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POLICY **BRIEF**

NO. **004**

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KEY POINTS

- Nations use minimum wage policies to ensure individuals can maintain a minimum quality of life.
- When labour is priced at a higher rate, employers will generally want to use less of it and workers will generally want to supply more of it.
- Research has shown that increase in minimum wage is always followed by reductions in employment.

How Realistic is the Cry for Raising Minimum Wage in Nigeria?

The current minimum wage rate in Nigeria of N18,000 was implemented in 2011 and it was equivalent to $116.99 at that time. However, with the current official exchange at N306, the minimum wage of N18,000 is now equivalent to $58.82 implying a 49.72% decline in the purchasing power of an average Nigerian worker. Cumulatively also, prices of commodities as measured by Consumer Price Index have risen by 77% within the period. Both measures therefore show that the pay of a Nigerian worker has declined substantially in the face of changes in market conditions and high cost of providing basic needs.

Hence, the recent cry to increase minimum wage to N56,000 appears justifiable. But there is another side to the issue of minimum wage deriving from the eco-nomics perspective on the minimum wage generally and the current reality in Nigeria.

Governments set minimum wage as the lowest remuneration permitted by law that employers must legally pay their workers. Nations use minimum wage policies to ensure individuals can maintain a minimum quality of life. In general, there are two fiscal and social arguments on minimum wage. Supply side economists see a minimum wage as an overreaching burden placed on small business while demand side economists argue wages set too low will result in higher levels of poverty. Also, if the minimum wage is increased by the government, more skilled and educated workers will also seek pay increases not because of market forces but government policy. This increases volatility in the labour market as experienced and skilled workers are forced to reassess their value upward which may not be accepted by employers.

Dominant economic argument against minimum wage is that when labour is priced at a higher rate, employers will generally want to use less of it (underdemand for labour) and workers will generally want to supply more of it (oversupply of labour), leading to a gap between offers of work and opportunities for work. The long run effect is that businesses have an opportunity to substitute away from labour towards capital intensive modes of production. Hence, labour-saving capital investment becomes more attractive when low-skilled workers are more expensive by minimum wage laws. Hence, the minimum wage law increases wages but decreases employment.

Researches in some countries have found that increases in the minimum wage were followed by reductions in employment. This was more pronounced among young people, where minimum wage had a large effect on labour demand. Thus, a consistent negative relationship exists between the minimum wage and labour demand.

Based on the current economic reality in Nigeria where unemployment rate is already high at 13.9% in Q3 2016, cost of production is equally high and government revenue has fallen resulting in debt accumulation, one would be right to doubt the capacity of the economy to accommodate a wage increase. In addition, many state governments have been unable to pay the present mini-mum wage and are even owing months of salaries, most businesses are still paying far below the existing wage rate. Despite all these, inflation is still high at 17.26% as at March, 2017.

Balancing these arguments, which it may be difficult to argue against the current demand for wage rate increase; but great care and timing need to be exercised. In the short term, the government may wish to first stabilise the economy and raise its absorptive capacity. The increase in wage rate can be delayed to the medium term when the inflationary and exchange rate pressures will be much more under control. Finally, the long-term solution is not higher minimum wage but increase in labour productivity, improved competitiveness, lower prices and a vibrant private sector that generates qualitative jobs.

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