

Decentralization of Minimum Wage Setting in Russia – Causes and Consequences

Version 1.0

Anna Lukyanova
Nina Vishnevskaya
Centre for Labour Market Studies,
National Research University –
Higher School of Economics,
Moscow, Russia

IBES DISKUSSIONSBEITRAG

Nr. 206

November 2014

Decentralization of Minimum Wage Setting in Russia – Causes and Consequences

Version 1.0

Anna Lukyanova (alukyanove@hse.ru)

Nina Vishnevskaya (vishnev@hse.ru)

Impressum: Institut für Betriebswirtschaft und Volkswirtschaft (IBES)

Universität Duisburg-Essen

Universitätsstraße 12

45141 Essen

E-Mail: IBES-Diskussionsbeitrag@medman.uni-due.de

Contents

List of figures 4

List of tables 5

1. Introduction..... 6

2. The institutional framework of minimum wage fixing in Russia and the role of social partners ... 7

3. Why the decentralization of minimum wage fixing became an urgent problem?..... 11

4. The reform of minimum wage setting mechanism and its consequences 15

5. Final remarks 20

References 21

Annex..... 23

List of figures

Fig. 1. Kaitz index, Russian Federation, 1992-2013..... 12

Fig. 2. Kaitz index by branches, Russian Federation 13

Fig. 3. Kaitz indexes based on federal MW: average, regional maximum and minimum, 1999-2013... 16

Fig. 4. The minimum wage and subsistence level of the working-age population (IV quarter of each year)..... 17

Fig. 5. Share of regions with regional minimum wage, per cent 18

List of tables

Table 1. Variation of regional minimum wages (RMW) 19

Table 2. Ratio of RMW to regional subsistence minimum 19

I. Introduction

As the market economy fails to provide adequate insurance against income risks to which workers are exposed, different forms of labour regulations became an institutional response to those risks [Bertola, 2009]. Minimum wages are nearly universal policy instrument – they are applied in more than 100 countries [ILO, 2008]. At the same time this institution remains one of the most controversial issues in labour economics and economic policy, reflecting Freeman’s “institutionalist - - distortionist” divide [Freeman, 1993]. From the “institutionalist” point of view, most consistently expressed in [Eyraud and Saget, 2008], the main aim of the introduction of the minimum wage is to provide necessary guaranties for workers against economic volatility and strong bargaining power of employers. Adherents of this view consider wage minima both in a rights-based framework and as a social policy instrument. From the “distortionist” point of view, the institute of minimum wages may have the unintended negative outcomes. A minimum wage set above the market-clearing level may have detrimental effects on employment and unemployment, in particular, on less productive workers [see Neumark and Wascher, 2007; Betcherman, 2013 for the survey]. In economic policy, the setting of minimum wage involves a trade-off between reducing poverty among the most vulnerable groups of workers and shutting down low productivity jobs.

The effects of the level of the minimum wage or, more often the ratio of the minimum wage to the average/median wages (the so called Kaitz index) on the unemployment rate of different groups of workers, poverty or wage distribution is one of the most studied topics in economic research [Betcherman, 2013]. Much less attention has been paid to different types of the minimum wage fixing mechanism and its possible economic consequences. Moreover, for a long time it has been believed that the system for setting minimum wage has no significant independent effects on overall performance of the labour market.

Actually, the effects of minimum wages on labour market outcomes depends on the fine-tuning of the minimum wage to the elasticity of labour demand and supply and presence of other labour market institutions. In this respect, the minimum wage setting mechanism is very important as it affects not only the level but the responsiveness of the minimum wage to changes in the economy.

One of the most cited studies that investigate the link between the mechanism of the minimum wage setting and its level is the paper of [Boeri, 2012]. Although the minimum wages constitute a key labor market policy instrument in developed, developing and transition countries there is no international consensus on the process of setting, adjusting and enforcing minimum wages. Boeri identifies three main types of minimum wage setting, which range from conditions where a minimum wage is set by the government or parliament (“government-legislated minima”), to “consultation process” where the wage floor is the result of formal negotiations between the

government representatives and social partners; and at least to the “bargaining process”, where the minimum wage is determined exclusively by social partners. Wherein the wage floor fixed in collective agreements it can vary substantially between branches.

The system of minimum wage fixing may be a determinant of its level and dynamics and institutional variations may lead to different levels of the minima. The fact that the Kaitz index in the countries using the third type of the minimum wage setting mechanism amounts to 47 per cent while in the countries with the “government-legislated minima” accounts only for 31 per cent, speaks for the importance of the setting system.

The development and quality of industrial relations can be an important determinant of the minimum wage setting mechanism [Aghion, Algan and Cahuc, 2008]. When industrial relations are well developed, national employers’ organizations and trade unions are influential, and collective wage bargaining covers the majority of workers there is little need for “government-legislated minima”. This is the case in Germany and Denmark where the minimum wages are established in the branch collective agreements. The government intervention in the process of establishing of the wage floor becomes a necessity when trade union movement is weak and employers fragmented. At the same time, as authors notified, when social partners rely mostly on the government a number of negative consequences may appear, and above all the “active government” can serve as an obstacle to the development of effective industrial relations.

Since 2007 Russia has started the reform of minimum wage setting mechanism with the aim to decentralize this process. The main motivation of the paper is to explore the determinants of changes in the minimum wage policy, its main features and consequences for the Russian labour market. We are especially interested in the question, if the regional minimum wages under the new system of setting more precisely correspond to the level of prices and living standards in the different parts of Russia? The dataset used in this paper was assembled from several sources. Its key source is the data on nominal minimum wages that were taken from federal legislation. The data on regional minimum wages were received from the monitoring survey conducted by the Federation of Independent Trade Unions of Russia (FITUR). The statistics on average wages and other economic indicators are from official publications of Russian statistical office (Rosstat), in particular from Labour Force Survey.

2. The institutional framework of minimum wage fixing in Russia and the role of social partners

The minimum wage in transition Russia is not a new phenomenon as it has already existed in the Soviet period. The former USSR belonged to the group of countries with the government – legislated minima. Its rate was set by the central government and approved officially by the Supreme Soviet (the USSR parliament). The negotiations with unions on the minimum wage rate took place

but were predominantly of formal character. At the same time the relative value of the minimum wage during the Soviet times was comparable to what is now observed in many OECD economies. In 1985, for example, the minimum wage amounted for 70 Rubles, which, given the average wage in the country (about 190 Rubles), implied a Kaitz ratio of about 37 percent [<http://modern-econ.ru/micro/resursy/trud/minimal.html>]. Even in 1991, the year before the launching of economic reforms and a period of deep economic crisis, this indicator was equal to 25%. However, it should be stressed that in the international perspective the wages of Russian workers during the socialist period were very low.

After the launch of economic reforms in Russia the minimum wage fixing mechanism inherited many features from the central planning era. As before, the country has the federal minimum wage which is applied nationwide. Up to 2007 the Russian model of minimum wage setting was very centralized since regions were completely deprived of the opportunity to influence its level. Different countries use single- or multi-tiered approach to minimum wage fixing. According to ILO estimates [ILO, 2010], the majority of countries -- more than 65 per cent, have the complex set of minimum wages differentiated by age, branch or even occupation, while only one third of the countries use a single minimum wage. Transitional Russia belongs to the latter groups. As in the Soviet period the federal minimum applied to all groups of workers, without any differences by age, occupation or industry. It means that 16-19-years old workers and employees with long tenure receive equal minima. Countries differ not only how the minimum wage is initially set, but also in its subsequent "upgrading" for inflation. In Russia, the legislation has not identified the period of minimum wage adjustment. During the transition period adjustments of the minimum wage were irregular and varied greatly in size.

What level of the minimum wage is used as an initial rate in Russia? In developed and developing countries two main approaches are usually used [Euraud and Saget, 2005]. The first method is to base minimum wage rate on the average wage rate. The second approach, while setting the wage floor, takes into consideration the cost of living. In that case the minima should cover the basic needs of workers and in some cases the needs of his family. However, in many countries a number of economic factors are taken into consideration, that are the rates of economic development and productivity, dynamics of unemployment and some others [Belser and Sobeck, 2012]. In other words, the level of the minimum wage is often determined not only on the assumption of the workers' needs but also of the financial possibilities of employers to pay the increased minima. The economic situation in the country on the whole is very often taken into account.

Introduced in 2002 the Russian Labour Code when determining the level of the minimum wage adheres as a target to the cost of living of an average worker. Any economic factors are not taken into consideration. However, this legislative provision should be implemented by a special law enactment of which all the time delays. At the same it should be stressed that the average

subsistence level cannot be a reliable target for adjusting the minimum wage because of enormous regional variations in the prices and standards of living across Russian regions. Actually, while determining the wage floor there is no binding target in the process of the minimum wage fixing.

According to the Russian labour legislation the minimum wage is officially introduced by the Duma (the Russian Parliament) on the proposal of the federal government. However, first of all the consensus must be achieved about the level of minimum wage within the tripartite Committee which constitutes of representatives of employers' peak associations, trade unions and the federal government. All three sides sign a tripartite agreement on the principles for establishing the minimum wage. The tripartite Commission sits on a permanent basis, but it is especially active during the preparations and signing the two-year General agreement, which serves as the ideological symbol of operative partnership in the transitional Russia. In that sense, the system of the minimum wage determination may be characterized, according to the classification of [Boeri, 2012], as "consultation process" when the new level of the minima became the result of negotiations between the state and the social partners.

It should be admit that in comparison with the centrally planned economy the role of social partner stopped to be formal. But at the same time Russian trade unions and employers' organizations did not jet become equal partners to the government. The government plays still the leading role in the tripartite Commission while deciding the level of the wage floor. It must be not forgotten that the role of the federal government is supported by the fact that the state is an important employer. Though during the transition period the number of employees engaged in the state enterprises showed the tendency to decline, in 2013 almost 30 per cent of all employees worked in the state sector of the economy, another 6 per cent worked in the enterprises which belonged to the state on the par with private owners. At the same time the state was not especially good in balancing the interests of capital and labour. As we show further in the first period of transition the state, trying to support employers, let the minimum wage to fall to negligible level, but over the 2000s the wage floor began to "jump" abruptly.

From a formal point of view, the Russian unions may be proud of high representation. The majority of Russian unionized workers are members of the Federation of Independent Trade Unions of Russia (FITUR) which is a successor to the traditional communist unions. Though the FITUR suffered a severe membership decline from almost 100 per cent in the communist period to 33 per cent of total employment in 2013¹ the federation remains the most powerful organization in the modern Russia. The 'autonomous' or independent trade unions which have been established over transition period are still very small in size with only 5 per cent of the total union membership and

¹ www.fnpr.ru The membership data are not based on administrative sources (the Russian statistical office stopped to collect the data on trade unions membership) but on files reported by the union federation. On the whole, the data from different surveys prove this information.

do not play any important role in the public life [Chetvernina, 2009]. Namely the FITUR represents the Russian workers in the tripartite Commission.

The decline in the trade union membership in Russia (as in other former socialist countries) has, to some extent, different roots from declining unionism in the developed economies. Russia has witnessed declining union density because of the transformation from an obligatory system to entirely voluntary union membership and to a market economy. In addition, the falling level of unionism in Russia is partly due to high levels of unemployment and falling living standards during the first decade of transition. It should be not disregard the fact that the FITUR made little efforts to organize or recruit in the emerging private sector, in the expanding area of the service economy and among SME enterprises. One of the reasons for declining membership is the withdrawal of the management from the trade unions which was the usual practice in the communist trade unions. The trade union movement as a whole was increasingly confined to the residues of the old state industrial sectors of the economy. The most “numerous” members of the FITUR are large and medium-sized companies in manufacturing and extracting branches. In these sectors, the density rates amounted to 70 per cent of wage workers. However, we should stress that despite the downward trend the total density rate of Russian trade unions remains rather high by international standards.

The traditional trade unions were very vulnerable following the collapse of the Soviet system because they had been an integral part of the party-state apparatus at all levels. While the FITUR has generally been able to hold on to considerable part of their property they lost some of the rights that they enjoyed during the socialist period, among them the right of the legislative initiative and the control over social insurance funds. Most significant changes occurred in 2007, when trade unions lost control over dismissals at the enterprises.

The feature of the current situation in Russia is that collective bargaining agreements have weak regulatory impact on the wage policy and working conditions at the enterprise level. Industry trade unions do not keep effective control of wage determination in companies. The system of wage setting in Russia can be called “managerial”. Namely managers determine wages in Russian enterprises [Kapelyushnikov, 2007]. Under the conditions when Russian trade unions are not effectively able to determine wages and working conditions of their members they adhere to the strategy to negotiate these issues with the government, rather than directly with the employers. It is a widespread hope among the FITUR leaders that legislation and government regulation can achieve what unions are unable to achieve by their own efforts. The traditional unions embraces the principles of social partnership as collaboration with the state apparently provided them with some guarantee of retaining their former privileged status. Moreover, collaboration with the state through the institutions of social partnership enables the Russian peak trade union organization not only to secure its institutions survival but to fend the challenges of the alternative trade unions as well. The weakness of Russian trade unions may be proved by the inability of Russian unions to insist on a decent minimum wages during the initial period of the transition reform.

Another barrier to the development of social partnership in Russia was the fragmentation of employers' organizations to serve as the unions' counterpart. Unlike trade unions which existed in the Soviet times, employers' organizations were set up only after the launch of economic reforms. The first such organizations represented predominantly the largest state and former state enterprises. The main purpose of these organizations was not to present the enterprises as employers but to provide channel for lobbying the federal and regional authorities for tax credits and other privileges and establish personal connections with the government office holders. In subsequent years several hundreds of employers' organizations on the national, regional and industry level which represent the interest of employers in different fields, mainly in the goods market, were set up. Thereby a more fragmented organizational structure exists in Russia on the employers' side than on the workers' side.

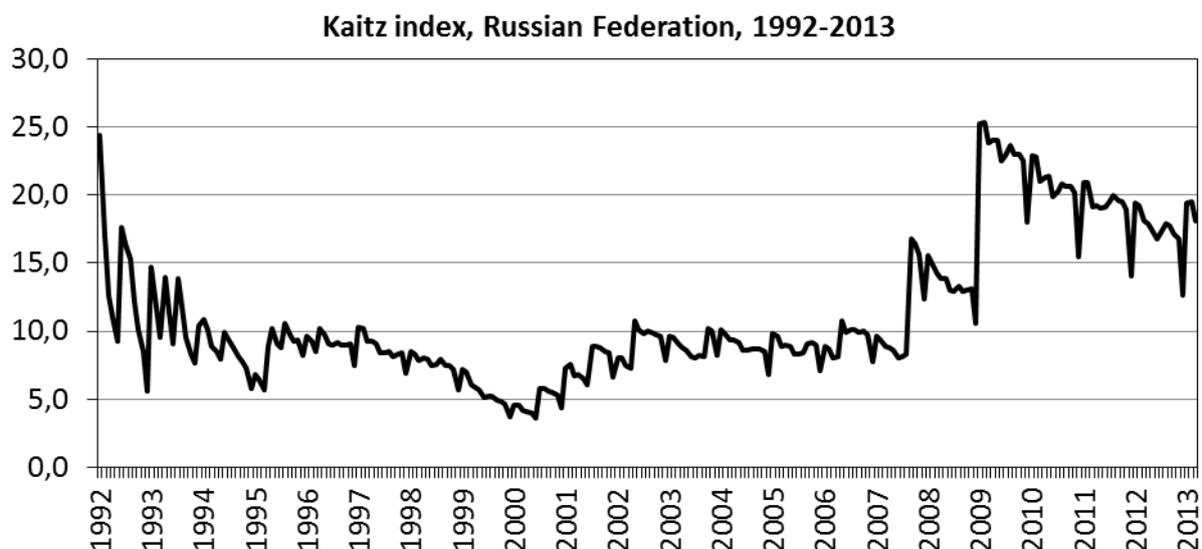
Over the transition period, Russia experienced difficulties of establishing a united front of employers' umbrella organizations. As a result, several cross-sector peak employers' organizations exist now but with different political weight. The leading employers' organization is Russian Union of Industrialists and Entrepreneurs (RUIE) which represents interests of large and some medium-sized enterprises. RUIE is the most powerful peak organization. Namely this organization is a main social partner in the Committee, setting the minimum wage framework. Small and medium-sized enterprises which are organized separately encouraged participating in the Commission, but they do not possess the reasonable industrial relations power.

Summing up, the limited membership of the employers' organizations, their underdevelopment at sectoral and regional levels, on the one hand, and the lack of "fighting spirit" by Russian trade unions, on the other hand, lead to the fact that both social partners look to the state rather than to their immediate counterparts to undertake the obligations of social partnership including the setting of the minimum wage.

3. Why the decentralization of minimum wage fixing became an urgent problem?

The levels of minimum wages relative to average wages vary widely across countries, but there is a relatively high frequency at around 40 per cent of average wages" [ILO, 2008, p. 35]. In Russia this indicator never reached this ceiling. As Fig.1 shows, before the year 2000 the minimum wage in Russia was so small that it can be defined, using the expression of C.Saget, as "mini minimum wage". More than that, over the first decade of economic transition the Kaitz index demonstrated even the downward trend with short-lived upsurges at the points of minimum wage hikes. As a result, by the middle of 2000 this indicator fell to 4 per cent.

Fig. 1. Kaitz index, Russian Federation, 1992-2013



In the economic literature low level of the minima is usually considered as unintended consequences of the link between minimum wages and the level of social benefits including old-age pensions, maternity benefits and unemployment benefits [Saget, 2008]. Indeed, over the 1990s and the greater part of 2000s the wage minima in Russia was used as a reference value for several welfare provisions, inter alia, child allowances, unemployment benefits, and some fines. However, the main reason for the low wage floor lay in the specific adjustment model of Russian transition. In Russia, during the economic reconstruction, wages were flexible while employment remained inelastic [Gimpelson and Kapelyushnikov, 2011]. In this model minimum wages were subjects to irregular and low indexations. The Russian government avoided the frequent indexations of the wage floor, fearing that increase in the wage threshold would further rise wage arrears, the number of defaults and on the whole worsen the economic conditions for enterprises. Russian trade unions were too weak to insist on minimum wage hikes. The minimum wage increases, when they occurred, were motivated by political factors. Clear correlation can be found between the increases of the minima and electoral cycles. Between 1992 and 1997, the level of minimum wage was raised 11 times, including 7 revisions that occurred in the pre-election periods.

The Russian minimum wage policy changed radically from the second half of 2000s. The real minima started to increase rapidly. In 2000-2012 the minimum wage in real terms increased 13-fold. The Kaitz index which was equal to 4 per cent in 2000, rose to 8-10 per cent in the next two years and from 2007 it escalated to the highest point of 26 per cent, which was reached in 2009. The economic crisis has had a negative impact on the dynamics of this index, but the ratio of the minimum wage to the average wages did not drop below 20 per cent.

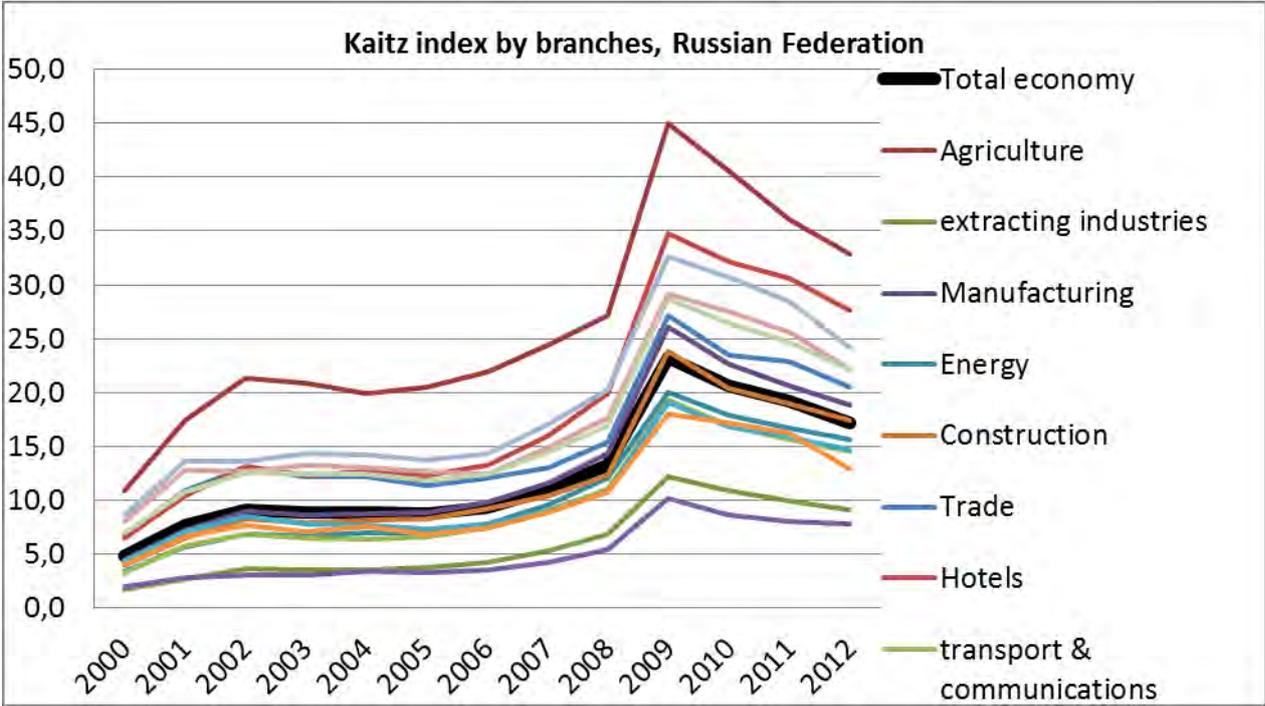
The shift in the policy towards minimum wages was the result of changes in political “milestones” which occurred since 2000 and the trend towards greater state intervention in the economy. During the period of economic growth, which was observed over the most part of the

previous decade, the low level of the minimum wage became unacceptable for political reasons. Moreover, Russian trade unions and employers' organizations gradually became more influential, especially on the regional level. And at last, high oil prices and budget surpluses made it possible to increase wages of public sector workers who constitute the majority of minimum wage recipients in Russia.

As many empirical studies show, whether dis-employment effects are important or not mostly depends on the minimum wage level and on the size of the minimum wage hikes. For any given level of the wage floor relative to the average or median wage, a minimum wage may have different impacts on employment depending on the distribution of skills and individual productivity levels across the labour force. At low levels of the minima to the average wage, both economic theory and empirical evidence are ambiguous as to the impact of the minimum wage on employment. But if the wage floor is too high this may reduce the employment prospects of some groups of workers, primarily low-productivity labour [Betcherman, 2013]. This consideration is especially important for countries in the period of rapid inflation

Despite relatively low level of Russian minimum wage this institution has significant impact on the wage setting in some economic branches (Fig. 2). If we look at the “peak” year (2009) when Kaitz index for the whole economy was equal to 26 per cent, in agriculture it amounted to 45 per cent, in hotels and catering this indicator approached 35 per cent, while in industries with high wages – finance and extracting industries -- it never exceeded 11 per cent.

Fig. 2. Kaitz index by branches, Russian Federation



The economic impact of the minimum wage depends on the proportion of workers receiving the wage floor and their composition because minimum wage earners are unevenly distributed among the demographic groups and sectors of the economy. Abrupt changes in the minimum wage level determined the changes in the number of receivers. In Russia, over the first part of 2000s only 1-2,5 per cent of all employees receive wages below the federal minimum [Rosstat, database]. The sharp increase in the minima in the late 2000s led to an increase in the proportion of minimum wage earners to 3 per cent in 2009. In 2011 their share dropped again to 1,8 per cent. This figure is significantly lower than in many developed and transition economies, where this ratio often exceeds 5-15 per cent [OECD Employment Outlook, 2009].

In 2012, the proportion of workers with the minimum wage ranged from 0.2-0.5 per cent in mining, finance and electricity to 5.8 per cent in agriculture. Except agriculture, among the industries in which the share of minimum wage recipients was higher than the average (1,8 per cent), we can distinguish public and social services (4,3 per cent), education (3,8 per cent), communications (3,6 per cent), health care (2,3 per cent).

The surveys of the Russian statistical office show that the majority of low-paid workers (73 per cent in 2012) are concentrated in the public sector of the economy. Therefore, the public sector organizations bear the financial burden of the minimum wage increases. In addition to the direct impact minimum wage increases have some spillover effect on those who receive wages above the minimum. Such increases are explained by the need to preserve the structure of relative earnings and the necessity to maintain incentives by more productive workers.

Regarding gender structure it is necessary to note that in Russia the proportion of women among the minimum wage receivers is much higher than in many other transition countries. In 2012 their share reached 64 per cent. Furthermore, the gender difference is rather stable over time. The overrepresentation of females is largely due to the industry distribution of minimum wage receivers, and in the first place high female participation in industries with high share of low-paid, namely some services and education.

The minimum wage recipients are characterized by large age differences. As compared with all Russian workers, among low paid dominated workers of young and senior age groups. As might be expected, among the recipients of the minimum wage are overrepresented groups with low (secondary school or less) education and under-represented groups with tertiary education. However, it should be noted that about a tenth of the minimum wage recipients have university diplomas.

4. The reform of minimum wage setting mechanism and its consequences

In 2007, the Russian government with the support of social partners initiated the reform of the minimum wage setting mechanism. The reform had several objectives but one of the main aims was to differentiate the real minimum wages across Russian regions in order to better reflect the levels of regional average wages, prices and differences in subsistence levels. At the same time the reform was planned in such a way that to shift the financial burden of raising the minimum wages from the federal to regional budgets. All 89 Russian regions (later their total number was reduced through the administrative reform to 83) were empowered to define their own regional minimum wage with the only condition that the regional minima should be set above the federal floor. The international experience shows, that the centralized model does not allow taking into account the variations in the regional economies: levels and dynamics of employment and unemployment, shares of low-wage workers. Large countries with vast territories use very often decentralized mechanism of minimum wage determination and respectively a multiplicity of minimum wages (for example, the United States, Canada or Brazil). For Russia the experience of the latter economies is of special importance taking into consideration country's vast size.

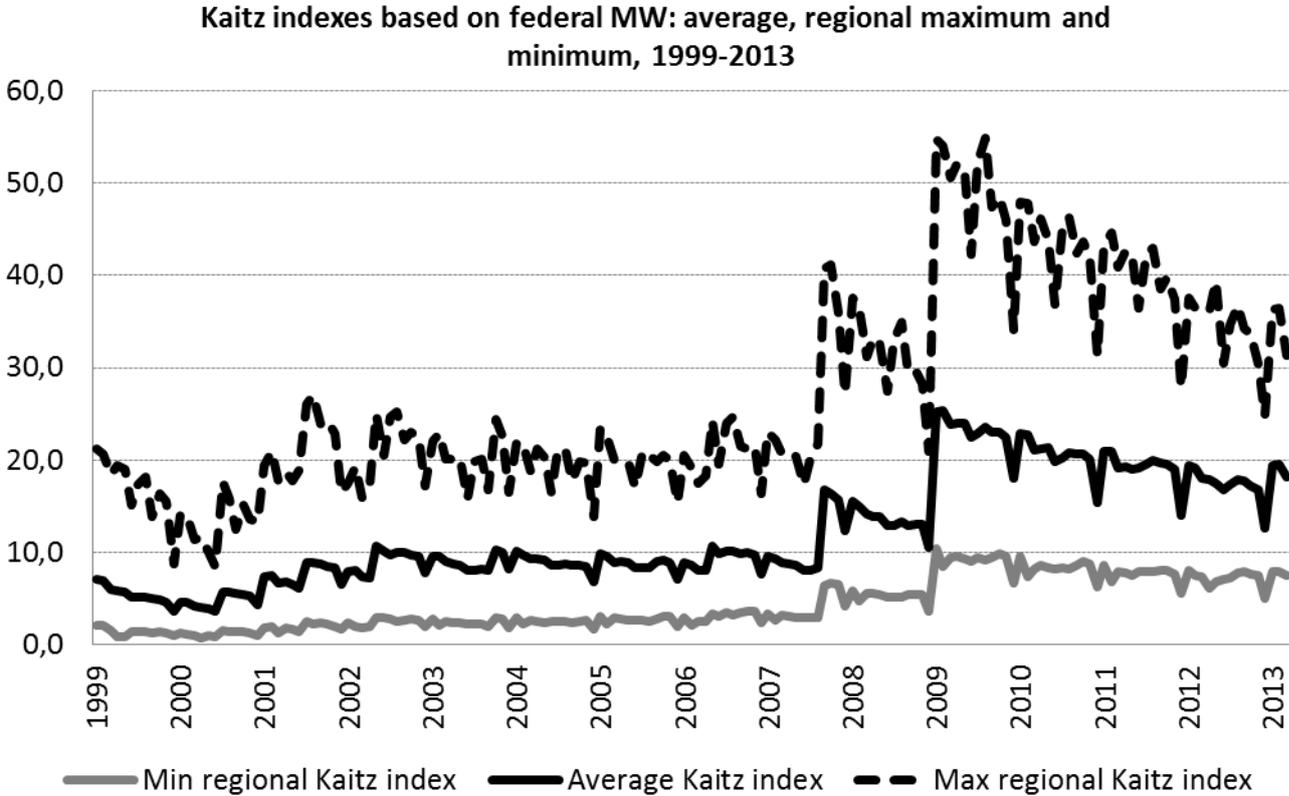
The fulfillment of all these goals needed more active cooperation between local authorities and social partners at the regional levels as the rate of the regional wage floor is now established by consent of all parties: regional employers' associations, trade unions and local authorities. This is a very important aspect because the parties agree on the wage floor which is acceptable for the majority of local employers. We can say that one of the consequences of the reform is the strengthening of social partnership at the regional level. The regional wages are more flexible than the federal minima because, firstly, regional social partners are empowered not only to establish the new minima, but also to abandon the RMW in worsening economic conditions, and, secondly, employers in critical financial situation may postpone the introduction of a new wage floor. Though, and this should be stressed, local authorities use very often the "administrative resources" to avoid opportunistic behavior of such employers.

Over the early period of transition, Russia tried to differentiate minimum wage across Russian regions by using the so called Northern coefficients. In a number of Russian regions, mostly North and Far East territories but also in some continental regions with adverse climatic conditions, the federal minimum wage was multiplied by regional coefficients which varied from 1,15 to 2. Northern coefficients were used as a financial instrument to attract and keep labour in highly industrialized but low-populated areas. At the same time the authorities of these regions could not influence either the value of the federal minimum wage, or the size of regional coefficients.

At the same time, serious diversity in the purchasing power of minimum wages existed not only among Northern territories. The ratio of the federal minimum to regional average wages varies

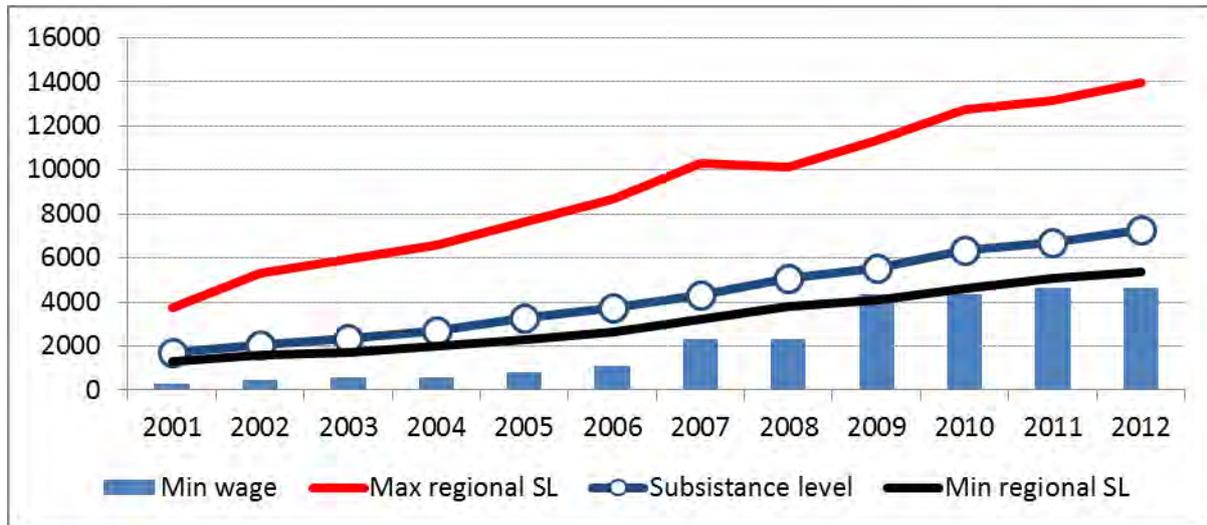
dramatically across Russian regions. Regretfully, the regional data are available only from 1999. Fig. 3 shows that in the poorest region the Kaitz ratio has not been below 10 per cent over the period and peaked at 55 per cent in 2009. At the same time in the richest region it only reached 10 per cent level in 2009. Substantial cross-regional variation in the Kaitz index existed in the most parts of the country because of the enormous differences in the average wages and wage distribution in general across Russian regions. This finding suggests that the federal minimum wage creates very differential institutional environment at the regional level.

Fig. 3. Kaitz indexes based on federal MW: average, regional maximum and minimum, 1999-2013



The same can be said about the link between the minimum wage and subsistence level. Fig. 4 demonstrates that the federal minimum wage in Russia never reached the subsistence level of the working age workers. The difference between the federal minimum wage and the regional subsistence level does not look enormous in less-developed regions with low level of prices. However, in the parts of the country with high prices the subsistence level was 5 times higher than the wage floor prior to the reform.

Fig. 4. The minimum wage and subsistence level of the working-age population (IV quarter of each year)



Simultaneously with the introduction of regional wage floors the procedure for calculating the minimum wage was modified. It was made to neutralize the possible negative impact of the rapid increases in the minimum wages. Till 2007, it was the basic tariff rate that must be not less than the minima and all awards and bonuses were paid in excess of the wage floor. The introduction of a new approach to the calculation of the minima can be explained by the peculiarities of the wage formation in Russia. Various bonus systems are used fairly frequently in many countries as there has been the tendency to decentralization of wage setting in recent years. For example, in Finland payments by results were quite common, especially in the private sector where 43 per cent of firms or workplaces used some form of payment by result and around 95 per cent of those who were covered by bonus system received a bonus [Johansson, 2006]. In Russia, the use of unstable part of wages is much more frequent and the share of bonuses in wages is much higher than in other countries. According to Rosstat, the share of tariff wages in 2012 was equal to 41 per cent. The analysis of industry collective bargaining agreements shows also that the share of non-tariff wages amounted to 40-50 per cent [Vishnevskaya, Kulikov, 2009]. In the United States bonuses did not exceed 5 per cent [<http://ftp.bls.gov/pub/special.requests/ocwc/ect/ececqrtn>]. Thus, if the use of regional minima led to the increase in the minimum wage rate (at least in many parts of the country), the changes in the definition of the wage floor were aimed to curbing its growth.

As can be seen on the Fig.5, the Russian regions not only received the right to introduce their own minima, but actively took advantage of this right. Regional tripartite agreements, setting the wage floor, take into account the economic and social situation in the particular region and the phase of the economic cycle as well. To the end of 2007, 27 per cent of all Russian regions introduced the regional minima, which was higher than the federal wage floor. The group of “pioneers” constituted of the most developed regions. To the end of 2008 the share of regions with their own minima

reached 49 per cent. At the same time the regional minimum wages turned up very sensitive to the economic cycle. During the 2008-2009 crisis, the proportion of regions which abandoned the regional minima was reduced by more than a third to 32 per cent. However, with the improvement of the economic situation in Russia some regions returned to the legislation of their own minima. According to the monitoring of the trade union federation, in 2013 the regional minima existed in 62 per cent of all Russian oblasts.

Fig. 5. Share of regions with regional minimum wage, per cent



Our analysis shows that the results of the decentralization reform of the minimum wage setting mechanism are mixed. We should admit that the introduction of regional minimum wages led to the increases in nominal minima and regional Kaitz indexes. The Maps for 2007 and 2011 in the Annex clearly show that the introduction of regional minimum wages led to the increases in the minima. From 2007 to 2011, the number of regions where the regional Kaitz index exceeded 23 per cent increased substantially, while the number of regions with the minimum floor lower than the federal one has noticeably declined.

The other consequence of the reform is the narrowing of the variations in the regional minimum wages. The Table 1 demonstrates that the coefficient of variation which in 2005 was equal to 0.36 to 2011 fell to 0.22.

Table 1. Variation of regional minimum wages (RMW)

Year	Average RMW by regions, rubles ^{*)}	Minimum RMW by regions, rubles	Maximum RMW by regions, rubles	Coefficient of variation
2005	945.0	800	3600	0.36
2007	2560.4	2300	5829.1	0.26
2009	4793.9	4330	7956.8	0.18
2011	5513.8	4611	9912.3	0.22

Note: regional minimum wages in each region are corrected for differences in coverage.

^{*)} – unweighted average

At the same time, the reform did not result in any narrowing of the variations of the ratio of regional wages to the regional subsistence levels (Table 2).

Table 2. Ratio of RMW to regional subsistence minimum

Year	Average by regions ^{*)}	Minimum	Maximum	Coefficient of variation
2005	0.30	0.20	0.64	0.18
2007	0.63	0.24	1.33	0.25
2009	0.86	0.38	1.39	0.17
2011	0.80	0.39	1.41	0.19

Note: regional minimum wages in each region are corrected for differences in coverage. ^{*)} – unweighted average

At the same time the co-existence of the federal minimum wage and regional wages has led to new imbalances. In the majority of regions the federal employees are excluded from regional minimum wage coverage. In some regions regional and municipal employees are also exempt from the regional regulation and the regional wage floor applies exclusively to the private sector workers. In 2012 the share of such regions approached 52 per cent. This means that in the same region the substantial groups of workers rely on a lower minimum wage. The lower minimum wage paid to the federal employees (besides it should be taken into account that the wage floor is used as a

benchmark for wage scales) is not only socially unacceptable but leads to the negative selection to the public sector. It should be taken into account that non-coverage of state employees occurred more often in economically poor regions, especially in those that receive subsidies from the federal budget. Wherein, the share of public sector workers is higher in economically less developed parts of the country. The coexistence of different MWs reduces also the regulatory transparency and complicates enforcement.

Then it should be noted that the abolishment of the Northern multiplier, previously set in the federal legislation put some regions with the adverse living conditions at a disadvantage. Some of these northern territories were not financially able to increase the nominal minimum wage what had negative social consequences.

5. Final remarks

Our findings suggest that the decentralization reform of the MW setting mechanism accelerated the growth of the wage floor for Russian workers and narrowed the variation in the minima between regions. At the same time, the coexistence of the federal and regional minimum wages has led to new imbalances. All these mean that the reform of the minimum wage setting mechanism in Russia cannot be considered final and further steps are required for better functioning of this institute.

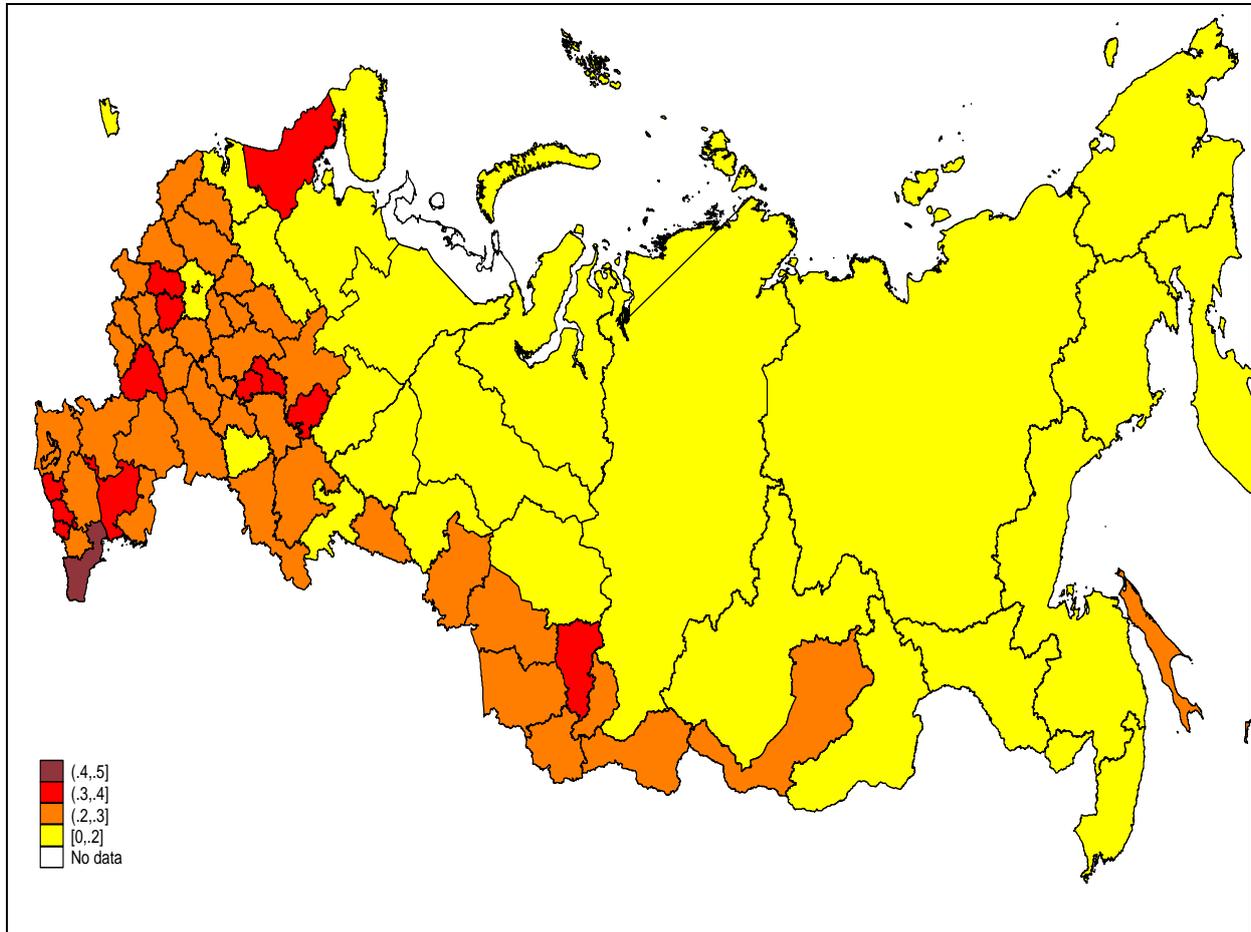
References

- Aghion, P., Y. Algan and P. Cahuc. (2008) "Can policy interact with culture? Minimum wage and the quality of labour relations". IZA DP No. 3680.
- Bertola, G. (2009) "Labour Market Regulation: Motives, Measures, Effects". Conditions of Work and Employment Series No. 21, Geneva. ILO
- Belser, P. (2012) "Minimum wages: institutional aspect". – ILO. Available at: http://www.ilo.org/public/english/region/arpro/beirut/downloads/events/2012/wage_2012/presentation3.pdf
- Betcherman, G. (2013) "Labor market institutions: a review of the literature" *Background paper for the World Development Report 2013*
- Boeri T. (2012) "Setting the Minimum Wage". *Labour Economics*. Vol. 19
- Chetvernina, T. (2009) "Trade Unions in the Transitional Russia – Peculiarities, Current Status and New Challenges" Institute of Economic Research Hitotsubashi University WP 16
- Eyraud, F. and C. Saget. (2008). "The Revival of Minimum Wage-Setting Institutions." in *Defence of Labour Market Institutions: Cultivating Justice in the Developing World*, ed. Janine Berg and David Kucera, 100–18. New York: Palgrave Macmillan and International Labour Organization
- Eyraud F. and Saget C. (2005) "The fundamentals of the minimum wage fixing". ILO
- Freeman, R. (1993) "Labor Market Institutions and Policies: Help or Hindrance to Economic Development?" *Proceedings of the World Bank Annual Conference on Development Economics* Washington, DC: The World Bank.
- Freeman, 1993 or 1996 look at Betcherman Freeman R.B. The Minimum Wage as a Distributive Tool, (1996), *Economic Journal*, Vol. 106, pp. 639-649
- Gimpelson, V. and R. Kapelyushnikov. (2011) "Labor Market Adjustment: Is Russia different?" Institute for the Study of Labor (IZA). *Discussion Paper No. 5588*
- ILO, (2008) *Global Wage Report*, ILO, Geneva
- ILO, (2010) *Working Conditions Laws Report 2010: A Global Review*, ILO, Geneva
- Johansson A. (2006). *Wage setting in Finland: increasing flexibility in centralized wage agreements*". ECO/WKP 31, OECD. Paris
- Kapelyushnikov, R. (2007). "The wage-setting mechanism in the Russian industry". In *Wages in Russia*. Moscow Publishing House of HSE
- Lee, S. (2012) "Varieties of Minimum Wage System" through the Dubious Lens of Industry-based Rankings". *International Labour Review*. Vol. 151. No. 3
- Muravyev, A., Oshchepkov, A. (2013). "Minimum Wages and Labor Market Outcomes: Evidence from the Emerging Economy of Russia", HSE Working Papers, Series: Economics, WP BRP 29/EC/2013/. IZA
- Neumark, D. and Wascher, W. (2007) "Minimum Wages and Employment", *Foundations and Trends in Microeconomic*. Vol. 3, Nos. 1-2
- Rani, U., Belser, P. and M. Oelz. (2013) "Minimum wage coverage and compliance in developing countries". *International Labour Review*, Vol. 152, No. 3–4
- Saget, C. (2008). "Fixing minimum wage levels in developing countries: common failures and remedies". *International Labour Review*. Vol. 147. No. 1. ILO

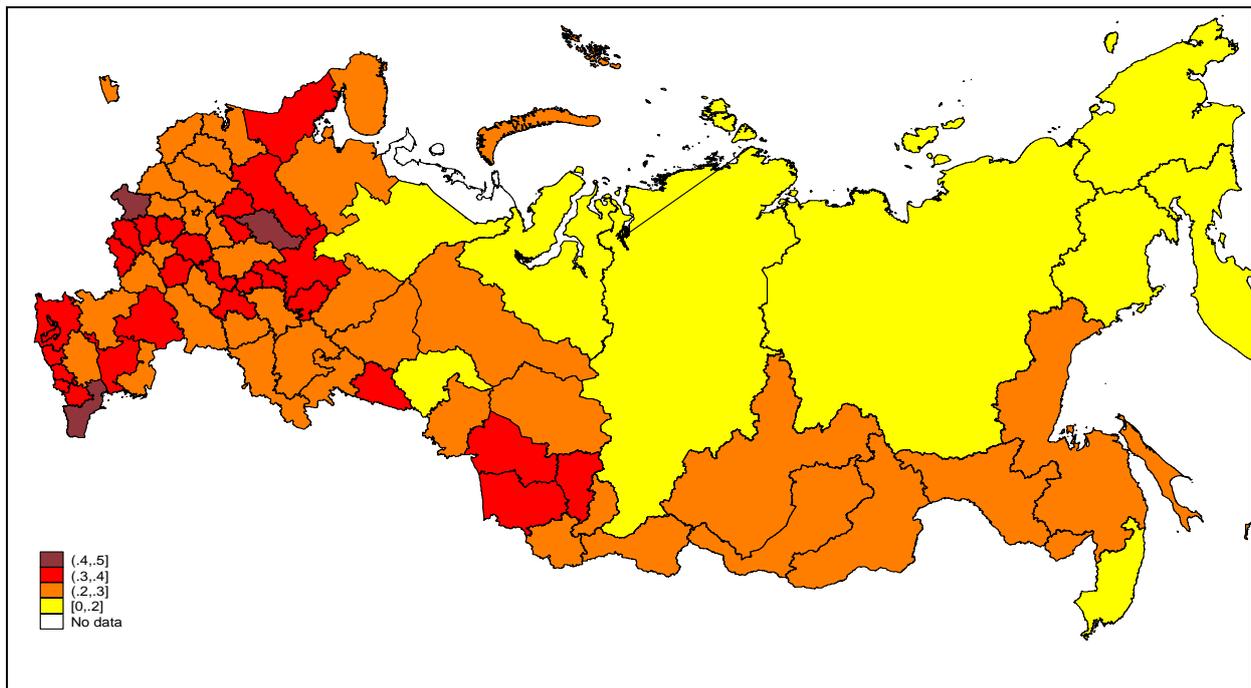
Vishnevskaya N., Kulikov O. (2009). "Wage Formation in Russia: the Role of Industry-Wide Agreements" (in Russian). *Voprosi Ekonomiki*. No.4

Annex

Map I. Kaitz ratio for regional minimum wages, Russian Federation, 2007



Map 2. Kaitz ratio for regional minimum wages, Russian Federation, 2011



IBES



ISSN-Nr. 2192-5208 (Print)
ISSN-Nr. 2192-5216 (Online)

