Low Pay Commission

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The Rt Hon Vince Cable MP
Secretary of State for Business, Innovation and Skills
1 Victoria Street
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Dear Secretary of State,

THE 2014 RATE AND THE FUTURE PATH OF THE NATIONAL MINIMUM WAGE

I enclose the 2014 Report of the Low Pay Commission.

At the end of September you asked us to take a longer-term view of the minimum wage and the conditions that need to be in place in order to allow a faster increase, taking into account the implications for employment. Our report includes a chapter on this, which we are also submitting separately.

The minimum wage has shown its worth during the economic slowdown. It has continued to rise faster than median earnings since the onset of recession in 2008, thus increasing the relative pay of the lowest paid. This is quite different from what has happened in earlier recessions going back at least to the 1970s, when the pay of those at the bottom tended to fall behind that of other people.

The wages of the lowest paid are now higher relative to those of other workers than they have been for decades. However during the slowdown the real value of the minimum wage has fallen, even though the minimum wage has risen faster than other wages, because both it and average wages have been exceeded by inflation. We regret that, but it has been unavoidable if the jobs of the low paid were not to be put at risk.

An abrupt increase in the minimum wage at this early stage of the recovery would indeed we believe put employment at risk, particularly bearing in mind the pressure of the minimum wage in low-paying sectors and small firms. The bite – the minimum wage as a proportion of median wages – has continued to rise in recent years and is now at or near its highest level ever.

We do believe however that the economic recovery should this year allow an increase in the real value of the minimum wage, the first increase for at least five years. So we are recommending that the adult rate should increase by 3.0 per cent on 1 October, compared to the consensus CPI forecast of 2.3 per cent. This is likely to increase the number of jobs covered by the minimum wage by over a third to around one and a quarter million.

Provided the economy continues to improve we expect to recommend further progressive real increases in the value of the minimum wage, restoring and then surpassing its previous highest level, so that 2014 will mark the start of a new phase – of bigger increases than in recent years – in the work of the Commission.

Our response to your letter discusses in detail the conditions that will be needed for this to be achieved.

We share the generally held view that a sustained increase in real wages depends on increased productivity: for wage increases to be sustainable they must be affordable, which generally requires an increase in overall output per head. We shall need, as in the past, to base our assessments on the prospects for wages generally (both as a guide to changes in productivity in the economy and for the relationship between the minimum wage and other wage levels), on the outlook for employment, particularly in low-paying sectors and small firms, and on expectations for economic growth. We will also continue to be influenced by what we learn from meetings with employers and employees in all parts of the UK and by the oral and written evidence we receive.

To achieve our shared aim of faster increases in the minimum wage without risk to the employment of the low paid, we believe it would be necessary to see rising real wages in the economy more generally; stable or rising employment, particularly in low-paying industries and small firms; and an expectation of sustained economic growth.

Our response to your letter discusses, as you asked, the effects of government policies. This could be a huge undertaking and we have had to work within the limits of our knowledge and the time available. The essential conclusion of course is that government measures to reduce employer costs increase the scope for higher pay, and the opposite. But for the purposes of the minimum wage the effects of government policy are often felt more at a sectoral level. Local authority spending on social care and regulation in many industries are cases in point.

Government can also have a substantial impact in the way that it can encourage and support training and education and other methods to increase productivity in low-paying industries, recognising that higher productivity is in the longer term the only real answer to low pay.

We have also considered the effects of tax and national insurance, as you asked, and this is discussed in the report. We do not take impacts on take-home pay into account: they do not affect employer affordability and ability to pay. We do on the other hand consider the effects of particular government policies on business, as an important element, but one among many, in the financial position of employers.

I would note finally that around a quarter of minimum wage workers are not employed in the low-paying sectors. Many employers may be able to raise their wages without damage to their businesses. We welcome the current pressures on such employers to raise the pay of the lowest paid.

I am copying this letter to the Prime Minister and Deputy Prime Minister.

Yours sincerely

David Norgrove

David Norgrove

Chairman
Low Pay Commission