HOUSING INDUSTRY ASSOCIATION

Submission to the
Fair Work Commission

National Annual Minimum Wage Review 2023

31 March 2023

HOUSING INDUSTRY ASSOCIATION

contents

Housing Industry Association

1. INTRODUCTION

The residential building industry is one of Australia's most dynamic, innovative and efficient service industries and is a key driver of the Australian economy.

The aggregate contribution from the industry to the Australian economy was over $110 billion per annum in 2022, with over one million workers in the construction industry, of which tens of thousands are small businesses reliant on the industry for their livelihood.

The residential building industry is one of the most important sectors of the Australian economy providing housing for millions of Australians. A home is often the greatest source of wealth and savings for many families. The industry contributes to the economy in a number of ways providing hundreds of thousands of Australians with jobs, generating billions of dollars of economic output each year and stimulating spending on housing services.

The residential building industry ranges from single dwelling construction to multi-unit apartment buildings, and also encompasses the home renovations market. The industry has important linkages with other sectors, such as manufacturing and retailing, so that its impacts on the economy go well beyond the direct contribution of construction activities. The flow-on or "multiplier" effects of construction activity on the outputs of other industries are well recognised.[1]

HIA submits that for its 2022-2023 Annual Wage Review, the Expert Panel should consider the following specific issues confronting the residential building industry:

- The industry's economic performance, including productivity, viability, inflation and employment growth, particularly in light of the economic downturn;
- The impact of natural disasters and world events;
- Broader societal issues such as housing affordability and housing supply that are essential to maintaining adequate living standards and which should also be taken into account considering the public interest.

1.1 IMPACT OF NATURAL DISASTERS AND WORLD EVENTS

The residential building industry has been severely impacted over the last few years as a result of various issues, including the pandemic, flooding in Northern NSW, Queensland and South Australia, as well as the ongoing Ukraine/Russia Conflict. In 2022, the industry saw significant impacts as a consequence of supply chain issues for building products, labour supply issues and the increased pressure on prices due to inflation and fuel prices.

These issues impacted not only existing home building contracts, but future projects. The supply chain is severely stretched, with many building components regardless of their place of manufacture, being in short supply. The industry had expected, and hoped, to see an improvement in these ongoing pressures in 2023, however these recent world and local events mean that the existing pressure on labour supply and delays in materials availability will now stretch well into 2023.

[1] See speech by Christopher Kent, Assistant Reserve Bank Governor for a summary of the importance of housing to the Australian economy: http://www.rba.gov.au/speeches/2013/sp-ag-140313.html

1.2 OTHER FACTORS

A vast majority of employers in the industry are small businesses. These employers have been hit the hardest by the changing economic conditions and rely heavily on award rates of pay and terms and conditions. They operate in a very competitive market where costs are tightly controlled and profit margins are low. These employers are highly sensitive to economic conditions affecting them, including the effects of employment regulation and wage increases.

Whilst measured increases to household income may help alleviate some affordability stresses, ongoing labour input costs and supply chain issues in the construction of housing, without any link to productivity improvements, will impact project costs. This in turn affects housing affordability. Increases in wages inherently place added cost pressures on businesses making them less likely to grow, invest or take on additional employees. This can also create demand side implications including tightening the supply of existing skilled trades and reducing the entry of new apprentices to the industry placing further pressure on existing businesses to meet demand.

Wage decisions also have implications for interest rate decisions by the RBA and may complicate the RBA's attempts to reign in inflation. Higher inflation can require higher interest rates for longer, with negative consequences for household finances, businesses in home building and other industries, and for housing affordability. This is explained further in item 2.1 below.

Additionally, there are further increases to the superannuation guarantee contribution which many employers are required to pay to employees, if employees have been hired on a salary plus superannuation basis. The Expert Panel should be mindful that the contributions will increase from 10.5% to 11% in 2023 and will reach 12% by 2025. HIA submits that the Expert Panel should take the further increase in the superannuation guarantee into account in this annual wage review

1.3 APPROACH TO MINIMUM WAGE INCREASE IN RECENT YEARS

In recent years, the Expert Panel has taken a more nuanced approach to the implementation of the minimum increase in light of the COVID-19 pandemic and other factors. This included a staggered approach in 2021 and a delay to the commencement of increases for certain modern awards, excluding modern awards applicable for the residential building industry, in 2022. Further, in 2022, the Expert Panel awarded a $40 a week increase for employees earning below $869.60 per week, whilst those earning above that amount received a 4.6 per cent increase to their wages.

With businesses continuing to be directly impacted, the economy is now experiencing a range of aftershocks of varying magnitude attributable to the pandemic and other world events, which are now compounded by the additional global developments.

While HIA strongly submits that a cautious approach be taken, if an increase is to be awarded, HIA would encourage the Expert Panel to, once again, take a more nuanced and conservative approach to any increase.

2. MINIMUM WAGES

In making a national minimum wage order, the Expert Panel must be guided by the minimum wages objective in section 284 of the *Fair Work Act 2009* (FW Act):

> *The Fair Work Commission must establish and maintain a safety net of fair minimum wages, taking into account:*

- *the performance and competitiveness of the national economy, including productivity, business competitiveness and viability, inflation and employment growth; and*
- *the need to achieve gender equality, including by ensuring equal remuneration for work of equal or comparable value, eliminating gender-based undervaluation of work and addressing gender pay gaps; and*
- *promoting social inclusion through increased workforce participation; and*
- *relative living standards and the needs of the low paid; and*
- *the principle of equal remuneration for work of equal or comparable value; and*
- *providing a comprehensive range of fair minimum wages to junior employees, employees to whom training arrangements apply and employees with a disability.*

HIA address those factors affecting the residential building industry below.

2.1 Performance And Competitiveness Of The National Economy

Since May 2022 the RBA has undertaken the steepest interest rate increasing cycle in a generation in an attempt to bring inflation back to target. Unfortunately, this will bring the volume of new detached homes commencing construction to its lowest level in more than a decade.

The RBA adopted a similar strategy after the GFC, increasing rates seven times in 2009 and 2010, creating a downturn in home building and having to start cutting the cash rate again in 2011. Again in 1994, they increased the cash rate rapidly and causing a two-year decline in home building activity before being forced to cut the cash rate again.

Similar to these two previous cycles, we expect the number of new detached home starts to fall by more than 40 per cent in response to the RBA's cash rate increases. Sales of new homes across Australia are already almost 50 per cent lower than a year earlier. The impact of the 2022 rate increases are not yet fully reflected in recent data. With further increases expected, the trough in new home sales may not be visible until mid-year.

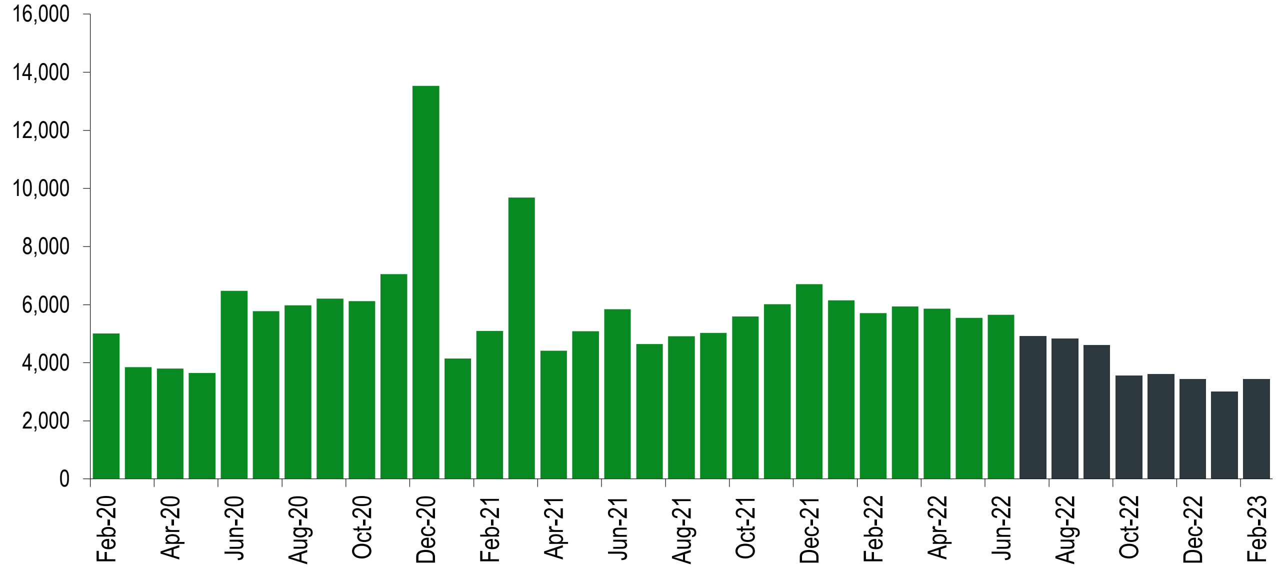
The number of detached homes commencing construction in 2022 (120,050) were already lower than in the previous year by 19.6 per cent. Despite the large decline, this remains the second largest number of detached starts in a year on record. After a further 8.9 per cent moderation in 2023, the weight of interest rate increases is expected to push this down by another 12.0 per cent to just 96,310 in 2024.

This would represent the weakest calendar year since 2012. A slow recovery is expected in 2025 with just 97,820 starts before the market recovers from this cycle with 105,179 in 2026.

Multi-unit starts remain very low, at or close to their lowest volume in a decade. The affordability constraints, a rental shortage and the return of overseas migrants has not been sufficient to offset the constraints on overseas investors or interest rates. It is anticipated there will have been just 69,480 starts in 2022, down by 15.1 per cent on 2021, as supply constraints have delayed the commencement of new projects. This is around the weakest levels for multi-unit starts since 2012. Starts are expected to bounce back by 13.3 per cent and 4.6 per cent to 82,360 in 2024. Modest growth is expected in 2025 and 2026 with 84560 and 86,410 starts respectively.

There remains a large volume of homes under construction at the start of 2023 and a volume of work that has yet to commence construction that has accumulated throughout the pandemic. This pipeline is expected to continue to shrink quickly as the adverse impact on rates increases starts to slow work on the ground in the second half of 2023. This will see the boom-and-bust cycle of the last couple of years continue with a trough of activity expected in late 2024 or early 2025.

Private New House Sales - Australia (SEASONALLY ADJUSTED)



Source: HIA New Home Sales Report

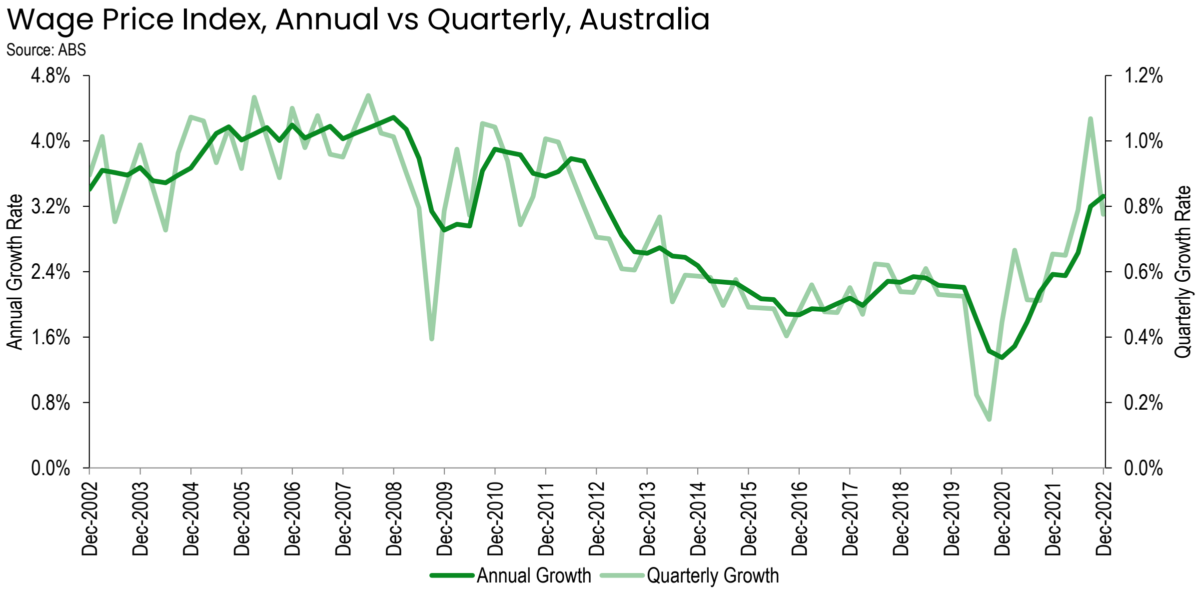
Beyond weighing on confidence in the new home market, the RBA is also compounding a problem that has been brewing for over a decade.

In the aftermath of the GFC financial market regulators embarked on a reform agenda which sought to ensure that Australia had an 'unquestionably strong' banking system. These reforms progressively tightened prudential standards and these are now restricting the extent to which banks can lend to households purchasing homes. They have restricted the amount that banks can lend to households with a given income, and households' access to financial products that provided flexibility such as interest-only lending. Reforms have also increased the costs to banks for home lending, especially to those with less than a 20 per cent deposit.

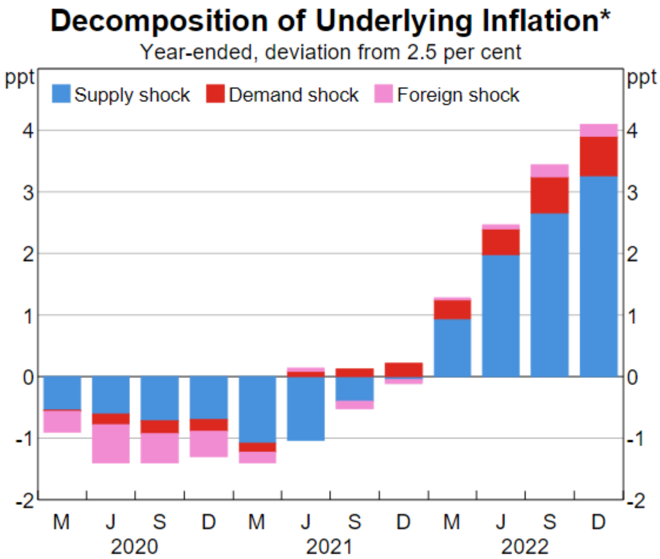
This tightening of lending standards was intended to address a problem that did not seem to exist in Australia. Mortgage delinquencies in Australia remained very close to zero through the GFC, the decade that followed and the pandemic. Part of the reason for this is that as macro-prudential restrictions have been tightened it has become increasingly attractive for banks to lend to those who are well capitalised. This typically means it is preferable to lend to someone who already owns a home rather than a first home buyer. The 'unquestionably strong' banking system has come at the expense of home ownership over the past decade.

The adverse impact of this belt and braces approach to lending has been obscured by the decline in interest rates over the past decade but the sudden increase in the cash rate in 2022/23 will draw attention to these exceptionally tight lending standards.

The RBA, and the HIA, are concerned that this short term, supply-side, inflationary cycle could feed into a 'wage price spiral' such as occurred in the 1970s and 80s.



Recent RBA data continues to confirm that this inflationary pressure remains on the supply-side, and should ease as global supply chains improve. The figure below shows that more than half of Australian inflation was driven by supply factors.



This contained, supply-driven inflation should be much easier for the RBA to bring back down than the wage-driven inflation of the 1970s and 80s.

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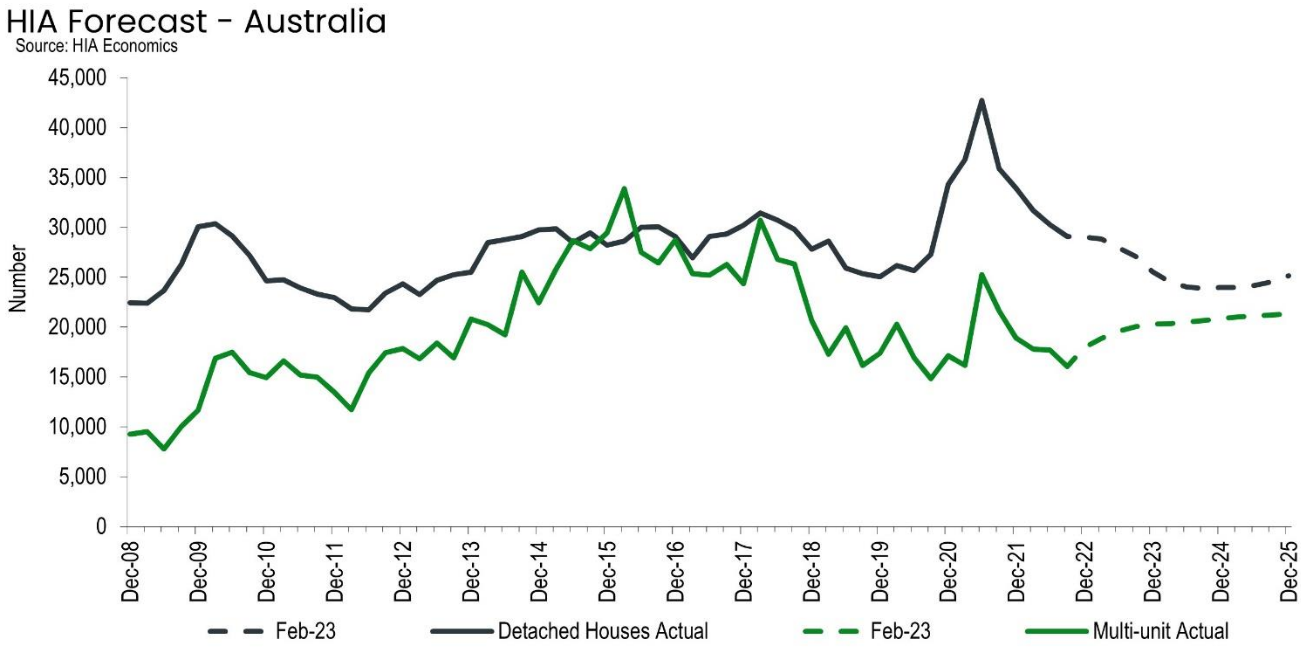
Unfortunately, this leads to a perverse outcome where the RBA continues to increase the cash rate and slowing new home commencements as as migration recovers and stimulates demand on top of the existing acute shortage of dwelling stock. The implications for longer term housing affordability are unambiguously negative.



2.2 WORKFORCE PARTICIPATION AND APPRENTICESHIPS

As noted above, the pipeline of detached house construction is expected to be exhausted in the first half of 2023. From this point, the volume of homes under construction will start to decline rapidly. Accordingly, it is critical that any minimum wage increase considers the current pipeline of works and the outlook for the industry, to ensure that businesses are not overstretched.

Apprenticeships are a common entry point into the residential building industry, however, labour shortages remain the worst on record.

Since the September quarter of 2021, the HIA Trades Availability index has recorded a trades shortage that is worse than all prior readings of the index, going back to 2003. Driven by this persistent shortage, the price of skilled trades rose by 9.4 per cent over the year to the December quarter 2022.

The shortage is evident across all regions. However, the shortage in regional Australia appears more persistent than in capital cities. Tellingly, the three areas with the worst shortages are Regional Western Australia (-1.31), Regional South Australia (-1.00) and Regional Queensland (-0.96). A feature of this pandemic boom has been a shift to lower density areas, including in Australia's regions.

The shortage is also evident across all trades. The trades with the most severe shortages are Bricklaying, with an index of -1.37, Roofing (-1.10) and Carpentry (-1.06). The fact that some of these trades tend to be deployed at the start of building projects suggests the shortage of trades will persist for some time. It may even get worse in finishing trades, such as joiners, plastering, painting, etc., in coming quarters.

HIA forecasts suggest the number of homes under construction will remain highly elevated for some time, meaning these shortages will remain troublesome.

Also to be considered are the costs associated with 'on the job' training carried out by the employer. The cost of the failure to adequately support businesses in the residential building industry to increase their capacity or attract new entrants is extraordinarily high, as it is likely to lead to further substantial skills shortages and potentially a decline in quality of building.

The majority of apprentices in the residential building industry are employed by small businesses with a turnover of less than $500,000. For some of these firms the increases in apprentice wages, especially in the first two years of progression, have made employing an apprentice financially unviable.

While the Expert Panel cannot directly influence Government policy on these matters the Panel can certainly give weight to these challenges faced by industry when carrying out its annual wage review.

Given that a range of Government support, including a wage subsidy (which has now lapsed), have in recent years been targeted at apprentices to address the real decline in commencements that existed prior to the pandemic, it appears untimely, if not inappropriate, that the minimum wages for apprentices be increased. This would simply erode those government stimulus measure.

HIA submit that the Expert Panel should have regard to these factors during this minimum wage review.

3. CONCLUSION

It is important that minimum wage policy settings as determined by the Expert Panel encourage both investment and employment.

The residential building industry is preparing for a rapid decline in construction commencements whilst also being heavily impacted due to natural weather events, the COVID-19 pandemic and world events.

The impacts of prices increases, delays and material and labour shortages are continuing to adversely affect the day to day financial circumstances of many in the residential building industry, including the many small businesses that operate in the sector.

Finally, the current conditions affecting apprentice employment deserves special consideration. Wage increases undoubtedly affect the capacity of businesses, particularly small business, to sustain the continued employment of apprentices to obtain completion status, leading to the eventual heightening of skills shortages in industry.

Noting that in recent years there has been many government stimulus measures targeted at supporting employment, particularly wages, HIA asks the Panel to be mindful of any erosive effect a minimum wage increase at this time could have on the residential building industry, especially at a time where government stimulus for wages has lapsed and there has been significant labour cost increases over the last 12 months and labour shortages remain the worst on record.

The cumulative impact of minimum wage increases, inflation issues, the ongoing tightening of builder margins, the ongoing market conditions arising from COVID-19 and its flow on impacts, combined with the precarious global circumstances suggest the economy has limited capacity to manage a significant wage increase.

Employers in the residential building industry are unlikely to be able to sustain further increases in this magnitude.

In light of the current landscape, HIA strongly submits that the Expert Panel takes a conservative approach in this year's minimum wage review.