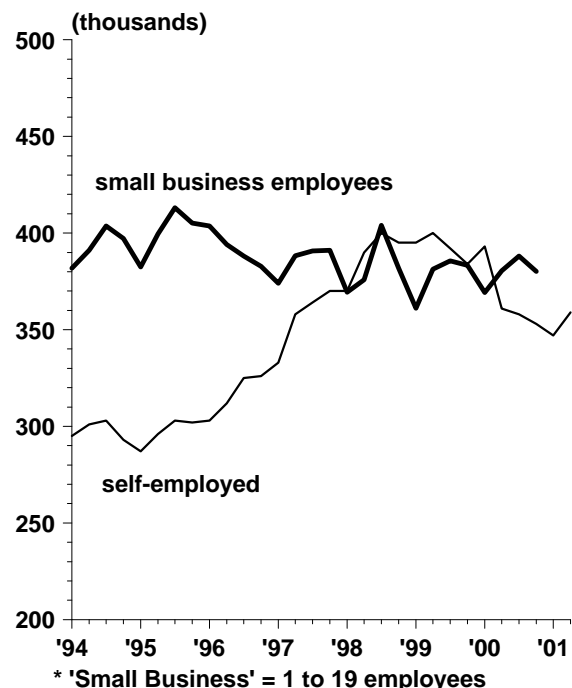


## Small Business Quarterly ♦ Second Quarter 2001

- The number of self-employed in British Columbia rose 3.5% from the first to the second quarter of 2001, almost regaining all the ground lost over the last year. This was despite a 2.1% drop in the number of self-employed persons with employees of their own. The number of self-employed persons without paid help jumped 6.0% from the previous quarter to its highest level since the first quarter of 2000.
- The number of small businesses in British Columbia (excluding self-employed persons) was unchanged in the second quarter compared to the same period in 2000. Micro-businesses (i.e., those employing less than 5 people) increased 1.5%, but all other size categories experienced some decline. Businesses with 5 to 9 employees fell 1.7% and the number of businesses with 10 to 19 employees dropped 5.6%. The largest decline was in the 20 to 49 employee category, which fell 6.1%.
- New business incorporations were down almost 9% in the second quarter 2001 compared to the same quarter in 2000 continuing a yearlong trend.
- Both business and consumer bankruptcies in the province fell slightly from the first to second quarter of 2001, but both are still much higher than the same period a year earlier. Business bankruptcies were down 0.7% and consumer bankruptcies fell 0.8%, but were respectively 11.7% and 5.7% higher compared to the second quarter of 2000.
- The prime rate dropped an entire point between the second quarter of 2000 and

the same period in 2001. It fell 75 basis points from the first quarter to the second quarter 2001 and has since declined further. Despite the lower cost of borrowing, chartered bank business loans in British Columbia have continued to shrink, dropping 10.6% over the last year.

**Employees in B.C. Small Businesses, \*  
and Numbers of Self-Employed**



## The Benefits and Costs of a Higher Minimum Wage

The recent changes to the British Columbia minimum wage have rekindled the debate regarding its effects and effectiveness. As of November 1, 2001, the BC minimum wage was raised from \$7.60 an hour to \$8.00 an hour. In addition, a “first-job” wage rate of \$6.00 an hour was established effective November 15.

Supporters of minimum wage policy suggest that not only does it ensure fair pay, but it also helps redistribute wealth to the poorest in society. Also, increases to the minimum wage can create incentives to enter the labour force.

Critics of minimum wage policy suggest that the minimum wage is a poor method of redistributing income and it also tends to hurt the very people it is intended to help. They suggest that hikes in the minimum wage inevitably lead to reductions in employment as the increased cost to business forces employers to either reduce the number of employees or at least cut the number of hours per employee. Another argument against raising the minimum wage is that, in British Columbia, it is already the highest in Canada, and higher than that of other nearby competitors. It is also suggested that most of the beneficiaries of increased minimum wages do not reside in low-income households. Rather, they are young people living with their parents, or second-earners in a dual-income family.

There are numerous studies that examine the effect of minimum wage increases on businesses and employment, but many of these studies have contradictory findings. In reality, the effects of minimum wage increases depend on a large number of variables, which means that the findings of any one study may not be applicable to a particular place or a particular time.

### Employment Impacts

According to an OECD report based on a 1998 study of minimum wage changes in nine countries,

a 10% increase in the minimum wage is associated with a 1½–3% decline in teenage employment...The evidence also shows that hikes in the minimum, on their own, can explain only a small fraction of the large falls in teenage employment rates observed over the past two decades in almost all countries. The cross-country evidence suggests that the minimum wage has no significant impact on overall employment.<sup>1</sup>

This suggests that employment impacts depend on a variety of circumstances and it is misleading to suggest that a raise in the minimum wage will necessarily lead to widespread job loss.

The impact on youth employment may be due to businesses being able to attract more experienced workers at the higher wages, leaving less-experienced younger workers with fewer opportunities. Another possibility is that employers may find ways to do without some of the younger, less-skilled employees, either by substituting capital or increasing the workload of other employees.

It has been argued that a lower training wage, like BC's new first-job wage rate, may be one way to help alleviate youth unemployment. The rate applies to the first 500 hours worked in any job. Once a person has recorded 500 hours of employment, any further work they do, for either their current employer or a future employer, must be paid at least at the regular minimum wage.

Proponents of this wage rate, like the BC Restaurant and Foodservices Association and the Retail Merchants' Association of

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<sup>1</sup> “Towards an Employment-centred Social Policy,” *The OECD Observer No. 213* (August/September 1998).

BC, say that this lower training wage will encourage the hiring of teens and enable young people with no experience to get work.

Those against the new first-job rate, including various labour groups such as the BC Federation of Labour, suggest that the new wage rate is open to abuse. They point out that there is nothing to prevent an employer from terminating an employee once they reach 500 hours and hiring someone else at the lower rate. They also suggest that some people may choose to take the lower rate even though they have worked over 500 hours rather than risk losing their job.

A differential minimum wage for younger, unskilled employees is also in place in Ontario, Nova Scotia and the territories.

### Comparison with other jurisdictions

British Columbia's minimum wage was already the highest in the country before the recent increase to \$8 an hour, but it is not necessarily higher than rates in the United States. With a simple exchange rate comparison, the United States' federal minimum wage of \$US 5.15 an hour is close to \$8 as well (using a Canadian dollar worth in the range of \$0.62-\$0.65 US dollars). In fact, in neighbouring Washington State, the minimum wage is \$US 6.72 or about \$10.35 in Canadian dollars (at an exchange rate of \$0.65). There is a proposal to raise the federal minimum wage in the United States to \$6.65 by 2003. This is well over \$10 an hour in Canadian currency at current exchange rates.

However, exchange rate comparisons ignore the differences in the cost of living between jurisdictions. A better method for comparing wages in different currencies is to examine their purchasing power parity (PPP). PPPs are rates of currency conversion that eliminate the differences in price levels between countries. Based on comparative price levels developed using a July 2001 PPP, the \$8 BC minimum wage is well above the federal US minimum wage (ap-

proximately \$6.44 after adjustment), but is still below that of Washington (\$8.40), Oregon (\$8.13) and California (\$8.44), as well as some other states. A concept similar to PPP is not readily available to compare provincial price levels, but based on Statistics Canada studies of retail price differentials, the minimum wage gap is likely somewhat narrower than it appears, although the BC wage would still be the highest in the country.

A look at the minimum wage over time adjusted for inflation using the Consumer Price Index shows that even at \$8 an hour, the minimum wage is still significantly below its peak in the mid-seventies. This means that the increased labour cost to businesses paying minimum wage has been less than the overall rate of inflation over the last 25 years.

### Inflation has eroded minimum wage



Although the evidence does not support complaints that minimum wage hikes create serious disemployment effects and arguments about competitive disadvantages are less clear-cut than they appear, there is still the question of whether or not the minimum wage is a good tool for income redistribution.

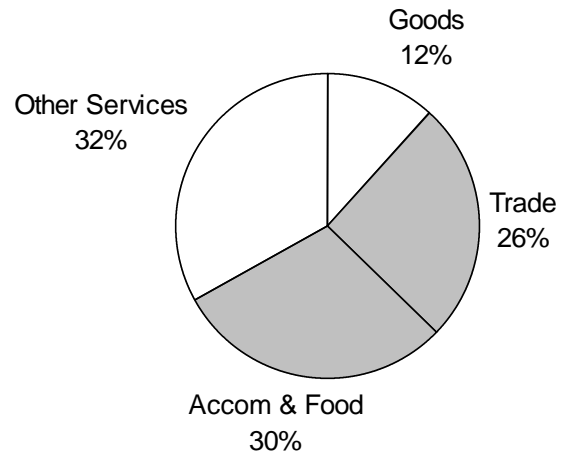
## Profile of minimum wage earners

Detractors of minimum wages argue that raising the minimum wage will not help the poor because most minimum wage earners are middle-class teenagers living at home or secondary earners in dual-income families. The profile of the minimum wage earner may support this view, although the numbers would have to be examined in more detail to come to a definitive conclusion.

Based on Statistics Canada data, in 2000, 61% of minimum wage earners in British Columbia were adults (i.e., over 19) and almost 45% were over 25. Approximately two thirds of all minimum wage earners were in dual earner families, and about 14% were single earners with one or more children under 18 years old.

Although there is little data available to examine minimum wage earners by business size, a majority of the businesses in the industries in which minimum wage jobs are most prevalent are classified as small businesses. The large majority of minimum wage jobs are in the service sector (88%), particularly in accommodation and food (30%) and retail and wholesale trade (25%). It is no surprise then, that the restaurant industry is one of the most vocal opponents of minimum wage increases, particularly since many of their employees receive tips to supplement their wages and therefore are actually making more than the minimum wage. One approach to alleviate this concern that has already been implemented in Quebec and Ontario is to have a lower minimum wage for those people who regularly earn tips to supplement their income.

## Most minimum wage jobs are in the accommodation & food or trade sectors



## Alternative redistribution methods

The clear beneficiaries of minimum wage hikes are those workers earning minimum wage, but the main criticism is that many of these workers are in households with incomes above the median, while those households with no workers do not benefit at all. While higher minimum wages may achieve the goal of ensuring fair pay, they may also fail at the second goal of redistributing income.

The BC Chamber of Commerce suggests that an alternative to raising the minimum wage is to offer more tax credits to lower-income families. The usual criticism of this kind of strategy is that these families do not pay much tax, if any, to begin with. Another problem with offering tax credits in lieu of better wages is that it operates as a subsidy to businesses that pay lower wages, possibly at the expense of those businesses willing to pay higher wages.

The OECD suggests that policies on minimum wages and tax/benefit systems should not be considered separately, but rather as complementary parts of an overall system designed to redistribute income. An example of this would be to combine a minimum wage increase with a payroll tax deduction. This would have the effect of not only boosting the earnings of low-income work-

ers, but also allowing them to keep more of that income instead of putting it toward payroll taxes. Also, it would offset the cost of the salary increase for businesses since they would no longer have to pay as much in payroll taxes.

Of course, such a policy would have to be implemented carefully. Too much of a wage increase could not only lead to a reduction in employment for some portions of the labour force, but could also cause a significant rise in inflation. Too much of a decline in payroll taxes could leave the programs they are supporting (such as the Employment Insurance program) vulnerable to downturns in the economy.

### **Conclusion**

The effects of changes to the minimum wage tend to be exaggerated by both detractors and supporters. There are many factors that must be considered in determining the effect of a minimum wage in-

crease, including the size of the wage bump, the business cycle, the kind of tax and benefit systems in place, and the labour supply, just to name some.

This last item will become increasingly important over the next decade. Demographers agree that North America is facing a labour shortage in the coming years as the proportion of working-age population declines relative to that of retirement age. This could make the entire minimum wage debate moot, as employers will need to raise wages to attract scarce labour.

On its own, a minimum wage hike may not be the best method of redistributing income and may actually have some disemployment impacts on the younger members of the labour force. A policy that combines an increase to the minimum wage with a decline in payroll taxes could have benefits for both low-income people and small business.

## Feature Articles Listed by Issue Number

**01-1:** *'Small Business On-Line: Internet Use Among SMEs'* (released Sept. 2001)

**00-4:** *'Co-operatives Grew Steadily Throughout the 1990s'* (released May 2001)

**00-3:** *'Profile of Self-Employed in British Columbia'* (released Mar. 2001)

**00-2:** *'Latest Small Business Employment Numbers Show Three Year Changes'* (released Jan. 2001)

**00-1:** *'Some Distinctive Features of The Small Business Workplace'* (released Oct. 2000)

**99-4:** *'Transfers of Corporate Charters to Other Provinces Suggest Business Migration From British Columbia'* (released July 2000)

**99-3:** *'755 Thousand British Columbians Rely On Small Businesses For Jobs'* (released Mar 00)

**99-2:** *'A Quarter of All Employees In British Columbia Work For Small Employers'* (released Nov 99)

**99-1:** *'Self-Employment In British Columbia Takes On New Profile'* (released Sep 99)

**98-4:** *'Co-Operative Movement Grows Through the 1990s'* (released Apr 99)

**98-3:** *'The Long and the Short of Working Hours For Self-Employed'* (released Dec98)

**98-2:** *'People Trying Self-Employment As A Second Job'* (released Aug 98)

**98-1:** *'British Columbians Still Making Their Own Jobs'* (released May 98)

**97-4:** *'Business Bankruptcies Ease With Low Interest Rates, But Consumer Bankruptcies Continue to Climb'* (released Mar 98)

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**97-2:** *'Doing Our Thing In Lotusland - The New Self-Employed In British Columbia'* (released Sep 97)

**97-1:** *'Immigrants Boost Self-Employment In British Columbia'* (released Aug 97)

**96-3:** *'Changes in Business Confidence Expressed In Numbers of New Incorporations'* (released Mar 97)

**96-2:** *'Bankruptcies Rise With Self-Employment and Mounting Consumer Debt Loads'* (released Oct 96)

**96-1:** *'Counting the Business Community in British Columbia'* (released Jul 96)