

MINIMUM WAGE POLICY EFFECTS ON ECONOMIC GROWTH

By

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ABSTRACT

The purpose of this study is to examine the relationship between minimum wage policy and economic growth for the period 2000 – 2005. To achieve the objective, we estimate a growth model by employing the panel ordinary least square (OLS) and panel estimated generalized least square (EGLS) method. A sample consists of 61 countries with and without minimum wage and 33 were used in this study. For the minimum wage measure, we used minimum wage dummy, excess wage and minimum wage ratio to GDP as separate variables. We also include additional variables namely initial GDP, population growth, investment, trade openness, government expenditure and gross enrolment ratio. The results of the study show that, first, countries with minimum wage policy have higher economic growth. Second, the level of minimum wage does not affect economic growth for the countries that have the minimum wage policy. Based on the findings, countries should implement minimum wage policy since it would increase income for the worker and at the same time have positive effect on economic growth. The results also support the minimum wage policy that will be implemented in Malaysia.

ABSTRAK

Tujuan utama penyelidikan ini adalah untuk mengkaji hubungan di antara polisi upah minimum dan pertumbuhan ekonomi bagi tempoh 2000 – 2005. Untuk mencapai objektif ini, kami menganggarkan model pertumbuhan dengan menggunakan kaedah panel kuasa dua terkecil biasa (OLS) dan panel kuasa dua terkecil umum (EGLS). Sampel yang digunakan di dalam penyelidikan ini terdiri daripada 61 buah negara yang mempunyai dan tidak mempunyai upah minimum dan 31 buah negara yang mempunyai upah minimum. Untuk mengukur upah minimum, kami menggunakan dumi atas patung upah minimum, upah lebihan dan nisbah upah minimum kepada KDNK sebagai pembolehubah yang berlainan. Kami juga menggunakan pembolehubah bebas tambahan iaitu KDNK asal, pertumbuhan populasi, pelaburan, keterbukaan perdagangan, perbelanjaan kerajaan dan kadar *enrolment* kasar. Keputusan kajian menunjukkan bahawa pertama, negara yang mempunyai polisi upah minimum mempunyai kadar pertumbuhan ekonomi yang lebih tinggi. Kedua, tahap upah minimum tidak mempengaruhi pertumbuhan ekonomi bagi negara yang mempunyai upah minimum. Berdasarkan kepada penemuan ini, negara seharusnya melaksanakan polisi upah minimum disebabkan polisi ini boleh meningkatkan pendapatan pekerja dan pada masa yang sama memberi kesan yang positif terhadap pertumbuhan ekonomi. Hasil kajian juga menyokong pelaksanaan polisi upah minimum di Malaysia.

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LIST OF ABBREVIATIONS

BLUE	Best Linear Unbiased Estimation
CPS	Current Population Survey
COTU	Central Organization of Trade Unions
EGLS	Estimated Generalized Least Square
ENROL	Gross Enrolment Ratio
EW	Excess Wage
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GOVEXP	Government Expenditure
GR	Growth Rate
GSP	Gross State Product
ILO	International Labor Organization
INIGDP	Initial GDP
INV	Investment
MEF	Malaysia Employees Federation
MW	Minimum Wage
MWD	Minimum Wage Dummy
MWRATIO	Minimum Wage Ratio
OECD	Organization for Economic Cooperation and Development
OLS	Ordinary Least Square
POPG	Population Growth
OPEN	Trade Openness
UNESCO	United Nations Educational, Scientific and Cultural Organization

CHAPTER ONE

INTRODUCTION

1.1 Introduction

'Why, when the economist gives advice to his society, is he so often coolly ignored? He never ceases to preach free trade...and protectionism is growing in the United States. He deplores the perverse effects of minimum wage laws, and the legal minimum is regularly raised each 3 or 5 years.' – George Stigler, cited in Rustici (1985).

According to international standards, the minimum wage is the lowest monetary value which may be paid to workers in a region and a point of time, either through existing acts or through collective bargaining. In some countries the minimum wage is determined by law, while in others it is determined through dialogue or negotiation, or through collective agreements between workers and employers. The minimum wage has the purpose of safeguarding the income and living conditions of workers who are considered to be the most vulnerable in the labor market.

The minimum wage has long been a controversial issue since its passage in the Fair Labor Standard Act of 1938. Most of the economists argue that the minimum wage may price out low-skilled workers, discriminate against minorities, and cause unemployment to rise. However, its supporters typically argue that it actually can reduce poverty and increase the income of the lowest-paid workers.

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