

Does Increasing the Minimum Wage Increase **inflation**?

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This brief examines the potential impact of a minimum wage increase in Nigeria, taking into account the current economic state and the factors driving inflation. It also provides a minimum wage recommendation to guide the government and labor unions in reaching a realistic minimum wage

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Introduction

In Nigeria, minimum wage refers to the lowest monthly pay the government or any other employer of labor is required to pay an employee at the end of the month. Recently, there has been a demand by the organized labor unions of the Nigeria Labour Congress (NLC) and Trade Union Congress (TUC), for the government to increase the minimum wage by 10 to 15 folds to cushion the effect of inflation on Nigerian workers. However, the government has stated that “the amount is not realistic”, citing that such action will disrupt the economy. On June 7, 2024, the tripartite committee proposed a new minimum wage of N62,000. This has sparked extensive debate about the potential impact of increasing the minimum wage. While there are some insinuations that increasing the minimum wage significantly will further worsen inflation due to the increase in disposable income, which will push prices higher, others argue that it will not. However, pros and cons arguments have been driven more by theory and emotions than by data. In this brief, we explore the current state of the economy, the pattern of inflation that defines it, the potential implications of increasing the minimum wage, and some policy recommendations for the government.

Understanding Inflation: Demand-Pull vs. Cost-Push

Inflation is defined as an increase in general price levels over a given period in an economy. Typically, it is a broad measure of trends in the overall price or the cost of living in a country¹. It is important to understand not only the concept of inflation but also the types of inflation and which one best describes the Nigerian context.

- Demand-pull inflation: This occurs when the demand for goods and services exceeds its supply. For instance, when there is an excess of money in circulation chasing too few goods in the market. This type of inflation is often driven by an increase in consumer spending, which can be caused by higher wages, tax cuts, or increased government spending. Here, the more significant the gap between the aggregate demand and the aggregate supply, the more rapid the inflation².
- Cost-Push Inflation: On the other hand, cost-push inflation occurs as a result of an increase in the costs of production, leading producers to raise prices to maintain profit margins. Factors contributing to cost-push inflation include increased wages, higher costs of raw materials, and increased taxes or tariffs³.

¹ <https://www.imf.org/en/Publications/fandd/issues/Series/Back-to-Basics/Inflation>

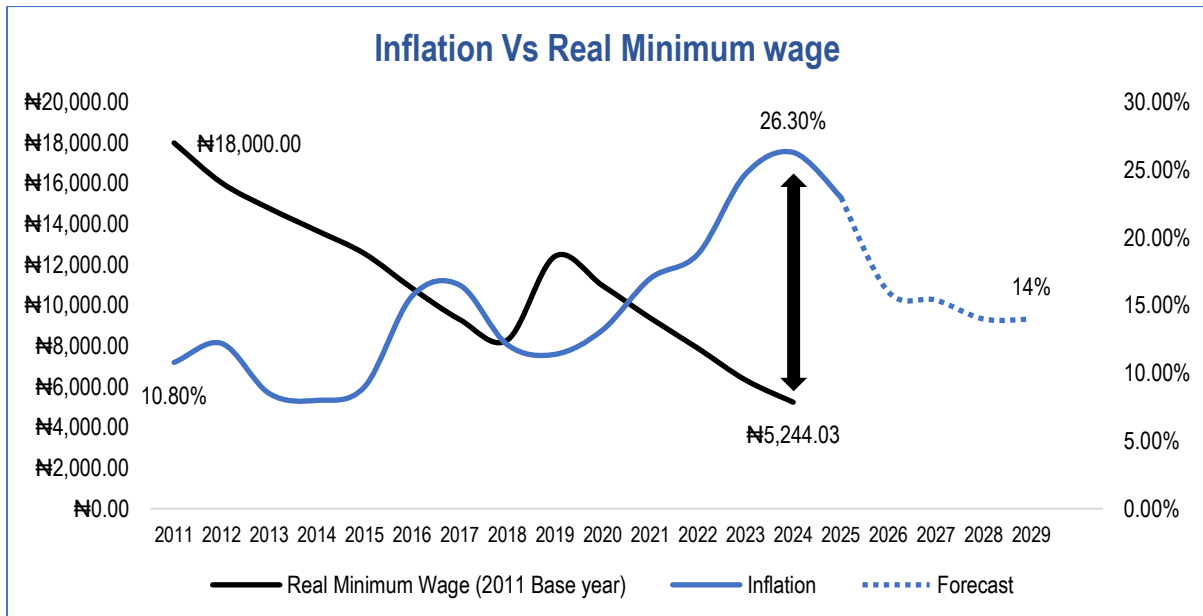
² https://www.researchgate.net/profile/Jalil-Totonchi/publication/265893432_Macroeconomic_Theories_of_Inflation/links/55b9f05208aec0e5f43c5de1/Macroeconomic-Theories-of-Inflation.pdf

³ <https://www.cbn.gov.ng/out/eduseries/seriesinflation.pdf>

The Nigerian Context

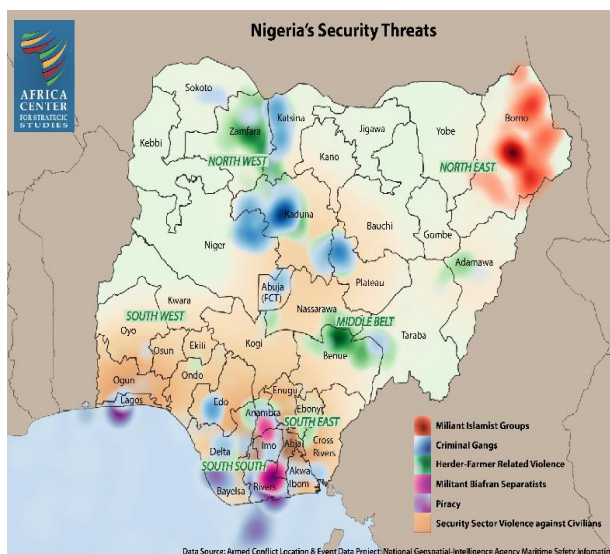
Figure 1 shows the trend in inflation and real minimum wage over the years, which highlights a concerning struggle of workers as inflation outpaces the minimum wage increases. For instance, a worker earning N18,000 minimum wage in 2011 might have been able to purchase a bag of rice. However, due to inflation, today's minimum wage of N30,000 is insufficient to purchase the same bag of rice. When accounting for inflation with 2011 as a base year, the real monetary value of a worker's earnings today is only N 5,244.03, despite the minimum wage being N30,000.

Fig 1. Inflation Vs Real Minimum Wage



Source: IMF (2024)⁴ and estimation by authors using available data from NSIWC

The Nigerian economy is currently characterized by cost-push inflation which has several factors contributing to it, including:



- Insecurity:

Ongoing insecurity and conflicts, including banditry, farmer-herder clashes, Boko Haram, and kidnapping in most northern states like Borno, Benue, Katsina, Zamfara, Kaduna, and Sokoto, have caused significant instability and disruption in the country's agricultural sector and logistics management. This has resulted in severe food inflation because these regions produce most of the food items.

Fig 2. Map showing Insecurity threat in Nigeria⁵

⁴ <https://www.imf.org/external/datamapper/PCPIPCH@WEO/OEMDC/ADVEC/WEOWORLD/NGA>

⁵ <https://africacenter.org/spotlight/nigeria-diverse-security-threats/>

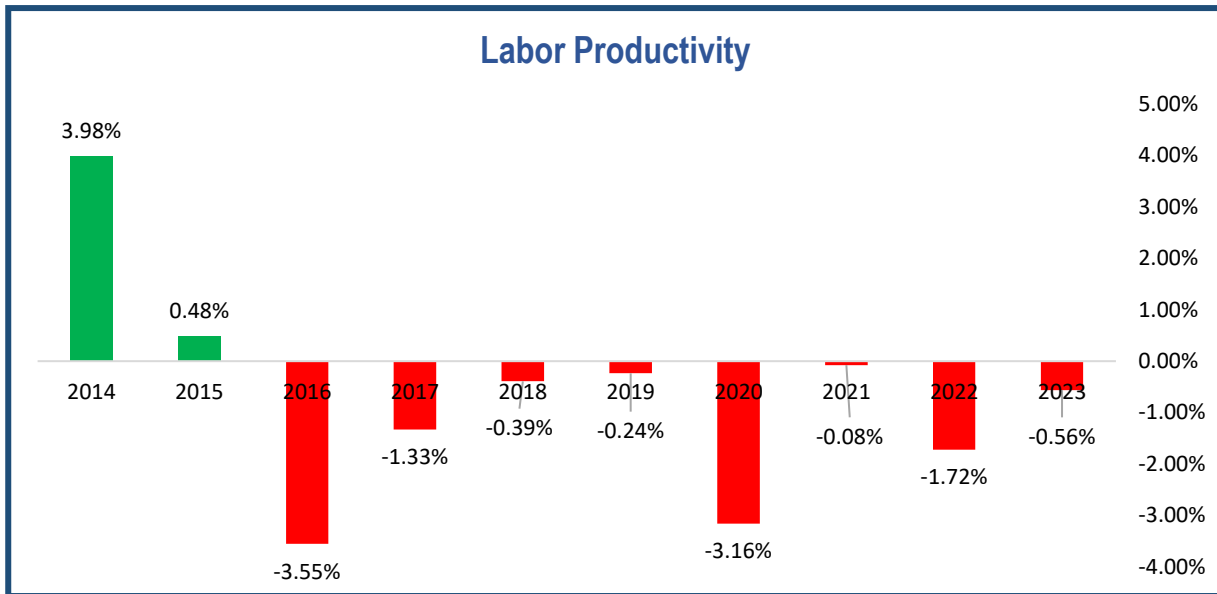


Fig. 3 Labor productivity
Source: ILO (2024)⁶

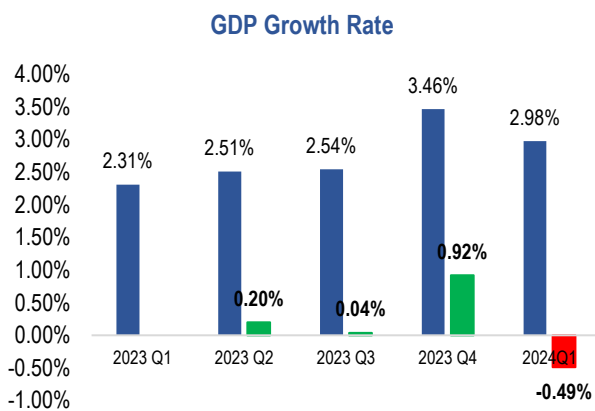


Fig. 4 GDP Growth Rate

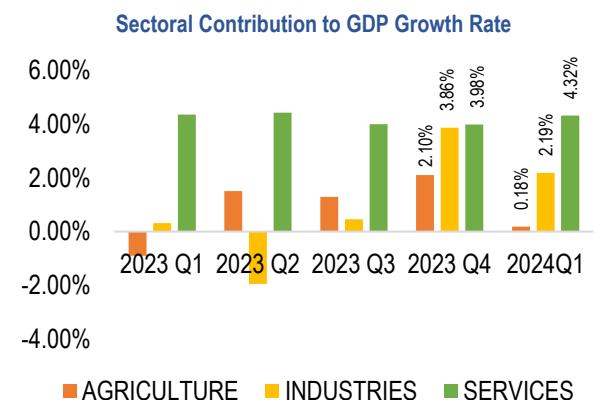


Fig. 5 Sectoral Contribution to GDP Growth Rate
Source: NBS (2024)⁷

- Low Productivity: Labor productivity gives insight into the efficiency and quality of human capital in the country's production process, measuring how effectively inputs are used in an economy to produce goods and services. Therefore, it is a key indicator of economic growth, competitiveness, and living standards (ILO). We used the average output per worker data from the ILO to highlight how low productivity has affected the economy and fueling inflation. Despite the GDP growth rate appearing promising, the GDP growth rate in the first quarter of 2024 fell by 0.49% compared to the growth rate recorded in Q4 of 2023, highlighting the economic slowdown. This slowdown can be seen from the sectoral contribution growth rate over the period; for instance, the growth rate of the agricultural sector to GDP was 2.10% in 2023 Q4, industries were 3.86%, and services were 3.98%.

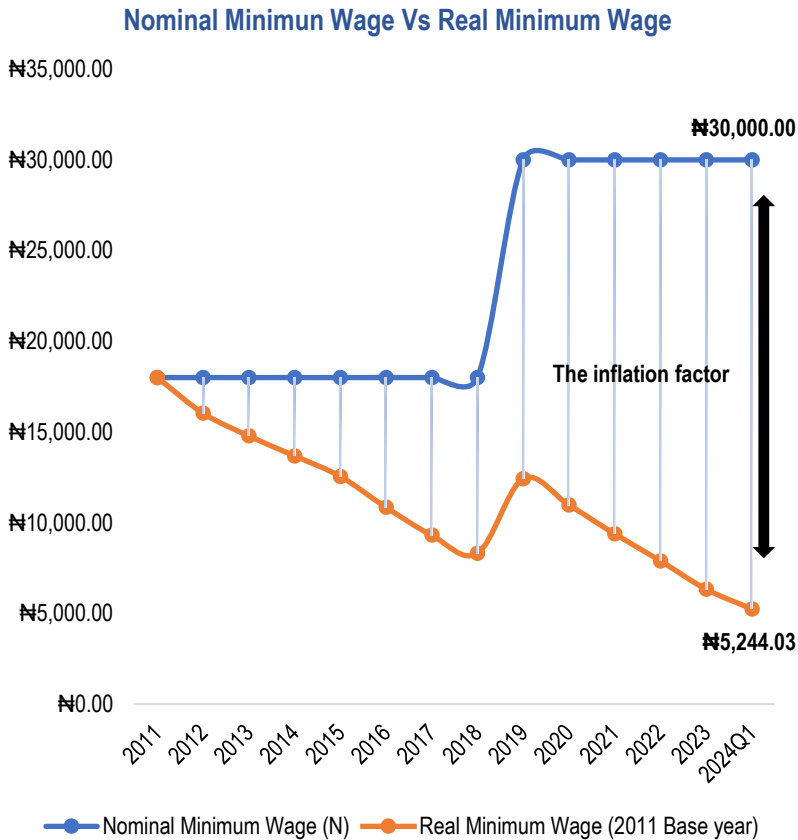
However, the growth declined significantly in Q1 of 2024, with agricultural sector growth standing at 0.18% and industries at 2.19%, except for services, which grew by 0.34% in Q1 2024 compared to Q4 2023. To further probe this decline, we looked at the average labor productivity year on year, which has consistently been negative over the years, reflecting reduced performance and inefficiency within the workforce. These performances, especially within the agricultural sector, can be linked to the security issues highlighted above, which are directly linked to food inflation.

⁶ <https://ilostat ilo.org/topics/labour-productivity/#>

⁷ <https://nigerianstat.gov.ng/elibrary/read/1241506>

- **Rising Production Costs:** Several factors have contributed to recent major increases in production costs. These include rising energy costs from increased diesel prices, which is used in generators for power supply, higher petrol prices due to the removal of fuel subsidies, increased electricity tariffs, depreciation of the Naira, higher interest rates, and various taxes, all of which contribute to cost-push inflation.

Minimum Wage and Inflation



Source: Our estimation is based on available data from NSIWC

Minimum Wage and Inflation

Does increasing the minimum wage increase inflation in Nigeria's context?

No, in Nigeria's current economic context. Here's why

A careful look at the trend over years of the nominal and real minimum wage gives us an idea of how much monetary value workers have received over the years. Given the existing high inflation rate of over 33%, the purchasing power of many workers has already been significantly eroded. An increase in the minimum wage in such a scenario is unlikely to lead to further substantial inflation. Additionally, many Nigerians are currently living in a hand-to-mouth economy, where any increase in income is quickly absorbed by basic necessities rather than discretionary spending, which could drive up demand-pull inflation.

Inflation is influenced by many factors including those we highlighted above. However, the relationship between minimum wage increases and inflation is clear from the above charts, where we highlighted that while the real minimum wage has been falling over the years, the inflation rate has spiraled consistently over the years.

Policy Recommendations

In this section, we offer a minimum wage recommendation to the government and organized labor based on the current economic reality. Our recommendations are grouped into two scenarios: the best-case and worst-case scenarios.

1. Best Case Scenario.

Here, we used data from the National Bureau of Statistics (NBS) and other sources. According to the April 2024 NBS reports, the average cost of a healthy diet in Nigeria is ₦1,035 per day. The average intra-city transport fare for bus commuters is ₦967.76, and the average fare for Okada (motorcycle) is ₦476.49. Additionally, a poll conducted in May 2023 by [NOI Polls](#)⁸ indicated that 47% of Nigerians spend an average of ₦5,000 per month on electricity bills. Given that an individual must have three regular meals daily (breakfast, lunch, and dinner) to maintain a healthy and quality life, we based our calculations on this for 30 days. We also considered the average transportation fare for Okada, reflecting the reality of many working Nigerians who use Okada at least twice daily, commuting to and from work, assuming a 20-day working month. To incorporate other basic life necessities, we referred to the NBS consumption pattern report, and the breakdown we provide is detailed below:

Basic Necessities	Monthly Average
Food	₦93,150.00
Rent	₦849.18
Transport Okada	₦19,059.60
Health	₦984.13
Education	₦971.62
Electricity Bill	₦5,000.00
Clothing AND Footwear	₦729.03
Savings (20% of Income)	₦23,148.71
Proposed Minimum wage/month	₦143,892.28

Source: NBS (2020)⁹ and our estimations

In a best-case scenario, we applied the 50-30-20 rule, where workers are expected to save at least 20% of their monthly income for emergencies or other future goals.

2. Worst Case Scenario

In the worst-case scenario, we assume that individuals live in a hand-to-mouth economy, without savings, and in an unelectrified environment.

Basic Necessities	Monthly Average
Food	₦93,150.00
Rent	₦849.18
Transport Okada	₦19,059.60
Health	₦984.13
Education	₦971.62
Clothing and footwear	₦729.03
Proposed Minimum wage/month	₦115,743.56

Finally, to ensure that workers receive a living wage, we recommend that the Federal Government adopt and implement this proposal. Our research shows that many states have not implemented the ₦30,000 minimum wage since its approval. Therefore, we also recommend that as the final approver, the federal government should enforce compliance among state governments as this will enable the workers to achieve a minimum wage that supports a decent standard of living.

In response to the concerns about the government's ability to fund the proposed minimum wage, we suggest financing it by reducing wasteful and over-bloated expenses.

⁸ <https://www.noi-polls.com/post/only-57-percent-of-nigerian-electricity-customers-are-metered>

⁹ <https://nigerianstat.gov.ng/elibrary/read/1094>