

BERR | Department for Business
Enterprise & Regulatory Reform

**Government evidence to the
Low Pay Commission on the
economic effects of the
National Minimum Wage**

DECEMBER 2008

Contents

Executive summary	3
1 Macroeconomic conditions and outlook	6
2 Evidence on pay.....	14
3 Impact on the labour market.....	27
4 Developments in the labour market for younger workers	36
5 Other issues	40
ANNEX A Employment in low-paying industries.....	47
ANNEX B Employment and unemployment rates by age group.....	51
ANNEX C Regional employment in low-paying industries	56
ANNEX D International comparison of minimum wage rates.....	58
ANNEX E European employment and unemployment rates.....	59
ANNEX F Review of recent minimum wage research	62
ANNEX G Beneficiaries of the 2008 NMW uprating by sex and region .	70
ANNEX H Technical note.....	71

Executive summary

The Government welcomes this opportunity to present the Low Pay Commission (LPC) with economic evidence on the National Minimum Wage (NMW) in the LPC's twelfth year of operation. This document forms the second half of the Government's annual submission, covering the economic effects of the NMW. It should be read in conjunction with the previous Government submission on the non-economic evidence.

It is widely agreed that the NMW has been successful and is now firmly established as a key element of UK labour market policy. The Government is determined to keep the NMW under close review, and has examined the developing evidence of its economic and labour market impact. The main findings of the Government's assessment on the economic evidence are:

Macroeconomic conditions and outlook

Since mid-2007, the world's economies have been hit by two major shocks: a credit shock that has intensified into the worst global financial crisis for generations and a surge in commodity prices, which had built over a number of years. These economic shocks have affected all countries.

The UK economy has slowed as credit conditions tightened and food and energy prices squeezed household incomes and company profits. The combined effects of these shocks has been to push the UK economy into recession and inflation to a 16 year high.

While global commodity prices have come down significantly, financial instability grew steadily, peaking in the weeks following the collapse of Lehman Brothers.

The events of September and early October 2008, when the global financial system was at risk of collapse prompting an unprecedented global policy response, illustrate vividly the exceptional uncertainties now surrounding any economic forecast, even for near-term prospects. Short and medium-term growth prospects in the UK remain subject to exceptional uncertainty.

Since the introduction of the minimum wage in 1999 the UK labour market has fared well, with the level of employment increasing by around 2.4 million. However, employment has fallen in recent months. Despite this, employment remains high by historical standards and the labour market remains strong in a historical perspective. While the unemployment rate has improved over this period, it has been rising since the beginning of 2008.

Evidence on pay

Average earnings have risen faster than price inflation since 1999 and the minimum wage has increased faster than average earnings. As a consequence, the minimum wage as a percentage of the median wage – known as the 'bite' - is now around 51 per cent, an increase of around 5 percentage points since 1999. The bite is higher for small firms (58 per cent) and the low-paying sectors (ranging from 65 per cent to 90 per cent). As the NMW has risen, an increasing proportion of employees are earning wages near the minimum wage. The NMW may also have had knock on or an 'upward ripple' effect causing quicker rises in pay amongst the group just

above the NMW. However, this ripple effect dissipates as it moves up the wage distribution.

Impact on the labour market

While UK academic research to date has not found overwhelming evidence that the adult minimum wage has reduced employment, there has not yet been time for the full impact of the recent minimum wage upratings to be seen. In addition, the minimum wage has not yet been in place through a significant economic downturn or recession. Early indications from Dickens and Draca (2005) which looked at the impact of the minimum wage increase in 2003 and Mulheirn (2008) which examined the impact of the 2006 uprating found no significant evidence of an adverse employment impact.

There has been a slight decline in the share of UK employment in low-paying sectors since 1999. However, there is no evidence that this is the result of the minimum wage and the trend also predates the introduction of the NMW.

There is some evidence of a small impact of the NMW on hours worked. Over 1999-2008 total hours worked in the low-paying sectors grew around 5.6 per cent, less than the 6.5 per cent growth in the non low-paying sectors. The slight decline in the share of UK employment since 1999 in low-paying sectors partly explains the smaller growth in total hours worked but there has also been a slight fall in mean hours worked in low-paying sectors.

The evidence presented so far has been in the context of a growing labour market. There is less evidence, from both the UK and internationally, of the impact of minimum wages in periods of economic downturn. Within the context of the current economic climate and the associated macroeconomic risks and uncertainties, and coupled with an increasing bite and coverage of the NMW, it is even more important that the available evidence is taken in context and the wider economic and labour market impacts are considered when setting the NMW rates.

Developments in the labour market for younger workers

The labour market has proved challenging for some younger workers. The employment rate of 16 and 17 year olds, excluding full-time students, has been declining for the last decade, although it has slightly improved over 2007 and the first half of 2008. The 18-21 year old age group has also experienced a fall in employment rates since around mid 2001, but this drop is much smaller than for their younger counterparts.

Past experience suggests that unemployment amongst young people tends to grow faster than for older workers during an economic downturn.

Other issues

Section 5 of this report covers other issues which include the use of tips as part of the NMW, holiday entitlement, apprentices and migration. More detail can be found in section 5.

The Government is consulting on the use of tips as part of the NMW which will mainly affect the restaurant and hotel sectors. If tips are excluded from NMW payments this may have some upward cost implications for NMW employers in tipping sectors.

The Government is increasing the current statutory minimum holiday entitlement from 4 weeks to 5.6 weeks, to take account of 8 bank holidays that should be paid in addition to 4 weeks holiday entitlement. Half of the increase

has already taken effect from October 2007 and the remaining increase will be introduced in April 2009. As a large proportion of those benefiting from the minimum wage will also benefit from the extension of leave, this will have upward cost implications for many NMW employers.

Total immigration (inflows) fell in 2007, but emigration (outflows) fell faster resulting in a marked rise in net inward migration. However, more recent evidence from 2008 suggests inward migration from some areas, such as A8 countries, are slowing, continuing a trend first seen in the second half of 2007. Many recent migrants continue to be employed in lower paid jobs and sectors. The proportion of foreign-national workers in low paying sectors increased further in 2007.

1 Macroeconomic conditions and outlook

Since mid-2007, the world's economies have been hit by two major shocks: a credit shock that has intensified into the worst global financial crisis for generations and a surge in commodity prices, which had built over a number of years. These economic shocks have affected all countries.

In the UK, these shocks struck after a prolonged period of strong and stable growth in output and employment underpinned by low inflation. However, the combined effect has been to push the UK economy into recession and inflation to a 16-year high.

Following the introduction of the minimum wage in 1999 the UK labour market has fared well, with the level of employment increasing by around 2.4 million in the nine years to the end of 2007. Strong output growth in 2007 fed through to strong employment growth, with employment rising by more than 100,000 a quarter from the second quarter of 2007 to the first quarter of 2008. As output growth has slowed, employment flattened in the second quarter and fell by around 100,000 in the third quarter. Unemployment has begun to increase: the claimant count measure has risen by 186,000 since the start of the year, though from a very low level: January 2008 was the first time since mid-1975 that the claimant count had fallen below 800,000.

The Government's latest assessment of the outlook for the UK economy was published as part of the Government's 2008 Pre-Budget Report (PBR).¹

Economic growth

Since mid-2007, the world's economies have been hit by major shocks. Developments in the US subprime mortgage market triggered a credit shock that has intensified into the worst global financial crisis for generations, a crisis that is being addressed by a global policy response of unprecedented scale and scope. The surge in commodity prices, which had built over a number of years, peaked in July 2008 and has since reversed. These economic shocks have affected all countries.

In the UK, these shocks struck after a prolonged period of strong and stable growth in output and employment underpinned by low inflation. GDP grew by 3 per cent in 2007 and employment reached a record high of around 29.5 million. The global credit shock affected property markets in the UK quickly while the rise in commodity prices until the summer squeezed household real incomes and company profit margins. Together with financial market distress, the combined effect has been to push the UK economy into recession and inflation to a 16-year high.

In 2006 and 2007, GDP grew by 2.75 and 3 per cent respectively. Reflecting the impact on the economy of the major shocks it has faced, growth has slowed progressively as credit conditions tightened and real incomes were squeezed by high commodity prices. Quarterly GDP growth in the first half of

¹http://www.hm-treasury.gov.uk/prebud_pbr08_repindex.htm

2007 averaged 0.8 per cent, before slowing progressively to average 0.6 per cent in the second half and 0.1 per cent in the first half of 2008. In the third quarter of 2008, GDP contracted by 0.5 per cent, the first fall in output since 1992, with negative growth across most sectors of the economy.

The 2008 Pre-Budget Report forecast GDP growth in 2008 at $\frac{3}{4}$ per cent. The recession is forecast to continue into the first half of 2009, with GDP contracting by $-1\frac{1}{4}$ to $-\frac{3}{4}$ per cent in the year as a whole.

Lower commodity prices and easing inflation are set to support real incomes in 2009, sterling has depreciated, and monetary and fiscal policies have both been eased to support the economy through the downturn. Together these factors lay the foundations for recovery. Uncertainty remains over how effectively the global financial crisis can be resolved and therefore how soon the financial system can resume its normal function of intermediating funds from savers to borrowers, in order efficiently to finance investment, house purchase and consumption and spread concentrations of risk. Having slowed progressively over the past year, GDP is forecast to fall by a $\frac{1}{4}$ per cent on a year earlier in the second half of 2008, leaving output in 2008 as a whole up $\frac{3}{4}$ per cent on a year earlier. The recession is forecast to continue into the first half of 2009, before GDP growth begins to recover in the second half of the year as credit conditions start to ease and the boost to real incomes from lower commodity prices, the stimulus from monetary and fiscal policy, and the effects of sterling's depreciation, takes hold.

The events of September and early October 2008, when the global financial system came close to collapse prompting an unprecedented global policy response, illustrate vividly the exceptional uncertainties now surrounding any economic forecast, even for near-term prospects. Short and medium-term growth prospects in the UK remain subject to exceptional uncertainty. For instance, the 2008 PBR forecast is based on a number of key forecasting judgements, in particular relating to the path of credit conditions back to a new norm and the structural and cyclical implications of the global financial crisis.

Table 1.1 shows the annual rate of economic growth rose by 0.25 percentage points between 2006 and 2007 from 2.75 per cent to 3.0 per cent. Since Budget 2008, the average of independent forecasts for GDP growth in 2008 has been revised down from 1.7 per cent to 0.9 per cent, close to the 2008 Pre-Budget Report forecast. With independent forecasters expecting contractions in private consumption and investment in 2009, forecasts for GDP growth next year have been revised down progressively and significantly, from 1.9 per cent at the time of Budget 2008 to -0.9 per cent. Since August 2008, this downward trend has quickened as the independent average has fallen from 0.9 per cent to -0.9 per cent.

Forecasts

Table 1.1: Independent forecasts of UK economic outlook

	2006 Actual	2007 Actual	2008 Forecast	2009 Forecast
GDP (%)	2.75	3.0	0.9	-0.9
Consumer spending (%)	1.9	3.1	1.7	-1.4
Claimant unemployment (Q4:million)	0.9	0.8	1.01	1.44
Average earnings (%)	4.1	3.9	3.6	3.4

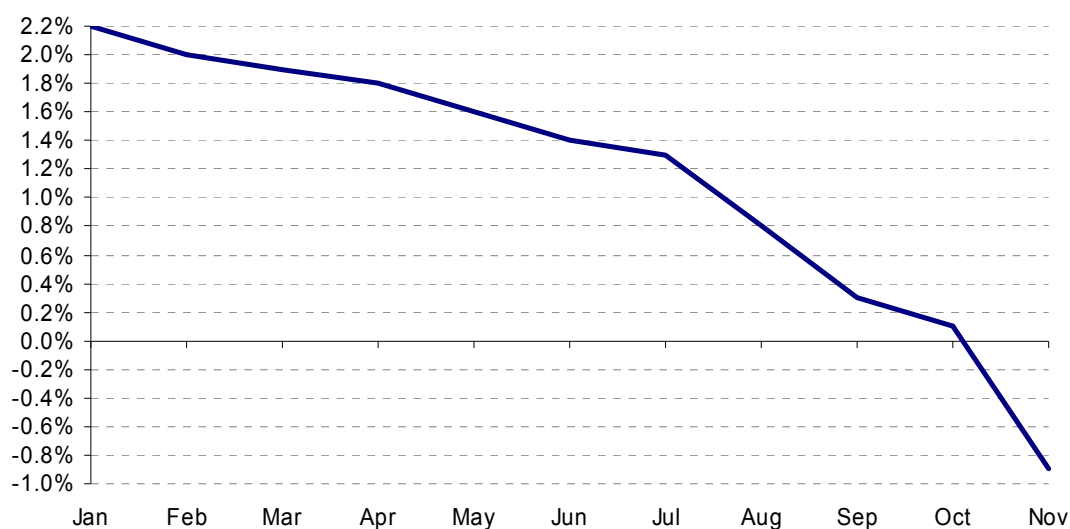
Source: Office for National Statistics; HMT November 2008 survey of independent forecasters

GDP, consumer spending and average earnings (including bonuses) are annual average per cent growth; unemployment is claimant count.

The independent forecasts above were compiled in November 2008. An alternative set of forecasts for GDP growth are collated by Consensus Economics. Similarly to those forecasters surveyed by HM Treasury, Chart 1.1 shows that the average GDP forecast for 2009 has been revised down successively since the start of 2008. It is worth noting that HM Treasury forecasts for GDP growth since 1997 have, on average, outperformed the independent consensus.

Chart 1.1: Consensus forecasts for 2009 GDP growth

Annual percentage change



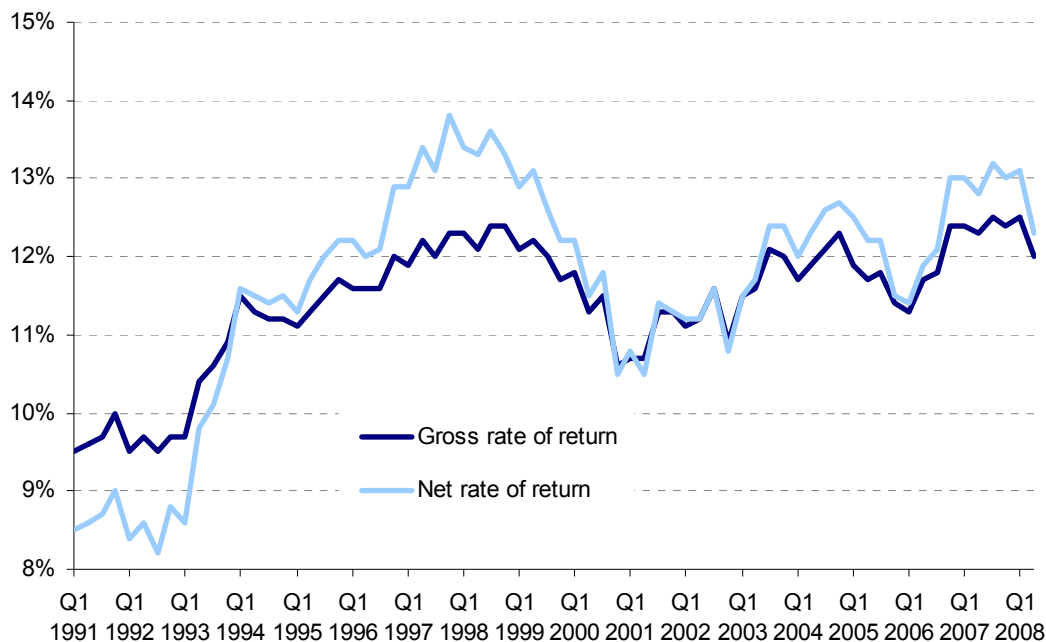
Source: HMT November 2008 survey of independent forecasters

UK company profitability

After a rise in UK company profitability from 2006, profitability begins to dip in the latter part of 2007 and the start of 2008 (see chart 1.2).

Chart 1.2: UK company profitability*

Per cent return



Source: Office for National Statistics

*UK Private Non-Financial Corporations, excluding Continental Shelf Non-Financial Corporations.

The labour market

Since the introduction of the minimum wage in 1999 the UK labour market has fared well, with the level of employment increasing by around 2.4 million in the nine years to the end of 2007. Over the same period the employment rate has touched historic highs and the unemployment rate historic lows.

Strong output growth in 2007 fed through to strong employment growth, with employment rising by more than 100,000 a quarter from the second quarter of 2007 to the first quarter of 2008. As output growth has slowed, employment flattened in the second quarter and fell by around 100,000 in the third quarter. The employment rate has fallen since May 2008 (see Chart 1.3) and is currently 74.4 per cent (2008 Q3) for the working age population.

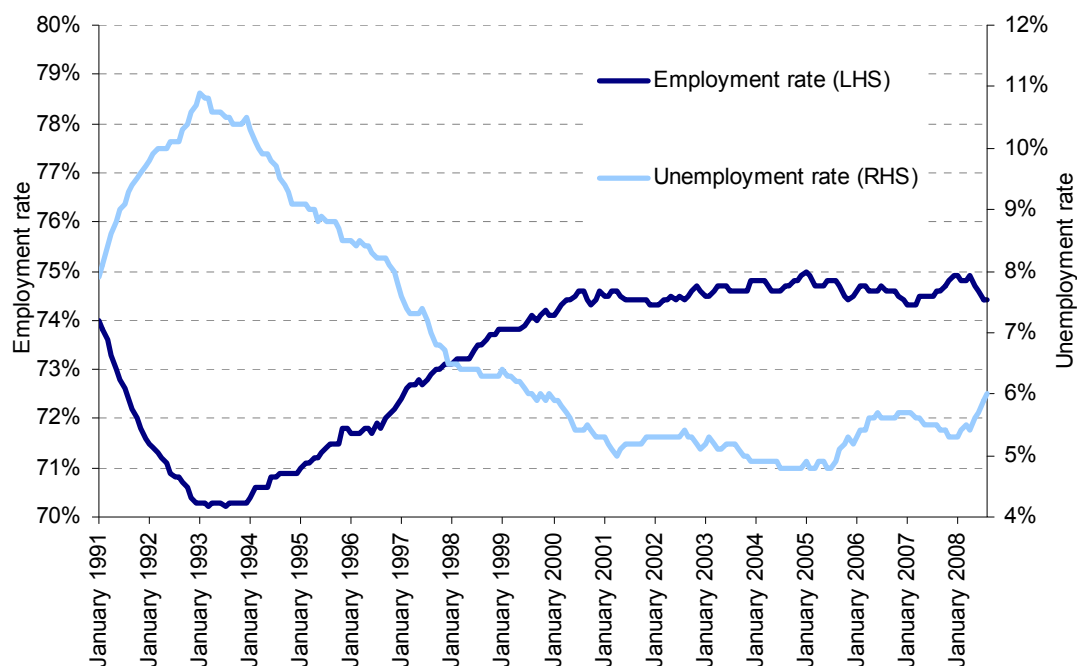
Unemployment has begun to increase, with the Labour Force Survey (LFS) measure of the unemployment rate rising from 5.25 per cent to 5.75 per cent over recent months. The more timely claimant count measure has risen by 186,000 since the start of the year, though from a very low level: January 2008 was the first time since mid-1975 that the claimant count had fallen below 800,000.

Working age inactivity has improved and is down by over 50,000 in the year to 2008 Q3 and the inactivity rate was down 0.2 percentage points in the year to 2008 Q3.

Looking ahead as the economy is forecast to enter a recession, outside forecasters expect employment levels fall further. Independent forecasters also expect unemployment to rise: the average of independent forecasts for the claimant count in the fourth quarter of 2009 is 1.44 million (see table 1.1). The claimant count as at October 2008 is 980.9 thousand.

Chart 1.3: UK labour market

Proportion of working age population



Source: Office for National Statistics, Monthly data, Labour Market Statistics

This slow down needs to be kept in context – the labour market is still performing well relative to recent history and the labour market remains strong in comparison to the wider economy.

Employment groups

Since the introduction of the minimum wage 0.2 million more people of working age who are DDA disabled² and have a work-limiting disability³ entered employment. The employment rate for this group has increased by 3.4 percentage points from 30.4 per cent in 1999 Q1 to 33.8 per cent in 2008 Q3. The unemployment rate has increased by 0.2 percentage points from 13.4 per cent to 13.6 per cent over the same period. Inactivity rates have fallen by 4 percentage points from 64.9 per cent in 1999 Q1 to 60.9 per cent in 2008 Q3.

Between 2001 Q1 and 2008 Q3 over 1 million more people of working age from ethnic minorities have entered employment. The employment rate of minority groups has increased by 4.6 percentage points over the same period, from 56.7 per cent to 61.3 per cent. The unemployment rate has decreased by 0.5 percentage points from 12.0 per cent to 11.5 per cent again over the same period. Inactivity rates have fallen by 4.8 percentage points from 35.6 per cent in 2001 Q1 to 30.8 per cent in 2008 Q3.

² The Disability Discrimination Act (DDA) defines a person as DDA disabled as someone who has a physical or mental impairment that has a substantial and long-term adverse effect on his or her ability to carry out normal day-to-day activities.

³ Change in employment levels since 1999 Q1 to 2008 Q3.

Since the introduction of the minimum wage employment for males and females has both increased by around 1.2 million. The working age employment rate for men decreased by 0.3 percentage points from 78.6 per cent in 1999 Q1 to 78.3 per cent in 2008 Q3. The working age employment rate for women increased by 1.4 percentage points from 68.7 per cent to 70.1 per cent over the same period. The working age unemployment rate for men fell from 6.9 per cent in 1999 Q1 to 6.4 per cent in 2008 Q3, for women the unemployment rate remained unchanged at 5.5 per cent over the same period. The working age economic inactivity rate for men increased by 0.8 percentage points from 15.5 per cent in 1999 Q1 to 16.3 per cent in 2008 Q3. For women the economic inactivity rate fell from 27.3 per cent to 25.8 per cent over the same period.

Average earnings and pay settlements

Average earnings growth remained steady in 2008, close to the rates recorded in 2007 on most measures (see table 1.2). Overall wage growth remains modest (see chart 1.4). Chart 1.4 also plots annual NMW increases; the largest percentage rise in the NMW was in October 2001. The October 2008 increase (3.8 per cent) was similar to average earnings and median pay settlements.

Table 1.2. Growth in various wage measures

Annual per cent change, June quarter

	2006	2007	2008
Average earnings (incl. bonuses) - all sectors	4.5	3.6	3.4
Average earnings (incl. bonuses) - private sector	4.7	3.7	3.5
Average earnings (incl. bonuses) - public sector	3.7	3.2	3.2
Average weekly earnings (experimental)	4.8	4.3	4.1

Average weekly earnings (LFS)

Sources:

AEI & Average Weekly Earnings (Experimental) – Office for National Statistics, Monthly Wages and Salaries Survey.
 (Note: The AWE is an experimental series published on the Web one week after the AEI. Both the AEI and AWE use the same data source, the Monthly Wages and Salaries Survey. The AEI is a measure of the growth in average earnings, derived by calculating the growth in the weighted average pay for businesses responding to the survey in successive months (the 'matched' sample). The AWE, on the other hand, is a measure of the level of average earnings, derived by separately weighting the earnings and employment data for the sampled businesses in each month and then calculating the ratio. The growth in AWE can be calculated and compared with the growth in AEI.)

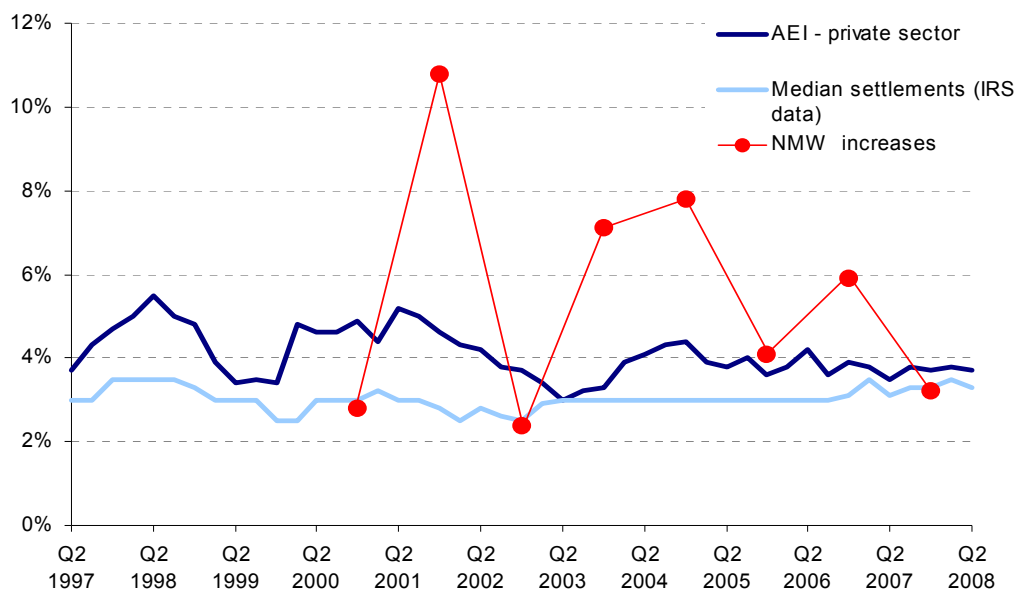
Average Weekly Earnings (LFS) – Office for National Statistics, Labour Force Survey.

(Note: Gross weekly and earnings data are known to be underestimated in the LFS. This is principally because of proxy responses.)

Unit Labour Costs – Office for National Statistics

Chart 1.4: Average annual earnings growth, pay settlements and NMW increases

Proportion of working age population



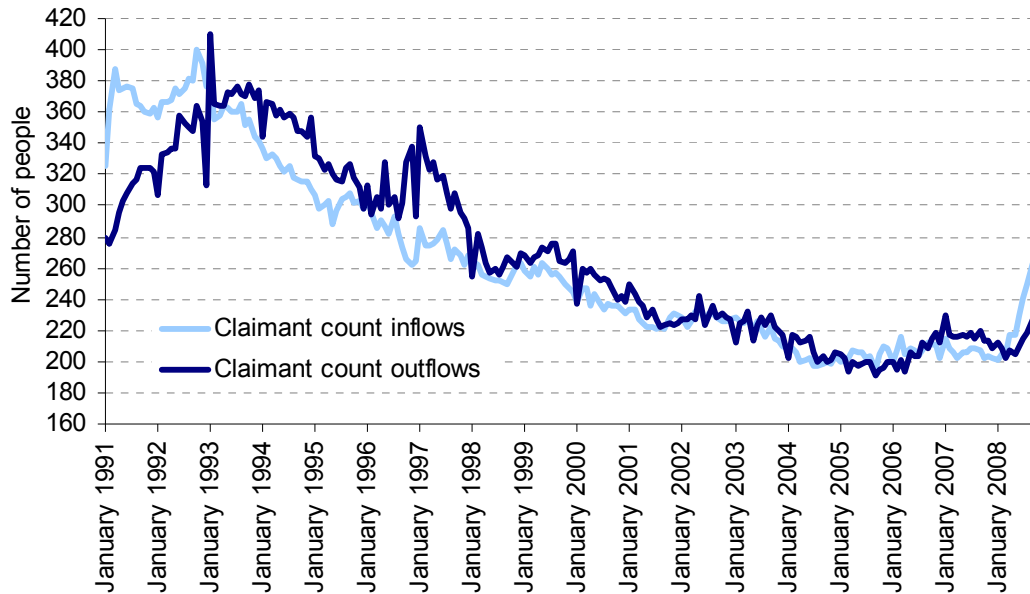
Source: Office for National Statistics, Average Earnings Index (excluding bonuses); Median settlement (IRS data)

Leading indicators

Claimant count inflows – the numbers joining the claimant count - are generally accepted as a leading indicator to the economy, due to the timely release of the data. Chart 1.5 shows that claimant count inflows have increased sharply in recent months indicating a slow down in activity. Since April 2008 monthly claimant count inflows have increased by over 50,000. Claimant count outflows have also been rising, since April 2008 outflows from the claimant count have increased by over 20,000. Despite recent increases in the claimant count and ILO unemployment, there are still over half a million vacancies posted each and every month and more claimants are leaving job seekers allowance (JSA) to move into work.

Chart 1.5 Standardised Inflows and outflows of Claimant Unemployment

Thousands



Source: Office for National Statistics, Labour Market Statistics, Monthly data

Redundancies have also started to increase. In 2008 Q3 156,000 people were made redundant, up 29,000 on the previous quarter. The redundancy rate was 6.1 per 1,000 employees, up by 1.1 percentage points from the previous quarter.

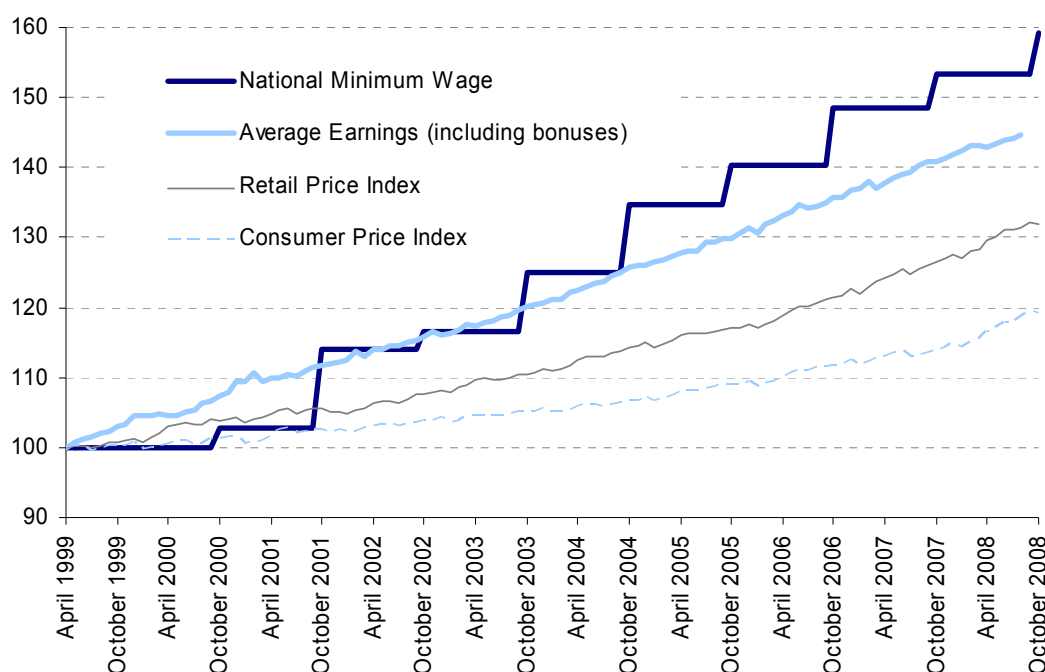
2 Evidence on pay

Average earnings have risen faster than price inflation since 1999 and the minimum wage has increased faster than average earnings. As a consequence, the minimum wage as a percentage of the median wage – known as the ‘bite’ - is now around 51 per cent, an increase of around 5 percentage points since 1999. The bite is higher for small firms (58 per cent) and the low-paying sectors (ranging from 65 per cent to 90 per cent). As the NMW has risen, an increasing proportion of employees are earning wages near the minimum wage. The NMW may also have had knock on or an ‘upward ripple’ effect causing more rapid rises in pay amongst the group just above the NMW. However, this ripple effect dissipates as it moves up the wage distribution.

The NMW has increased substantially faster than both average earnings and prices, especially since 2001. Since it was introduced in April 1999 the adult NMW has risen by around 59 per cent. In comparison, the Average Earnings Index has risen by only around 46 per cent (see Chart 2.1) between April 1999 and the end of September 2008. The Retail Price Index has increased by around 32 per cent over the same period, while the Consumer Price Index rose by around 19 per cent. The October 2008 NMW rise of 3.8 per cent was more than the latest annual earnings growth of 3.3 per cent⁴.

Chart 2.1: Adult NMW increases compared to earnings growth and inflation

Index Rebased to April 1999 = 100



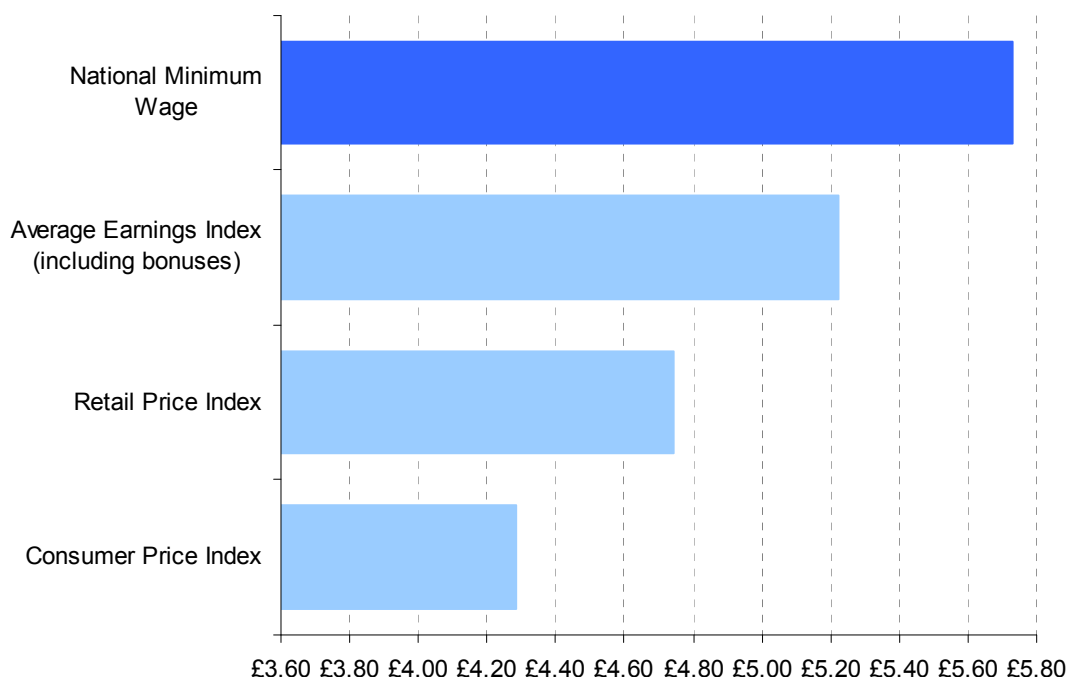
Source: Office for National Statistics; Retail Price Index, Consumer Price Index and Average Earnings Index Low Pay Commission; National Minimum Wage

Another way of looking at NMW growth is to compare the actual NMW with what it would have been if it grew in line with average earnings or prices. The adult NMW was increased to £5.73 in October 2008. If the initial rate of £3.60

⁴ This is Average Earnings Index growth, including bonuses – three months to September 2008 compared to the three months to September 2007 (series LNNC).

had instead been indexed to average earnings, the October 2008 rate would have been £5.22. If it had been indexed to the Retail Price Index it would have been £4.76 and if indexed to the Consumer Price Index it would have been £4.30 (see Chart 2.2). However, reflecting a cautious approach, the NMW was initially set at a relatively low level and therefore increases above inflation and average earnings may have been expected in its early years.

Chart 2.2: Adult NMW indexed to earnings growth and inflation*



Source: BERR estimates; Office for National Statistics

*AEI Index as at end of September 2008, RPI and CPI Index as at end of October 2008. Adult NMW rate as at October 2008.

The bite of the minimum wage

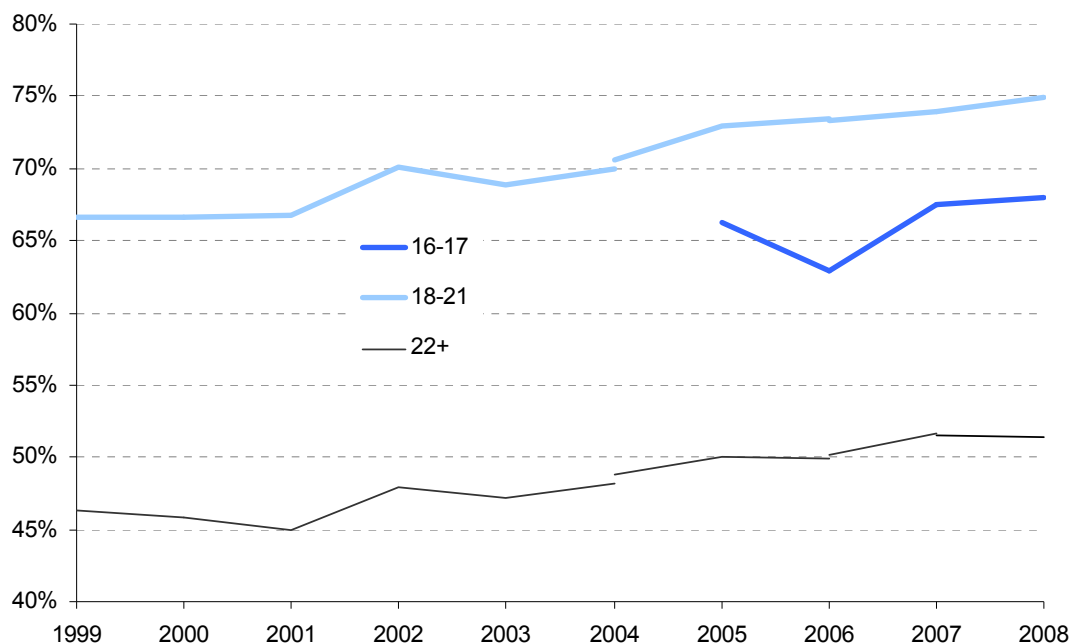
The minimum wage as a proportion of average earnings is often termed the 'bite' and is a measure of how high up the earnings distribution the NMW cuts in. Usually median earnings are the preferred measure of average earnings. Since its introduction the bite of the adult NMW has increased from 46.4 per cent of the median wage to 51.3 per cent in April 2008 (see Chart 2.3).

Therefore, the bite has increased by around 5 percentage points since the NMW was introduced in 1999. It increased by 1.4 percentage points between April 2006 and 2007, reflecting the October 2006 £0.30 increase in the adult minimum wage. This bite estimate does not include the October 2008 uprating in the minimum wage, as we do not yet have median earnings data for this period. However, the October 2008 minimum wage increase (3.8 per cent) was broadly in line with average earnings growth in 2008, suggesting the bite might be broadly stable between 2008 and 2009.

The rate for 18-21 year olds also continued to increase, reaching 75 per cent of the median in 2008. There was a big jump in the 16-17 year old bite due to the uprating to £3.30 in October 2006. Their bite increased from 63 per cent in Spring 2006 to around 68 per cent in Spring 2007. Since then it has remained constant, the bite for 16-17 year olds in 2008 is 68 per cent.

Chart 2.3: The bite of the NMW

Minimum wage as a per cent of median earnings



Source: Office for National Statistics, Annual Survey of Hours and Earnings
 1999-2004 ASHE data - excluding supplementary information
 2004-2006 ASHE data - old methodology
 2006-2008 ASHE data - new methodology
 See Annex H for further information on the changes to ASHE data.

International comparisons of the bite

Chart 2.4 provides a comparison of the bite with other countries. These comparisons are limited by differences in data methodologies.

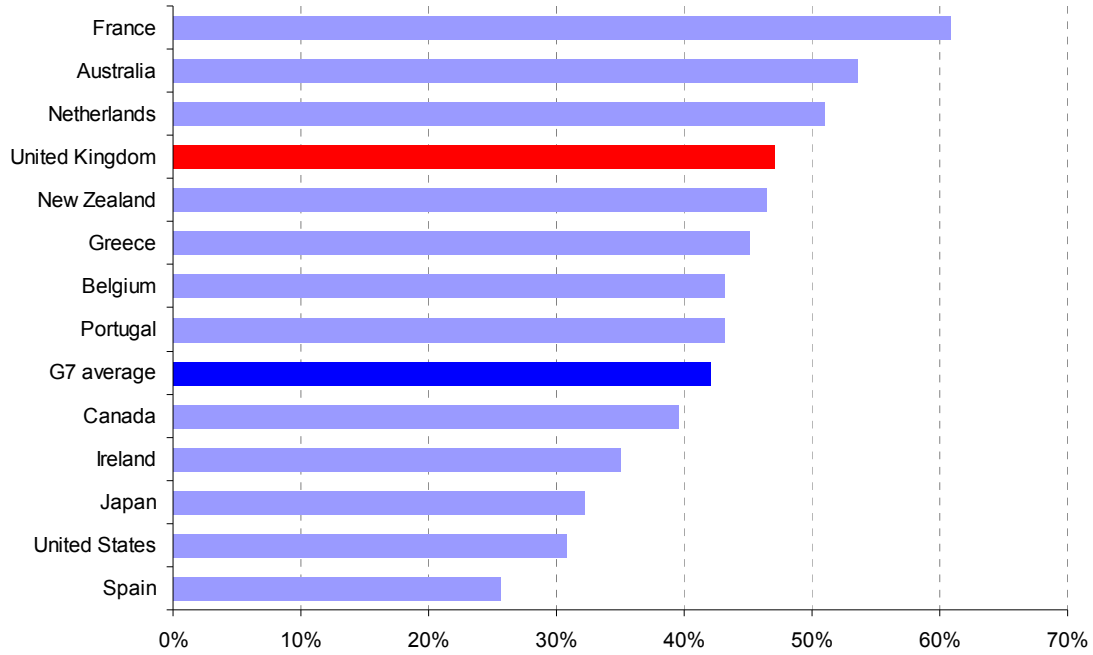
However, on the available evidence using the countries identified in chart 2.4, the UK bite is greater than the unweighted G7 average with France, Australia and Netherlands all having a higher bite.

The level of the UK minimum wage is compared internationally by adjusting for purchasing power parity (see Chart 2.5)⁵. However, these purchasing power parity figures should be treated only as a rough guide as they are sensitive to the assumptions used and can be buffeted by exchange rate fluctuations.

⁵ Purchasing power parity is a method measuring the relative purchasing power in different countries' currencies over the same type of goods and services. Because goods and services may cost more in one country than in another, PPP allows us to make more accurate comparisons of standards of living across countries.

Chart 2.4: International comparisons of the minimum wage bite

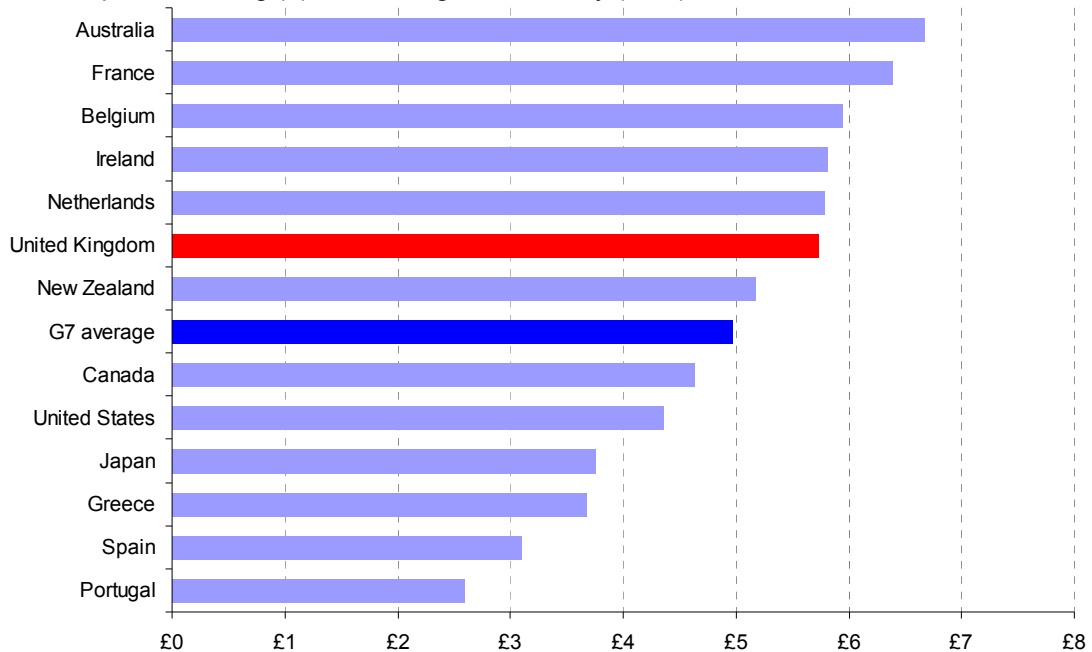
Per cent of median earnings



Source: Various (see Annex D)

Chart 2.5: International comparisons of the minimum wage

NMW in pound sterling (£) Purchasing Power Parity (PPP) terms



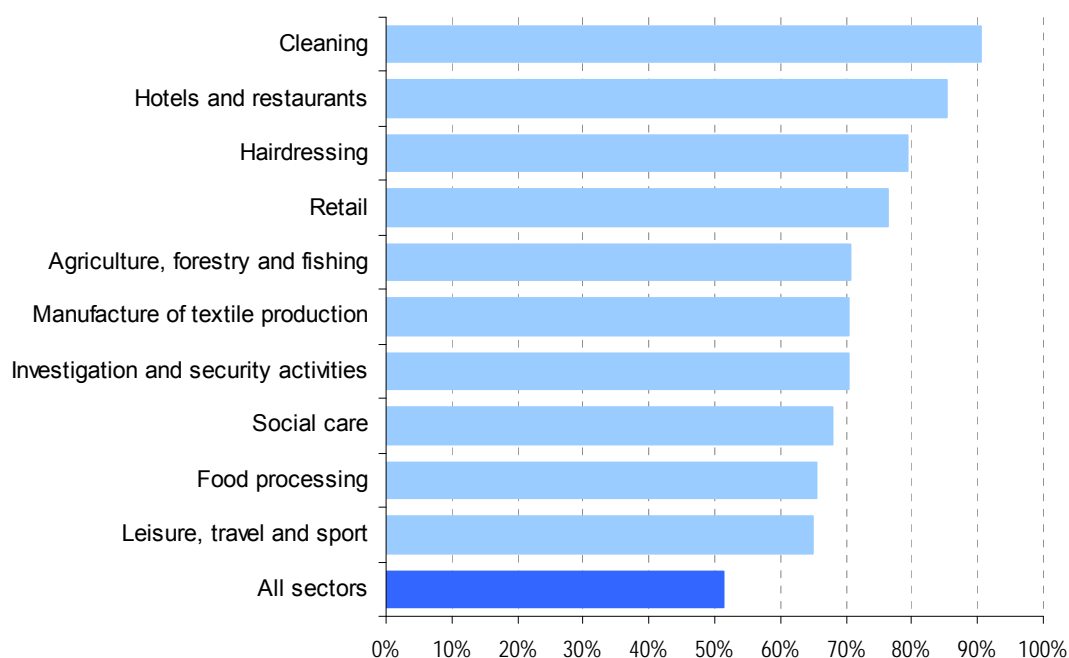
Source: Various (see Annex D)

The minimum wage and low paid sectors

The minimum wage is more likely to impact on employment in those sectors that are more reliant on low-wage workers. The LPC defines a number of sectors as being 'low-paid', which employ large numbers of people earning near the NMW⁶. The adult bite is much higher in these sectors, with an unweighted average bite of around 74 per cent. The bite ranges from 65 per cent of the median in leisure, travel and sport to 90 per cent in cleaning (see Chart 2.6). In addition, some of the largest low-paid sectors such as retail trade and hotels and restaurants, have some of the biggest bites at 76 per cent and 85 per cent respectively.

Chart 2.6: The bite of the NMW in low-paid sectors

Adult minimum wage as per cent of median wage, 2008



Source: Office for National Statistics, Annual Survey of Hours and Earnings
Those aged 22+.

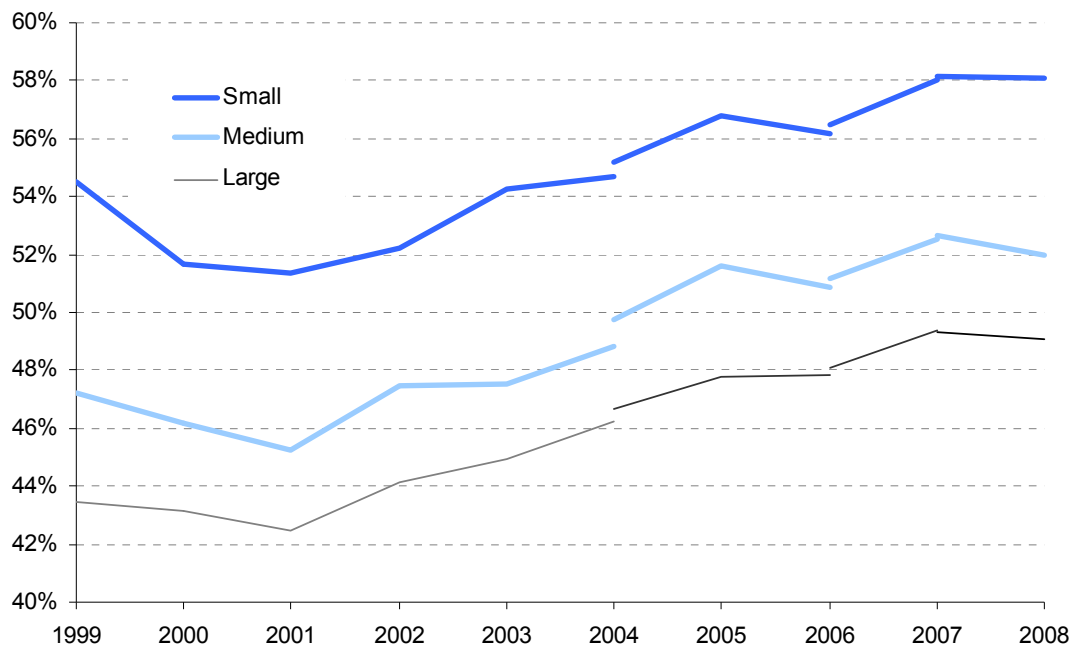
The bite for small firms

Chart 2.7 highlights that the minimum wage as a per cent of the median wage tends to be higher for smaller firms than for medium and larger firms. The bite for smaller firms was over 58 per cent in 2007, compared to around 52 per cent for medium sized firms and 49 per cent for larger firms. This highlights that the minimum wage is having a greater impact on the costs and profitability of smaller firms.

⁶ Defined as hotels and restaurants; cleaning; hairdressing; retail; agriculture, forestry and fishing; investigation and security activities; manufacture of textile products; food processing; social care; leisure; and travel and sport.

Chart 2.7: The bite of the NMW by organisation size*

Adult minimum wage as per cent of median wage



Source: Office for National Statistics, Annual Survey of Hours and Earnings

1999-2004 ASHE data - excluding supplementary information

2004-2006 ASHE - old methodology

2006-2008 ASHE - new methodology

*Small organisations are defined as 1 to 49 employees, medium as 50-249 employees and large is 250 + employees.

See Annex H for further information on the changes to ASHE data.

Those aged 22+.

Proportion of employees earning the minimum wage

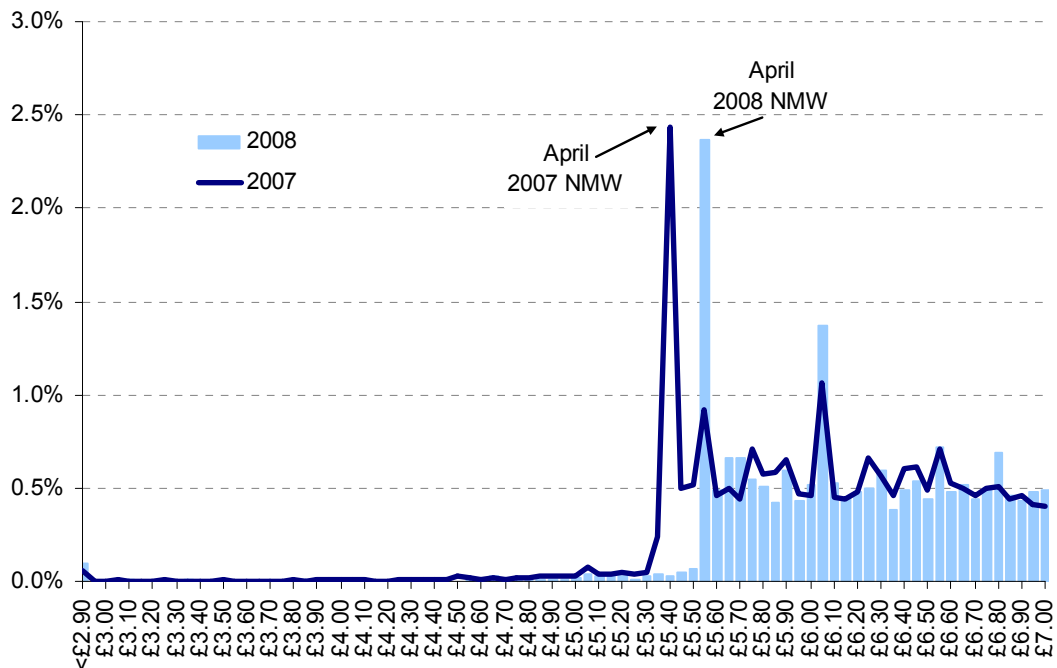
Chart 2.8 shows the proportion of adult jobs at different points across the hourly pay scale in 2007 and 2008. It highlights a jump in the distribution of adult hourly pay at the point where the minimum wage cuts in. In particular, the uprating of the adult minimum wage from £5.35 to £5.52 in October 2007 resulted in this spike moving from the old rate to the new higher rate between April 2007 and 2008.

The number of jobs paying the NMW remained unchanged between 2007 and 2008. The number of jobs earning the NMW was around 2.4 per cent in 2007 and 2008. If the NMW continues to grow faster than median or average earnings, it will become the wage-setting mechanism for an increasing proportion of the workforce.

A similar effect can be seen for the Development Rate, paid to 18–21 year olds. Chart 2.9 shows a spike in the distribution of hourly pay around the Development Rate of £4.60 which prevailed in April 2008. There has been a slight rise in the number of employees who earn the Development NMW (from 2.9 per cent in 2007 to 3.1 per cent in 2008). Chart 2.9 also shows a significant proportion of 18-21 year olds who were being paid at the adult NMW rate in 2008 (7.6 per cent in 2008 compared to 7.1 per cent in 2007). In total, almost 82 per cent of employee jobs for those aged 18-21 were paid at or above the adult NMW in 2008.

Chart 2.8: Adult low-pay distribution, April 2008

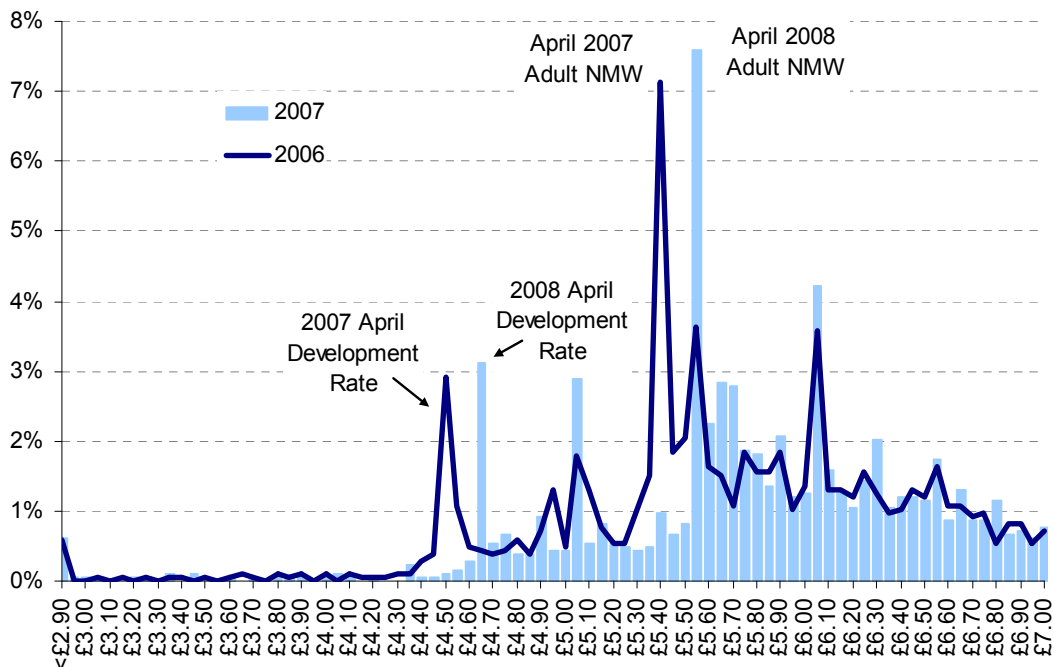
Per cent of adult jobs (22 years or older)



Source: Office for National Statistics, Annual Survey of Hours and Earnings

Chart 2.9: 18-21 year old low-pay distribution, April 2008

Per cent of 18-21 year old jobs



Source: Office for National Statistics, Annual Survey of Hours and Earnings

The numbers of jobs paying less than the National Minimum Wage rates

It is of critical importance to the Government that everyone entitled to the NMW actually receives their entitlement. The Government has introduced new penalties for all employers who underpay the NMW and a fairer system of paying arrears under the Employment Act 2008. These new measures will come into force from 6th April 2009.

However, there are some workers who are paid below NMW rates, which for some does not reflect non-compliance. There are a number of circumstances where the NMW does not apply and so individuals may legitimately earn less than the appropriate NMW rate for their age. For example, employees may not be receiving the NMW in cash terms because employers can legitimately reduce rates to take into account the cost of accommodation provided, for which there is a standard level of deduction. Individuals may also be on Government training programmes or apprenticeships, where they are exempt for the first year, up to the age of 26.

According to the latest Office for National Statistics (ONS) estimates of low pay based on data from the new ASHE survey in Spring 2008, there were 288,000 jobs held by people aged 16 or over paying less than the appropriate NMW rate. This is equivalent to 1.1 per cent of all UK jobs. This comprised of 17,000 jobs held by 16-17 year olds, 47,000 jobs held by 18-21 year olds and 224,000 jobs held by those 22 and older.

Table 2.1 provides more details of the proportion of jobs paid at hourly wage rates less than the prevailing NMW rate. It should be noted that these estimates are approximate, and subject to revision.

Part-timers have benefited by more than full-timers. Between 1998 and 2008, the number of jobs held by part-time workers earning below the NMW rate fell from 14.1 per cent of part-time jobs to 1.8 per cent. This compares with a decline in the number of jobs held by full-time workers earning below the NMW rates from 2.4 per cent in 1998 to 0.8 per cent in 2008.

Table 2.1. Proportion of UK jobs paid below minimum wage

		1998*	1999	2000	2001	2002	2003**	2004	2005	2006	2007	2008
All		5.6	2.1	1	1	1.4	1	1.1	1.2	1.2	1.2	1.1
All (18+)		5.6	2.1	1.0	1.0	1.4	1.0	1.1				
All (16+)**									1.2	1.2	1.2	1.1
All 16-17									4.0	3.8	4.1	3.9
All 18-21		7.2	2.4	2.2	2.1	2.7	2.3	2.3	3.0	2.3	2.5	2.6
All 22+		5.4	2.1	0.9	0.9	1.3	0.9	1.0	1.0	1.0	1.0	0.9
All men		2.9	1.4	0.6	0.7	0.8	0.7	0.9	1.0	0.9	0.9	0.8
All women		8.4	2.8	1.3	1.4	2.0	1.4	1.4	1.4	1.4	1.4	1.4
Men	full-time	1.8	0.8	0.3	0.3	0.5	0.4	0.7	0.9	0.7	0.7	0.7
	part-time	14.4	7.0	4.0	4.4	4.4	3.5	2.5	2.2	2.4	2.2	1.3
Women	full-time	3.6	1.1	-	-	0.7	0.5	0.8	0.9	0.9	0.8	1.1
	part-time	14.1	4.9	2.3	2.5	3.6	2.4	2.1	2.1	2.2	2.1	1.9
All full-time		2.4	0.9	0.4	0.3	0.5	0.4	0.8	0.9	0.8	0.8	0.8
All part-time		14.1	5.3	2.6	2.8	3.7	2.6	2.2	2.1	2.2	2.1	1.8

Source: Annual Survey of Hours and Earnings (ASHE); Office for National Statistics

Notes:

- Sample size too small for reliable estimate.

* Figures for 1998, before the NMW was introduced, are for jobs paid less than £3.00 p/h (aged 18-21) or £3.60 p/h (aged 22 and over).

** Estimates for 1998-2003 are based on a central estimate of the LFS and ASHE.

*** Before 2005 the estimates are for employees aged 18 and over, from 2005 the estimates are for those aged 16 and over.

Number of jobs paid at less than £3.00 per hour (aged 18-21) or £3.60 per hour (aged 22 and over) for 1998 to 2000.

Number of jobs paid at less than £3.20 per hour (aged 18-21) or £3.70 per hour (aged 22 and over) for 2001.

Number of jobs paid at less than £3.50 per hour (aged 18-21) or £4.10 per hour (aged 22 and over) for 2002.

Number of jobs paid at less than £3.60 per hour (aged 18-21) or £4.20 per hour (aged 22 and over) for 2003.

Number of jobs paid at less than £3.80 per hour (aged 18-21) or £4.50 per hour (aged 22 and over) for 2004.

Number of jobs paid at less than £3.00 per hour (aged 16-17) or £4.10 per hour (aged 18-21) or £4.85 per hour (aged 22 and over) for 2005.

Number of jobs paid at less than £3.00 per hour (aged 16-17) or £4.25 per hour (aged 18-21) or £5.05 per hour (aged 22 and over) for 2006.

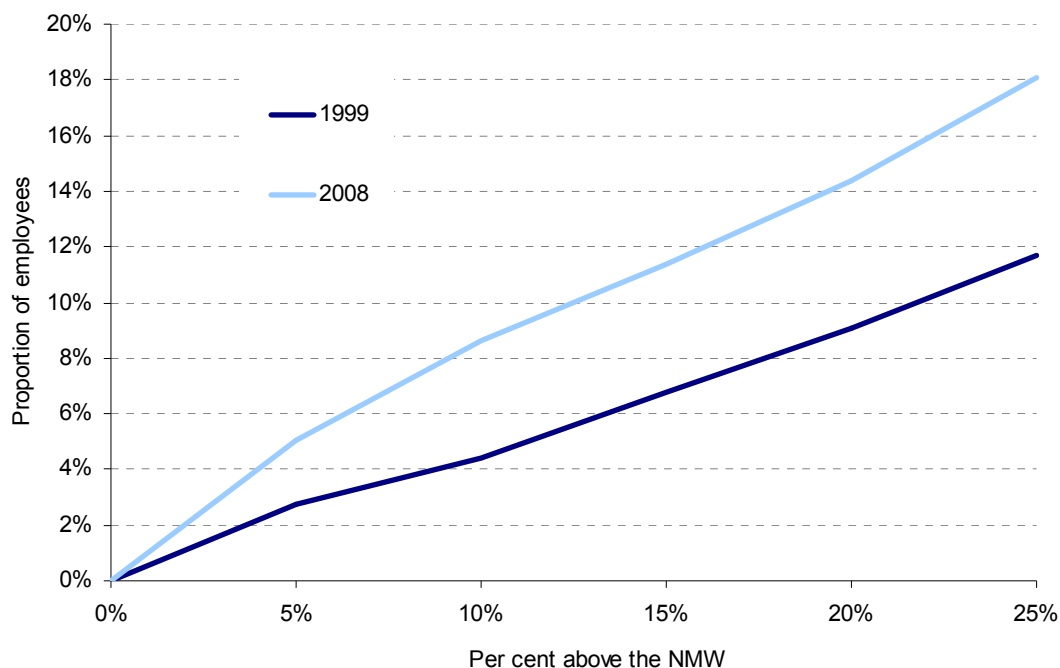
Number of jobs paid at less than £3.30 per hour (aged 16-17) or £4.45 per hour (aged 18-21) or £5.35 per hour (aged 22 and over) for 2007.

Number of jobs paid less than £3.40 per hour (aged 16-17) or £4.60 (aged 18-21) or £5.52 per hour (aged 22 and over) for 2008

Compression of the earnings distribution

As the NMW increases relative to median earnings, there is an increase in both the proportion of employees earning the minimum wage and those earning relatively close to it. For example, around 9 per cent of employees worked between the NMW and 20 per cent above it in Spring 1999. This had increased to over 14.4 per cent by Spring 2008 (see Chart 2.10). In the low-paying sectors these proportions are higher, with around 34 per cent of employees in these sectors being paid within 20 per cent of the NMW (up from around 21 per cent in 1999).

Chart 2.10: Proportion of employees earning within a certain per cent above the NMW

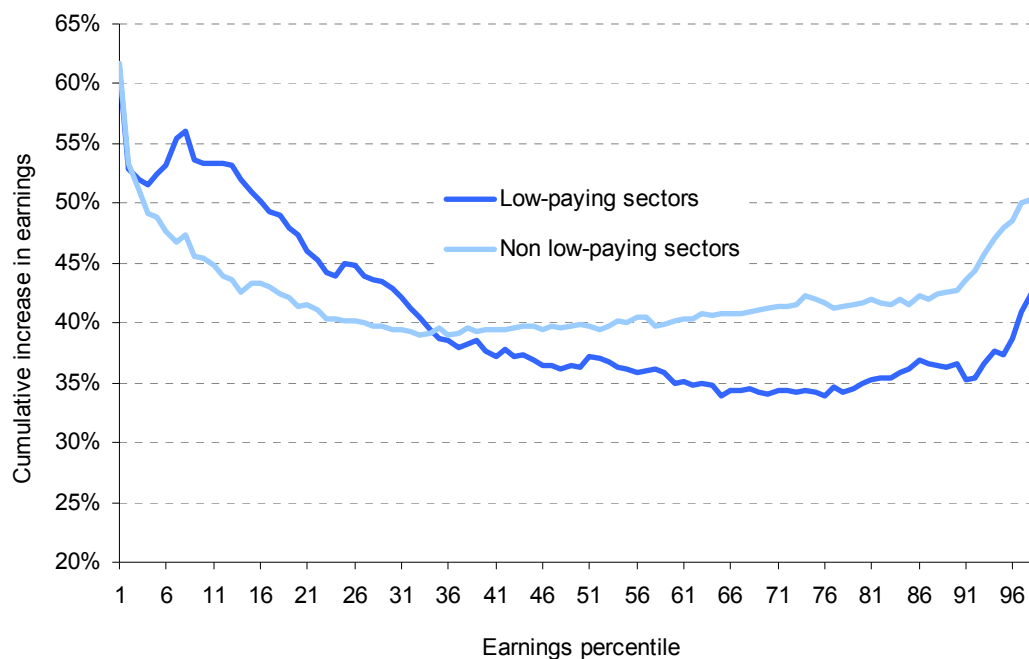


Source: Office for National Statistics, Annual Survey of Hours and Earnings
1999 - ASHE data - excluding supplementary information
2008 - ASHE data - new methodology
See annex H for further information on the changes to ASHE data.

In addition, the introduction and uprating of the NMW has not just benefited the bottom few per cent of employees. There has been an 'upward ripple' effect, with NMW increases influencing pay scales above the NMW. Chart 2.11 shows the increase in hourly pay across the earnings distribution, from the lowest to highest income earners, between 1999 and 2008 for both the low-paying and non low-paying sectors. It highlights that employees at the lower end of the pay scale have received larger percentage increases in their pay than those at the middle or top end over this period. This is particularly true for employees working in the low-paying sectors. This trend appears to be continuing. In the most recent 2008 ASHE data, the earnings growth for full-time employees of the bottom decile increased by 3.5 per cent compared with a growth of 4.4 per cent for the top decile between 2007 and 2008. These upward ripple effects mean a growing number of employees' wages are influenced by the NMW when it increases faster than average earnings growth.

Chart 2.11: Cumulative increase in earnings by percentile, 1999-2008

Per cent increase



Source: Office for National Statistics, Annual Survey of Hours and Earnings
1999 - ASHE data - excluding supplementary information
2008 - ASHE data - new methodology
See annex H for further information on the changes to ASHE data.

Incentives for progression also depend on interactions with the tax and benefit system. Marginal Deduction Rates (MDRs) show how much of each additional pound of gross earnings is lost through higher taxes and withdrawn benefits or tax credits. In 2009-10 there will be an increase in the number of families who may face MDRs above 70 per cent, largely due to the introduction of a disregard for Child Benefit in Housing and Council Tax Benefits (CTB) from October 2009. This measure makes Housing Benefit and CTB more generous for working families with children, extending support to households further up the income scale. Although MDRs will have increased for some families, this is over a relatively short income interval. Overall, the numbers on MDRs above 7 per cent have more than halved since 1997, to 305,000.

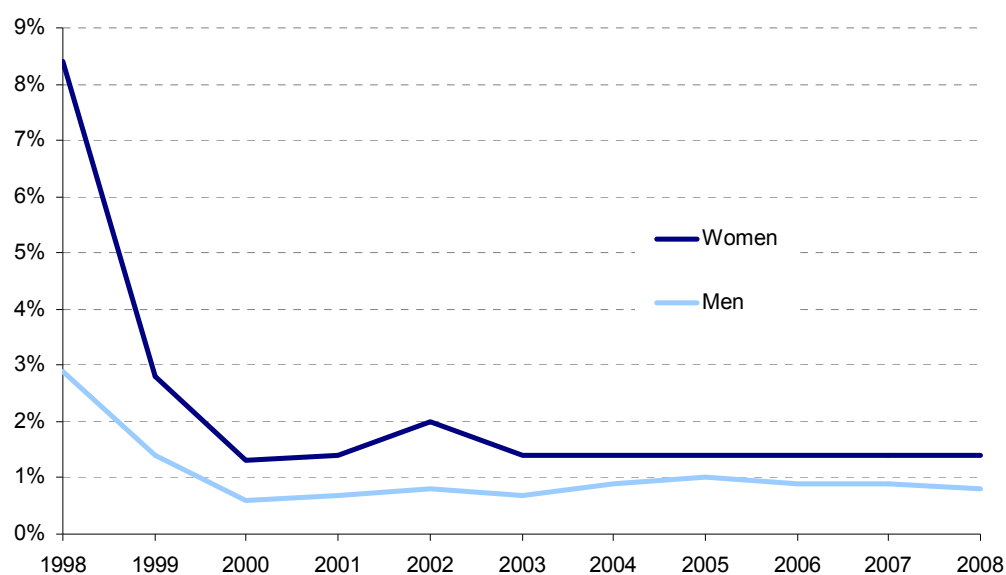
By reforming the tax benefit system, many low paid workers now receive more in disposable income from a given pay rise than they did 10 years ago. The MDR faced by different workers varies according to household composition and circumstances as well as the number of hours worked, but all workers earning the minimum wage will be better off as a result of an increase.

Gender wage gap

While not the underlying purpose for the introduction of the NMW, it has helped reduce gender inequality as more females than males have been lifted up to a higher wage rate. Chart 2.12 shows that the number of jobs held by women paid less than the NMW fall from 8.4 per cent (940,000 women) in 1998 to 1.4 per cent in 2008 (185,000 women), while the number of men fell from 2.9 per cent (340,000 men) in 1998 to 0.8 per cent in 2008 (103,000 men).

Chart 2.12: Female and male jobs earnings less than the NMW

Per cent of total jobs

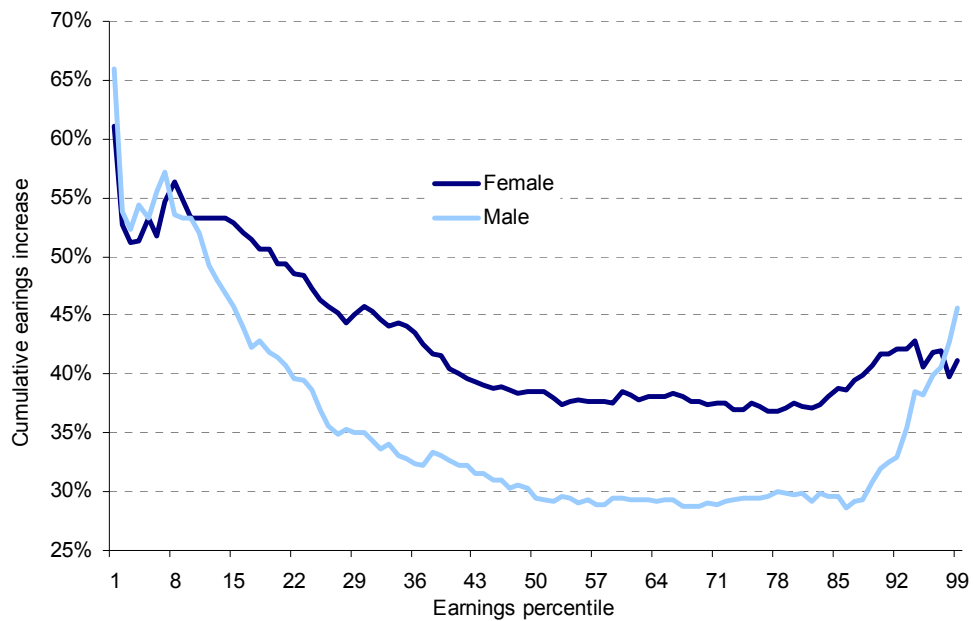


Source: Estimates for 1998 to 2003 are based upon the central estimate of the LFS and ASHE. 2004+ based on ASHE. Not seasonally adjusted. 1998-2004 data covers those earnings less than the 18-21 year old rate and the adult rate. 2005 onwards also includes those earnings less than the 16-17 year old rate.

Chart 2.13 highlights that female earnings have also grown faster than male earnings in the low-pay sectors at almost all parts of the wage distribution since the introduction of the NMW in 1999. The exception is the top 5th percentile, where the gender wage gap continues to widen. This chart shows that in the bottom deciles, since the NMW was introduced, there was no gender pay gap at this level – men and women receive the same rate.

Chart 2.13: Cumulative increase in earnings by percentile for low paying sectors, 1999-2008

Per cent increase



Source: Office for National Statistics, Annual Survey of Hours and Earnings
1999 - ASHE data - excluding supplementary information
2008 - ASHE data - new methodology
See Annex H for further information on the changes to ASHE data.

3 Impact on the labour market

While UK academic research to date has not found overwhelming evidence that the adult minimum wage has reduced employment, there has not yet been time for the full impact of the recent large minimum wage upratings to be seen. However, early indication from Dickens and Draca (2005)⁷ which looked at the impact of the minimum wage increase in 2003 and Mulheirn (2008)⁸ which examined the impact of the 2006 uprating found no significant evidence of an adverse employment impact.

There has been a slight decline in the share of UK employment in low-paying sectors since 1999. However, there is no evidence that this is the result of the minimum wage. The trend also predates the introduction of the NMW.

There is some evidence of a small impact of the NMW on hours worked. Over 1999-2008 total hours worked in the low-paying sectors grew around 5.6 per cent, less than the 6.5 per cent growth in the non low-paying sectors. The slight decline in the share of UK employment since 1999 in low-paying sectors partly explains the smaller growth in total hours worked but there has also been a slight fall in mean hours worked in low-paying sectors.

With a recession forecast for 2009 coupled with an increasing bite and employees affected by the NMW uprating, careful consideration of all the economic evidence will be required when setting the 2009 NMW rates.

The evidence presented so far has been in the context of a growing labour market. There is less evidence, from both the UK and internationally, of the impact of minimum wages in periods of economic downturn.

A simple perfectly competitive model of the labour market would suggest that the introduction of a minimum wage above the market-clearing wage will tend to result in supply of workers outstripping demand for workers resulting in a fall in employment and a rise in 'involuntary unemployment'. In reality this is only one way in which the minimum wage might affect the labour market.

Other effects that do not result in unemployment are equally plausible. For example if the labour market is not highly competitive or there are labour market frictions, there may be opportunities for firms to keep wages relatively low. In these circumstances a minimum wage will not necessarily lead to increased unemployment, and might even increase employment.

Empirical evidence from the UK has not tended to find significant evidence that the adult minimum wage has reduced employment. However, this

⁷ Dickens R and Draca M (2005) The employment effects of the October 2003 increase in the National Minimum Wage. Centre for Economic Performance, February. Report prepared for Low Pay Commission.

⁸ Mulheirn, I (2008) The impact of the 2006 National Minimum wage rise on employment. Economic Labour Market Review, Vol 2, No 9

evidence must be seen in context; most of the evidence focuses on a period in which there was a growing labour market and there is little evidence, both in the UK and internationally, of the relative impact of minimum wages in an economic downturn.

The current adult NMW bite has increased to over 51 per cent and an increasing proportion of employees are now earning near the NMW.

Therefore, within the context of the current economic climate and coupled with an increasing bite and coverage of the NMW, it is essential that the increased level of uncertainty and risk, both in the macroeconomy and labour market, are actively considered.

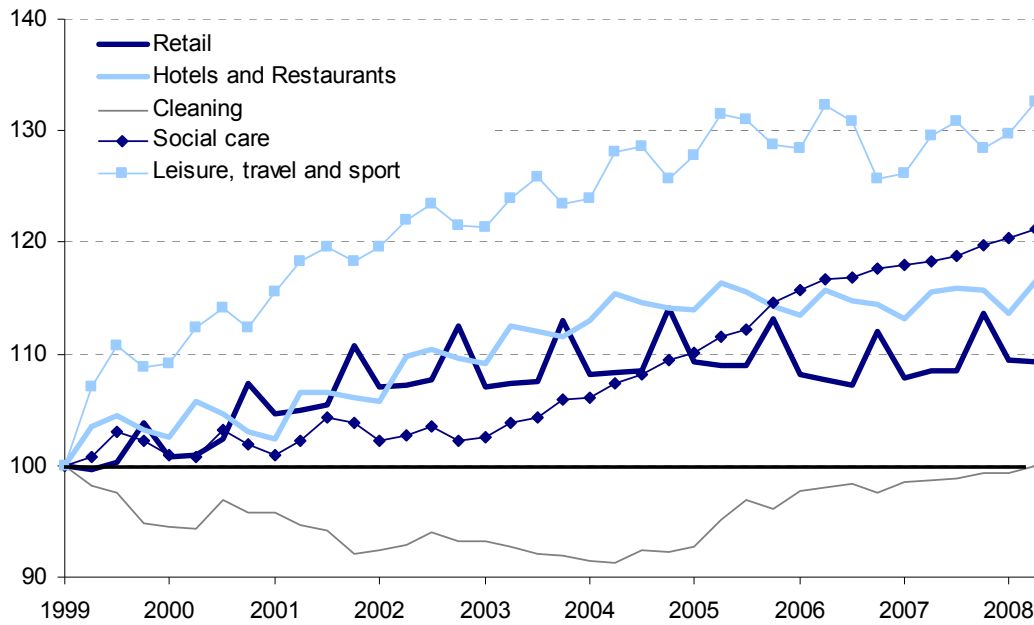
This chapter reviews the most recent data on employment using ONS employee jobs data and the Annual Survey of Hours and Earnings (ASHE) for any emerging employment trends. Employee jobs data are only available up to 2008 Q2 at the time of publication of this report. Trends in employment may therefore not reflect the recent falls in employment seen in the LFS nor does it reflect the impact of financial turbulence on the UK labour market.

Employment in low-paying sectors

Total employment in the low-pay sectors has been increasing since the introduction of the minimum wage in 1999. The number of jobs in the low-paying sectors has increased by 668,000 (8.5 per cent), compared to an overall jobs increase of 2.2 million (8.9 per cent) in the nine years to 2008. The largest job increases have been in the retail sector (up 286,000) and in hotels and restaurants (up 257,000), the two largest low-paying sectors. But the largest percentage rise in the major low paying sectors (32.6 per cent) has been in leisure, travel and sport, as Chart 3.1 shows. Of the smaller low paying sectors security has increased by 37.1 per cent since 1999.

Chart 3.1: Jobs in major low-paying sectors since 1999

Index Rebased to 1999 Q1 = 100

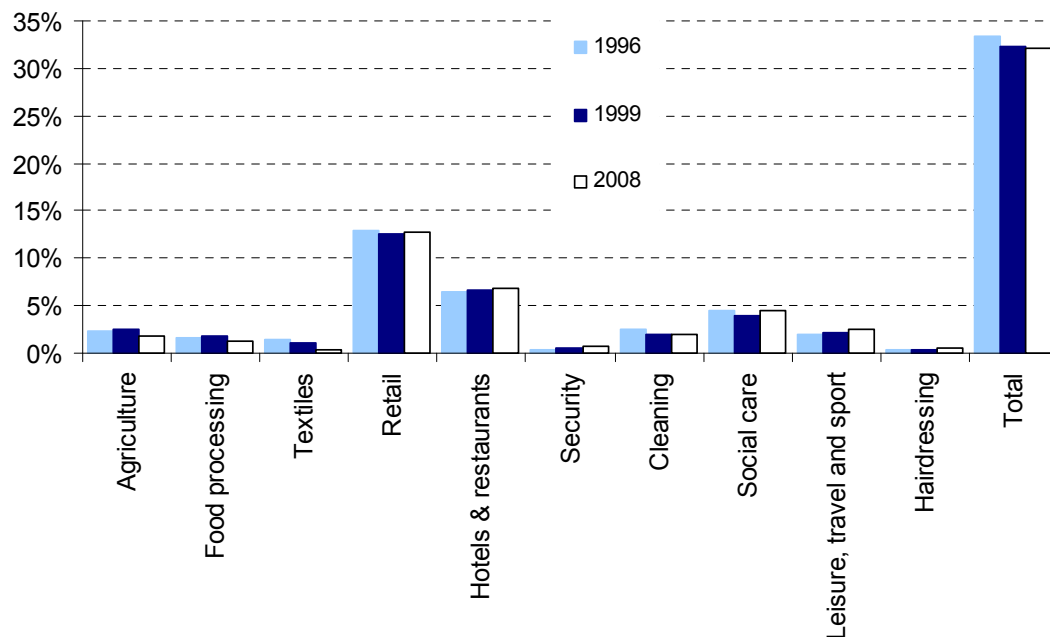


Source: Office for National Statistics, Employee jobs

Employment in the low-paying sectors has tended to grow more slowly than other sectors between 1999 and 2008. As a consequence, the share of the low-pay sectors in total employment has also fallen slightly; by about one tenth of a percentage point between June 1999 and 2008 (see Chart 3.2). However, although the share has dropped slightly employment continues to grow and the research evidence suggests that the relatively small drop in the share is not due to the effect of the NMW.

Chart 3.2: Low pay sectors share in total employment

Per cent of total employment, March quarter

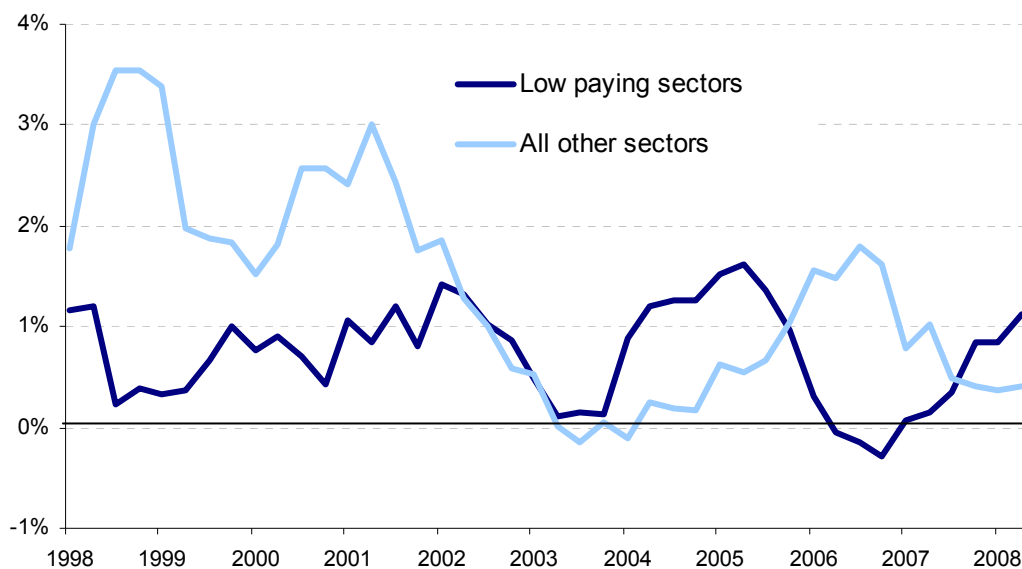


Source: Office for National Statistics, Employee jobs

In addition, when the minimum wage began to rise more rapidly in 2001 to 2005, (the average annual growth in the NMW was 7 per cent) job growth in the low-paying sectors tended to at least match the annual growth rate in the rest of the economy (see Chart 3.3). Between the middle of 2005 and the end of 2006 annual growth in low-paying sectors decreased, from mid 2007 to the most recent period up to Q2 2008 job growth has been greater in low paying sectors than in the rest of the economy.

Chart 3.3: Annual jobs growth

Annual per cent change

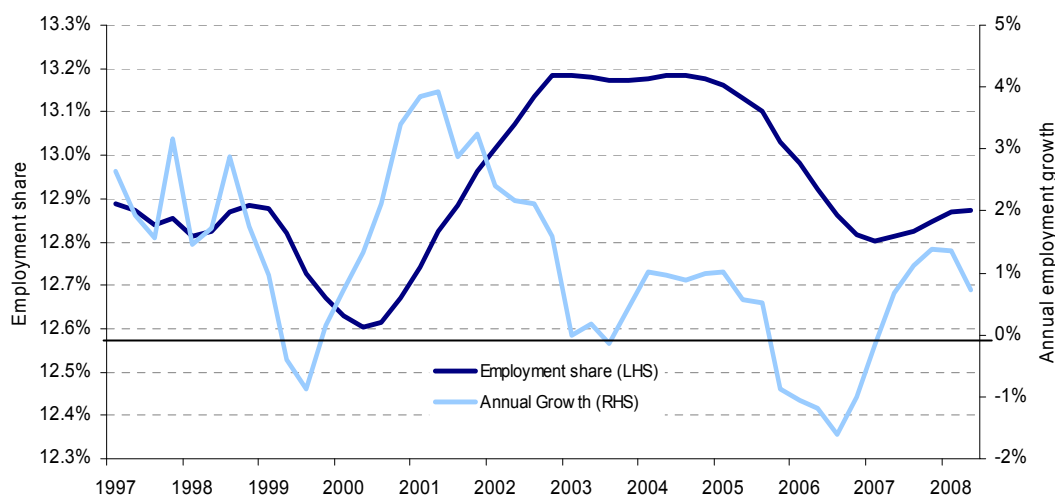


Source: Office for National Statistics, Employee jobs

The annual job growth rate in the retail sector has a big impact on the overall annual growth rate in low-paying sectors (chart 3.2 shows retail is the largest low-paying sector). In 2006 the annual growth rate in the retail sector was negative, however the rate of decline slowed, which corresponds to the positive annual job growth in the low paying sectors. Since June 2007 annual job growth in the retail sector has been positive and the year to June 2008 the annual growth rate is 0.73 per cent.

Chart 3.4: Annual jobs growth and share in retailing

Annual per cent change

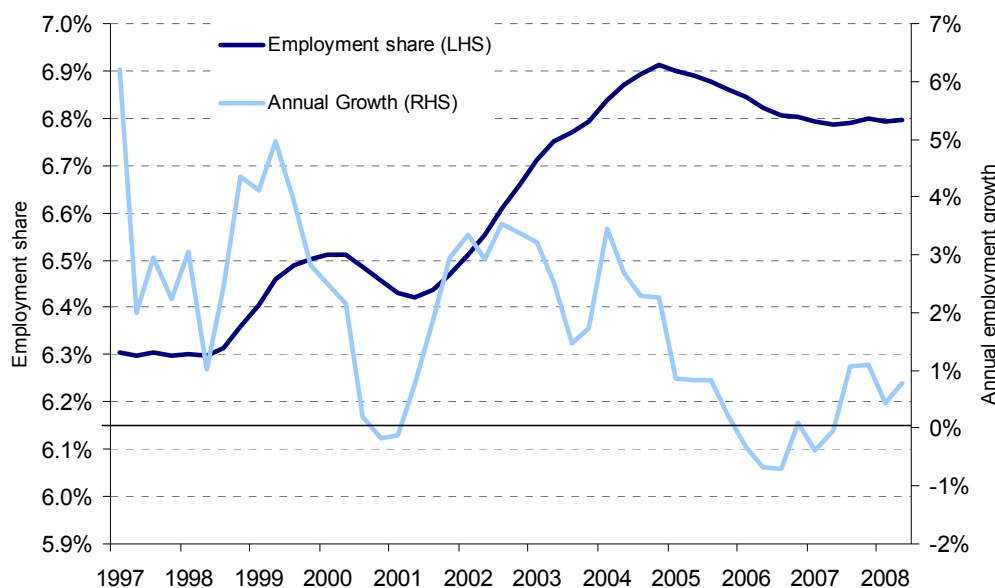


Source: Office for National Statistics, Employee jobs

The annual growth rate in employee jobs in hotels and restaurants, the second largest low paying industry, has been similar to the retail sector. In the year to June 2008 jobs in the hotel and restaurant sector increased by 14,000 (0.8 per cent), this compares to 24,000 (0.7 per cent) jobs created in the retail sector. In contrast, social care, the third largest low paying sector has had strong positive annual employee job growth since 1999. The employment share of social care of all employee jobs has increased from 4 per cent in 1999 to 4.5 per cent 2008. Currently the annual job growth in social care is 2.5 per cent

Chart 3.5: Annual jobs growth and share in hotels and restaurants

Annual percentage change



Source: Office for National Statistics, Employee jobs

Low paid sectors and previous recessions

Employment levels in low paying sectors and all other sectors tend to fall in recessions. However, the falls in low-paying sectors have tended to be less than in all other sectors. In the early 1980's recession employment in the low-paying sectors fell at roughly the same rate as elsewhere and as a result the employment share remains virtually unchanged. In the early 1990's recession job losses in the low paying sectors were less than elsewhere and so the employment share rose. These results should be interpreted carefully as it provides a historic reflection of the employment share of low paid sectors but is not necessarily an indicator of how the low paid sector employment share will react in the future and in previous recessions the UK did not have a NMW.

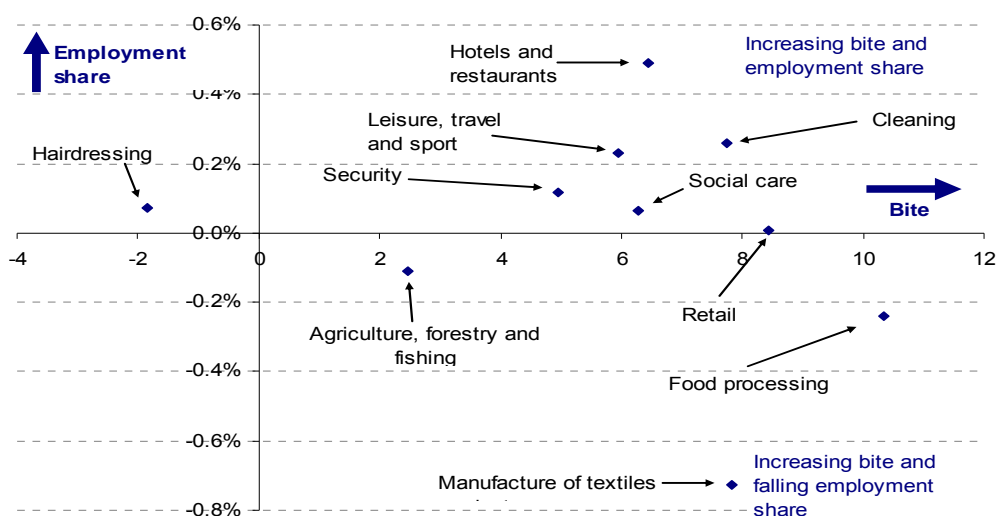
Looking ahead, pressure on employment in low paying sectors might increase. Many low paying sectors are affected by consumption levels and as such are particularly sensitive to changes in demand. Any changes may lead to firms paying particular attention to their costs.

Impact of the bite on employment sector shares

It is difficult to draw conclusions from broad trends in employment in low-paying sectors, as they are driven by a number of factors other than the

minimum wage. One approach to dig deeper into the relationship between employment and the impact of the minimum wage is to explore whether there is any relationship between the sectors that have experienced the largest increases in the bite and those that have seen the largest falls in their share of total employment. This is shown in Chart 3.6, which includes low-paying sectors as defined by the LPC. While this chart suggests some (negative) correlation between increasing bite and declining employment share, there is no evidence that this is causal. Such a relationship is not borne out by the evaluation evidence on the NMW and is more readily explained by trade-induced changes in the UK's industrial structure.

Chart 3.6. Change in bite against change in employment share, 1999 to 2008
Per cent change in low paid sectors



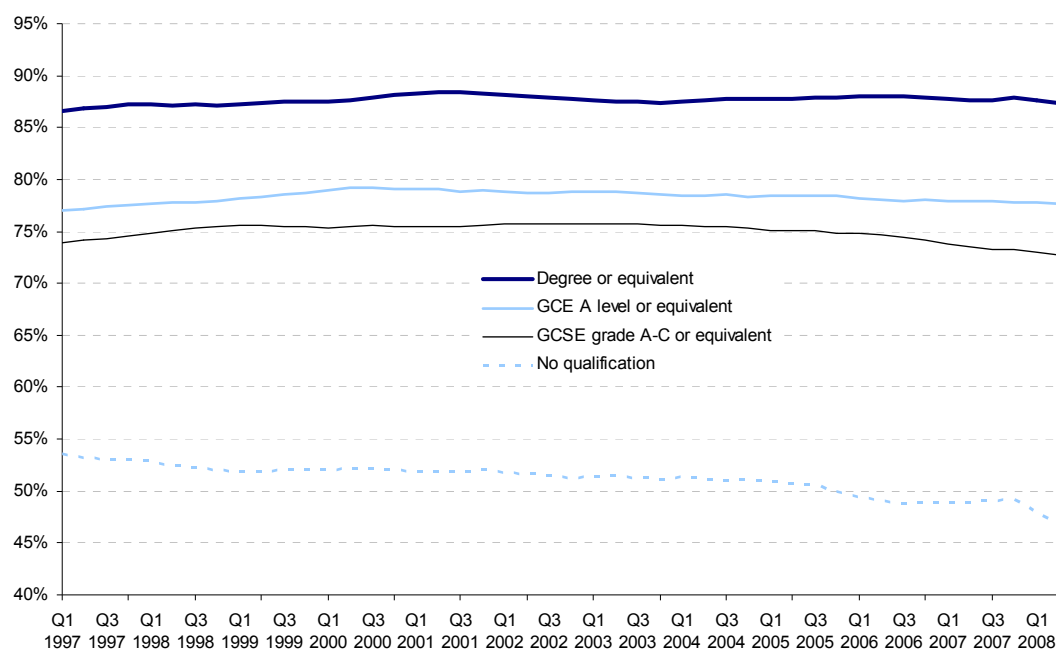
Source: Office for National Statistics, Annual Survey of Hours and Earnings
1999 - ASHE data - excluding supplementary information
2008 - ASHE data - new methodology
See annex H for further information on the changes to ASHE data.
Those aged 22+.

Employment of low skilled

As well as looking at low-paying sectors, another way to explore the impact of the NMW is to analyse the labour market outcomes of the low-skilled, who are the most likely to be beneficiaries of the minimum wage.

Chart 3.7 highlights the large and growing gap between the employment outcomes of unqualified and qualified workers. Unqualified workers have experienced a relative deterioration in employment rates from around 54 per cent in 1997 to around 47 per cent in 2008. This is slightly less than half the employment rate of those with a degree or equivalent.

Chart 3.7. Per cent of working age population, four quarter moving average



Source: Office for National Statistics, Labour Force Survey.
Not seasonally adjusted.

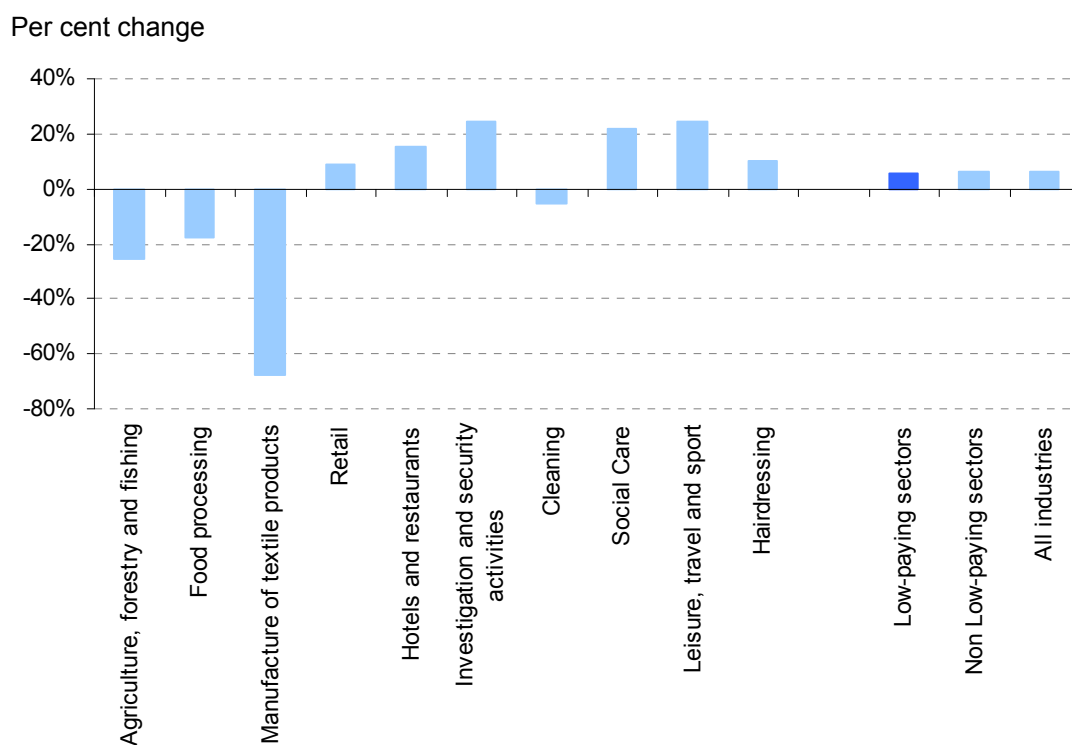
Evidence on hours worked

Employers may alter hours rather than levels of employment in response to minimum wages. This is particularly likely for low paying sectors as they have low fixed costs per worker, little on-the-job training, high labour turnover, limits to the substitution of capital for labour and a high incidence of part-time work. Empirical studies have found some impact of minimum wages on hours for example Stewart and Swaffield (2006)⁹ (see Annex F).

Over 1999-2008 total hours worked in the low-paying sectors grew around 5.6 per cent, less than the 6.5 per cent growth in the non low-paying sectors (see Chart 3.8). The variation across the low paid sectors has been significant. It is not possible to disentangle the impact of the NMW from the UK being exposed to lower-cost international competition and other factors.

⁹ Stewart M and Swaffield (2006) The other margin: Do minimum wages cause working hours adjustment for low-wage workers? Unpublished paper. University of Warwick.

Chart 3.8: Changes in hours worked for low pay sectors, 1999-2008

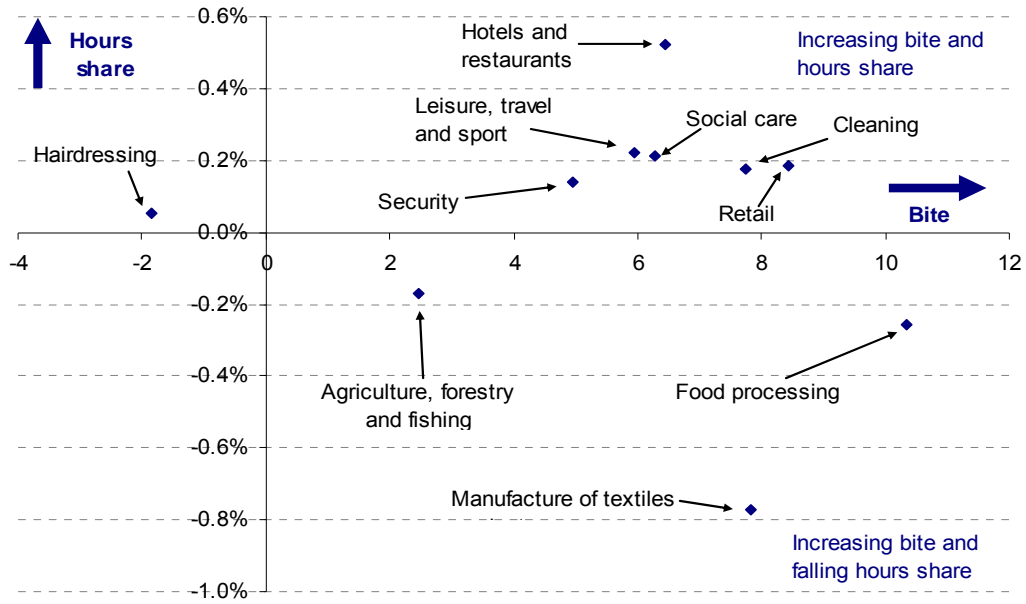


Source: Office for National Statistics, Annual Survey of Hours and Earnings
1999 - ASHE data - excluding supplementary information
2008 - ASHE data - new methodology
See annex H for further information on the changes to ASHE data.

Chart 3.9 shows a small correlation between changes in the bite and hours. However, this relationship is not consistent across sectors and, as with employment, may be driven by wider sectoral changes in the UK economy.

Chart 3.9: Change in bite against change in hours share, 1999 to 2008

Per cent change



Source: Office for National Statistics, Annual Survey of Hours and Earnings
 1999 - ASHE data - excluding supplementary information
 2008 - ASHE data - new methodology
 See annex H for further information on the changes to ASHE data.
 Those aged 22+.

4 Developments in the labour market for younger workers

The labour market has proved challenging for some younger workers. The employment rate of 16 and 17 year olds, excluding full-time students, has been declining for the last decade, although it has slightly improved over 2007 and the first half of 2008. The 18-21 year old age group has also experienced a fall in employment rates since around mid 2001, but this drop is much smaller than for their younger counterparts. Past experience suggests that unemployment amongst young people tends to grow faster than for older workers during an economic downturn.

This section includes a separate analysis of younger workers. This focus is warranted as evidence suggests that the labour market outcomes of younger workers are more at risk from the uprating of the minimum wage. As younger workers are typically paid less than older workers, the bite of the NMW is significantly higher for younger age groups than for adults. In addition, the NMW can potentially change the balance of incentives between education and employment. Therefore, it is important to monitor the labour market outcomes of this group closely to strike the right balance between protecting young workers while not jeopardizing their employment and education prospects.

More details on employment and unemployment rates by age group can be found at Annex B.

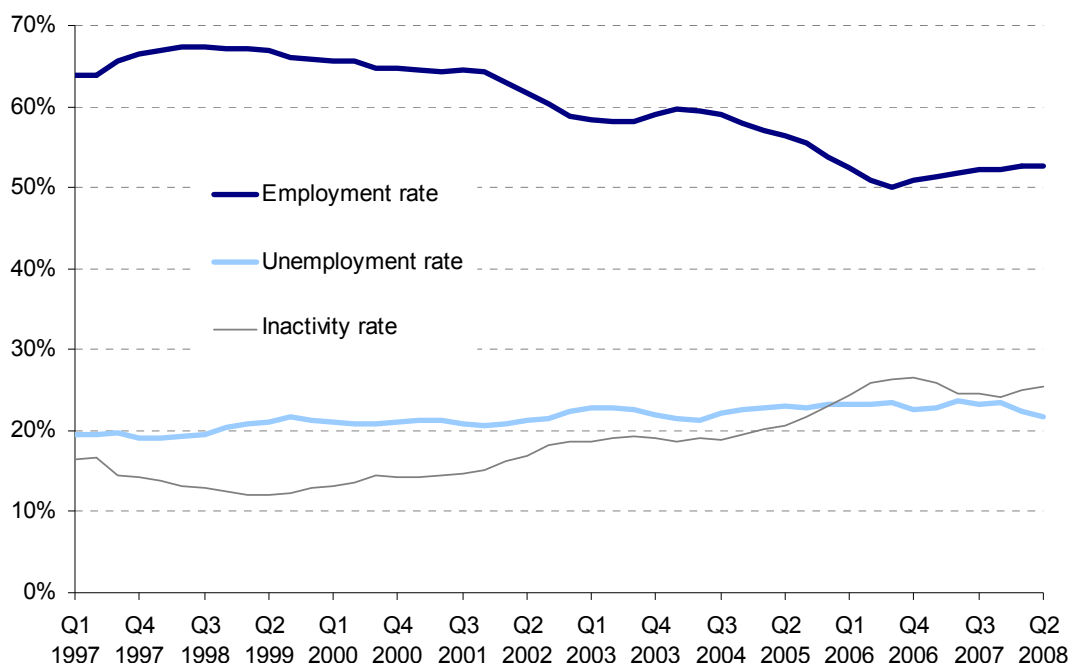
16-17 year olds

The minimum wage rate for 16-17 year olds was introduced in October 2004. It was initially set at the rate of £3.00 and was increased to £3.30 from October 2006, then £3.40 from October 2007 and £3.53 from October 2008.

Chart 4.1 indicates that the employment rate of 16 and 17 year olds, excluding full-time students, was declining until late 2006, when the trend started to improve slightly. It has continued to improve into the first half of 2008. However, the outlook for further improvements is uncertain given the current slowdown in economic activity.

Chart 4.1: Employment, unemployment and inactivity rates of 16-17 year olds, excluding full time students and graduates

Per cent of age group, four quarter moving average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See Annex H for further information.

The deterioration in labour market outcomes for 16-17 year olds has taken place over a period when the employment rates of most disadvantaged groups have risen faster than the overall working age employment rate. However, the deterioration largely pre-dated the introduction of the NMW and since its introduction there has been some improvement. Therefore the relationship between the employment of 16-17 year olds and the NMW is not simple.

It may also partly reflect the increasing participation of 16 and 17 year olds in education. Participation in full-time education for 16 and 17 year olds has increased significantly since 2004. This may be because any inducement of the 16-17 NMW to enter employment has at least been partly offset by the introduction of the Education Maintenance Allowance¹⁰ at the same time. As more stay on in full-time education, those entering the labour market may increasingly be those that will find it most difficult to find employment.

18-21 year olds

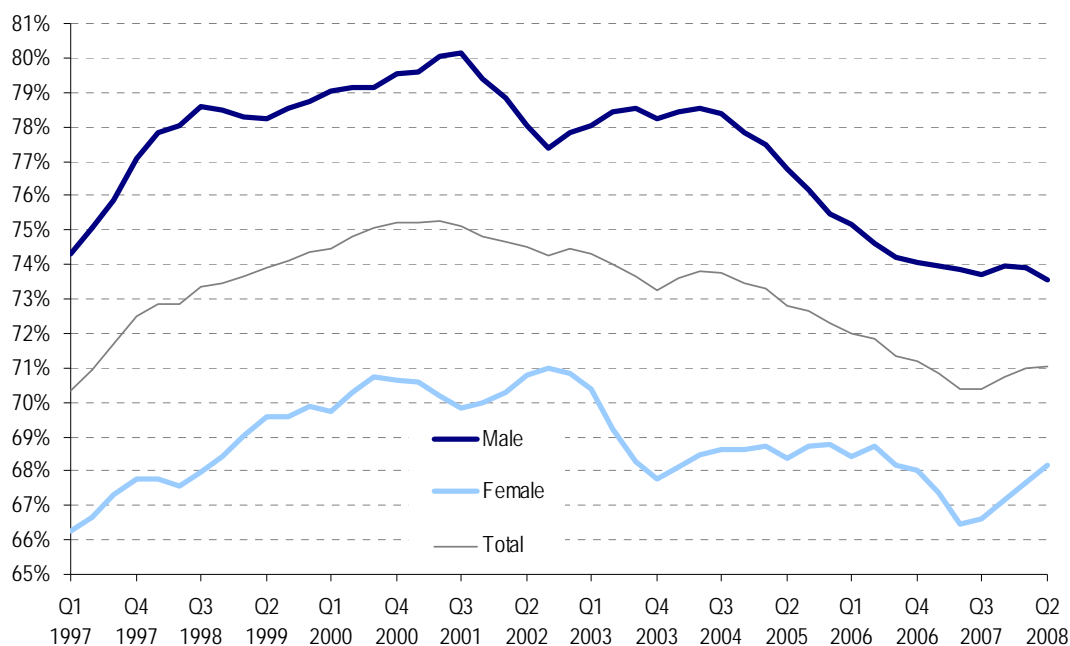
The employment rate amongst 18 to 21 year olds, excluding full time students and graduates, is now lower than at the time the minimum wage was introduced in 1999 (see Chart 4.2). However, the employment rate for males and females has shown a notable diversion in employment rates since early 2007 - with the employment rate for males continuing to decline and the rate

¹⁰ Education maintenance allowance is a payment of up to £30 a week to eligible 16-18 year olds who have left, or are about to leave, compulsory education to assist them financially if they pursue further education.

for females increasing. The unemployment rate has similarly diverged in the same period. (see Chart 4.3)

Chart 4.2: Employment rate of 18-21 year olds excluding full-time students and graduates

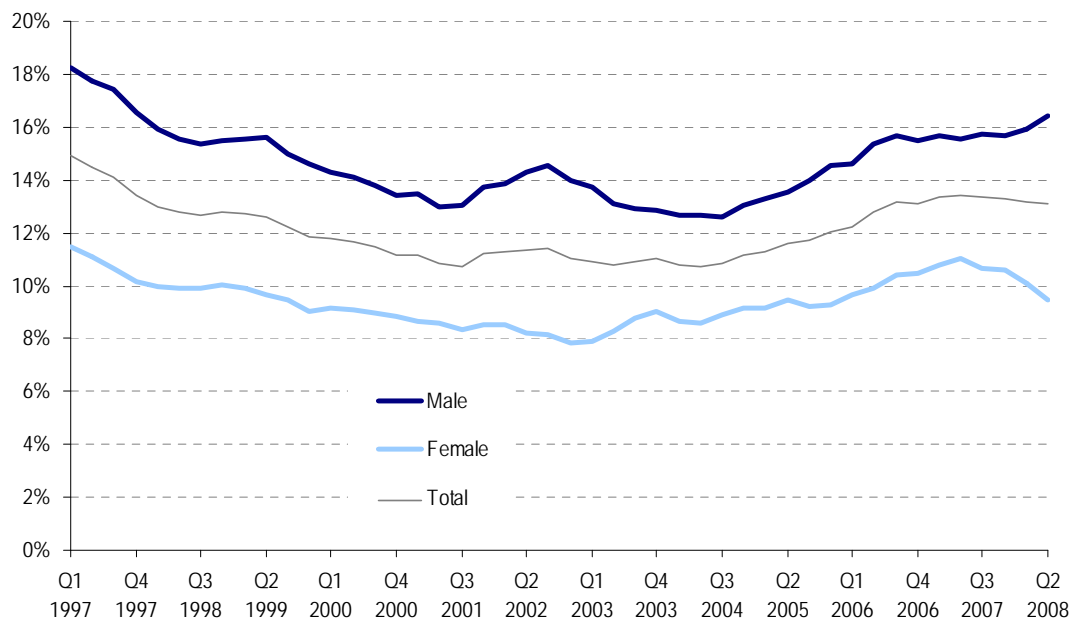
Per cent of age group, four quarter moving average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See Annex H for further information.

Chart 4.3: Unemployment rate of 18-21 year olds excluding full-time students and graduates

Per cent of age group, four quarter moving average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See Annex H for further information.

Currently 21 year olds are covered by the Development rate, as the Government believed last year that the labour market performance of 21 year olds resembles more closely that of 18-20 year olds than older workers. Looking at the employment rate (excluding students and graduates) by individual age, in the past the employment rate of 21 year olds moved more in line with the 19-20 year old rate. However, from around mid 2006 the employment rate of 21 year olds appears to be closer to 22-23 year olds than 19-20 year olds.

In addition, the unemployment rate of 21 year olds also remains above that of 22-23 year olds but below that of 19-20 year olds. Past experience suggests that unemployment amongst young people tends to grow faster than for older workers during an economic downturn.

The 21 year old bite (68 per cent) is around 18 percentage points higher than the adult minimum wage as a per cent of median earnings, while it is around 8 percentage points below the 18-20 year old bite.

5 Other issues

The Government is consulting on the use of tips as part of the NMW which will mainly affect the restaurant and hotel sectors. If tips are excluded from NMW payments this may have some upward cost implications for NMW employers in tipping sectors.

The Government is increasing the current statutory minimum holiday entitlement from 4 weeks to 5.6 weeks, to take account of 8 bank holidays that should be paid in addition to 4 weeks holiday entitlement. Half of the increase has already taken effect from October 2007 and the remaining increase will be introduced in April 2009. As a large proportion of those benefiting from the minimum wage will also benefit from the extension of leave, this will have upward cost implications for many NMW employers.

Total immigration (inflows) fell in 2007, but emigration (outflows) fell faster resulting in a marked rise in net inward migration. However, more recent evidence from 2008 suggests inward migration from some areas, such as A8¹¹ countries, are slowing, continuing a trend first seen since in the second half of 2007. Many recent migrants continue to be employed in lower paid jobs and sectors. The proportion of foreign-national workers in low-paying sectors increased further in 2007.

Government is committed to establishing apprenticeships as a key route to building the national skills base, working with employers to help young people and adults get the skills and qualifications that employers value.

Tips and the National Minimum Wage

On November 21st 2008 the Government launched its consultation on the use of tips as part of the NMW. The Government is consulting on removing the use of tips as part or whole payment of the NMW. The partial impact assessment based on ASHE data estimates that between 4,500 and 44,800 workers could be affected by the change in the legislation.

Sectors that are likely to be affected include hotel and restaurants, taxi operations, gambling and betting activities and hairdressing and beauty. A change in the law will increase employers labour costs. Employees will benefit through increases in take-home pay (assuming tips are passed on to the employee) and there will be a transfer to the Exchequer because of increased employer and employee National Insurance contributions. The table below is taken from the partial impact assessment which summarizes the costs and benefits¹².

¹¹ The A8 countries are Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia

¹² <http://www.berr.gov.uk/consultations/page48902.html>

Table 5.1. Summary table of costs and benefits of amending NMW regulations on the use of tips

		Option 1	Option 2
Costs	Increase in employers' labour costs	Up to £6.5 - 66.8 million	Up to £6.5 - 66.8 million
	Increase in employees' NICs	Up to £0.6 - 6.5 million	Up to £0.6 - 6.5 million
	Increase in administrative costs	Small	Small
	Implementation costs	Small	Small
Benefits	Better quality of service, equalisation of NICs treatment across sectors, eligibility for statutory benefits and less administrative burden	Small - Not quantified because the number of people concerned is small	
	Transfer to the Exchequer	Up to £1.4 - 14.1 million	Up to £1.4 - 14.1 million
	Increase in pay for employees	Up to £5.7 - 59.2 million	Up to £5.7 - 59.2 million

Figures have been rounded and totals may not sum to individual parts due to rounding
Option 1 - all tips, service charges, gratuities and cover charges, whether discretionary or mandatory, are excluded from counting towards the NMW, and consumer information and awareness is improved;
Option 2 - only discretionary tips and gratuities, and mandatory and discretionary service charges are excluded from counting towards the NMW and consumer information and awareness is improved.
Options 1 and 2 have similar costs and benefits although option 2 provides more flexibility for employers as cover charges can be included in the NMW

Holiday entitlement

The Government plans to increase the current statutory minimum holiday entitlement from 4.8 weeks to 5.6 weeks (maximum 28 days), to implement its commitment to make paid time off for bank holidays additional to the previous four-week holiday entitlement.

The increased holiday entitlement has been implemented by amending the current Working Time Regulations regarding the quantum of annual leave. The introduction of the increased holiday is phased – the entitlement increased to 4.8 weeks (equivalent to an extra four days' holiday for someone working five days a week) from October 2007 and the remaining increase will be introduced in April 2009.

The final Impact Assessment estimated that a total of 6 million people will benefit from the increased holiday entitlement (including 4.5 million employees and 1.5 million other workers).¹³ The estimated annual wage cost for implementing this is between £2.6 billion and £3.5 billion. Adding on non-wage labour costs implies an annual total labour cost of £3.3 billion to £4.4 billion.¹⁴ There are also expected to be additional administration costs; £140 million transitional costs and £43 million ongoing administrative cost.

As an example, Table 5.2 looks at the cost for a representative NMW worker who benefits from the full 8 day increase in holidays. The first tranche of increased holiday leave is estimated to have added nine pence to the wage cost of this representative NMW employee and ten pence to the total labour

¹³ See BERR (2007) *The Working Time (Amendment) Regulations 2007. Final Regulatory Impact Assessment*. June 2007. (<http://www.berr.gov.uk/files/file39873.pdf>).

¹⁴ This includes non-wage labour costs of 20 per cent, which is consistent with the Labour Cost Survey.

cost. Assuming the same level of minimum wages, the second tranche of additional holiday to be introduced in April 2009 should have a similar cost.

Table 5.2. Example: cost of additional holiday entitlement for a representative person on the NMW who receives full 8 day increase

Element of cost	Cost £	Assumptions
Wage cost of first holiday tranche (from 1 Oct 2008)	£0.09	Annual per cent increase = $0.8/52\text{weeks} = 1.5\%$ Cost = $1.5\% * £5.73$ (NMW from 1 Oct 2008)
Wage cost of second holiday tranche (from 1 April 2009)	£0.09	As above
Total wage cost	£0.17	Annual per cent increase = $1.6/52\text{weeks} = 3.1\%$ Cost = $3.1\% * £5.73$ Or sum of tranche 1 and 2.
Total labour costs of first tranche	£0.10	Wage cost * 1.20 (20% non-wage labour costs are consistent with the Labour Force Survey)
Total labour costs of second tranche	£0.10	As above
Total labour cost	£0.21	Sum of tranche 1 and 2
Administration costs	£0.003	Annual admin costs are £6.53 based on total admin costs divided by number of beneficiaries. Converted to an hourly cost assuming a 37 hour working week ¹⁵
Total cost per person	£0.21	Sum of total labour cost and administration costs

Source: Methodology is taken from BERR (2007) The Working Time (Amendment) Regulations
Numbers may not sum due to rounding.

This gives a total additional labour cost to an employer of the representative NMW worker of around 21 pence. Adding on additional administration costs from processing the increased holiday entitlement provides a total per person, per hour cost of still around 21 pence.¹⁶ This is an absolute maximum cost, as a number of people on the NWM will already have some or all of the extra statutory eight days entitlement.

Apprenticeships

In September, Department for Innovation, Universities & Skills (DIUS) and the Department for Children, Schools and Families (DSCF) announced that from August 2009 the Learning and Skills Council's minimum weekly earnings for apprentices in England will be increased from £80 to £95 a week.

The increase follows a review by DIUS and DCSF of apprentice pay carried out this year. The average net earnings of an apprentice each week is £170. The increase was to ensure that the earnings of all apprentices are fair and reflect the support given to young people pursuing other qualifications.

The new £95 minimum will benefit an estimated 26,000 (about 10 per cent) apprentices, mostly those in traditional less well paid sectors such as hair dressing and social care - of whom 90 per cent are women.

¹⁵ It assumed that processing the additional holiday entitlement would take 15 minutes of management time per worker.

¹⁶ This is only the ongoing annual cost of implementing the additional holiday leave and excludes the one-off transitional cost from introducing the new legislation.

Over 130,000 employers are offering apprenticeship places in over 180 different types of apprenticeships across 80 industry sectors. Apprenticeships have increased rapidly from 65,000 in 1996/97 to 184,000 in 2006/07 and they are projected to grow to almost 210,000 by 2010/11, on the way to the Government's ambition to increase the number of apprentices in line with the Leitch target of 400,000 in England. Apprenticeship completion rates are also increasing, having reached an all time high in the recent period of 63 per cent in 2006/07 compared to 24 per cent in 2001/02. Apprenticeships are a key route to building the national skills base, working with employers to help young people and adults get the skills and qualifications that employers value.

Migration

Net migration in 2007 rose to 237,000. However, both inward and outward migration fell. The rise in net migration occurred because emigration (outflows) fell faster than immigration (inflows).

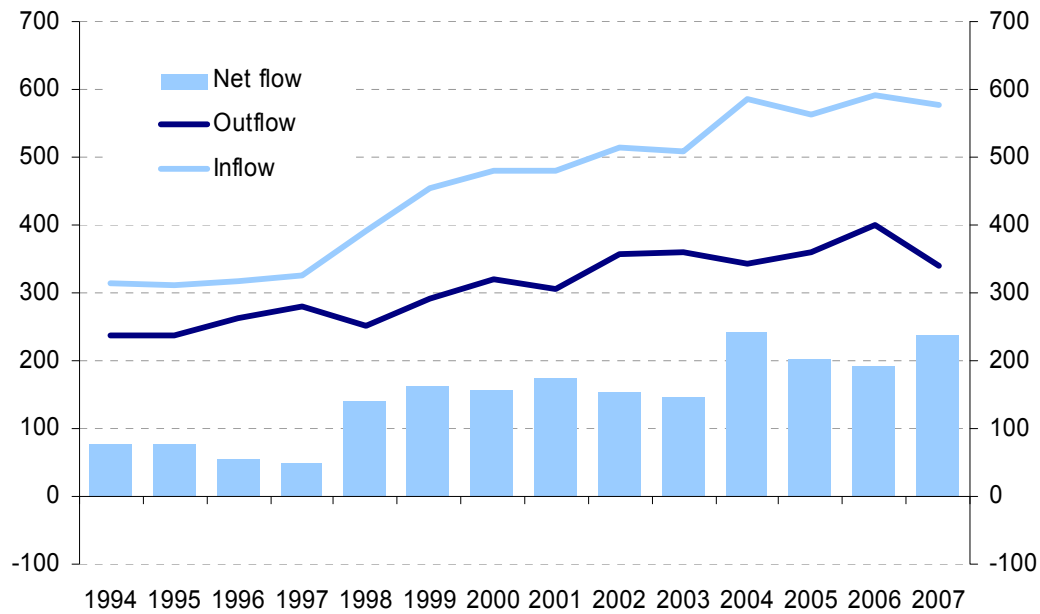
One of the main drivers of the increase in inflows of migrants in recent years has been the influx of people from the 8 new EU member states since their accession in 2004. The numbers increased year on year until 2007 but later information from the Worker Registration Scheme (WRS) suggests that the numbers, although still substantial, are now falling. There are also some indications from other sources that immigration overall has peaked. What effect this has on net migration will depend more on the numbers emigrating. However, estimates of recent data on migration are not available.

In the labour market many migrants appear, at least initially, to enter the lower end of the labour market. While the majority of new European immigrants are relatively well-educated in comparison with the indigenous population, they predominantly work in the least skilled occupations and the low-paying industries such as administration, hospitality and catering, and food processing¹⁷.

¹⁷ See Saleheen, J. and C. Shadforth (2006) The Economic Characteristics of Immigrants and their Impact on Supply. *Quarterly Bulletin*, Vol. 46, No. 4, Bank of England, London.

Chart 5.1. Inflows and outflows of migrants into the UK

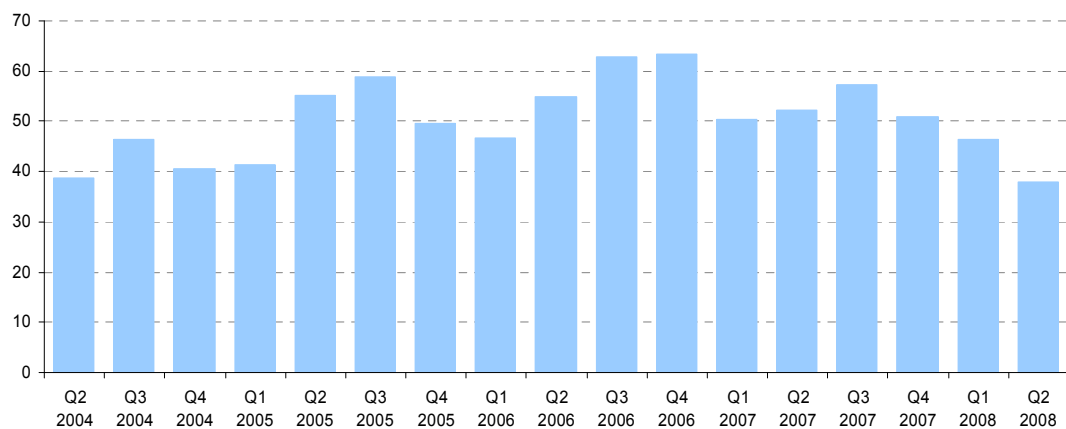
Thousands



Source: Office for National Statistics, International Passenger Survey

Chart 5.2. Approved applications for the Workers Registration Scheme

Thousands



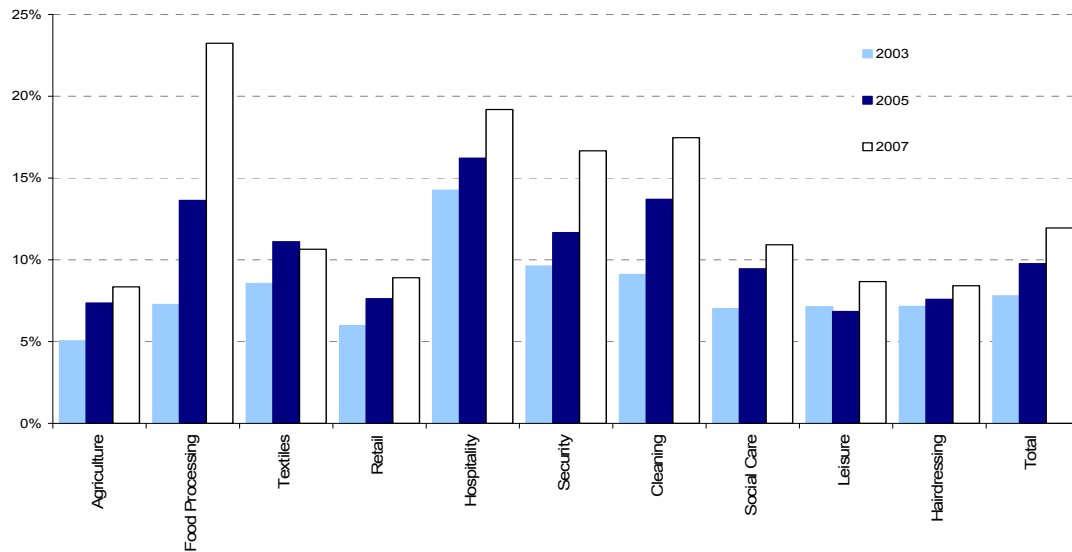
Source: WRS, Home Office

This table shows applicants rather than the number of applications made. The figures are for initial applications only and do not include multiple applications, where an individual is doing more than one job simultaneously, or applications to re-register, where an individual has changed employers.

Chart 5.3 highlights that the proportion of all foreign-national workers in the low paid sectors – both A8 and non-A8 workers - has generally been increasing.

Chart 5.3. Proportion of foreign-national workers in low-pay sectors

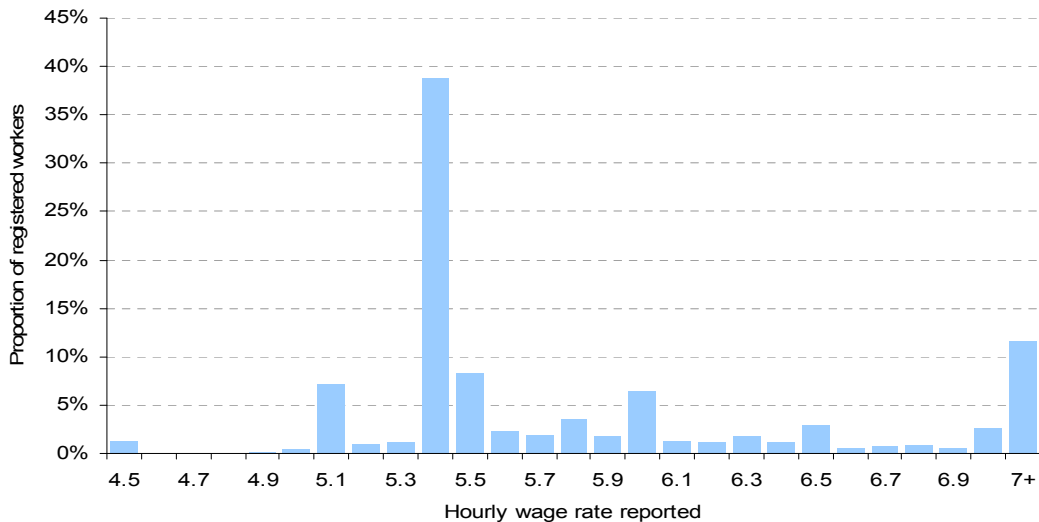
Per cent of total



Source: Office for National Statistics, Labour Force Survey

Also, a high proportion of the recent relatively large inflows of A8 migrants are affected by the NMW. Data on the hourly rate of pay of A8 migrants from the WRS show that a high proportion – just over 40 per cent of registrations reported pay at or close to the minimum wage rate of the time (see Chart 5.4)¹⁸.

Chart 5.4. Distribution of reported hourly pay of workers registering on the WRS between October 2006-March 2007



Source: Workers Registration Scheme, Home Office

The figures have been sorted so as to include only people aged 22 or older, all application outcomes (approved, cancelled, exempt, refused, withdraw) and to exclude people registered as from "other" nationality (other than A8).

The economic and fiscal impacts of immigration were summarized in a 2007 cross-departmental submission to the House of Lord Select Committee on

¹⁸ The Workers Registration Scheme (WRS) requires employees (but not the self-employed) from the A8 countries to register before taking work.

Economic Affairs.¹⁹ As migration increases the supply of labour, there are often concerns that it will depress wages or increase unemployment for domestic workers. However, this fear is often based on a 'lump of labour' fallacy that there is a fixed number of jobs to go around. As migrants consume as well as work, they increase the demand for, as well as the supply of labour. In addition, if migrants fill skill shortages in the labour market they may allow some sectors to expand, increasing employment opportunities for domestic workers. Indeed the broad academic consensus is that the impact of migration on native labour market outcomes in the UK is negligible.²⁰

In the labour market the broad academic consensus is that the impact of migration on native labour market outcomes is negligible²¹. For example, the most recent UK analysis, based on claimant count data²², found no support for the argument that accession country immigrants have contributed to overall unemployment or that of younger workers – a group most likely to be affected.

A significant increase in the labour supply through migration may also be expected to put downward pressure on wage growth. However, generally research has tended to find that any effects are small. A recent UK study found that the inflow of migrants between 1997 and 2005, which largely predated the recent A8 immigration, boosted the wage growth of most domestic workers. However, at the lower end of the wage distribution, although wages continued to grow, the rate of increase was slightly slowed by migration. The impacts were small, perhaps reflecting the insulating role played by the NMW. Over the period considered, the real (inflation-adjusted) hourly wage grew by an average of 18 pence per year at the first decile. Without immigration, this figure would have been 0.7 pence higher. Further up the wage distribution, immigration added about 1.5 pence per year to real hourly wage growth at the median, and 2.3 pence at the ninth decile.²³

¹⁹ Home Office and Department for Work and Pensions (2007) *The Economic and Fiscal Impact of Immigration*. A Cross-Departmental Submission to the House of Lords Select Committee on Economic Affairs.

²⁰ See, for example, Dustmann C, Fabbri F, Preston I and Wadsworth J (2003) *The local labour market effects of immigration in the UK*. Home Office Online Report 06/03 (www.homeoffice.gov.uk/rds/pdfs2/rdolr0603.pdf0) or Blanchflower, D., Saleheen, J. and Shadforth, C. (2007) *The Impact of the Recent Migration from Eastern Europe on the UK Economy*, Bank of England. (<http://www.bankofengland.co.uk/publications/speeches/2007/speech297.pdf>).

²¹ Gilpin, N. et al. (2006) *The Impact of Free Movement of Workers from Central and Eastern Europe on the UK Labour Market*. Working Paper, No. 29, Department for Work and Pensions, London.

²² Gilpin, N. et al. (2006) *The Impact of Free Movement of Workers from Central and Eastern Europe on the UK Labour Market*. Working Paper, No. 29, Department for Work and Pensions, London.

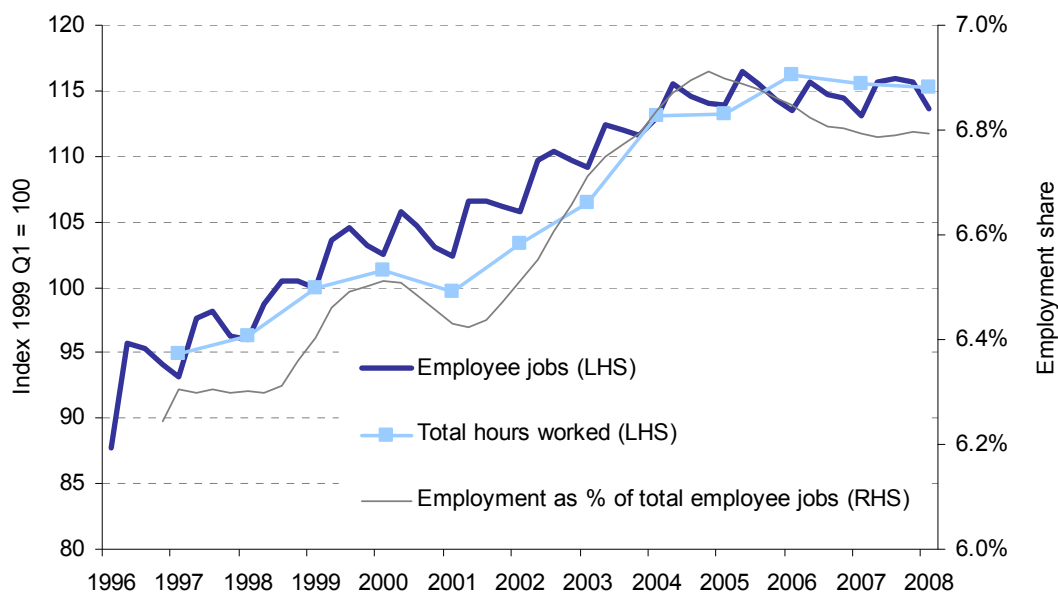
²³ Dustmann, C., Frattini, T. and Preston, I. (2007) *A study of migrant workers and the national minimum wage and enforcement issues that arise*. Report commissioned by the Low Pay Commission (<http://www.econ.ucl.ac.uk/cream/pages/LPC.pdf>).

ANNEX A Employment in low-paying industries

This annex looks at trends in employee jobs in the main low-paying sectors in the UK economy: hotels and restaurants, textile and textile products, security, cleaning, leisure, social care and retail.

Chart A1. Employee jobs and total hours in hotels and restaurants

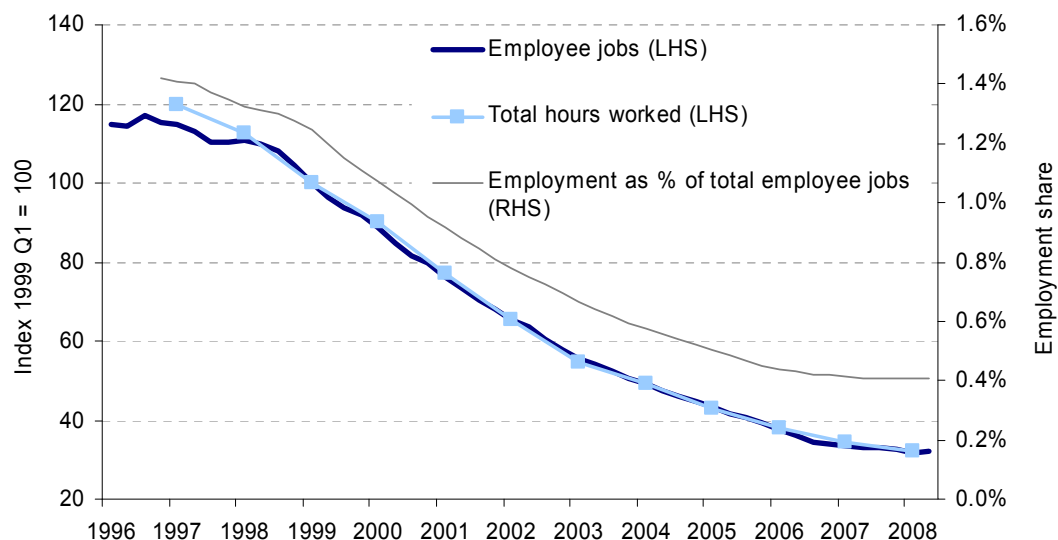
Index and per cent of total



Source: Office for National Statistics, Employee jobs, 4-quarter averages
Not seasonally adjusted.
Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A2. Employee jobs and total hours in textiles and textile products

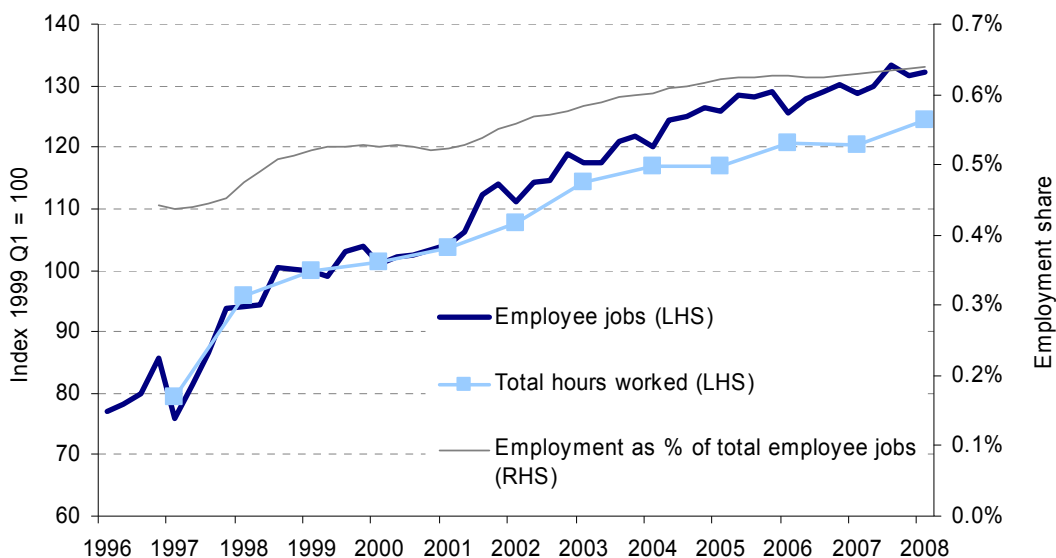
Index and per cent of total



Source: Office for National Statistics, Employee jobs, 4-quarter averages
Not seasonally adjusted.

Chart A3. Employee jobs in investigation and security activities

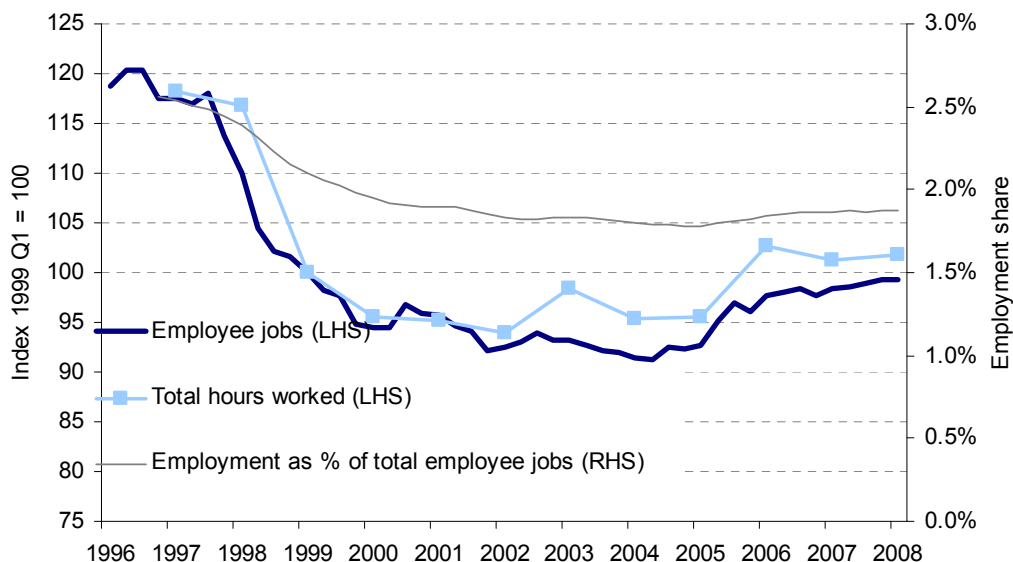
Index and per cent of total



Source: Office for National Statistics, Employee jobs, 4-quarter averages
 Not seasonally adjusted.
 Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A4. Employee jobs and total hours in cleaning

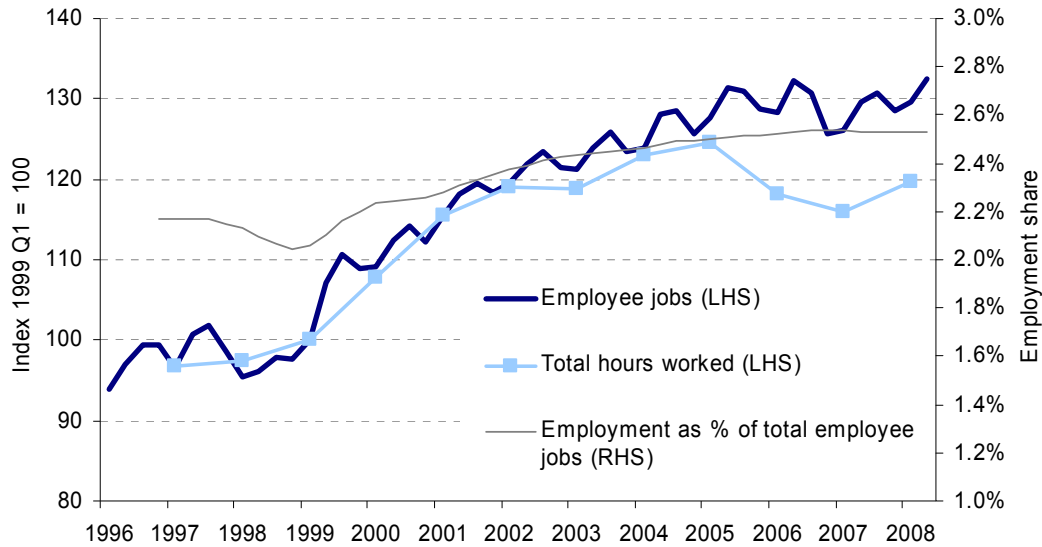
Index and per cent of total



Source: Office for National Statistics, Employee jobs, 4-quarter averages
 Not seasonally adjusted.
 Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A5. Employee jobs and total hours in leisure, travel and sport

Index and per cent of total



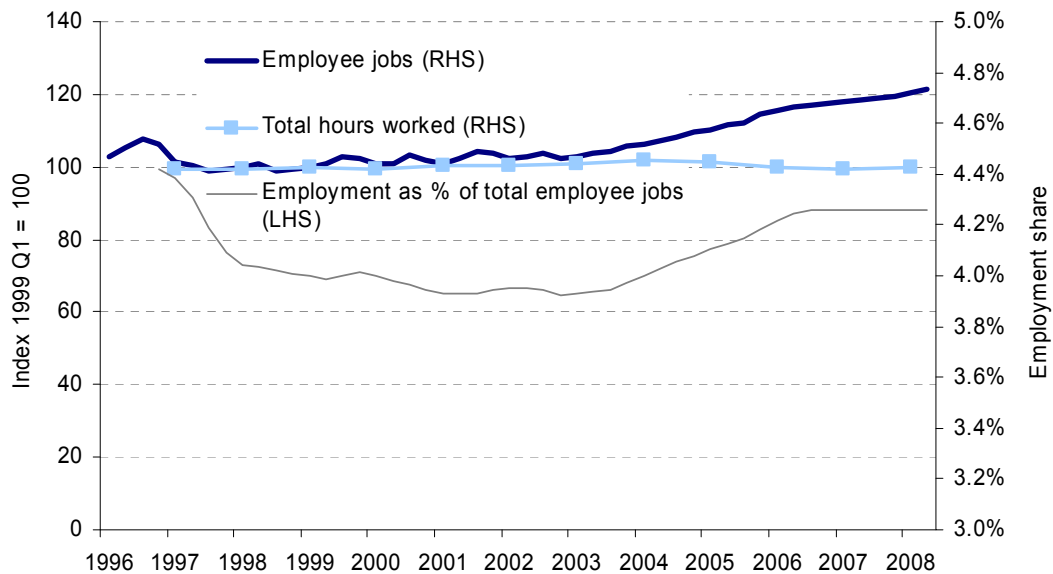
Source: Office for National Statistics, Employee jobs, 4-quarter averages

Not seasonally adjusted.

Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A6. Employee jobs and total hours in social care

Index and per cent of total



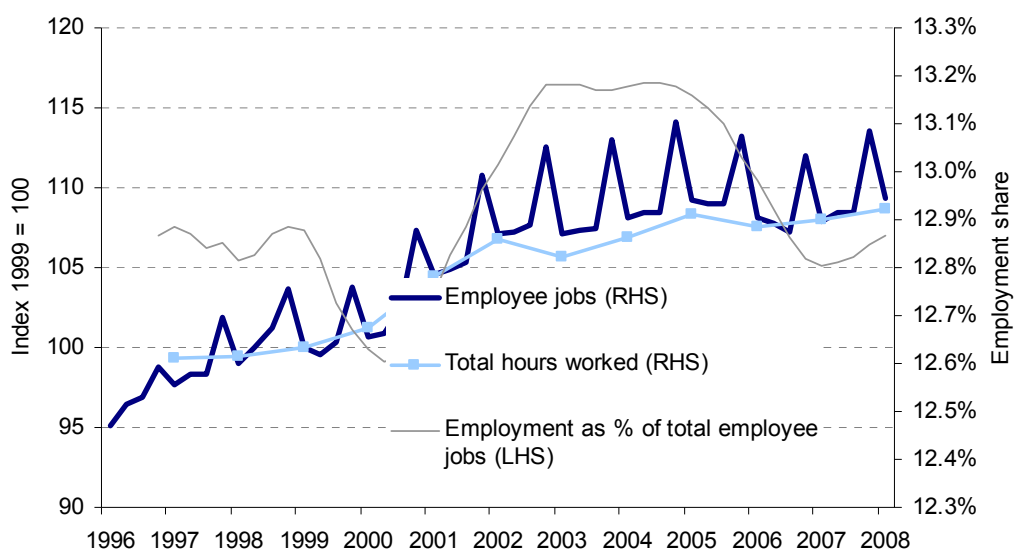
Source: Office for National Statistics, Employee jobs, 4-quarter averages

Not seasonally adjusted.

Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A7. Employee jobs and total hours in retail

Index and per cent of total



Source: Office for National Statistics, Employee jobs, 4-quarter averages

Not seasonally adjusted.

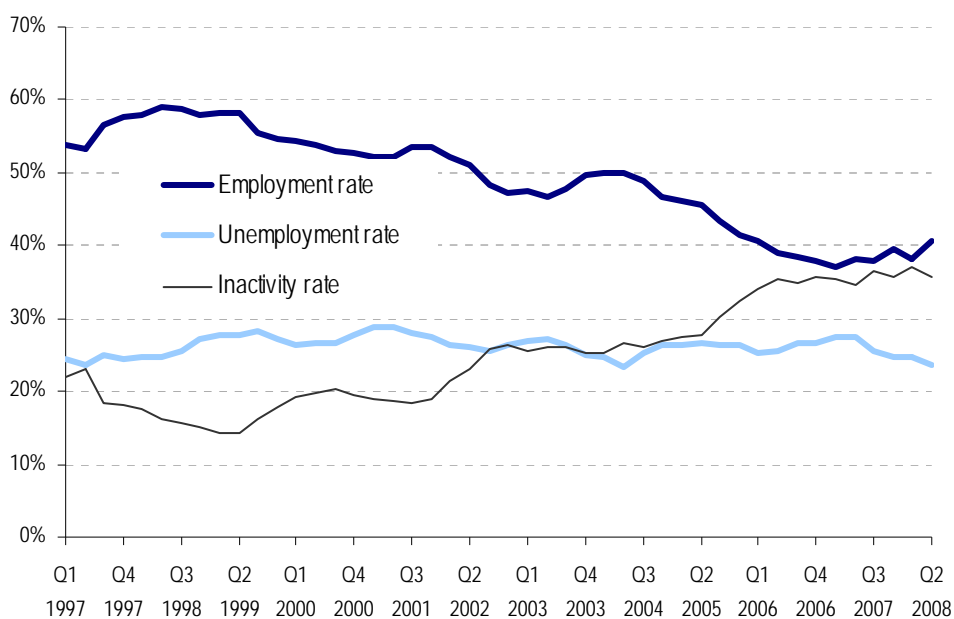
Total hours worked: employee jobs * mean weekly total hours from ASHE.

ANNEX B Employment and unemployment rates by age group

This annex provides a breakdown of employment and unemployment rates for the 16 to 23 year olds. It is a complement to the analysis in section 4 on the labour market for younger workers.

Chart B1: Employment, unemployment and inactivity rates of 16 year olds excluding full-time students and graduates

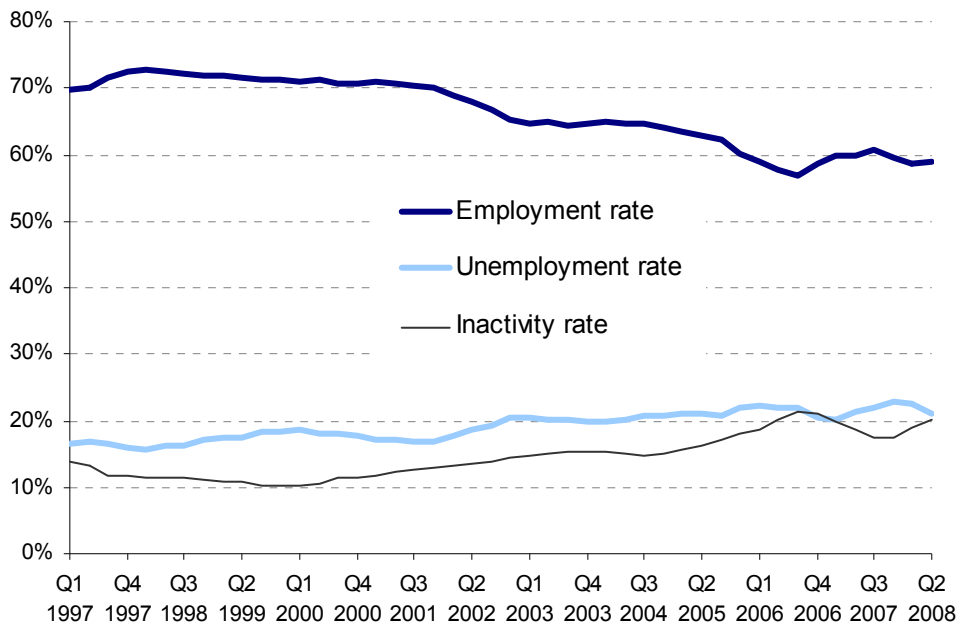
Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
Not seasonally adjusted.
Results have been updated with new weights back to 1997.
See annex H for further information.

Chart B2: Employment, unemployment and inactivity rates of 17 year olds excluding full-time students and graduates

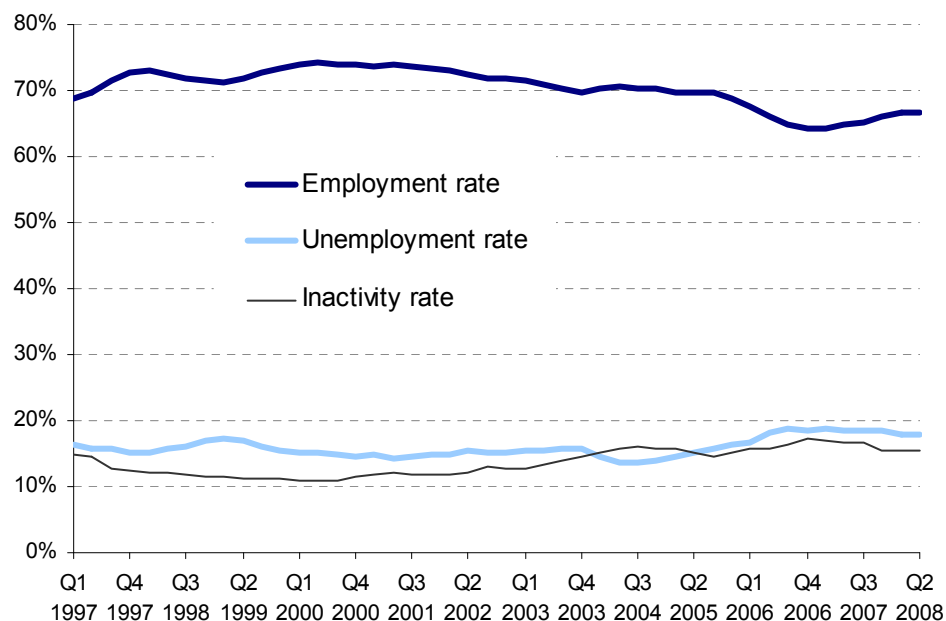
Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See annex H for further information.

Chart B3: Employment, unemployment and inactivity rates of 18 year olds excluding full-time students and graduates

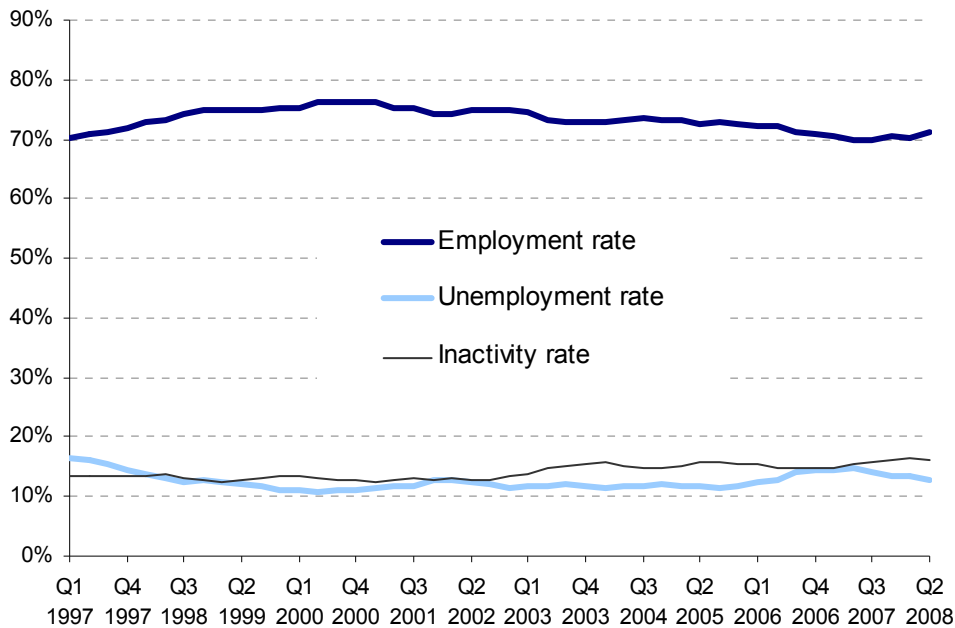
Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See annex H for further information.

Chart B4: Employment, unemployment and inactivity rates of 19 year olds excluding full-time students and graduates

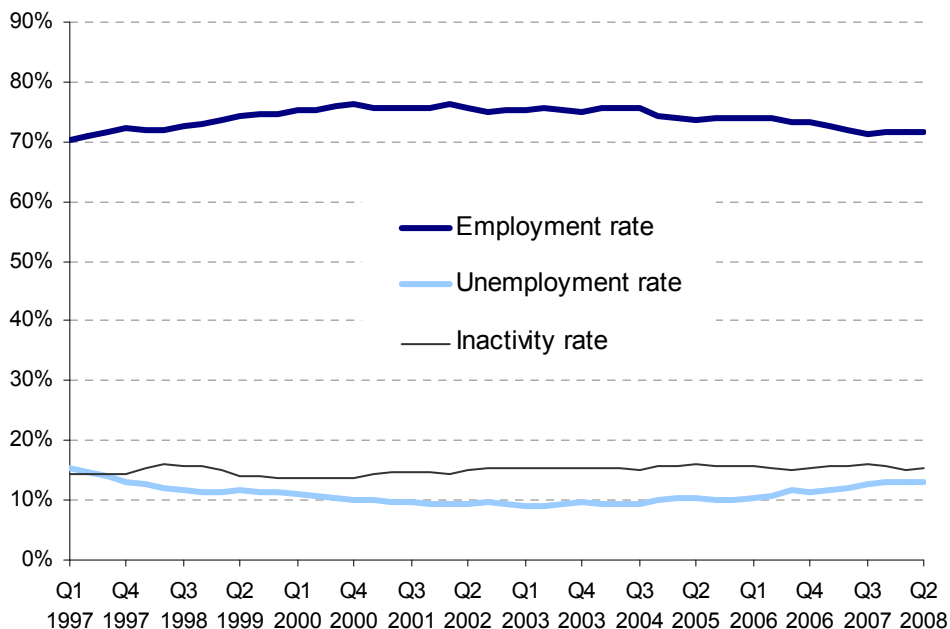
Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See annex H for further information.

Chart B5: Employment, unemployment and inactivity rates of 20 year olds excluding full-time students and graduates

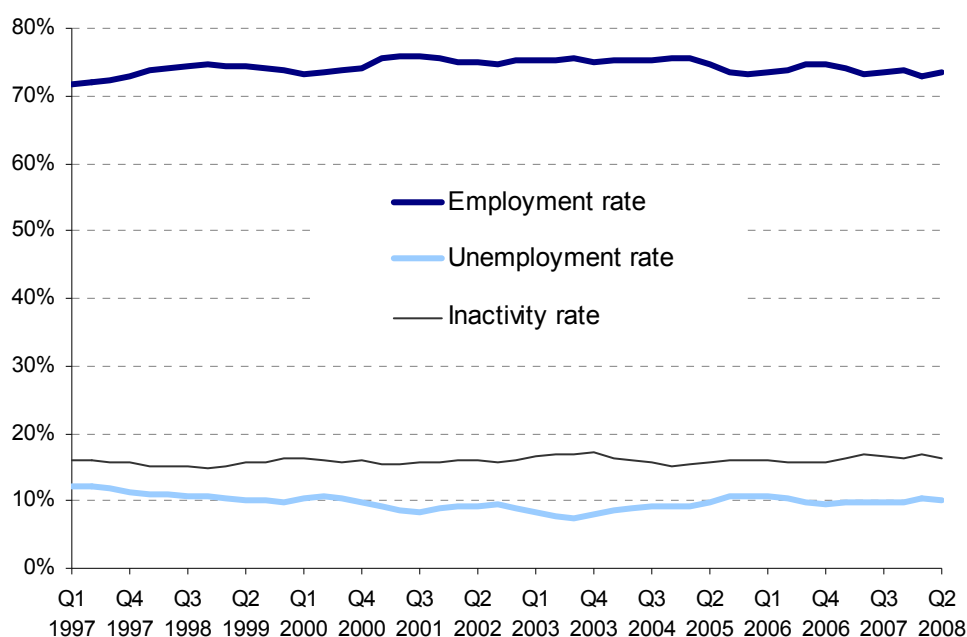
Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997
 See annex H for further information.

Chart B6: Employment, unemployment and inactivity rates of 21 year olds excluding full-time students and graduates

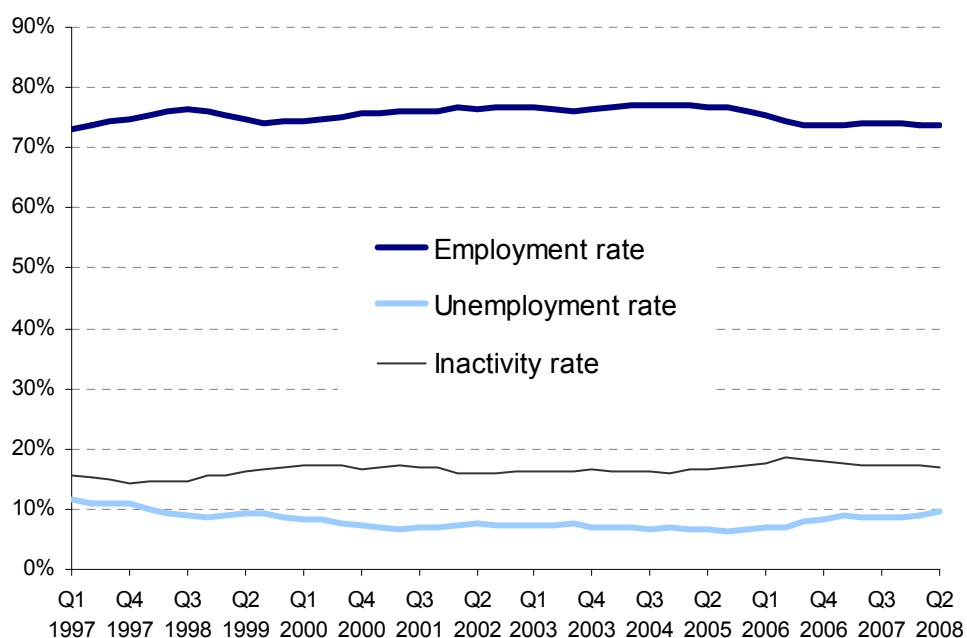
Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See annex H for further information.

Chart B7: Employment, unemployment and inactivity rates of 22 year olds excluding full-time students and graduates

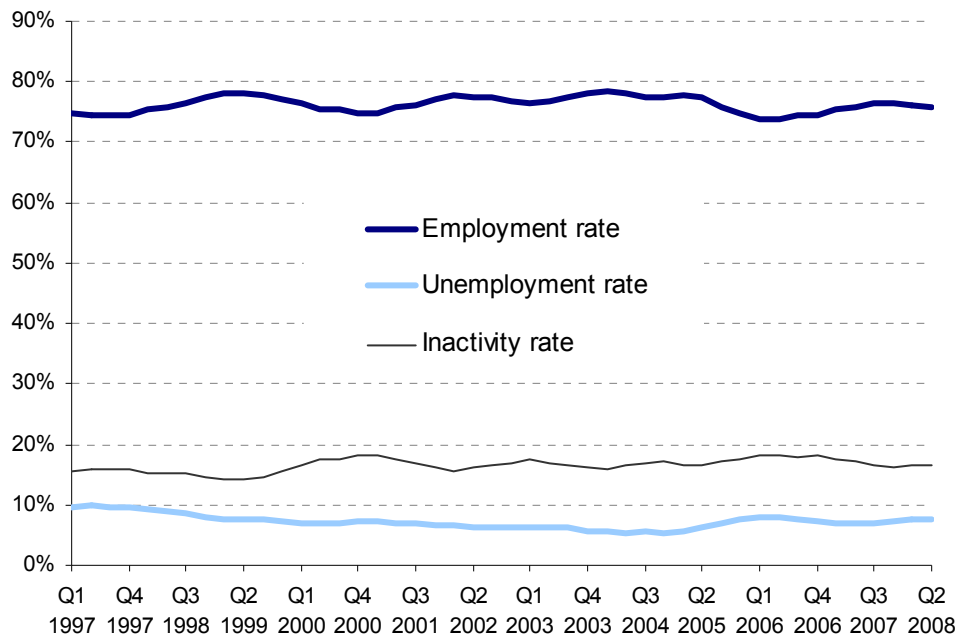
Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See annex H for further information.

Chart B8: Employment, unemployment and inactivity rates of 23 year olds excluding full-time students and graduates

Per cent, four quarter (annual) average



Source: Office for National Statistics, Labour Force Survey. 4-quarter averages.
 Not seasonally adjusted.
 Results have been updated with new weights back to 1997.
 See annex H for further information.

ANNEX C Regional employment in low-paying industries

Table C.1. Employee jobs in the low-paying sectors by region (000's)

	North East	North West	Yorkshire & Humber	East Midlands	West Midlands	Eastern	London	South East	South West	Wales	Scotland	Great Britain	Y/Y*
Agriculture, Forestry and Fishing Sic 01-05													
1998	6	20	20	27	23	40	4	47	36	16	39	279	
1999	6	18	20	25	22	37	3	45	33	16	37	262	-5.9
2000	5	17	18	24	20	35	5	41	30	13	38	244	-7.0
2001	6	17	18	24	21	35	4	42	29	12	39	246	0.8
2002	5	16	17	22	20	34	3	41	28	12	38	237	-3.8
2003	5	15	16	22	18	32	3	40	27	13	36	226	-4.5
2004	5	15	17	22	20	32	3	41	28	14	36	233	3.0
2005	5	16	16	22	21	32	2	40	28	14	36	232	-0.2
2006	4	15	16	22	21	30	2	40	26	14	36	221	-2.1
Childcare Sic 85.32													
1998	21	53	39	33	42	39	77	58	45	28	38	472	
1999	21	60	41	30	45	37	75	59	43	28	48	487	3.1
2000	21	57	40	30	42	36	75	60	42	28	46	477	-2.2
2001	23	63	45	32	44	44	77	68	45	31	48	520	9.0
2002	23	62	50	34	44	38	82	70	42	33	53	531	2.1
2003	25	61	52	42	47	36	76	72	43	34	60	547	3.0
2004	24	61	55	37	48	40	81	74	47	37	66	569	4.1
2005	25	66	55	43	58	46	87	79	53	41	74	625	9.7
2006	28	66	53	42	59	48	87	85	53	37	72	631	0.9
Cleaning Sic 74.7, 93.01													
1998	17	54	44	33	53	51	96	62	32	18	47	508	
1999	14	50	41	27	44	45	96	62	29	18	42	469	-7.7
2000	12	47	42	26	43	49	102	64	31	18	48	482	2.8
2001	14	52	38	24	46	43	96	62	31	13	46	463	-3.9
2002	15	53	39	25	46	45	93	63	33	14	41	466	0.7
2003	14	49	39	19	45	42	89	69	34	14	45	459	-1.5
2004	15	45	35	21	45	38	98	73	31	15	46	461	0.4
2005	18	43	39	21	43	40	104	72	36	17	48	481	4.2
2006	19	47	35	25	45	41	111	67	32	17	54	492	2.4
Food Processing Sic 15.1 - 15.8													
1998	15	62	55	53	33	45	24	30	41	21	32	410	
1999	15	63	55	58	34	43	26	28	39	19	33	413	0.7
2000	16	60	53	56	33	41	26	28	37	21	32	403	-2.4
2001	15	56	52	56	31	39	24	27	34	21	31	387	-4.0
2002	15	54	52	54	31	37	24	24	33	21	30	375	-3.1
2003	15	56	51	53	31	37	24	21	32	21	29	369	-1.5
2004	13	54	47	51	29	35	24	20	31	21	28	355	-4.0
2005	12	51	46	50	30	34	24	20	31	21	27	347	-2.1
2006	14	50	44	48	30	32	23	19	32	21	26	340	-2.2
Hairdressing Sic 93.02, 93.04													
1996	4	10	7	7	9	10	13	16	8	5	9	98	
1997	4	10	7	6	8	10	15	16	8	4	8	97	-1.0
1998	5	10	7	6	9	9	14	15	8	4	9	95	-1.8
1999	5	12	7	6	9	10	15	16	9	4	9	102	6.8
2000	4	12	7	6	9	10	15	17	9	5	9	103	0.9
2001	4	11	7	6	9	10	15	17	8	4	9	100	-2.5
2002	4	13	8	7	8	10	13	15	8	4	9	101	1.3
2003	5	13	8	7	10	11	14	18	8	4	10	108	6.1
2004	5	14	8	8	9	10	15	17	9	5	10	111	2.9
2005	5	13	10	9	10	11	14	19	9	5	11	117	5.8
2006	5	14	9	9	11	11	17	20	11	5	11	123	5.0

	North East	North West	Yorkshire & Humber	East Midlands	West Midlands	Eastern	London	South East	South West	Wales	Scotland	Great Britain	Y/Y*
Hospitality Sic 55													
1998	60	188	133	99	130	126	245	208	149	70	156	1564	
1999	66	182	129	100	134	126	273	224	143	77	151	1606	2.7
2000	59	176	128	100	129	135	265	232	149	67	165	1605	0.0
2001	63	187	127	103	134	136	275	229	159	75	168	1656	3.2
2002	63	202	129	105	136	138	289	243	164	69	169	1708	3.1
2003	63	207	130	106	133	141	299	245	173	73	168	1737	1.7
2004	63	204	142	107	147	144	289	256	172	81	173	1777	2.3
2005	70	204	137	112	146	134	300	254	169	81	174	1781	0.2
2006	70	210	137	108	158	144	285	241	176	82	176	1786	0.3
Leisure Sic 92.13, 92.3, 92.6, 92.7													
1998	17	46	33	24	30	37	77	60	30	18	40	411	
1999	18	47	34	27	35	42	88	64	33	20	42	450	9.6
2000	18	51	39	31	35	43	86	73	34	21	43	473	5.1
2001	17	52	40	31	39	44	98	79	37	20	45	502	6.1
2002	21	57	41	34	39	48	93	78	39	21	49	521	3.8
2003	23	56	42	32	40	48	87	80	39	21	49	516	-1.0
2004	22	60	44	33	41	46	92	78	40	24	49	530	2.7
2005	25	59	46	36	43	49	89	81	38	23	50	539	1.7
2006	23	60	46	35	48	47	91	77	39	26	52	544	0.9
Retail Sic 50,52													
1998	125	379	280	221	285	317	406	473	287	143	279	3195	
1999	128	387	262	211	282	295	439	484	291	137	278	3194	0.0
2000	128	387	284	224	292	325	431	502	303	145	280	3302	3.4
2001	126	401	290	235	304	331	440	529	310	154	306	3426	3.8
2002	134	402	302	236	305	344	435	531	325	159	306	3479	1.6
2003	134	408	307	246	304	353	424	521	333	160	304	3493	0.4
2004	136	419	317	260	318	351	423	519	335	166	297	3541	1.4
2005	136	405	301	252	311	353	426	519	327	169	298	3498	-1.2
2006	132	384	290	236	294	337	411	478	308	161	282	3314	-5.3
Security Sic 74.6													
1998	5	16	13	8	9	7	31	17	7	4	10	128	
1999	6	17	11	8	9	7	34	18	6	4	12	133	3.7
2000	6	17	10	7	8	9	33	17	6	4	13	132	-0.7
2001	7	18	9	8	10	10	39	18	8	5	14	146	10.5
2002	6	20	11	11	11	10	39	20	9	5	12	152	4.3
2003	7	20	11	10	11	12	40	19	9	5	13	156	2.4
2004	6	21	12	10	11	13	38	19	13	5	14	162	3.9
2005	6	20	12	12	11	12	39	21	12	6	16	165	2.1
2006	5	21	13	12	10	14	41	20	11	4	16	165	0.1
Social Care 85.31													
1998	19	55	38	30	36	40	42	64	45	19	34	421	
1999	22	57	41	31	38	40	40	67	44	20	33	433	2.9
2000	22	58	38	32	38	44	41	68	45	21	36	443	2.3
2001	22	57	41	34	38	48	41	69	47	21	37	455	2.6
2002	23	58	41	32	38	46	41	67	47	22	40	455	-0.1
2003	24	59	43	34	40	48	41	67	46	22	40	463	1.8
2004	23	59	43	36	43	49	43	68	49	22	41	477	3.1
2005	24	61	43	37	44	49	45	73	51	23	44	494	3.6
2006	23	57	43	35	43	49	43	72	51	25	43	484	-2.0
Textiles and Clothing Sic 17,18													
1998	15	58	42	71	23	9	22	7	10	11	32	299	
1999	12	51	36	60	20	8	21	7	10	9	29	263	-12.2
2000	9	50	33	53	17	7	17	6	7	7	22	227	-13.4
2001	8	41	29	43	15	7	14	5	8	7	19	194	-14.6
2002	6	37	24	33	13	6	12	5	7	6	17	165	-14.8
2003	5	32	21	28	11	6	11	4	7	5	14	145	-12.4
2004	4	29	18	25	9	6	10	4	6	4	13	127	-12.2
2005	3	24	17	20	8	5	10	4	6	4	11	112	-12.1
2006	3	22	15	18	6	4	8	3	5	4	10	98	-12.2

Source: 1998-2006 Annual Business Inquiry. ONS. Y/Y shows percentage change of total regional employment from previous year.

ANNEX D International comparison of minimum wage rates

Table D1. Current adult national minimum wage rates

	In National Currency expressed as hourly rate ¹	In UK £, using Exchange rates ²	Using PPPs ³	NMW as percentage of median earnings ⁴	Date of last uprating
Australia	AUS \$13.41	5.87	6.67	53.6	Oct-08
Belgium	€ 8.00	6.31	5.95	43.2	May-08
Canada ⁵	Can \$8.42	4.28	4.64	39.6	(⁶)
France	€ 8.71	6.87	6.39	60.8	Jun-08
Greece	€ 3.92	3.09	3.68	45.1	Jan-08
Ireland	€ 8.65	6.82	5.81	35.0	Jul-07
Japan ⁷	¥618-739	3.99-4.67	3.42-4.09	32.2	Oct-08
Netherlands	€ 7.70	6.07	5.79	51.0	Jan-08
New Zealand	NZ \$12	4.33	5.17	46.4	Apr-08
Portugal	€ 2.71	2.14	2.59	43.2	Jan-08
Spain	€ 3.46	2.73	3.10	25.6	Jan-08
United Kingdom	£5.73	5.73	5.73	47.0	Oct-08
United States	\$6.55	4.06	4.36	30.8	Jul-07
G7 average ^{8,9}		5.05	4.97	42.1	

1. For countries where the minimum wage is not expressed as an hourly rate, the rate has been converted to an hourly basis assuming a working time of 8 hours per day, 40 hours per week and 173.3 hours per month.

2. Exchange rates as of October 2008.

3. Purchasing Power Parities (PPPs) from OECD, 2007

4. Median earnings data are estimates based on extrapolating data for earlier years in line with trend in average earnings.

5. Average of minimum wage rates in 12 provinces.

6. Date of uprating varies between provinces.

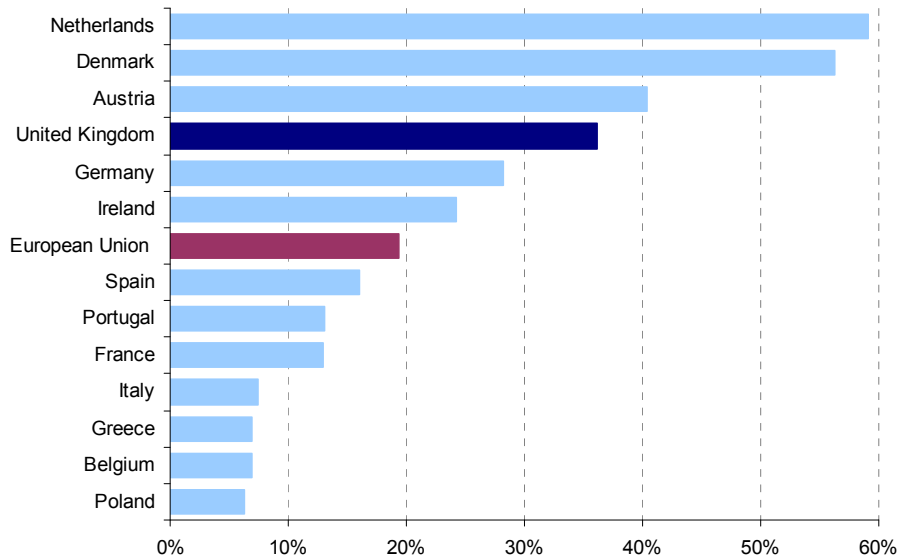
7. National Minimum wage varies according to industry and region.

8. Average of G7 countries that have minimum wage rates - excludes Germany and Italy

9. For Japan, the mid-point of the range is used.

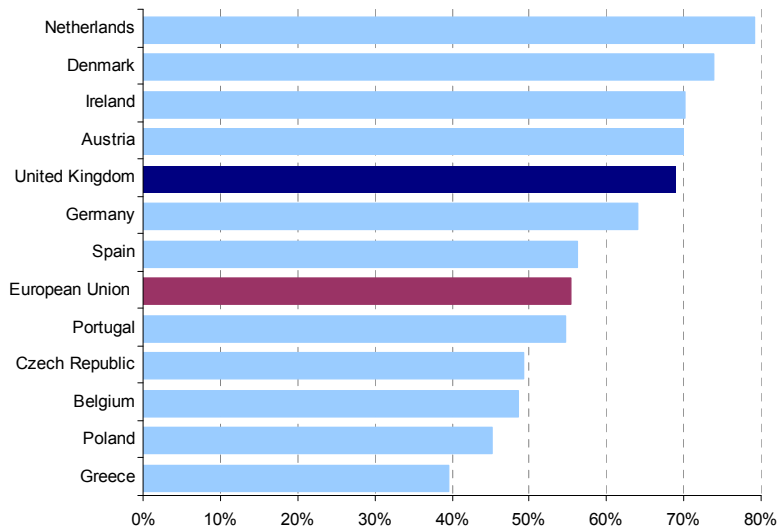
ANNEX E European employment and unemployment rates

Chart E1. Employment rate 16-19 year olds, average of 4 quarters to Q2 2008



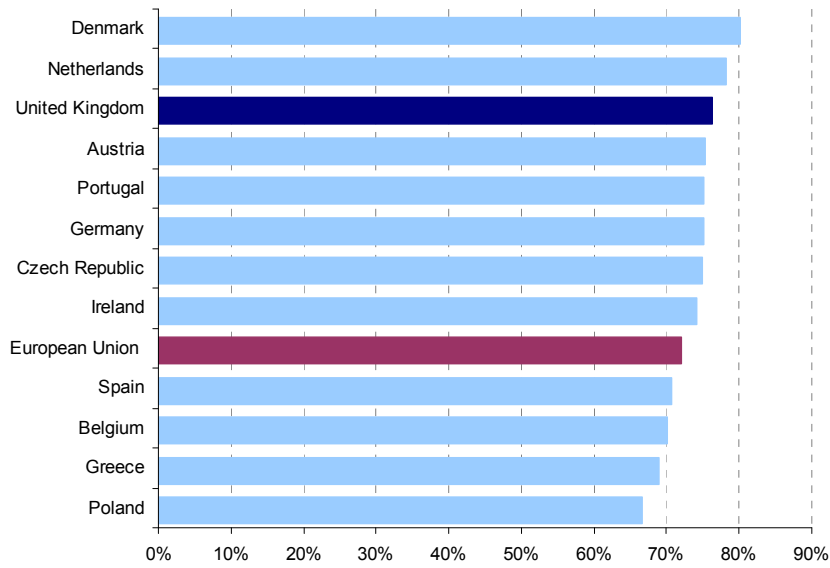
Source: Eurostat
Germany rate for Q1 2005

Chart E2. Employment rate for 20-24 year olds, average of 4 quarters to Q2 2008



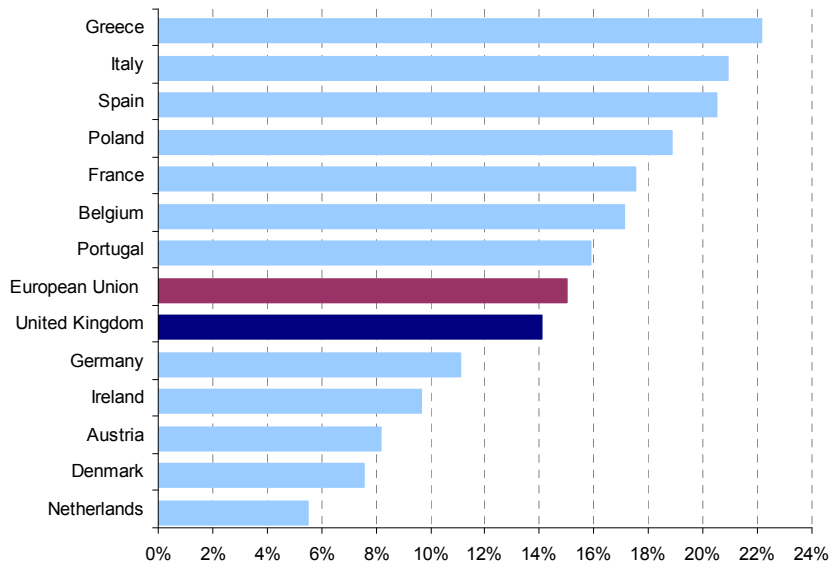
Source: Eurostat

Chart E3. Employment rate for 25-64 year olds, average of 4 quarters to Q2 2008



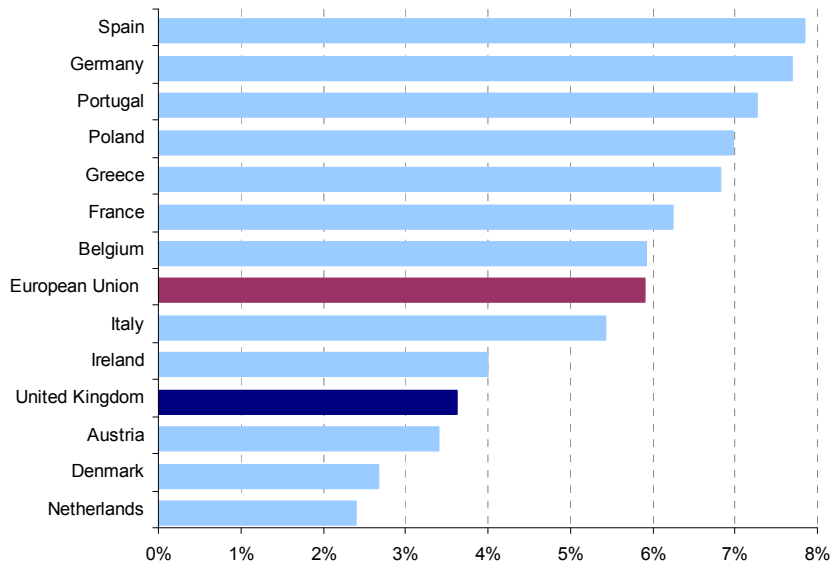
Source: Eurostat

Chart E4. Unemployment rate for 15-24 year olds, average of 4 quarters to Q2 2008



Source: Eurostat

Chart E5. Unemployment rate for 25-64 year olds, average of 4 quarters to Q2 2008



Source: Eurostat

ANNEX F Review of recent minimum wage research

This short review summarises the recent empirical analysis of the labour market impacts of minimum wages. It focuses on UK research but also highlights some international, particularly US, evidence. For completeness this overview considers the recent literature which has been commissioned by the LPC. The evidence presented so far has been in the context of a growing labour market. There is less evidence, from both the UK and internationally, of the impact of minimum wages in periods of economic downturn.

Employment effects

There are three broad approaches to analysing the impact of minimum wages on employment using:

- **Individual-level longitudinal data to estimate the impact on individual employment and hours worked.** For example, Stewart (2004a and 2004b) compared the employment experience of individual workers affected with those not affected by the minimum wage. He found little evidence that the introduction of the National Minimum Wage, or the 2000 and 2001 upratings, had an adverse impact on the probability of employment. Dickens and Draca (2005) considered the 2003 uprating, finding insignificant disemployment effects. Similarly, Mulheirn (2008) looked at the 2006 uprating and found no evidence of an adverse employment impact and also found a positive effect on job retention for males from the uprating. Alternatively, Robinson and Wadsworth (2007) investigated the impact of the minimum wage on the incidence of second job holding in Britain. Their results suggest there is little evidence that the extra pay provided by the introduction of the NMW and its subsequent upratings was sufficient to affect the incidence of second job holdings. Jones et al (2006) found that increases in the exit rate from employment, as measured by ASHE, was actually less for the low-paid than the high paid.
- **Spatial data to explore whether employment declined more in areas with a high proportion of low-wage jobs.** Stewart (2002) analysed employment changes across 140 areas for the period straddling the introduction of the NMW. Stewart's estimates show no or negative impacts on employment (for example, a 5 per cent rise in the wages for the 5th and 10th percentile was reflected in a 2 per cent reduction in employment), but the latter was not statistically significant. However, Galindo-Rueda and Pereira (2004) did find that the net growth in employment was slightly less in areas with a relatively high proportion of workers affected by the NMW. While Experian's (2006) study of the relationship between the NMW bite and regional employment found no association for retail, there was a small negative impact on employment in the hospitality sector from the 2003 and 2004 upratings.

- ***Using firm level data to examine whether or not employment fell relatively more in those workplaces with a high proportion of low paid individuals.*** Kersley et al (2004) used the Workplace Employment Relations Survey to find no difference in closure rates between low-paying and other workforces, and low-paying workplaces were less likely to experience a fall in employment of over 25 per cent. Draca et al (2006) also found no correlation between the introduction of the NMW and closures, although they found a fall in profit margins. However, a number of studies of the care home sector have found employment effects. Machin and Wilson (2004) found that those firms affected by the NMW were likely to suffer relative employment falls: for example, a 10 per cent increase in the proportion initially paid below the NMW was associated with 1.3 per cent lower employment growth. There is also evidence of a negative effect on hours.

Overall, while evidence is mixed, there is a lack of strong evidence of negative employment consequences from the introduction and subsequent upratings of the adult National Minimum Wage. However, Neumark and Wascher (2007) argue that the evidence for the UK is not unambiguous. In particular, the existing UK research is limited to estimating short-term effects and there may be longer-term impacts of the minimum wage. In addition, the employment effects of the relatively larger rise in the minimum wage from 2003 to 2006 have not yet been sufficiently studied. Also since the introduction of the NMW the UK has yet to experience an economic downturn. A report by the Income Data Service (2006) studied the UK labour market in the last recession and found that the impacts on low paying sectors were minimal and that the level of employees in hospitality and retail remained relatively stable over this time period. It should be noted past performance does not necessarily reflect future performance and in previous recessions the UK did not have a NMW.

Indeed there are a much wider range of estimates of the effects of minimum wages on employment in the US. In particular, longer panel studies that incorporate both state and time variation in minimum wages tend to find statistically significant employment effects from minimum wage increases. In contrast, the majority of US studies that found zero or positive effects of the minimum wage on low-skill employment were either short panel data studies or sector-specific case studies (Neumark and Wascher, 2007). One exception to this was a paper by Lutterman (2007) who studied the 1990/91 increase in the federal minimum wage. By estimating the wage corresponding to a constant skill level change over time and using this information to infer each worker's skill from actual wage paid to this individual. Lutterman evidence showed the increase in minimum wage reduced the employment among unskilled workers, however their employment reduction seems largely compensated for by increased employment among the next skill group, which is likely to be a close substitute.

Effects on hours worked

Employers in low-paying sectors may alter hours rather than levels of employment in response to minimum wages.²⁴ Therefore, it is important to look at the impact on hours worked to understand the impact of the minimum wage on the labour market.

There is some evidence that introduction of the UK National Minimum Wage may have led to a reduction of working hours, particularly over the longer-term. For example, Stewart and Swaffield (2006) found a small but insignificant effect of the minimum wage on hours worked in the UK. However, the lagged effect of the minimum wage on hours is always negative, larger in value and generally statistically significant. The study concludes that the introduction of the minimum wage led to the reduction of one to two hours per week for affected workers. Couch and Wittenburg (2001) found that raising the minimum wage reduced the hours of work of teenagers in the US. As a result, they argue that estimates of the elasticity of teen labour demand with respect to the minimum wage based on employment data consistently understate the effect of minimum wage increases on labour utilisation by 10 per cent to 30 per cent.

Effects on wage distribution

The bottom quarter of the earnings distribution has experienced faster growth than the median since the introduction of the minimum wage, with these increases being greater for those who were lowest paid (Butcher, 2005 and OECD, 2006). This implies an upward 'ripple effect' from the National Minimum Wage within the bottom part of the wage distribution. Lam et al (2006) showed that wages for jobs near the minimum level have moved closely with the minimum wage, maintaining differentials. Other studies have found no strong evidence of ripple effects when the NMW was introduced in 1999 or uprated 2000-02 (Dickens and Manning 2004a, 2004b; Dickens and Draca 2005). However, there is evidence of such effects from the 2003 uprating onwards (Butcher 2005 and Dickens and Manning 2006).

However, as these ripple effects dissipate as they move up the wage distribution, there has also been compression with the average and median wage. Metcalf (2004) found that workers in the bottom decile of pay experienced above average pay rises between 1998 and 2002, with no effects further up the wage distribution. Cameron and Fernandez (2007) find that the difference between the low paid and the average paid (whether mean or median) has been compressed. However, the upper part of the income distribution has been pulling away from the middle at the same time as the lower part has been compressing the middle.

This is an area where further research is needed. Lam et al (2006) suggest that more analysis of small firms is needed, as a number of low paying sectors are dominated by very small firms, where the impact of small pay changes may be large.

²⁴ This is because low-pay sectors have low fixed cost per worker, little on-the-job training, high labour turnover, limits to the substitution of capital for labour and a high incidence of part-time work (OECD 2006).

Effects on younger workers

The academic evidence for the impacts of minimum wages on the young are a little more mixed, with somewhat more evidence for disemployment effects than is the case with adults.

Neathey, Ritchie and Silverman (2005) found little evidence in the retail and hospitality sectors of a link between the minimum wage and decisions to employ young workers of various ages. However, Frayne and Goodman (2005) found that every 1 per cent increase in the 16–17 year old wage resulted in a 3.6 per cent decrease in employment in hours amongst this group, implying that a minimum wage of £3.00 would reduce employment in hours by around 6 per cent.

Several international studies have found evidence that minimum wages can have disemployment effects on the young. Campolieti, Fang and Gunderson (2005) found minimum wage elasticities ranging from -0.3 to -0.5 . Wessels (2005) found significant negative effects on teenager labour force participation for 16-19 year olds in the US.

Dickerson and Jones (2004) found that a minimum wage set between £2.50 and £4.00 will have negligible effects on education participation of 16-17 year olds. However, Rice (2006) finds that the probability of continued participation of young men in full-time education declines significantly as the expected wage increases, although the effects for young women are smaller and not statistically significant. Based on this analysis, Rice (2006) suggests that the impact of 'a cautiously set' minimum wage for 16 and 17 year olds on educational and employment outcomes is likely to be small. A NMW set at a level corresponding to the lowest decile of the observed distribution of actual earnings would reduce the expected participation rate in full-time further education among young males by no more than 1 percentage point. A more generous NMW set at the equivalent of the lower quartile would result in a decline of between 1 and 2.4 percentage points depending on the extent of the spillover effects on the overall distribution of wage offers.

Effects on profitability and prices

The impact of the minimum wage on employment will be muted the greater the extent to which the rise in labour costs is passed on in the form of higher prices or absorbed in a fall in profits.

The impact on overall inflation of the NMW is likely to be small, as the NMW only applies to a relatively small proportion of total jobs. However, there is some evidence of increases in the relative prices of goods and services produced by minimum wage workers. Wadsworth (2007) found prices rose, on average, by an extra 0.8 per cent a year relative to the RPI after the NMW was introduced. Wadsworth (2007) also found that there was considerable variation in the inflation rate movement of individual minimum wage goods, as identified by Wadsworth. Hotels for example experienced a 2 per cent raise above general inflation, while the price of pub drinks followed the general price inflation.

There is also some limited evidence that the initial introduction of the NMW caused a relative fall in profits in the more affected firms. Draca et al. (2006) found that average profit margins fell for those most affected by the National

Minimum Wage by 8 per cent to 11 per cent, compared to the control group of higher-wage firms. Their analysis of a sample of care homes also shows that those that had to raise their wages the most experienced the biggest drop in profits. In a follow-up study, Georgiadis (2006) found a negative association between homes with a larger fraction of affected workers and profitability, but it was not statistically significant. Experian (2006) found that relative gross operating surplus in the retail and hospitality sectors between 1999 and 2004 was lower in regions where the bite of the NMW was strongest but again the association was not statistically significant.

Effects on small firms

The Department for Business Enterprise and Regulatory Reform previously conducted an annual small business survey between 2004 and 2006, in which they asked 9,000 small and medium enterprises (SMEs) views on a host of issues including obstacles to achieving business success. Around 20 per cent of respondents see regulation as the main barrier to business success, of these respondents only a minority (about 2 per cent) felt that the NMW was the main regulatory barrier. Further, from 2004 – 2006 the number of respondents who felt the NMW was the main barrier of business success has fallen from 3.6 per cent in 2004 to 1.4 per cent in 2006, this is a fall of 2.2 percentage points. Mason et al (2006) uses the biennial membership survey of the Federation of Small Businesses and finds that the NMW has had a limited effect on small business.

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ANNEX G Beneficiaries of the 2008 NMW uprating by sex and region

Table G.1. Number of workers that stand to benefit from the October 2008 National Minimum Wage uprating by age and sex

	Male	Female	Total
16-17	16	13	29
18-21	64	48	111
22 and over	332	663	985
Total	402	724	1,125

Source Office for National Statistics, Annual Survey of Hours and Earnings

These data take account average earnings growth between the period April 2008 and September 2008; uprating from £3.40 to £3.53 for 16-17 year olds, £4.60 to £4.77 for 18- 21 year olds and from £5.52 to £5.73 for those 22 and over. ASHE measures number of jobs; therefore beneficiaries calculated assuming workers do not hold more than one job at the NMW. Numbers may not sum to total due to rounding.

Estimates of beneficiaries by country and government office region are also provided (Table G.2).

Table G.2. Number of workers that stand to benefit from the October 2008 National Minimum Wage uprating by country and government office region

Country or region	Beneficiaries
Wales	66
Scotland	102
Northern Ireland	51
England	906
North-East	64
North-West and Merseyside	132
Yorkshire & Humberside	108
East Midlands	93
West Midlands	127
Eastern	105
London	87
South East	111
South West	79
United Kingdom	1,125

Source Office for National Statistics, Annual Survey of Hours and Earnings

These data take account average earnings growth between the period April 2008 and September 2008; uprating from £3.40 to £3.53 for 16-17 year olds, £4.60 to £4.77 for 18- 21 year olds and from £5.52 to £5.73 for those 22 and over. ASHE measures number of jobs; therefore beneficiaries calculated assuming workers do not hold more than one job at the NMW. Numbers may not sum to total due to rounding.

ANNEX H Technical note

Annual Survey of Hours and Earnings (ASHE)

The Annual Survey of Hours and Earnings (ASHE) provides information about the levels, distribution and make-up of earnings and hours paid for employees within industries, occupations and regions.

In this report, estimates for 2004-2008 have been produced using ASHE, which replaced the New Earnings Survey (NES) in 2004. ASHE improves on the NES by extending the coverage of the survey sample and introducing weighting.

From 1997-2003, estimates are based on NES datasets that have been reworked using ASHE methodology. However, these datasets exclude the supplementary ASHE information and as a result there is an inconsistency between estimates in 2003 and 2004.

A further break in the data was also introduced in 2006 when ONS introduced a small number of methodological changes, including changes to the sample design itself as well as the introduction of an automatic occupation coding tool.

To identify these changes, ONS publish two estimates for both 2004 and 2006 – one on the new methodology and one based on the previous methodology. Where appropriate these inconsistencies are identified in this report.

Labour Force Survey (LFS)

In May 2008 the structure of the Labour Force Survey switched from a seasonal quarter basis to a calendar quarter basis on all quarterly data back to 1992. The ONS also brought in new weights for all data back to 1992 based on new information.

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