the past' and it recommended governments improve income support and unemployment insurance benefit systems, which it had previously said would decrease flexibility.[19]

Sceptisim in the OECD grew such that, by 2018, after long support for decentralisation in wage fixing, it shifted to support multi-employer ('sectoral') bargaining as a means of facilitating structural adjustment to external shocks. It found that 'co-ordinated collective bargaining systems are associated with higher employment, lower unemployment, a better integration of vulnerable groups and less wage inequality than fully decentralised systems'.[20]

The OECD was not the only institution that was rethinking the policy model based on perfectly competitive markets. In 2013, the managing director of the International Monetary Fund (IMF) had told the World Economic Forum at Davos that '[e]xcessive inequality is corrosive to growth; it is corrosive to society'.[21] In 2015, the IMF published a working paper that said the 'decline in unionization is related to the rise of top income shares and less redistribution, while the erosion of minimum wages is correlated with considerable increases in overall inequality'.[22] By 2019, the IMF was publishing a working paper that said '[r]ecent research generally concludes that the change in employment caused by an increase in the minimum wage is close to zero'.[23]

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[16] A. Schwab (2011). Ratings agencies: how toxic loans became a gleaming security. *Crikey!*, 26 August www.crikey.com.au

[17] Organisation for Economic Cooperation and Development. (2004). *Employment Outlook 2004*. OECD, Paris, p165. https://doi.org/10.1787/empl_outlook-2004-en

[18] Organisation for Economic Cooperation and Development. (2008). Growing Unequal? Income Distribution and Poverty in OECD Countries. OECD, Paris. https://www.oecd-ilibrary.org/social-issues-migration-health/growing-unequal_9789264044197-en

[19] Organisation for Economic Cooperation and Development. (2009). Employment Outlook. OECD, Paris. https://www.oecd-ilibrary.org/employment/oecd-employment-outlook-2009_empl_outlook-2009-en

[20] Organisation for Economic Cooperation and Development. (2018). Employment Outlook 2018. OECD, Paris, p110. https://www.oecd-ilibrary.org/employment/oecd-employment-outlook-2018_empl_outlook-2018-en

[21] C. Lagarde (2013). "A New Global Economy for a New Generation", International Monetary Fund, 23 January, https://www.imf.org/en/News/Articles/2015/09/28/04/53/sp012313

[22] F. Jaumotte and C. Osorio Buitron, C. (2015). Inequality and Labor Market Institutions, IMF Staff Discussion Note SDN/15/14, International Monetary Fund. https://www.imf.org/external/pubs/ft/sdn/2015/sdn1514.pdf

[23] P. Sodsriwiboon and G. Srour (2019). Does a minimum wage help workers?' International Monetary Fund, pp 40-41, https://www.imf.org/en/Publications/fandd/issues/2019/03/does-a-minimum-wage-help-workers-basics

This is not to say that neoclassical ideas have suddenly been totally abandoned by international economic institutions. 'Zombie' ideas die hard.[24] Bodies such as the IMF and OECD remain dominated by orthodox economic thinking, albeit less so than in earlier times, and the IMF, for example, is still heavily criticised for adherence to a very restrictive perspective in its approach to structural adjustment policies in countries with high debt.[25] That said, by the 2020s even bodies such as the European Central Bank (ECB) had, as mentioned, joined the OECD and IMF in accepting some or all of the ideas behind "sellers'" or "profit-driven" inflation,[26] acknowledging the discretion that firms have in determining prices and, by implication, raising doubts about the pure competitive model in other areas such as the labour market.

WHAT HAD BEEN THE PERFECTLY COMPETITIVE IDEAL OF LABOUR MARKETS?

For a long time, but particularly from the 1980s, when policy approaches referred to as 'economic rationalism' and then 'neoliberalism' became ascendent in Australia and other industrialised countries, the dominant view of the labour market, implicitly or explicitly, was the perfectly competitive model. In this model, the forces of supply and demand inevitably push towards an equilibrium outcome in which there is full employment, and a flexible wage that itself ensures full employment. Simple observation of the real world tells us that most countries experience unemployment, which should not exist in the perfect competition model. To its adherents, however, the existence of unemployment does not refute the model. Rather, over the long run it mostly signifies interference in the operation of the model through either government intervention, or monopoly actions by unions, that raise the wage above the equilibrium level, reducing employment below full employment and creating unemployment. In the short term, unemployment may be either frictional (caused by workers leaving jobs to search for better ones), cyclical (due to the business cycle) or structural (mismatches between the industries or localities of the supply and demand for labour) but, over the long run, in an unimpeded market only frictional unemployment would persist. Thus, the existence of unemployment becomes an argument for moving closer to a free market by reducing government intervention or combating trade unionism (that is, reducing workers' power without using the word 'power').

In the perfect competition model, firms do not have a choice as to what wage they offer workers. They must offer a wage equivalent to the 'market-clearing' wage, meaning the wage at which the labour market experiences full employment and so the market is 'cleared'. If a firm does not offer the market-clearing wage, it will be outcompeted for labour, and have no workers. Alternatively, a firm that pays a wage above the market-clearing rate will go out of business, as other forms with cheaper labour will be able to undercut them. In this situation, a full-employment equilibrium is achieved, and only unions or government

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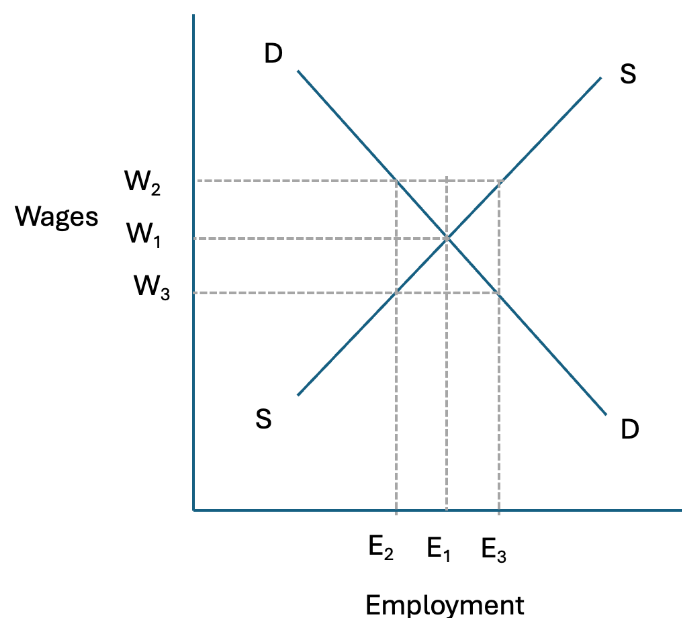
[24] John Quiggin (2010). *Zombie Economics*. Princeton University Press, New Jersey.
[25] M. Stojanovic (2020). Human Rights and Austerity: The IMF as a Handmaiden of Neoliberalism. Seven Pillars Institute. https://sevenpillarsinstitute.org/human-rights-and-austerity-the-imf-as-a-handmaiden-of-neoliberalism/
[26] See n7 above.

intervention can prevent a market-clearing wage from being reached, by enforcing a wage that is too high.

The perfect competition model is often depicted graphically, along the lines of the supply and demand curves shown in Figure 3. The two major lines show the supply of (SS) and demand for (DD) labour. The supply curve is upward-sloping, meaning as the wage goes up, more workers are willing to offer their labour to employers. The demand curve is downward-sloping, meaning that as the wage increases, employers demand less labour. Wages increase or decrease until they settle at W_1, where supply equals demand. As a result, employment is at E_1. All workers offering their labour at that wage have a job, so there is no unemployment — that is, the economy is at full employment. If something forces the wage to W_2, such as a minimum wage law or union power, employment falls to E_2 (because only E_2 of labour is demanded by employers), but E_3 workers want jobs, to there is unemployment equal to the distance between E_3 and E_2. This unemployment will persist until the wage is allowed to fall to W_1.

Alternatively, if the wage is only W_3, there will be a shortage of labour, as employers will demand E_3 workers but only E_2 are available. Employers will raise wages until all jobs are filled, that is they will raise wages to W_1.

Figure 3: Supply and demand curves in the simple perfect competition model



So, in the world of perfectly competitive labour markets, full employment is always achieved because labour supply perfectly balances with labour demand. It operates just like many product markets: if the supply of a good — like bananas — goes down, or demand goes up, the price goes up. And vice versa.

Observers of reality would note that there are actually many different wages paid, not just one market-clearing wage. Economists would explained this variously by: differences in the productivity of workers, mainly reflecting differences in their skill levels of workers, which in

turn were a function of their different levels of education and experience; differences in the efficiency of employers which would also shape the productivity of the workers they hired (though in the long run these inter-firm differences would disappear, as inefficient firms were forced out of business); and 'compensating wage differentials' that were paid to compensate workers for doing work that was unusually dangerous of otherwise unattractive.[27] The existence of these wage differences, again, was not seen as invalidating the perfect competition model, just complicating it. Some economists probably spend most of their time writing about situations outside this perfectly competitive model. The aim is to show what imperfections exist and what needs to be done to remedy it. Such analyses do not concede, though, that it is not the details that matter, it is the flaws at the core of the model that render it problematic.

The perfect competition model is built on many assumptions. Amongst the most significant is the existence of a large number of buyers and sellers of labour — that is, of employers and workers. The number must be so large that no individual firm (or worker) can influence the going wage. Instead everyone must be a price taker, and the wage is externally determined by the operation of the market. The model also relies upon the existence of perfect information: every market participant knows everything that is relevant to their wage, including the existence of any alternative job opportunities. It also relies upon perfect mobility: workers must be able to move from one job to another, if the latter offers higher wages (or better conditions that are not offset by lower wages).

Yet the perfect competition model that treats workers as if they are pure commodities like bananas does little to explain wages and employment outcomes for workers. Many factors that affect wages do not influence the price of pure commodities like bananas. Banana vendors readily change the price of bananas daily. Wages do not change daily. Bananas do not taste bitter if you threaten or pay too little for them. Bananas do not define themselves in terms of where they are located in the fruit market or how they are labelled. Bananas do not starve if they do not get bought. Even if they did starve, nobody would care, because bananas do not vote. Most importantly for this report, bananas do not know how to organise. That is, bananas do not exercise power, and so the price paid for bananas has nothing to do with the power of the bananas themselves.

This is not to say that traditional economics has *nothing* to offer in understanding labour markets. An emphasis on how supply and demand work is very useful and provides many insights. Understanding how incentives affect behaviour is very important. But providing insights into how *some* forces work does not tell us how *all* forces affecting labour markets work. Pop economics books like *Freakonomics!*[28] offer a lot about supply and demand but not much about other economic forces. As Krueger pointed out, what some people call 'imperfections' are best understood as 'the way the labor market works. The assumption of perfect competition is the deviation from the norm of "imperfection" as far as the labor

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[27] e.g. G.S. Becker (1964). *Human Capital: A Theoretical and Empirical Analysis, with Special Reference to Education*. Harvard University Press, cited in C. Goldin (2014). 'Human Capital' In C. Diebolt and M. Haupert (eds.), *Handbook of Cliometrics,* Springer-Verlag,. pp 55-86.
[28] Steven D. Levitt and Stephen J. Dubner, *Freakonomics: A Rogue Economist Explores the Hidden Side of Everything*, William Morrow, New York, 2005.

market is concerned.'[29] Yes, excess supply can depress wages growth and excess demand can raise it, but it need not follow that a market-clearing equilibrium will be reached.

Let us put this in terms of charts of the supply and demand curves that textbook economics tells us determine the equilibrium wage, as shown in Figure 3. Those supply and demand curves might,[30] if drawn correctly, show the *gap* between labour supplied and labour demanded at a given wage *and* a given level of economic activity. But they do not tell us what *determines* that wage. The actual wage paid will be a function of many forces, including the power balance between the parties. The actual wage paid may be at W_1, W_2, W_3 or many other places along the y-axis of that chart. There may be many reasons why the actual wage paid is above or below that shown as W_1 in Figure 3, some of which are discussed in the next section. This is not a market imperfection that needs to be offset; it is an inherent part of the wage determination process.

A REALISTIC PERSPECTIVE ON WAGES

In reality the labour market operates quite differently to the perfect competition model. Fundamentally, the assumptions behind the model are wrong. Recognition of this leads to the key conclusion that the wage rate is not externally set but can be influenced by market participants. That is, *employers have discretion in setting wage offers*, and *employees can influence accepted wage rates through collective bargaining or political influence* (that may lead, for instance, to legislated minimum wages). Recognition of this is not just a minor matter of detail, to show that 'nothing is perfect'. It fundamentally changes the predictions that are made.

It is obvious to anyone who has engaged in wage negotiations that employers are not price takers, and they have some discretion in the wages that they offer and pay. If this was not the case, there would be no point in wage negotiations, as the wage payable to any worker could be identified by reference to the market wage, with much lower transaction costs to both sides.

Inherent barriers to competition

The perfectly competitive ideal of a market-clearing wage equilibrium is rarely achieved, partly because firms offering higher wages do *not* necessarily out-compete low-wage firms for workers. This happens because workers cannot readily move to higher-wage firms in large enough numbers. Perfect mobility of labour does not exist. Moreover, there are (increasingly) incentives facing firms that prevent them from offering higher wages. In addition, the (increasingly) weaker bargaining power of workers means that firms do not *need* to offer higher wages. Hence, to the extent that some firms (mostly larger firms) offer

[29] Alan B. Krueger, 'Luncheon Address: Reflections on Dwindling Worker Bargaining Power and Monetary Policy', Jackson Hole Economic Policy Symposium, Federal Reserve Bank of Kansas City, 2018, p280.
[30] We say 'might' because the level of employment is driven by the level of economic activity, which is not directly shown in Figure 3, though it influences (shifts) the labour demand curve.

higher wages than others, the number of firms that offer these higher wages is enough to enable them to maximise their own profits, but it is not enough to clear the labour market.

Why do other firms not step in and make up the shortfall? In a perfectly competitive product market, they would. But product markets themselves are often not perfectly competitive. There are barriers to entry to most markets. Established sellers have reputations and distribution mechanisms that new entrants lack. They can often temporarily undercut the prices charged by new entrants, at least for long enough to drive them out of the market. So it is rare that new players would enter a market to compete with larger established firms, especially as they would typically have to sell at higher prices than those established firms. Large established firms, recall, are paying lower wages than would clear the market, with lower employment and those lower wages are one factor assisting their charging lower prices.

In some markets, the need for firms to charge lower prices than potential competitors is often the main reason that they choose to pay lower wages. This is especially common in markets where small firms compete to provide services or goods for a larger, monopsonistic corporation (such as a supermarket or a mining company), in what we call 'agentic monopsony' markets in a later report.[31] In a US panel study of publicly traded companies over 1978-2014, dependence on large buyers 'lowered suppliers' wages and accounted for 10 percent of wage stagnation in nonfinancial firms.[32]

So a new entrant is unlikely to get very far with competition unless they have a new technology or innovation that enables them to offer a better product or a cheaper price, plus the financial resources to withstand temporary undercutting of prices by established dominant players. Even if they could compete, there is no guarantee they would offer higher wages.

Gender, ethnicity and wages

An analogous situation applies in the relationship between gender and wages. It is widely known that wages for female workers have long been lower than wages for males doing equivalent work. The existence of this discrimination was inexplicable in the perfectly competitive model, since in that model firms that underpaid female workers would quickly be displaced by firms that paid them their due. So, neoclassical economists would try to argue that women's productivity was lower[33] (as if lower wages had no impact on productivity) or that firms who wanted, in terms of wages, to discriminate against workers of a particular gender or race would willingly lose money (pay a 'premium') to do so. One famous economist argued that "discrimination by firms…is measured by how much

[31] D Peetz, Monopsony and structural power in wages, Carmichael Centre, to be released in 2025.

[32] N. Wilmers (2018). 'Wage Stagnation and Buyer Power: How Buyer-Supplier Relations Affect U.S. Workers' Wages, 1978 to 2014' *American Sociological Review*, 83(2), 213–242. https://doi.org/10.1177/0003122418762441

[33] Some still do, e.g. Yana Gallen (2018), 'Mothers' low productivity hurts overall pay for women', *The Hill*, 2 August, https://thehill.com/opinion/finance/400077-firms-pay-females-less-because-they-produce-less-on-average/

profits…they forfeit to avoid hiring…members of a group that is disliked”.[34] This model was unable to persuasively explain how discriminatory firms, suffering this loss in profits, would then be able to stay in business. It should have taken only a small number of firms running non-discriminatory wage policies to drive discriminatory firms out of business.

So how was it that firms could underpay women and not go out of business? Put simply, those firms had the *power* to pay them less. A norm existed amongst employers that women would not be paid men’s wages, so a female could not improve her situation by moving to a different employer. Women lacked the associational power to force employers to pay higher wages, until they successfully unionised and obtained power within the unions to force them to take their concerns seriously.

Labour market segmentation theory[35] illustrates how firms, within bounds, choose wages for various parts of the workforce. Due to segmentation of labour markets (e.g. into segments for women, non-English speaking migrants, young workers), employees with similar productivities can be paid different wages. This model incorporates power into its framework. Through a related process, high pay for highly educated workers reflected employers using education as a signalling device, enabling them to cheaply identify the workers who were more likely to be more productive.

Wage stickiness

In sum, then, the less ideal but more realistic economic world in which people live and work is unlike the perfectly competitive model. In the world that actually exists, it is only through luck that the prevailing wage might happen to coincide with full employment – and even then, monetary policy would intervene to recreate the desired level of (purportedly non-inflationary) unemployment. Rather, the number of jobs is driven by the level of economic activity, not of wages. Nor can wages rapidly adjust to match changing patterns of economic activity. Wages are ‘sticky’.

Wages are sticky both upwards and downwards, for different reasons. On the one hand, people in jobs do not drop their wages when unemployment is high; and employers do not ask them to. People are not bananas. The price of bananas might fall when there is a surplus of bananas. Wages are not like that, regardless of unions or collective bargaining.

On the other hand, employers do not even necessarily raise their wages when unemployment is low. Barriers to mobility (such as the difficulty of moving cities, especially in couple housegolds) may hinder the ability of workers to move between jobs, and they may never even become aware of the availability of jobs in other cities and the wages they might receive there. These things enhance the ability of firms to offer lower wages than the market-clearing wage.

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[34] G.S. Becker (1993). The Economic Way of Looking at Behavior. *Journal of Political Economy*, 101(3), 385-409

[35] e.g. P. Brosnan, D. Rea & M. Wilson (1995). ‘Labour Market Segmentation and the State: The New Zealand Experience’. *Cambridge Journal of Economics*, 19(5), 667–96.

The supply and demand model of the labour market assumes that employers will raise wages when there is not enough labour. But what if employers refuse to raise wages, even when there is a shortage of labour? What if they decide to do anything but raise wages? This would be irrational in the neoclassical world, but actually describes quite accurately the recent state of the labour market. Jobs and Skills Australia, the federal government agency responsible for minimising shortages, asks employers about what they do in response to a skills shortage. In 2023, only 1 per cent said they would adjust remuneration. In 2022, it was only 0.4 per cent. Much more common were readvertising (73%), restructuring the organisation (7%), change position requirements (4%), give up (5%), or don't know (3%).

This can be rational behaviour, at least for the individual employers. Employers may be able to maximise their profits at a lower wage than the market-clearing wage. There may indeed be pressures for them to keep that wage low, if the firms to whom they are supplying demand a low cost structure. They may decline to raise wages to attract new recruits, as they would face intense pressure from existing employees to do the same for them.

Power, wages and norms

When we look at the difference between the perfect competition model of the labour market, and what actually happens, we can see that, at every stage, the key difference is related to a failure to take account of power.

EMPLOYER DISCRETION OVER WAGE RATES

When a worker does not take up an alternative job offer that would provide them with better pay, because they do not know about its existence or because it is too difficult to move jobs or homes, the power of their existing employer is shown to be enhanced. That existing employer has the power to pay less to the worker than they would have to if there genuinely was perfect information and perfect competition.

If a 'non-compete' clause in an agreement constrains a worker, who has left their job, from taking a job with another firm in the same industry, then the power of their former employer is enhanced. That firm has the power to force a lower wage upon that departed worker. Indeed, the impact it has on the alternatives available to that worker may be so great that they choose to stay with the original firm rather than leaving. Thus the original firm, through that 'non-compete' clause, has the power to pay a lower wage to that worker than they would have to pay if that clause did not exist. Firms may have 'no poaching' agreements that likewise prevent wages from being bid upwards.

Those are examples of 'monopsony' — where the seller of labour (the worker) faces only one or a small number of buyers (potential employers). It is a situation analogous to 'monopoly', which is just the same concept reversed: a buyer (consumer) faces one or only a small number of sellers (producers or retailers). The monopolist has power over the consumer. The monopsonist has power over the worker. Many of the failed assumptions of the perfectly competitive model relate to concepts that are addressed in theories of monopsony, which we turn to, in more detail, shortly.

If workers are hesitant to move quit their job or move locality, or unaware of alternative job opportunities that they do not see advertised or of wages that might be offered elsewhere, or have skills that, in part at least, are specific to their current firm and not easily transferred or valued elsewhere, the effect is similar to that of reducing the number of employers that are competing for the services of the employee. They reduce the bargaining power of employees. They increase the monopsonistic tendencies in that labour market. Studies suggest that lower job-switching rates are associated with lower wages growth.[36]

[36] Christopher Ball, Nicolas Groshenny, Özer Karagedikli, Murat Özbilgin and Finn Robinson (2019) Low wage growth and job-to-job transitions: Evidence from administrative data in New Zealand , Reserve Bank of New Zealand Analytical Note Series AN2019/11 , Reserve Bank of New Zealand , Wellington, December; Karahan, F, R Michaels, B Pugsley, A Şahin, and R Schuh (2017) 'Do job-to-job transitions drive wage fluctuations over the business cycle?" *American Economic Review*, 107 (5), 353–357.

The idea that firms have no discretion on how they set wages — that instead they have to take some market-clearing wage — ignores the power that firms have to choose a wage. This power may arise from monopsony. But it may also arise from developments in the collective organisation of labour — in the unionisation of workers, their collective bargaining and taking of collective industrial action.

Collective bargaining is a way by which workers bunch into a collective of labour to bargain with a collective of capital called a corporation. Individual shareholders know pretty quickly that they can make more money by being in a collective called a corporation than just trying to do something on their own with their money. Many individual workers know the same thing about labour — that they can earn more money by being in a collective called a union than just trying to negotiate wages on their own with their labour. Collective bargaining has been an attempt to force employers to offer higher wages. Collective bargaining thus also exists as a counter to monopsony — to employers' tendency to offer wages lower than marginal productivity.

If collective bargaining declines, then the effects of employer monopsony power on wages can be intensified. One recent American study showed not only that greater employer concentration led to lower wages, but that the effect increased over time: that is, a given increase in employer concentration led to a greater reduction in wages than had been the case in the past. The authors attributed this to two things: declining labour mobility made it harder for workers to offset the impact of employer concentration on local labour markets by moving; and weaker unionism made it harder for unions to offset the impact of employer concentration on local labour markets by bargaining. Previously they had found, when comparing local labour markets, that the effects of employer concentration in reducing wages were over one and a half times stronger in local labour markets without unions than in local labour markets with average levels of unionisation.[37] The OECD also concluded that the impact of employer concentration has increased over time.[38]

So, the impact of employer monospony power on wages can increase in time *even if there is no increase in employer concentration itself*, due simply to a reduction in other sources of employee power.

POWER EFFECTS ON WAGE RATES

So the power of labour and the power of employers affect wages and employment outcomes. The supply of, and demand for, labour play critical roles in the determination of wages, but they are not the only factors, and the failure to take account of power in the perfect competition model, a reflection of the false assumptions of that model, leads to mistaken predictions and policy outcomes.

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[37] E. Benmelech, N.K. Bergman & H. Kim (2022). Strong Employers and Weak Employees: How Does Employer Concentration Affect Wages? *Journal of Human Resources, 57* (S), S200-S250. doi: https://doi.org/10.3368/jhr.monopsony.0119-10007R1

[38] OECD (2021), *The Role of Firms in Wage Inequality: Policy Lessons from a Large Scale Cross Country Study*, OECD Publishing, Paris, https://doi.org/10.1787/7d9b2208-en.

Other factors shaping labour market outcomes include the choices made by employers regarding the conditions of employment, the attitudes of workers towards wage relativities, and the institutional forces shaping dispute resolution, minimum wage setting, unemployment benefits and jobseeker services. We do not consider such factors here, because our interest in this series is in the question: *why are low wages normalised despite tight labour markets?*

The answer to that lies in a better understanding of the role of power in the operation of labour markets, and outcomes for wages and employment. Power is the ability of one party to achieve its objectives, typically despite their being against the objectives (or at least the interests) of another party. It may take many forms. Four key dimensions in this context include:

- market power (through having high demand, or low alternative supply, of the services one can supply);
- institutional power (through having rules, procedures or norms that affect power);
- associational power (through joining together with other players to boost your relative importance);
- and structural power (through occupying strategic locations for which there are few if any alternatives, thereby making it inherently easier to achieve objectives).

When applied to the labour market, it could be said, for example, that:

- psychiatrists may have high market power (demand highly exceeds supply), while most musicians have low market power (there are many people with the skills but demand for them is well below the supply);

- train drivers have high associational power (most belong to a union) while kitchenhands have low associational power (very few belong to a union);

- chemical plant controllers have high structural power (no-one else can readily do their job) while labourers have low structural power (there are many people available who can supply this work);

- workers in large public sector organisations have high institutional power (there are myriad rules and procedures that protect them) whereas workers in small businesses have low institutional power (there are few internal rules, enforcement is difficult and small businesses are even exempt from some labour laws).

In the prefect competition model, ‘market power’ is not expressed as any form of power, and instead is replaced simply by use of the terms of supply and demand. The term ‘power’ is mostly only applied to trade unions, expressed in terms of the concept of ‘monopoly power’ that interferes with the operation of supply and demand.

Thus ‘power’ is treated as something that needs to be removed as it has no appropriate role in the operation of a market, and the forces of supply and demand should be allowed to operate to set quantities and prices in markets. This conception of power is, of course, highly

asymmetrical: reducing the 'power' of unions is seen as good, but the corollary, of increasing the power of employers, has no normative frame attached to it because employer power does not exist.

Some heterodox versions of economics (diverging from the perfectly competitive model) also aim to account for 'monopsony', in which there is one buyer (as opposed to one seller) of a good or service — principally, labour. This is, indeed, a major advance and one that must be considered. A subsequent report in this series will focus extensively on monopsony.[39] However, monopsony is not the only source of power that employers have, and redressing the imbalance of power at the workplace is not achieved simply by promoting a perfectly competitive labour market in which employers cannot exercise monopsony power. Understanding labour market outcomes requires an appreciation of all forms of power (including institutional, structural, associational and market), and monopsony — as a form of structural power — is not the whole of that story.

The growth of casual employment makes it harder for workers to unionise, engage in collective bargaining or take industrial action. It thus reduces workers' associational power. Statutes or legal interpretations that make it easier (or harder) to hire workers on a casual basis weaken (or strengthen) workers' institutional power.

These four forms of power, although frequently downplayed or ignored in the economics literature, have received considerable attention in the industrial relations literature. It is not necessary at this stage to go into great detail about what the literature has said on each of these. However, one concept is worth elaboration here because it has been barely canvassed elsewhere. That is the concept of wage norms. It is the focus of the next sub-section, and of a subsequent report in this series.[40]

THE NATURE OF WAGE NORMS

When negotiating wages, workers and firms pay attention to the wage norms in that industry and for that occupation. They pitch their pay demands and offers in relation to those norms. The choices employers make on wage offers are influenced by factors specific to their organisation as well as broader factors that are common to multiple organisations

A wage norm can be defined as

> *a view common to a group regarding the appropriate wage to pay workers.*

There may be *employer wage norms* (the view common to employers regarding the appropriate wage to pay workers) and *employee wage norms* (the view common to employees regarding the appropriate wage they should be paid). When the two align, we can talk of *agreed wage norms.*

[39] D Peetz, Monopsony and structural power in wages, Carmichael Centre, to be released in 2025.
[40] D Peetz, Wages norms and wages growth, Carmichael Centre, to be released in 2025.

Employee wage norms have, interestingly, been frequently discussed in various literatures, though with different names and in a different framework. For example, scholars have written of the importance of 'relative pay deprivation', as opposed to 'objective pay deprivation', in influencing workers' wage demands.[41] People put much more effort into avoiding losses than they will put into securing gains of equivalent value.[42]

By contrast, employer wage norms have received very little attention. One of the few occasions in which they received public attention was in 2019 testimony by the then Governor of the Reserve Bank of Australia, Philip Lowe, who said:

> wage caps in the public sector are cementing low wage norms across the country, because the norm is now two to 2½ per cent, and partly that's coming from the decisions that are taken by the state governments.[43]

He later added

> The public sector, directly and indirectly, employs roughly one-third of the labour force, and they're saying wage increases across the public sector may be averaging two per cent. That has as indirect effect on the private sector, because there's competition for workers and it reinforces the wage norm in the economy at two-point something.[44]

An employer wage norm is analogous, but not identical, to the equilibrium wage in neoclassical models of the labour market, discussed earlier in this report. Its similarity lies in the fact that it is a prevailing wage, paid by many employers. It is not, however, just a function of supply and demand for labour curves. It is also influenced by shared beliefs amongst employers about what is right, appropriate or necessary – and their relative power to enforce those beliefs.

A big difference to the neoclassical understanding of labour markets is that firms can readily diverge from the wage norm (provided they do not diverge too far). Indeed, it is not necessary that the wage norm is the same as the wage rate at which 'market clearing' would occur. The wage norm can be at a level that allows for unemployment or one that allows for labour 'shortages' (more precisely, unfilled vacancies). Wage norms can make the wage 'too low' to clear the market. There is no reason why they would equate to a market-clearing level, because of the existence of barriers that prevent market-clearing mechanisms.

Wage norms may be influenced by several factors related to power. These include: reference points set by institutions such as industrial tribunals' setting of awards or public sector pay outcomes; pressure from other institutions such as employer organisations or government agencies; the operation of product markets; employer actions within labour markets; wage stickiness; macroeconomic circumstances; and collective organisation amongst employees and their ability to engage in collective bargaining and action.

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[41] e.g. W.G. Runciman (1972) *Relative deprivation and social justice*, Penguin, Harmondsworth.

[42] D. Kahneman (2011*). Thinking, Fast and Slow*. Farrar, Straus and Giroux, New York.

[43] P Lowe (2019) in House of Representatives, Hansard, Standing Committee on Economics, Reserve Bank of Australia annual report 2018, Canberra, 9 August, 2,15.

[44] Ibid, p19.

Amongst CEOs and senior executives, wage norms (more accurately, compensation norms) are set and understood through regular benchmark surveys by remuneration consultants. Remuneration committees of firms consciously decide whether to pitch CEO pay at, above, or (very rarely) below the norm identified by those consultants. Although, in theory, CEO pay may sometimes be linked to the performance of the firm, in practice this mainly (if ever) occurs when the firm experiences growth. In periods of decline various devices are used to minimise losses that CEOs would otherwise experience.[45] This, however, is a quite exceptional labour market as 'bargaining' is asymmetrical (both 'sides' of the 'bargaining table' are from the same social milieu and so there is minimal resistance to upward pressure for pay increases. Thus, the power of CEOs in remuneration setting should be seen not vis-à-vis the firm's board but vis-à-vis workers and customers.

Wage norms are a function of power. Collective bargaining exists in part as a counter to employer power that is partly manifest in monopsony — more precisely, as a counter to employers' tendency to offer low wages. Collective bargaining is a way by which workers coalesce into a collective of labour to bargain with a collective of capital called a corporation. Individual shareholders know that they can make more money by being in a collective called a corporation than just trying to do something on their own with their money. Employees often know something similar.

Collective bargaining has thus been an attempt to force employers to offer higher wages. However, with the decline in union density, and the incidence of collective bargaining, unionism can no longer be accessed by the majority of workers, and collective bargaining becomes less effective in securing wage gains.

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[45] David Peetz, 'An institutional analysis of the growth of executive remuneration', *Journal of Industrial Relations*, 57(5), November 2015. DOI: 10.1177/0022185615590903

How has power been influenced over time?

As mentioned earlier, if workers' power falls (for example, through declining unionisation), then workers' wages are more easily reduced as a result of greater employer concentration in labour markets (that is, by greater monopsony power of employers).[46] This appars to be exactly what has happened in Australia. One study showed that, in the mid 2000s, the gap between wages in a labour market with low and high employer concentration was only 2 per cent, but by the early 2010s this gap had more than doubled, to 5 per cent.[47] That finding suggests a trend decline in worker power and hence in workers' ability to offset employers' power where it is exercised. This section considers whether we can identify sources of changes in power and whether they are consistent with a decline in workers' power.

A decline in worker power would help explain how low wages growth seems to have been normalised, despite low unemployment. To investigate this further, we consider the various ways that power has been affected, both by changes in the economy and by changes in public policy.

ECONOMIC AND LABOUR MARKET FACTORS AND POWER

Table 1 shows 16 factors that have influenced or indicated the power of workers over the past half century, with broad depictions of movements in those factors and their consequent impacts on workers' power. We say both 'influenced' and 'indicated' because some of the factors identified here can be both. Most obviously, changes in union density can be both an indicator of changing workers' power (of reduced associational power), and a cause of it (since, for example, a decline in union density may lead to less involvement of unions in policy processes and hence reduced institutional power). The table points to the direction in which power has changed but, with few exceptions, does not attempt to quantify the magnitude of individual effects on workers' power.

[46] See note 37 and associated text.
[47] Hambur, J. (2023), 'Did Labour Market Concentration Lower Wages Growth Pre-COVID?' Australian Treasury Working Paper No 2023-01, Australian Treasury, Canberra.

Table 1. Factors influencing or indicating workers' power

Indicator	Broad movement in indicator (period)	Influence on or indication of workers' power
1. Trade union density	Declined (1975-2024)[48]	Reduction in worker power
2. Collective bargaining coverage	Declined (2000-2024)[49]	Reduction in worker power
3. Industrial conflict	Declined (1975-2007), low but broadly stable since then[50]	Reduction in worker power
4. 'Gig' economy	Expanded since 2014 (but still small)[51]	Reduction in worker power
5. Labour hire	Gradually expanded since 1990s[52]	Gradual reduction in worker power since 1990s
6. Casual employment	Significantly increased from 1980s to 2000s, relatively stable since then[53]	Reduction in worker power from 1980s to 2000s
7. Supply of and demand for labour	Unemployment increased from 1975, high (and variable) through to 2010, declined since then[54]	Reduction in worker power for most of the period since 1975, but increase in worker power from 2010 to 2023, slightly decreased 2024
8. Job switching	Gradual decline identified by Treasury to 2020[55]	Reduction in worker power
9. Use of contracting out and outsourcing	Increase (mainly qualitative observations)[56]	Reduction in worker power
10. Impact of concentration amongst employers	Increase[57]	Reduction in worker power
11. Use of temporary visa holders	Increase[58]	Reduction in worker power
12. Non-compete clauses	Probably growing[59]	Reduction in worker power
13. Franchising	Small traders increasingly are outlets for products of large (franchisor) firms	Reduction in worker power
14. Gender pay gap	Gradual decline (with variation) 1975-2024[60]	Gradual increase in (female) worker power

[48] Australian Bureau of Statistics (ABS), Characteristics of Employment, and Trade Union Members.
[49] Department of Employment and Workplace Relations, Trends in Federal Enterprise Bargaining; and ABS Labour Force.
[50] ABS, Industrial Disputes, Australia. https://www.abs.gov.au/
[51] ABS, Digital platform workers in Australia, https://www.abs.gov.au/
[52] Geoff Gilfillan, Use of labour hire and contract workers in Australia, Parliamentary Library, Canberra, 31 May 2024, https://parlinfo.aph.gov.au/parlInfo/download/library/prspub/9770735/upload_binary/9770735.pdf
[53] ABS, Labour Market Statistics and Characteristics of Employment.
[54] ABS, Labour Force.
[55] ABS, Labour Mobility; Meghan Quinn, What's driving low wages growth in Australia?, speech to Australian Conference of Economists, Melbourne, 16 July 2019.
[56] e.g. Power Retail and VirtualStaff365, 'Outsourcing Trends 2024', https://www.virtualstaff365.com.au/.
[57] Hambur, J. (2023), 'Did Labour Market Concentration Lower Wages Growth Pre-COVID?' Australian Treasury Working Paper No 2023-01, Australian Treasury, Canberra.
[58] Brendan Coates, Trent Wiltshire, and Tyler Reysenbach, Short-changed: How to stop the exploitation of migrant workers in Australia, Grattan Institute, Melbourne, 2023.
[59] Dan Andrews and Bjorn Jarvis, The ghosts of employers past: how prevalent are non-compete clauses in Australia, 61 MICRO NOTE, e61 Institute, 19 June 2023; Jack Thrower, New data shows many businesses are now using non-compete clauses – and that's bad for workers, Australia Institute, 21 February 2024, https://australiainstitute.org.au/post/new-data-shows-many-businesses-are-now-using-non-compete-clauses-and-thats-bad-for-workers/
[60] Workplace Gender Equity Agency (2025) The ABS data gender pay gap, https://www.wgea.gov.au/

15. Share markets	Increased importance of finance capital in corporate decision making from 1980s	Significant reduction in worker power
16. Trade	Increased competition from low-wage imports	Reduction in worker power

As we see from Table 1, in broad terms, almost everything that has happened outside the policy space in the past half century has reduced workers' power. The one major thing that has gone in the opposite direction, but only relatively recently, has been the reduction in unemployment over the past decade (setting aside the temporary spike in unemployment during the pandemic). Of 16 developments in the labour market in recent times, 14 signalled a deterioration in worker power, one an improvement in power only for female workers, and one an improvement since 2010 (lower unemployment until 2023)

PUBLIC POLICY AND POWER

Clearly, those other factors have outweighed the benficial impact on workers' power of reduced unemployment. That said, we must also consider what has happened in public policy. This is what Table 2 attempts to do. This is a more complex process, as public policy shifts according to who is in government and, indeed, may have many nuances within the term of a government. So Table 2 has a much more restricted time frame — it only covers policy changes over the past decade — and passes over the details of policy nuances, instead focusing on the borad direction of policy within a period of only a decade. Moreover, some may argue that some specific events not assessed should have been included. Nonetheless, the table covers 34 policy events: seven due to the federal government prior to 2022; 21 due to the federal government after 2022; five outside the government; and one 'other' that involved multiple agencies and government levels.

As background, it should be noted that industrial relations policy had several major swings in the quarter century before 2014. Legislation in 1992 and 1993 (the 'Industrial Relations Reform Act') paved the way for the introduction and spread of single-employer bargaining. Although this was negotiated between the Labor Government and the ACTU, and so was, overall, aimed at increasing workers' power, it was later seen as having the opposite effect in some ways, due to the clarification of the legal status of industrial action (formally making some strikes illegal) and also by restricting the scope of awards.

The subsequent Workplace Relations Act of 1996, introduced by a Liberal-National Party government, unambiguously favoured employers and reduced workers' power, by providing for non-union agreements, enabling individual contracts, reducing unfair dismissal rights, and tightening procedures for legal industrial action. The 2006 'WorkChoices' amendments were seen as the most radical industrial relations laws, enabling individual contracts ('Australian Workplace Agreements' or AWAs) to have pay and conditions inferior to awards, abolishing all unfair dismissal protections for workers in small to medium sized enterprises and some in larger firms, prohibiting union preference provisions, and further tightening procedures for legal industrial action and penalties for breaches. Earlier amendments had established an Australian Building and Construction Commission. All these amendments served to broadly

reduce workers' power. The laws were credited with playing a major role in the electroal defeat of the then government in 2007.

The Fair Work Act, mostly introduced in 2009, abolished AWAs and reinstated unfair dismissal protections, but left many of the existing provisions regarding legal and illegal industrial action (for eample, on the role of secret ballots) largely in place. Its effects were thus very ambiguous: on some matters it clearly increased the power of workers, on many others it left in place the reductions in workers' power that the earlier legislation had enacted. Hence, referring to the sum total of legislative change in Australia up to the 2010s, Stephen Kinsella and John Howe declared "the erosion of workers' rights is the most consequential, and actionable, factor behind the stagnation of wages in Australia".[61]

It is in this context that we need to consider Table 2. As we see in Table 2, a significant shift occurred in policy in 2022, and so that table distinguishes between those federal government policies implemented before 2022 and those implemented later. It also identifies policies that straddled the period, driven by institutions outside the federal government (the Fair Work Commission and state governments).

Table 2: How public policy has influenced wages 2014-2024

Public policy issue	Impact on economic variable	Impact on workers' power
FEDERAL POLICIES BEFORE 2022		
1. Establishment of Registered Organisations Commission (ROC)	Tighter regulation of internal affairs of trade unions	Reduction in worker power
2. Establishment of Australian Building and Construction Commission (ABCC)	Reduced capacity for union organisation and industrial action in construction	Reduction in worker power
3. Abolition of Road Safety Remuneration Tribunal	Prevented regulation of pay and conditions in heavy vehicle transport	Reduction in worker power
4. Sexual harassment	Defined and introduced orders for	Increase in worker power
5. New provisions for casual employment	Defined casual by reference to employer depiction, plus other changes	Mixed but overall reduction in worker power
6. Making some franchises and holding companies liable for certain actions of their subordinate organisations	Tighter regulation of franchises and holding companies	Increase in worker power
7. Government approaches to bargaining	Non-recognition or attempted circumvention of unions	Reduction in worker power
FEDERAL POLICIES FROM 2022 ONWARDS		
8. Government approaches to bargaining	Recognition and no attempted circumvention of unions	Increased worker power
9. SJBP: Gender equality	Prioritised reduction of gender equality	Increase in worker power
10. SJBP: Pay secrecy	Prohibited pay secrecy	Increase in worker power

[61] Stephen Kinsella and John Howe, 'Global perspectives on wage stagnation', in Andrew Stewart, Jim Stanford & Tess Hardy (eds) *The Wages Crisis in Australia: What it is and What to do About it,* University of Adelaide Press, Adelaide, pp 41-56.

11. SJBP: Sexual harassment	Tighten prohibitions	Increase in worker power
12. SJBP and Loopholes: Casual employment	Deem some as permanent employees	Increase in worker power
13. SJBP: Small claims	Expand eligibility for simplified procedures	Increase in worker power
14. SJBP: ABCC and ROC	Both bodies abolished	Increase in worker power
15. SJBP: Enterprise bargaining	Expand situations for multi-employer bargaining	Increase in worker power
16. SJBP: Fixed-term contracts	Limited use of fixed-term contracts	Increase in worker power
17. SJBP: Flexibility	Expanded right to request procedures to make acceptance more likely	Increase in worker power
18. SJBP: BOOT test	Simplified BOOT test	Slight reduction in worker power
19. PWE: Migrant workers	Protections for migrant workers	Increase in worker power
20. CL: Definition of employee	Made it harder for firms to classify workers as non-employees	Increase in worker power
21. CL: Regulation of 'employee-like work'	Enabled tribunal to regulate pay and certain conditions for many gig workers (including heavy vehicle drivers)	Yet to take effect, but likely to increase worker power from 2025
22. CL: Delegates' rights	Expanded delegates rights	Increase in worker power 2024
23. CL: 'Same job same pay' amendments	Should reduce pay gap between employees and labour hire workers	Yet to see full effect but likely to increase worker power from 2025
24. CL: Right to Disconnect	Prevents employers from contacting workers outside working hours in certain circumstances	Increase in worker power
25. CL: Wage theft	Introduced criminal penalties for egregious forms for some employers	Increase in worker power
26. CL: Small business	Clarified anomalies in small business exemptions	Reduction in worker power
27. CL: Right of Entry	Improved union access to workplaces	Increase in worker power
28. CL: Protected action	Compulsory conciliation in defined circumstances	Probable increase in worker power
29. CL: Discrimination	Additional protections	Increase in worker power
30. Non-compete clauses	Banned in employee contracts	Increase in worker power
POLICIES OUTSIDE THE FEDERAL GOVERNMENT		
31. State government rules on wage ceilings	Expanded since 2011, though abolished in NSW in 2024	Reduction in worker power until 2023, Increase in power 2024
32. FWC changes to awards regarding female-dominated occupations	Often ineffectual or reinforcing male-favouring relativities, but sometimes reducing gender gaps in awards	Mixed but on average gradually increasing female workers' power
33. High Court decisions on definition of employee	Made it easier for firms to classify workers as non-employees	Reduction in worker power
34. FWC decisions on industrial action 'essential services'	Made it easier for industrial action to be halted	Reduction in worker power
35. Reserve Bank monetary policy	Gradually reduced interest rates to 2019, increased interest rates aggressively from 2022.	Increase in worker power to 2019, reduction in worker power to 2022.
OTHER		
36. Pandemic response	Major closures and lockdowns, income support, all mostly reversed as pandemic eased	Mixed effects, with lockdowns and closures reducing worker

		power, income support measures increasing power

Notes: SJBP = Secure Jobs, Better Pay legislation (2022); PWE = Fair Work Legislation Amendment (Protecting Worker Entitlements) Act (2023); CL = Closing Loopholes Act (2023 (No 1) and 2024 (No 2)).

Prior to 2022, most major public policy initiatives acted to reduce worker power, though there were a few lesser actions that increased workers' power. However, perhaps the most notable aspect of industrial relations legislation in this period was the small quantity of it. This was because much proposed legislation did not pass through the Senate. Most of the legislation that was rejected in the Senate would have had the effect, if passed, of reducing workers' power.

After 2022, almost all federal legislation had the effect of increasing workers' power.
In total, among those policy events assessed, of those seven arising from actions of the federal government prior to 2022, two increased worker power and five reduced it; of the 23 arising from actions of the federal government after 2022, 22 increased worker power, one decreased it; and among the six that were either outside the government or involved multiple agencies and government levels, the pattern was very mixed. While there might be debate about the inclusion or exclusion of specific items, this would not effect the overall pattern: policy reduced workers' power before 2022; policy increased workers' power after 2022.

Over this period, there was a substantial volume of legislative reform, but some of it was only passed in 2024 and so has not yet had time to influence any outcomes. For example, although the Closing Loopholes legislation created new powers to enable the FWC to determine pay and certain conditions for many digital platform workers and road transport workers, no hearings under these provisions have yet occurred. The most recent change (a ban on non-compete clauses) was only announced in March 2025.

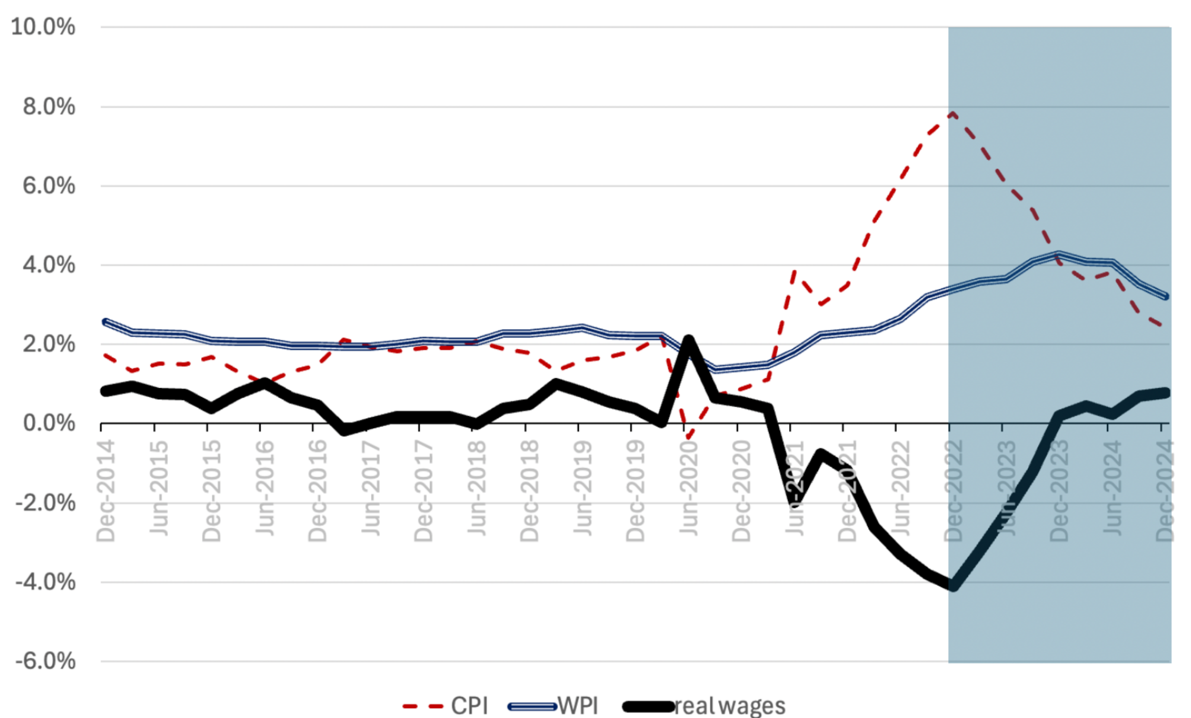
The effects on wages after a change in policy

The change in policy direction in 2022 could be expected to have some impact on wages, but not immediately, especially as some of it had not even come into force at the time data were published. However, early signs were positive.

EVIDENCE FROM INDEXES OF WAGE RATES

The first sign is from estimates of nominal and real wages from the Australian Bureau of Statistics (ABS), shown in Figure 4, over the decade 2014-2024: growth in in the consumer price index (CPI), the wage price index (WPI) and the real value of the WPI, as discounted by the CPI. The shaded (right hand) part in the period shows these series from December 2022, when the first major round of industrial legislation (the Fair Work Amendment (Secure Jobs, Better Pay) Act was proclaimed. The unshaded (left hand) part shows growth in these items in that part of the decade prior to December 2022.

Figure 4: Growth in consumer prices and nominal and real wages



Source: ABS Consumer Price Index and Wage Price Index.

Nominal wages grew at a little over 2% per year through most of the period from 2014 onwards, falling then recovering in the pandemic. After September 2022, as per the right panel, nominal wages grew more quickly, to over 4% per annum through 2023-24. In every

quarter after September 2022 it was higher than in every quarter in that decade before then.

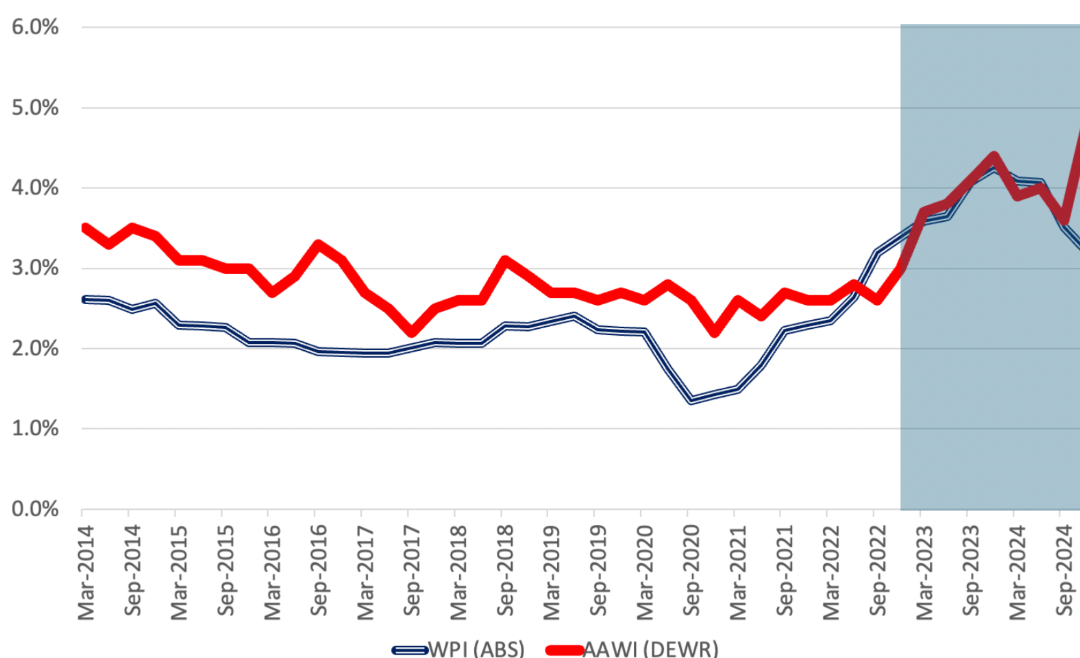
Real wages typically grew by between 0 and 1 per cent a year over the period, then after a brief increase[62] fell substantially to the end of 2022. The right hand panel shows a recovery in real wages growth after then, with positive real wages growth through 2024, peaking at 0.8% in the year to December 2024. Significantly, the increase in real wages growth came from both lower inflation and higher nominal wages growth.

A strength of the WPI is also a limitation. That feature is the fact that the WPI is looking solely at wage changes within firms in the same jobs. As many employees obtain wage increases by moving between firms (or suffer wage cuts from having to shift from jobs located within a large firm to an equivalent job in a contracting firm) this does not pick up wages changes arising through job changes. So we consider two other sources of information on wages.

EVIDENCE FROM ENTERPRISE AGREEMENTS

A second source of data is data on wage outcomes from current enterprise agreements with quantifiable wage increases. This is shown in Figure 5.

Figure 5: Average annualised wage increases (AAWI) under new quantifiable enterprise agreements and the Wage Price Index (WPI).



Source: DEWR, ABS.

[62] The temporary spike in real wages in early 2020 reflected, in no small part, a composition effect arising from the closure of many lower-wage industries in the economy (such as hospitality, retail, and personal services), which had the effect of increasing the average productivity of those who remained employed; that temporary effect was reversed when those industries re-opened.

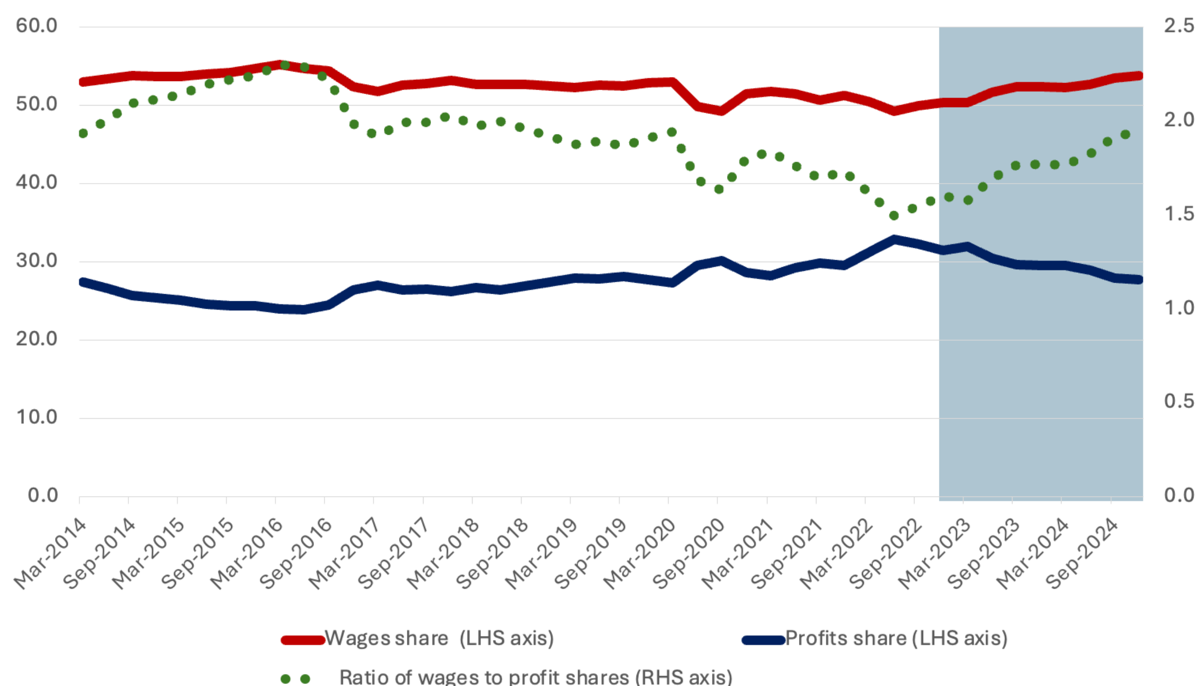
Figure 5 shows average annualised wage increases (AAWI) under all new enterprise agreements, and for comparison annual nominal increases in the wage price index (as per Figure 4). We can see that AAWI in enterprise agreements gradually declined from around 3.5% per annum in 2014 to close to 2.5% by 2022. However, in the two years after that, wage growth accelerated, peaking at 4.8% by end-2024. Again, in every quarter since December 2022 it has been higher than in every quarter between 2014 and 2022.

EVIDENCE FROM THE NATIONAL ACCOUNTS

It might be argued that the increase in wages growth shown above is solely a result of the temporary surge in inflation — after all, inflation is one factor shaping wage claims, and the gain in wages did come some time after this surge. If this was the case, the national accounts would show us that there had been no increase in the *share* of income going to labour.

The simplest way of testing this question is to look at the shares of national factor income going to profits (gross operating surplus) and to wages, salaries and supplements. These are shown in Figure 6, which also shows the ratio of the wages share to the profit share in total factor income.

Figure 6: Wage and profit shares of total factor income, and ratio of wages to profit shares, Australia, 2014-2024.



Source: ABS, National Accounts.

In March 2014 the wages share was 53.0% of factor income and by March 2016 it was as high as 55%, but by December 2022 it had fallen to just 50.3%. As shown in the shaded part of the chart, over the period to December 2024 it rose back to 53.8% of factor income.

Between March 2014 and December 2022, the profit share rose from 27.4% to 31.5%, but then fell back to 27.7% in December 2024. The ratio of wages, salaries and supplements to profits fell from 1.93 in in March 2014 to 1.60 in December 2022, then back up to 1.92 by September 2024. The ratio wages share had been over double the profit share through most of the early part of the decade; it fell to 1.6 times by late 2022, but rose again to over 1.9 times by late 2024.

One should always be careful of one quarter's data in the national accounts, especially as no trend series have been calculated since the pandemic, but it is noteworthy that the national accounts show a pattern that is broadly consistent with the one shown in the WPI and AAWI series. Most importantly, it refutes the idea that the recent growth in wages is simply a response to the temporary surge in inflation. The increase in wages growth cannot be dismissed as a response to inflation. Instead it reflects a genuine, recent change in the balance of power, favouring workers and facilitating wages growth.

Indeed, it has occurred in a period when inflation has been falling — from over 7% at the end of 2022, to below 3% at the end of 2024. A shift in power towards workers has led to higher nominal and real wages growth and an increasing share of wages in national income, yet it also accompanied a decline in inflation. Reversing (at least partially) the previous shift in power *away from* workers was no more inflationary than that was earlier shift against them.

What may seem like a paradoxical outcome is really a reflection of the fact that the 2020s surge in inflation had nothing to do with any 'wages explosion', and achieving a reduction in inflation had nothing to do with keeping wages in check.

ARE GAINS RESTRICTED TO UNION MEMBERS?

Normally, AAWI growth is higher than WPI growth, probably because union members usually obtain higher wage increases than non-members.[63] (Hence wage gains in union agreements are normally higher than wage gains in non-union agreements.) Interestingly, the acceleration in WPI growth from 2020 through 2022 was stronger than the corresponding pick-up in AAWI growth. This is probably because wages under enterprise agreements are typically 'locked in' for the duration of an agreement, so a sudden surge in inflation takes longer to pull on AAWI than on WPI growth. WPI growth thus 'caught up' to AAWI wage gains, after lagging well behind AAWI growth through the previous decade. After 2023, both series increased at similar rates up until September 2024, before AAWI growth substantially outpaced WPI growth in December quarter 2024.

The overall pattern suggests, though, that the increases in workers' power experienced after 2022 were felt by both union and non-union workers (contrary to claims by some that these reforms were privileging union members alone). The declines in workers' power for most of the past half century were felt by union members and non-members alike, and increases in workers' power since 2022 have been enjoyed both by unionists and non-unionists.

[63] The series are also calculated in different ways using different data sources.

Whether they increased by the same amounts is not so clear, especially as the lags created by agreement processes make it hard to compare like with like. Another way of examining this question is to do a more like-with-like comparison: between wage outcomes in union and non-union agreements before and after the first tranche of recent legislation. Between 2014 and 2022, AAWI in union agreements averaged 2.83% per quarter; afterwards it rose to 4.08%, an increase of 1.24 percentage points or 44%. Between 2014 and 2022, AAWI in non-union agreements averaged 2.58% per quarter; afterwards it rose to 3.35%, an increase of 0.77 percentage points or 30% — about a third lower than the 44% increase in wages growth through union agreements. So, while workers covered by both union and non-union agreements benefited, the benefit for those covered by non-union agreements was about a third lower. We should be very cautious about interpreting the latter as representing non-union members generally: non-union agreements cover barely 5% of all workers on enterprise agreements, and only 1.3% of all non-union employees. But even amongst this group, a significant portion of the benefits from increased worker bargaining power have accrued to non-members.

The overall conclusion that can be drawn from these sources is that the wage gains associated with increased worker power are *not* just restricted to union members. They are also experienced by non-members, who themselves obtain an increase in wage bargaining power, but it is likely not as large an increase as is experienced by union members.

Conversely, the loss in worker bargaining power arising from policy changes in early years likely affected both union members and non-members adversely, albeit with a larger effect on union members.

Conclusions: power, markets and wages

In *Silver Blaze*, Sherlock Holmes solves the mystery and the horse is found and returned.[64] So it is that the mystery of low wages growth can be solved and wages, in part at least, have returned to growth rates of a recent past — though there is still a long way to go. Real wages in December 2024 had recovered to be at the same level as December 2011. There was still the 15.1% gain in labour productivity[65] between those dates to be made up, and then whatever subsequent growth in productivity had occurred by that time wages catch up to that.

Changes in the economy and the labour market over the past half century have almost unanimously reduced workers' power, some dramatically. The total effect is substantial: an unambiguous reduction in workers' power. The return of unemployment to the levels it was at half a century ago has not offset the tremendous loss of power caused by other economic and labour market factors over that period.

The substantial movement in power over that half century has meant that workers can no longer extract the wage increases that they previously could from wage negotiations, especially at times of high inflation. Unlike in the 1970s, they simply do not have the bargaining power to prevent real wage declines during periods of rapidly rising prices. Nor, consequently, do they play any role in intensifying inflationary pressures or even threatening to do so. Power has been partially returned to workers without any evident increase in inflation.

On average, provisions to increase workers' power have been far more common under Labor governments than under Coalition governments, and provisions to reduce workers' power have been more common under Coalition governments. In the end, the one countervailing force in recent times has been public policy which, since 2022, has sought to increase workers' power. Compared to the impact of the underlying economic and labour market forces that have reduced workers' power, these legislative changes are small. Wider changes to the socio-economic order would be necessary to alter that. However, the changes that have been made have been enough to significantly increase the rate of nominal wages growth for both unionists and non-union workers, and sufficient to at least see a return to real wage growth in recent years.

Wages may not yet have recovered as well as *Silver Blaze* did, but it is a start.

[64] I apologise if this spoils the ending for some, but you have had 131 years to read the story. Anyway, I haven't told you who stole the horse, let alone about the murder.
[65] Measured by gross value added per hour worked in the market sector. ABS 5206.0 Australian National Accounts: National Income, Expenditure and Product, Table 1. Key National Accounts Aggregates.