

# Introducing a statutory minimum wage in middle and low income countries

## Successful implementation of a statutory minimum wage depends on context, capacity, and institutional design

Keywords: minimum wages, institutional design, developing countries, informality, enforcement

### ELEVATOR PITCH

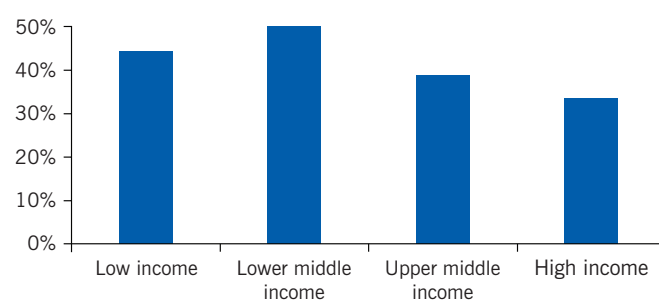
Motivations for introducing a statutory minimum wage in developing countries include reducing poverty, advancing social justice, and accelerating growth. Attaining these goals depends on the national context and policy choices. Institutional capacity tends to be limited, so institutional arrangements must be adapted. Nevertheless, a statutory minimum wage could help developing countries advance their development objectives, even where enforcement capacity is weak and informality is pervasive.

### KEY FINDINGS

#### Pros

- ⊕ There is often public demand for a statutory minimum wage, providing political cover for implementing it.
- ⊕ The prevalence of market frictions and monopsony power in developing countries means that the conditions under which minimum wages can increase employment often hold.
- ⊕ Minimum wages can protect workers with low bargaining power from exploitation.
- ⊕ Minimum wages can increase household income when the employment shifts to the informal sector are not large.
- ⊕ Institutional mechanisms can be developed and adapted for developing countries.

Share of countries without a statutory minimum wage



Source: [1], [2]

IZA  
World of Labor

#### Cons

- ⊖ Other tools for poverty reduction can be more effective than a minimum wage.
- ⊖ Minimum wages can cost formal sector jobs and increase the size of the informal sector.
- ⊖ Political economy and analytical capacity concerns must be addressed in designing governance institutions.
- ⊖ Developing countries may be tempted to set initial minimum wages too high (at levels that reduce total employment) relative to the productive structures of their economy.
- ⊖ Enforcement, coverage, and complexity are major problems for institutional design in developing countries.

### AUTHOR'S MAIN MESSAGE

When the conditions are right, developing countries could consider introducing a minimum wage as one tool for reducing poverty and worker exploitation and for potentially enhancing total (formal plus informal) employment and growth. The institutional mechanisms set up to implement the minimum wage, however, influence how effective it will be in attaining its objectives. Political economy issues require attention to ensure that the policy is implemented as effectively as possible.