

**National
Minimum
Wage**



Low Pay Commission

The National Living Wage:

A summary of the LPC's findings on
the £7.20 introductory rate

Introduction

This report provides brief summary analysis of the impact of the introductory rate (£6.70) of the National Living Wage (NLW), the new minimum wage rate for workers aged 25 and over which was introduced in April 2016. We assessed its impact using written and oral evidence from employer and employee representatives, visits to different areas across the UK, commissioned research and comprehensive analysis of the available economic data.



National Minimum Wage	National Living Wage
Age 21+, 1 October 2015 to 31 March 2016	Age 25+ from 1 April 2016
Ages 21–24 from 1 April 2016	£7.20

For comprehensive analysis see the Low Pay Commission's full report at



<https://www.gov.uk/government/publications/national-minimum-wage-low-pay-commission-autumn-2016-report>



<https://twitter.com/lpcminimumwage>



The NLW was a major intervention

The introduction of the NLW for workers aged 25 and over on 1 April 2016 was a significant intervention in the labour market.

The introductory rate of the NLW was set at £7.20. The LPC's remit is to advise on the path of the NLW, with the ambition of reaching a target of 60 per cent of median earnings by 2020.

In surveys, employer representatives reported that a third to a half of firms faced higher wage bills. The scale of the effects and ways of responding to the NLW varied.

THE MINIMUM WAGE FOR WORKERS AGED 25 AND OVER INCREASED BY **10.8%** OVER THE YEAR THE JOINT LARGEST EVER INCREASE

According to employee representatives, many workers have benefited from higher pay. A typical minimum wage worker (who works an average of 26.2 hours per week) would earn £680 more in a year after moving onto the NLW, or £590 adjusted for inflation.

Growth in the NMW/NLW compared to different points in the earnings distribution for workers aged 25 and over, UK, 2015–2016

	April 2015	April 2016	Growth
Minimum wage for those aged 25 and over	£6.50	£7.20	10.8%
Median hourly earnings	£12.38	£12.77	3.1%
Mean hourly earnings	£15.52	£16.16	4.1%
10th percentile of hourly earnings	£7.10	£7.50	5.6%
25th percentile of hourly earnings	£8.74	£9.04	3.5%

Source: LPC estimates using: ASHE April 2015 and 2016, standard weights, excluding first year apprentices, UK. Note: Hourly earnings estimates exclude overtime.

1.6m workers (25+) are now paid the NLW

The substantial increase is reflected in the fact that around

1.6m workers



OF THOSE AGED 25 AND OVER – WERE COVERED BY THE NLW IN APRIL 2016

rising to about

1.9m workers

OF ALL AGES (7.1% OF JOBS) COVERED BY THE NLW OR ONE OF THE OTHER MINIMUM WAGE RATES

compared with

1m covered by

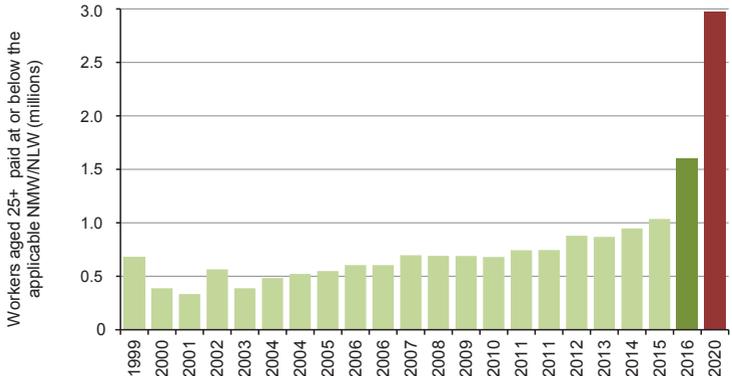


THE NATIONAL MINIMUM WAGE FOR THOSE AGED 25+ IN APRIL 2015

Up to 3m workers

AGED OVER 25 WILL BE COVERED BY THE NLW BY 2020

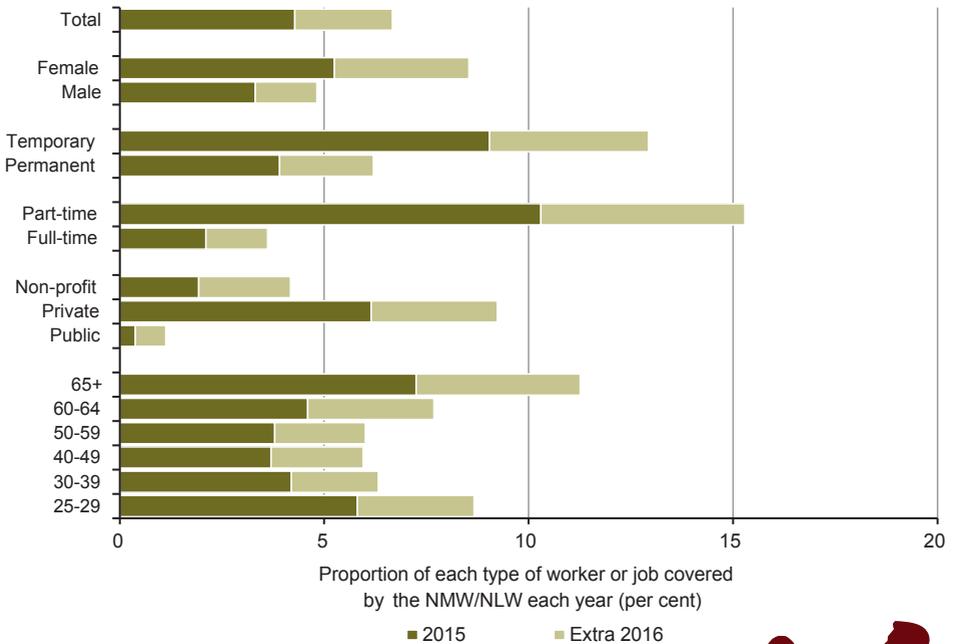
Coverage of the NMW/NLW for workers aged 25 and over, UK, 1999-2020



Coverage has grown for a range of workers...

In April 2016, coverage, which is the share of workers paid at or below the NLW, was higher for workers in the private sector (9 per cent), for 25-29 year olds (8 per cent) and those aged 65 and over (11 per cent). Coverage was particularly high for part-time workers, with one in seven of those aged 25 and over on the NLW (15 per cent) compared with less than one in twenty five full-time workers (4 per cent).

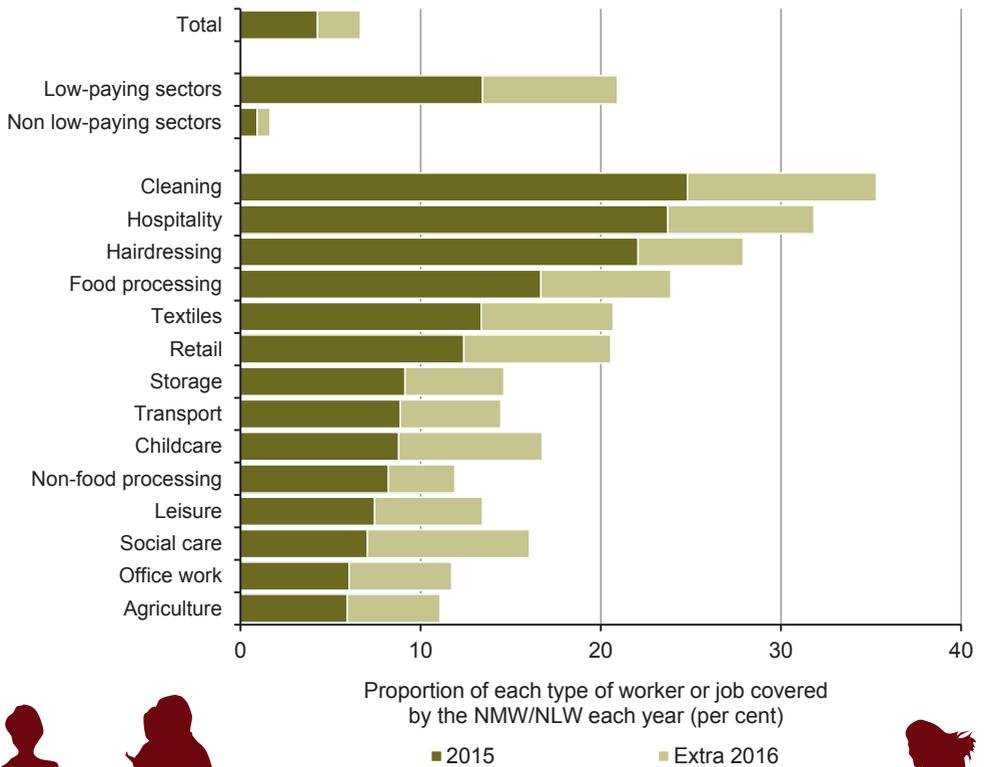
Coverage of the NLW/NMW for workers aged 25 and over, by worker and job characteristics



... and in all low-paying sectors

All low-paying sectors saw increases, with on average one in five workers in these occupations now covered. In sectors including cleaning, hairdressing and hospitality more than a quarter of the workforce aged 25 and over was paid at or below the NLW in April. In social care, the proportion was lower, but the change bigger with coverage more than doubling to 16 per cent.

Coverage of the NLW/NMW for workers aged 25 and over, by occupation



Summary of stakeholder views

We received a wide range of views on the effects of the NLW so far, but they could generally be divided into three groups:

- Supporters and those little affected
- Those concerned about the affordability of the introductory rate
- Those concerned about the path to 2020

Affected firms reported a range of consequences for...

- Pay
- Employment
- Competitiveness

Certain sectors were more concerned about the introductory rate of £7.20:

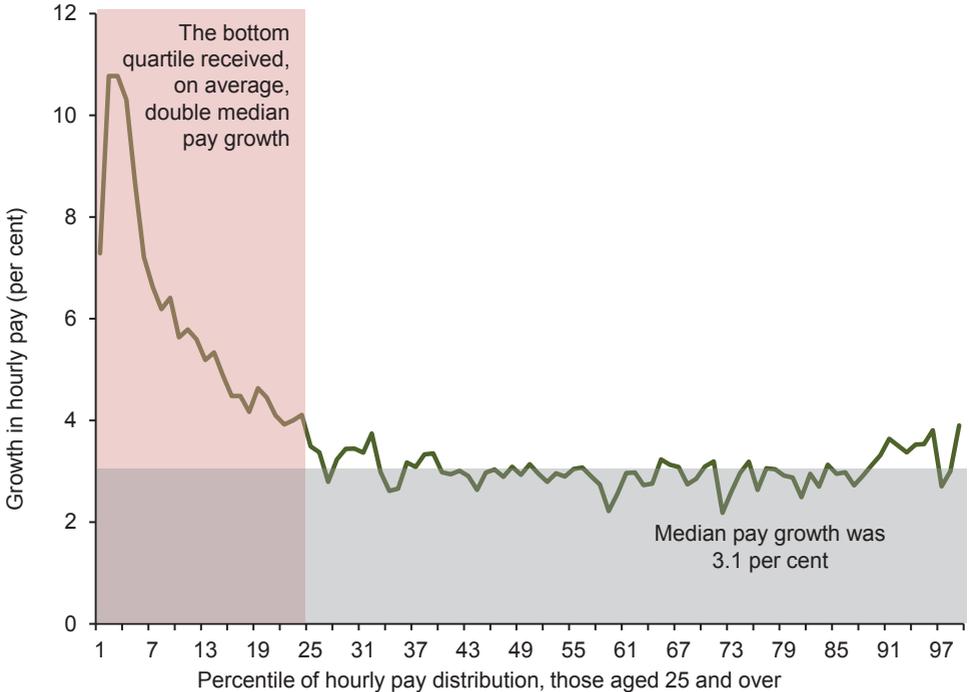
- Adult social care
- Horticulture
- Convenience stores
- Childcare
- Textiles

Stakeholders suggested that more sectors will be affected by the NLW as it rises towards the 2020 target of 60 per cent of median earnings. This included representatives of the hospitality and retail sectors.

Pay growth was higher at the bottom end...

The NLW not only increased pay for those at or close to the previous NMW rates but also had ripple effects further up the distribution. Pay growth above the average is seen for the entire bottom quarter of the distribution, or workers earning up to £9 per hour in 2016.

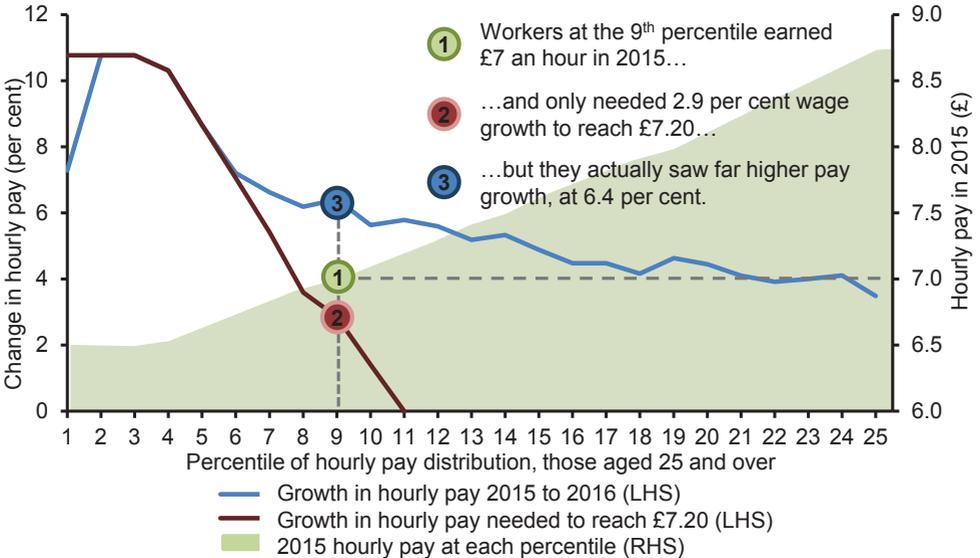
Percentage growth in the hourly wage distribution for workers aged 25 and over, UK, 2015-2016



...but the NLW has had ripple effects up the pay distribution

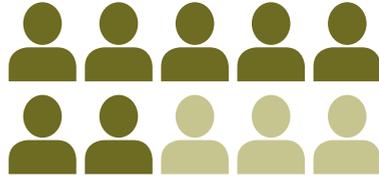
This chart shows the hourly pay of workers in the bottom quartile in 2015 (green area), the minimum pay increase they would need to reach £7.20 (maroon line) and the pay increase they actually received (blue line). Many workers received larger increases than necessary to keep their pay compliant. For example, those on hourly wages of £7.00 in 2015 (at the ninth percentile), required an increase of 2.9 per cent to reach £7.20. But in actual fact wages at this level increased by 6.4 per cent between April 2015 and April 2016, to reach £7.45.

Percentage growth in the hourly wage distribution for workers aged 25 and over, UK, 2015-2016



Many younger workers have benefited

These spillovers not only benefitted those further up the pay distribution, but also workers aged under 25.



UP TO



OF 16-24 YEAR OLD
EMPLOYEES WERE
LIFTED ABOVE

£7.20

IN RESPONSE TO THE RATE

7/10

WERE PAID AT OR ABOVE
THE NLW IN APRIL 2016,
UP FROM

6/10

AT THE EQUIVALENT
LEVEL IN 2015

**Proportions of 16–24 year olds paid at or above the NLW level,
UK, 2015–2016**

	Paid at or above NLW-level in 2015	Paid at or above NLW in 2016	Increase between 2015 and 2016
	(per cent)	(per cent)	(percentage point)
16–17	16	25	9
18–20	46	52	7
21–24	76	84	8
16–24	62	69	7

Source: LPC estimates based using: ASHE April 2015–2016, low pay weights.

These pay increases benefit workers but create costs for employers

Some stakeholders in affected sectors reported reductions in differentials, presenting challenges for progression and motivation of staff paid just above the minimum.

A FARM IN HEREFORDSHIRE TOLD US THAT IT HAD REDUCED THE DIFFERENTIAL BETWEEN THE NLW AND SUPERVISORS' RATES FROM 11 PER CENT TO A MAXIMUM OF 5.5 PER CENT. 70 PER CENT OF ITS PRODUCTION COST IS LABOUR SO THE BUSINESS IS SENSITIVE TO CHANGES IN WAGE RATES.

Representatives of the horticulture sector told us that there have been widespread reductions in differentials. Businesses have in many cases not been able to afford to maintain the gap between workers on the NLW and higher pay bands.

In social care, research (Gardiner, 2016) found that pay has become more bunched at £7.20, with a third of the workforce paid at the NLW, compared to a fifth on the adult rate of the NMW previously. However, the research also found that there had been spillovers further up the distribution, with firms surveyed spending twice as much in raising pay than the minimum required to meet the NLW.

In other sectors employers have sought to maintain differentials fully, but at higher wage cost. In hospitality, the Association of Licensed Multiple Retailers said that a large majority of its members had done so.

Our analysis suggests that the biggest differences in pay increases, between minimum wage workers and those slightly above were seen in office work and storage. Other sectors, such as hospitality, cleaning and childcare, tended to pass on more of the increases to slightly better-paid workers (likely reflecting that

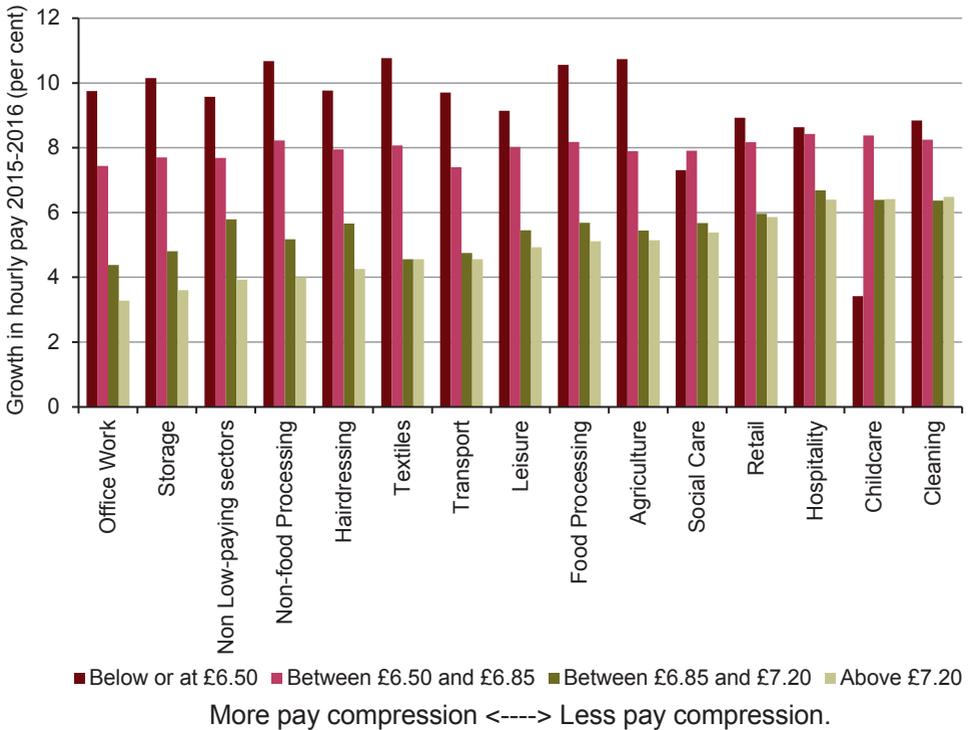
these sectors already had very compressed pay).

In line with media reports on the NLW, stakeholders told us that, in some cases higher wage costs may have been offset by reductions in benefits and premium pay – though we find no significant change in the use or levels of shift premium pay and overtime pay in the aggregate data so far (which could be a timing issue, or a compositional effect).

Use of youth rates

We received few reports of firms increasing use of the youth rates of the minimum wage to reduce costs. In social care and horticulture, we saw little evidence of firms differentiating pay by age, at this stage. However, pubs, bars and restaurants reported that use of the youth rates had been common for some time in hospitality, and some thought that they may explore this option further in the future.

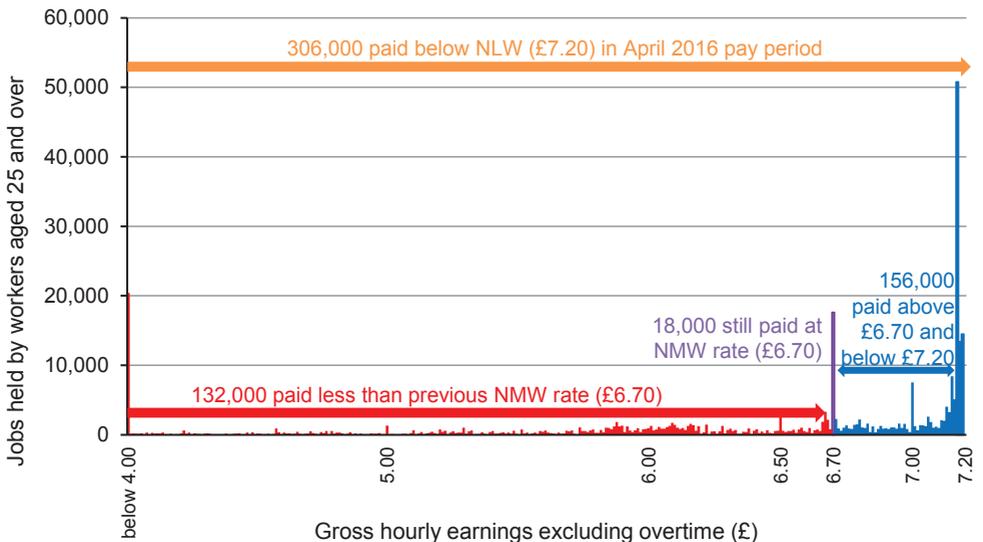
Growth in hourly pay for workers aged 25 and over, by sector



Despite pay growth some are underpaid

Increases in pay appear to have been accompanied by a rise in temporary underpayment. On our best estimate, 306,000 workers aged 25 and over were paid less than the applicable rate in April 2016 (1.3 per cent of all over-25s, or 19 per cent of coverage), up from 158,000 workers aged 25 and over in April 2015. The increase may reflect higher non-compliance at the start of the NLW year. A change in the minimum wage calendar means the April survey that measures underpayment now captures its level just after the uprating rather than at the mid-year point, as previously. However, even if some of the increase in underpayment is simply frictional, as some employers take time to adjust to the new rates, it is still illegal, disadvantageous to workers and (on these data) large-scale, affecting up to a fifth of workers covered by the NLW. (It should be noted that not all cases where workers are paid less than the applicable rate are non-compliant; this is because some deductions are permitted, for example the accommodation offset).

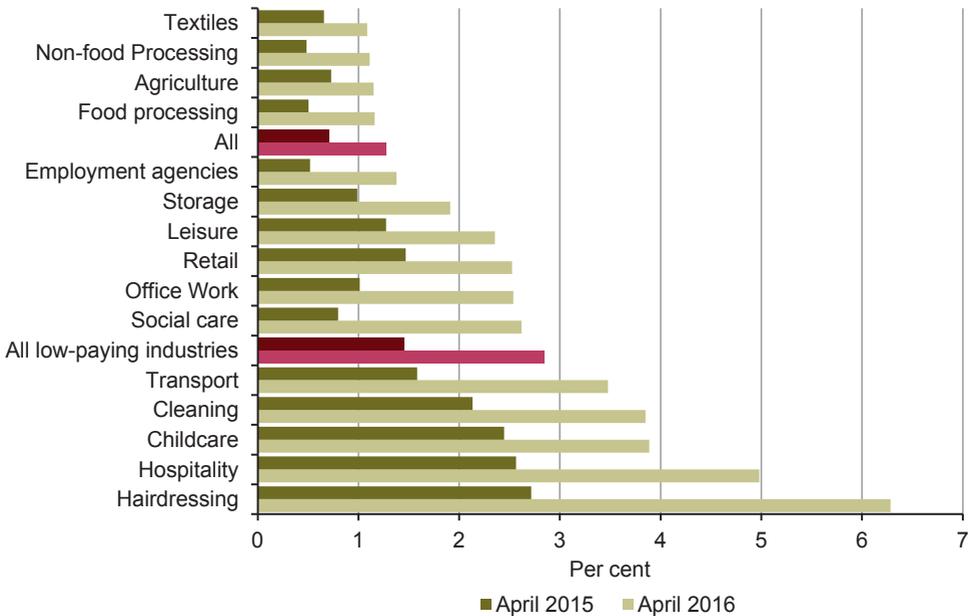
Hourly earnings distribution below NLW, for employees aged 25 and over, 2016



Underpayment highest in hairdressing, hospitality, childcare and cleaning

The chart illustrates the apparent increase in measured underpayment across all sectors in 2016 compared with 2015 (noting that these data contrast different points in the minimum wage year). Whilst the share of workers in low-paying sectors and who are underpaid increased from 1.5 per cent to 2.8 per cent, the highest rates of underpayment were found in hairdressing, hospitality, childcare and cleaning.

Proportion of employees aged 25 and over paid below the NMW/NLW by Sector, UK, 2015-2016



There is little evidence of an aggregate employment effect in the limited data available so far

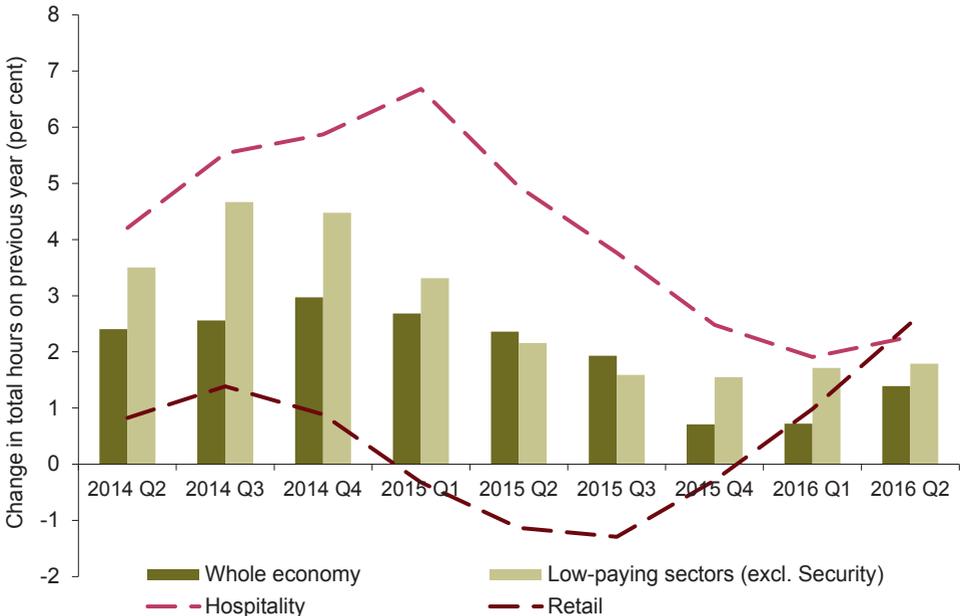


At the time of writing there was only one quarter of labour market data available following implementation of the NLW, five quarters following its announcement. On this data, we have identified no clear evidence of aggregate employment or hours effects arising so far from the NLW, with strong employment performance among the types of workers most likely to be on the NLW and no clear patterns in changes to employment or jobs. However some low-paying sectors have warned that they reduced working hours, job growth or employment in response to the introductory rate, with concerns about future sustainability.

When looking at employment change by age we see that those age groups most likely to be on the NLW, 25-29 year olds and those aged 60 and over, have seen relatively strong employment growth.

Equally, growth in the number of hours worked in low-paying sectors continues to outstrip that in the rest of the economy, with growth in retail and hospitality.

Change in hours by low-paying sector and the whole economy, UK, 2014-2016



The key low-paying sectors warning of reduced employment include horticulture, textiles and convenience stores. For example:

- Three quarters of respondents to a survey by the Association of Convenience Stores had reduced hours, and two thirds had reduced staff numbers.
- In a survey by the National Farmers' Union, one fifth of affected horticulture firms had reduced the number of people they employ.
- Hours reductions were a more common response than job losses in hospitality, according to the ALMR and British Hospitality Association.

We also heard of businesses reducing their use of labour through hours on our visits.

It was, though, difficult to identify the overall scale of any employment effects from the stakeholder evidence we received. Surveys did not establish how many jobs would be lost in sectors that reported employment effects, or whether these jobs would be replaced by new ones. We will look at employment effects in much

greater depth as further evidence emerges.

Profits, prices and productivity

The most common effects of the NLW identified in survey data were to the competitiveness of businesses. In response to the NLW, many firms report accepting lower profits, some raising prices, and others seeking to raise productivity.



Profits

- Absorbing the cost with the consequent lowering of profits was the most common response in surveys by the Chartered Institute of Personnel and Development and Federation of Small Business, with 17 and 30 per cent of respondents respectively reporting that approach.
- In specific sectors, it was also a popular response, being the most common action taken by firms in surveys by the National Farmers' Union and National Hairdressers' Federation, though representatives tended to argue this would be harder for future increases.



Prices

- Price rises – passing the cost of the NLW on to customers – was also a common response. Respectively, 14 and 12 per cent of respondents in Resolution Foundation and British Chambers of Commerce surveys had increased prices, compared to between 6 and 9 per cent reporting reduced hours or recruitment.
- The British Hospitality Association said that where market conditions have tolerated it, prices have increased.

THE BRITISH RETAIL CONSORTIUM TOLD US THAT FEW FIRMS IN THE SECTOR HAD RAISED PRICES, REFLECTING PRICE DEFLATION IN RETAIL, AN EXTREMELY COMPETITIVE SECTOR WITH CLEAR GEOGRAPHICAL AND SECTORAL DIVERGENCES IN PRICING BEHAVIOUR.

- However, firms in some sectors said they had been unable to raise prices – both price competitive sectors facing

structural change like retail and internationally traded sectors like textiles.



Productivity

- Stakeholders generally agreed that raising productivity remains central to the long-term sustainability of the NLW.
- Resolution Foundation found that more firms affected by the NLW (two thirds) had sought to increase productivity than unaffected firms (just under half).

A CHAIN OF CONVENIENCE STORES IN NORTHERN IRELAND TOLD US THAT DUE TO THE £45,000 COST OF THE INTRODUCTION OF THE NLW (REACHING UP TO £200,000 BY 2020), INVESTMENT HAD BEEN POSTPONED. NEW TILLS AND FREEZERS WOULD HAVE COST £65,000, BUT THE MONEY WAS NEEDED TO PAY FOR THE NLW.

- However, the BRC and CIPD suggested that, while firms wanted to raise productivity, specific ways of doing so had yet to fully emerge.

- Some warned that investment, which is important for productivity, was affected by the increase in costs brought about by the NLW. In affected sectors including farming and convenience, but also in hospitality, some firms reported that investment has been cancelled or decisions delayed.
- Stakeholders suggested that in the long-term, productivity gains could arise from a combination of investment and automation, job redesign, or work intensification - with the effects on employment likely to vary by sector.
- Representatives of other sectors said that raising productivity was a real challenge. In horticulture, soft fruit farmers said that the technology to automate harvesting does not yet exist;

in hospitality, some hoteliers were concerned that levels of customer service would be affected if they used more technology, such as self-service check-in. Across a number of sectors, business representatives thought higher wage costs might drive structural change: with, on the one hand, high-labour premium services and, on the other, low-labour budget services.

- Other employers and employee representatives were optimistic about the scope for productivity gains, with some arguing that higher pay would improve motivation, reduce absenteeism and staff turnover costs, and encourage investment in training.

Again, we will investigate changes in productivity further as more data emerges.



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