Australian Government
Productivity Commission

Wage Decoupling in Australia: A Forensic Look

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Recent Productivity Trends

- Over the last decade, Australia's productivity growth has averaged just 1.1 per cent per year – the slowest growth rate in 60 years.
- Over the year to June, productivity went backwards by 3.6 per cent.
- In the five quarters since March 2022, labour productivity has declined in all but one.
- GDP per hour worked is now at its lowest level since March 2016.

Wage Decoupling?

- Some have questioned the importance of productivity growth in driving real wages, pointing to the phenomenon of ‘wage decoupling’ that has emerged in some advanced economies.
- The policy implication seems to be that sustained real wage increases can be secured with little or no reference to productivity growth – and that productivity-enhancing reforms don’t matter for living standards and should not be pursued.
- Others point to factors such as the characteristics of recent technological change, or more malign factors such as the existence and misuse of market power in labour or goods markets – with consequences for tightening up competition policy or labour market regulation.

Our Research

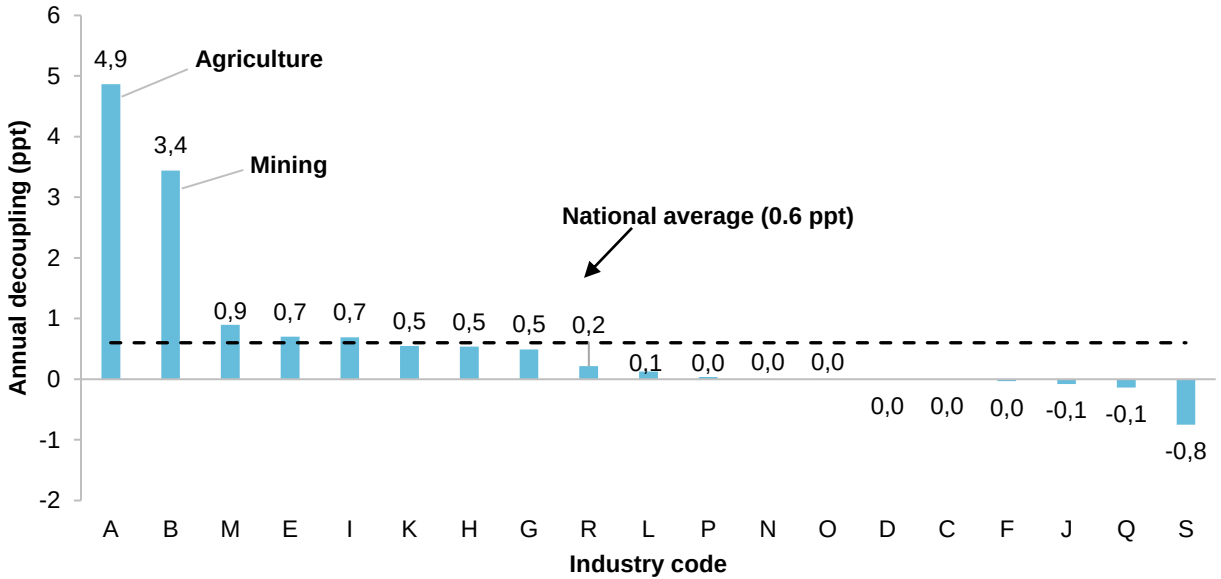
- Our research examines aggregate wage decoupling - defined as average annual labour productivity growth minus average annual producer wage growth.
- It shows that the link between productivity and real wages is robust.
- But to properly understand the Australian situation, we need to look beyond the aggregates.

Findings

- Since 1995, only two sectors have exhibited strong wage decoupling: mining (4.9 percentage points) and agriculture (3.4 percentage points).
- These two commodity-exporting – and highly productive – sectors account for a combined 4% of total employment, but around 18% of total value added. They therefore have a disproportionate impact on economy-wide estimates of wage decoupling.
- If we strip them out and examine the rest of the economy, average decoupling since 1995 has been just 0.1 percentage points. In more than half of the sectors outside of mining and agriculture, decoupling has been zero or negative.

Figure 1

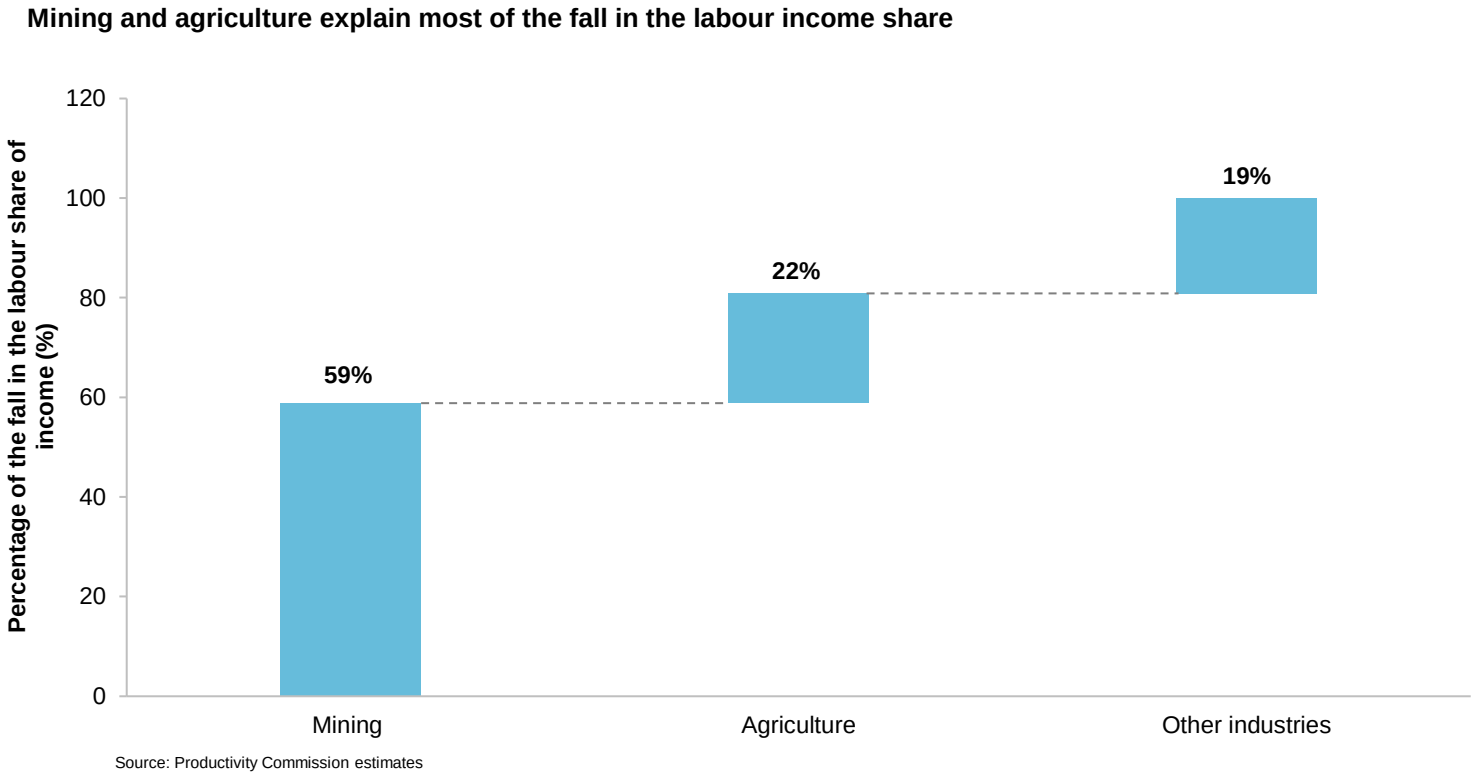
Wage decoupling is noticeably high in 2 of 19 industries, (1995–2022)[a,b,c]



a. Wage decoupling is expressed in percentage points as the average annual labour productivity growth minus average annual producer wage growth, over a defined period (27 years in this paper). **b.** Nominal wages are compensation of employees per hour. Compensation of employees for each industry is in the national accounts, but hours worked by employees needs to be derived by multiplying the share of hours worked by employees (as opposed to those worked by owner-managers of unincorporated enterprises) in the *Labour Force Survey* by the total hours worked for the industry in the *Labour Account*. **c.** Industry codes are: Agriculture, forestry and fishing (A); Mining (B); Manufacturing (C); Electricity, gas, water and waste services (D); Construction (E); Wholesale trade (F); Retail trade (G); Accommodation and food services (H); Transport, postal and warehousing (I); Information media and telecommunications (J); Financial and insurance services (K); Rental, hiring and real estate services (L); Professional, scientific and technical services (M); Administrative and support services (N); Public administration and safety (O); Education and training (P); Health care and social assistance (Q); Arts and recreation services (R); Other services (S).

Source: Productivity Commission estimates using: ABS (*Australian System of National accounts, 2021-22*, Cat. no. 5204, table 6; *Labour Account Australia, March 2023*, Cat. no. 6150.0.55.003, industry summary tables; *Labour Force, Australia, Detailed, April 2023*, Cat. no. 6291.5.001, table EQ05).

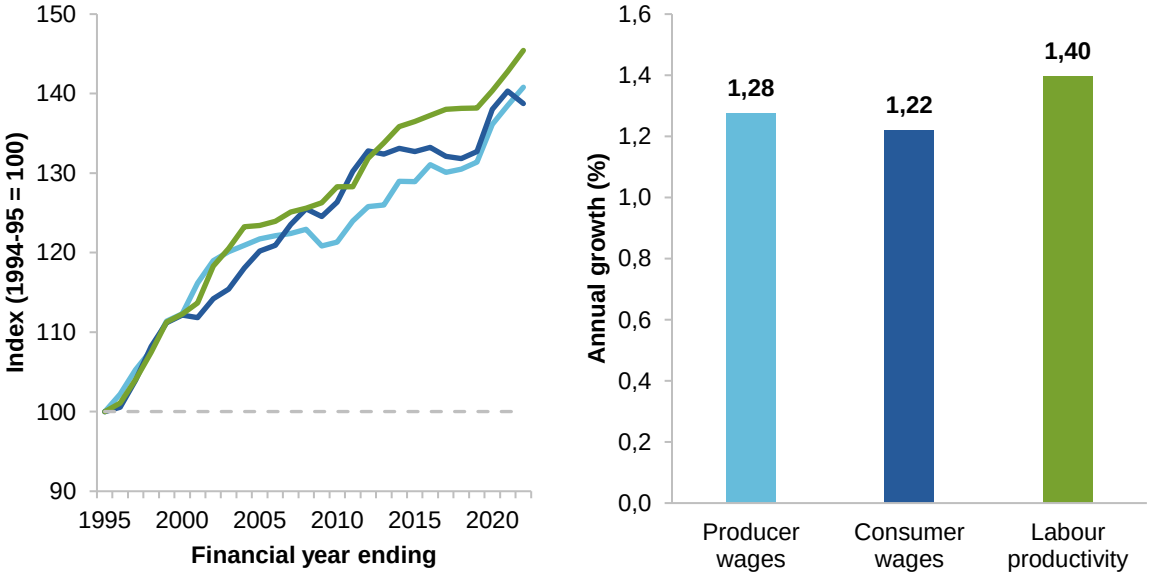
Figure 2



Source: Productivity Commission estimates

Figure 3

A smaller gap between labour productivity and real wages for 95% of employees[a,b,c]

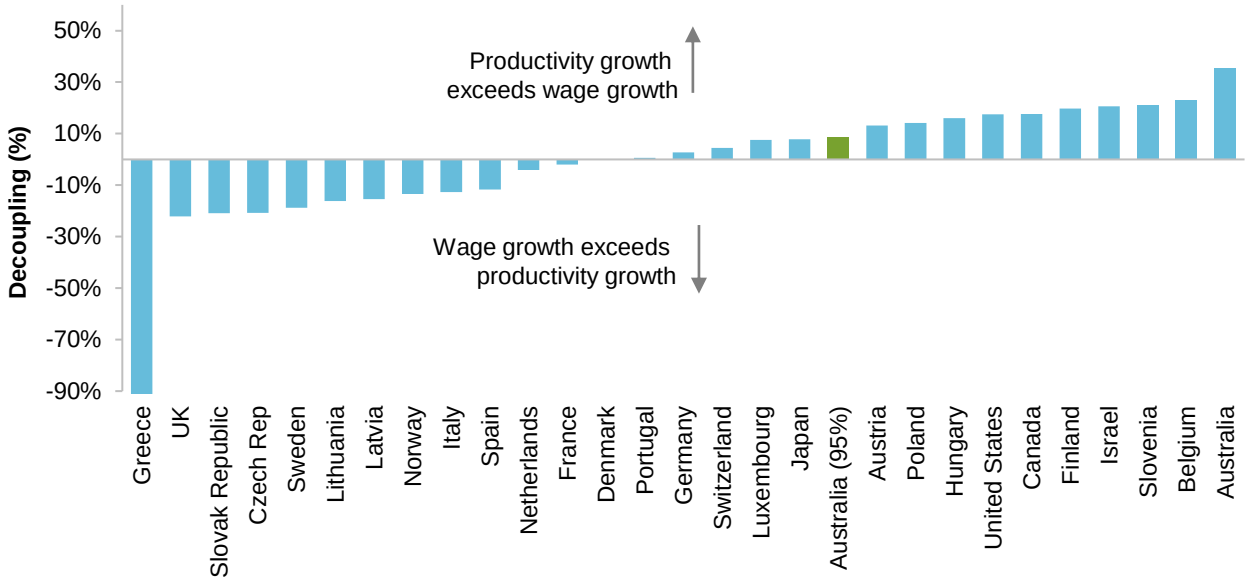


a. The industries excluded are Mining and quarrying, and Agriculture, forestry and fishing. All other Division (1 digit) industries of the Australian and New Zealand Standard Industrial Classification are included. **b.** Methodology outlined in appendixes A and B.1. **c.** Producer wages are wages deflated by producer prices (GVA deflator) and consumer wages are wages deflated by consumer prices (consume price index). Labour productivity is defined as GVA per hour (for all industries other than mining and agriculture) rather than GDP per hour.

Source: Commission estimates using: ABS (Australian System of National Accounts, 2021 22, Cat. no. 5204.0., table 46; Labour Account Australia, March 2023, Cat. no. 6150.0.55.003., industry summary tables; Labour Force, Australia, Detailed, April 2023, Cat. no. 6291.0.55.001., table EQ05; Consumer Price Index, Australia, Cat. no. 6401.0., table 1).

Figure 4

The international experience of decoupling is varied[a]



a. Decoupling is measured as the percentage difference between annual growth rates in labour productivity and real producer wages over the period from 1995 to 2020 with the exception of Canada (1997–2018) and the United States (1997–2020).

Source: Productivity Commission estimates, OECD (2023).

‘Recoupling’ Versus Productivity Enhancing Reforms

- Since 1995 the wages of over 95% of Australia’s working population have risen very closely in line with productivity.
- Moreover, our research shows that productivity-enhancing reforms are likely to be far more effective at boosting incomes than measures targeted at wage decoupling.
- Even in the presence of 0.1 percentage point decoupling, if productivity growth had returned to rates previously seen in the 1990s (of 2.2%) then average real incomes would today be around $25,000 higher than current levels.
    - If, instead, productivity remained constant, but the wage decoupling gap was completely closed for the 95%, average real incomes would today be around $3,000 higher.

Figure 5

Average wages in 2023 under various productivity growth and wage decoupling scenarios[a]

Wage decoupling (percentage point) \ Productivity growth (%)	0	1	1.4	1.8	2.2
-0.20	$79,903	$104,474	$116,090	$129,223	$143,626
-0.10	$77,778	$101,722	$113,044	$125,845	$139,887
0	$75,707	$99,040	$110,075	$122,553	$136,241
0.10	$73,689	$96,426	$107,181	$119,344	$132,687
0.12	$73,277	$95,893	$106,590	$118,689	$131,962
0.18	$72,112	$94,383	$104,919	$116,835	$129,909
0.20	$71,723	$93,879	$104,360	$116,216	$129,223

a. The table shows real wages in 2023 under various productivity growth and wage decoupling scenarios, assuming a starting annual salary of $75,706 in 1995.

Source: Productivity Commission estimates

Conclusion

- In other words, the average income gain from a productivity lift is more than eight times the potential gain from eliminating the limited decoupling across most of the economy.
- Productivity growth remains the best way – and in the long run, the only way - for policymakers to increase real wages, improve living standards and guarantee Australia's future prosperity.

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