Submission to Commonwealth Grants Commission

2023 Update: Wages Data – January 2023

These comments respond to the Commonwealth Grants Commission's (CGC's) *2023 Update – seeking State views on wages data* paper.

The CGC has identified concerns that COVID-19 lockdowns have distorted its 2021-22 wages regression and has provided the States with three options:

1. Use alternative measure of hours worked.
2. Adjust the data to remove identified respondents.
3. Use the unadjusted data.

The CGC has also raised the issue of whether options 1 or 2 should be applied to all data years, or just the 2021-22 data year.

As touched on in its paper, the CGC has only identified what it considers to be a data problem for the 2021-22 data year. As per usual, the 2023 Update draft terms of reference says that the CGC should use methods consistent with the previous Update, but allows method changes to address data problems. We believe **making changes to any other data year would constitute a method change beyond the scope of an annual update, rather than a data-driven change**.

Even for the 2021-22 data year, we **prefer option 3 – to use the data without adjustments**. The main reasons for this are outlined below.

1. **Data volatility**

   The CGC's paper states there is unusual degree of volatility in the 2021-22 data. However, the wages data is usually volatile, and significant year-on-year changes are common. Although the variations were the largest experienced for four States, the variations for the other four States were significantly below their most variable previous results, and WA and SA had both previously had larger variations (in 2017-18) than what is now seen for NSW and VIC. The largest variations in the latest data are for ACT and NT, which due to their smaller sample size would be thought to be naturally prone to more variation.

   While we acknowledge there are issues with the data, we feel that making adjustments to an already volatile assessment will further complicate an already complex calculation.

2. **No adjustments have been made in previous data years.**

   Prior to the 2019 Update, we requested the CGC reconsider the wage costs results due to our concerns about the wage costs regression model and the volatility of the data. That is, the CGC's wages model estimated public sector wage cost pressures in WA decreased from 5% above the national average in the 2016-17 data year to 0.3% below the national average in the 2017-18 data year, and then increased back up to 3% above the national average in 2018-19. A similar pattern, although not quite as large, occurred for SA in those years. In our view, this clearly suggested that the 2017-18 data year did not reflect actual wage pressures

The CGC provided a response stating ‘the Commission has made no changes to the wage costs assessment method and only used the latest available data. The wage costs results provided to the States reflect the changes in the wages data set (the ABS Characteristics of Employment Survey (CoES).’’ It is unclear to us how the current situation is different.

3. **Concerns about the suggested adjustments**

When comparing the established method and the method that uses *hours paid* data instead of *hours usually worked* data, there is an increase in the explanatory power of the model (when looking at the R-squared statistic). However, this increase is present across all years included in the regression, not just in August 2021. This implies that the adjustment is addressing something broader than just the specific issue of lockdown-affected respondents, so it is difficult to determine the degree to which the adjustment addresses the specific problem. If this adjustment is having impacts other than addressing the specific problem identified by the CGC, it would constitute a substantive method change that should be explored in the 2025 Review.

This suggests that while it is possible that this method produces a regression that fits the data better, it is not evident that the CGC’s concern of COVID lockdowns occurring in August 2021 artificially reducing wages is being addressed by this adjustment. Also, it appears that any differences in explanatory power between the established method regression and the lockdown adjusted regression are marginal, and the very slight increase in explanatory power would not justify a significant departure from existing assessment methods.

It would not be appropriate to apply a significant adjustment like this based on the regression findings in an annual update – this should instead be considered as part of the 2025 Review.

4. **Limited Timeframe**

We acknowledge there is limited time frame to take a full analysis on the data and feel this timing means it is impractical for the Commission to follow its standard practice to make a fully informed decision.

Furthermore, as suggested in the multilateral meeting, we do not support the delay of the release of the 2023 Update. If there is not sufficient time to make a fully informed decision, prior to the 2023 Update, then the unadjusted ABS data should be used, and further analysis be performed in the 2025 Review or the 2024 Update.

To assist with States’ budgeting it would be appreciated if we could be advised of the CGC’s decision in advance of the 2023 Update release.

These current issues further confirm our general concerns with the CGC’s regression model, and we support thorough review of the wages assessment in the 2025 Review.