

ANALYSIS OF THE MINIMUM WAGE IN THE CZECH REPUBLIC AND ITS EFFECT ON SELECTED ECONOMIC INDICATORS

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Abstract

In this article, we attempted to contribute to the ongoing debate about the impact of the minimum wage on selected elements and factors of economic development, especially on the level of employment, unemployment, and the overall situation in the labour market. The text is primarily focused on the Czech Republic, but we are not avoiding assessment of some other comparable countries, particularly in the EU. The author is aware that the given topic has been and is intensively subjected to all kinds of analyses and discussions, but it is still necessary to recapture the given context in the light of current data and facts.

The author provides an overview of some other ways of forming quantities that are supposed to influence the social and income situation on the labour market, such as a decent wage or a living wage. The article also describes the current positions of the EC and ETUC on the introduction of the EU standards in this area. The main weight of the article is in its last part, where, on the basis of the latest data, the relationship between the development of the minimum wage and unemployment, real wages, and real GDP growth

Key words: Minimum wage, labour market, economic indicators

JEL Code: J30, J3, J51

Introduction

In this article, we will again try to contribute to discussions about the impact of the minimum wage on some elements and factors of economic development, especially on the level of employment, unemployment, and the general situation on the labour market, especially in the Czech Republic, but of course, in this context, we cannot avoid assessing the context. Of the other comparable countries, especially EU countries. The author is aware that the given topic has been and is subjected very intensively in many other analyses and discussions; however, it is still necessary to recapture the given context in light of current data and facts.

The issue of the minimum wage is a very frequent topic of economic discussions in the theoretical or practical spheres. In principle, two basic views on this phenomenon and its application have appeared very often. The first of them is market-orientated, emphasises the philosophy of an ideal, or rather idealistic perfect market or perfect competition, and considers the minimum wage to be a kind of suspicious element that violates these principles.

The second approach considers the minimum wage as a necessary factor that has its irreplaceable place in the modern economy, as it guarantees to a certain extent the maintenance of acceptable social standards and also has a significant effect on the positive stimulation of basic economic variables, such as total consumption and, consequently, overall economic performance measured through GDP.

Especially this second view that we will try to analyse in this article.

1. Definition and content of the terms minimum wage and guaranteed wage

In this phase of the interpretation of the minimum wage, let us start from the basic definitions and characteristics that are contained in the materials of the International Labour Organisation. They can be cited as follows:

The term 'wages' is generally understood as payment made by an employer to his employees - including employees in regular, casual, short-term, intermittent, or seasonal employment, as well as apprentices and trainees. This broad definition of 'wages' is given in Article 1 of the Convention on the Protection of Wages of the ILO 1949 (No. 95):

'...the term wage means remuneration or earnings, however determined or calculated, can be expressed in money and fixed by mutual agreement or national laws or regulations, payable under a written or unwritten contract of employment by an employer to an employee for work performed or intended or for provided or planned services.'

(www.ilo.org)

In this general sense, the term "wage" is often synonymous with terms such as "earnings" or "remuneration". It does not include income from self-employment.

Let us recall that in general economic theory, wages are defined as the price of work and are theoretically the result of the law of supply and demand in this market. It is, of course, the subject of a number of analyses interested in to what extent the labour market corresponds to the theoretical concepts of market functioning, since the such fact that the "goods" that are traded are human beings who are existentially dependent on this mechanism, even if it has the ability to apply itself on this market. Many other factors are also related to this, such as the issue of qualifications, people's ability to relocate, to combine their family life with work, etc. All these aspects greatly influence the hypothetical model of supply and demand on the labour market, at least because in the countries in question there are always several separate labour markets, which have little permeability according to regional and qualification criteria, and, moreover, these market mechanisms must be supplemented in order to maintain social stability with social (non-market) measures, which include the minimum wage.

Some countries only, basic wages are considered for minimum wage purposes. In other countries, most other components of wages are also included. In some countries where

there is no clear legal definition of what the minimum wage should include, the issue may even be the subject of a court decision.

The current definition of the minimum wage in the Czech Republic is as follows.

The Czech Republic has a minimum wage regulated in Act No. 262/2006 Coll. in the Labour Code. Here, in 111, the minimum wage is defined as: "... the lowest permitted amount of remuneration for work in a basic employment relationship according to 3. The salary, salary, or remuneration of the agreement must not be less than the minimum wage.,, (see www.mpsv.cz)

According to the Czech Labour Code, the minimum wage is the lowest permissible amount of remuneration for work in a basic employment relationship. The amount of the basic rate and other rates of the minimum wage, including the conditions for its provision, is determined by the government by regulation, usually with effect from the beginning of the calendar year. If the employee's wage, salary, or remuneration does not reach the minimum wage, the employer must provide him with a supplement.

The minimum wage is not the same as the so-called guaranteed wage. This is set according to the difficulty of the work performed, and the minimum wage represents its lower limit, below which the income in any profession should not fall. It applies both in public services and administration, as well as in the business sector, unless a collective agreement has been negotiated.

2. Minimum wage function, living wage, decent wage

The minimum wage is currently fulfilling two main functions:

- Social function
- Economic function

These functions should be defined like this:

"The social protection function of the minimum wage is to protect employees from poverty and enable them to live at a level of modest material consumption and social contacts. For employers, the protective function of the minimum wage is to ensure basic equal conditions of wage competition (it is to prevent wage undercutting of domestic and foreign workforces).

The economic-criterion function of the minimum wage creates prerequisites for the income motivation of citizens to search for, accept and perform work, i.e., for favouring employees through work income compared to people with social income. For employers, the minimum wage represents the lowest level of employee wage costs". (Pícl, M., 2020)

It means that proper setting of minimum wage can promote social justice, wrong setting of this indicator can have significant negative consequences. The most important

issue is the amount of the minimum wage so that its setting actually fulfils its functions in a consistent and coordinated manner.

It should consider economic factors that include the requirements of economic development, the level of productivity, and the need to achieve and maintain a high level of employment.

Regarding the historical view of the minimum wage institute in the Czech Republic, it can be stated that Czechoslovakia acceded to the Convention on the Implementation of the Methods of Setting the Minimum Wage in 1950, when (June 12) the ratification was registered by the General Director of International Labour Office. Exactly one year later, on June 12, 1951, it entered into force for Czechoslovakia. In October 1990, the then Federal Ministry of Foreign Affairs announced the Czech version of the convention in the Collection of Laws, thus confirming its validity in the newly reconstructed legal order.

In the Czech Republic, dependence on the minimum and so-called guaranteed wage still applies. The following definitions were applied to guaranteed wages:

Living wage (living minimum)

Another concept related to the effort to ensure and express values that would enable a dignified life for individuals in a market economy is the living wage.

In the Czech Republic, the living wage is defined as follows:

"The living wage is the socially recognised minimum level of income to ensure nutrition and other basic personal needs. A living wage is the minimum level of income considered necessary to provide nutrition and other basic personal needs at a level that allows an individual to survive. In order to increase the motivation of adults in material need, a minimum subsistence institute is being introduced in addition to the living wage. The living wage cannot be used for dependent children, recipients of old age pensions, persons with third-degree disabilities, and people over 68 years of age. "

(www.mpsv.cz)

The functions of this parameter should be identified as follows:

- ensuring a minimum income for citizens;
- protection from poverty: The minimum minimum basic income level is designed to protect citizens from poverty and social exclusion.
- supporting equality and social justice;
- improving people's living conditions.
- promotion of economic growth: The level of the minimum level of subsistence influences aggregate demand and thus contributes to economic growth.

In general, the minimum level of subsistence has an important role to play in protecting and supporting basic needs of citizens and in achieving greater equality and social justice within society.

Decent wage

At the end of April, the Expert Platform for a Minimum Decent Wage (an expert group at the Friedrich Ebert Stiftung Foundation) presented in accordance with establishing the level of the quality of life indicator named decent wage. They also calculated actual levels of this indicator. Considering the current record inflation, the remuneration for work, which would allow workers and their households to cover all ordinary expenses, amounts to almost 40,000 CZK gross for Prague and almost 34,000 CZK gross for a slightly cheaper life outside the capital. Up to half of our employees do not receive decent remuneration for their work.

In this context, this platform has defined the typical characteristics of people who do not receive wages at the level of a living wage.

- fall into debt traps due to low or no financial reserves.
- work at the expense of free time to ensure sufficient income (according to the OECD, in 2018, the number of working hours in the Czech Republic was the third highest in the EU). This often has negative effects on health and family life;
- are more likely to face health problems. Research shows the negative effects of a long-term uncertain economic situation, especially on mental health or cognitive abilities;
- are placed in an unequal or dependent position in partner relationships.
- they will more often prioritise price at the expense of quality, which may also result in the impossibility of purchasing organic or local products (which otherwise may not only be purchased by people with high incomes);
- they have poorer access to health care. In particular, these are paid actions, e.g., in the framework of dental care, psychological care, supportive and preventive medicines, for the poorest, also supplements for medicines, etc.;
- they have worse opportunities for children's education.
- they may have more limited possibilities of participating in social life

Determining a living wage is precisely what prevents these negative social phenomena.

The above-mentioned variables have a common character in the sense that they seek to reconcile market mechanisms, which in capitalist economies lead to negative pressure on the social conditions of citizens and can expose them to significant social deprivations, and the socioeconomic aspect through the regulation of the income level of individuals. At the same time, an approach is embedded here that sees this social aspect of the functioning of society not as an additional or residual (or even superfluous) factor limiting its economic prosperity but, on the contrary, as a necessary precondition for its effective development.

3. Development of the minimum wage in the Czech Republic

Here, we present specific indicators of the development of the minimum wage in the Czech Republic.

Table 1: Development of the minimum wage in the Czech Republic (in CZK per month)

1991	2000
1992	2200
1996	2500
1998	2650
1999	3250
1999	3600
2000	4000
2000	4500
2001	5000
2002	5700
2003	6200
2004	6700
2005	7185
2006	7570
2006	7955
2007	8000
2013	8500
2015	9200
2016	9900
2017	11000
2018	12200
2019	13350
2020	14600
2021	15200
2022	16200
2023	17300

Source: Ministry of Labour and Social Affairs 2023

For a better illustration, see the following chart:

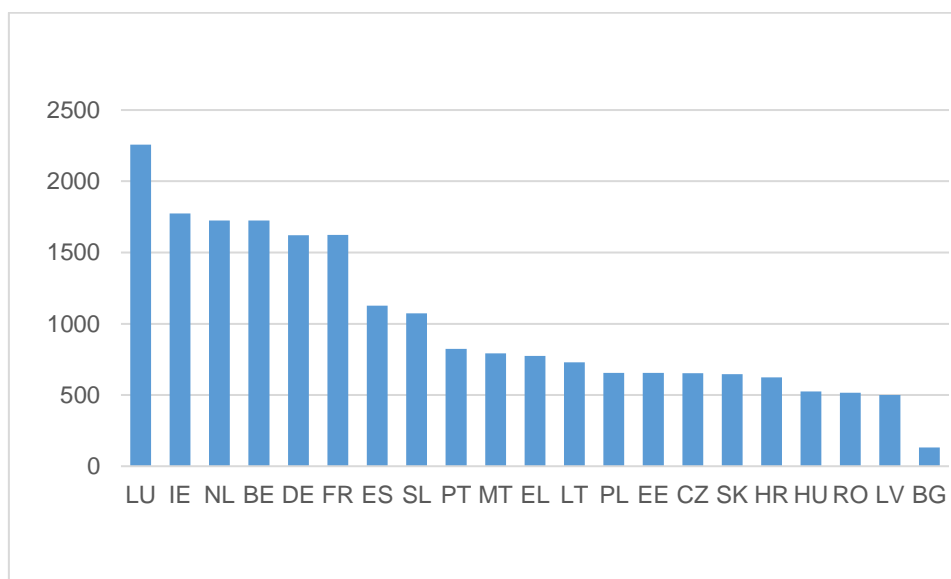
The development of the minimum wage in the Czech Republic went through several phases, which were partly determined by objective circumstances, i.e. the development of the economy and above all the situation on the labour market, and partly by the political and ideological orientation of the current government formations. A typical example of the influence of ideology on determining the level of the minimum wage is the period of 2008-2012, when the minimum wage stagnated and yet there was a significant increase in unemployment. This phenomenon will be analysed in the following text. Since 2013, there has been a relatively smooth increase in the minimum wage, although, from the point of view of trade unions, for example, this growth is insufficient. For example, the largest trade union headquarters MKOS demanded an increase in MW for the year 2023 to the amount of CZK 18,200, that is, to the level of about 45% of the average wage. This demand was rejected by the government and employers as excessive.

4. Minimum wage level in the EU

Let us now try to briefly examine the situation in the EU countries.

We have at our disposal a comparable amount of the minimum wage in PPS units (purchasing power standard) units for the year 2021. We present it here for clarity in a graphic form.

Figure 1: Minimum wage level in PPS units in 2021 (EU countries)



Source: Eurostat

If we wanted to outline the situation in EU countries based on the level of nominal financial amounts in euros, then we would get this overview.

The EU social policy is based on the principle that ensuring that workers in the Union earn an adequate minimum wage is essential to ensure adequate working and living conditions, as well as to build fair and resilient economies and societies, as set out in Principle 6 of the European Pillar of Social Rights.

It is assumed that both workers and businesses in the Union benefit from better working and living conditions, including through adequate minimum wages. Adequate minimum wages contribute to ensuring fair competition, stimulating productivity growth, and promoting economic and social progress. They can also help reduce the gender pay gap, as more women than men earn the minimum wage. (also see BAŠTÝŘ, I. 2005)

5. Minimum wage and the development of some macroeconomic parameters

In this part of the text, we will deal with the relationship between the development of the minimum wage in the Czech Republic and some important macroeconomic variables. This issue has been the subject of many analyses and has been the subject of many controversial discussions, which often reach completely contradictory conclusions.

For example, P.Cahuc and P.Michel (1996) came to the conclusion in their analysis that in the model of overlapping generations with endogenous growth, minimum wage legislation does not necessarily have negative consequences on economic performance. Such legislation can have a positive effect on growth by inducing a greater accumulation of human capital. "

The impact of the minimum wage on the position of younger employees was investigated by D.Neumark and O.Nizalova (2007) and they state that "exposure to minimum wages at a young age could lead to adverse long-term effects through reduced experience and tenure in the labour market and reduced education and training, while beneficial long-term effects could occur if minimum wages increased skill acquisition.

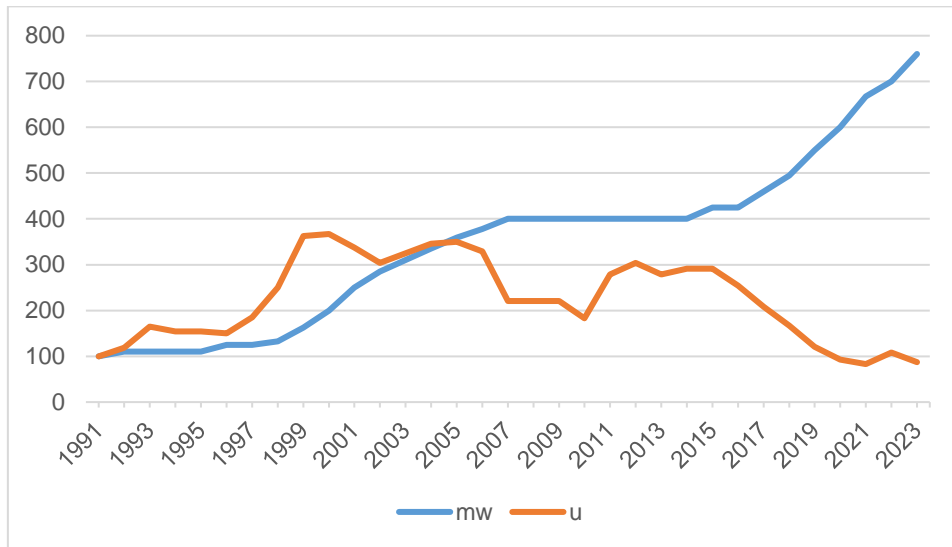
Other authors (e.g. J.Sabia 2015) question the positive effect of the increase in the minimum wage both on economic performance and in terms of ensuring an acceptable social level of employees.

The next authors find a significant negative effect of the increase in the minimum wage on marginal types of employment, such as part-time employment, and, conversely, a strong and significant positive effect on standard types of employment (see O.Holtemhler 2020).

So, let us try to focus on the characteristics that could illustrate the development and relationship of the minimum wage to some basic macroeconomic indicators in the last more than 30 years in the Czech Republic. Methodologically, it will be a relative (percentage) comparison of these quantities over time based on an assessment of their index development from the starting point.

First, of course, we present a comparison of the development of the minimum wage and the unemployment rate.

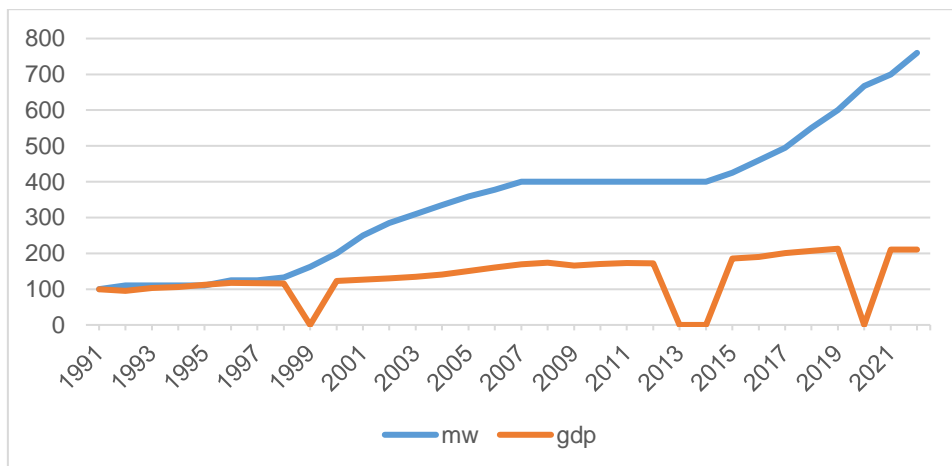
Figure 2: Development of the minimum wage and the unemployment rate in the Czech Republic (1991 = 100)



Source: Czech Statistics Office, own calculations, Note: unemployment rate according to the ILO methodology

This graph shows the relative changes of the relevant quantities for the period 1991-2021. There are obvious basic tendencies and several periods in terms of the development of these quantities and their mutual correlation. The invalidity of the basic liberal (free market) postulate about the negative effect of the growth of the minimum wage on the situation on the labour market, or to the growth of unemployment, appears mostly in periods 2007-2011, when the minimum wage stagnated and unemployment rose. In other words, developments in the Czech Republic show that precisely in periods of stagnation of the minimum wage, unemployment increased, and vice versa. Thus, in periods when governments proceeded to raise the minimum wage, the level of unemployment actually fell. Even this simple graphical outline convincingly shows that the growth of the minimum wage, if it does not exceed at least 50% of the real wage, has no effect on employment or unemployment.

Figure 3: Development of the minimum wage and real GDP (1991 = 100)



Source: The Czech statistical office, Eurostat, own calculations.

The same principle can be used to compare the development of the minimum wage and the level of real GDP. Again, the principle of assessing the development of indices of excessive quantities is used here, with the year 1991 as the starting point.

Therefore, the graph shows the relative changes in GDP and minimum wages. Here, too, it is confirmed that the development of GDP is not affected by the change in the minimum wage. Fluctuations in GDP growth in the Czech Republic in 1991-1992, 2009-2011, and 2020-2021 were not caused by a change in minimum wage, but by other factors, initially due to the so-called transformation, then exogenous effects of the currency crisis in the USA, and finally due to the covid epidemic. The influence of the minimum wage and its changes on the overall development of economic performance in the negative sense of the word is not documented here, on the fact that even the development of other important macroeconomic parameters does not confirm the negative effect of changes in the minimum wage. Their growth rates (changes) remained basically stable to changes in the minimum wage, and their fluctuations were caused again by other factors, contrary, after a long period of stagnation of the minimum wage in the years 2007–2013, and the decline in real GDP occurred relatively soon as a result of the currency crisis in capitalist economies in the years 2009– 2011, which was solved by massive state interventions in economies in order to save large corporations and economies as a whole, not by loosening and supporting the so-called free market mechanisms. The same thing happened again in 2020-2021, when the GDP in the Czech Republic fell due to the effects of the coronavirus epidemic, and this situation was also solved by state interventions in the economy to support production and consumption, not by relaxing market mechanisms in the style of perfect market balance, including the idealistic concept of the labour market, where minimum wages and its increase are allegedly caused by an imbalance in the form of an excess of labour supply over demand for it and thus the growth of unemployment.

Figure 4: Development of the minimum wage and the real wage (1991=100)

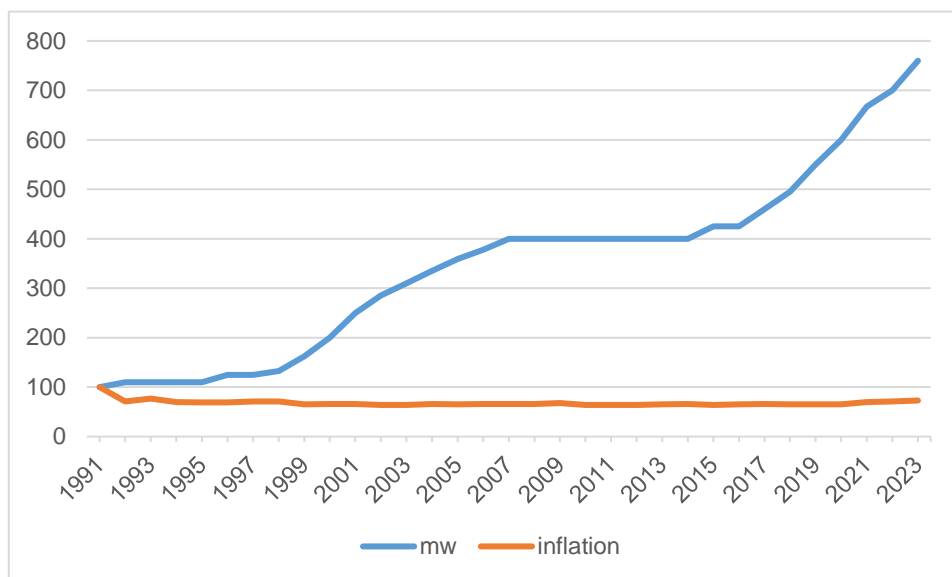


Source: The Czech statistical office, Eurostat, own calculations.

Even the development of other important macroeconomic parameters does not confirm the negative effect of changes in the minimum wage. Their growth rates (changes)

remained basically stable to changes in the minimum wage, and their fluctuations were again caused by other factors.

Figure 5: Development of changes in the minimum wage and inflation in the Czech Republic (1991 = 100)



Source: The Czech statistical office, Eurostat, own calculations.

Unfortunately, this chart does not yet include the acceleration of inflation in 2022-2023, which was a response to the failure to manage situations related to the covid pandemic and the armed conflict in Europe, when the conditions, especially in the energy markets, changed radically. Here, too, it appears that changes in the minimum wage do not play a significant role here.

Conclusions

The subject of our research was the impact of minimum wages on the growth of unemployment in the Czech Republic. For example, according to the neoclassical labour market, the introduction of a minimum wage has negative effects on the labour market. Therefore, we were interested in whether this assumption is actually valid and whether it corresponds to reality. We set out to determine whether an increase in the minimum wage has an effect on overall unemployment in the Czech Republic.

Based on the analysis, we found that the minimum wage does not have a significant effect on the unemployment rate in the Czech Republic.

Furthermore, the effect of the minimum wage on the level of GDP is minimal. However, what we consider essential to mention in conclusion is that the minimum wage has not been increased in the Czech Republic for many years and thus has not reflected wage growth in the long term. If the government does not want to increase the minimum wage in proportion to the growth in average wages in the future, we think it would be a good idea to adjust the minimum wage at least for inflation. In this case, it is then important

to resolve whether to adjust the minimum wage by the rate of inflation ex post or by the rate of inflation expected in the current year (usually at the end of the current year). In the event that the inflation rate falls in the future, this may ensure that the real value of the minimum wage increases and vice versa.

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