National Minimum Wage

Low Pay Commission

National Minimum Wage

Low Pay
Commission Report
2024

National Minimum Wage Low Pay Commission Report 2024

Presented to Parliament
by the Secretary of State for Business and Trade
by Command of His Majesty

February 2025

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Introduction

1 We, the Low Pay Commission (LPC), are the independent body that advises the Government on the levels of the National Minimum Wage (NMW), including the National Living Wage (NLW). This report – our 26th – provides the evidence and rationale behind our recommendations that apply from 1 April 2025. We submitted our recommendations to the Government on Friday 25 October. Our recommendations were informed by evidence available up to Thursday 24 October, so this report does not include any data or forecasts available after this point. The Government announced its acceptance of our recommendations on Tuesday 29 October, the day before the Autumn Budget.

2 Our recommendations reflect a consensus between all members of the Commission, including representatives of workers, employers, and labour market experts, reached through careful consideration and discussion of the available evidence. However, this task was made more difficult this year by the fact that only two of the three worker Commissioners were in post at the time when we agreed our recommendations. This is the second consecutive year that this has happened, as the position has been vacant since the beginning of 2023. We urge the Government to ensure that this does not happen again.

3 The July 2024 General Election heralded a new Government, and with it, a new remit for the LPC, published on 30 July (Department for Business and Trade, 2024a). For the NLW, there were three parts to our remit. We were asked to ensure that the NLW did not fall below two-thirds of median hourly earnings; to take account of the cost of living, including inflation to March 2026; and to take account of the impacts on businesses and the wider economy. The focus on living costs is new for our remit and is part of the new Government's plans to make work pay and deliver a genuine living wage. We explore the relationship between the minimum wage and living costs in Chapter 4, describe how we accounted for future inflation in Chapter 10, and explain the impact this had on our recommendations in Chapter 11.

4 The Government has said it is determined to deliver a "genuine living wage" for all adults. This means that the 18-20 Year Old Rate will be removed. We were asked to narrow the gap between the 18-20 Year Old Rate and the NLW, "taking steps year by year in order to achieve a single adult rate". In recommending the 18-20 Year Old Rate for 2025, we were also asked to take account of the effects on employment of younger workers, incentives for them to remain in training or education, and the wider economy. For the 16-17 Year Old Rate and Apprentice Rate, we were asked to lift the rates as high as possible without damaging employment.

5 Issues with the evidence base made our job more difficult this year. Last year we noted the problems with the Labour Force Survey (LFS), a key evidence source on the labour market. While the survey's response rate has begun to improve, there is still some way to go to match previous levels. The poor response rate seems to particularly affect young people and those with low incomes, which is a problem for informing our work. We urge the Government to support the Office for National Statistics' (ONS) efforts to improve the LFS. We also extend our thanks to HM Revenue and Customs (HMRC) for providing additional data that helped to fill gaps in our understanding of the current state of the labour market. Going forward, we will continue to work with HMRC for better and more timely access to its Real Time Information (RTI) data. This report makes further detailed recommendations on this matter.

6 A few weeks before we were due to provide advice to the Government, the ONS told us it was changing the methodology for the Annual Survey of Hours and Earnings (ASHE), the key data source for information on pay. Its rationale was that the ASHE appears to undercount workers with very high pay, making it inconsistent with other sources. The ONS changed its method such that cases (i.e. individual workers) who had previously been excluded because their pay was deemed unusual, and therefore erroneous, would now be included.

7 This change meant that the published estimate of median hourly pay in April 2023 was revised up, and the April 2024 median was significantly higher than we had anticipated. As our remit has linked our recommendations on the NLW to the median since 2016, this had a direct impact on our recommendations. We explain this in Chapter 10.

8 It is entirely right for the ONS to strive for accuracy, and we understand the rationale for this change. That said, we note that the ONS also intends to review the ASHE methodology over the coming year and so may make further changes. This raises the question as to why these changes have been introduced before the methodological review is complete. With further methodological changes due shortly, the picture will likely change further, again adding to the uncertainty. We recommend that the ONS work with all who use ASHE to inform policy decisions across Government, so they have sufficient notice of further methodological changes and to agree the most appropriate time to make these changes. We also make several other recommendations about the evidence base, without improvements to which our ability to give the Government the best advice is compromised.

9 It should be noted that a large part of our evidence-gathering took place before the General Election on 4 July and the Government's publication of an updated remit on 30 July. Many of the submissions we received and the discussions we had with stakeholders took place on the basis of a different remit, published by the previous Government in March. However, we continued to meet with stakeholders from July onwards, and indeed our discussions from 22 May onwards (when the election date was announced) were held in the knowledge of the approaching election and the possibility of a change to our remit.

10 We received 63 written consultation responses and met with more than 100 businesses, unions, workers and other bodies across the UK. As ever, we are grateful to all those groups and individuals who contributed to this year's evidence-gathering process. Appendix 1 lists those stakeholders who responded to our consultation and whom we met over the year, and who agreed to be listed.

11 This report is structured as follows:

- Chapter 1 sets out the state of the UK economy based on the data available at the time we made our recommendations.
- Chapter 2 considers recent developments in the labour market.
- Chapter 3 looks in more detail at who NLW and NMW workers are and their experiences in and out of the workplace.

- Chapter 4 explores various measures of living standards, particularly those for low-income households, and their relationship to the minimum wage.
- Chapter 5 looks at the strength of the labour market for workers eligible for the NLW.
- Chapters 6 and 7 do the same as Chapter 4, but for younger workers affected by the age rates of the NMW and apprentices respectively.
- Chapter 8 then looks at other ways employers have responded to the rising minimum wage, including through raising prices.
- Chapter 9 considers the workings of the minimum wage, including the Accommodation Offset and certain aspects of compliance and enforcement.
- Chapter 10 discusses the path of the NLW to 2025, how we have taken account of future inflation, stakeholder views on the prospective NLW rate, and potential approaches to reducing the NLW age to 18.
- Chapter 11 sets out our recommendations and their rationale.

The Commissioners

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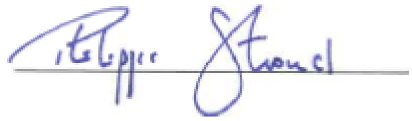

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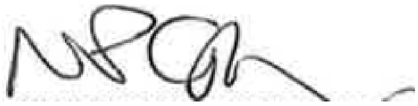

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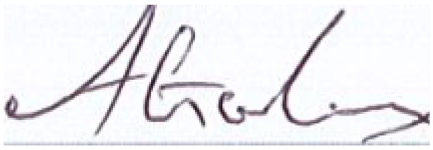

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The Government's remit to the Low Pay Commission

The text below is reproduced from the Government's remit for the Low Pay Commission in 2024 (Department for Business and Trade, 2024a)

The government is committed to making work pay and protecting the lowest earners in our society. The National Minimum Wage was introduced in April 1999, and has been one of the most successful economic policy interventions over the last quarter of a century. Despite recent increases to the minimum wage rates, working people have faced the brunt of an unprecedented cost of living challenge. It is therefore more important than ever that we protect and boost low earnings, whilst maintaining competitiveness and protecting the UK's economy as a whole.

National Living Wage and National Minimum Wage Rates

The government is determined to deliver a genuine living wage, backed by evidence and consistent with delivering inclusive growth for working people and competitive businesses across the UK. We ask the Low Pay Commission to recommend a National Living Wage which should apply from April 2025. This should take into account the impact on business, competitiveness, the labour market, the wider economy and the cost of living, including the expected annual trends in inflation between now and March 2026. The Low Pay Commission should ensure that the rate does not drop below two-thirds of UK median earnings for workers aged 21 and over, a recognised measure of low hourly pay.

The government is committed to ensuring that every adult worker benefits from this genuine living wage, and we will remove discriminatory age bands for adults. In the interim, we ask that the Low Pay Commission recommends a National Minimum Wage rate that should apply to 18 to 20-year-olds from April 2025. This should continue to narrow the gap with the National Living Wage, taking steps year by year in order to achieve a single adult rate. This ambition should be pursued while also taking into account the effects on employment of younger workers, incentives for them to remain in training or education and the wider economy.

The government also asks the Low Pay Commission to monitor and evaluate the levels of the other National Minimum Wage rates (under 18 and apprentice rates) and make recommendations on the increases it believes should apply from April 2025 so that the rates are set as high as possible without damaging the employment prospects of each group.

In addition, we ask the Low Pay Commission to recommend the accommodation offset rate that should apply from April 2025.

The government notes that the Low Pay Commission will continue to expand its evaluation capabilities and commission minimum wage research from leading experts, using new methods and sources of evidence for its assessment of the impact of the National Living Wage.

To further expand the evidence base, the government asks the Low Pay Commission to continue to gather particular evidence on groups of low paid workers with protected characteristics.

Additionally, we ask the Low Pay Commission to continue to gather evidence on the differing impact across the United Kingdom of increases to the minimum wage rates, to inform how the minimum wage helps to deliver greater prosperity and living standards for working people in all areas of the UK.

Timing

The Low Pay Commission is asked to provide a final report in response to this remit to the Prime Minister and the Secretary of State for Business and Trade by the end of October 2024.

Executive Summary

1 The task of the Low Pay Commission (LPC) is to advise the Government on the levels of the National Minimum Wage (NMW), including the National Living Wage (NLW). This report, our 26th, contains the evidence and rationale for our recommendations to apply from April 2025. We met to agree our recommendations on 23-25 October 2024 and so only consider evidence available up to that point throughout this report. We provided our advice to the Government before the Budget on 30 October.

2 To inform our recommendations we consider the state of the economy and labour market, the cost of living and the level of pay relative to two-thirds of median hourly pay, which is the international benchmark for "low pay". Our work has been made more difficult this year by the ongoing issues with the Labour Force Survey (LFS) and changes to the methodology of the Annual Survey of Hours and Earnings (ASHE) – our key source for pay data.

The economy and labour market

3 GDP growth, while improved, is still fairly weak by historic and international standards and productivity growth remains subdued. In October 2023, when we made our recommendations for April 2024, the economy was expected to grow weakly in 2024 (around 0.4 per cent). However, growth in the first half of the year comfortably beat these projections. This led forecasters to more than double their growth estimates for 2024 as a whole. They also expect growth to be higher still in 2025.

4 Despite this improved macroeconomic picture, the labour market has continued to loosen, with vacancies falling for the last two years and nominal earnings growth coming down from its high point in summer 2023. However, we believe this largely reflects an unwinding of exceptionally strong recruitment post-pandemic. Levels of vacancies and the vacancy rate are still at or above those in 2019, which itself was a period of tight labour markets where both measures were at or close to historic highs. Forecasters expect unemployment to remain at historically low levels, albeit increasing slightly. Pay growth slowed over 2024 but remained higher than was forecast (in October 2023) at 4-5 per cent. Falling inflation resulted in real-terms wage rises for workers, something that is expected to continue for the next 18 months.

5 The low-paid labour market is in a similar position. April 2024 saw a second successive major increase in the NLW, and the share of jobs covered by the NLW increased meaningfully for the first time since it was introduced in 2016. Coverage of all minimum wage rates increased this year to 1.91 million but remains below pre-pandemic levels as a share of all eligible jobs.

6 At first glance, this suggests a loosening of the low-paid labour market. But the coverage share (the share of eligible jobs paid the NLW) remained below pre-pandemic levels, despite an increase due to 21-22 year olds who became entitled to the NLW from April this year. The rate at which NLW workers moved into higher-paying employment, and the wage premium for doing so, both fell, but, again, remained above pre-pandemic levels. This suggests that the low-paid labour market has loosened to an extent but remains robust.

The National Living Wage

7 The robustness of the low-paid labour market does not mean that employers, especially small businesses, found it easy to respond to the large NLW increase. Employers in low-paying sectors were more worried about their cash reserves, debt obligations and risk of insolvency than those in other sectors. Few of them, though, are planning redundancies, and growth in input costs has slowed.

8 Employers are also concerned about earnings differentials – the gap in pay between those on the wage floor and those just above them in the pay distribution, including their managers and supervisors. Differentials in low-paying industries are more compressed than in the past and becoming increasingly so. Employers worry this is harming staff retention, recruitment and morale. Some workers have also told us that the reduction in differentials has reduced their incentive to progress.

9 Passing on the costs of the NLW increase to customers through price increases remained a common response among employers. Some, though, continued to say there was a limit to how long this could be sustained, particularly as overall inflation itself waned. Some sectors remained constrained in their ability to pass on cost increases. Firms who compete internationally, and publicly funded sectors like social care, local government, and childcare are less able to increase prices. While retail and hospitality sectors had been able to pass on costs through prices, they say their ability to do so now has diminished.

Youth and apprentice labour markets

10 The ongoing issues with the LFS make understanding the state of the youth labour market more difficult. One the face of it, youth employment has weakened, in part due to increased inactivity, in turn driven by rising ill health. However, this rise in inactivity may be overstated. On the positive side, hourly pay growth remains strongest for young workers, suggesting robust demand. And the bite of the youth minimum wages (the ratio of the NMW to median hourly earnings) remains below the levels seen prior to 2016. Despite large increases in minimum wage rates, the coverage of the youth rates (for 16-20 year olds) only increased by two percentage points this year and remains below 2019 levels.

11 Against this, demand has fallen in the low-paying sectors where young people often work. Youth employment in hospitality and retail weakened over the past year, consistent with trends in the adult labour market, which has also seen strong post-pandemic recruitment in hospitality slow down. However, the share of those unemployed and not in education has fallen over the last year and is just below pre-pandemic levels.

12 The impact from 21-22 year olds becoming entitled to the NLW has been limited. As expected, we have seen a large increase in the share of 21-22 year olds paid at their minimum wage but initial econometric analysis has found no significant impact on employment or hours worked for this group.

13 Unions and charities supported reducing the NLW entitlement to 18 years, while the views of employers were more mixed. Achieving this for 18-20 year olds carries more risk than it did for 21-22 year olds as they are more likely to be in education, working part-time, and earning below the NLW than

21-22 year olds were. The gap between the 18-20 Year Old Rate and the NLW is greater than was the case for the 21-22 Year Old Rate.

14 Apprentice pay growth has weakened over the past year; apprenticeship starts were similar to the previous year, but the long-term trend in England remains one of declining starts among the age cohorts most likely to be paid the Apprentice Rate. Despite most stakeholders telling us they do not use the Apprentice Rate, pay data suggest the rate is widely used; coverage is highest for those aged under 19 and has jumped in the past year. Our recommendations on the Apprentice Rate have been linked to the 16-17 Year Old Rate since April 2022. We continue to think it is right to hold these two rates together, but in the future, we will need to take account of substantial reforms planned by the Government to apprenticeship provision in England.

Living costs

15 The inclusion of living costs is a significant change to our remit, particularly the ask to take account of future inflation. Most Government policies that take account of changes in the cost of living, such as pensions or benefits, look backwards at historic inflation. We are tasked with looking forwards. Living costs have always been key to LPC recommendations, but this is the first time they have formally been in our remit. As such, our approach may evolve over time, particularly as Government sets out more detail on how a "genuine living wage" is to be defined.

16 We have looked at a range of measures of living costs to understand the price pressures faced by different types of households. While NLW workers are found throughout the household income distribution, they tend to be in households towards the lower end, and so we focus on inflation measures for households with below-average incomes. After the pandemic, inflation for the lowest-income households (Deciles 1-3 of the Household Cost Indices) rose much faster than for other deciles. Increases in energy, rents, fuel and food prices had a larger impact on those in lower-income deciles because these goods take up a larger share of income among these groups.

17 While inflation has slowed, workers and employers are keen to remind us that this just means that prices are now growing more slowly. It does not reverse the damage done to living standards in recent years. While energy prices have fallen, they are far higher than prior to the recent spike in inflation, as are the prices of food and other essentials. However, we are pleased to note that the NLW has increased in real terms since 2019, as it has since its introduction.

18 Workers told us they are still suffering from the recent dramatic increases in the cost of living and have seen their spending power and living standards decline in recent years. NLW upratings are appreciated but seen as a partial mitigation at best. We also heard that insecure work is common and that it exacerbates this financial insecurity. Many workers told us about the difficulty of securing sufficient working hours.

19 However, the recent shock to energy prices is only a recent part of the UK's living standards story. Average real weekly wages are barely higher than they were in 2008. This absence of growth for more than 15 years is unprecedented and breaks a consistent trend of wages growing faster than prices since at least 1963, which includes the price shocks of the 1970s and 1980s. In strong contrast, the real value of the minimum wage, particularly after the introduction of the NLW, has kept well ahead of rises in living costs and has improved the relative position of the lowest paid in the UK.

Our recommendations

National Living Wage

20 Our new remit asks us to balance the living standards of workers, business conditions for employers and the Government's aim for the NLW not to fall below two-thirds of median pay. Taking all of this into account, we recommend an NLW of £12.21 should apply to those aged 21 and above (an increase of 77 pence or 6.7 per cent).

21 This is the rate required to meet the Government's ambition not to fall below two-thirds of median earnings. In October 2023, when we made our recommendation of £11.44, we expected that it would achieve this level. However, the combination of wage growth outstripping forecasts and the ONS changing the Annual Survey of Hours and Earnings methodology – our key source for measuring pay – meant that £11.44 was not high enough to reach it. This means there is ground to make up to reach this threshold in 2025, so our recommended increase of 6.7 per cent is higher than expected median wage growth. The combination of a larger than expected increase being required to hit the threshold, and business conditions weakening in some areas, has led us not to recommend an increase above the two-thirds threshold.

22 Because of the welcome return of real wage growth and forecasters' expectations that this will continue, we believe our recommended rate is sufficient to stay ahead of expected inflation on a range of measures up to March 2026. The labour market has loosened, but demand remains robust. And while some business conditions have deteriorated – with more firms worried about cash, debt and insolvency – others have improved. Labour shortages have reduced, and the growth in input costs has slowed. If monetary policy loosens in response to lower inflation, then this may further bolster economic growth, which is expected to be greater in 2025 than it was in 2024. We believe this increase is consistent with the state of the labour market and the wider economy.

Youth rates of the minimum wage

23 The Government wants "every adult worker" to benefit from a "genuine living wage" and to lower the NLW age threshold to 18 years of age. Rather than make this change straight away, the remit suggests we should "take steps year by year" and in 2025 we should "continue to narrow the gap" between the 18-20 Year Old Rate and the NLW. In making this change, we are asked to take account of the effects on employment of younger workers, incentives for them to remain in training or education and the wider economy. Our remit for the youngest workers, those aged 16 and 17, is different again. Here we still have our traditional remit of pushing the wage as high as possible without damaging employment.

24 Last year we recommended ambitious increases for young people and apprentices and acknowledged some risk in doing so. However, while the labour market has softened for young people there is no robust evidence to suggest that last year's large increases have caused harm.

25 The increase for 18-20 year olds in April 2024 was the highest ever (£1.11 or 14.8 per cent) and has already started to close the gap with the NLW. With such a large increase we would expect coverage (the share of jobs paid the rate) to increase in tandem, but it only increased very slightly. Also, effective coverage – those paid between their age rate and the NLW – remained below pre-pandemic levels. Wage growth among this age group was also strong. All of this is consistent with healthy demand for 18-20 year old workers so we recommend an increase that continues to narrow the gap with the NLW, with a recommended rate of £10 an hour for 18-20 year olds (an increase of £1.40 or 16.3 per cent).

26 We will consult in spring 2025 on the appropriate pace and approach to closing the gap the rest of the way, whether by raising the level, lowering the age threshold or a combination of the two. As with the NLW, other changes to policy will be important considerations here.

27 Following a substantial increase in the wage floor for 16-17 year olds (£1.12 or 21.2 per cent) in April 2024, coverage rates for this group rose to their highest ever level, though they remain below those for some apprentices and 21-22 year olds. Also, as wages have been growing rapidly for these workers, the very large increase in their wage floor has only returned the bite (the ratio of the minimum wage to the median wage) to its pre-pandemic levels. We recommend a rate of £7.55 (an increase of £1.15 or 18 per cent) that returns the 16-17 Year Old Rate to the relativity it had with the adult rate when it was introduced.

28 In our advice on the National Minimum Wage Beyond 2024 (Low Pay Commission 2024b), we recommended that, in the long term, the Apprentice Rate changes to a simple discount of the adult rate. However, we said that this should not happen at the same time as major changes to the youth rates. We also note the Government's intention to change policy on apprenticeships and the levy, which will have implications for the system in England. As such, we don't recommend significant change at this stage and the Apprentice Rate should stay aligned with the 16-17 Year Old Rate, so we recommend a rate of £7.55 for them also (an increase of £1.15 or 18 per cent).

Accommodation Offset

29 We recommend increasing the Accommodation Offset in line with the percentage rise in the NLW, to £10.66 (an increase of 67 pence or 6.7 per cent). This is in line with the conclusion of our review of the offset in 2022, where we stated that "The value of the offset as a proportion of the NLW will not increase significantly until we have some assurance that there are robust minimum standards in place for accommodation quality and that these are enforced."

Recommendations on the evidence base

30 Without improvements to the evidence base, our ability to give the Government the best advice we can is compromised.

31 We recommend that the ONS work with all parts of Government that use the Annual Survey of Hours and Earnings to inform policy decisions, so that in future they have advance notice of further methodological changes and the chance to agree the most appropriate time to make these changes.

32 We urge the Government do all it can to enable the ONS to improve the Labour Force Survey as soon as possible and successfully transition to the Transformed Labour Force Survey.

33 Robust econometric analysis is not possible with the Labour Force Survey in its current state. This means we cannot rigorously assess the impacts of changes to the minimum wage rates on employment and hours. Improved access to HMRC's Real Time Information (RTI) could provide a partial alternative:

- We recommend that the Government provides us with an ongoing RTI dataset that covers all employment by minimum wage age group and low-paying sector for each local authority area in the UK since RTI data became available in 2014.
- We recommend that the Government provide access to far more timely RTI micro-data through the HMRC Datalab and ultimately through the Integrated Data Service being established by ONS.

34 The Government's focus on living standards has shown the need for forecasts of living costs. At the moment, we are not aware of any reputable forecasts for the Housing Cost Index (HCI). We recommend that HM Treasury asks the OBR and its panel of forecasters to begin forecasting HCI inflation, particularly for lower-income households.

Recommendations on policy

35 We recommend that the Government ensures the question of sleep-in shifts' entitlement to the minimum wage is addressed in the planned Fair Pay Agreement for the social care sector. We cover this issue, and the situation of the social care sector more generally, in Chapter 8.

36 We recommend the Government look more widely at the entitlement to and enforcement of the NMW for seafarers, including via full implementation of the Seafarers Wages Act. We discuss evidence on seafarers in Chapter 9.

Recommendations

Rate recommendations

We recommend that the following rates apply from 1 April 2025:

	2025 rate	Annual increase (£)	Annual increase (per cent)
National Living Wage	£12.21	£0.77	6.7
18-20 Year Old Rate	£10.00	£1.40	16.3
16-17 Year Old Rate	£7.55	£1.15	18.0
Apprentice Rate	£7.55	£1.15	18.0
Accommodation Offset	£10.66	£0.67	6.7

Recommendations on policy

- We recommend that the Government ensures the question of sleep-in shifts' entitlement to the minimum wage is addressed in the planned Fair Pay Agreement for the social care sector. We cover this issue, and the situation of the social care sector more generally, in Chapter 8.
- We recommend the Government look more widely at the entitlement to and enforcement of the NMW for seafarers, including via full implementation of the Seafarers Wages Act. We discuss evidence on seafarers in Chapter 9.

Recommendations on the evidence base

- We recommend that the ONS work with all parts of Government that use the Annual Survey of Hours and Earnings to inform policy decisions, so they have advance notice of further methodological changes and the chance to agree the most appropriate time to make these changes.
- We urge the Government do all it can to enable the ONS to improve the Labour Force Survey as soon as possible and successfully transition to the Transformed Labour Force Survey.
- Robust econometric analysis is not possible with the Labour Force Survey in its current state. This means we cannot rigorously assess the impacts of changes to the minimum wage rates on employment and hours. Improved access to HMRC's Real Time Information (RTI) could provide a partial alternative:

  - We recommend that the Government provides us with an ongoing RTI dataset that covers all employment by minimum wage age group and low-paying sector for each local authority area in the UK since RTI data became available in 2014.
  - We recommend that the Government provide access to far more timely RTI micro-data through the HMRC Datalab and ultimately through the Integrated Data Service being established by ONS.
- The Government's focus on living standards has shown the need for forecasts of living costs. At the moment, we are not aware of any reputable forecasts for the Housing Cost Index (HCI). We recommend that HM Treasury asks the OBR and its panel of forecasters to begin forecasting HCI inflation, particularly for lower-income households.

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Chapter 1

The economic context

Key findings

- **This chapter, focusing on the wider economy and inflation, is based on evidence available to us up to 25 October 2024 only –** This was the point at which we submitted our recommendations to the Government.
- **Inflation fell below the Bank of England target in September 2024 –** CPI is expected to pick up in the next six months as energy prices rise but is forecast to remain below 3 per cent. However, prices remain far higher than they were pre-pandemic and well above their pre-crisis trend. This has clear implications for both real wages and living standards, which we discuss in Chapters 2 and 4.
- **Economic growth has surpassed expectations in 2024 so far –** In October 2023 we expected GDP growth of 0.4 per cent in 2024, but this looks likely to be comfortably surpassed in 2024, with growth of 1 per cent now expected. However, this is still weak by historic standards and both GDP growth per head and per hour (productivity) have fared worse than GDP growth.
- **Consumer spending is weak, while investment and government spending are driving growth –** As inflation has fallen, real incomes have risen, but rather than increase spending, consumers are saving more. Unlike previous recoveries, trade and consumer spending are showing weak recoveries, while investment and government spending drive growth.
- **Weak consumer spending hits consumer-facing services –** Real output of consumer-facing services like retail and hospitality remains well below pre-pandemic levels. Over four years after the pandemic began, the output of retail, food and drink and accommodation are 4, 5 and 10 per cent below their output in 2019 respectively.
- **The outlook for GDP growth is much better than last year but still weak historically –** The combination of inflation waning, real incomes rising and the Bank of England lowering interest rates should boost GDP growth. As a result, forecasters expect economic growth in 2025 to be stronger than in 2024, and most have revised up their estimates following 2024's stronger than expected growth. However, the numbers projected are still weak by historic standards.

Introduction

1.1 The Government asked us to recommend a National Living Wage (NLW) that takes account of the impact on business; competitiveness; the labour market; the wider economy; and the cost of living, including the expected annual trends in inflation between now and March 2026. These factors will be covered in this Report. This chapter focuses on the wider economy and inflation and is based on evidence available to us up to 25 October 2024.

While inflation was expected to continue to slow, economic growth was forecast to be weak in 2024

1.2 At the time (October 2023) we made our recommendations for minimum wage rates in April 2024, we noted that the UK economy had recovered to its pre-pandemic level of GDP by the end of 2021, but subsequent growth had been weak as inflation eroded real incomes. Inflation had been more persistent than previously forecast but was expected to continue slowing towards 2.5 per cent by the end of 2024. Pay growth was expected to remain above pre-pandemic levels boosting real incomes, although its impact on spending was likely to be dampened by the freeze in personal tax thresholds. Strong pay growth raised concerns among interest rate setters at the Bank of England that this would lead to more persistent inflation.

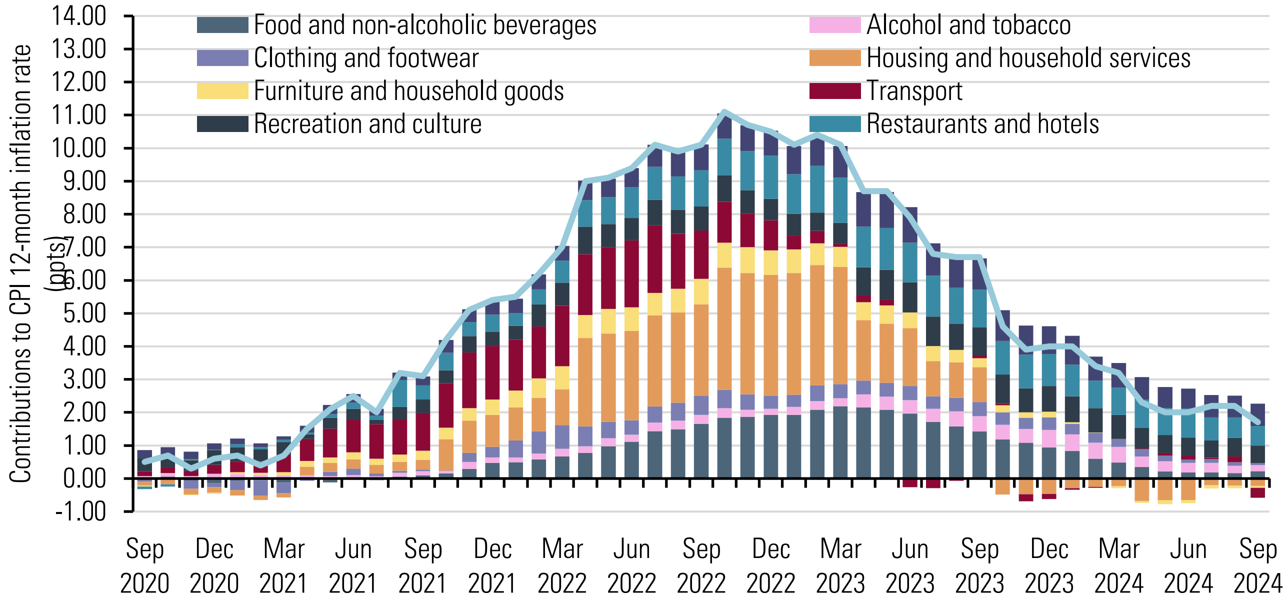
1.3 While high interest rates help curb some inflationary pressures, they also affect GDP growth. Firms, households and the Government will be affected. Rising interest rates and uncertainty about the economic outlook both in the UK and globally were likely to dampen business investment, which had been weak since 2016. While increased interest rates boosted savings, they also led to increased debt payments for households and the Government. GDP growth was expected to be around 0.4 per cent in 2024.

Inflation has slowed but prices remain elevated

1.4 As shown in Figure 1.1, prices of housing and household services (including gas and electricity) and the prices of furniture and household goods have fallen for much of 2024 with food inflation slowing and fuel prices no longer rising. Inflation slowed from 6.7 to just 1.7 per cent in the year to September 2024. The main upward pressures over the last year have come from going out (recreation and culture) and eating out (hotels and restaurants).

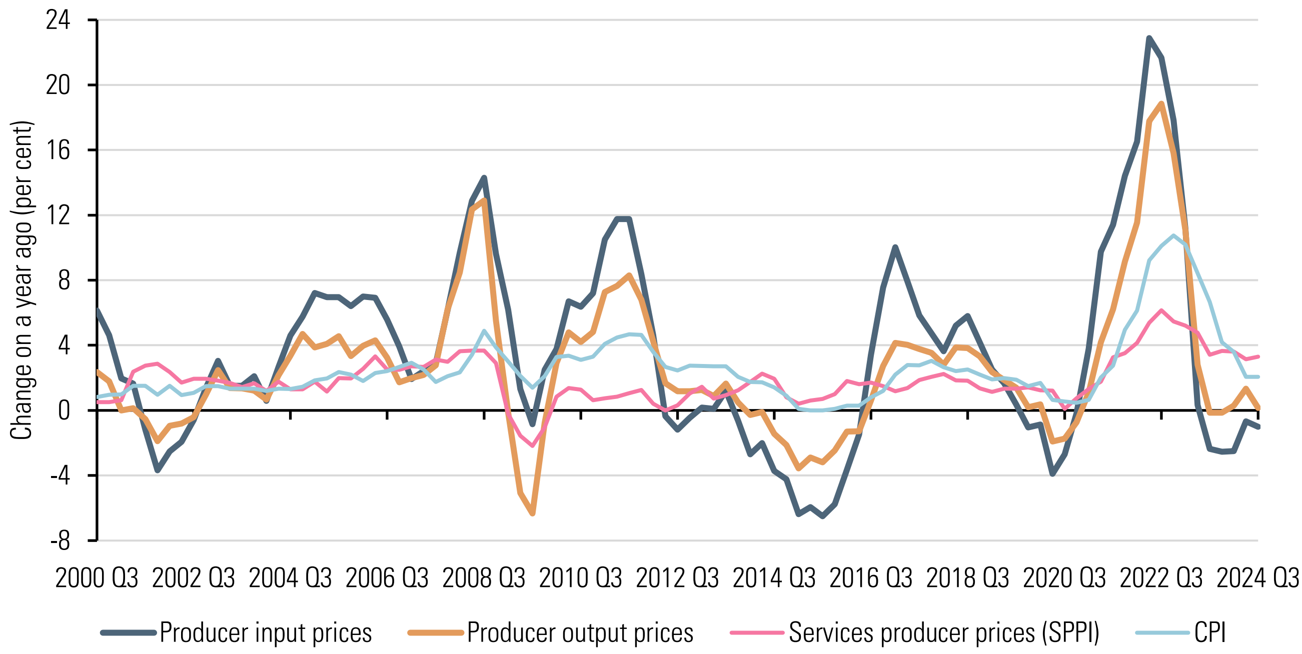
1.5 The reduction in price pressures was also evident for businesses. As shown in Figure 1.2, producer input prices had fallen by 1 percentage point over the year to the third quarter of 2023, while output prices had grown by only 0.1 per cent. Business-to-business services price growth slowed from a peak of 6.2 per cent in the third quarter of 2022 but remained elevated at 3.3 per cent in the third quarter of 2024 – still higher than for most of the last 24 years.

Figure 1.1: Contributions to annual consumer price inflation, UK, 2020-2024



Source: LPC estimates based on ONS data. Consumer price index (CPI) inflation, UK: CPI inflation all-items index (D7BT); Food and non-alcoholic beverages (D7BU); Alcohol and tobacco (D7BV); Clothing and footwear (D7BW); Housing and household services (D7BX); Furniture and household goods (D7BY); Transport (D7C2); Recreation and culture (D7C4); Restaurants and hotels (D7C6); and other goods and services (includes Health (D7BZ), Communication (D7C3), Education (D7C5), and Miscellaneous goods and services (D7C7)), monthly, UK, September 2020-September 2024.

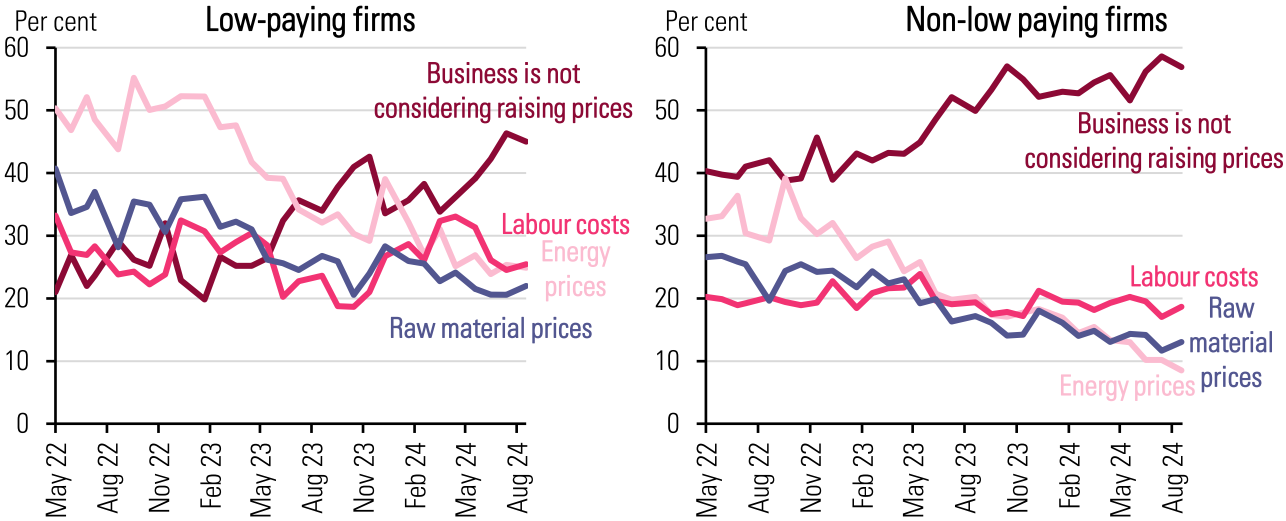
Figure 1.2: Producer price and consumer price inflation, UK, 2000-2024



Source: LPC estimates using ONS data. Producer input prices, inputs into manufacturing (GHIP); producer output or factory gate prices, manufactured products for domestic market, excluding duty (GB7S); Services Producer Price Index (SPPI), top level, sections H to U excluding K (HQTI); and Consumer price index (D7BT), seasonally adjusted, quarterly, Q3 2000-Q3 2024.

1.6 Figure 1.3 shows the share of firms citing different factors in response to the question "Which of the following factors, if any, are causing your business to consider raising prices?" from the ONS BICS survey. It shows that the share of firms saying increases in energy, raw material and labour costs are feeding into their selling prices fell in the twelve months to August 2024. As a consequence, a higher share of firms in August 2024 were saying they were not considering raising prices. However, firms in low-paying sectors remained more likely to be considering rising prices, with pressures from energy, labour and raw material costs falling more slowly. Nevertheless, despite a large NLW rise in April 2024, low-paying firms were less likely to cite labour costs as a cause of price rises after that point.

Figure 1.3: Factors firms in low-paying (LHS) and non-low paying sectors (RHS) say are causing them to consider price rises, UK, 2022-2024

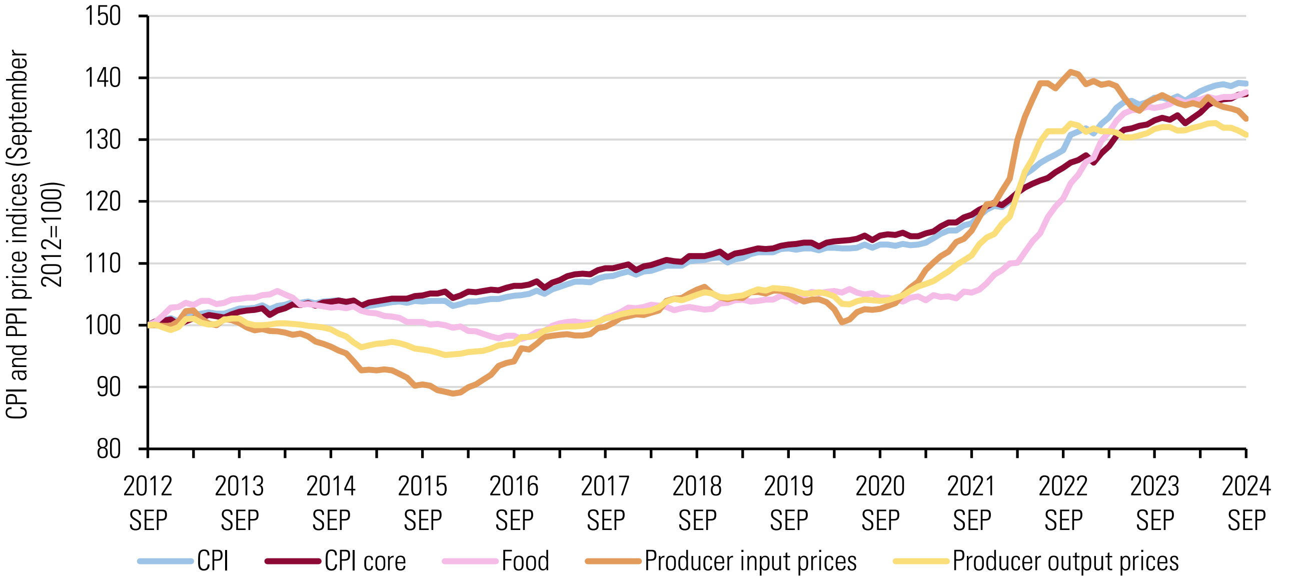


Source: LPC estimates using ONS Secure Research Service Metadata Catalogue, BICS Waves 55-114, Sep 2021-Sep 2024, UK.
Note: Chart shows the share of firms choosing various categories in response to the survey question: "Which of the following factors, if any, are causing your business to consider raising prices in [month] [year]?"

1.7 Although inflation has slowed, prices remain much higher than they were before the pandemic. Figure 1.4 shows that CPI was around 39 per cent higher in September 2024 than in September 2012. Only a third of that increase was in the first eight years, while around two-thirds was in the four years after September 2020. Core prices have followed a similar trajectory. The change in prices is even more stark for food, producer inputs and producer outputs. Between September 2012 and September 2020, all three increased by around 4-5 per cent. As pandemic restrictions eased, producer input and prices increased sharply. Input prices rose by around 36 percentage points and output prices by nearly 30 percentage points in just two years. They have since fallen back but input prices are still around 30 percentage points higher than pre-pandemic (and output prices around 26 percentage points higher).

1.8 Food prices increased by just over 5 percentage points in the nine years up to September 2021 but in the following three years they have increased by around 32 percentage points. The change in energy prices (not shown) has been even more extreme. Between September 2012 and September 2019, energy prices increased by 26 per cent before falling back by 15 percentage points over the next 18 months. Energy prices then started to rise from March 2021 onwards (increasing around 28 percentage points by March 2022). Then Russia invaded Ukraine, triggering further and more dramatic increases. Despite Government intervention with a price cap, energy prices more than doubled (up 118 percentage points in the twelve months to March 2023). Energy prices have since fallen back, but in September 2024, were still 24 per cent higher than before the Russian invasion.

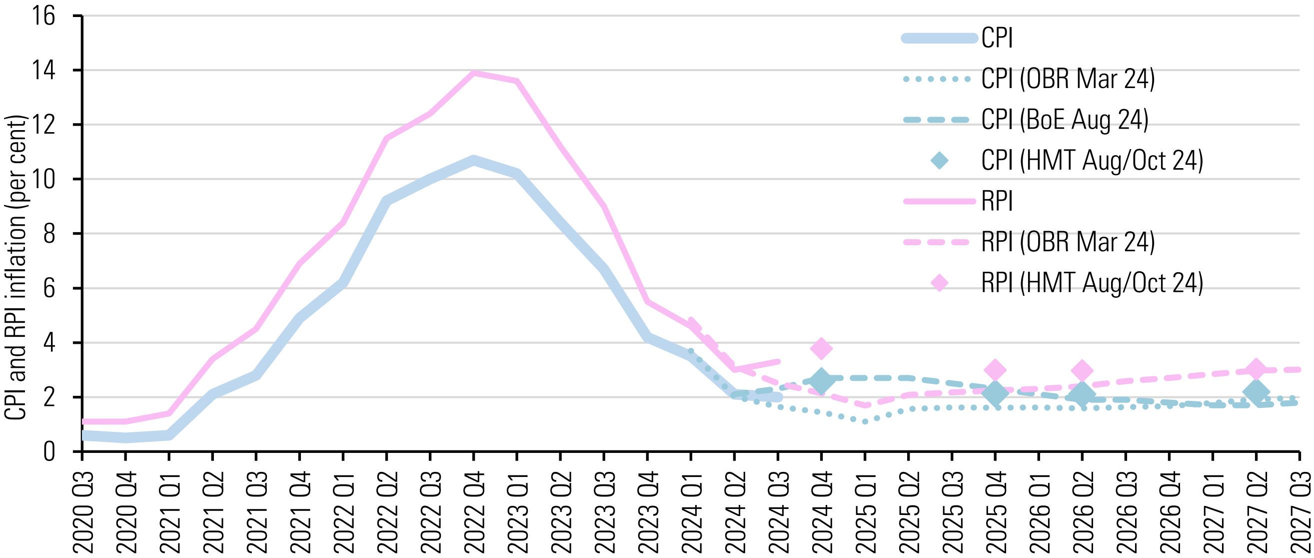
Figure 1.4: Consumer and producer price indices, UK, 2012-2024



Source: LPC estimates using ONS data. Producer input prices, inputs into manufacturing (GHIP); producer output or factory gate prices, manufactured products for domestic market, excluding duty (GB7S); Services Producer Price Index (SPPI), top level, sections H to U excluding K (HQTI); and Consumer price index (D7BT), seasonally adjusted, quarterly, Q3 2000-Q3 2024.

1.9 Looking forwards, both the Bank of England and the HM Treasury panel of independent forecasters expected CPI inflation to remain relatively low and close to its target of 2 per cent. However, recently announced increases in utility prices were expected to push inflation towards 3 per cent in the next 6 months or so, as shown in Figure 1.5, before slowing back towards 2 per cent by early 2026.

Figure 1.5: Actual and forecast inflation, UK, 2020-2027



Source: LPC estimates using ONS data and forecasts from OBR, HMT and Bank of England. CPI (D7G7) and RPI (CZBH), quarterly, seasonally adjusted, 2020 Q3-2024 Q3. Forecasts from OBR Economic and Fiscal Outlook March 2024, Bank of England Monetary Policy Report August 2024 (market median from MPC forecasts of annual CPI inflation), and HM Treasury panel of independent forecasts: median from Tables 2 and 5 (August 2024 and October 2024).

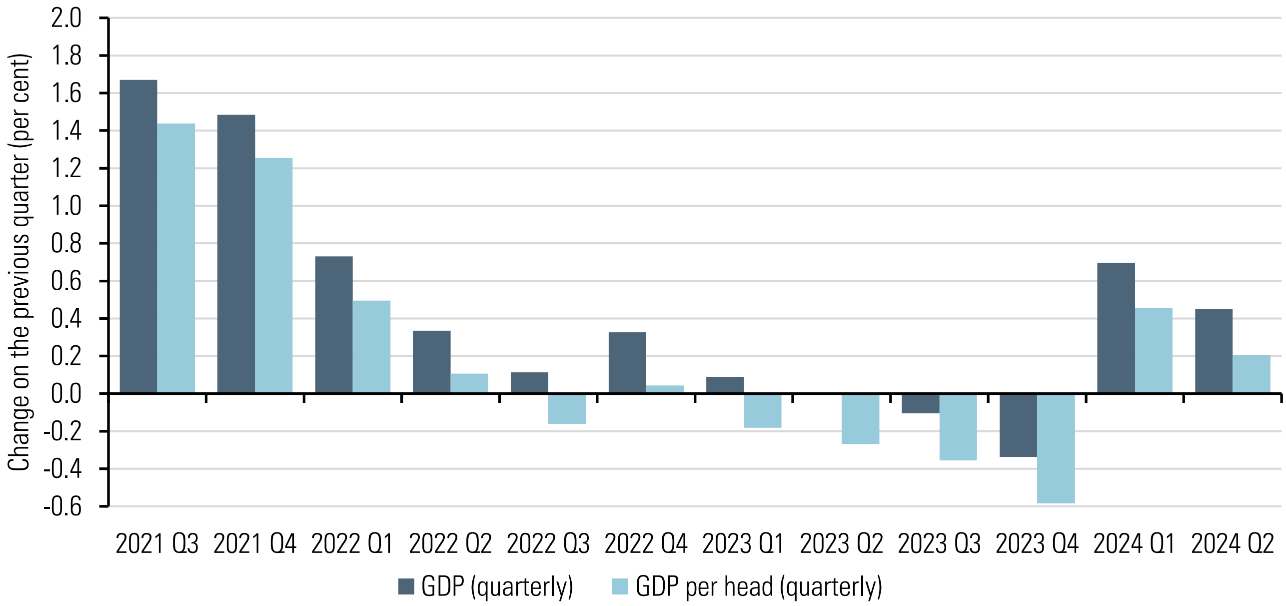
1.10 In this section, we have focused on macroeconomic inflation measures. We consider other measures of inflation, with a greater focus on household costs, in Chapter 4. With inflation low and the outlook for prices subdued, there was an opportunity for real wages to recover some of the ground lost since the onset of the financial crisis. We consider this in the next chapter.

The economy went into recession at the end of 2023 but bounced back strongly in the first half of 2024

1.11 At the time we made our recommendations for April 2024 in the autumn of 2023, the consensus of forecasts was that GDP would grow by around 0.4 per cent annually in both 2023 and 2024. Growth in 2023 turned out weaker (0.3 per cent), but growth in the first half of 2024 was much stronger than those forecasts.

1.12 After the strong rebound in the second half of 2021, GDP growth slowed in each subsequent quarter before turning negative in the second half of 2023, with the UK going briefly into recession (as shown in Figure 1.6). However, the economy has rebounded strongly in the first half of 2024 with expectations that annual growth will be double that of the forecasts.

Figure 1.6: Quarterly growth in GDP and GDP per head, UK, 2021-2024



Source: ONS. LPC estimates using real gross domestic product (ABMI) and real GDP per head (IHXW), seasonally adjusted, UK, 2021 Q3-2024 Q2.

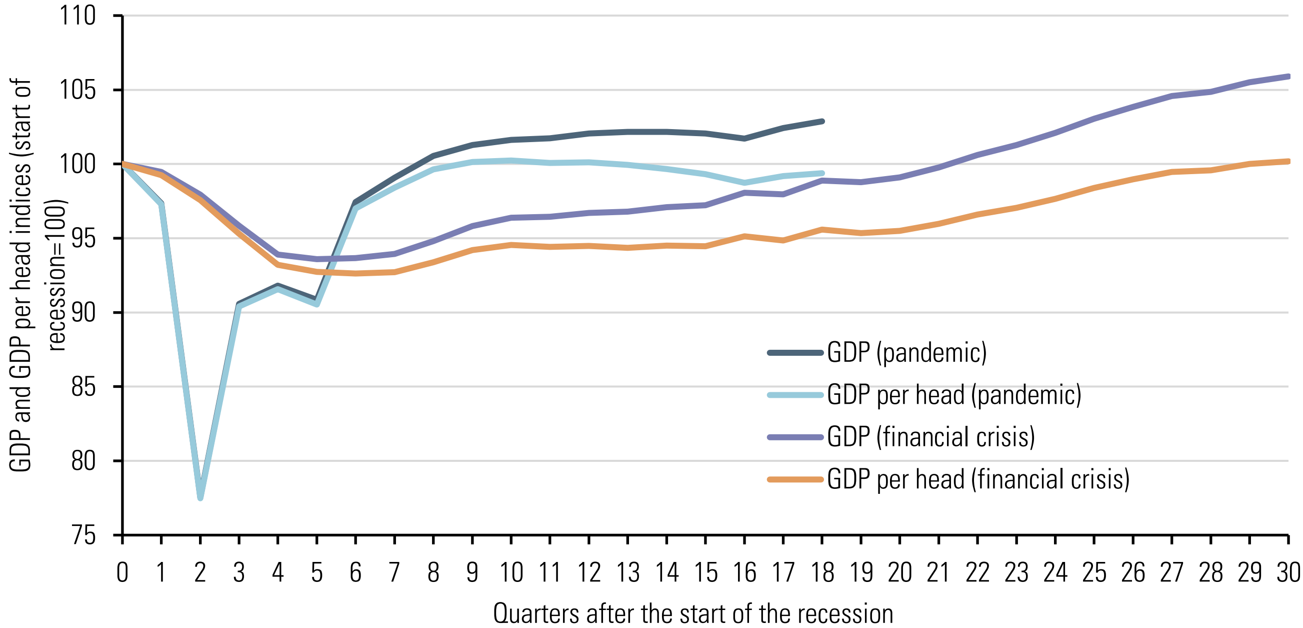
1.13 Growth in GDP per head has been much weaker. Indeed, Figure 1.6 shows GDP per head fell in five of the six quarters between the third quarter of 2022 and the fourth quarter of 2023, then rebounded somewhat in the first half of 2024.

1.14 Figure 1.7 shows that GDP is now higher (2.9 per cent) than just before the pandemic (Q4 2019), but GDP per head is still lower (0.6 per cent). Nevertheless, the recovery from the pandemic has been stronger on both measures than the recovery from the financial crisis.

1.15 In 2023, labour productivity (output per hour) grew by 0.2 per cent, the slowest pace of growth since 2013. Productivity growth has been anaemic since the financial crisis, growing by an average

0.4 per cent per year in the 16 years since 2007, compared with an average of 2.2 per cent in the 16 years prior to 2007.

Figure 1.7: Comparisons of GDP and GDP per head between the financial crisis and the pandemic, UK, 2008-2024



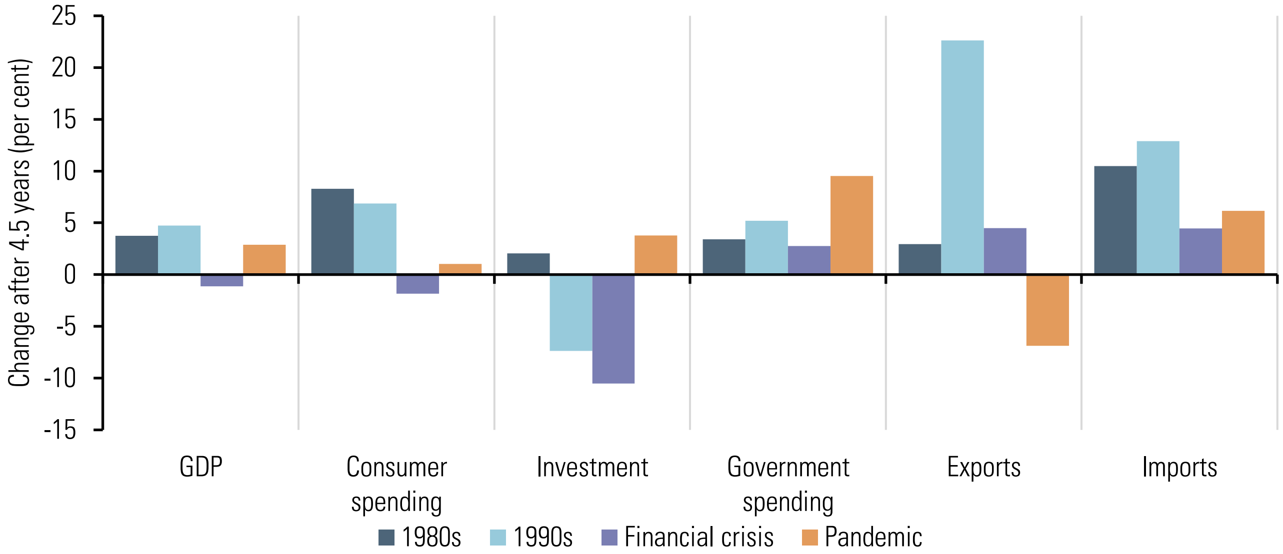
Source: ONS. LPC estimates using Real gross domestic product (ABMI) and real GDP per head (IHXW), seasonally adjusted, UK, 2008 Q1-2024 Q2.
Note: Period 0 in the financial crisis is 2008 Q1 and in the pandemic is 2019 Q4.

The recovery from the pandemic has been driven by government spending and investment

1.16 We have now had 18 quarters (four and a half years) since the onset of the pandemic. Although the recovery in GDP after the pandemic was stronger than that after the financial crisis, it was weaker than the recoveries from the 1980s and 1990s recessions after 4.5 years (Figure 1.8). The orange bars show the growth in GDP components after the pandemic, where government spending was the main driver, aided by total investment (public and private), which was also heavily dependent on the Government. Consumer spending has been weak, while trade has weighed on growth (with imports increasing and exports falling). Trade continues to be affected by geopolitical conflicts (with resultant disruptions to supply chains and increased transport costs, as shipping diverts to safer but more costly routes), and the UK's new trading relationships with the EU and other countries). The recovery from the pandemic is the only one in which exports have detracted from growth.

1.17 That contrasts starkly with weak recovery after the financial crisis (purple bars). Again, Government spending was the main driver but was aided by trade (with exports increasing marginally faster than imports). Consumer spending and investment both fell over this period. The 1980s (dark blue bars) and 1990s recoveries (light blue bars) had been led by the consumer with assistance from investment in the 1980s and trade in the 1990s.

Figure 1.8: Changes in real GDP expenditure components in the 4.5 years after each recession since 1980, UK

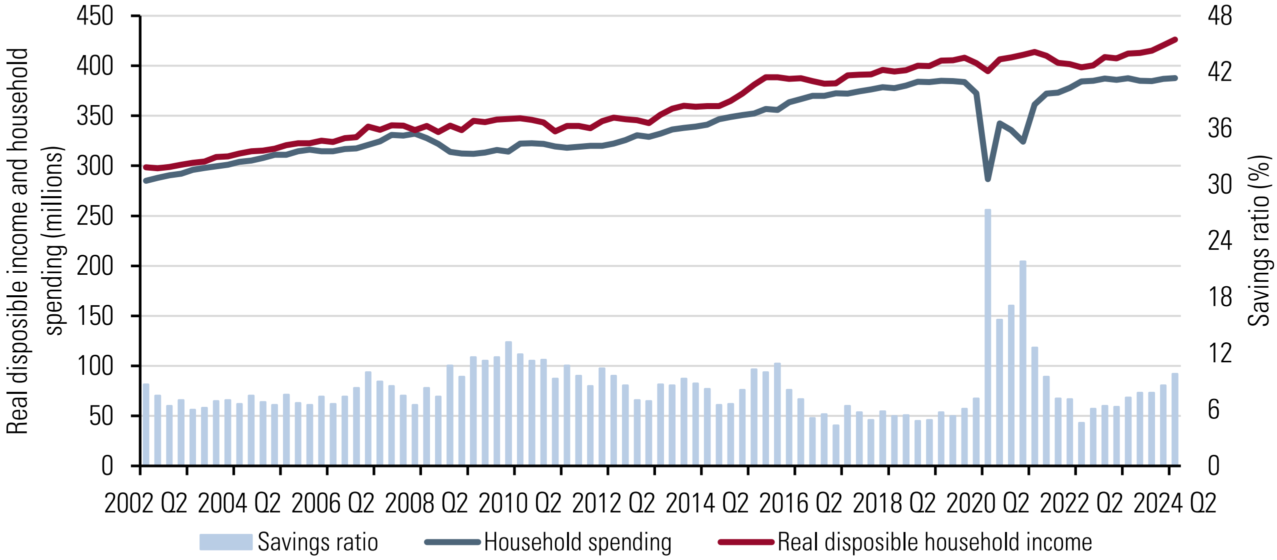


Source: LPC estimates using ONS data. Real GDP (ABMI), consumer spending (ABJR), total investment (NPQT), Government spending (NMRY), exports (IKBK) and imports (IKBL), chainlinked volume measures (real), quarterly, seasonally adjusted, UK, Q4 1979-Q2 2024.
Note: Data is for change in expenditure components after the start of each recession. Comparisons are made with the quarter before the start of recession: 1979 Q4 (1980s), 1990 Q2 (1990s), 2008 Q1 (financial crisis), and 2019 Q4 (the pandemic); and 18 quarters later 1983 Q2 (1980s), 1993 Q4 (1990s), 2011 Q3 (financial crisis), and 2024 Q2 (the pandemic).

Since late 2022, increases in consumers' real disposable incomes have tended to be saved rather than spent

1.18 Rising inflation dampened consumer spending as the economy came out of the pandemic. Figure 1.9 shows that real disposable income fell between the third quarters of 2021 and 2022 as inflation spiked, but it has since recovered as wage growth has been strong. However, while real incomes have increased, consumer spending has remained flat, and savings have increased instead.

Figure 1.9: Real disposable household income, consumer spending and savings, UK, 2002-2024



Source: LPC estimates using ONS data. Real disposable household income (NRJR), household spending (ABJR), and household savings ratio (NRJS), quarterly, seasonally adjusted, UK, Q2 2002-Q2 2024.

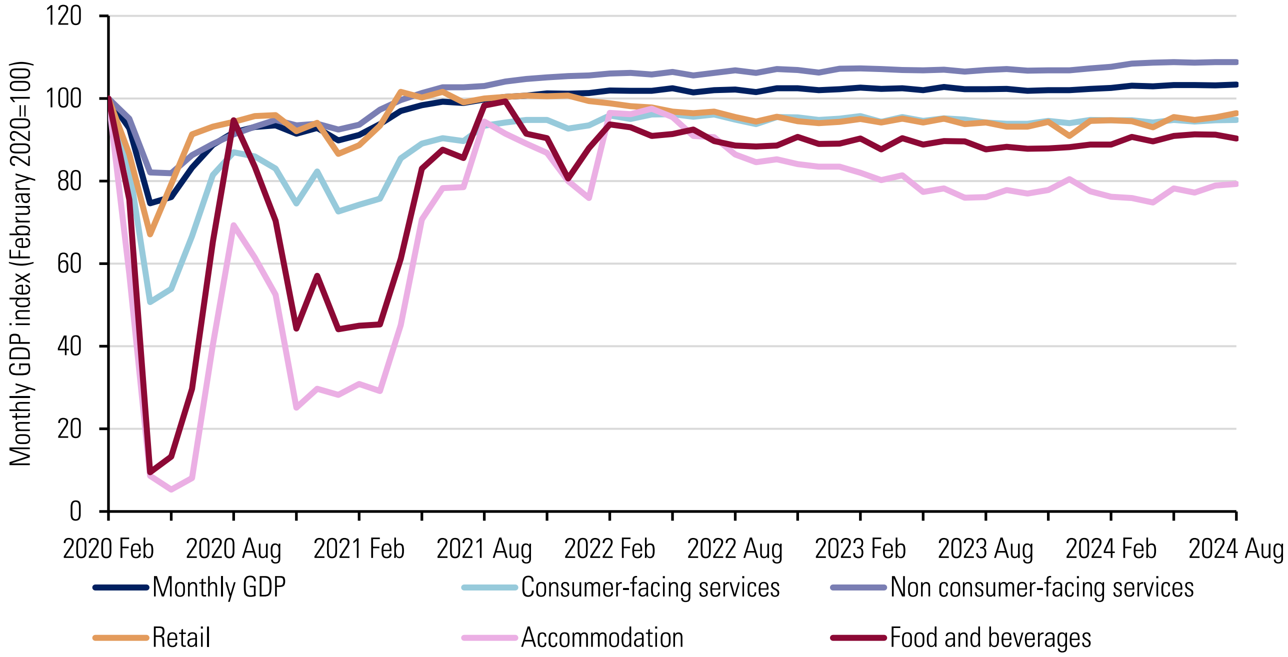
Consumer-facing industries, many of which are low-paying, have struggled since the pandemic

1.19 With consumer spending weak, consumer-facing services (many of them covering low-paying sectors) are still to see real output recover to pre-pandemic levels. Both the accommodation, and food and beverages industries recovered strongly in 2021, but have struggled since 2022 with real output levels 20 and 10 per cent less than pre-pandemic respectively (Figure 1.10).

1.20 Retail was less affected by the pandemic and had recovered to its pre-pandemic level by the spring of 2021. However, since the beginning of 2022, as the inflation rate rose sharply, real gross value added in retail has fallen and remains around 3.6 percentage points below its pre-pandemic level.

1.21 Retail sales show a similar pattern. Retail sales volumes recovered quickly during the pandemic and were around 5 per cent higher by the start of 2022 than in February 2020. Since then, retail sales have declined – falling to around 97 per cent of their pre-pandemic level by October 2022 and remaining there until July 2024. They have picked up in the past two months, but retail sales volumes (including and excluding fuel) are still below their pre-pandemic levels.

Figure 1.10: Monthly real gross value added by service sector, UK, 2020-2024

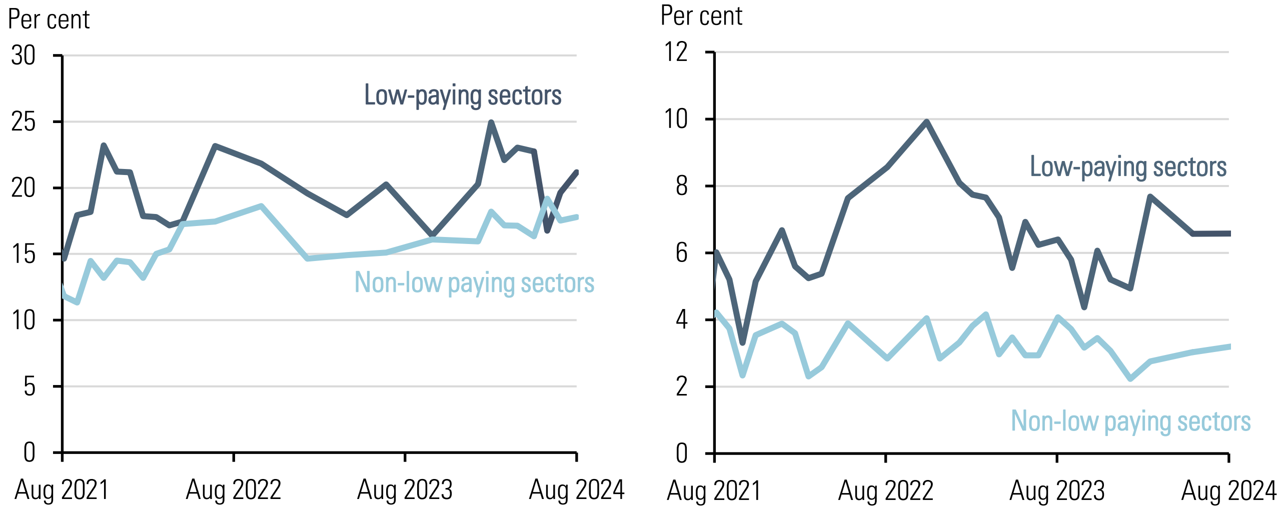


Source: LPC estimates using ONS data. Monthly chained volume indices for real gross value added (ECY2), consumer-facing services and all other services (both from Figure 4 in GDP monthly estimate, UK: August 2024), wholesale and retail (ECYD), and hospitality (ECYH), seasonally adjusted, monthly, UK, February 2020-August 2024.
Note: Consumer-facing services refer to retail trade, food and beverage serving activities, travel and transport, and entertainment and recreation (Standard Industrial Classification 2007 codes: 45, 47, 49.1, 49.2, 55, 56, 68.1, 68.2, 75, 79, 92, 93, 94, 96 and 97). All other services refer to all services (ECYC) except consumer-facing services.

Smaller firms and those in low-paying sectors are more likely to have concerns about their businesses

1.22 Cash reserves are a key metric for businesses, as they can act as a buffer, helping firms when exposed to market downturns or sudden shocks. The left panel of Figure 1.11 shows an uptick in the share of firms saying they have less than one month's cash reserves in the year to August 2024. The right panel of Figure 1.11 shows that, after falling in 2023, the proportion of firms with low or no confidence in meeting their current debt obligations has increased in the first half of 2024, particularly among firms in low-paying sector. BICS data is weighted by count to be reflective of all UK businesses – this allows the experience of small businesses (0-9 employees) to be represented as they comprise 90 per cent of all UK firms but only 10 per cent of respondents.

Figure 1.11: Share of firms with less than one month's cash reserves (LHS) and with low or no confidence in meeting current debt obligations (RHS), UK, 2021-2024



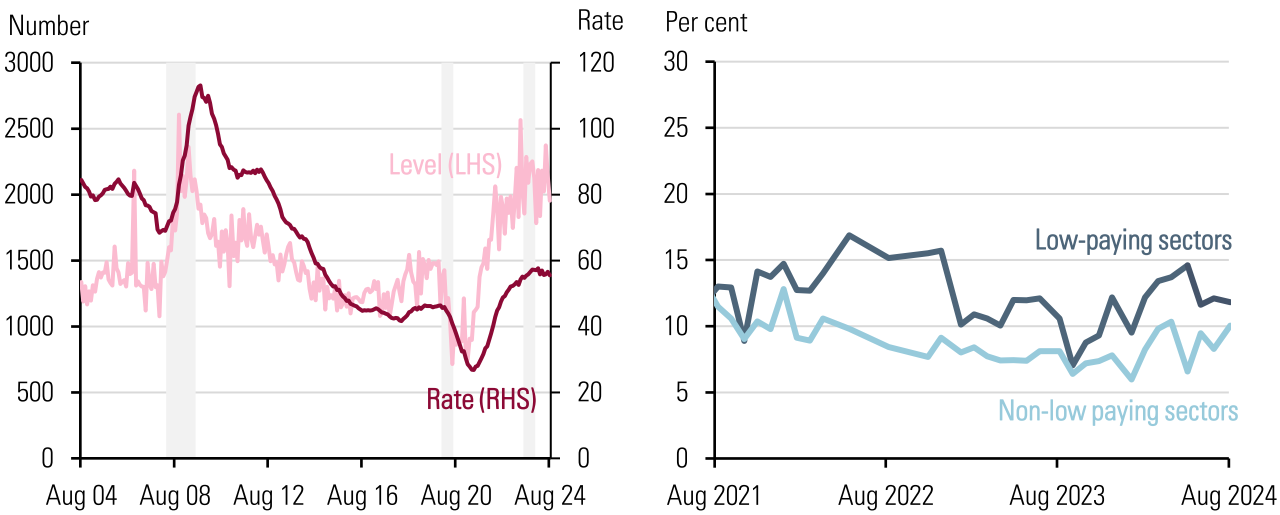
Source: LPC estimates using ONS Secure Research Service Metadata Catalogue, BICS Waves 38-115, Aug 2021-Aug 2024, UK.

Insolvency rates have stabilised, but fears have increased slightly

1.23 The number of company insolvencies fell during the pandemic following Government initiatives to support and protect firms. This is the opposite of what happens during a normal economic downturn, when insolvencies tend to rise. As the support measures were removed, insolvencies increased sharply, though this was largely catch-up from the fall during the pandemic. Monthly numbers have since stabilised at around 2,000-2,500, above pre-pandemic levels (left panel of Figure 1.12). The insolvency rate has risen to around 55 insolvencies per 10,000 companies (or one in 180). This is also above the pre-pandemic rate but much lower than the peak of 113 per 10,000 companies seen in the aftermath of the financial crisis. The reason for the divergence in these two indicators is because the rate depends on the total number of companies on the effective register, which has more than doubled over this period.

1.24 Despite insolvencies increasing, the proportion of firms' considering their insolvency risk to be moderate or severe fell slightly over 2022 and much of 2023 (right panel of Figure 1.12). But, over the past year, the share of firms with these concerns picked up to around one in ten, with firms in low-paying sectors reporting a slightly higher risk.

Figure 1.12: England and Wales Insolvency monthly level and rate per 10,000 companies, England and Wales, 2004-2024 (LHS) and share of firms with a moderate or severe risk of insolvency, UK, 2021-2024 (RHS)

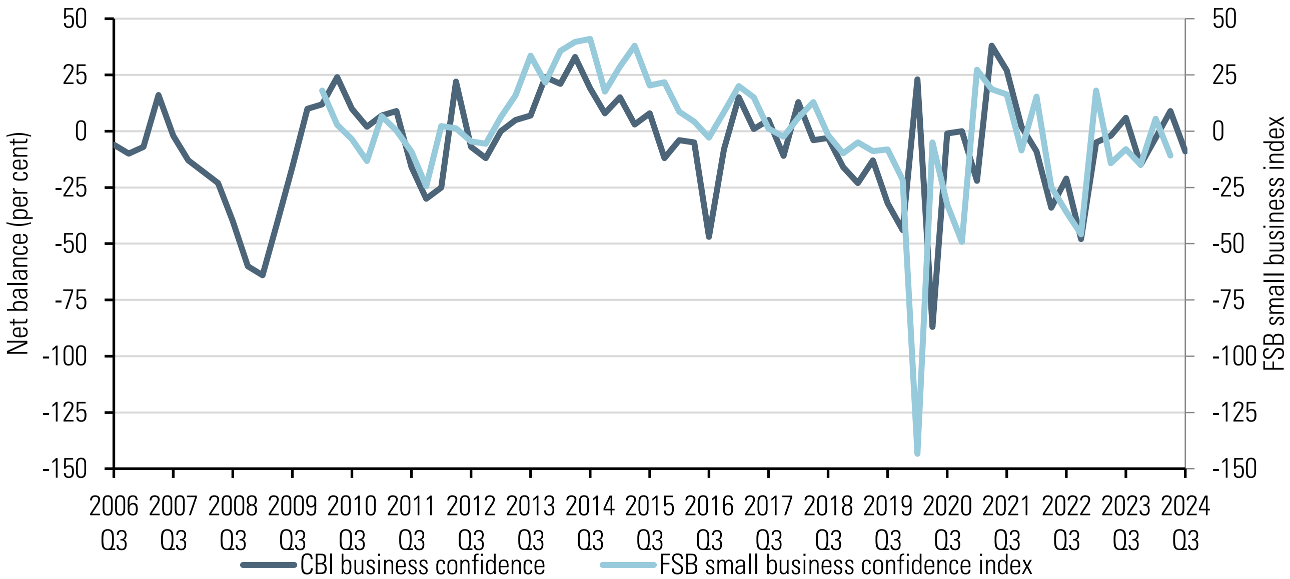


Source: LPC estimates using Company Insolvency Statistics: August 2024 (total_ew_sa and tot_rate_ew) and ONS Secure Research Service Metadata Catalogue, BICS Waves 37-114, Aug 2021-Aug 2024, UK.

Business confidence has generally held up

1.25 Business confidence has picked up since the end of 2022. Both the Confederation of British Industry (CBI) and the Federation of Small Businesses (FSB) measures of business confidence show similar trends with business confidence falling sharply during the pandemic in 2020 and again in 2022 as energy costs rose sharply and interest rates increased. Both measures show business confidence is similar now to what it was in that observed in the period from 2010 to 2014 (Figure 1.13).

Figure 1.13: Business confidence, UK, 2006-2024



Source: CBI and FSB. CBI business optimism index net balance, quarterly, UK, Q3 2006-Q3 2024; and FSB small business index, quarterly, UK, Q1 2010-Q2 2024.

Some employers had a positive view of the economy, pointing to rising confidence as cost pressures eased…

1.26 The FSB told us that small businesses were feeling more confident. In the first quarter of 2024, FSB's headline confidence score reached above zero for the first time since 2018, indicating that "more small businesses are positive than negative about their prospects in the next three months compared to the previous three months". There were big variations between sectors, with manufacturing the most positive and accommodation and food services the least.

1.27 Make UK told us growth expectations for manufacturing had improved slightly, with forecast growth of 1.2 per cent in 2024 and 0.8 per cent in 2025. Recruitment and retention in manufacturing had improved, but challenges remained, particularly with technical skills shortages and immigration policies. The National Hair and Beauty Federation (NHBF) told us the hair and beauty sector had seen a "slow and steady" recovery, with businesses increasing prices to cope with financial pressures and with low recruitment intentions. Survey results showed some positivity into the spring. Slightly more businesses (45 per cent, up from 40 per cent in January) were making a small or good profit and 43 per cent of businesses are breaking even. Fewer businesses (12 per cent) are either making a small or substantial loss.

…but others thought economic conditions were sluggish with businesses nervous and uncertain

1.28 The British Chambers of Commerce (BCC) were representative of views from a broad range of employers in describing the economic outlook as sluggish, with business conditions showing only a small improvement in early 2024. They stated that inflation and recruitment difficulties persisted, but also that many SMEs had been forced to make redundancies. Small businesses, it argued, particularly those in consumer-facing sectors such as retail and hospitality, had been hit harder than larger firms and professional service sectors due to weakened consumer confidence and reduced profitability caused by absorbing inflationary pressures.

1.29 UKHospitality's (UKH) submission on 7 June 2024 described businesses' "nervousness and uncertainty" over the future. This was driven by very low levels of growth, a continuing squeeze on real living standards and a shortage of labour: "People are still going out less […] and being more careful when they do go out". So far in 2024 "there hasn't been a week of positive like-for-like [trading volumes] from last year, they've all been negative". The British Beer and Pub Association (BBPA) similarly characterised their members' situation as perilous due to "continuing high costs of doing business (which will include wage increases), cost-of-living pressures, and an inability to simply increase what they charge in order to match cost increases." Based on ratings data analysed by BBPA, around 500 pubs across the country closed for good in 2023. In Hospitality Ulster's quarterly survey, 17 per cent of businesses were loss-making, 28 per cent broke even, 24 per cent had no cash reserves and 49 per cent were making some degree of profit.

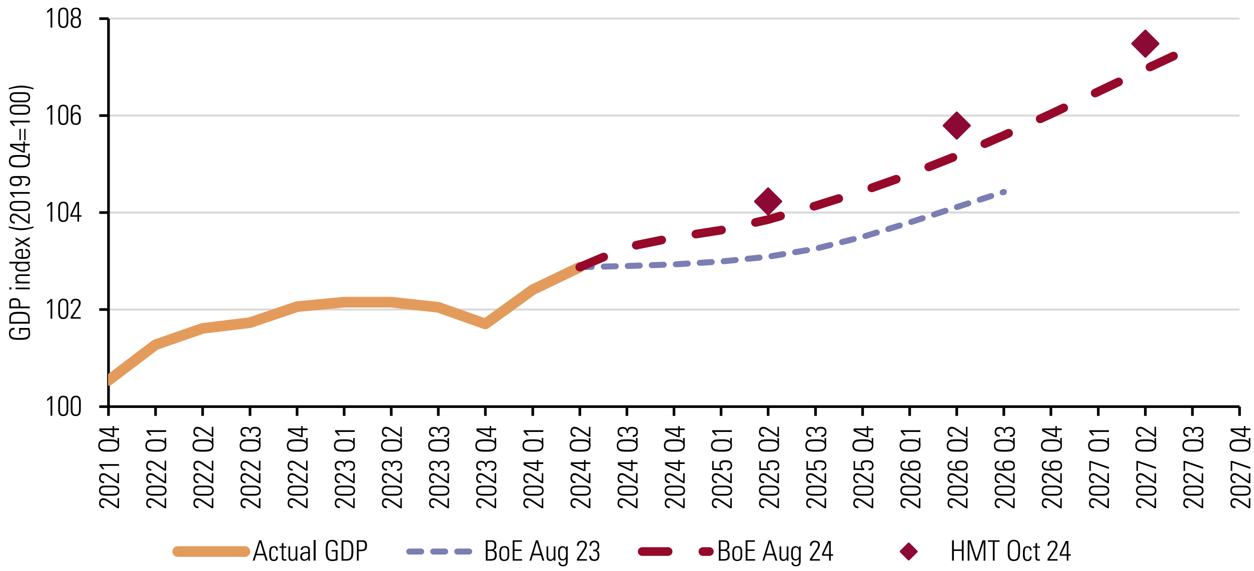
1.30 In agriculture, the National Farmers' Union (NFU) told us that Average Farm Business Income was forecast to fall considerably in 2023/24. Lower prices for wheat and milk would be compounded by persistently high input costs, as a result of the war in Ukraine and the ensuing energy crisis. In contrast, livestock and specialist pig farms were likely to see an increase in incomes as feed costs fall. Farm business confidence, they stated, had fallen sharply since 2021 and lagged that of the whole economy. For the Horticultural Trades Association (HTA), overall garden centre sales for April 2024 were down – 10 per cent on April 2023 and 13 per cent on April 2022. The sector also faced large cost increases (energy, transport, labour and regulatory).

1.31 The UK Cinema Association (UKCA) told us the cinema sector had yet to recover from the pandemic. Trade was "still around 30 per cent down on pre-pandemic levels, and … significantly increased operating charges across a range of areas including utilities and staffing are calling into question the viability of an increasing number of cinema sites." The Booksellers Association told us there was no consensus regarding the economic outlook. "Around a quarter responded with generally positive sentiments regarding their outlook for the next 12 months. However almost 60 per cent believe the next year will be challenging with several respondents stating they are very concerned about their business' ability to survive until the next financial year. The remaining respondents believe trading conditions will be mixed."

GDP outlook looks challenging but there are some encouraging signs

1.32 Forecasters expect economic growth in 2025 to be stronger than in 2024. Over the year to August 2024, the Bank of England became more optimistic about the prospects for UK economic growth, as shown in Figure 1.14. As inflation returns to target, real incomes rise and the Bank is able to lower interest rates, all of which feed into GDP growth. However, uncertainty is still heightened. Tensions in the Ukraine and the Middle East, increased protectionism and the UK's less advantageous trading relationship with its largest market, the EU, all detract from growth.

Figure 1.14: Actual and forecast GDP, UK, 2021-2027



Source: LPC estimates using ONS data and forecasts of GDP growth from the Bank of England, and the HM Treasury panel of independent forecasts. Real GDP (ABMI), quarterly, seasonally adjusted, 2021 Q4-2024 Q2. Bank of England projections of ABMI, August 2023 and August 2024 (2023 Q2-2027 Q3) and HM Treasury median of ABMI forecasts (Tables 1, 4 and M1), 2024-2027.
Note: GDP data was revised in September 2024. The forecast GDP level has been projected from this new base using forecasts of GDP growth.

1.33 Despite the improvement, the Bank's projections are still weak (1.3 per cent for 2024 and 1.0 per cent for 2025) and below the projections from the HMT panel of independent forecasters. Both the IMF (2024) and the OECD (2024) predict the UK to grow by 1.1 per cent in 2024, with the IMF slightly more optimistic about 2025 (1.5 per cent) than the OECD (1.2 per cent).

Conclusion

1.34 Inflation has slowed and, despite recent increases in utility bills, is expected to be around 2-3 per cent over the next year or so. Core and services inflation remain elevated but are on a downward trajectory. However, prices (especially for food and energy) are significantly above what they were three years ago.

1.35 The UK has emerged from its brief recession in the second half of 2023, with strong GDP growth in the first half of 2024. Expectations of growth have been revised up for this year and next but (at around 1-1.5 per cent) are still weak by historical standards.

1.36 In the next chapter, we consider what has happened to the labour market in recent years, before looking forwards over the next 18 months or so.

Chapter 2

The labour market

Key findings

- **Data issues make understanding the labour market difficult** – Despite the ONS working to address falling response rates, the Labour Force Survey (LFS), our main evidence source on the labour market, remains volatile. The ONS continue to advise caution so we bolster our analysis with a range of other sources.
- **Growth in the number of payrolled employees continues to slow** – PAYE RTI shows growth in the number of payrolled employees slowed nationally in 2024, though Northern Ireland's growth was more resilient. Employment growth remained robust in the social care and leisure sectors but weakened sharply in hospitality, one of the largest low-paying sectors.
- **Together with falling employment growth, the continued slowing of job vacancies suggests falling demand for labour** – Having reached unprecedented levels in 2022, job vacancies have been falling for over two years now. Though their level remains close to pre-pandemic levels, and above for smaller employers.
- **As labour demand has eased, worker shortages are less prevalent, but they remain and cause problems for employers** – Recruitment difficulties eased 2023 but remained relatively flat across 2024. While low paying firms are still more likely to report worker shortages, the gap with other firms has narrowed. Stakeholders agree that recruitment remains difficult and only easing because demand for labour is declining. They also say labour shortages are constraining growth and intensifying work.
- **Overseas workers have plugged employment gaps but policy changes will likely reduce numbers –** Immigration to the UK for work has been high in recent years, though the use of targeted visas for workers from outside the UK appears to be falling, in line with government policy to reduce net migration. However, some sectors – particularly agriculture and social care – are reliant on them.
- **Inactivity may have been rising, reducing labour supply, but is hard to measure with certainty –** The LFS suggests inactivity has risen since the pandemic, with ill health the key driver. Claims for health-related benefits have also risen. However, if the LFS undercounts employment it may be overcounting inactivity and health-related benefits can be claimed by those in work.
- **Despite falling demand for labour, unemployment remains close to recent lows** – Unemployment remained at around four per cent in 2024, close to pre-pandemic lows. Similarly, numbers of redundancies were virtually unchanged, and firms did not appear any more likely to make them in the near future. Forecasters expect unemployment to remain low in 2025.

- **The tight labour market has contributed to higher than expected wage growth** – Pay growth slowed over 2024 but remained higher than was forecast at between 4 and 5 per cent. With inflation falling, wages increased in real terms and this is expected to continue for the next 18 months.

2.1 We outlined in Chapter 1 the state of the economy. Inflation fell back quickly from its recent highs to below the Bank of England 2 per cent target, and while expected to pick up late in 2024 it was forecast to remain below 3 per cent in the short-term. Despite rising real wages consumer spending is weak. This specifically impacts low-paying consumer facing services like retail and hospitality where output remains below pre-pandemic levels. Despite this economic growth was above forecast in the first half of 2024. And output for 2025 was forecast to be even stronger, although weak by historic standards.

2.2 In this chapter we look at the state of the labour market and how it has changed in the twelve months to September 2024. This is our assessment of the data at the time we made our recommendations in October, ahead of the autumn budget. In many ways this year is an extension of many of the themes we discussed in our 2023 Report (2024a): the slowdown in aggregate employment growth has continued as firms demand for labour dropped; vacancy numbers have continued to fall month-on-month although levels are still high historically. Falling inflation coupled with strong wage growth has resulted in wages increasing in real terms across most of the period.

Data issues have made it more difficult to understand the labour market

2.3 The problems with the Labour Force Survey (LFS) response rate that emerged last year have continued to limit our ability to examine at changes to employment, unemployment and inactivity. Measures introduced by the Office for National Statistics (ONS) have improved response levels and rates, but achieved sample sizes remain some way below pre-pandemic levels. Lower response rates lead to small sample sizes, which mean increased volatility and risk non-response bias. This is a particular problem for younger age groups and other subsets of the population e.g. ethnic minorities.

2.4 The ONS re-weighted the LFS in February 2024 to incorporate the latest estimates of the size and composition of the UK population. These revisions covered the period from July to September 2022 onwards. While headline indicator levels and rates include historical estimates back to 2011, the unavailability of re-weighted microdata prior to quarter 3 of 2022 creates a discontinuity when looking at all other LFS series. This is particularly troublesome and prevents us from looking at changes for specific groups or by characteristics since the pandemic e.g. inactivity by age or reason. Further revisions re-weighting back to 2019 are planned for December 2024 with a full re-weighting exercise back to 2011 to be carried out in 2025.

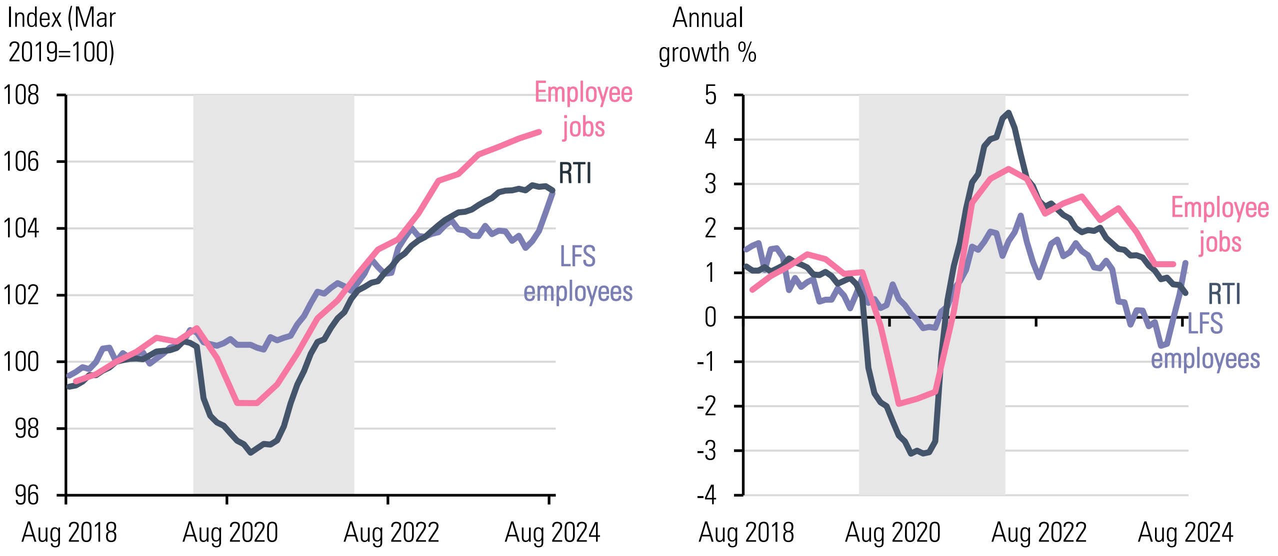
2.5 ONS have continued to advise caution when interpreting short-term changes in LFS headline rates and recommend users also use a wide range of other data sources such as HMRC’s Pay As You Earn (PAYE) Real Time Information (RTI), Workforce Jobs (WFJ) and claimant count data.

LFS volatility is evident when comparing with other data sources

2.6 The uncertainty in the LFS estimates is apparent when comparing the change in LFS estimates of employee numbers with equivalents from Employee jobs data (taken from WFJ) and PAYE RTI data. This is shown in Figures 2.1. Prior to the pandemic all three were growing at roughly the same rate but then diverged. Employee jobs and PAYE RTI employment both fell in 2020, while the number of LFS employees did not. RTI and WFJ employment recovered strongly in 2021 and the start of 2022, but growth was noticeably lower for LFS estimates.

2.7 During the 3 months to August, PAYE RTI employment was levelling off, but LFS data showed an increase of over 370,000 employees. However, these large recent movements are likely to be the result of improved LFS response rates feeding through into aggregate employment figures. Indeed Figure 2.1(LHS) shows that LFS employees and PAYE RTI both show similar overall growth in LFS employees and PAYE RTI since March 2019 (around 5 per cent).

Figure 2.1: Indexed level (LHS) and annual change (RHS) of LFS employees, Employee jobs and PAYE RTI employees, UK, 2018-2024



Source: LPC estimates using ONS data: 16+ employees (MGRN], Workforce jobs employee jobs (BCAJ) and HMRC PAYE RTI payrolled employees, seasonally adjusted, monthly, UK, August 2017 (September 2017 for employee jobs) - August 2024 (June 2024 for employee jobs).

2.8 Because of unreliable LFS data, the next section focuses on PAYE RTI data to examine changes in employee numbers by age, geography and sector. This excludes self-employed workers who are not entitled to the minimum wage.

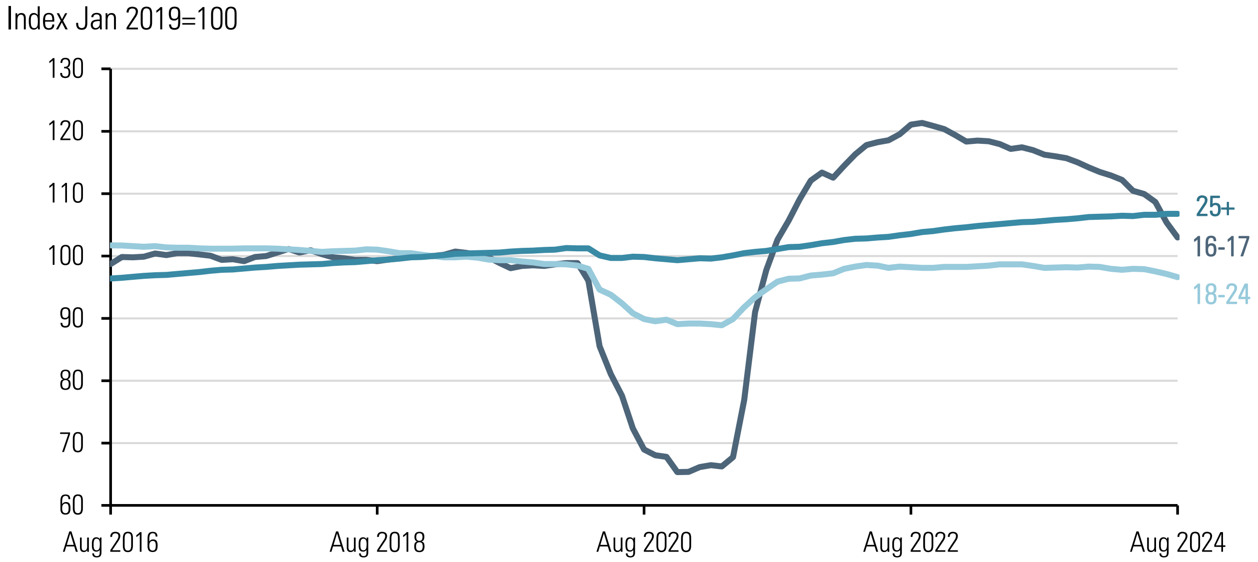
Growth in RTI employment continues to slow

Younger workers have seen employment growth weaken recently

2.9 The level of youth employment has been much more changeable than for older workers in recent years. 16-17 year olds saw the largest impact of the pandemic – Figure 2.2 shows how their employment levels fell by one third before recovering strongly in 2021 and 2022. Since September 2022 the number of employees has steadily dropped among this age group and in August 2024 was only 3 per cent higher than in January 2019.

2.10 18-24 year old employment is different. Numbers in PAYE RTI employment were already falling prior to the pandemic. They fell further in 2020, recovering their losses in 2021 before plateauing in 2022 and 2023. In the first half of 2024 18-24 employment appears to be returning to its pre-pandemic trend of slow decline, partly reflecting a declining 18-24 population. We discuss the employment of younger workers in more detail in Chapter 6.

Figure 2.2: Indexed number of PAYE RTI employees by age, UK, 2016-2024

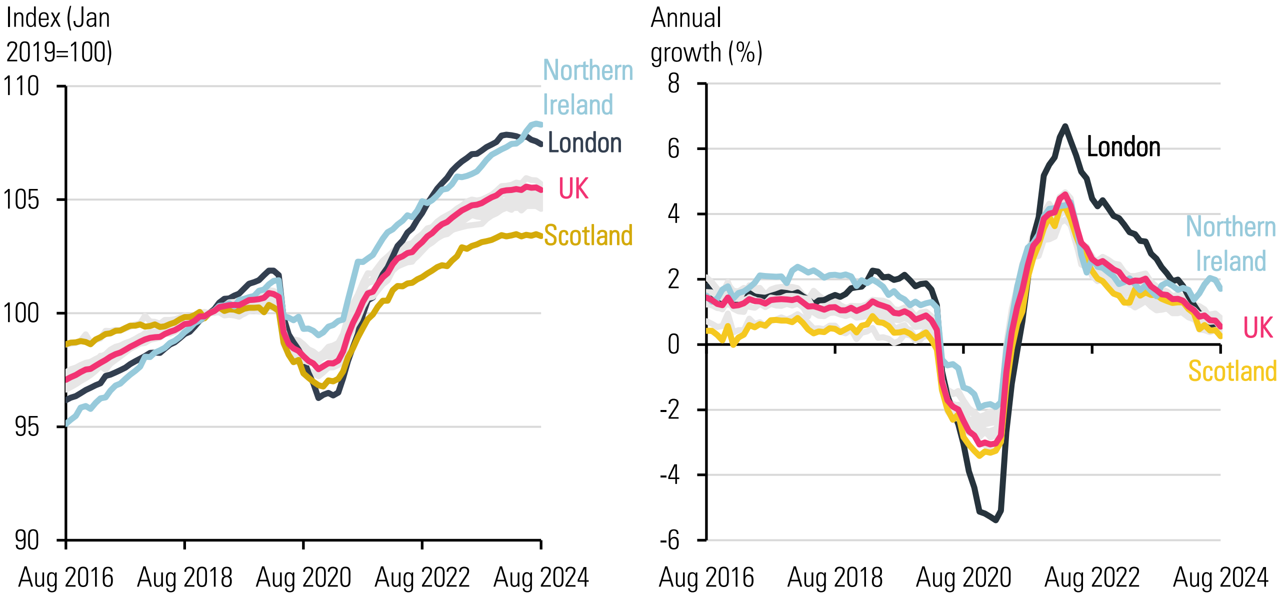


Source: LPC estimates using HMRC data: RTI payrolled employees by age, seasonally adjusted, monthly, UK, August 2015 - August 2024.

2.11 The number of RTI employees aged 25 and over was hardly affected by the pandemic, and we have seen levels continue to grow over recent years. The rate of growth has slowed somewhat, however, falling from two per cent in the year to August 2023 to just one per cent twelve months later.

Northern Ireland employment is resilient as growth slows for the rest of the UK

Figure 2.3: Indexed level (LHS) and annual change (RHS) in PAYE RTI employees by region/nation, UK, 2016-2024



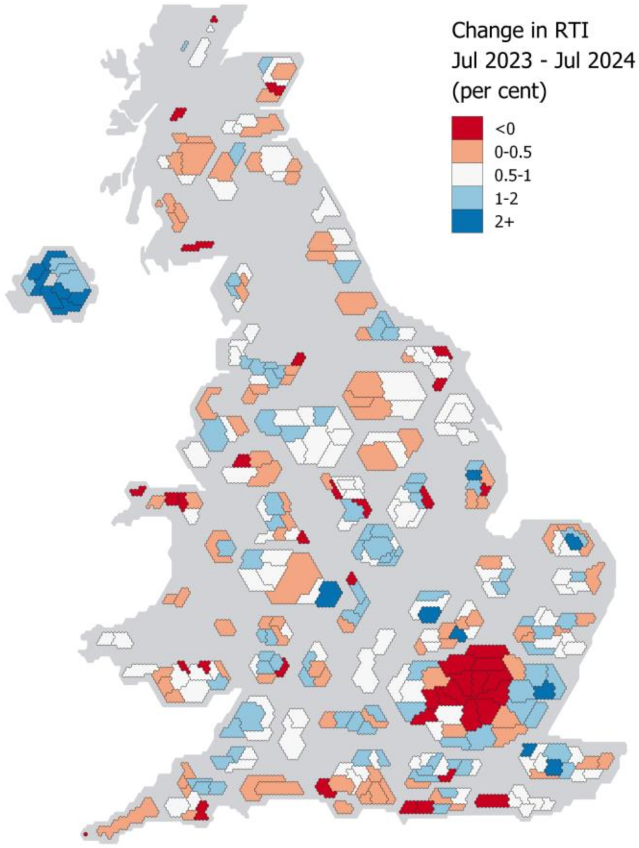
Source: LPC estimates using HMRC data: RTI payrolled employees by NUTS1 region, seasonally adjusted, monthly, UK, Aug 2015 - Aug 2024.

2.12 In the years prior to the pandemic, annual employment growth was highest in London and Northern Ireland at around two per cent, and lowest in Scotland and the North East at less than one per cent. London saw the largest drop in employment levels (5 per cent) during the pandemic but recovered strongly with growth over six per cent by early 2022. The rest of the UK saw employment fall by around 2-3 per cent followed by subsequent growth in the region of four per cent.

2.13 In recent years employment growth has slowed nationally, falling to just 0.5 per cent in the year to August 2024, lower than the pre-pandemic average. This is similar for all regions and nations except for Northern Ireland, where employment has continued to grow at close to two per cent for the last 18 months.

2.14 Employment growth varies within, as well as across, nations and regions as shown in Figure 2.4. Across the country there are pockets of local authorities where PAYE RTI employment fell in the year to July 2024. Much of London saw falls, as did parts of the South East, the Midlands, Wales and Scotland. Northern Ireland has appeared to buck this slowdown in employment growth with all local authorities growing by at least one per cent.

Figure 2.4: Annual change in PAYE RTI employees by local authority, UK, 2023-2024



Source: LPC estimates using HMRC data: RTI payrolled employees by local authority, seasonally adjusted, monthly, UK, July 2023-July 2024.

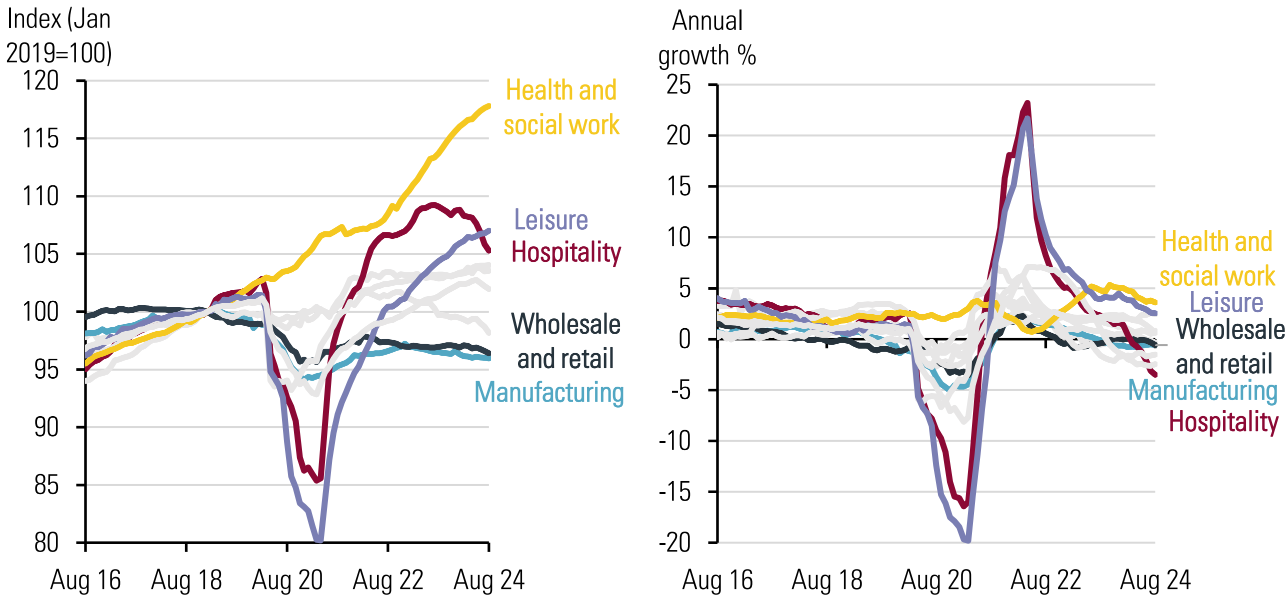
Health and social care employment continues to grow strongly while growth in consumer facing sectors slows or declines

2.15 In Figure 2.5 we show changes in levels of RTI employees by sector, highlighting the sectors where we find large numbers of low-paid workers. These illustrate both the polarising impact of the pandemic and the effect of recent business conditions on employment across sectors.

2.16 The health and social work sector has been the most resilient in recent years, both during the pandemic period and in the last twelve months. Employment in the sector is 15 per cent higher than in 2019 and was still growing at around 4 per cent in the year to August 2024. Most sectors have seen slow or even falling employment growth in the last twelve-month period. Both wholesale and retail and the manufacturing sectors entered the pandemic with falling employment and this trend has continued in recent times.

2.17 Leisure and hospitality were the two sectors most impacted during the pandemic as lockdowns restricted their ability to operate. But large employment falls during this period were matched by subsequent boosts during the recovery period. The last 18 months however have seen very different responses. Employment growth in the leisure sector, while slowing, has remained relatively strong, growing by 2.5 per cent in the year to August 2024. Hospitality on the other hand, despite employment levels still being five per cent higher than in January 2019, has seen a sharp recent drop, falling by 77,000 or 3.5 per cent in the twelve months to August 2024.

Figure 2.5: Indexed level (LHS) and annual growth (RHS) in PAYE RTI employees by sector, UK, 2016-2024



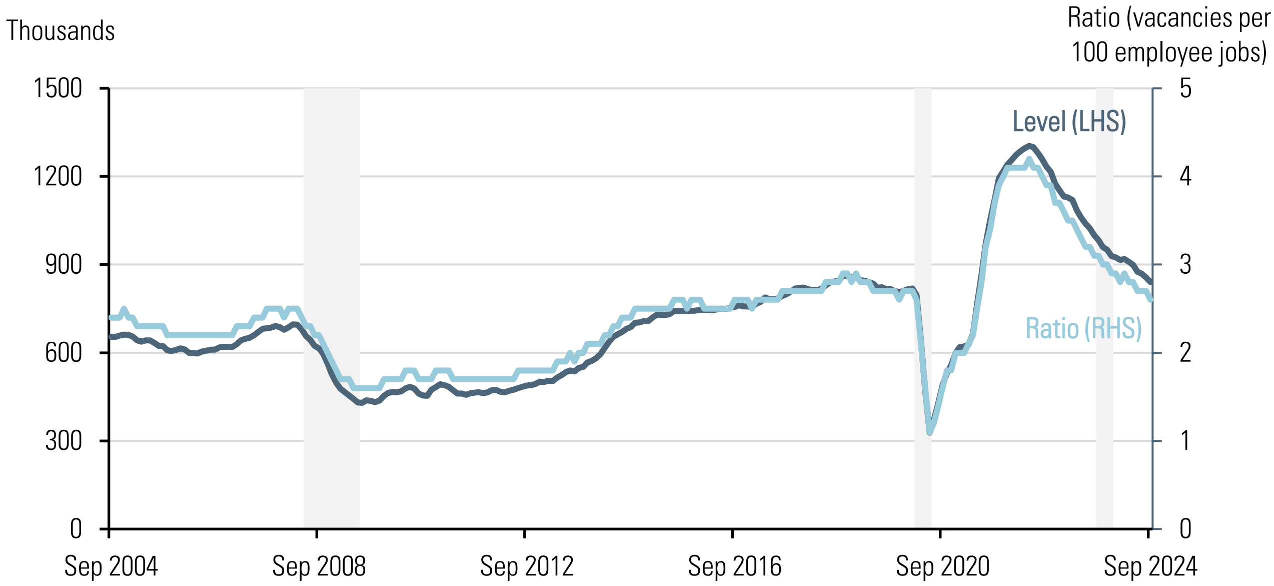
Source: LPC estimates using HMRC data: RTI payrolled employees by industry, seasonally adjusted, monthly, UK, August 2015 - August 2024.

Demand for labour continues to fall and recruitment difficulties are beginning to ease, but shortages remain

2.18 The slowdown in employee growth is at least partly explained by a reduction in job vacancies, which indicate the extent to which firms are hiring. As the UK economy emerged from the pandemic the unprecedented levels job vacancies suggested high demand for workers. At first this may have been a reaction to a dramatic reduction in hiring during the pandemic, but vacancy levels soon rose well above pre-pandemic levels, peaking in spring 2022.

2.19 However, reported job vacancies show month on month reductions for 28 consecutive months up to September 2024. Vacancies have fallen by 463,000 from their peak of 1.3 million in May 2022. Figure 2.6 shows however that vacancy levels (841,000) and rates (2.6 per 100 employee jobs) in September 2024 were around their pre-pandemic highs of 2019, a period when the labour market was considered ‘tight’.

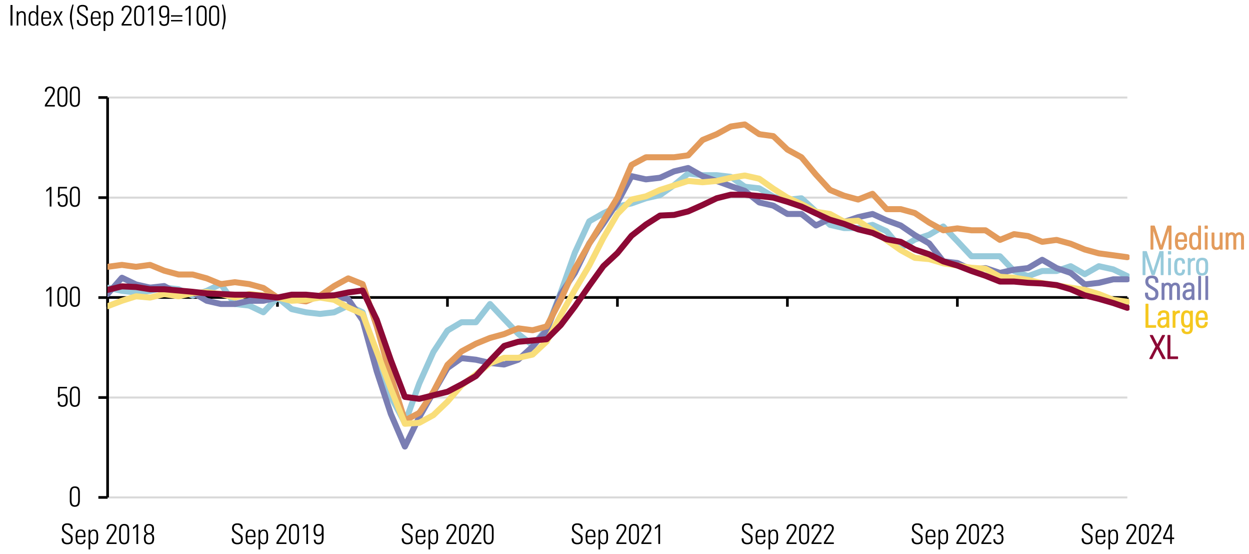
Figure 2.6: ONS Vacancies, UK, 2004-2024



Source: LPC estimates using ONS vacancies (AP2Y and AP2Z), seasonally adjusted, monthly, UK, September 2004 - September 2024.

2.20 Vacancies in large (250+ employees) and very large employers (2500+ employees) appear to have returned to 2019 pre-pandemic levels. Micro (0-9), small (10-49) and medium (50-249) sized firms' vacancies, while falling in the last year remain above 2019 levels.

Figure 2.7: ONS Vacancies by firm size, UK, 2018-2024

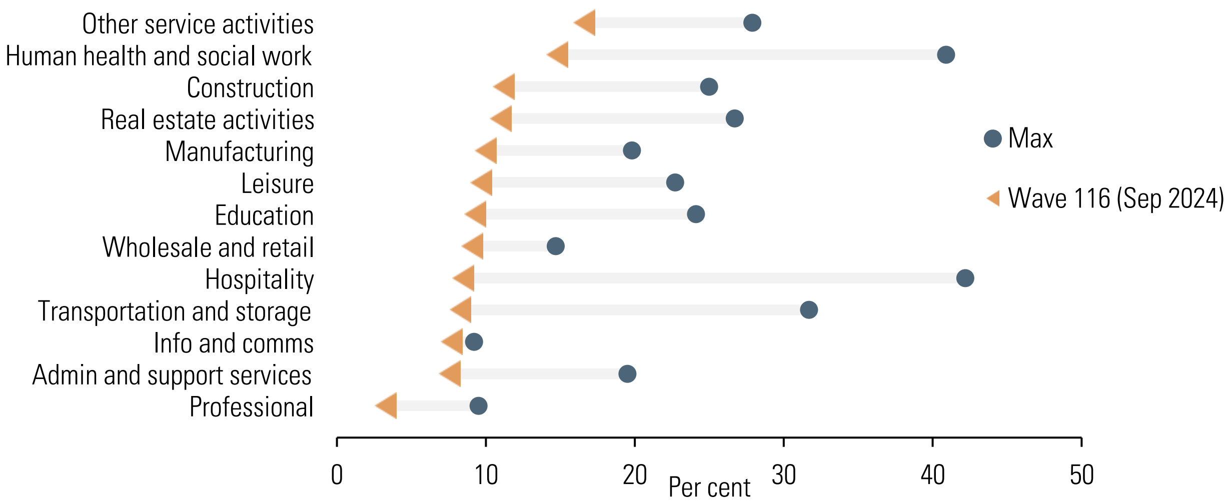


Source: LPC estimates using ONS vacancy data by firm size (ALY5, ALY6, ALY7, ALY8 and ALY9), seasonally adjusted, monthly, UK, September 2018 - September 2024.

2.21 As demand has eased, vacancies have fallen, as have reported staff shortages. Figure 2.8 compares the proportion of firms reporting staff shortages in September 2024 to the peaks in 2021 using data from ONS' Business Insights and Conditions Survey (BICS). This data is representative of all businesses across the UK and so is weighted more towards small firms who comprise the majority of businesses in the economy.

2.22 While all sectors have seen falls, the largest have been in the low-paying sectors of hospitality, health and social work, and transportation and storage. Around one in ten firms in most sectors in September 2024 said they still had worker shortages – although in health and social work the rate is higher at 15 per cent.

Figure 2.8: Worker shortages by sector, BICS, UK, 2021-2024

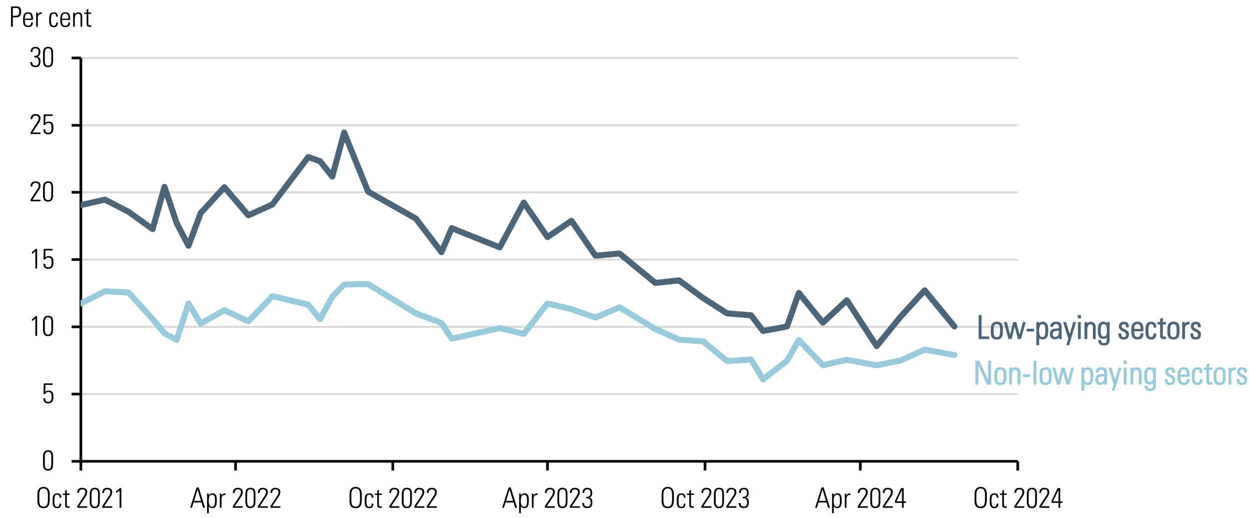


Source: LPC estimates using ONS BICS data, Waves 42-116, October 2021- September 2024.
Note: The BICS survey asks firms "Is your business currently experiencing a shortage of workers?"

2.23 Figure 2.9 shows that while firms in low paying sectors are more likely to report worker shortages than those in non-low paying sectors, the gap has narrowed (see Appendix 3 for sector definitions). It also shows that after falling in 2023 the share of firms stating they have worker shortages remained relatively flat across 2024 – albeit with some variation across low-paying sector firms. When considering this alongside a period of falling vacancy numbers it could suggest some firms are choosing to carry vacancies and operate with fewer staff. The Recruitment and Employment Confederation (REC) said that between the election and the autumn budget many employers were taking a 'wait-and-see approach' to hiring, following a decline in job posting data in September 2024 taken from their Labour Market Tracker (2024).

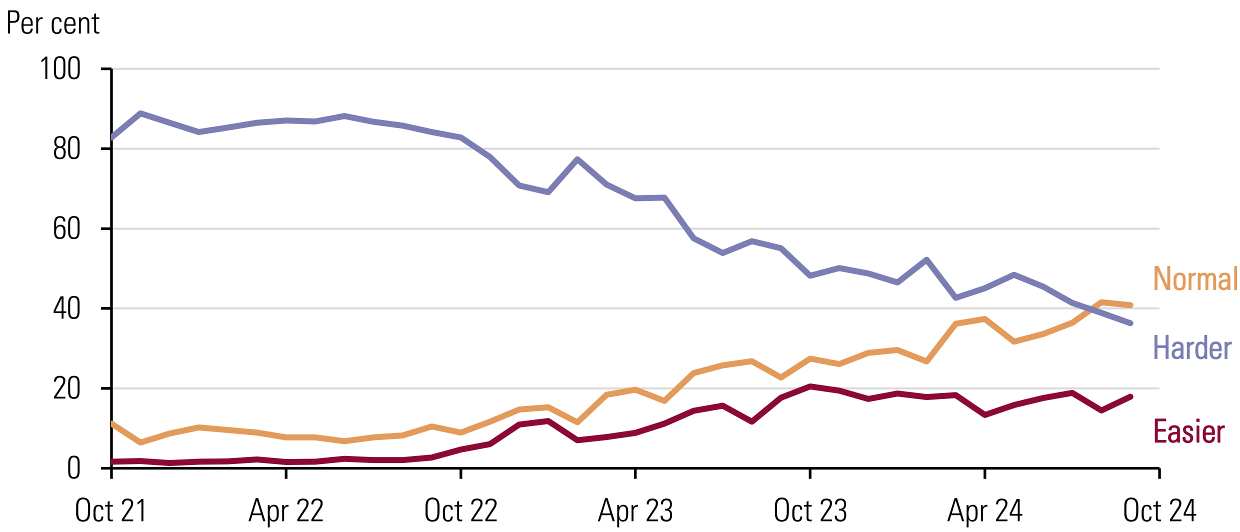
2.24 This easing of recruitment difficulties is shown in Figure 2.10, which shows data from the Bank of England Decision Maker Panel (2024h), a survey of over 2,000 UK firms with 10 or more employees. In the last 18 months, there has been a convergence in the share of firms saying recruitment is "normal" and those saying it is "harder" than normal. In September 2024 for the first time more firms thought recruitment was back to normal (41 per cent) compared to harder than normal (36 per cent).

Figure 2.9: Share of firms with worker shortages, BICS, UK, 2021-2024



Source: LPC estimates using BICS microdata using ONS' Secure Research Service, fortnightly, UK, October 2021 – August 2024.
Note: The BICS survey asks firms "Is your business currently experiencing a shortage of workers?"

Figure 2.10: Ease of hiring compared to normal, UK, 2021-2024



Source: LPC estimates using Bank of England Decision Maker Panel data, UK, September 2024.
Note: Figures do not sum to 100 as excludes firms responding 'not applicable - not recruiting at the moment'.

Employer groups agree that recruitment remains difficult and only easing because demand for labour is declining

2.25 The Confederation of British Industry (CBI) said businesses continued to report staff shortages constraining output and vacancies above pre-pandemic levels (albeit "more acute in fewer sectors"). It said shortages had eased primarily because of weak demand, rather than businesses being able to find the staff they need. In its survey (carried out in August and September), 58 per cent of firms saw access to labour as a threat to competitiveness that would remain over the next five years. The CBI said long-term demographic pressures mean "it seems highly unlikely that there will be a return to the pre-pandemic trend of modest year-on-year increases in the size of the labour market."

2.26 Likewise, UKHospitality (UKH) estimated that a lower vacancy rate had helped to ease recruitment issues, although there was still a "hot, tight labour market […] for certain skilled roles" such as chefs. The British Beer and Pub Association (BBPA) agreed the labour market was better than 12 months ago but quality of staff and availability particularly in kitchens were still an issue.

2.27 The Recruitment and Employment Confederation (REC) said: "labour market activity continues to be dampened by skills shortages and economic uncertainty. Fuelled by high inflation and interest rates, labour market activity has seen a gradual decline generally since the beginning of 2022." The British Retail Consortium (BRC) noted that there were 25.8 per cent fewer vacancies and 200,000 fewer jobs than before the pandemic.

2.28 The British Chambers of Commerce's (BCC) survey found that in Q1 2024, 66 per cent of firms who had recently tried to recruit had faced difficulties, down from the 76 per cent in the preceding quarter. For the Association of Convenience Stores (ACS), the labour market was "slightly looser" than in recent years, but the sector had "got used to a baseline of probably understaffing". Make UK told us that recruitment and retention had improved, with lower labour turnover and higher success rates in filling vacancies. Technical skills shortages remained the biggest barrier to recruitment and the increase in the salary threshold for skilled worker visas was expected to negatively impact the ability to fill vacancies in certain occupations.

Unions acknowledge weakening labour demand but note the labour market remains strong and could be strengthened by good policy

2.29 The TUC noted the strength of the labour market since the pandemic, but also "early signs of loosening … It is important that the government takes appropriate action to sustain employment. The ongoing strength of the labour market will depend on government investment, consumer confidence and demand, and the state of the healthcare system."

2.30 Other unions argued low unemployment and strong nominal pay growth demonstrated labour market resilience. Unite showed median pay awards holding steady around 5 per cent. Unison pointed to the long-term picture of low unemployment rates and robust vacancies rates, including in low-paying sectors. They argued that even with a slight upturn in unemployment, there remained ample scope for minimum wage increases. Usdaw noted that several major retailers had been actively recruiting more staff and whilst the unprecedented tightening of the labour market post-pandemic had eased slightly, by historic standards employment, including youth employment, remained extremely strong.

Labour shortages are constraining growth and intensifying work

2.31 The CBI argued that the tightness of the UK labour market set a cap on growth: "growth is returning. But businesses know the UK no longer has a labour market capable of supporting it … when demand does pick up… [current LFS inactivity levels] suggests businesses will again not have access to enough people to grow." The British Chambers of Commerce (BCC) also told us that recruitment problems limited growth and harmed job quality (and ultimately retention) for remaining staff. Likewise, the SWC argued that Brexit and the loss of EU labour intensified low-paid work: "the reduction in staff pools has placed increased pressure on remaining UK-based staff, particularly in hospitality and social care roles. These sectors have a majority women workforce, ultimately disproportionately impacting women workers."

2.32 Unite identified vacancy rates and resultant short staffing in hospitality as an important issue for their members, with workloads going up and serious issues with retention linked to low wages and poor working conditions. Hospitality Ulster spoke of a rise in self-employment models and a move towards cash wages for chefs and other skilled hospitality workers. A BBPA survey found more members this year talking about "deskilling their kitchens" by taking out chef roles and buying food in.

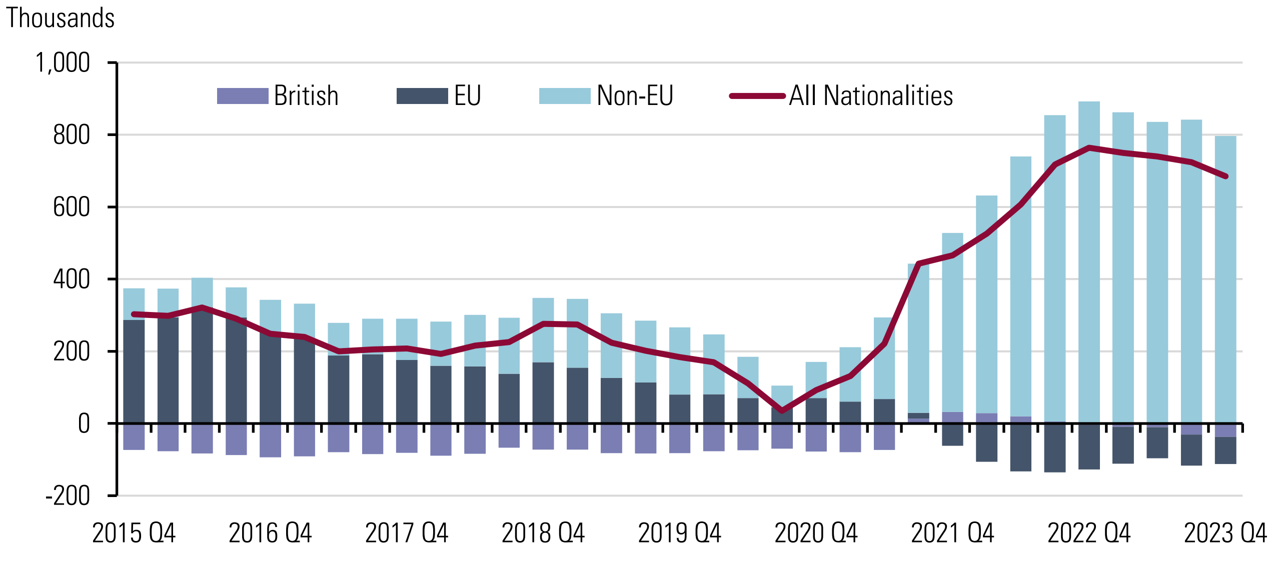
2.33 A group of hotel owners we met on a regional visit told us that the shortage of experienced workers had created productivity issues, leading to a rise in headcount while turnover dropped, as the hotel had to recruit more less experienced workers. "It's more of an onus on the business to train that person up. But you're still paying that person that same salary you would have paid somebody back in the days." This means "we currently probably have now 20 per cent more heads in the hotel … we used to run the hotel with 35 people, we now probably have closer to 50 people in one hotel … The payroll is probably 30 per cent more than before, but the turnover is probably only about 15 per cent more."

Overseas workers have plugged employment gaps but policy changes will likely reduce numbers

2.34 Workers from abroad play a significant role in the UK labour market. Since the decision in 2016 to leave the EU, net migration from the EU started to fall, to be replaced by increasing numbers of immigrants from outside the EU. In the year ending December 2023 there were over 1 million non-EU arrivals (both visa holders and their dependents), accounting for 85 per cent of total immigration. Of that total, non-EU immigration for work-related reasons was 423,000 in 2023, an increase from 277,000 in the year ending December 2022, overtaking study as the main reason for long-term migration.

2.35 Figure 2.11 shows provisional total net migration figures for the year ending December 2023 were 685,000, down from high of 764,000 a year previous. The net flow of non-EU nationals was 797,000. The recent trend of more EU nationals leaving than arriving continued (net migration was -75,000).

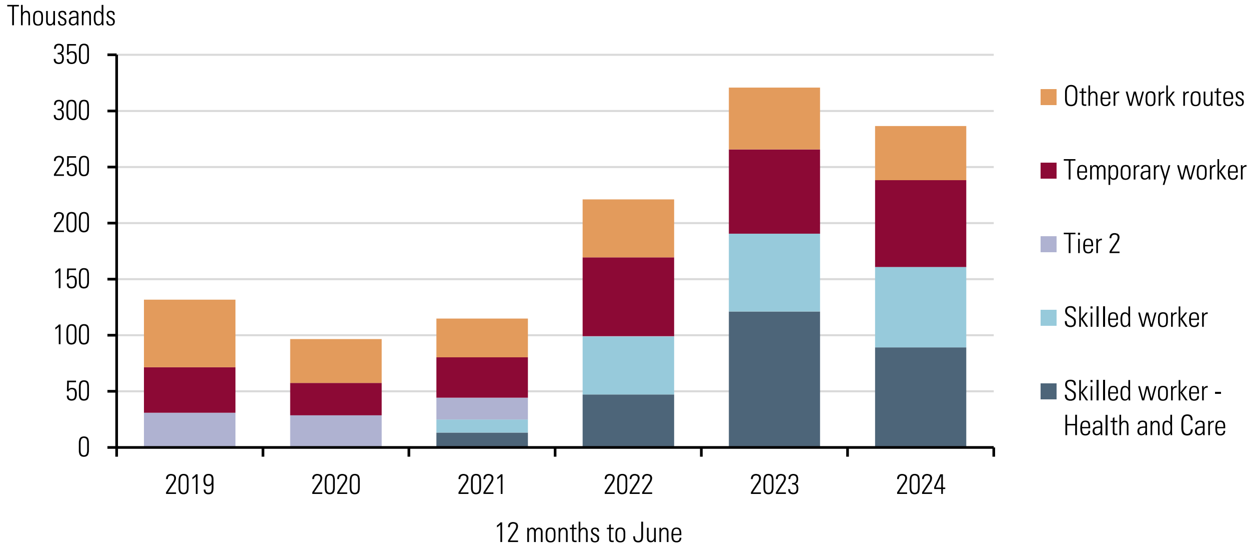
Figure 2.11: Long-term international net migration by nationality, 2015-2023



Source: LPC estimates using ONS long-term international migration data, provisional: YE June 2012 to YE December 2023.

2.36 Stakeholders told us how the agriculture and social care sectors increasingly rely on labour from outside the UK via targeted visas. Figure 2.12 shows how visa numbers for main applicants picked up sharply in the post pandemic period as old Tier 2 visas were replaced by more targeted routes, rising to over 300,000 in the twelve months to June 2023. The number of annual temporary worker visas, mainly used in the agriculture sector also doubled in number after 2021 to over 70,000.

Figure 2.12: Main applicant work visas granted by visa route, UK, 2019-2024

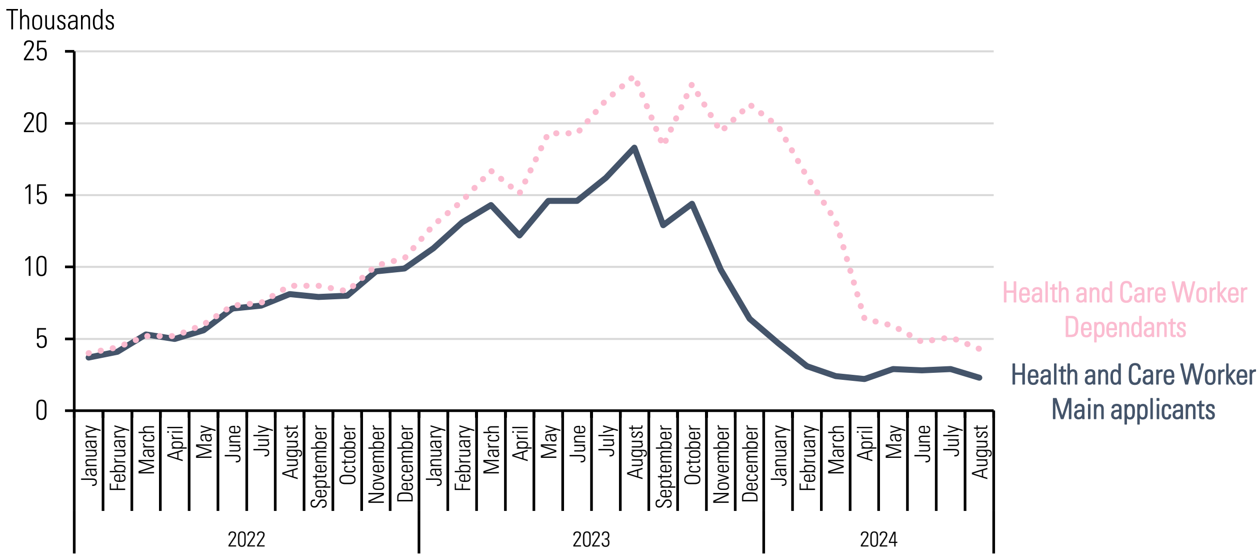


Source: LPC estimates using Home Office Immigration system statistics (Vis_D02), year ending June 2024.

2.37 Workers arriving on skilled worker and health and care visas were entitled to bring their dependents with them via dependent visas, meaning dependents were also entitled to work in the UK. Numbers of dependent applications increased sharply in 2023, overtaking those of main applicants, peaking at 23,000 in August 2023 as shown in Figure 2.13. However, in December 2023 the previous government announced a policy change to prohibit visas for health and care worker dependents from 11 March 2024. Since that announcement we have seen large falls in applications for these visas, though most of the fall in main applicants happened before.

2.38 The first half of 2024 saw other changes to UK immigration policy including 50% increases in the general salary threshold to £38,700. The Shortage Occupation List (SOL) was also replaced by a new Immigration Salary List (ISL) following recommendations from the Migration Advisory Committee (2024). As part of this change the 20% 'going rate' salary discount for occupations on the SOL was abolished – a move aimed to prevent employers undercutting domestic workers and the exploitation of migrant workers. Occupations on the new ISL will still receive a 20% discount – but from the new higher general salary threshold (subject to not reducing salaries below the occupation specific threshold).

Figure 2.13: Monthly Health and Care Worker main applicant and dependent visa applications, UK, 2022-2024



Source: LPC estimates using Home Office Monthly Entry Clearance Visa Applications (Monthly_Vis_01), August 2024.

The Work Rights Centre (WRC) argue the new migration system is a "bad deal" for both workers and employers.

2.39 The WRC argued that the new migration system "has thus far been a bad deal for all involved." Employers face significant administrative and cost burdens, while workers find themselves in "a lopsided relationship of dependency" with their employer. The Home Office faces a much greater compliance burden which the WRC argue it is not equipped to manage: "while the number of suspensions and revocations of sponsor licences by the Home Office increased slightly in the first quarter of 2024 relative to annual totals for the previous couple of years, this compliance activity has dropped significantly since before the Brexit referendum. At the same time, the number of sponsors has effectively tripled."

Agricultural employers depend on migrant labour and are pleased the Seasonal Agricultural Workers Scheme (SAWS) scheme will remain but are concerned about minimum working hours requirements

2.40 Employers we spoke to in agriculture tended to rely on the seasonal worker visa. Only 24 per cent of NFU members expected sufficient availability of permanent domestic labour and the same share expected enough seasonal workers to be recruited via the visa scheme. For NFU members, the scheme was "very useful … I don't know how horticulture would survive in Northern Ireland [without it]." One farm owner we met described how many of the farm's production decisions had been driven by an effort to work around the six-month visa and regularise the labour it needed over this period. The Horticultural Trades Association (HTA) told us that SAWs workers made up around a third of their sector's Full-time equivalent (FTE) labour input. They welcomed the May 2024 announcement of an extension of the scheme for five years.

2.41 NFU Scotland members had concerns about costs, with businesses seeing the requirement of a minimum of 32 hours of work as a downside: "they have to pay regardless of whether they have got that level of work, they'll certainly have it most of the time, but there's some weeks they don't and they still have to pay that." Another factor increasing the cost of SAWs staff was that a leading retailer-imposed audit now specified that farms had to cover workers' recruitment and visa costs, when previously workers had covered these. One NFU Scotland member was concerned this would lead to more staff absconding: "because they've invested in getting here it means they're more committed to work. And I would be concerned that, if we had to cover that cost, it would be financially and you'd probably have a bigger number of people coming over who think 'it's not cost me anything to get here.'"

2.42 The Association of Labour Providers (ALP) noted that a significant proportion of UK food growers and manufacturers reported that they had rationalised or reduced their output due to labour shortages. 16 per cent of respondents to ALP's May survey reported doing this in the last six months, although this had fallen from 25 per cent in November 2023 and 49 per cent in May 2022.

Inactivity appears to have been rising, reducing labour supply, but it is hard to measure with certainty

2.43 Rising inactivity over the last few years is another factor limiting labour supply. This increase has received considerable attention, though measuring it accurately has proved difficult because of the issues highlighted with the LFS. In the aftermath of the great 2008 financial crisis, inactivity peaked at 23.6 per cent. Figure 2.14 shows it then began an almost decade long downwards trajectory, helped by increasing levels of female employment. It then picked up following the onset of the pandemic but has remained between 21 and 22 per cent in the last few years. However, unlike most international counterparts the UK has not seen inactivity return to its pre-pandemic trend of decline. Some stakeholders worry that higher levels of inactivity may restrict the capacity of the economy to grow.

Figure 2.14: Working age (16-64) inactivity rate, UK, 2011-2024

Source: LPC estimates using ONS data (LF2S), seasonally adjusted, monthly, UK, Aug 2011 - Aug 2024.

2.44 The Labour Force Surve suggests those inactive due to long-term sickness increased from 2.1 million in February 2020 to 2.75 million in August 2024 and is now the largest single inactive group, overtaking students (2.5 million). But comparisons with pre-pandemic levels are currently difficult to interpret – the ONS' re-weighting of LFS data only went back to the third quarter of 2022 (figures have increased by over 100,000 since this point), introducing a structural break to the time series.

2.45 Data from DWP also shows rising levels of health-related (incapacity and disability) benefit claimants since the onset of the pandemic. The working-age disability benefit caseload has increased by 39 per cent from 2.2 million in 2019-20 to 3.2 million in 2023-24 with those claiming incapacity rising by 28 per cent from 2.5 million to 3.2 million. However, this is not directly analogous to inactivity, as some claimants are working.

2.46 Concerns with the underlying LFS data should not be underestimated. Inactivity is simply one minus the participation rate (those not in or seeking employment as a proportion of the working age population). And so were the LFS to inaccurately record levels of employment and/or use out of date population projections to estimate totals it is conceivable that this could also result in imprecise inactivity levels and rates. Figure 2.2 showed the divergence of employment by different sources. It also showed the abrupt alignment of LFS and RTI measures of employment, possibly due to improvements in the LFS sample. This may also explain why inactivity fell in the final data point in Figure 2.14.

2.47 We know that the LFS has been undercounting total employment growth relative to alternative data sources. We also know that the current population projections being used to weight-up estimates within the LFS data are likely to be underestimating the true UK population. This has implications for rates as well as levels. If employment rates are currently lower than we might expect inactivity is likely being overestimated. But it is difficult to accurately state the extent of any error in these figures. Revisions to the LFS are likely to have implications to some degree for all measures of labour market levels and rates.

2.48 The ONS are planning a fuller re-weighting exercise of the LFS in 2025 using latest mid-year population projections. In conjunction with other measures already introduced we hope this will result in more clarity to better understand what is really happening within the labour market.

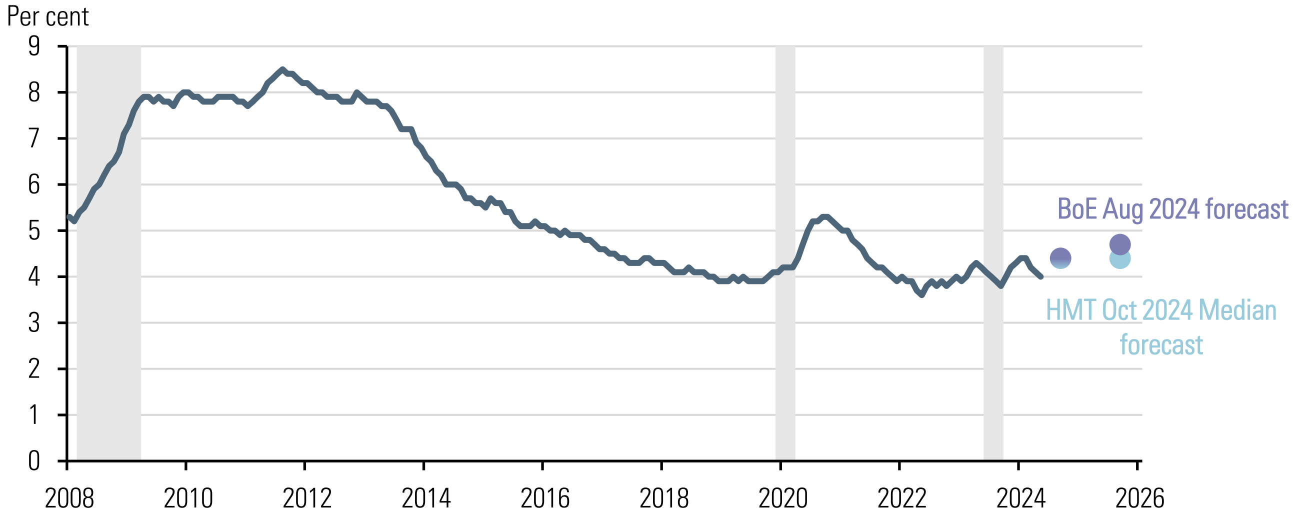
Despite falling demand for labour, unemployment remains close to recent lows

2.49 In August 2024 the estimated unemployment[1] rate stood at four per cent, close to its pre-pandemic low. Though, as it is derived from the LFS, this estimate has been volatile in recent periods. Forecasts from both the Bank of England (2024c) and HMT (2024j) are for unemployment to rise slightly, but stay close to historic[2] lows – reflecting softening but robust demand for labour.

[1] ILO definition of unemployment, which is someone who i) is not employed ii) available for work within two weeks iii) has actively sought work in the last four weeks or have found a job that starts in the next three months. Receipt of benefits (or not) has no bearing on whether someone meets this definition

[2] The unemployment rate fell to 4 per cent in 2018, the last time it had been this low before then was 1975

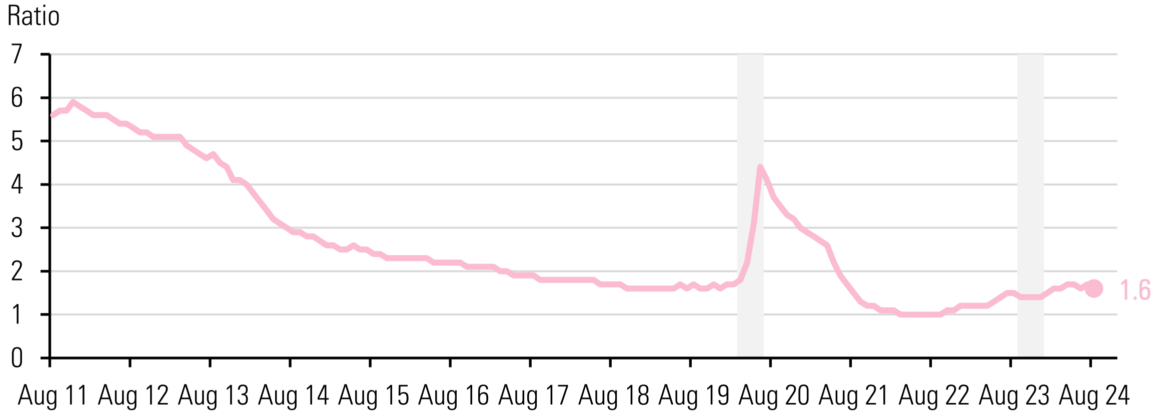
Figure 2.15: Unemployment rate and forecasts, UK, 2008-2025



Source: LPC estimates using ONS data (MGSX), Bank of England August 2024 forecasts and HMT panel October 2024 forecasts, UK, Apr 2008-2025 Q4.

2.50 Even with vacancies falling, the ratio of unemployed to the number of job vacancies in the economy remains low. Figure 2.16 shows how in 2022, a period of high labour demand, there was only one unemployed person per job opening. This is the lowest the ratio has been this century. As demand has softened, vacancies dropped and the pandemic effects unwound the ratio has increased - it was 1.6 in August 2024, similar to back in 2019, a period when the labour market time was considered to be relatively tight.

Figure 2.16: Unemployment to vacancy ratio, UK, 2011-2024

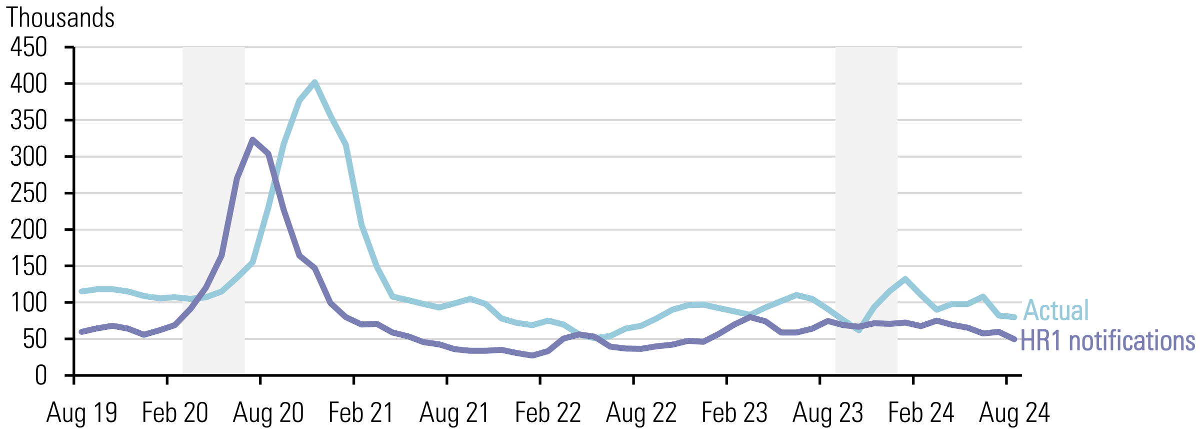


Source: LPC estimates using ONS unemployment (MGSC) and total vacancies (AP2Y) data, UK, Aug 2011 - Aug 2024.

Softening of labour demand has not yet fed into higher redundancies

2.51 In periods of uncertainty firms are more likely to freeze hiring and allow labour turnover to lower headcount – with redundancies often seen as a last resort. The latest redundancy data shows that firms are not planning to lay off workers in increasing volume. Figure 2.17 compares ONS recorded redundancy levels[3] with insolvency Service HR1 notifications – these are required from firms planning (but not necessarily making) 20 or more redundancies within a period of 90 days or less. It shows the strong relationship (albeit with a slight lag) between the HR1 notification data and the actual ONS outturn figures. Actual redundancy levels have remained close to 100,000 per quarter for the last couple of years. Latest HR1 notifications show little change in the months to August 2024, suggesting there will not be a spike in redundancies in the short term.

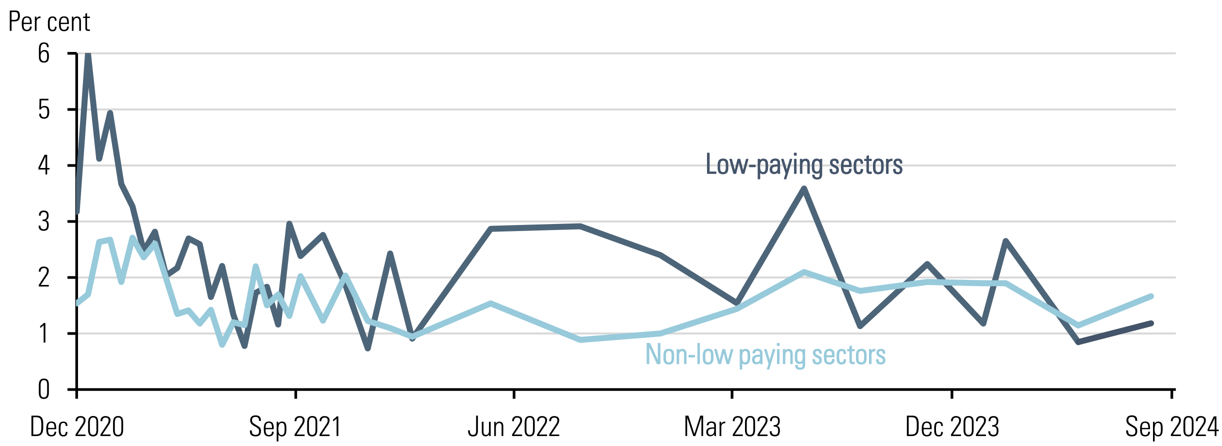
Figure 2.17: HR1 potential redundancy notifications and actual redundancies, UK, 2019-2024



Source: LPC estimates using ONS redundancy data (BEAO) and Insolvency Service HR1 notifications, UK, Aug 2019 - Aug 2024.
Note: Figures are for a rolling 3 month period.

2.52 Figure 2.18 shows there has also been no real change in the proportion of firms expecting to make redundancies in the next three months. This has remained between 1-2 per cent over the last year with no real difference in expectations between low-paying firms and other firms.

Figure 2.18: Firms expecting to make redundancies in next 3 months, UK, 2020-2024



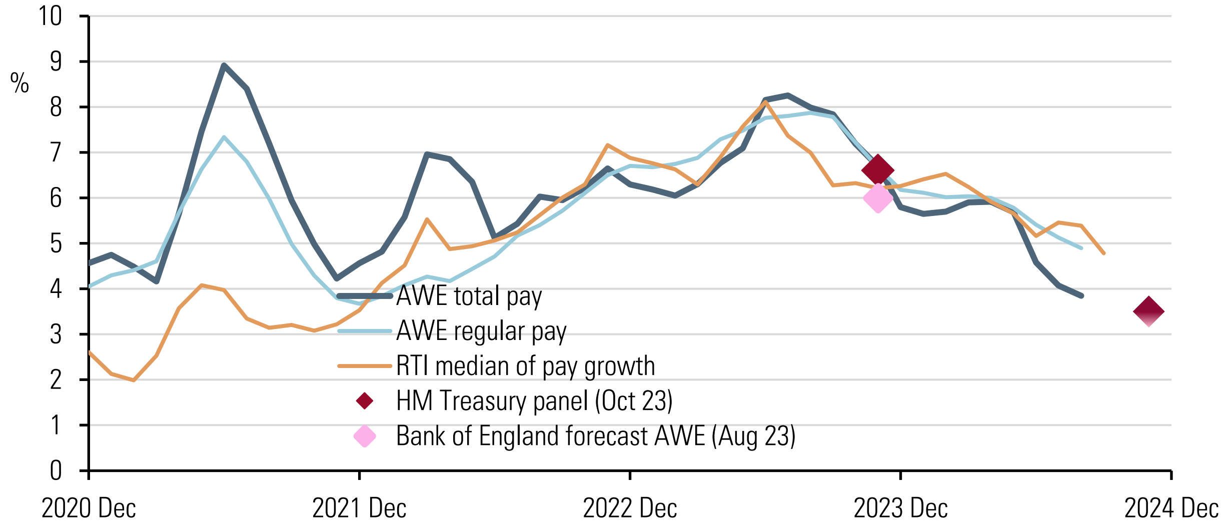
Source: LPC estimates using BICS microdata using ONS' Secure Research Service, fortnightly, UK, Dec 2020-Sep 2024.

[3] Defined as the number of people who say they were made redundant within the last 3 months in the LFS. This is separate to someone's labour market status, they can be employed, unemployed or inactive and have been made redundant in the previous 3 months.

The tight labour market has contributed to higher than expected wage growth

2.53 In autumn 2023, forecasters expected wage growth would almost halve from around 6.0-6.6 to 3.5 per cent between the fourth quarters of 2023 and 2024 as inflation slowed and the labour market loosened. However, pay growth has remained above the forecasts. Figure 2.19 shows that total pay – in dark blue – was heading towards the forecast 3.5 per cent at the end of 2024. But the drop in growth is caused by one-off payments to public sector workers boosting pay in summer 2023 and so lowering growth a year later. These bonuses will drop out of the annual comparisons as we move into the autumn of 2024 and total pay growth is expected to pick up again. Indeed, private sector and regular pay are not affected by these bonuses and remain above total pay.

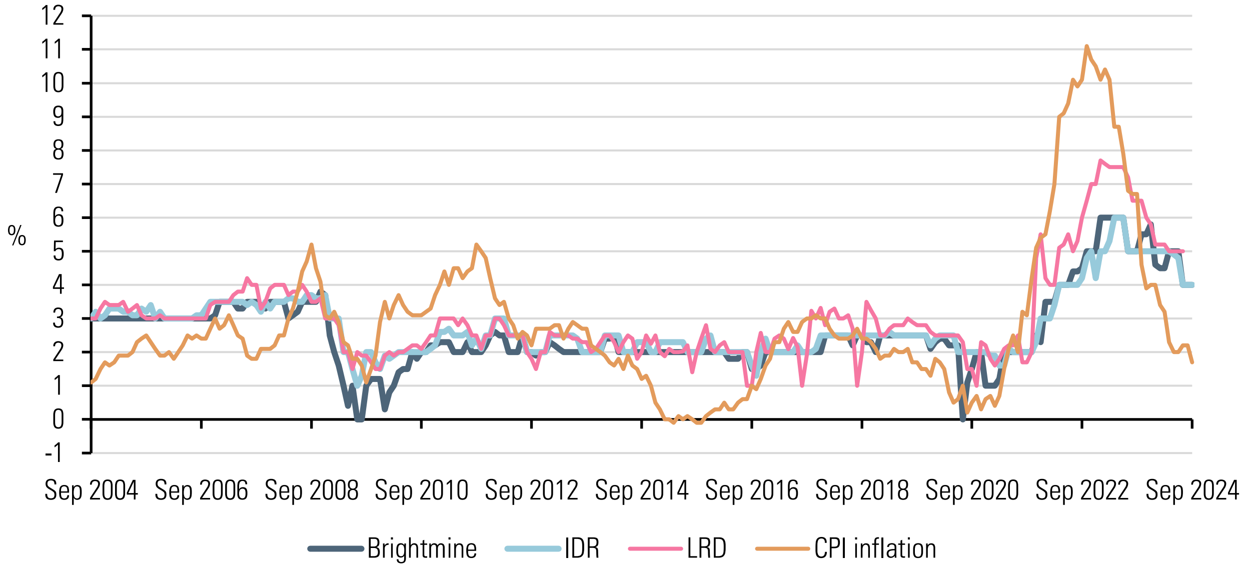
Figure 2.19: Annual change in average weekly wages, forecasts and out-turns, 2020-2024



Source: LPC estimates using ONS data, Dec 2020-Sep 2024, Bank of England forecasts Aug 2023 and HM Treasury panel forecasts Oct 2023.

2.54 As inflation accelerated in 2021 and 2022, pay settlements also increased but with a lag. As inflation slowed pay settlements were also expected to moderate, and have done so, but remain higher than pre-pandemic levels and pre-financial crisis levels, as shown in Figure 2.20. In autumn 2023 employers expected the median of pay awards to slow to 5 per cent in 2024, as shown in Figure 2.21. They have slowed a bit more than that – to 4 per cent – with fewer awards at 5 per cent than expected and more just under that – at 4.0-4.9 per cent. Despite that slowing, there were still more than one in eight awards that were 7 per cent or more.

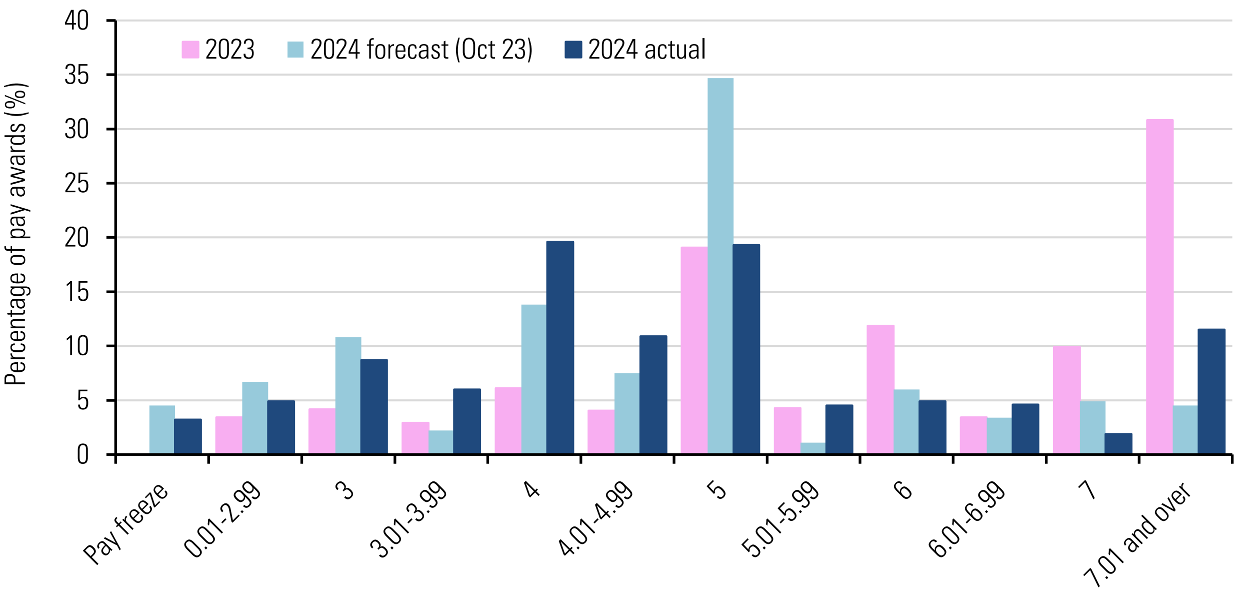
Figure 2.20: CPI inflation and annual change in pay settlements, 2004-2024



Source: LPC estimates using data from pay researchers and ONS, Sep 2004-Sep 2024.

2.55 Perhaps surprisingly, given the size of the increase in the National Living Wage, the pay settlement data have showed little differences across sectors in the last two years. According to Brightmine, pay awards in retail have been a little stronger than average in both years but those in hospitality have remained around the average for the whole economy.

Figure 2.21: Pay settlements, actual and forecast, by size of annual pay award 2023-2024

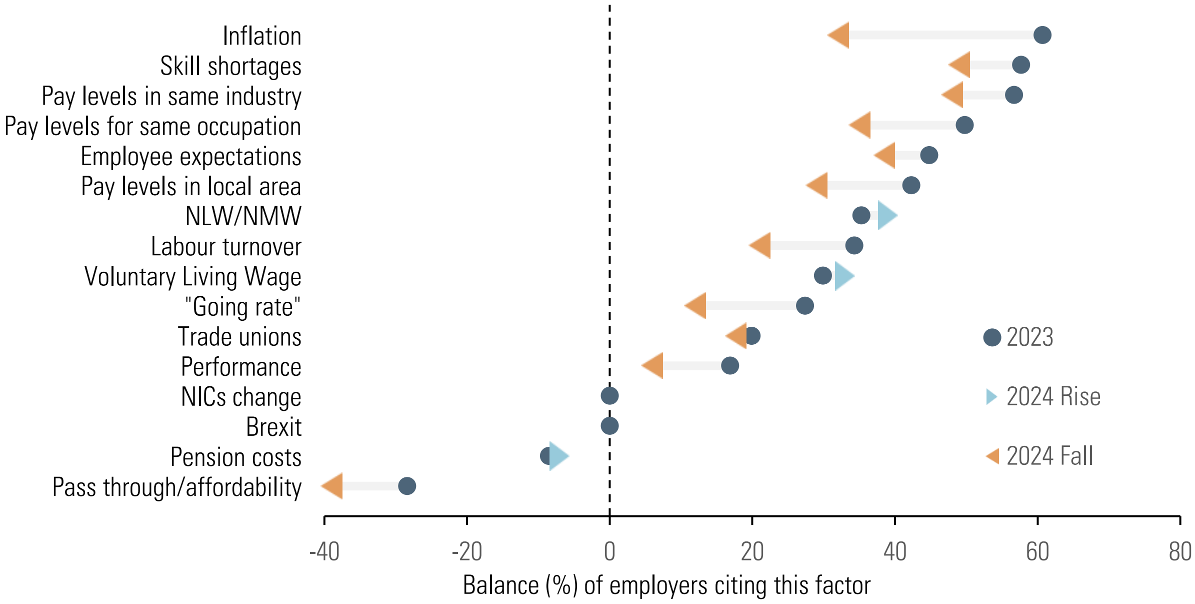


Source: LPC estimates using data from pay researchers, 2024.

2.56 Figure 2.22 explains why settlements have slowed, as many of the upward pressures on pay have reduced since 2023 with fewer employers citing inflation, labour shortages and market factors ("going rate", pay levels by industry and occupation) as driving their settlements higher. There is only slight upward pressure from the NLW, Living Wage and pension costs. As a result (Figure 2.23), both

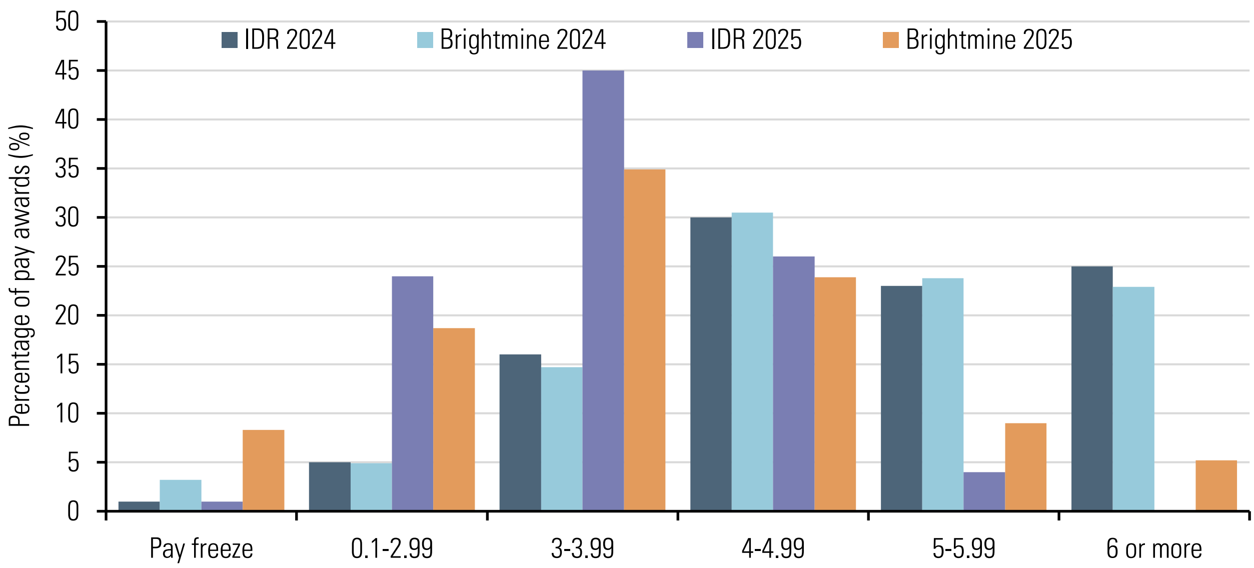
Brightmine and IDR expect a sharp reduction in pay awards of 5 per cent or more in 2025 with the median slowing to 3-4 per cent, while a quarter of deals are expected to be less than 3 per cent.

Figure 2.22: Drivers of pay settlements, 2023-2024



Source: LPC estimates using Brightmine data, 2024.

Figure 2.23: Pay settlements, actual and forecast, by size of annual pay award, 2024-2025



Source: LPC estimates using data from pay researchers, Brightmine and IDR, 2024-2025.

2.57 Average wage growth is also expected to slow in line with lower pay settlements. As shown in Table 2.1, forecasters are expecting average wage growth to slow as we move into 2025 and 2026. The median of the HM Treasury panel of independent forecasts has wage growth slowing to 3.6 per cent by the fourth quarter of 2025 and 3.1 per cent for the whole of 2026. The Bank of England has projected even weaker wage growth – at around 2.5 per cent in the fourth quarter of 2025 and less than 2 per cent for the whole of 2026.

Table 2.1: Actual and forecast wage growth, 2023-2026

HM Treasury panel and Bank of England (average wage forecasts)	Actual	Forecast		
	2023 Q4	2024 Q4	2025 Q4	2026 Q4
Median (whole economy AWE)	5.9	4.6	3.6	3.3
Bank of England (private sector)	6.3	5.0	3.0	2.8

Source: LPC estimates using data from ONS and forecasts from Bank of England and HM Treasury panel of independent forecasters.
Note: HMT panel forecast for 2026 is for the calendar year, all other forecasts are Q4 on Q4.

2.58 After a few of years of strong nominal wage growth, pay settlements and wages are likely to increase more slowly going forwards – with both pay settlements and wage growth expected to grow at around 3-4 per cent. However, with expected inflation lower, there is likely to be real wage growth over the next 18 months at least.

Conclusions

2.59 Continuing concerns with the Labour Force Survey make it difficult to accurately establish changes to employment, unemployment and inactivity. This is especially true for subsets of the data where smaller samples introduce greater volatility.

2.60 Aggregate employment growth using PAYE RTI has stagnated in 2024 although there is variation across ages, sectors and parts of the country. This is in line with falling demand for labour with vacancies back to pre-pandemic levels, though this was a period of tight labour markets. Despite this drop off in demand, unemployment is little changed and expected to grow only slightly, remaining at historically low levels.

2.61 Pay growth remains a positive story for workers. Although slowing over 2024 it remains higher than was forecast at 4-5 per cent. And falling annual increases in inflation has resulted in real-terms wage rises that are expected to continue for the next 18 months, despite pay growth projected to slow somewhat in 2025.

2.62 Taking all these metrics as a whole it is evident we have seen some loosening of the labour market in the last year. But looking historically we would still likely consider the current position as relatively tight with high employment, large numbers of vacancies and low levels of unemployment. There is, though, a degree of uncertainty in the economy – with many firms waiting to see how new government policies, particularly the forthcoming 2024 budget affect them.

Chapter 3

Who are minimum wage workers?

Key findings

- **Minimum wage coverage increased this year to 1.91 million but remains below pre-pandemic levels as a share of all eligible jobs.**
- **The largest increases in coverage this year were among demographic groups where levels of coverage were already relatively high –** For example, coverage increased noticeably for younger workers and older female workers.
- **The share of jobs in very large businesses that are minimum wage jobs increased from 4.9 per cent to 7.4 per cent in 2024 –** While coverage rates remain highest in micro businesses, very large businesses now account for more minimum wage jobs than other businesses.
- **Retail and hospitality were among the occupations with the largest increases in coverage in 2024 –** The number of minimum wage workers in retail increased by almost 100,000 to 360,000, and hospitality coverage increased by almost 40,000 to over 280,000. Hair and beauty occupations have the highest coverage rate at 40 per cent, up from 36 per cent in 2023.
- **There is significant cross-over between low pay and insecure work** – Worker testimony suggests that at its root, the insecurity of low-paid work is about working hours. Low-paid workers are more likely to work part-time or work on a zero-hours contract. They may face volatility in their pay and hours or simply be unable to work as many hours as they would like.
- **Workers tell us that features of the benefit system can exacerbate this insecurity** – especially where the benefits workers receive fluctuate from month to month. Although the benefits system influences people's work choices, in many instances it seems the rules are poorly or partially understood.
- **The pervasive sense of insecurity – as well as the fear of losing employment rights – make low-paid workers more averse to moving jobs** – feeding a common sense of "better the devil you know." Contributing to this, the training available to low-paid workers is often limited, which undermines their confidence in moving between occupations and seeking progression in different areas.
- **Other factors inhibit workers' agency as well** – The cost and availability of childcare is key in limiting employees' work choices (particularly for women). And a lack of transport options, especially outside cities, stops workers accessing jobs.

3.1 In this chapter we look in more detail at who minimum wage workers are. We look at how many workers are paid the minimum wage, their characteristics and changes that have occurred over the past year and since 2019. These topics are also covered in more detail for each rate population in Chapters 5, 6 and 7. We also look at the experience of low-paid workers, using examples heard directly from workers on our visits and from stakeholder evidence.

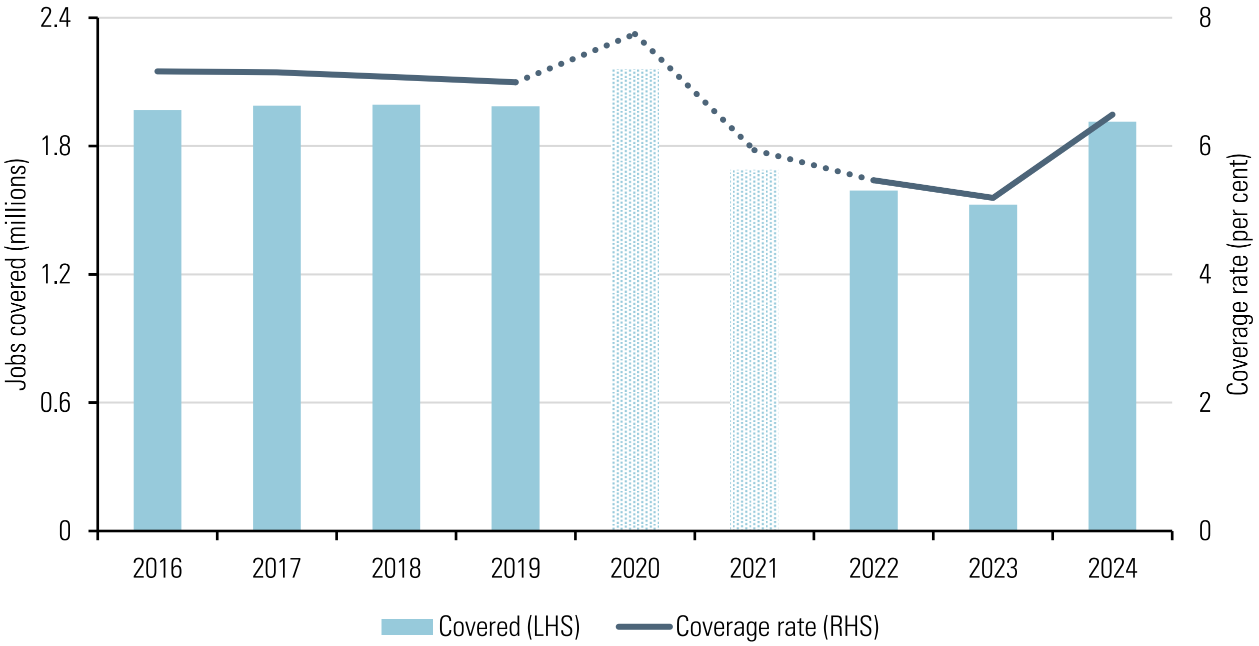
Coverage

Minimum wage coverage increased in 2024

3.2 The term coverage refers to the number of jobs paid up to 5 pence above the minimum wage (that applies to the person in that job). While the NLW applies to workers aged 21 and over, separate minimum wage rates apply to younger workers and apprentices. Coverage refers only to jobs done by employees, as self-employed workers are not eligible for the minimum wage. We measure coverage in terms of jobs rather than workers, as a worker could be employed in multiple jobs at different wage rates. We estimate coverage using data from the Annual Survey of Hours and Earnings, which provides a snapshot of pay in April of each year.

3.3 In 2024 we estimate total minimum wage coverage increased by 387,000 to 1.91 million jobs. This is the first meaningful increase in coverage since the NLW was introduced in 2016. (During the pandemic years, data issues and government support schemes made measuring coverage accurately impossible.) The coverage rate increased to 6.5 per cent in 2024, up from 5.2 per cent in 2023. Despite these increases, both the number and rate of minimum wage jobs remain below pre-pandemic levels. Between 2016 and 2019 the number of minimum wage jobs ranged between 1.97 and 1.99 million and the coverage rate was 7 per cent or higher.

Figure 3.1: Minimum wage coverage, UK, 2016-2024



Source: LPC analysis of ASHE, low-pay weights, chain-linked, UK, 2016-2024. Patterned bars/dotted lines indicate the period of the pandemic.

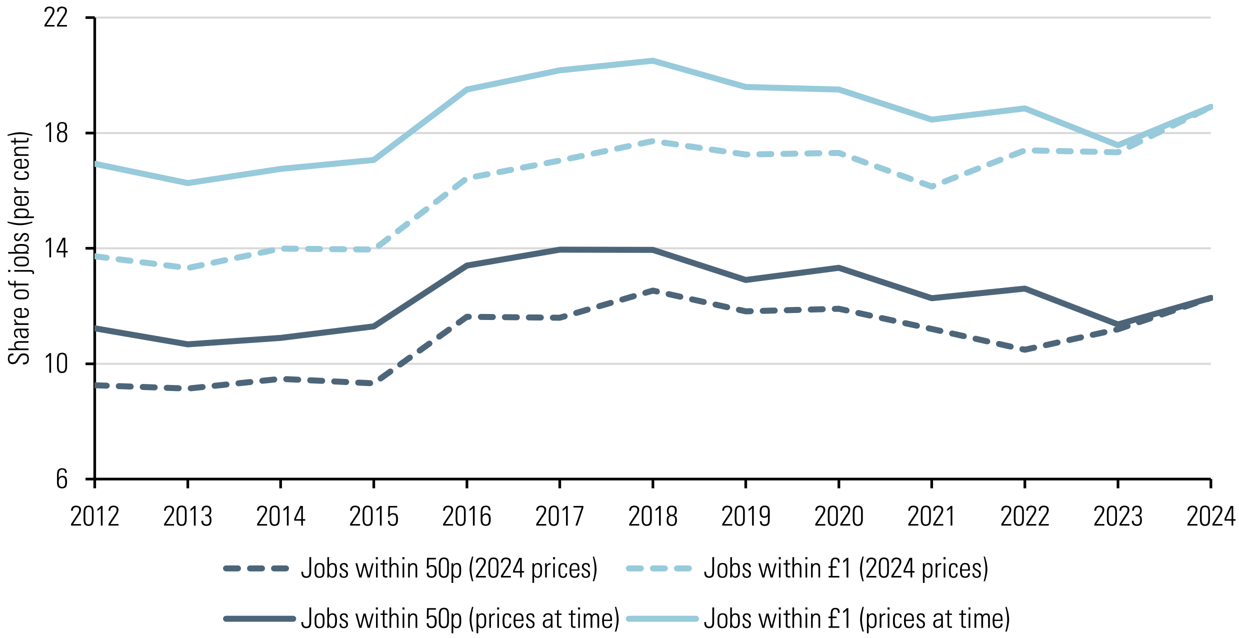
The number of jobs paid just above the minimum wage also continued to increase

3.4 Many employers do not wish to be seen as minimum wage employers and so will aim to pay close to, but above, the statutory minimum. Others need to pay above the minimum to attract and retain staff in a tight labour market. Setting rates above the required minimum can also reduce the risk of non-compliance. In the Chartered Institute of Personnel and Development's (CIPD) summer 2024 Labour Market Outlook survey, 30 per cent of employers said they paid above the minimum wage to avoid compliance problems.

3.5 In 2024 the number of jobs paying up to £1 above the minimum wage also increased by over 400,000 to 5.57 million. This represents 18.9 per cent of jobs, up from 17.6 per cent in 2023. This increase is entirely caused by the rise in coverage – the number of jobs paid between 6p and £1 above the minimum wage remained broadly flat.

3.6 We need to recognise, though, that inflation means £1 this year is worth less than £1 last year. Adjusting for this, the share of jobs paid up to £1 (in constant 2024 prices) above the minimum wage is the highest it has ever been (see the light blue dotted line in Figure 3.2). Similarly, the share of jobs paid up to 50p above the minimum wage also increased, to 12.3 per cent from 11.4 per cent (or 11.2 per cent in real terms).

Figure 3.2: Share of jobs paid just above the adult NMW/NLW, UK, 2012-2024



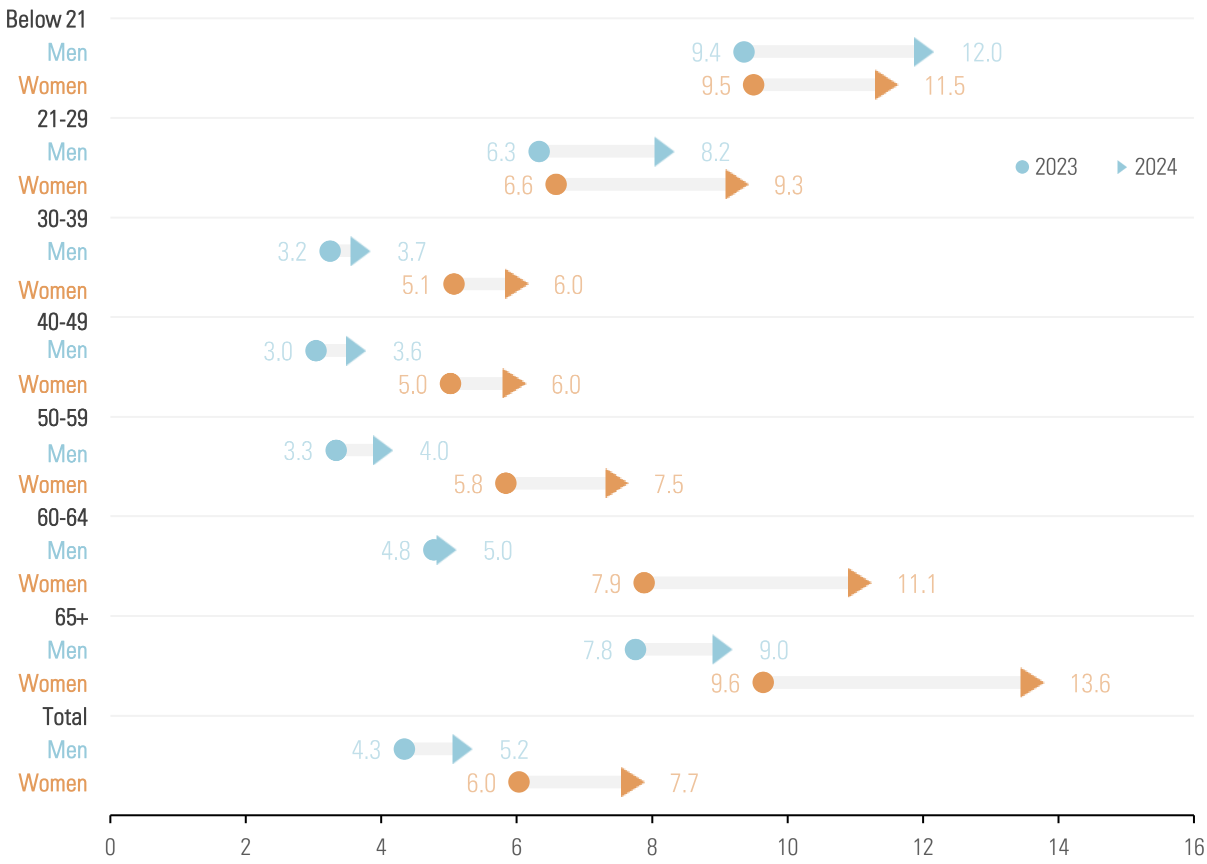
Source: LPC analysis of ASHE, UK, low-pay weights, 2012-2024. NLW eligible population refers to workers aged 25 and over before 2021, 23 and over from 2021 to 2023, and 21 and over in 2024, due to NLW eligibility change (excludes first year apprentices). Figures are chain-linked to adjust for methodology change in 2021.

Increases in coverage were generally larger for groups that already had relatively high rates of coverage

3.7 The largest increases in coverage in 2024 were generally seen among demographic groups that were already more likely to be covered. The coverage rate for women increased from 6 per cent to 7.7 per cent, equating to an extra 267,000 women working in minimum wage jobs. In contrast, the coverage rate for men only increased by 0.9 percentage points (equivalent to 120,000 jobs) to 5.2 per cent. However, since 2019 the number of women in covered jobs has fallen by 75,000, while the number of men in covered jobs is broadly the same.

3.8 Increases in coverage were also more pronounced among the youngest and oldest workers. Coverage rates for men under 21 increased from 9.4 per cent to 12 per cent, and for women under 21 increased from 9.5 per cent to 11.5 per cent. At the other end of the age spectrum the jump in coverage for women over 65 was particularly pronounced, increasing from 9.6 per cent to 13.6 per cent.

Figure 3.3: Coverage rates by sex and age, UK, 2023-2024



Source: LPC analysis of ASHE, low-pay weights, UK, 2023-2024.

Table 3.1: Number of employee jobs covered, by sex and age, UK, 2019, 2023, 2024

	Number of jobs covered (thousands)						Change (thousands)			
	2019		2023		2024		2019-2024		2023-2024	
	Female	Male	Female	Male	Female	Male	Female	Male	Female	Male
Under 21	94	86	71	66	82	79	-11	-7	11	13
21-29	225	176	178	172	253	210	28	35	74	38
30-39	258	157	179	117	217	134	-41	-23	37	16
40-49	254	129	168	96	204	114	-50	-15	35	18
50-59	267	117	181	97	235	118	-32	0	54	21
60-64	92	48	75	47	109	51	16	3	34	4
65+	46	38	42	37	62	46	16	8	20	9
Total	**1,236**	**751**	**894**	**632**	**1,161**	**752**	**-75**	**2**	**267**	**120**

Source: LPC analysis of ASHE, low-pay weights, UK, 2019-2024 chain-linked. Does not include employee jobs with missing gender or age data.

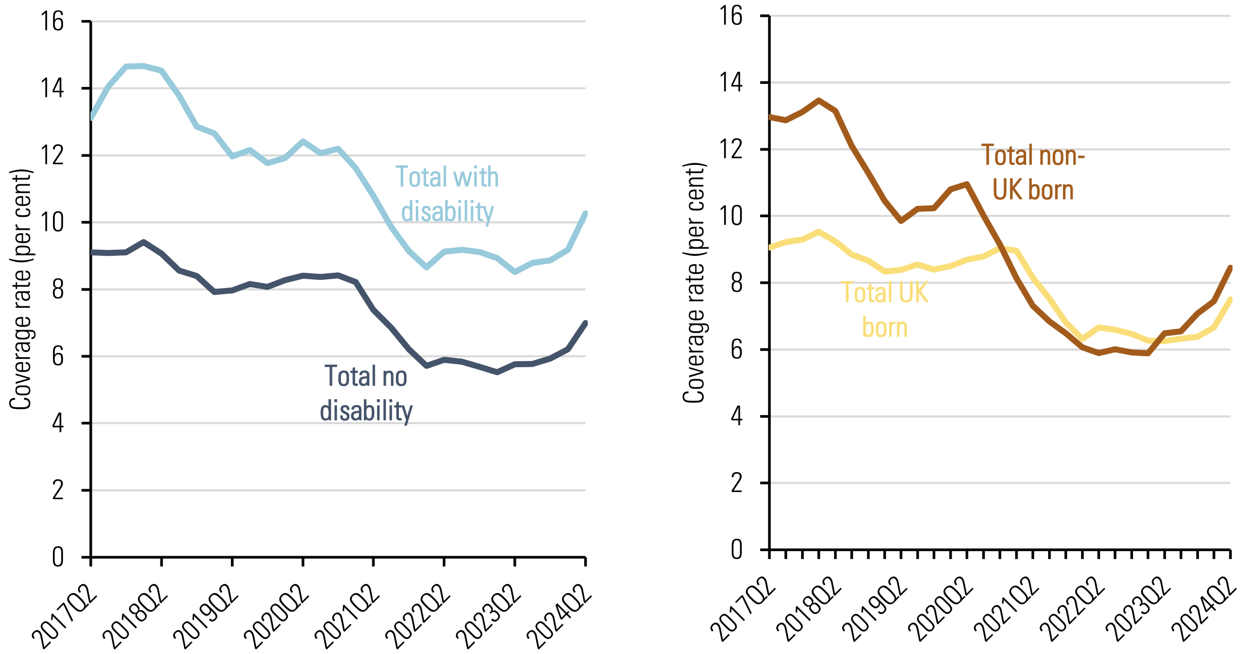
3.9 Several stakeholders reflected on gender disparities in pay and working conditions. The Women's Budget Group's submission noted Living Wage Foundation (LWF) evidence that women account for 59.5 per cent of jobs below LWF's living wage rates. They noted that women are also more likely to be part-time workers and more part-time jobs are below the LWF's rates than full-time jobs. Usdaw too argued that women's work is characterised by a one-sided experience of flexibility, a lack of parental and carer's leave options and a lack of affordable, accessible childcare. Unite argued a higher minimum wage could help close gender and ethnicity pay gaps. Women "are more likely to be trapped in lower-paid work and to suffer unequal pay gaps, poverty and income loss from austerity." UNISON advocated for the NLW to be pegged to male median earnings: "The 'all employee' figure incorporates the various factors that often drive down average wages for women."

3.10 While the personal characteristics reported in the Annual Survey of Hours and Earnings (ASHE) are limited, we can look at other characteristics of minimum wage workers using Labour Force Survey (LFS) data. The LFS includes information on workers' educational attainment, disability status, ethnicity and place of birth, among other characteristics. However, the sample size is smaller than ASHE and many respondents do not answer the questions on pay, or round their answers. This makes the pay-related data in the LFS less accurate than the ASHE data. Furthermore, since the pandemic, LFS data have become still more unreliable as sample sizes have dropped significantly. This is discussed further in Chapter 2. We should therefore be cautious before drawing any strong conclusions about particular demographic groups.

3.11 While coverage increased for workers both with and without qualifications this year, there was a noticeable increase in the gap in coverage between the two groups in 2024. During the pandemic period, coverage of workers without a qualification fell by almost 10 percentage points, narrowing the difference in outcomes with those with a qualification. This year, coverage of workers without a qualification increased by almost 5 percentage points, compared to a 1.3 percentage point increase for workers with qualifications.

3.12 Workers with a disability are around 50 per cent more likely to work in a minimum wage job than workers without a disability (right panel of Figure 3.3). Coverage for both groups increased this year – over recent years changes in coverage for disabled workers have tended to track changes in coverage for the rest of the population.

Figure 3.4: Coverage rates by disability status and country of birth, UK, 2017-2024



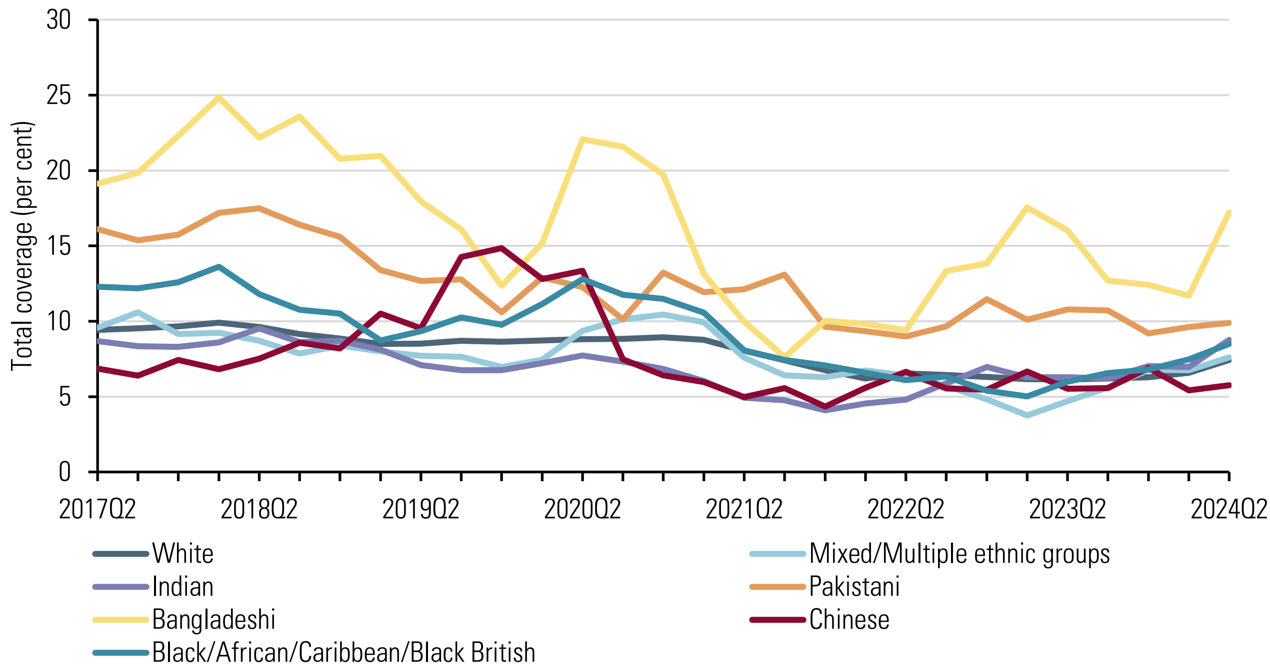
Source: LPC estimates using LFS microdata, imputed wage, quarterly, income weights, rolling four quarter average, not seasonally adjusted, UK, 2017 Q2-2024 Q2.
Note: Disability coverage figures use the LFS Discurr variable. This is different to analysis elsewhere in the report using the DISEA variable.

3.13 Respondents noted the disadvantages faced by disabled workers. Usdaw's evidence noted that disabled workers are more likely than non-disabled workers to say they feel financially worse off than five years ago (75 to 72 per cent) and to say financial worries are affecting their mental health (76 to 62 per cent). Unite's submission argued that: "Many disabled workers are part time workers and suffer a lot to make ends meet. They mainly don't say anything as they feel it will be hard for them to find another job that will be as accommodating."

3.14 The King's Trust (formerly the Prince's Trust) indicated that disabled people were more likely to be low-paid and have higher living costs. They cited research from Scope UK which found that "disabled households need an additional £975 a month to have the same standard of living as non-disabled households."

3.15 Since the beginning of the pandemic, coverage outcomes between UK-born and non-UK-born workers have broadly moved together. Prior to this non-UK-born workers were more likely to be covered. This year coverage rates increased for both groups, with a slightly larger increase for non-UK-born workers. Amongst various ethnic groups, workers of Bangladeshi or Pakistani backgrounds continue to have higher rates of coverage than workers from other backgrounds.

Figure 3.5: Coverage rates by ethnicity, UK, 2017-2024



Source: LPC estimates using LFS microdata, imputed wage, quarterly, income weights, rolling four quarter average, not seasonally adjusted, UK, 2015 Q4-2024 Q2.

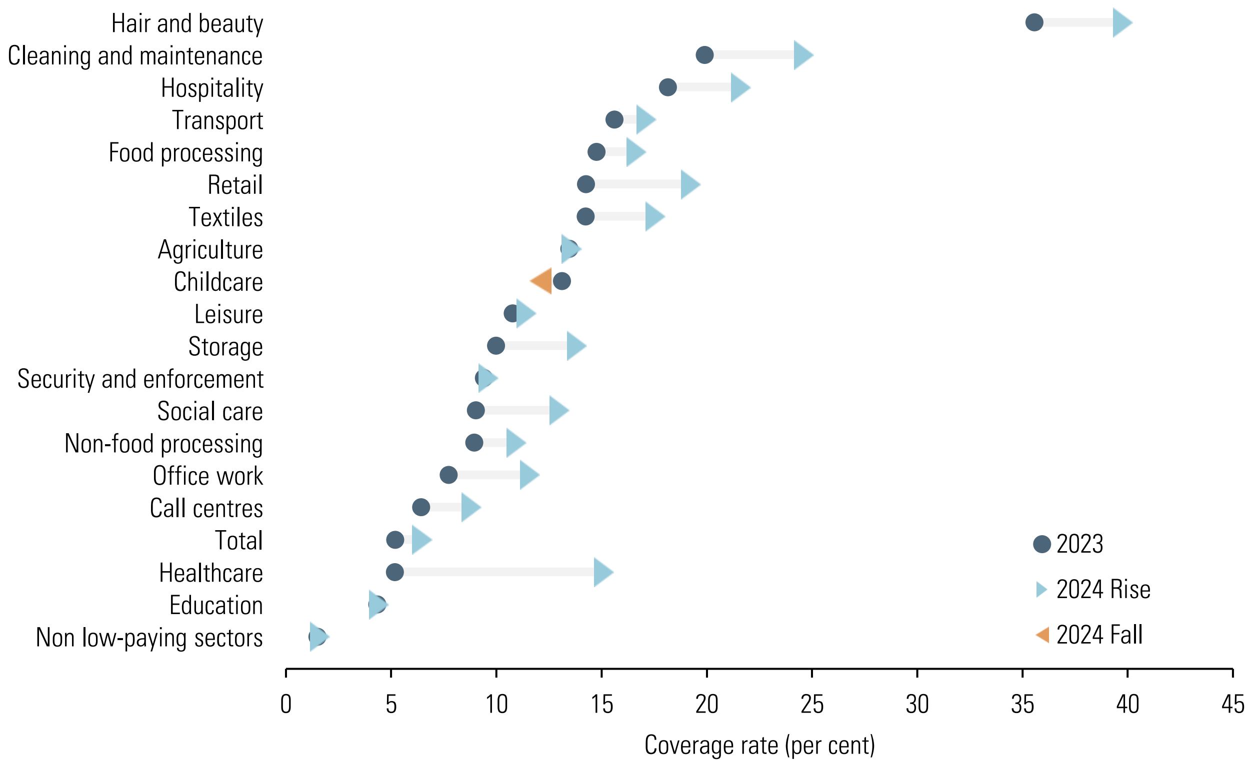
3.16 Usdaw noted that Black and Minority Ethnic (BME) workers continued to be "at the sharp end" of rising costs and were least likely to have the financial resilience to absorb further price increases. In Usdaw's cost of living survey, these workers are more likely to have relied on food banks in the last year (16 per cent) to feed themselves and their families compared to white workers (9 per cent), with this number increasing year on year compared with a slight drop for white workers. Unite noted "the positive role of the level of the NMW in addressing pay inequality gaps" for BME workers. The Scottish Women's Convention (SWC) noted their evidence-gathering showed that ethnic minority women "are often overlooked for promotions and are given low-skill tasks, notwithstanding ability or experience".

Coverage also increased by more in occupations with high coverage rates already

3.17 Historically, certain occupations have higher coverage rates than others. This year those occupations also registered larger increases in their coverage rates than occupations that had lower coverage rates in the first place. The share of minimum wage jobs in retail occupations increased by 5 percentage points to 19.3 per cent, representing nearly 100,000 more minimum wage jobs in retail. The number of minimum wage jobs in hospitality increased by 38,000, as the coverage rate in the hospitality occupation rose from 18.1 per cent to 21.6 per cent. Other noticeable increases in coverage rates were seen in social care, cleaning and maintenance, storage, and hair and beauty occupations.

3.18 Coverage rates also increased significantly (almost tripling) in healthcare occupations. However, as discussed in Chapter 5, we attribute much of this (measured) increase in healthcare coverage to delays in awarding NHS pay increases. These delays also contributed to, but were not wholly responsible for, the significant increase (around 120,000) in the number of public sector jobs paid at the minimum wage.

Figure 3.6: Coverage rates by occupation, UK, 2023-2024

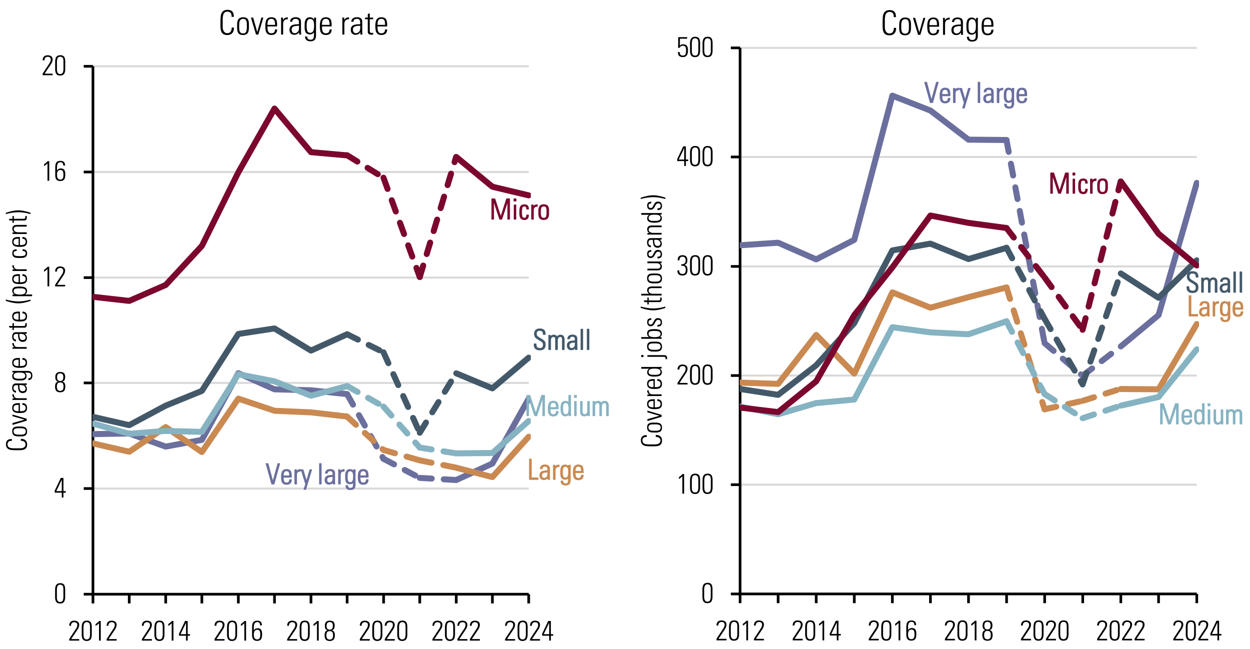


Source: LPC analysis of ASHE, low-pay weights, UK, 2023-2024.

There are now more minimum wage jobs in very large firms than micro firms

3.19 Coverage in the private sector increased by 250,000 in 2024, of which almost 230,000 were NLW jobs. Although the coverage rate remains highest in micro firms (those with fewer than 10 employees), this year the largest number of NLW jobs were found in very large firms (those with 2500 employees or more). The number of NLW jobs in very large firms increased by 121,000 to 377,000. In contrast the number of NLW positions in micro firms fell by 29,000 to 301,000. Pre-pandemic, very large firms consistently had more minimum wage jobs than smaller firms. However, as the labour market tightened after the pandemic, large firms paid above minimum wages in order to attract and retain staff. As the labour market has loosened over the past year, very large firms are employing more workers at the minimum wage again.

Figure 3.7: Coverage and coverage rates by firm size, private sector, 21+ population, UK, 2012-2024

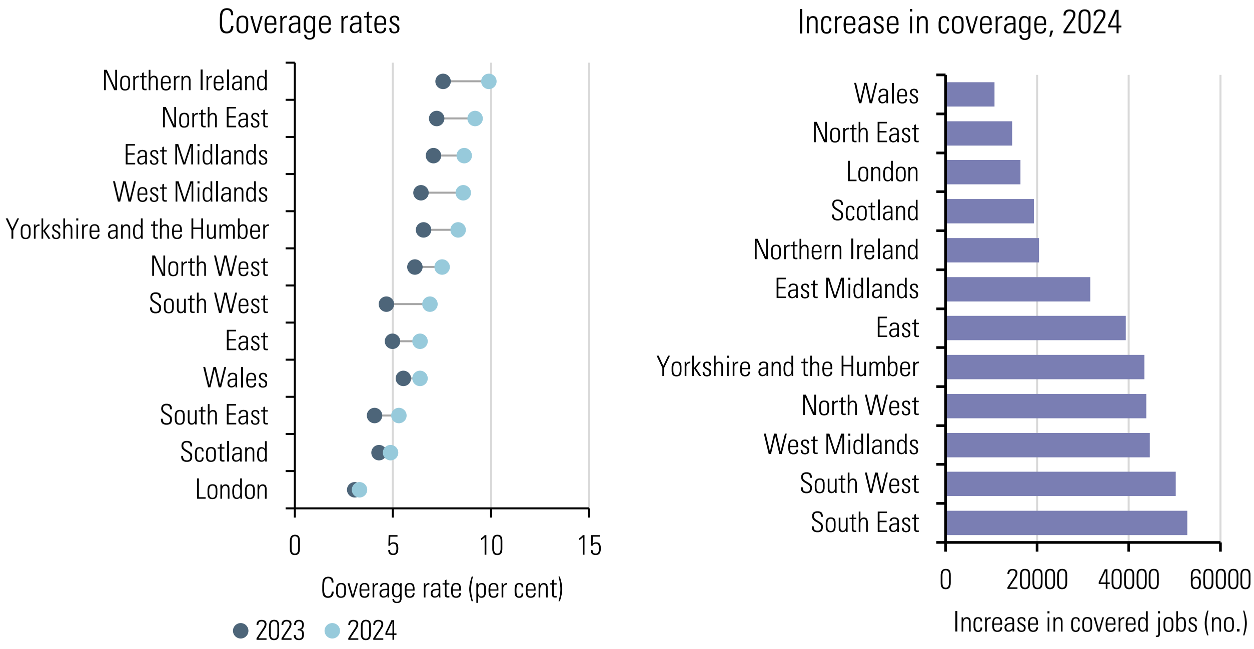


Source: LPC analysis of ASHE, low-pay weights, 21+ population, UK, 2012-2024, chain-linked.

Jobs outside London are more likely to be covered

3.20 Coverage rates continue to be significantly lower for jobs in London than in other parts of the country. In 2024, 3.3 per cent of jobs in London were minimum wage jobs (up from 3 per cent in 2023, but lower than pre-pandemic levels of around 4 per cent). Across the remaining English regions and UK nations, coverage rates ranged from 4.9 per cent in Scotland to 9.9 per cent in Northern Ireland (left panel of Figure 3.8). After Northern Ireland, coverage is also high in the Midlands, the North East and Yorkshire and the Humber. However, the largest relative increases in the number of covered jobs were in the South West, where coverage increased by 43 per cent (or 50,000 jobs) to 168,000, and the South East, where coverage increased by 32 per cent (or 53,000 jobs) to 218,000 (right panel of Figure 3.8).

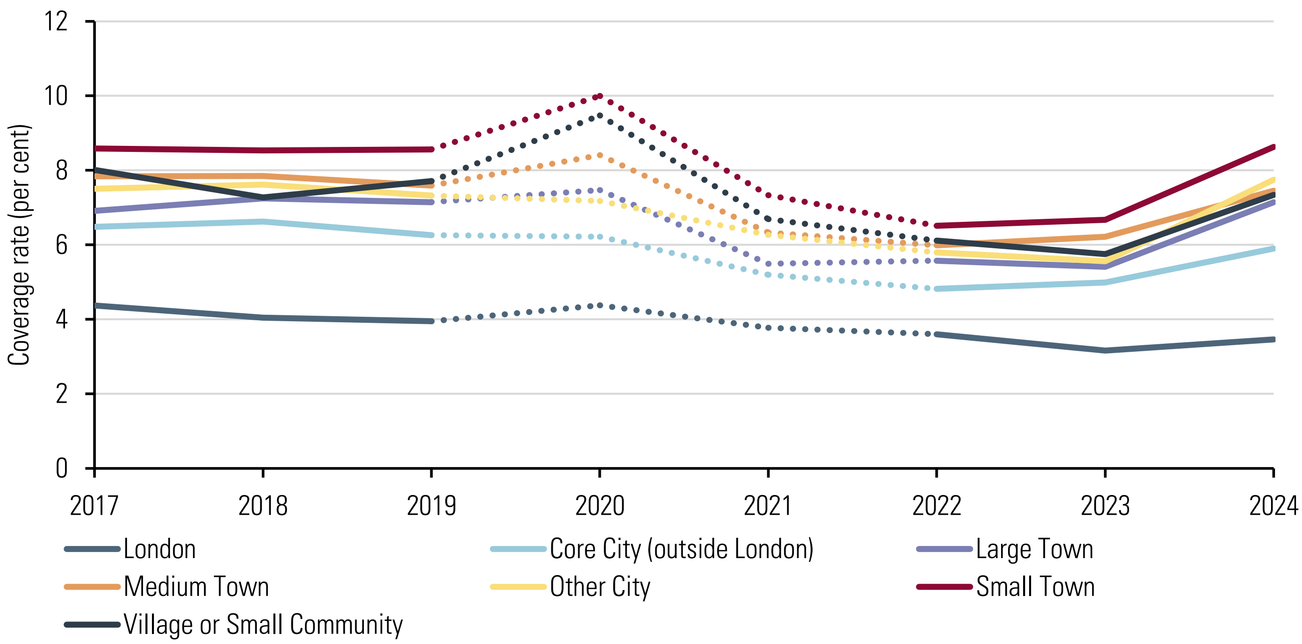
Figure 3.8: Coverage by region, UK, 2023-2024



Source: LPC analysis of ASHE, low-pay weights, UK, 2023-2024.

3.21 Coverage rates are generally higher in rural than in urban areas, both in terms of where people live and where people work. Generally speaking, smaller towns and communities have higher coverage rates than larger urban areas (Figure 3.9). However, we also observe that, in urban areas, coverage rates calculated on a work location basis are lower than coverage rates calculated on a home location basis, while the opposite is true for rural areas. This suggests that people who live in rural areas, but work in urban areas, are less likely to be minimum wage workers.

Figure 3.9: Coverage rate by city-town classification, job location, UK, 2017-2024



Source: LPC analysis of ASHE, low-pay weights, UK, 2017-2022, chain-linked. HOC City-Town Classification used to identify area types at LSOA level.

Job security, working conditions and mobility

Minimum wage jobs are often less secure than higher-paying jobs

3.22 Minimum wage positions often have less secure working conditions than non-minimum wage jobs. Since the introduction of the NLW, around 60 per cent of minimum wage jobs have been part-time, despite part-time jobs only making up around 28 per cent of all jobs. In 2024 14.1 per cent of part-time jobs were minimum wage positions (up from 11.4 per cent in 2023), compared to 3.6 per cent of full-time positions (up from 2.8 per cent in 2023). Similarly, 14.1 per cent of hourly-paid jobs were minimum wage positions in 2024 (up from 11.2 per cent in 2023), against 2.6 per cent of salaried positions (up from 2.1 per cent in 2023). Further, temporary jobs are more likely to be minimum wage jobs than permanent jobs.

Insecurity and precarity at work were central themes in evidence from unions, workers and other groups

3.23 Workers, their representatives and other bodies frequently tell us about the prevalence of insecure work and the challenges this creates. A submission from the Living Wage Foundation (LWF) offered some definitions of insecure work, with this most commonly a product of volatility in pay or hours among people paid below the median wage (2.9m workers in 2021/22) or low paid self-employment (2m workers). The LWF calculate that over half of low-paid workers (including the self-employed) were in insecure work, meaning that low-paid workers are "around five times more likely to be in insecure jobs than those paid above the real Living Wage." "Minority ethnic workers, workers with a disability, the youngest (those aged 16-24) and oldest workers (those aged 70 and over) are all disproportionately impacted by insecure work."

3.24 The Trades Union Congress (TUC) argued that insecure work characterised the post-2008 period, sharing their own analysis of LFS data showing that 3.9 million people (or one in nine of the workforce) are in insecure work, and this is skewed towards lower-paying industries. "This matters because insecure work has an enormous effect on workers. The prospect of having work offered or cancelled at short notice makes it hard to budget household bills or plan a private life." GMB argued that insecure work mitigated the benefits of the rising NLW. They pointed to LPC evidence in our 2023 report "showing the percentage of workers on low weekly levels of pay has fallen slowly by only around 5 per cent since 2011" despite the rising NMW. They argue insecure work compounds structural inequalities. Unison, citing the Gigs Rights Project survey of workers in the gig economy, found that nearly half of their sample were earning less than the NLW.

3.25 The Centre on Household Asset and Savings Management (CHASM) at the University of Birmingham noted that precarious workers had fewer employer protections such as sick pay or holiday pay, and that workers accepted financial inconsistency and lack of protection in exchange for flexibility. They described a "flexibility trap," where contracts increasingly offered flexible working practices that placed the financial risk of supply and demand onto workers. They identified this form of working as particularly prevalent in the food delivery and private transport industry.

3.26 Workers across several sectors told us about the difficulty of securing sufficient working hours. Usdaw noted that many people in the retail, warehouse or road transport sectors were employed on very short hours contracts. This left them wanting more hours but unable to get them. This was “a huge factor” in the financial insecurity many working families experienced. Security workers in Glasgow described a situation where “everyone's out here for themselves … everyone needs to get by doing X amount of hours during the weeks … it becomes competitive because we're all looking for work, we're all looking for money.” Security workers on zero-hours contracts uniformly agreed they’d prefer more hours and more predictability: “knowing that I have a set amount of hours per week for security would settle me a bit because sometimes you wonder where your next lot of money is going to come from. I think set hours would be a lot more settling and I could calm down a bit.”

3.27 Advisors at the Citizens Advice bureau on the Isle of Wight noted it was now harder for seasonal workers to find enough hours (and income) to survive through the year: "It used to be the case where you could go and work as many hours as you possibly can during that that window and then you'd know that you'd put money aside to cover the months that you were shorter. It’s not like that now." UKHospitality told us existing workers were requesting more hours due to the cost-of-living crisis, which “has eased some of that pressure to find new staff”. A hospitality worker in Glasgow told us it would be hard to bring up issues such as wanting more hours with their managers at their café job: “It’s hard to bring up formal conversations in an informal setting.”

Some workers prefer the flexibility this kind of work can offer

3.28 On the other hand, we met a limited number of workers – mainly young workers and students – throughout the year who were happier with flexible arrangements. One of the security workers in Glasgow noted that “when I was at university, the zero-hours contract definitely was beneficial for me because it allowed me to just focus on my studies when I really had to; when I had more free time, I could work.”

3.29 Retail workers in Northern Ireland told us that contracts with a lower number of fixed hours suited students. They could work their contracted hours during term time and additional hours over the summer. Employers generally “give you the leniency to do more” if desired. One worker told us “It suits me quite well during the uni year, but over summer I've just been working as much as I can, because I’ve not really got anything else to do.” Another worker, who was not a student, had a 30 hour contract with the option to do up to 40 hours: “it’s perfect for me and I’m happy enough.”

3.30 Hospitality workers in Glasgow told us their employer offered two sets of contracts, at 13.5 or 20 hours. Because of their length of tenure, they’d been offered “promotion” to the better contract – but preferred to have the flexibility. They felt lucky that coworkers were able and willing to swap shifts if they needed to do so. “They always need a pair of hands, there’s only three of us.” Other participants in the session each tended to work 20-25 hours per week but were only on 16 hour contracts. “The flexibility works for us,” they told us, but they did acknowledge they had other colleagues who wanted more hours.

Low-paid workers described inadequate benefits, rising housing costs and disincentives to work longer

3.31 Various respondents discussed low-paid workers’ experience of Universal Credit (UC). Usdaw noted that many of their members claimed Universal Credit and overwhelmingly considered it insufficient to live on. The Women’s Budget Group (WBG) argued the benefit cap had disproportionately affected women as they were more likely to claim housing benefit. They noted that private rents had increased by 9.2 per cent in the year to March 2024, compared with CPI rising by 2.3 per cent in the year to April 2024.

3.32 Usdaw again raised issues with the problem caused by Universal Credit assessing incomes monthly, when many retail workers are paid by their employer weekly or every four weeks. This results in workers being paid 13 times each year, with two payments in one assessment month, resulting in their UC payments being reduced or stopped altogether. Usdaw stated "it is not realistic to expect people to budget for the month when they receive little or no payment and the system causes havoc with their finances. Fixing this should be a significant priority when looking to improve the lives of low paid workers." Some Usdaw members were opting out of bonuses or taking unpaid leave in order instead to avoid disrupting their UC entitlement.

3.33 Other respondents raised the issue of low-paid workers having to make repayments to Universal Credit. The Scottish Women's Convention (SWC) gave examples of women who "had to pay sums back into the system, in cases where they have worked slightly more hours than they should have, putting them in breach of UC regulations." This created "significant financial burdens." Dover Big Local told us this meant "sometimes people don't claim things they're entitled to because they're frightened of being fined at the other end if they make a little mistake."

3.34 Submissions raised issues around the design of Universal Credit and its relationship with the NLW. GMB argued recent changes to conditionality thresholds should be reversed. The Administrative Earnings Threshold (AET) is the minimum an individual required by UC to work must earn to continue receiving the benefit; those earning below the AET must show they are actively looking for more or better-paid work. The AET has been raised to £872 for individual claimants, which is roughly 18 hours on the NLW. GMB were concerned that workers would not be able to find these additional hours and that this "will be particularly worrying for minimum wage workers in insecure jobs," given the average hours worked for those on zero-hours contracts was 18.3 hours in Q1 2024. More generally, they stated they were "shocked to see the penalisation of people trying to find work in an economy where you can't get enough hours."

3.35 At the same time, Usdaw told us members on benefits were rejecting additional work hours due to the tapering effect of UC (that is, the progressive reduction in UC payments as earnings increase) and fear of the impact additional income can have on a claim; and noted that the second earner in a household does not have a "work allowance" (a sum they can earn before tapering of UC payments commences) and so has less incentive to enter the workforce. At Dover Big Local, staff felt job seekers were often looking for part-time work, although it was unclear whether this reflected reliance on legacy benefits or a misunderstanding of how UC worked. The Recruitment and Employment Confederation (REC) told us that anecdotally they heard from members that some workers were less willing to take on additional responsibilities or work longer hours due to concerns that increased work will lead to them losing their eligibility to receive UC.

3.36 One of the big changes between the previous regime of tax credits and Universal Credit was the removal of the 16 hours threshold (whereby workers needed to work a minimum of 16 hours to receive working tax credits). Despite this, it is relatively common to hear it cited by both employers and workers. This is likely to reflect the legacy of tax credits in both job design and in workers' understanding of the rules. We also note that, despite changes to UC, eligibility for several other benefits is often linked to a weekly earnings threshold set at 16 hours multiplied by the minimum wage, although this threshold can operate in both directions. For example, to be eligible for tax-free childcare, workers need to earn a weekly income of at least 16 times the NLW rate. This means an NLW worker would have to work at least 16 hours a week to be eligible. On the other hand, to be eligible for the old incapacity benefit workers need to earn less than that amount.

3.37 The SWC argued that the benefit system pushes women into low-quality work. Women in receipt of benefits – particularly single mothers - “regularly feel that their needs are not considered.” Checks carried out by Job Centres “contribute to a sense of low self-worth … This has impacted single mothers’ ability to hold good quality jobs, as they are more likely to take on part-time or zero-hour work to mitigate the costs of childcare.”

3.38 A retail worker we met in Glasgow told us about his experience of UC. He received around £400 per month, which covered the rent for his “damp, mouldy” flat. “Once you’re on it, it’s very difficult to get off it … to graduate from UC, you have to go through this whole process of upping your hours. Having no UC for three months or something, while it works itself out you’re always going to be in the red during that transition period.” Interactions with DWP staff make “you feel like a burden to them … they’re trying to find a way to kick you off it” and treat you as if you’re a fraud. Overall, “it does feel a bit rubbish.”

There are a range of factors which make workers reluctant to switch jobs

3.39 Building on an increasingly prominent theme in recent years’ evidence, our consultation asked about workers’ experience of the job market. Several written submissions gave answers on this point, and in face to face meetings workers told us about their own attitudes towards moving jobs.

3.40 The overarching theme of security came up frequently. Usdaw told us that for many working people taking on a new role feels like a risk, not just because of familiarity with their current workplace, but also because of a lack of day one rights, employment security and the way many workers accrue better terms and conditions over time, such as annual leave entitlement, company sick pay and long-service awards. Hospitality workers in Glasgow echoed this point: “why move somewhere if you’re on worse conditions, starting at bottom of ladder … money is tight for everybody. It’s scary to jump to another job, not knowing is my contract going to protect me? Will I make enough to pay rent? it's easier to just to stick with what you've got if you know that I'm making ends meet at the moment.”

3.41 Staff at Dover Big Local, responsible for supporting job seekers, noted that people were reluctant to take jobs in unfamiliar occupations: “People who’ve been cleaners don't want to be kitchen staff and kitchen staff don't want to do gardening. And they sit and they go, well, I'm not going to do that. They’re just set in their ways … you get care assistants in here, they just want to do care assistant work. You say the jobs are there, but they say “I’ll stick to my cleaning thanks’. They’re stuck in their ways.” Dover Big Local added that transferable skills training is being offered by third sector organisations and is often successful but needs financial support to be continued sustainably by such organisations. A teaching assistant we also met on the Dover visit echoed this: “to retrain later in life is quite daunting – people don’t have the skills or the drive.” A retail worker in Glasgow expressed a similar sentiment: while other opportunities might be available in the local labour market, “because I’ve been with this company for so long, I can’t pass an interview.”

3.42 Dover Big Local staff thought employers' expectations of immediate competency contributed to this sentiment: "I'll take fruit picking as an example… the accuracy and speed that people are expected to pick at and that foreign nationals can run at because they're used to doing it … it's the hitting the ground running problem… the employers don't have the financial bandwidth for somebody to do the job badly for a month while they learn it ... There's lots of jobs out there for hospital cleaners aren't there? But the quality expected of the people and the speed of turnaround… You're supposed to be able to do that from day two."

3.43 Respondents also discussed working hours and flexibility as a barrier to moving jobs. A submission by Professor Deirdre McCann of Durham Law School argued that flexibility could be a strong reason for workers to stick with the job they have even in poor conditions. Her submission pointed to research showing "a lack of carer-friendly jobs prompts [workers] to prioritise working time arrangements that suit their needs. Many workers are prepared to endure poorer working conditions to have the working time flexibility that they need, dissuading them from moving to a better-paid job. She called for reforms to strengthen rights to flexible working and ensure regular consultation between employers and workers' representatives on working time and other working conditions. A retail worker in Glasgow echoed this, believing "there are vacancies out there," but that many of them would involve unreasonable hours. A worker on the Isle of Wight complained about the difficulty of getting a "hard and fast" full-time job on the island: "you'd only end up in care, and you'd be working weekends, and they'd be pulling you in hours and hours and hours… [supermarkets] will only give you a very limited contract… So it's very difficult to go and find a Monday to Friday job."

3.44 The Work Rights Centre (WRC) noted specific barriers faced by migrant workers, whose immigration status and visa conditions limit what they can do in the labour market. "By definition, sponsorship acts to inhibit the right of workers to withdraw their labour from an individual employer and move elsewhere … our view is that policymakers often do not appreciate how state-sanctioned rules on immigration can restrict worker mobility and facilitate exploitative practices." WRC proposed that "the cleanest way to end the exploitation of migrant workers would be to end the system of sponsorship and give migrants the freedom to work across the labour market," but also recommended several alternative measures.

3.45 Unite told us that a lack of local opportunities is a significant barrier to moving jobs. In their survey of hospitality workers, 48 per cent identified the lack of decent and well-paid jobs locally as a barrier to moving into better-paid work. 22 per cent mentioned childcare commitments; 17 per cent a lack of promotion prospects; and 13 per cent transport costs.

Progression opportunities are declining because of reduced training, pay compression and gender barriers

3.46 Various submissions dwelled on the issue of progression within the workplace. Usdaw's response lamented a lack of training opportunities for their members: "Progression opportunities and pathways in retail have been significantly depleted, with a scarcity of management level roles following the continual hollowing out of middle management roles to save on costs." Unite, too, noted concerns that workers in sectors they represent have little pay progression over time. They also noted that outsourced workers are less likely to receive training or progression than in-house ones.

3.47 Staff at Dover Big Local told us that traditional progression routes had disappeared: "the washer-upper through to kitchen through to sous chef route doesn't really exist like that anymore … [employers are] expecting them to come from college, trained at speed to be able to walk in the job and just do it … the margin isn't there in the business … to take up the slack of having to nurse people along." Job seekers, they argued, needed more advice on career progression – and opportunities to try new things "It would help to have education around 'look if you get this job, this is how you can move on ... that gives you the skills to go on to this, this and this and we can give you the training.'"

3.48 Some unions and workers linked low progression rates to pay compression. Community Trade Union told us that because higher-paid roles had not received equivalent increases to the NLW, there was a perception of people leaving skilled roles to work in "easier stress free jobs on minimum wage." Unite reps in Northern Ireland told us that narrowing differentials not only affected retention, but also "discourages upskilling and skill development," with the example given of bookmakers where workers were leaving because "there's no progression through the company." Retail workers in Glasgow noted that the premium for a team support role at their employer hadn't increased for four or five years, even while the associated responsibilities have got greater and greater; "they're almost doing management positions."

3.49 The SWC argued that misogyny is a key barrier to women's workplace progression. "Women recounted stories of being passed over for promotions, with ability and experience being discounted, contributing to poor feelings of self-worth and frustration." This is often linked to maternity leave, over the course of which "women can be viewed more negatively by employers and are, again, ignored when it comes to promotions."

3.50 Some young workers we spoke to this year had their own perspectives on progression. In Glasgow, security workers were unsure whether they wanted to progress in their roles: "I'm not too fussed if I progress or not because I don't see myself in this for the rest of my life, but I dare say the pay might be worth it." Young retail workers in Northern Ireland were not sure what the supervisor rate of pay would be at their workplace and were not interested in progressing. They wanted to get a different graduate level job after their degree, run their own business, or move countries: "I'm dealing with the workload of uni as well and I'm in this job already. It's kind of comfortable just to be in the position I am now, so I don't think it'd be worth it."

Low-paid workers report inadequate or non-existent training

3.51 Hospitality workers in Glasgow told us they received either inadequate – or non-existent – training in their roles. One participant's induction for working in a café amounted to "oh you've made a coffee before". Working at a cinema, she was given a one hour talk on alcohol licencing, then told if she had further questions to wait for a quiet spell and ask a co-worker. Another participant had also worked at a cinema – where she'd been put on a counter without any training and served customers cold hot dogs for a week. One participant recounted being asked to take part in a training session on spotting forged money – but the training was only based on English money and the cinema didn't take cash.

3.52 Another participant at the Glasgow meeting described the attitude to training at the hotel where he worked as "learn while you're there". For more serious matters such as health and safety there were online modules which had to be repeated every two months and for which training time was always unpaid. Staff tended to share answers, and didn't pay too much attention: "It's not an effective way to train people, people just want to get it out of the way."

3.53 Retail workers in Northern Ireland told us that when they started their job, their training mostly consisted of shadowing an existing worker: "I just watched another employee for a couple days, within different tasks. I feel like my job isn't exactly the hardest job in the world, so [it] probably […] makes the most sense to do that."

3.54 Security workers in Glasgow were more positive about training: workers felt there was plenty of training available and found it helpful in their jobs. Training covered subjects like health and safety and crowd control. Also, the link between the licence (SIA), the associated training and higher pay was clear and understood by all.

3.55 The SWC told us that poor training traps women in low-paid work, arguing that a lack of training and opportunities for skills development is "a major issue for women who work in private organisations/businesses, with employers rarely valuing their employees." They link this lack of training "to the high staff turnover experienced across low-paid work, such as retail and hospitality." The inability to build skills leads to "a sense of disenfranchisement within the job market." They quote one worker: "I worked in hospitality for years, and I mean the only training I got was the stuff they had to do, like the legal bits. They weren't going to actually put you forward for anything that would develop you as a worker, they didn't care."

High childcare costs and limited access are major barriers for low-paid workers

3.56 Usdaw's response stated: "The cost of childcare and ability to access childcare has a major impact on the lives of our members, including their ability to continue in employment, work more hours or seek out promotion … formal childcare is now beyond the reach of many low-paid workers." This was exacerbated, in their view, by "an even greater demand from retail employers for flexibility from their staff, as they revise and re-organise working hours in response to post-pandemic changes."

3.57 The response from CHASM agreed that childcare was a key barrier preventing female workers in precarious employment from moving to a new (and more secure) job. Women in the study were found to be taking and/or remaining on insecure working contracts because they offered greater flexibility around their childcare responsibilities compared to traditional and more secure employment. The SWC agreed that childcare was "a clear barrier to women's participation in the labour market, with the current NLW not effectively mitigating the financial burden placed on mothers/carers." They quote one participant in their research: "Unless something changes there will be more and more women unable to work. The financial implications of childcare are far too great for working class families."

3.58 WBG cited OECD statistics that the UK has the most expensive childcare system in the world, with 35.7 per cent of household income being spent on childcare. ""Labour market policies aimed at eradicating poverty and/or inequality need to work holistically in combination with other parts of the social protection system such as social security benefits and adult social care and childcare. Increasing hours and pay is insufficient if families can still not afford childcare, effectively locking one parent (usually the mother) out of the labour market." The soaring cost of childcare (up £2000 per year since 2010 according to the TUC) means low-paid workers either cannot work or can work limited hours. They cited survey evidence from Pregnant Then Screwed that “76 per cent of mothers who pay for childcare say it no longer makes financial sense for them to work.” They welcomed the Government’s planned expansion of free childcare but noted the workforce barriers to delivering this and the role of low pay. They highlighted that lack of available social care had similar effects, which again fell disproportionately on women. An additional barrier identified was the requirement under UC for low-income parents to pay childcare fees up front, then claim up to 85% of the cost back.

A lack of reliable and affordable public transport, particularly in rural areas, limits access to jobs

3.59 Several stakeholders on visits told us about the problems created by a lack of reliable and affordable transport. On the Isle of Wight, Citizens Advice told us that workers’ efforts to combine part-time jobs were hampered by public transport. The £2 price cap for bus journeys was due to end in October; before this fares had been “astronomical.” On top of this, services were infrequent; “if you're in a rural location you might have a bus once every two hours, which is no good if your work requires shift patterns.” Staff at Dover Big Local told us that unreliable public transport limited access to labour markets beyond Dover. As on the Isle of Wight, bus services were few and far between, and 48 per cent of Dover residents didn’t have a car. The scarcity of services hit workers with children and caring responsibilities particularly hard. A hotel owner we spoke to during a regional trip, who was struggling to recruit enough staff noted: “we've lost members of staff because they struggle with the commute”

3.60 The SWC’s response stated that women in rural locations struggled to access work due to lack of transport links: “Women in rural Scotland are continually let down by infrequent bus services, greatly limiting their ability to access town/city centres.” The implementation in Scotland of free bus travel for under-22s had been a positive development but the scheme had less impact in areas where bus links were poor. For older workers, SWC noted the cost of bus travel could be inhibiting. The submission from Public Health Wales stated that transport poverty was a real issue in Wales, with people’s ability to get to and from work heavily impacted by limited and unaffordable public transport options and the rising costs of car ownership. The submission cited Sustrans Cymru data that transport poverty affected 40-50 per cent of Welsh households, especially those living in rural areas, but also those working outside traditional “9 to 5” commuting hours or communities outside of city centres.

Conclusions

3.61 In 2024 there were an additional 387,000 minimum wage jobs, taking the total number of minimum wage jobs to 1.91 million. The increase in coverage mainly affected the occupations and demographic groups that already had relatively high coverage. For example, the increase in coverage was highest for women, young people, and older workers. Similarly, retail and hospitality were the occupations that saw the largest increases in the number of minimum wage jobs.

3.62 Although indicators of insecure work remained relatively stable this year, minimum wage workers are more likely to be in jobs with less secure working conditions, and job and income insecurity remain among the greatest concerns for minimum wage workers. We also heard from minimum wage workers about the barriers they face to working more and progressing in their careers. These include inadequate training, childcare responsibilities, uncertainty about their rights and conditions in new roles, the operation of, and knowledge about, state benefits, and lack of reliable transport.

Chapter 4

Earnings, household income and living standards

Key findings

- **The LPC's remit has been expanded to cover living costs –** Our remit this year asked us to take living costs (including future inflation) into account when recommending the National Living Wage (NLW) for April 2025. This chapter sets out how we have analysed living costs and how these are related to the National Minimum Wage (NMW) and NLW to date. Chapter 10 explains how we accounted for future inflation and Chapter 11 shows how this affected our recommendations. Living standards has always been key to LPC recommendations, but this is the first time it has formally been in our remit. As such, our approach may evolve over time, particularly as the Government sets out more detail on how a genuine living wage is defined.
- **Measures of living costs for low-income households are the most relevant –** NLW workers are spread throughout the working household income distribution, but are more likely to live in low-income households. NLW workers toward the lower end of the household income distribution are also more likely to be the main earner. Measures of inflation for lower-income households are therefore particularly pertinent to our considerations.
- **During the recent spike in inflation, living costs rose the most for low-income households –** The recent high inflation had more impact on lower-income households as they spend more on food and energy as a share of income. Although inflation has slowed, prices remain much higher than they were in 2021, hence the persistence of concerns about standards of living. Stakeholders across the country drew our attention to the difficulties of making ends meet.
- **The living standards challenge did not start with the recent bout of inflation –** After decades of strong real wage growth, there has been a prolonged squeeze in real wages following the 2008 financial crisis. During this period, the NMW and NLW have protected the lowest-paid workers.
- **The adult rate of the minimum wage has more than maintained its real value –** Despite exceptionally high inflation in recent years, the NLW has more than kept pace.
- **Fewer UK workers meet international definitions of "low paid" –** The previous target for the NLW of two-thirds of average earnings was chosen as it is the OECD benchmark for low pay. The increase in the NLW has meant large falls in those paid below two-thirds of median hourly pay. Progress on weekly low pay has been slower because the definition of low pay on a weekly basis includes relatively well (hourly) paid jobs that involve relatively few hours per week and so are not affected by the NLW.

- **NLW increases have translated into weekly pay rises –** NLW employees have seen weekly pay increases that match or exceed hourly pay rises, suggesting weekly hours haven't decreased despite large rate rises. However, workers are concerned about the uncertainty and volatility of weekly hours, making it harder to cope with cost of living increases, and sudden expenditure demands, such as a car break down or repair, essential to get to work in areas with limited public transport options.
- **Changes to the tax system have also affected employees' incomes –** The reduction in National Insurance (NI) rates has been offset for some by frozen Income Tax, NI and pension auto-enrolment thresholds. Even after accounting for this, NLW earners still see larger increases in nominal and real net pay than those on median wages.
- **Focusing solely on the costs of a basket of goods and services to determine the level of the minimum wage carries risks –** Comparing inflation measures shows whether NLW increases match prices but not if the NLW level is sufficient. However, the LPC has previously flagged the risks of relying on a basket of goods alone to set the minimum wage, as defining these baskets involves judgment and households' needs vary greatly. This makes such methods complex and subjective. Focusing solely on living costs also risks ignoring economic circumstances, harming the LPC's credibility and excluding worker and employer voices, weakening its social partnership approach. Few stakeholders we spoke to supported a basket of goods method for setting the minimum wage and many, including employers, trade unions, think tanks and academics, spoke against it.

The Government asked us to take account of the cost of living in recommending the National Living Wage

4.1 Alongside economic conditions, our remit for the National Living Wage (NLW) in 2025 is to ensure it does not fall below two-thirds of median hourly earnings for those aged 21 and over, and to take account of the cost of living (and expected inflation up to March 2026). This latter part of the remit is part of the Government's ambitions for a genuine living wage. The remit also specified that our NLW recommendations should account for the expected inflation up to March 2026.

4.2 This chapter sets out how we have analysed living costs and how these are related to the National Minimum Wage (NMW), including the NLW, to date. In Chapter 10 we explain how we accounted for future inflation and in Chapter 11 how this affected our recommendations.

4.3 In September we published a statement showing how we would respond to the living standards aspect, which is new to the LPC's remit (Low Pay Commission, 2024c). In essence, the requirements to take account of living costs and not fall below two thirds of median pay act like 'floors' to our recommendations. There is scope to recommend increases above the 'floor' if the economic evidence supports this, and we would only recommend an NLW below the 'floor' if this was necessary to avoid substantial negative outcomes. However, focussing on living costs is new for our remit and so our thinking may evolve over time.

Measuring changes in the cost of living

4.4 To fulfil our remit we need to measure changes in the cost of living. There are many measures available including headline inflation measures like the Consumer Price Index (CPI), newer indices like the Household Cost Indices (HCI), and more qualitative approaches like the Minimum Income Standard (MIS).Each of these measures serves a different purpose so, as the Royal Statistical Society (RSS) has noted, no single measure of inflation "can meet all needs" (Citizens Advice, the Financial Fairness Trust and the Royal Statistical Society, 2024). Because of their varied purposes, we have used a range of measures throughout our deliberations.

4.5 CPI is used for macroeconomic purposes like inflation targeting and international comparisons. CPIH includes housing costs, making it more relevant for households. CPI measures are weighted by total expenditure, favouring wealthier households. Because of this, CPI is not the best measure for understanding price rises as experienced by households, reflecting that this is not its purpose. The Retail Price Index (RPI) was originally intended to be a better measure of inflation at the household level and excludes pensioners and the wealthiest households. However, it has a number of methodological issues[4], is no longer a National Statistic and it is also skewed towards higher spending households. Nevertheless, the Government and some sectors still use the RPI and it still often features in pay bargaining as unions believe that it better represents inflation for workers.

4.6 As a result of the limitations of both the RPI and CPI, the Office for National Statistics (ONS) has developed HCIs to better measure inflation as experienced by different household types. Although not yet accredited as National Statistics, HCIs have been published since December 2023 with data from January 2005. The latest data available to us at the time of our recommendation covered the period up to June 2024. HCIs are available by household income decile, housing tenure and by parental[5] and retirement status.

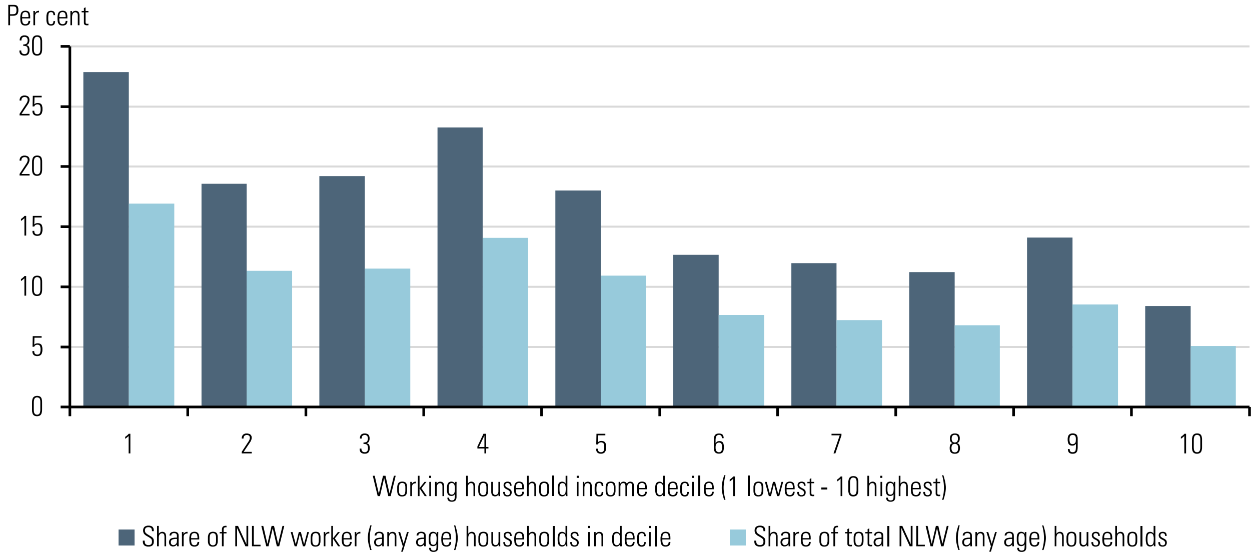
4.7 As with the other inflation measures considered here, HCIs are also subject to a further flaw. They are insensitive to product (or brand) choice, thereby not reflecting any difference in inflation rates between basic and luxury products (such as the phenomenon of 'cheapflation' highlighted by Chen, Levell and O'Connell (2024).

4.8 To understand the relationship between the minimum wage and living standards, we need to know which of these inflation measures are most pertinent to those NLW workers. Households with an NLW earner are found throughout the working household income distribution, but are more likely to be found in the lower part of the income distribution (for working households) (Figure 4.1).

[4] Due to known problems with the RPI regarding its methodology, its National Statistics status was withdrawn in 2013. A review of consumer price indices by Paul Johnson (2015) concluded that RPI should be maintained only as a legacy measure. The Statistics Authority and the ONS have advocated strongly against its use and intend to replace it by 2030.

[5] Parental status splits households into those with and without children.

Figure 4.1: Share of NLW households in each decile of the working household income distribution for working households, UK, 2022/23



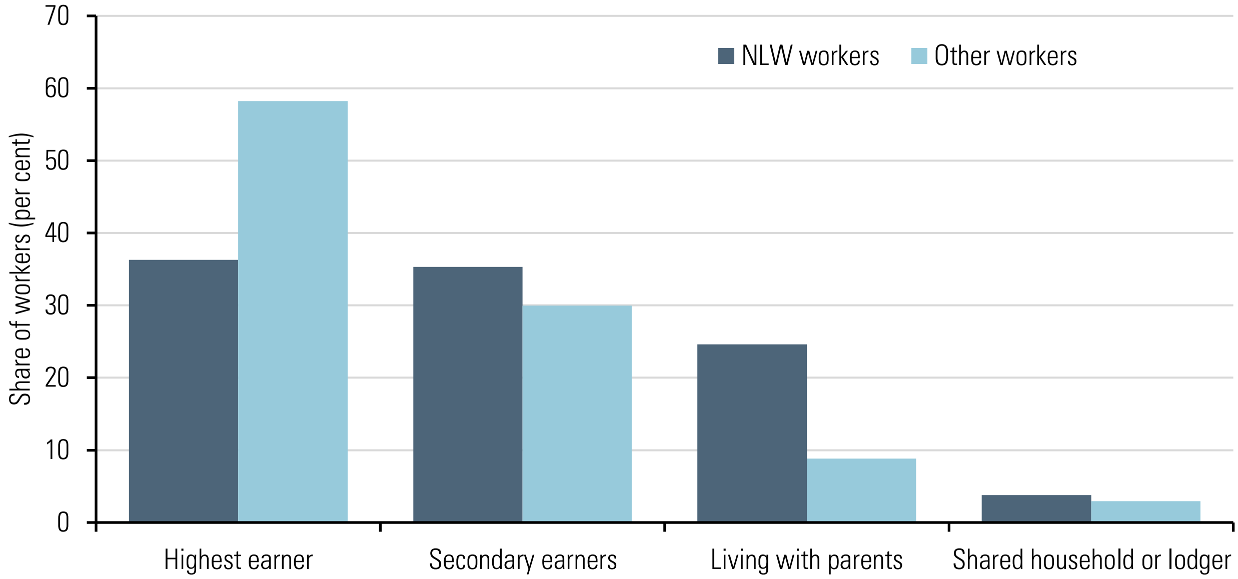
Source: Family Resources Survey, UK, 2022/23. Households with at least one working member. Income decile is defined using gross weekly income from all sources, not adjusted for household size.
Note: FRS estimates of coverage are higher than those derived from ASHE and so cannot be directly compared.

4.9 NLW worker households may include well-paid family members or have other sources of income, placing them higher up the household income distribution. Figure 4.3 shows that around one third of NLW workers are the highest earner (from work) in their household, while a similar proportion are secondary earners.

4.10 The HCI covers all households including non-working households, such as those with pensioners and those relying on benefits. There is no inflation measure only for minimum wage or NLW households. When we look at the income distribution for all households, NLW workers are more evenly spread, and concentrated around the middle of the distribution.[6] However, NLW workers at the lowest end of the income distribution (deciles 1-3 of all households) are overwhelmingly the highest earners in their household. Therefore, inflation measures for lower-income households are most relevant to our recommendations, although we also refer to the all household measure.

[6] Note that the HCI uses a different income measure to that we have used and so we cannot directly read across from one to the other.

Figure 4.2: Role of workers in their households, NLW workers compared to other workers, UK, 2022/23



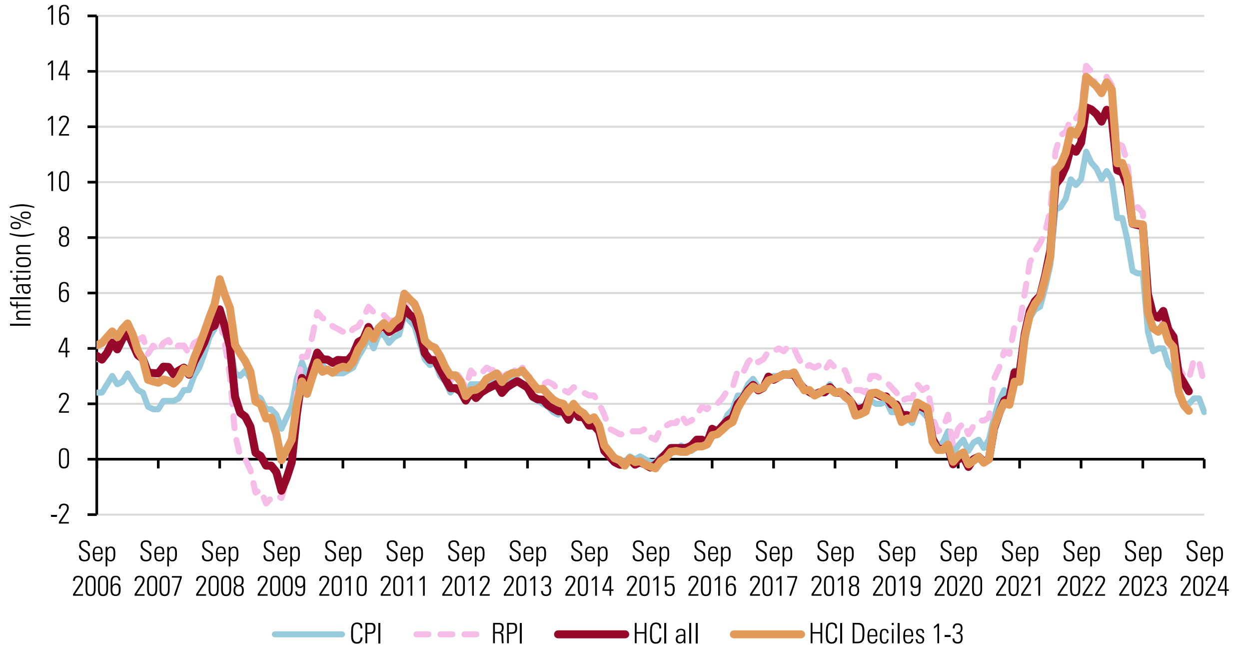
Source: Family Resources Survey, UK, 2022/23. Highest earner includes joint highest earners. Roles are attributed based on total weekly earnings from work. A full definition of each role is available in Appendix 3.

Lower income households experienced much higher inflation during the recent inflation spike

4.11 The differences in households' experience of inflation became more evident during the recent spike in inflation. Global supply chain disruptions were exacerbated by the Russian invasion of Ukraine and the UK changing its trading relationship with the EU, leading to a sharp rise in fuel, energy and food prices. After the pandemic, HCI deciles 1-3, which measures inflation for the lowest-income households, rose much faster than for other deciles. Increases in energy, fuel and food prices have a larger impact on those in lower-income deciles because they take up a larger share of those groups' income[7]. While inflation rates have slowed, as shown in Figure 4.3, price levels remain high and continue to rise. This help explains why workers continue to feel severe budgetary pressures despite increases in nominal wages.

[7] In the Household Cost Indices, just under half (47 per cent) of household income goes on food, housing, energy and utilities for the lowest income decile. It's around one third for the richest decile.

Figure 4.3: Comparisons of inflation rates since the financial crisis, 2006-2024



Source: LPC estimates using ONS data. Consumer price index (D7BT), and Retail price index (CHAW), monthly, September 2006-September 2024; Household costs index for all households (All items from Table 23: Household Costs Indices by all households, by division and selected groups, index (2015=100)), and Household cost index for the average of deciles 1-3 (All items for each decile from Table 3: and Household Costs Indices by income decile, by division and selected groups, index (2015=100)), monthly, September 2006-June 2024.

4.12 Submissions from several trade unions offered evidence on the living standards of low-paid workers. The Trades Union Congress (TUC) shared poll data (2024b) showing significant numbers cutting back on essential and non-essential spending; around a fifth said they had fallen behind on bills; and more than a quarter had taken out debt to cover unexpected expenses.

4.13 Usdaw shared results from its May 2024 cost of living survey: 73 per cent of respondents felt worse off compared to five years ago; 73 per cent could not afford to take time off work when they are ill; 62 per cent had taken out loans to pay everyday bills, 45 per cent were struggling to keep up with repayments; 70 per cent of parents believe their children are missing out on experiences because of financial worries. One of Usdaw's members said: "It seems to keep going up and up, yet the wages don't seem to go nearly as much, you can get a pay rise yet be worse off."

4.14 The Scottish Women's Convention (SWC) told us that: "women on low incomes have explained that rising living costs have seriously impacted their ability to afford basic necessities, including food, clothing and bills. Single women with children, have been the most acutely impacted by rising living costs, with a sole income often not being adequate to cover expenses."

4.15 Evidence from Organise included quotes from workers on how they struggled while working minimum wage jobs: "It is mentally, physically and emotionally crippling. You have to think about every penny. Even a cup of tea out is impossible, let alone a sandwich on the go. Putting the heating on becomes a treat!"

4.16 In our meetings with workers throughout the year, we heard a range of evidence on the hardship faced by low-paid workers and the decline in their living standards. A selection is set out below.

"Any increase we've got has been swallowed up … [colleagues] may have to either leave or look for something else to do [on top] – I mean you can't survive on what we're getting, I think, and live at the same time. Education worker, Isle of Wight

"Obviously you don't recognise it in your pay packet at all. You know, you don't see it because obviously the cost of living is just through the roof at the moment with everything: bills, food, petrol, everything." Warehouse worker, Coventry

4.17 The Work Rights Centre (WRC) told us that migrant workers too had been affected by the recent spike in inflation. They reported that their clients "have increasingly sought food vouchers from our team and have had to take tough financial decisions about meeting different living costs like food, utilities and childcare". In the year to May 2024, 89 per cent of WRC's clients reported having only 0-2 months of savings: "over the last year or so, our migrant worker clients are either barely earning above the living wage (men) or they are earning significantly below the living wage rates (women)."

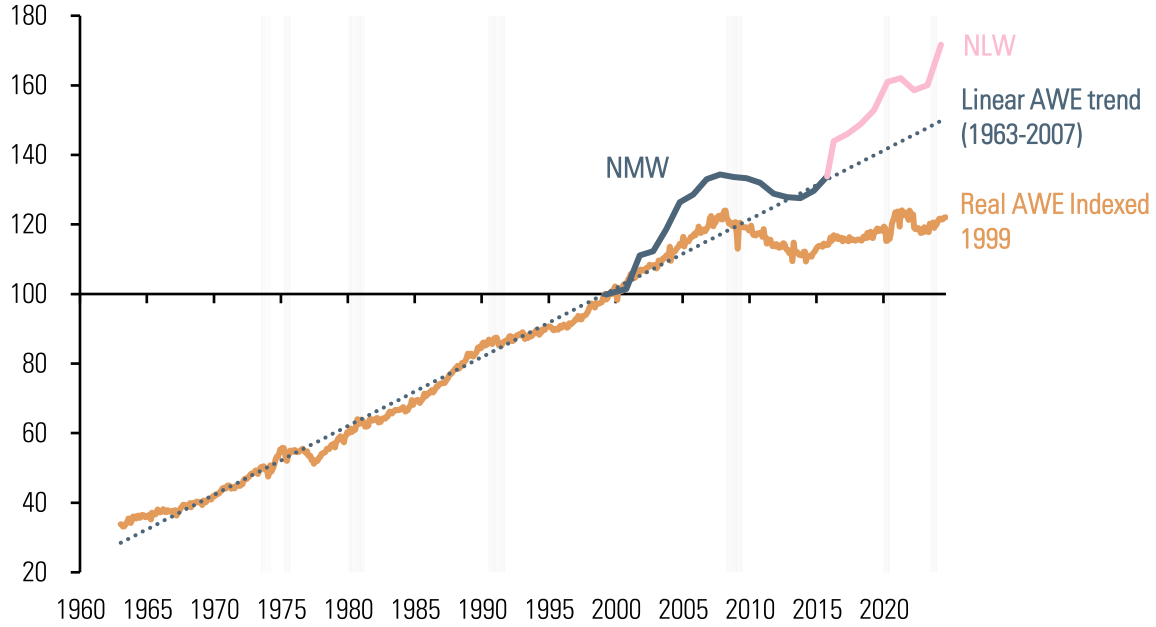
4.18 On our visit to the Isle of Wight, officials from the Citizens Advice bureau described the major debt and income problems they were seeing: "The demographic of the clients that we're seeing has changed as well … these are people working full time, National Minimum Wage normally, but they're barely able to break even each month. So there's nothing left over." Workers at the charity Babybox told us the present situation – with pandemic job losses compounded by cost-of-living increases – was worse than anything they'd previously seen, with the number of families they supported each week rising from around 30 before the pandemic to over 150 now.

The UK has experienced a prolonged and unprecedented squeeze in living standards, but the minimum wage has provided some protection

4.19 It is not just since the pandemic that living standards have been squeezed. Figure 4.4 shows that this has been going on for far longer. Having grown consistently from the early 1960s, average real weekly earnings (the orange line of Figure 4.4) stalled during the 2008 financial crisis and went into decline. Real wages are barely higher now than they were in 2008. This is unprecedented and breaks a more than 50 year trend which includes the inflation shocks of the 1970s and 1980s. If real wages had continued on the pre-financial crisis long-term trend, then nominal wages would be around 20-25 per cent higher than they are today. Only a handful of countries in the OECD have seen a worse performance (See Appendix 4 for further details).

4.20 Figure 4.4 also demonstrates the important role the minimum wage played from its inception in 1998. While real average wages have stagnated since 2007, the NMW/NLW has more than outstripped the pre-financial crisis trend. Since 1999 the NMW has risen by over 70 per cent in real terms, while real average wages have increased only 22 per cent. This is despite periods after the financial crisis and following the pandemic where it fell for short periods.

Figure 4.4: Real (CPI) AWE and NMW / NLW wages, GB, 1963-2024 (1999=100)



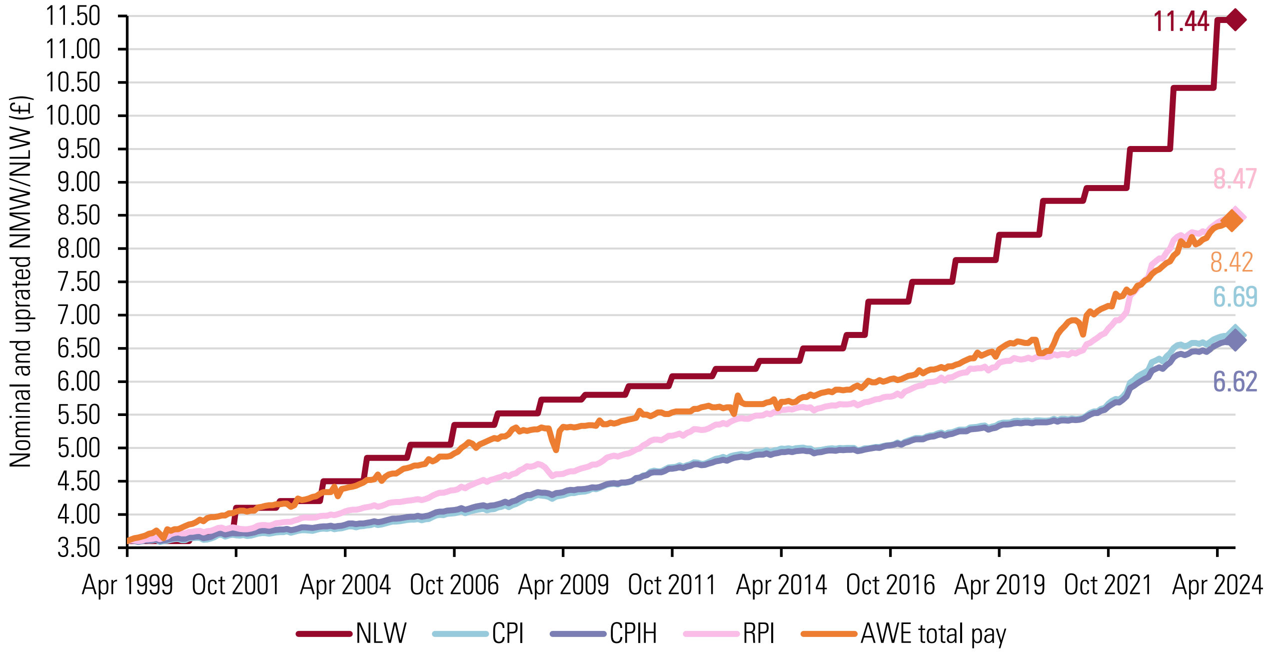
Source: LPC estimates based on BoE Millenium of Macroeconomic data for earnings from 1963 to 2000, ONS AWE (KAB9 series) from 2000 onwards, and CPI (JFDN series) for 1963 to 1988, D7BT for 1988 onwards). NMW/NLW series indicates the real value at implementation.

4.21 Figure 4.5 puts this into more concrete terms by showing what level the NLW would be if it had been uprated by a range of price and wage metrics since its inception. Tracking CPI, it would have reached £6.69 by September 2024 (but just £6.62 if uprated by CPIH). Following average weekly earnings total pay growth (AWE), it would have been £8.42 in August 2024 (and £8.32 if excluding bonuses and following regular pay growth). If increased in line with RPI, it would have been £8.47 in September 2024. The increase in real wages for NMW workers has been far greater than that for the worker on average wages.

4.22 Comparisons with 1999 cover a long period of low inflation. If we focus on the period since the two-thirds target for the NLW was announced (in 2019) and immediately before the sharp rise in inflation, we can also use the HCI as a measure of inflation. The NLW was £8.21 an hour in April 2019. Figure 4.6 shows that from this point an NLW of £10.46 would have been needed in April 2024 to keep up with HCI for all households;[8] a rate of £10.19 to keep up with CPI; and £10.97 to keep up with RPI. The actual NLW rate of £11.44 exceeded all of these.

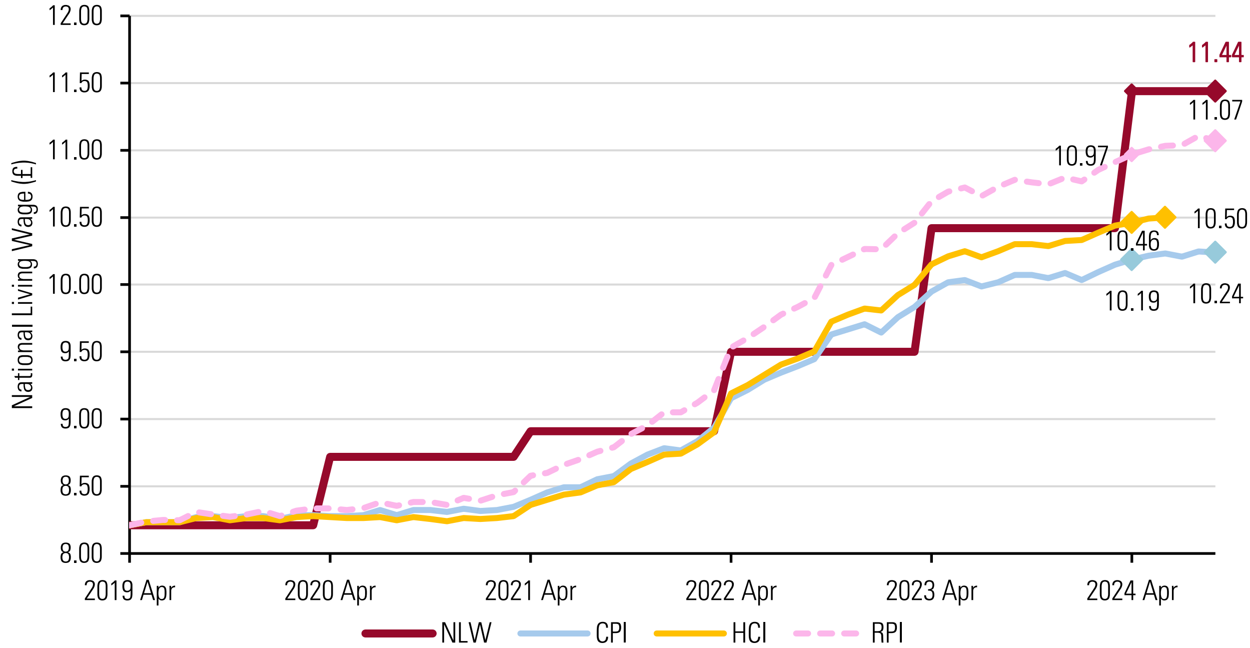
[8] It would also have been £10.46 if uprating in line with the average of deciles 1-3.

Figure 4.5: Uprating the National Living Wage by different price and wage inflation measures, UK, 1999-2024



Source: LPC estimates using ONS data. Consumer price index (D7BT), Consumer price index including housing costs (L522), and Retail price index (CHAW), monthly, UK, April 1999-September 2024; and Annual Earnings Index including bonuses (LNMQ), monthly, GB, April 1999-December 2000, and Average Weekly Earnings total pay (KAB9), GB, January 2000-August 2024.
Note: Price data are for the UK. Wage data are for Great Britain only.

Figure 4.6: Uprating the National Living Wage by different price inflation measures, UK, 2019-2024



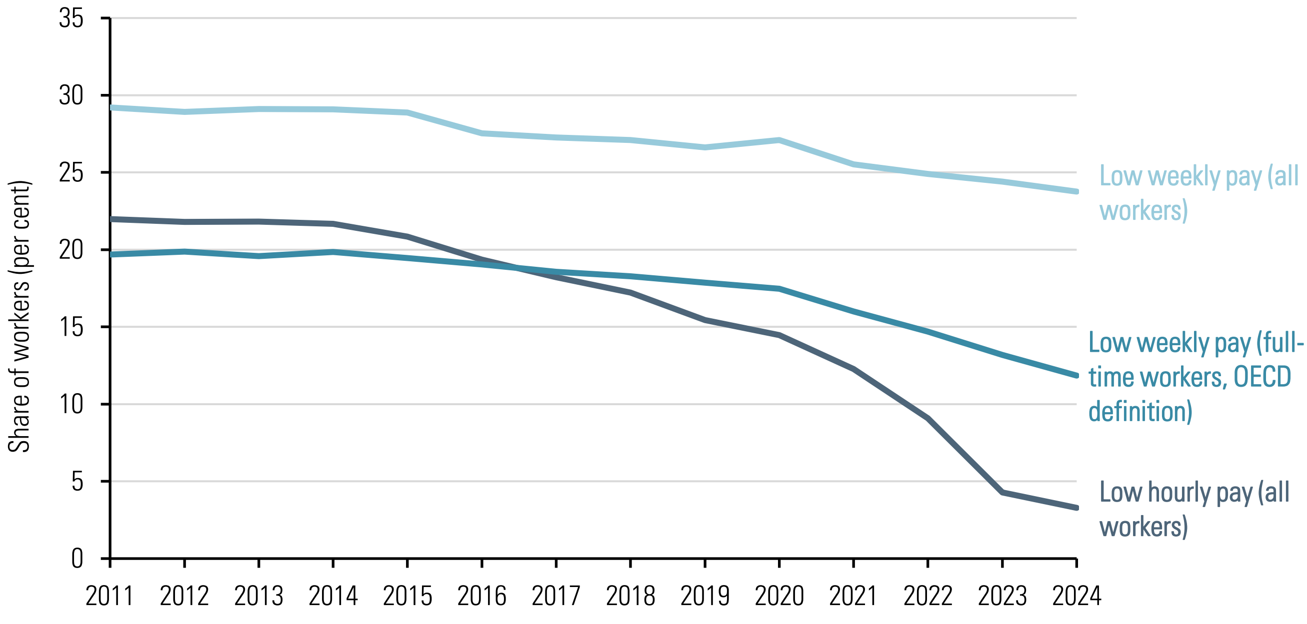
Source: LPC estimates using ONS data. Consumer price index (D7BT), and Retail price index (CHAW), monthly, UK, April 2019-September 2024; and Household costs index for all households (All items from Table 23: Household Costs Indices by all households, by division and selected groups, index (2015=100)). monthly, UK, April 2019-June 2024.

Progress in reducing hourly low pay has been more rapid than in reducing weekly low pay

4.23 The previous section showed that raising the NLW towards the two-thirds target meant the rate has more than kept pace with measures of price inflation. The two-thirds target was chosen as it is a recognised international measure of "low pay". The Organisation for Economic Cooperation and Development (OECD) defines low pay as earning less than two-thirds of median full-time earnings for workers aged 21 and over. The ONS applies this two-thirds metric to measures of both hourly and weekly low pay. Increases in the NLW have raised hourly pay, meaning fewer workers fall into the hourly definition of "low pay". As shown in Figure 4.7, around 3.3 per cent of workers are still considered to have low hourly pay, down from 4.3 per cent in 2023 but way down from rates of over 20 per cent before the NLW was introduced[9].

4.24 While progress in reducing low hourly pay is welcome, what really matters to workers' living standards is weekly pay. Workers' weekly pay depends on workers' hourly rate and the number of hours they work. Progress in reducing low weekly pay has been slower than for hourly pay, reaching 23.8 per cent in 2024 (down from 24.4 per cent in 2023). Likewise, low weekly pay among full-timers has also fallen slowly (by 5.7 percentage points since 2020, to 11.8 per cent). This suggests that increases in hourly pay for NLW workers have not translated into higher weekly pay, but as we show in the next section, this is not the case.

Figure 4.7: Share of employees that are low paid, UK, 2011-2024



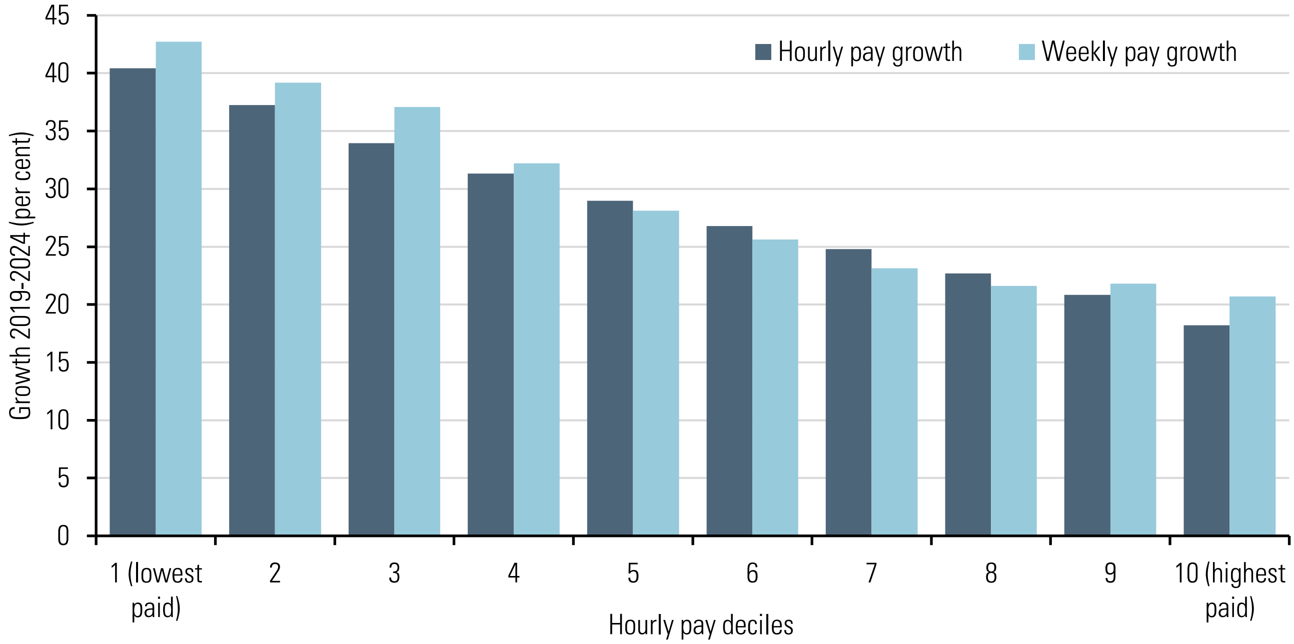
Source: LPC estimates of ASHE, SOC20 low-pay weights, 2011-2024, UK. Figures before 2020 use SOC10 weights and are chain-linked so they are on consistent basis with later figures. Both hourly pay and weekly pay measures exclude overtime. 'All worker' measures are for those aged 16 and over. OECD definition is based on full-time workers aged 21 and over.

[9] One reason that the share on low hourly pay is not zero despite the Government's target is that this includes all workers, not just those aged 21 and over (whom the target covered). We look at just those aged 21 and over later.

For low-paid workers, hourly pay increases have translated into weekly pay increases

4.25 The slower overall falls in weekly low pay outlined above could suggest NLW rises are not translating into higher weekly pay. There are plausible reasons this could be the case: NLW workers are more likely to work part-time and often face the challenge of getting enough hours to earn a sufficient income (see Chapter 3 for workers' experiences). They are also more likely to be underemployed – where a worker wants more hours in their current job, or another job with more hours. However, since 2019 growth in weekly pay for low-hourly-paid workers has surpassed growth in hourly pay (Figure 4.8). This implies that, over this period, average hours have increased for low-paid workers (discussed further in Chapter 5). In 2024, workers in the bottom two hourly pay deciles recorded weekly pay growth of over 10 per cent, stronger than growth in their hourly pay.

Figure 4.8: Nominal growth in mean hourly and weekly pay by hourly pay deciles, 21 and over, UK, 2019-2024



Source: LPC estimates of ASHE, SOC20 standard weights, 2019-2024, UK.

4.26 This raises a question: if the NLW has raised hourly pay, and these increases have translated into higher weekly pay, why hasn't weekly low pay fallen more? The answer is that the definition of weekly low pay includes many workers who aren't affected by the NLW. The UK labour market has many part-time jobs, some of which are well-paid. For example, an NLW worker doing 20 hours a week earns £228 a week[10]. Someone earning twice the NLW (and therefore in the top 30 per cent of all workers), but only working 10 hours a week earns the same per week. Both are counted as having low

[10] The 2024 NLW of £11.44 multiplied by 20 hours is £228.80 a week

weekly pay, but only the former's pay would be affected by increases in the NLW, as the latter's hourly pay is too high.

4.27 This relationship between low weekly pay and low hourly pay is illustrated in Table 4.1. For each decile of hourly pay, this table shows the share of workers in each decile of weekly pay. For example, the bottom right-hand cell shows that 84 per cent of those in the highest decile for hourly pay are also in the highest decile for weekly pay. This makes sense as these workers are overwhelmingly full-time. However, greater variation in hours worked among low-paid workers means more variation in their weekly pay outcomes than the highest hourly-paid workers. Of workers in the lowest hourly pay decile, just 38.5 per cent are also in the lowest weekly pay decile (top left cell). There are 12.3 per cent of workers with higher than median hourly pay (£17.19), who are in the bottom weekly pay decile. These are those workers we described earlier, who work few hours but have hourly rates higher than the NLW. Increases in the NLW have very little impact on the pay outcomes of these workers, and as a result cannot affect their low weekly pay. As part-time work has become more common in higher-paying jobs, the relationship between hourly and weekly pay has weakened.

Table 4.1: Share of employee jobs by weekly pay decile, conditional on hourly pay decile, UK, 2024

		Hourly pay decile									
		1	2	3	4	5	6	7	8	9	10
	Median pay	£11.45	£12.10	£13.08	£14.43	£16.12	£18.25	£21.10	£24.70	£30.15	£43.92
Weekly pay decile 1	£162.76	38.5	21.9	11.8	8.1	5.0	3.2	3.7	2.4	1.4	1.5
2	£310.47	25.6	23.2	17.2	12.1	7.4	4.3	3.1	2.5	2.5	1.3
3	£444.50	21.2	26.6	17.5	12.1	7.4	5.7	3.7	2.1	1.5	1.0
4	£507.98	9.5	17.4	34.2	22.7	6.8	3.3	2.3	2.2	1.0	0.7
5	£574.95	3.0	6.6	11.0	29.0	34.4	8.0	3.1	2.5	2.0	0.7
6	£657.75	1.4	2.5	5.2	9.9	25.5	41.9	9.0	2.9	2.2	0.6
7	£755.39	0.5	1.3	2.0	4.0	8.9	23.1	46.3	10.2	3.6	1.0
8	£882.31	0.2	0.4	0.8	1.8	3.3	7.6	22.2	50.9	11.7	2.0
9	£1069.39	0.0	0.1	0.2	0.4	1.1	2.5	5.8	22.3	61.2	7.0
10	£1558.70	0.0	0.0	0.0	0.1	0.1	0.4	0.8	2.1	13.0	84.1

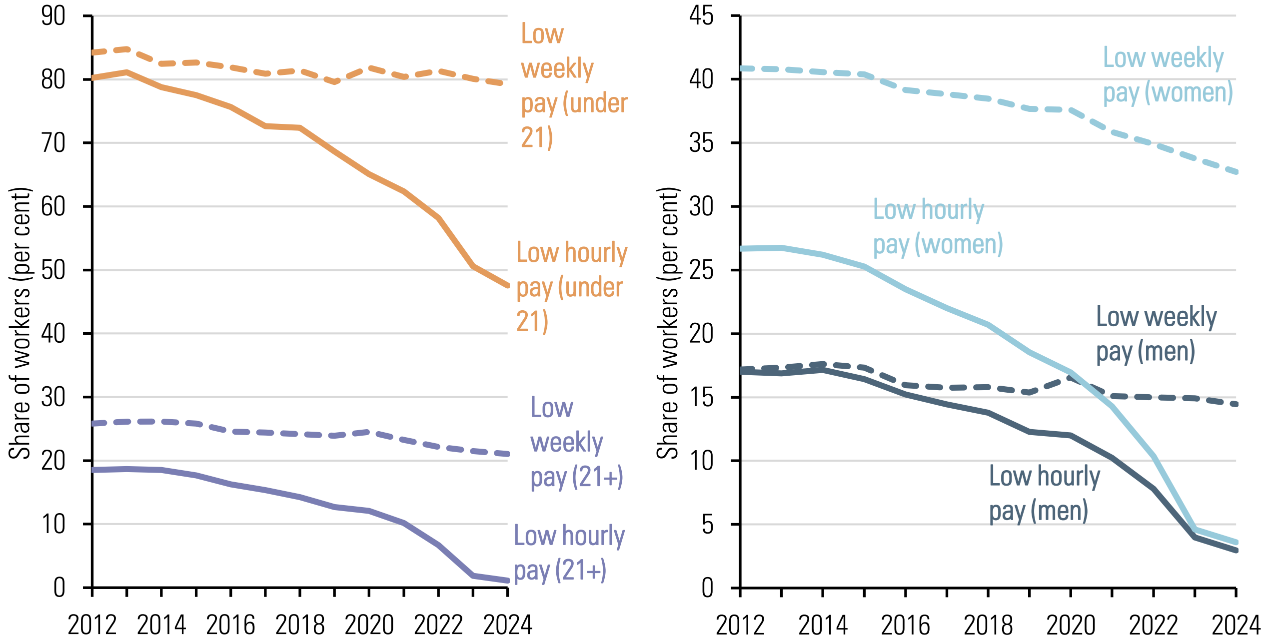
Source: LPC analysis of ASHE, SOC20 standard weights, 2024, UK. Both hourly pay and weekly pay measures exclude overtime.
Note: Figures shown are share of weekly pay decile. Each column sums to 100, although figures shown here may not sum exactly due to rounding.

Improvements in low pay outcomes have been broad-based

4.28 The improvements in low pay outcomes are seen across age and gender groups. Only 1.1 per cent of workers aged 21 or older are in low hourly pay, having fallen from 12.7 per cent in 2019 when the Government set the target for the NLW to reach two-thirds of median pay. While the incidence of low weekly pay for younger workers remains at around 80 per cent, the incidence of low hourly pay for workers aged under 21 fell below 50 per cent for the first time in 2024. Low hourly and weekly pay are more prevalent among younger people as they have lower age-specific minimum wages. They also usually work fewer hours than older workers (often because they are also in education).

4.29 The gender gap in low hourly pay has narrowed considerably in the past two years (Figure 4.9), falling by 9 percentage points. In 2024, 3 per cent of men and 3.6 per cent of women received low hourly pay. The gap in low weekly pay has also narrowed over the last decade, as a result of steeper falls in the rate for women – with the rate for men little changed. As women are more likely to be in minimum wage jobs than men, increases in the NLW have improved their relative position. At the same time, average hours worked by women have increased over the past decade.

Figure 4.9: Share of employees that are low paid, by age and gender, UK, 2012-2024



Source: LPC estimates of ASHE, SOC20 low-pay weights, 2012-2024, UK. Figures before 2020 use SOC10 weights and are chain-linked so they are on consistent basis with later figures. Both hourly pay and weekly pay measures exclude overtime. Low hourly and low weekly pay measures are defined relative to median earnings for all ages population. Right panel is for all ages.

Changes in the tax regime have affected take-home pay

4.30 Taxes also play a part in workers' incomes, so here we consider net pay (take-home pay after taxes). We begin with National Insurance Contributions (NICs), Income Tax (IT) and pension auto-enrolment for an individual on the NLW. Scotland and Wales can levy different rates of income tax rates and thresholds although only Scotland currently does this.[11] Our analysis therefore focuses on England, Northern Ireland, and Wales (the differences generally do not alter the findings for Scotland). Since 2019, the main changes implemented to these deductions from gross pay have concerned NICs. These are laid out below.

[11] Rates and thresholds for employers 2024 to 2025 - GOV.UK. In Scotland there is a starter rate of Income Tax of 19 per cent for earnings between £12,570 and £14,876, the basic rate of 20 per cent from £14,877 to £26,561 and the Intermediate Tax Rate of 21 per cent for earnings from £26,562 to £43,662. There are also differences further up the income distribution but well above the levels earned by minimum wage workers.

Recent changes to the UK tax regime

In the UK, Income Tax and National Insurance Contributions are levied on incomes above the personal tax threshold and primary threshold respectively. As shown in Table 4.2, these thresholds were different in 2019/20 – £240 for Income Tax and £166 for National Insurance. NLW employees could therefore work 20 hours a week before they started to pay NICs and 30 hours a week before paying Income Tax. Pension auto-enrolment is slightly more complex. NLW employees would start paying pension contributions if they earned more than £192 a week (above 23 hours a week) but the contribution would be based on earnings above £118 a week. The contribution rate of 5 per cent can be offset against Income Tax, effectively reducing the contribution rate to 4 per cent.

The thresholds for Income Tax and NICs were aligned in 2022/23 and have since been frozen at £242 a week. That means an NLW employee can work 21 hours a week before facing these deductions. The threshold for auto-enrolment is still £192 a week in 2024/25. However, with the NLW increasing, this means that an NLW employee starts paying pension contributions if they work more than 16 hours a week.

Since 2019, there have been several changes to the NIC rates (including increases to fund social care) but these were reversed with the rate cut from 12 per cent to 10 per cent in January 2024 and then to 8 per cent in April 2024. The rates of Income Tax and the auto-enrolment contribution have not changed since 2019.

Table 4.2: Changes in Income Tax, National Insurance and auto-enrolment for employees, England, Northern Ireland and Wales, 2019/20-2024/25

	Tax/NLW year (April-March)	
	2019/20	2024/25
NLW worker (£ per hour)	8.21	11.44
National Insurance Contribution weekly threshold for employees (£)	166.00	242.00
National Insurance Contribution rate for employees (%)	12.0	8.0
Income Tax weekly threshold (£)	240.00	242.00
Income Tax rate (%)	20.0	20.0
Auto-enrolment weekly threshold to start contributions (£)	192.00	192.00
Auto-enrolment weekly threshold for payments (if above other threshold) (£)	118.00	120.00
Auto-enrolment rate for employees (%)[b]	5.0	5.0

Source: HM Revenue and Customs.

Notes:

a. National Insurance Contribution thresholds are weekly. Income Tax and auto-enrolment thresholds are annual. We have estimated the weekly thresholds.

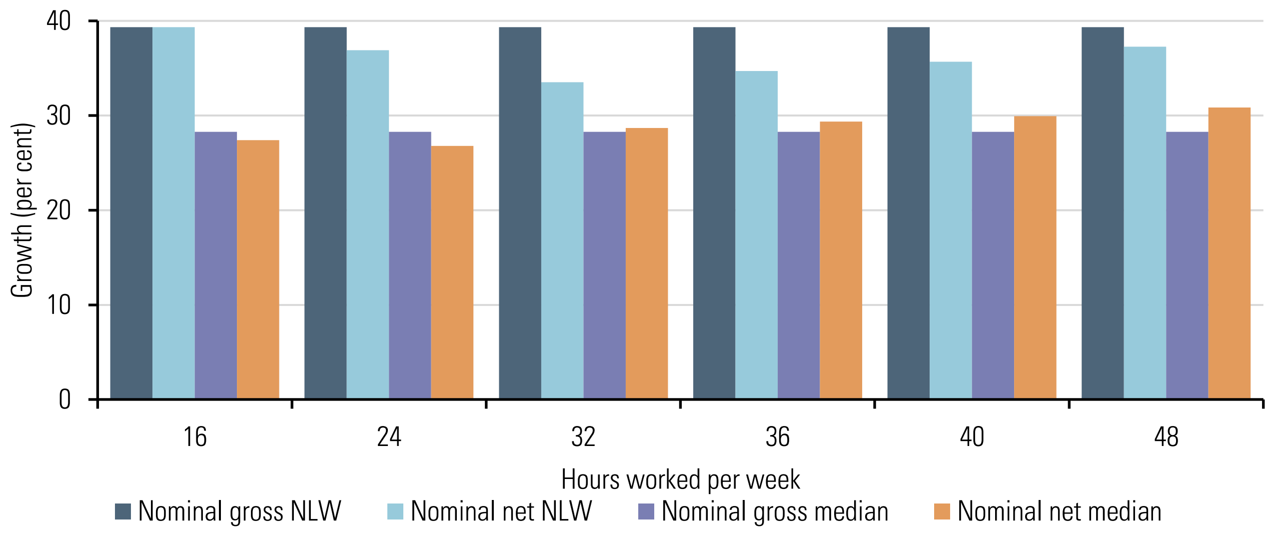
b. The auto-enrolment rate is 5 per cent for employees. However, the auto-enrolment contribution reduces employees' taxable income. So, for basic rate taxpayers this results in an effective reduction in take-home pay of 4 per cent.

Nominal and real net earnings have risen by more for NLW workers than for employees with median gross earnings

4.31 The dark blue bars in Figure 4.10 shows the 39 per cent gross increase in the NLW from £8.21 to £11.44 an hour for a range of different working hours. The change in those worker's net pay is shown by the light blue bars. Those working 16 hours remained below the tax thresholds throughout, and so their net and gross increases are the same. Regardless of hours worked, those on the NLW saw larger increases in net pay then those at the median (the orange bars). However, the freezing of the tax thresholds means NLW employees in 2024/25 working between 21 hours and 30 hours a week now pay income tax, whereas they did not in 2019/20. For those working 21 or 22 hours a week, the changes to NICs result in lower weekly NIC payments that offset the larger Income Tax payments. However, those working 23 hours or more paid more Income Tax and National Insurance in 2024/25 than 2019/20. Auto-enrolment payments have increased for those working more than 16 hours a week.

4.32 We can also see from Figure 4.10 that the changes from the three deductions overall affect NLW employees working 32 hours more than those working fewer hours (e.g. 16 or 24 hours) or more hours (e.g. 36, 40 or 48 hours). The change in net pay between 2019/20 and 2024/25 was 33.5 per cent for NLW employees working 32 hours a week. That compares with 36.9 per cent for those working 24 hours and 35.7 per cent for those working 40 hours a week.

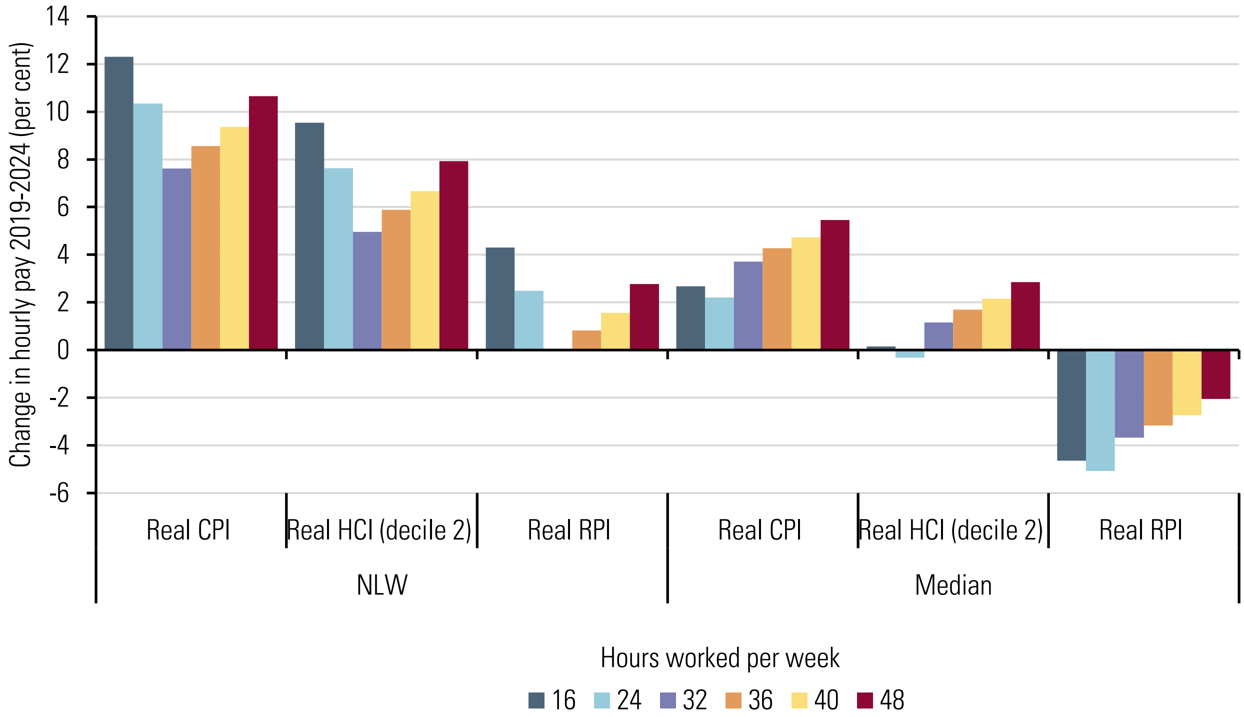
Figure 4.10: Change in nominal gross and net pay for National Living Wage workers and workers at the median, by hours worked, England, 2019/20-2024/25



Source: LPC estimates using HM Revenue and Customs information on thresholds and rates.
Note: The analysis has been conducted for England. Income tax rates and thresholds vary in Scotland and Wales.

4.33 The contrast between those paid at the median and NLW employees is more clearly shown when considering the change in real net pay. As shown in Figure 4.11, those on the NLW have experienced real net wage increases across the hours distribution. These real increases are larger if indexing against CPI than HCI. RPI is shown for illustrative purposes and, even then, all have experienced real increases in take-home pay. Real gains follow a U-shaped pattern, higher at the top and bottom of the hours spectrum. In contrast, for those paid at the median, Figure 4.11 shows much weaker real pay growth than for NLW employees.

Figure 4.11: Change in real net pay for National Living Wage workers and workers at the median, by hours worked, England, 2019/20-2024/25



Source: LPC estimates using HM Revenue and Customs information on thresholds and rates.
Note: The analysis has been conducted for England. Income tax rates and thresholds vary in Scotland and Wales.

4.34 In summary, NLW workers experienced faster increases in their gross and net pay between 2019 and 2024 than those paid the median wage. They also experienced larger real increases in take-home pay (irrespective of the inflation index used).

4.35 In the analysis above, we have not considered the interaction with the benefits system. This is more complex to consider as benefits are determined by the composition of the household and total household income. However, we should note that an employee who is a basic rate taxpayer (for example, any NLW employee working more than 21 hours a week) on Universal Credit will be subject to a marginal effective tax rate of 69 per cent. That is, for every extra £1 of gross income, they will only get to keep 31 pence.

Household income standards

4.36 While comparisons of wage and income growth to inflation measures tell us whether wage increases have kept pace with prices, they do not provide any information as to whether that *level* of income is sufficient to provide an adequate standard of living for the worker. One way to do this is by constructing a basket of goods and services that people need to achieve a basic living standard, and comparing its cost with household incomes.

4.37 The key question is what to include in the basket in the first place. Measures of inflation, such as CPI, are constructed based on the expenditure shares of different goods and services across the economy as a whole. This whole economy representative basket is unlikely to match to the consumption basket of any particular individual or even subset of the population, and therefore is unlikely to identify the actual cost of living for any such individual or group

Income standards are useful in assessing the adequacy of policy, but reflect judgements about living standards

4.38 The Joseph Rowntree Foundation (JRF), working with the Centre for Research in Social Policy at Loughborough University, has developed the Minimum Income Standard (MIS). The MIS is a basket of goods and services that constitutes a "minimum socially accepted standard of living". JRF constructs baskets for different types of households based on gender, marital status, pensioner status, and number and age of children. It then calculates the costs of each of these baskets and can produce a minimum standard for over 100 different household types[12], implying a different hourly wages requirement for each.

4.39 JRF's analysis claims that the gross income needed to reach a minimum acceptable standard of living in 2024 was £28,000 for a single person and £69,400 (joint) for a couple with two children. A person working full-time (37.5 hours) on the NLW in 2024 would earn £22,368 for the year, thereby falling short of the minimum standard as calculated by JRF.

4.40 Needs-based basket of goods approaches are subjective. However, the JRF's standard is underpinned by a rigorous, extensive and wide-ranging consultation with members of different household types, to reach a consensus over the "minimum socially accepted standard of living." The standard is updated every two years, to track changing conceptions of living standards over time. The judgements participants make reflect the core definition that a minimum standard of living "is more than just, food, clothes and shelter. It is about having what you need in order to have the opportunities and choices necessary to participate in society." In this way construction of the basket is not a statistical exercise in the same way that construction of inflation indices is.

4.41 Citizens Advice have published their own tool for understanding the impact of policy choices on living standards, the National Red Index. This uses detailed data from more than 300,000 individuals who have approached Citizens Advice for debt advice, "to understand what people at the sharp end of the living standards squeeze actually spend on costs like food, clothes and energy." Citizens Advice advisors help people in debt to restructure their spending; the National Red Index then combines this data on individuals' spending with national survey data on people's incomes and fixed costs like rent and council tax, to model how many people have a negative budget – that is, in a situation where their outgoings exceed their income. As such, the spending assumptions used by Citizens Advice reflect something other than the JRF's "minimum socially accepted standard of living"; Citizens Advice describe this as reflecting people's "revealed basic needs." These are "based on the real choices people make to stay afloat, and what they choose to prioritise when the chips are down."

4.42 This allows Citizens Advice to model the extent to which different policy interventions would lift individuals out of negative budgets. In October, they modelled that an NLW of £12.10 (our central

[12] More details on the JRF methodology can be found on the JRF website: https://www.jrf.org.uk/a-minimum-income-standard-for-the-united-kingdom-in-2024

projection at the time) would lift around 30,000 people, or 13,000 households, out of negative budgets. This would be a reduction of around 9.6 per cent.

4.43 Citizens Advice's work is not directly comparable to the JRF's, but it illustrates the point that there are different ways of assessing the adequacy of policy interventions when it comes to living standards. These can be based on a consensus view on the minimum individuals need to participate in society; it could be a narrower assessment of the minimum needed to survive, or a more generous one on standards that go beyond the minimum. Such standards help us understand the adequacy of the minimum wage in meeting people's needs, but there is still a large element of judgement in assessing where a genuine living wage should lie.

4.44 In our own advice to the previous Government on the NMW Beyond 2024 (2024b) we considered a number of different approaches to taking account of living costs for setting future rates of the NMW. At the time we argued that formula-based living wage approaches were unsuitable for national policy making. They can be overly complex, less responsive to economic conditions and leave less influence for the views of employers and workers. We agreed with our employer and worker stakeholders that living standards should be a key consideration for minimum wage decisions, but doing this need not be formulaic.

There is limited international evidence on the use of needs-based minimum wage setting

4.45 The European Union's directive (Official Journal of the European Union, 2022) on adequate minimum wages, adopted in October 2022, must be signed into national law by November 2024 (Eurofound, 2024). It states that minimum wages are considered to be adequate if "they are fair in relation to the wage distribution in the relevant Member State and if they provide a decent standard of living for workers based on a full-time employment relationship". Most EU countries have focused on the former rather than the latter. Only two EU countries – Romania and Slovenia have passed laws to introduce a statutory living wage. In Slovenia, the calculation of the minimum wage is based on a formula which takes into account the cost of living. In Romania, the law provides a method for estimating the living wage and stipulates that the minimum wage should take into account this estimate; but this approach has not yet been implemented. The Irish Low Pay Commission (2022) also considered adopting a needs-based living wage approach but recommended against using the Minimum Essential Standard of Living (MESL) approach for setting its National Minimum Wage in favour of a target approach, similar to that initially adopted in the UK (set at 60 per cent of the median hourly wage).

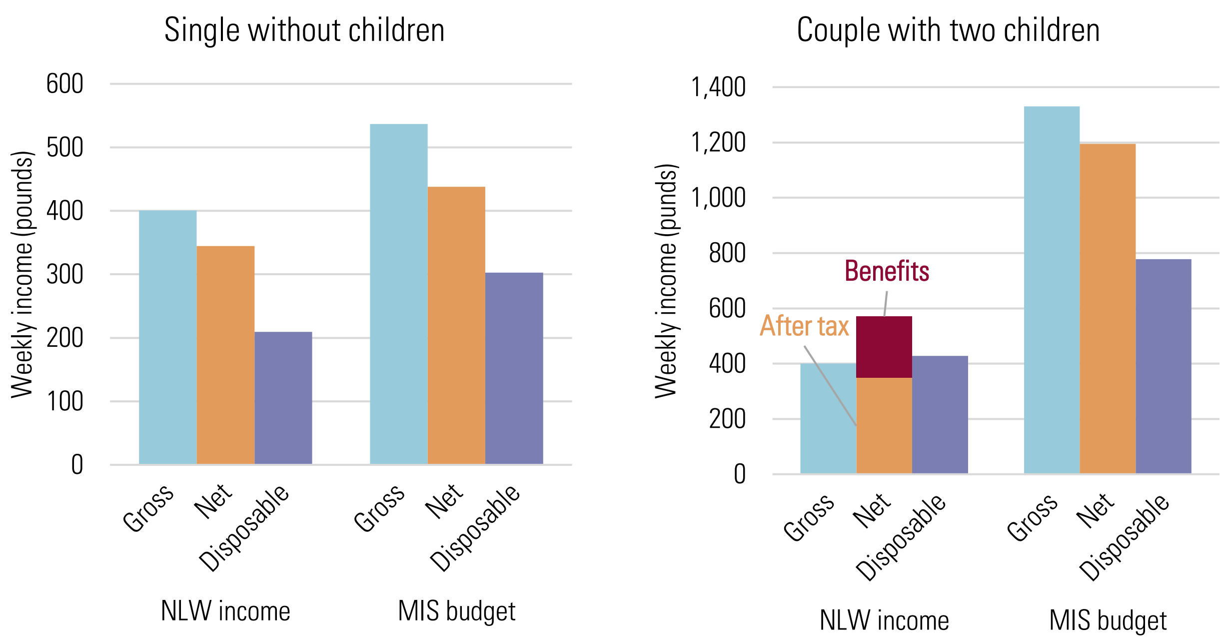
The NLW does not operate in isolation

4.46 Although the NLW aims to give people a meaningful wage for their work, it is a blunt tool that cannot address all inequalities and living standard concerns in and of itself. The minimum wage sets a wage floor applying to almost all adult workers irrespective of their household circumstances. To be effective and credible as a labour market instrument it must have regard for economic conditions, business competitiveness and labour supply and demand. Other policies and support mechanisms, including the welfare system, are more adept at targeting residual inequality and deficiencies in living standards.

4.47 As already noted, interactions with the welfare system are complex and highly dependent on individual circumstances, but we can supplement our net pay analysis to illustrate how certain people fare after benefits. In Figure 4.12 we exclude housing, council tax and childcare as these can all be dependent on how much individuals actually pay for those services. Because of this it is best to compare the purple 'Disposable' columns below as these show how NLW incomes compare with the MIS budget after housing and childcare costs (as measured by JRF) have been deducted from both sides.

4.48 We see that a single person without children who works full-time at the NLW does not receive any benefits – they still fall short of the MIS calculated by JRF. A married couple with two children, where one member of the couple works full-time and the other does not work, would benefit from Universal Credit and child benefit. Although their position improves after taking into account benefits, it still falls short of JRF's MIS requirement.

Figure 4.12: Comparison of NLW income with JRF Minimum Income Standard, England, 2024/25



Source: LPC estimates using HM Revenue and Customs information on thresholds and rates, and Joseph Rowntree Foundation (2024).
Note: Calculations exclude housing, council tax and childcare assistance. After tax is after income tax, national insurance contribution, and pension auto-enrolment. Disposable income is income after taxes, benefits, rent and childcare. Assumes working 35 hours per week. In the right panel, one member of the couple is assumed to work 35 hours/week, while the other does not work.

4.49 Needs-based basket of goods approaches embody some of the difficulties with taking living standards into account. Constructing a basket requires decisions about who the basket is for, and what is appropriate to include. However, we have also seen that minimum wage workers live and work across the country, in a range of different household and family situations, and with a variety of needs. Further, even if a needs-based approach can construct baskets for all these different household types, the challenge remains to map these various assessments of need into a single minimum wage figure. Such an exercise requires assumptions about hours worked, other sources of income, and how to weight different households.

4.50 Stakeholders gave their views on how we might interpret the living standards aspect of the remit. The Confederation of British Industry (CBI) felt that the cost of living was "not an economic term – it's highly subjective to talk about." It acknowledged the existence of some quantitative measures but argued that inflation stood out as truly objective and "that should have primacy when we're thinking about the cost of living." They and others also argued that the cost of living was to some extent already reflected in the NLW. The CBI saw the new remit as "a rhetorical change that doesn't appear to us to be a material change." British Beer and Pubs Association (BBPA) and UKHospitality argued that cost of living already "does get reflected in the average earnings" component which informed the NLW's bite target.

4.51 The Trades Union Congress (TUC) had concerns with "basket of goods" approaches: "we just don't think that you can do that in a way that gives a fair assessment of the different costs that different households experience." In addition, "it's not appropriate, as the economy grows … to determine workers' share of that growth as a result of changes in other measures." For example, changes in childcare or benefits policy would affect the calculation of the wage a worker needs. "We wouldn't want an approach that unwittingly led to a reduction in the contribution to living standards that wages would make below what was economically deliverable."

4.52 The TUC's view was "a higher proportion of median wages should be the target." Ensuring real wage growth should be treated as a baseline expectation but "we don't think a real living wage is best measured through looking at the relationship between that wage and inflation. We think wage rises should continually move beyond inflation and that's the best way to ensure that workers share in the rewards of growth and see their living standard improve."

Conclusion

4.53 Our remit asked us to specifically look at living costs for the first time, though in practice both actual and forecast inflation have always been part of our considerations when making our recommendations. While minimum wage workers are found throughout the household income distribution, they are more likely to be towards the lower end. Those near the bottom are often most reliant on the NLW as the household's main earner. For this reason, we have placed more weight on living costs of those on lower incomes. These workers were hit hardest by the recent inflation, spending more of their income on the food and energy whose prices increased so abruptly. While inflation has fallen, prices have not – they are still far higher than a few years ago and we heard about the toll this has taken on many workers.

4.54 However, it's important to remember that concerns about living standards did not start in 2022. The UK has suffered a fifteen-year real wage squeeze since the financial crisis. This is not only historically unprecedented, but poor by international standards. Only a handful of OECD countries have seen a similar or worse performance (see Appendix 4). So, it should not be surprising that the recent high inflation in 2022 had such a huge impact. And yet over its life, the NMW has grown faster than all metrics of living costs. Even over the period covering the pandemic and the recent inflationary spike, the NLW has risen faster than living costs.

4.55 Living standards among low-paid workers are not just determined by their hourly wage rate; their hours of work and how they are taxed also matter. Slower progress in reducing the number of workers whose weekly pay is below two thirds of the median is not because NLW increases are not translating into weekly pay increases. On the contrary, increases in weekly pay match or exceed increases in the NLW for workers on the wage floor. Instead, the abundance of part-time work with pay above the minimum but relatively few hours obscures the picture. Many of these jobs count as having low weekly pay, even with high hourly rates, because they involve few hours of work. Even with changes in tax thresholds and rates, real net pay (after deductions for tax) for NLW workers has risen faster than for workers at median pay levels.

4.56 While comparisons with inflation measures tell us whether NLW increases have kept pace with prices, they do not tell us whether the earnings of NLW workers are sufficient for their needs. This is what many would understand 'a genuine living wage' to mean. However, the LPC has previously set out the risks arising from solely focusing on a basket of goods and services to set the minimum wage. Defining the goods and services to include in such measures requires judgement and different households can have vastly different needs. This can make these approaches complex, subjective and unpredictable. Focusing on living costs to the exclusion of other evidence means not taking account of economic circumstances, which would harm the credibility of the LPC's recommendations. Sole focus on living costs also diminishes the voices of workers and employers in making decisions, undermining the social partnership approach of the LPC. We have spoken with employer bodies, trade unions, think tanks and academics about how to take living costs into account; none advocated for a basket of goods approach to determining the level of the minimum wage and many have pointed out the problems it creates.

4.57 In Chapter 10 we explain how we took expectations of future inflation into account and in Chapter 11 how all of this fed into our recommendations this year.

Chapter 5

The National Living Wage

Key findings

- **The National Living Wage increased relative to median pay in 2024, reaching 66.5 per cent of median pay for those aged 21 and over in April 2024, up from 64.5 per cent a year earlier –** However, despite the large increase in the NLW, it fell short of the Government's target to reach two-thirds of median hourly earnings by October 2024. A change to the ONS' methodology meant that median pay reported for 2023 was significantly higher than reported at the time the 2024 rates were decided.
- **The share of jobs paid at or below the NLW, increased for the first time since 2016, but remains below pre-pandemic levels –** Part of this increase was due to the inclusion of 21-22 year olds in the NLW, but most of the increase resulted from higher coverage for existing NLW eligible workers.
- **Relative pay differentials became more compressed in 2024, particularly in low-paying industries –** An increasing number of businesses cite pay compression as one of their main concerns as it reduces incentives for workers to take on roles with greater responsibility. Pay differentials were most compressed in very large firms, while they remained smallest in micro businesses.
- **Fewer minimum wage workers moved off the minimum wage this year, but the rate of progression remains higher than in 2019 –** Similarly, the pay premium for switching employers fell a little over the past year, but remains higher than pre-pandemic levels.
- **Jobs growth in low-paying industries has been lower than in other industries since the pandemic and has slowed recently –** However, it is difficult to separate out the causes of this, including the impacts of the pandemic on consumer facing services, the long-term decline in retail, cost-of living pressures, and the minimum wage. Despite the slowdown in some low-paying sectors, employment rates remain healthy among demographic groups that are most likely to be low paid and in the parts of the country where low-paid jobs are more common.
- **Data quality issues continue to hamper our ability to get a strong read on the employment outcomes of workers likely to be affected by the minimum wage –** These data issues also mean we have no robust statistical evidence to assess the employment impact of the NLW. Nevertheless, our view is that although conditions in the low pay labour market have softened it does not appear that weakening outcomes are a result of increases in the NLW.

5.1 This chapter summarises the evidence on the impacts of the 2024 increase in the National Living Wage (NLW) on pay and employment. We look at how the increase in the NLW affected the pay distribution, and explore how pay, hours and employment changed across different industries, firms, regions and personal characteristics. We compare outcomes for jobs and workers where minimum wage work is most common with outcomes for better-paid jobs and workers. We also summarise the internal and external research on the pay and employment impacts of the NLW.

Coverage and bite of the National Living Wage

The NLW is the highest it has ever been relative to median wages, but failed to reach the two-thirds target in 2024

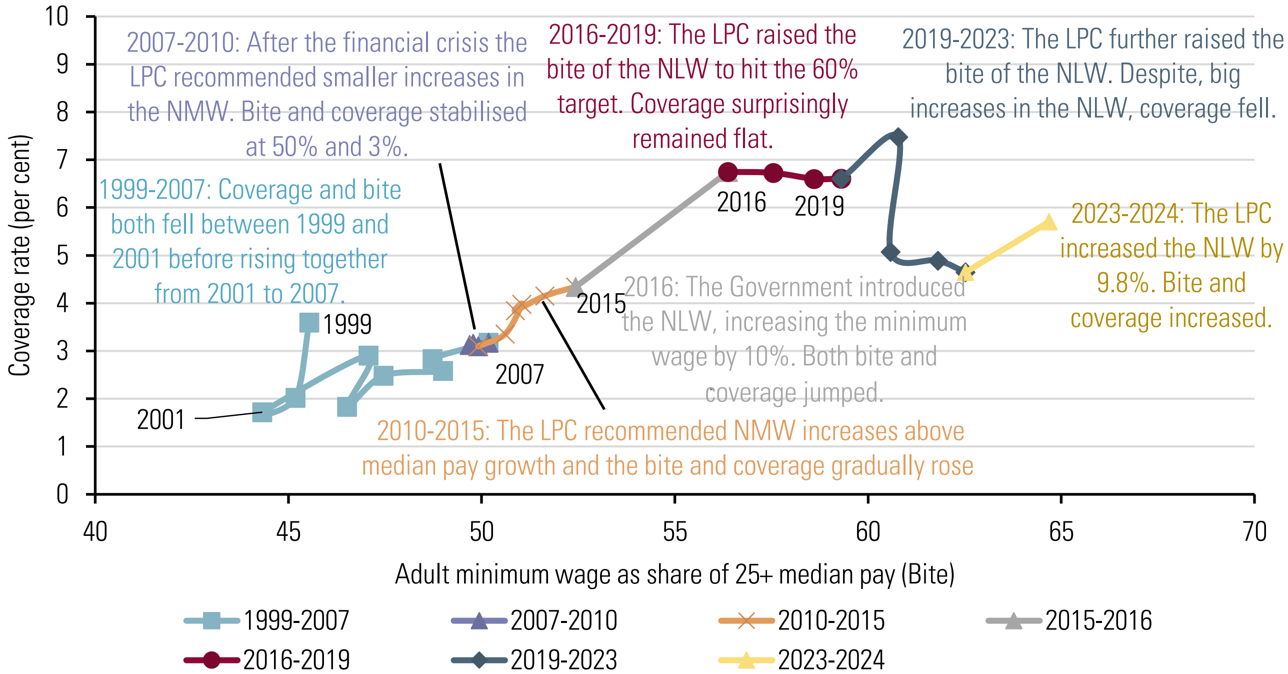
5.2 In 2024 the bite of the NLW (its value as a share of median hourly earnings) increased to its highest ever level, reaching 66.5 per cent in April 2024, up from 64.5 per cent a year earlier. However, the NLW fell short of the Government's target of two-thirds of median earnings in October 2024 (the mid-point of the financial year). We estimate that by October the bite had fallen to 64.9 per cent, and an NLW of £11.76 would have been needed to meet the Government's target.

5.3 When the Commission recommended the NLW rate for 2024, we did so believing that (subject to the usual uncertainty associated with forecasts) the rate of £11.44 would be sufficient to reach the two-thirds target. There are two main reasons why this did not happen – Office for National Statistics (ONS) revisions to the 2023 pay data, and our wage forecasts undershooting realised wage growth.

5.4 Each year the ONS revises the Annual Survey of Hours and Earnings (ASHE) data for the previous year. This year the revisions were larger than normal because of a methodological change made by the ONS. The change meant that observations that had previously been considered 'outliers' were now included in the dataset after investigation revealed them not to be outliers. This resulted in the inclusion of more higher-paid workers, which in turn pushed up median pay for 2023. This meant when forecasting pay for 2024, the Commission was doing so from a lower 2023 base than was published this year.

5.5 In addition, pay growth in 2024 ended up being stronger than forecast. We base our projections on the forecasts made by other public and private sector forecasters (for more detail on our method see Chapter 10), so we were not alone in being surprised by the strength in pay growth. Nevertheless the impact of the forecast miss was much smaller than the impact of the revisions to the 2023 data.

Figure 5.1: Bite and coverage rate of the adult minimum wage, 25+, UK, 1999-2024



Source: LPC analysis of ASHE 1999-2024, low-pay weights, UK, 25+ population. Excludes first year apprentices from 2013 onwards. Apprentices cannot be identified before then, so Apprentices aged 25 and over are included pre-2015. Coverage rate and bite are calculated for 25+ population rather than eligible population. There is increased uncertainty around coverage rate figures in 2020 and 2021 due to pandemic related data issues.

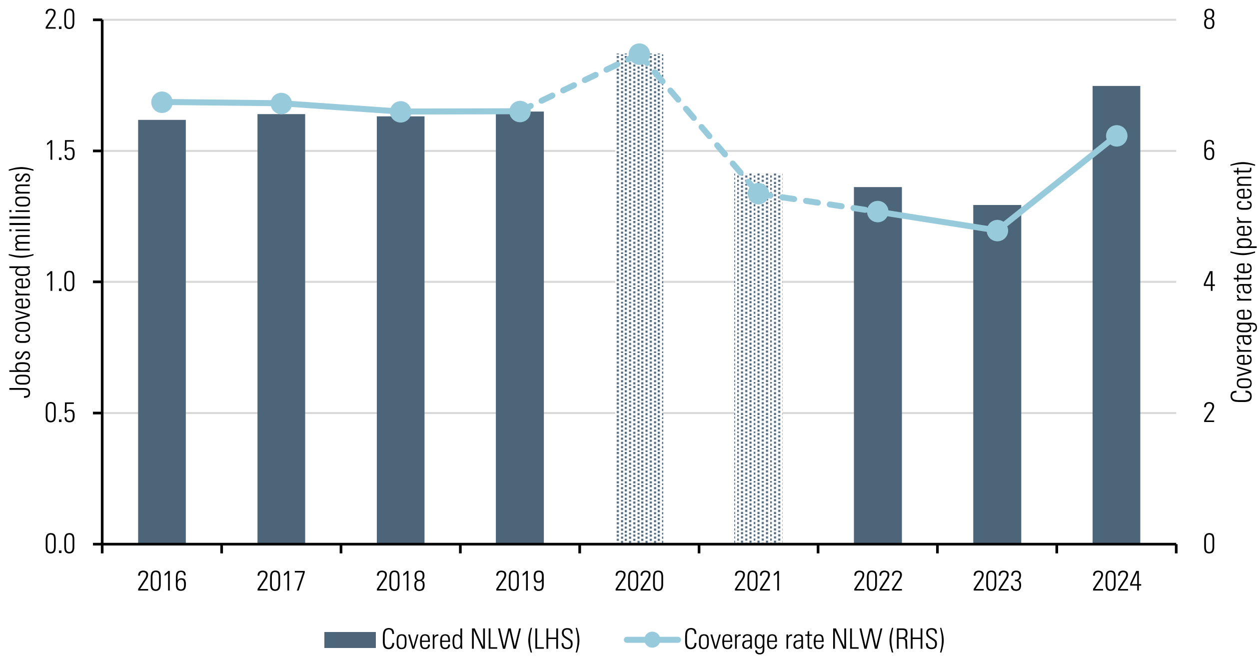
The coverage rate increased for the first time since the NLW was first introduced

5.6 The coverage rate is the share of jobs paid up to 5 pence above the NLW. In 2024 it increased to 6.2 per cent, up from 4.8 per cent in 2023. This represents an additional 454,000 NLW workers paid at or below the NLW, taking the total number of NLW workers to 1.75 million. Despite this increase, the coverage rate is still lower than it was pre-pandemic.

5.7 While the bite of the NLW has increased significantly since 2016, coverage has fallen for most of that period – 2024 represents the first meaningful increase in coverage since the NLW's introduction. It comes against the backdrop of weak economic growth in the second half of 2023 and a softening, although still healthy, labour market. Chapter 3 looked in more detail at who minimum wage workers are and how coverage has changed for different sub-populations.

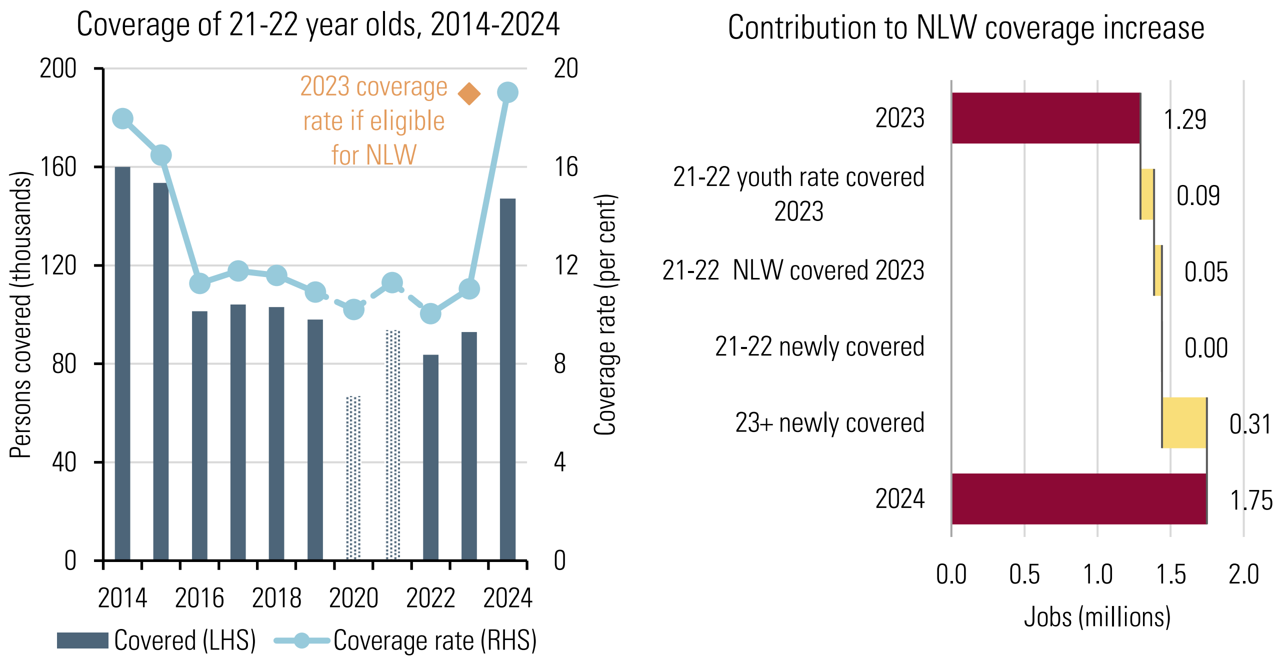
5.8 Around one third of the increase in NLW coverage (147,000 jobs) was due to 21-22 year-olds becoming eligible for the NLW this year. This increase in coverage was expected – the share of 21-22 year olds covered by the NLW this year is comparable to the share of 21-22 year olds that would have been covered by the NLW in 2023 had they been eligible for the NLW (the orange diamond in the left panel of Figure 5.3). The remainder is increased coverage among those aged 23 and higher.

Figure 5.2: NLW coverage and coverage rate, NLW eligible population, UK, 2016-2024



Source: LPC analysis of ASHE 2016-2024, low-pay weights, NLW population, UK. Figures are chain-linked to account for methodology change in 2021.

Figure 5.3: Coverage of 21-22 year olds, UK, 2014-2024



Source: LPC analysis of ASHE 2014-2024, low-pay weights, 21-22 population (left panel) and NLW population (right panel), UK. Figures are chain-linked to account for methodology change in 2021.

Delays to public sector pay increases affected the coverage data this year

5.9 Measurement issues also contributed to the increase in coverage this year. We estimate coverage using ASHE, which is conducted in April, the first month of the new financial year. Each year at the time of the survey, some workers' pay has not yet adjusted for the new financial year. This year two factors meant that slow pay adjustments impacted the coverage estimates more than usual.

5.10 Firstly, the NLW has caught up to the lowest pay bands in some public sector organisations. As a result, delays to public sector pay increases meant that in April 2024 some public sector workers' pay was only equivalent to the NLW, even if they later received pay increases (backdated to April 2024) taking their hourly rate above the NLW.

5.11 Pay increases for many public sector workers for 2024/25, including prison officers and NHS workers, were only announced in July, with workers receiving the increases (with backpay) in the autumn. For example, Band 1 and 2 NHS workers, who were paid an equivalent hourly rate of £11.45 for 2023/24 continued to be paid that rate in April 2024, when ASHE was conducted. Because we consider a worker 'covered' by the NLW if they are paid up to 5 pence above the NLW, these workers have been classified as covered in 2024. Subsequently, NHS Band 1 and 2 NHS workers received a pay increase backdated to April to take their hourly rate for 2024/25 to £12.08.

5.12 Similarly, Band 2 prison officers based outside London, whose 2023/24 hourly rate was below the new NLW, received a pay increase in April to bring them up to the NLW. They received a further 5 per cent pay increase in the autumn (backdated to April, taking their hourly rate to £12.03) following the recommendation of the Prison Service Pay Review Body.

5.13 Secondly, employers are not required to pay the new NLW until the start of the first pay period following the start of the new financial year. If the first pay period of the new financial year begins after the ASHE survey period, then these workers appear in the data to be paid at or below the NLW even if they receive the NLW or higher in the next month. This issue is also not new – each year there are many employers whose first pay period of the year commences after the ASHE survey date. However, this year one of the UK's largest employers fell into this group, meaning this measurement issue had a bigger impact than it has in the past.

5.14 Although these measurement quirks are not new, this year they had a bigger impact on our coverage estimated than in the past. We estimate that without the delays to NHS pay increases, coverage would be up to 0.24 percentage points lower than reported. We estimate if the large employer's pay period commenced before the ASHE reference date coverage would be another 0.15 percentage points lower. However, both issues are likely to continue to affect the coverage data in the future. If the NLW continues to increase faster than overall public sector pay, it is likely to catch up to more public sector pay bands and further temporarily inflate coverage numbers in the event of pay award delays.

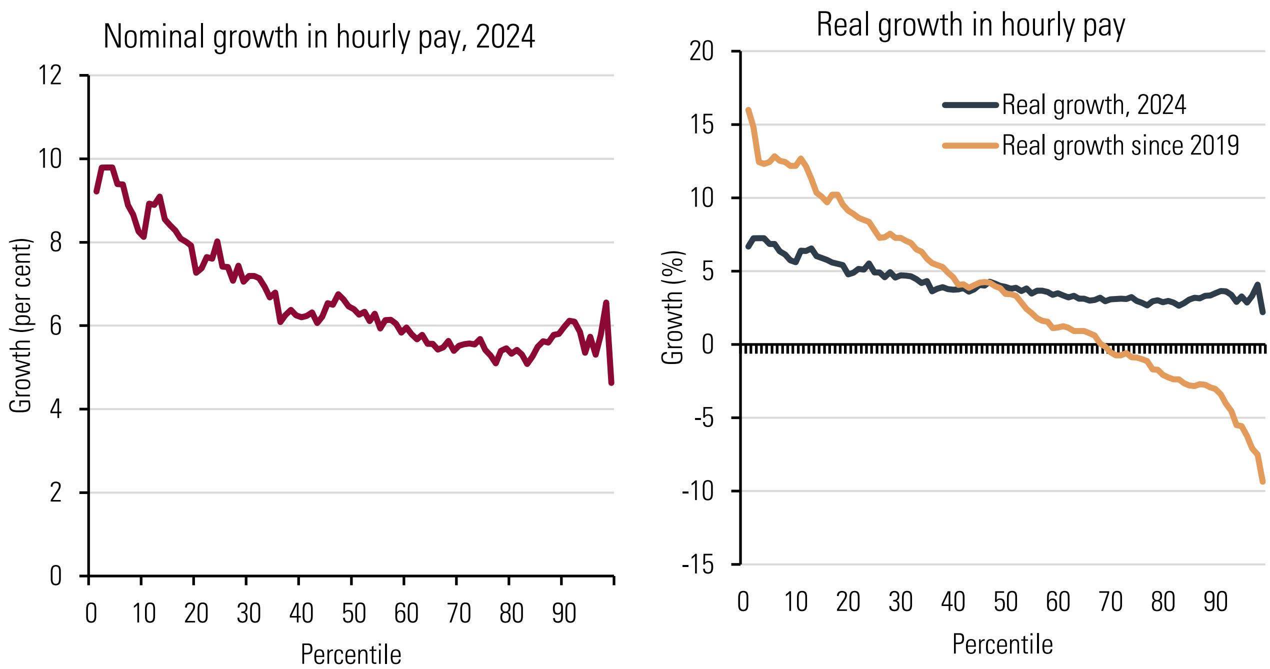
Pay growth

Pay growth was strongest at the lower end of the pay distribution

5.15 In 2024, hourly pay rose strongly across the pay distribution, but more so at the lower end – as has been the case in the past few years (Figure 5.4 left panel). NLW workers recorded the largest annual pay increases, of 9.8 per cent, against growth in median pay of 6.4 per cent, and growth at the 90th percentile of 6 per cent. Median pay growth was also stronger in low-paid industries than in other industries, although growth slowed relative to the previous year. Median pay growth in low-paid industries increased by 7.4 per cent, while median pay growth in other industries was 5.8 per cent.

5.16 With the inflation rate falling, these nominal pay increases also resulted in real pay increases (Figure 5.4 right panel). Between April 2023 and April 2024, NLW workers received a real pay rise of 7.2 per cent, while the median worker saw a 3.9 per cent rise. Since 2019, real wages have increased by 12.4 per cent for NLW workers but have fallen for top earners (the top third of the distribution).

Figure 5.4: Nominal and real hourly pay growth by pay percentile, 21+ population, UK, 2024



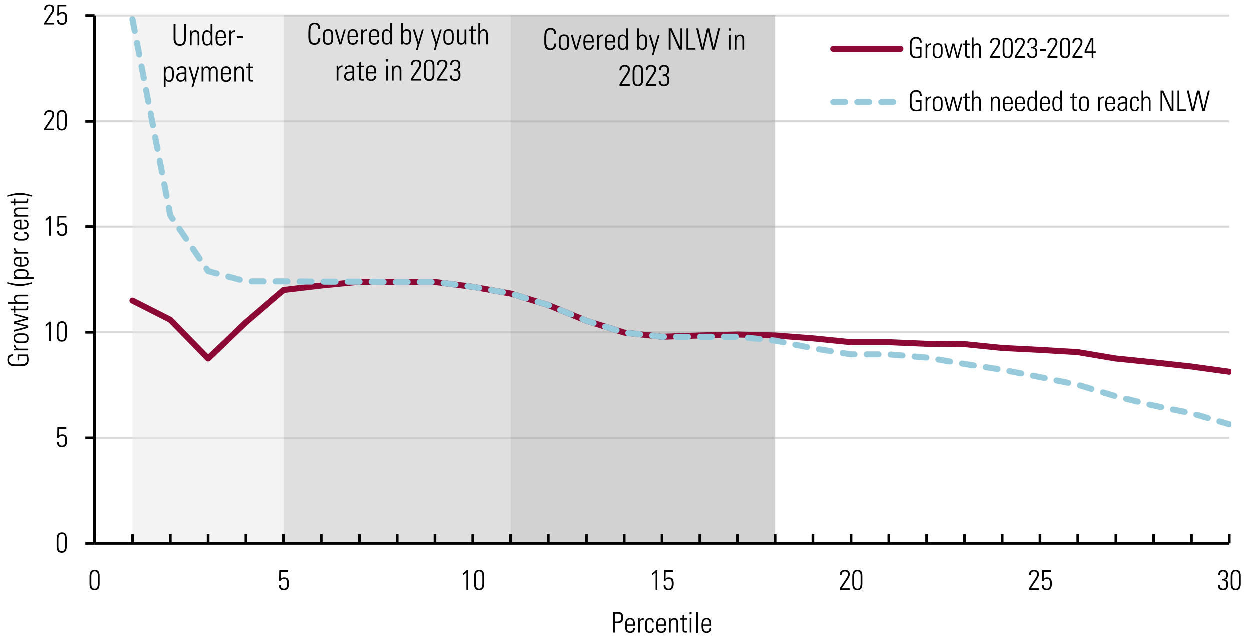
Source: LPC analysis of ASHE 2019-2024, standard weights, 21+ population, UK. Figures in right panel are chain-linked to account for methodology change in 2021.

5.17 Some of the strength in pay growth at the lower end of the distribution is likely due to spillovers from the NLW. Employers often point out that NLW increases influence pay rises for other workers as they try to maintain pay differentials between different roles and levels of experience. As can be seen in the left panel of Figure 5.4, pay growth for workers between the 6th percentile (NLW workers) and the 35th percentile is higher than pay growth for most other workers further up the pay distribution. While it is difficult to measure precisely, the additional pay growth these workers receive provides a rough estimate of the spillover effect generated by the NLW.

5.18 For example, pay for workers at the 13th percentile increased from £11 to £12 (or around 9 per cent) in 2024. If we assume that these workers would have received a 6 per cent pay rise absent any NLW increase (around the average pay growth received by workers from the 35th to the 80th percentile), then we can attribute the additional 3 percentage points of growth to NLW spillovers. This implies that around a third of the £1 pay increase received by these workers was due to NLW spillovers. This spillover effect becomes smaller as you move along the distribution. While difficult to measure precisely, the data are clear that workers who are paid the NLW are not the only ones to benefit from an increase in the NLW. Roughly the bottom third of all jobs receive a higher pay increase than they otherwise would have done following an NLW increase.

5.19 The lowering of the age of eligibility for the NLW to 21 years meant that pay increases for 21 and 22 year olds on the minimum wage were higher than for those already eligible for the NLW. Outside of cases of underpayment, 21 to 22 year olds previously paid between the youth rate and the NLW received pay increases to bring them up to the NLW and no further. This is shown in Figure 5.5 where the wage growth 21-22 years received (red line) matches the growth they needed to reach the NLW (dotted blue line).

Figure 5.5: Nominal hourly pay growth by pay percentile, 21 and 22 year olds, UK, 2024



Source: LPC analysis of ASHE 2023-2024, standard weights, 21-22 population, UK.

Businesses are increasingly concerned about pay compression

5.20 Faster pay growth for lower-paid employees than for those higher in the earnings distribution compresses relative pay differentials. The challenge of maintaining differentials is perceived by many employers as the largest impact of the NLW – they believe that narrowing differentials can create problems of morale, retention and progression.

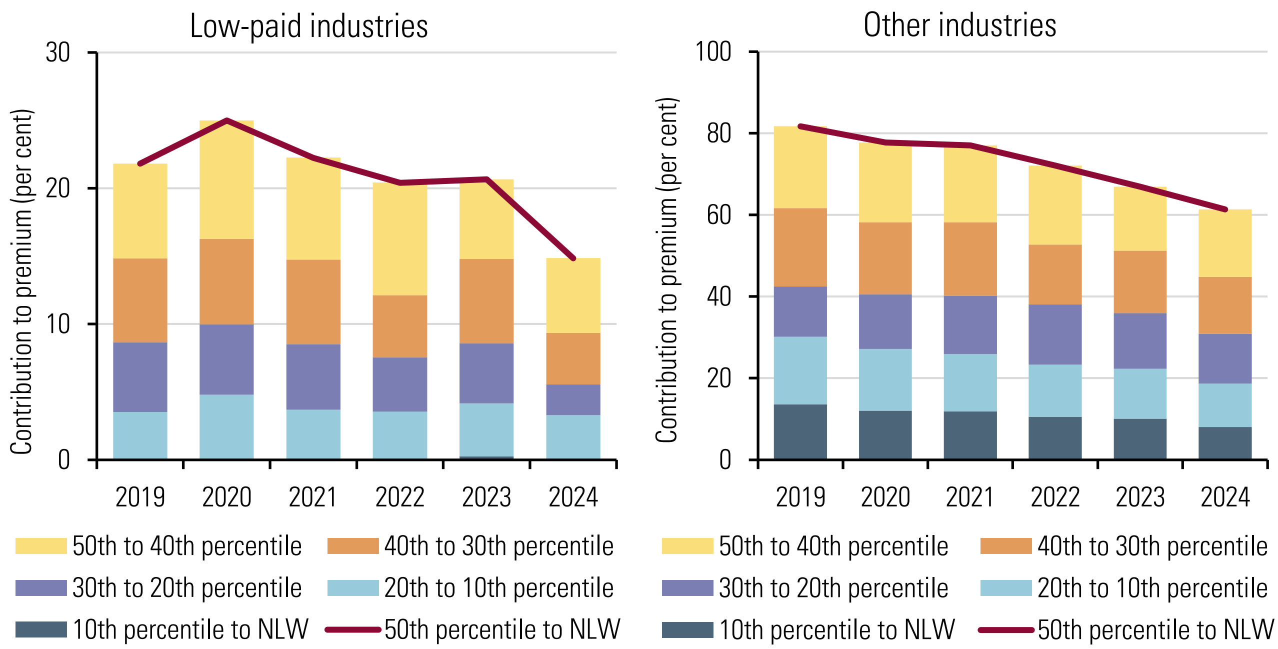
5.21 The Confederation of British Industry (CBI) reported that pay compression had resulted in concerns about workforce harmony and incentives to progress, with lower earners less inclined to take on more responsibility, seniority or training for a job that pays only marginally more.

5.22 The British Chambers of Commerce (BCC) said that impacts on pay differentials were the biggest cost to businesses. Around 17 per cent of BCC survey respondents said they had reduced pay growth for non-NLW staff as a result of the most recent NLW increase – up on previous years. Some businesses said they had removed entire job grades as they could no longer afford to maintain the pay differentials required. Some businesses reported that senior managers and directors had had their pay frozen in order to pay for wage rises lower down the pay scales.

5.23 Recent surveys from employer associations such as the British Retail Consortium (BRC), and the Federation of Small Businesses (FSB) reflected similar evidence. The BRC reported that more than one-third of their members (37.5 per cent in 2024) reduced pay differentials to control costs. While less frequent, growing proportions of employers in surveys by the FSB (10 to 16 per cent) said they had reduced pay differentials as a cost management strategy.

5.24 These trends are reflected in the official pay data. At an aggregate level, the policy of increasing the NLW towards a target based on a percentage of median wages inevitably produces relative compression in the lower-half of the distribution. In recent years, businesses in low-paying industries (industries with high shares of workers earning up to £1.50 above the NLW) have maintained differentials in order to recruit and retain staff in a tight low-paid labour market. Compression has instead come within other industries and from narrowing the pay differentials between low-paying and non-low-paying industries. However, as shown in Figure 5.6, this year the premium of median pay in low pay industries above the NLW fell by 5.8 percentage points or 45 pence. This compression was mainly seen between the 20th and 40th percentiles, where the gap in pay fell by 42 pence.

Figure 5.6: Premium of median wage above NLW by industry type, UK, 2019-2024



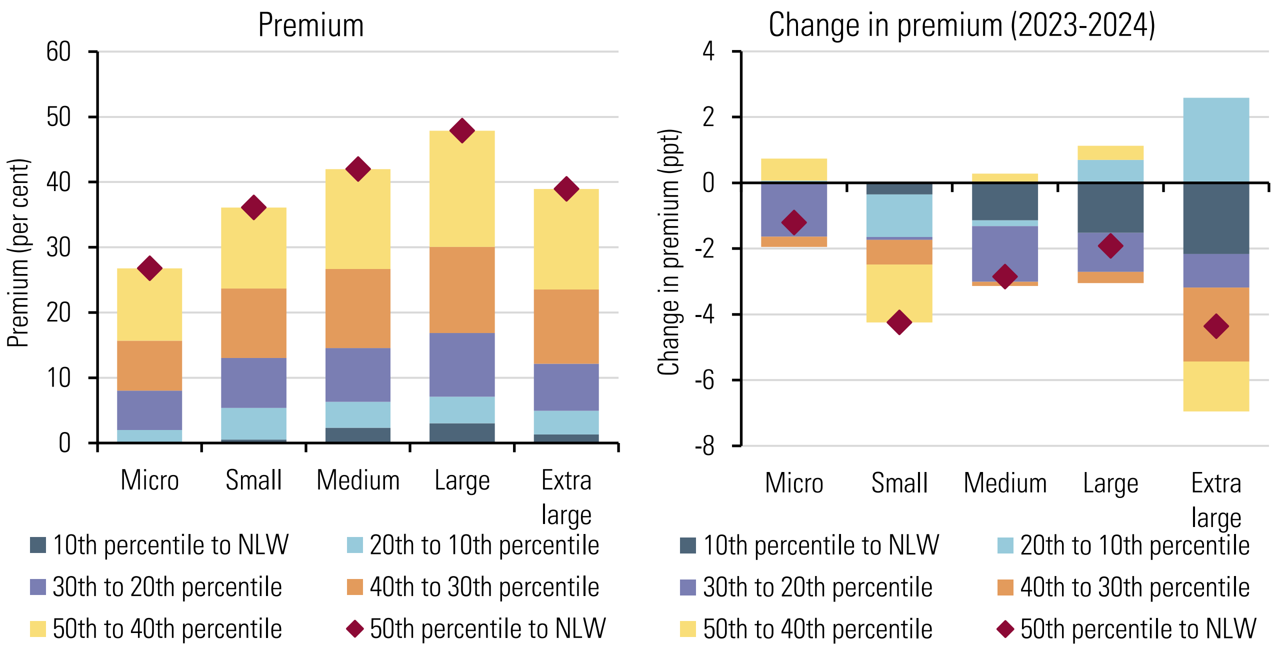
Source: LPC analysis of ASHE 2019-2024, standard weights, 21+ population, UK. Figures are chain-linked to account for methodology change in 2021.

The challenge of differentials is felt across small and large businesses as well as the public sector

5.25 Both large and small employers reported difficulties caused by narrowing differentials. One large retailer told us that maintaining differentials had an impact "not only on costs (particularly where the wage bill is a significant proportion of overheads) but on recruiting and retaining talent for the future and encouraging colleagues and potential new starts to take on additional responsibility." One manufacturer told us that pay compression "had always been an issue but last year was exceptional". After the 2024 NLW increase was announced, the employer had "a queue of people at my door asking: 'Why am I not getting that?'. So, these are people on 40, 50 grand [..] coming to my door saying: 'What do you mean you're going to give me an inflationary increase? This guy's getting 9 per cent.'" The Scottish Grocers' Federation (SGF) cited feedback from one small retailer that "one of his bakers, on £14 per hour, left the business because lower-paid staff in the workforce got a raise due to the increased NLW but the retailer could not afford to give the baker a raise."

5.26 Again, these concerns are reflected in the data. The right panel of Figure 5.7 shows that the fall in pay differentials in 2024 was greatest in very large businesses (those with more than 2,500 employees). Across these businesses the premium of median pay over the NLW fell from 43.3 per cent to 38.9 per cent. Although pay differentials only compressed by 1.2 percentage points in micro firms (firms with fewer than 10 employees) in 2024, these firms have little scope to reduce differentials further, with the premium of the median wage over the NLW at 27 per cent (shown in the left panel of Figure 5.7).

Figure 5.7: Premium of median wage above NLW by firm size, private sector, UK, 2024



Source: LPC analysis of ASHE 2023-2024, standard weights, 21+ population, UK.
Note: Firm sizes are Micro (1-9 employees); Small (10-49 employees); Medium (49-249 employees); Large (250-2499 employees); Extra large (2500+ employees).

5.27 In the public sector the Local Government Association (LGA) also noted the challenge of maintaining a gap between their pay grades and the NLW. Despite removing bottom point on their pay scale, differentials between the NLW and their lowest pay point are minimal. In April 2019 the lowest point on the National Joint Council (NJC) pay spine was £9, compared with an NLW of £8.21. By April 2022 they were at parity. To recreate headroom, the lowest NJC point was removed in April 2023, leaving the new bottom rung of £10.60 when the NLW was £10.42. Further increases took the lowest point to £11.59, but the NLW caught up substantially to £11.44, leaving only a 15 pence difference (pending a decision on pay in 2024).

Employers and employee representatives worry about the impact compression has on progression and motivation

5.28 Impacts on staff motivation were at the forefront of employers' minds. The Chartered Institute of Payroll Professionals (CIPP) said that affected firms have given higher percentage increases to lower earners. "This…makes progression less appealing and recruiting for roles with additional responsibilities harder." The National Farmers' Union Scotland (NFUS) told us that NLW increases reduce pay promotions for skilled workers. Royal Mencap told us they had had to remove a layer in direct services teams due to financial constraints, and this inhibited career development as the subsequent difference between roles was large. One manufacturer told us that squeezed differentials had reduced NLW workers' desire for progression; operators were now saying "Why would I bother taking the responsibility driving the fork truck when I can [work on the production line] for virtually the same money?"

5.29 Among workers we speak to, preferences around progression vary, often according to an individual's age, experience and life circumstances. We meet with some workers who, for different reasons, are not interested in moving into more senior roles in their current workplaces or occupations. For example, we spoke to a part-time retail worker in Northern Ireland who told us that he was comfortable to remain where he was, and career progression was not his priority. "I'm dealing with the workload of uni as well and I'm in this job already. It's kind of comfortable just to be in the position I am now, so I don't think it'd be worth it." However, as we set out in Chapter 3, we also meet with workers who evidently are interested in training and progression and motivated to get a better wage, but in some cases are not getting the opportunities they desire.

5.30 Similarly, some unions and workers linked low progression rates to pay compression. Unite representatives in Northern Ireland told us that narrowing differentials not only affected retention, but also "discourages upskilling and skill development," with the example given of a bookmaker where workers were leaving because "there's no progression through the company." Retail workers in Glasgow noted that the premium for a team support role at one large supermarket hadn't increased for four or five years, even while responsibilities have got greater and greater; "they're almost doing management positions." Community Trade Union told us that because higher-paid roles had not received equivalent increases, there was a perception of people leaving skilled roles to work in "easier stress-free jobs on minimum wage".

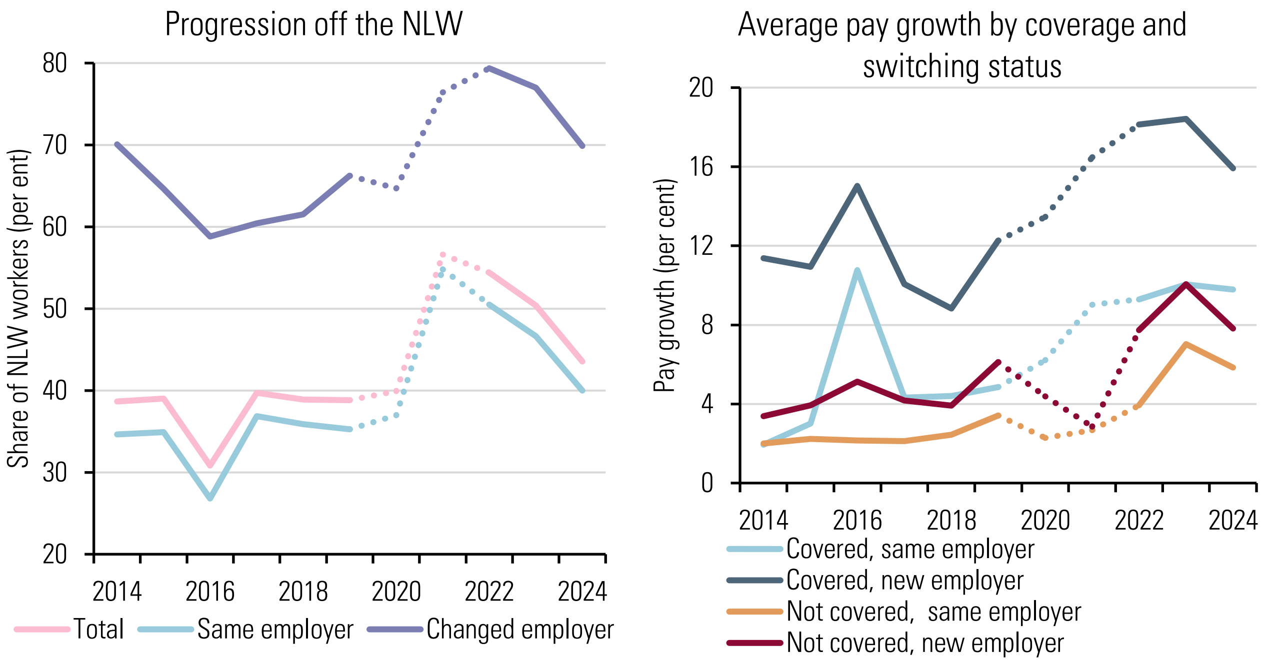
5.31 We also heard from Community Leisure UK that 80 per cent of its members (who manage swimming pools, libraries, museums, gyms, sports fields, parks and other leisure facilities) were "feeling the effect" of the erosion of differentials. The inability to apply the NLW uplift to all staff had resulted in reviews of gradings and pay scales. Some members had opted for a cash differential rather than a percentage. A member in north west England gave some examples of pay compression: the difference between a cleaner and lifeguard had reduced from 85 pence (11 per cent) in 2018/19 to just 22 pence (2 per cent) in 2024/25; in the same period the difference between a lifeguard and a duty manager had been squeezed from £3.45 (39 per cent) to £2.84 (24 per cent). Smaller differentials meant less incentive to progress. "[It is] difficult to encourage those on entry grades to take more responsibilities for not much more hourly pay" said a member in Central England.

Pay progression

The share of minimum wage workers progressing off the National Living Wage is returning to pre-pandemic levels

5.32 In recent years, the tight labour market has provided more opportunities for workers to move off the NLW than previously. This year the share of workers moving off the NLW fell, but remains a little above the rate seen before the pandemic. There were two main contributors to this. Firstly, fewer minimum wage workers switched employers this year – on average workers who change employers receive higher pay increases and are more likely to move off the NLW than those who stay with their current employers. The left panel of Figure 5.8 shows that 70 per cent of NLW workers (purple line) who switched employer moved into jobs which paid above the wage floor. This is down on previous years, but above pre-pandemic levels. Secondly, the premium that workers received for switching employers fell a little. The dark blue line in the right panel of Figure 5.8 shows the average increase in pay growth an NLW worker received if they moved employer – it too fell slightly but remains above pre-pandemic levels.

Figure 5.8: Share of NLW workers progressing off the NLW, UK, 2014-2024



Source: LPC analysis of ASHE 2014-2024, low-pay weights, NLW population, UK. Figures are chain-linked to account for methodology change in 2021. Only includes workers who are present in the ASHE data for two consecutive years.

5.33 While these data are consistent with the loosening labour market described in Chapter 2, employee motivations and incentives may also play a role in driving these outcomes. As discussed above in the context of narrowing differentials, a higher relative NLW may make it less likely for minimum wage workers to want to switch jobs, thereby improving retention.

Employment

More businesses indicated that they are altering headcount plans in response to the National Living Wage

5.34 As we saw in Chapter 2, it is difficult to get a precise read on the labour market given the ongoing issues with the Labour Force Survey (LFS), which, relative to administrative data sources, has consistently understated the level of employment in the economy for the last four years. Nevertheless, a consistent message from the LFS, the Real Time Information (RTI) data produced by HM Revenue and Customs (HMRC) and ONS's workforce jobs data is that labour market conditions have weakened and employment growth slowed in 2024. We are interested in determining, based on the data available to us and from consultations with stakeholders, whether and how much the NLW has contributed to weaker employment conditions.

5.35 This year a greater share of businesses indicated that they were likely to reduce headcount or slow recruitment in response to NLW increases. Nevertheless, reducing headcount was not the primary response for most businesses. Chapter 8 gives a more detailed overview of how employers respond to the rising minimum wage, and the frequency of reduced employment as a response.

5.36 In the Chartered Institute of Personnel and Development's (CIPD) summer Labour Market Outlook survey, the share of employers reporting redundancies or less recruitment in response to the NLW rose from 11 per cent in the three previous years to 16 per cent in 2024. This response was slightly more common in large employers (with 250 or more employees), with 18 per cent of that group citing it as a response compared with 13 per cent of small and medium employers.

5.37 In the BCC's survey, 18 per cent of respondents reported that they had scaled back recruitment plans, up slightly from previous years. Six per cent said they had made redundancies, roughly similar to previous surveys. Only 36 per cent of small businesses that responded to FSB's survey say they approach recruitment in the same way after April's increase in the NLW. A total of 38 per cent of small businesses say that they are more likely to seek to recruit individuals with higher levels of experience or higher levels of qualifications and/or be more wary about hiring individuals with lower levels of experience or someone who has a poor work history. The FSB's argument was that "those with poor work history, may be most impacted by changes to the level of the NLW. Changes to who small businesses recruit may be at least as important for overall participation over time as changes to the level of recruitment."

5.38 The CBI argued that while NLW increases "have typically defied predictions that they would result in a material macro uptick in unemployment … [there is] growing evidence that recent NLW increases are at least reducing headcount in NLW affected businesses even while the labour market has been tight."

5.39 The Recruitment and Employment Confederation (REC) argued its data showed the number of unique job postings for roles commonly paid at or near the NLW have decreased, suggesting the increase in the NLW may have had a negative impact on recruitment. The BRC told us the recent increase in the NLW had a negative impact on retailers' budgets and their capacity to hire and retain employees. It cited the fall in the number of retail job vacancies over the past year, but also noted that "[with] the ongoing transformation of the industry, it is difficult to attribute shifts in the labour market to a single factor". On the other hand, Usdaw argued that several major retailers had been actively recruiting more staff.

Pressures are felt more in some industries than others

5.40 Some industries say they have felt the pressure of NLW increases more than others. In hospitality, UKHospitality told us the NLW increase had led to declines in recruitment. During our Glasgow visit, a hospitality establishment told us staff numbers had fallen from 160 to 124 and they had closed four venues, with labour costs a leading factor in creating "the most difficult trading environment for hospitality in the 43 years that I've been doing this." One British Beer and Pubs Association (BBPA) member noted a decrease in employee numbers across all locations due to the rising wage costs. Another told us they had been forced to cut headcount in the kitchen, with many chefs unhappy as it meant less support and more lone working.

5.41 A business owner in Northern Ireland told us he was reducing headcount, rather than reducing the number of contracted hours for existing employees. It has become "a bit more competitive for hours". New starters are increasingly likely to be brought in on a 16 hour contract rather than a 40 hour contract "to give us a bit more flexibility". Another participant told us his full-time staff always worked on a 40 hour contract, but he was trying to save costs on part-time staff by bringing them in on a 16 hour contract to avoid pension costs and NICs contributions.

5.42 Retailers, particularly smaller ones, also reported employment effects. The Association of Convenience Stores (ACS) told us that 41 per cent of members had reduced employee numbers in response to the NLW increase and 47 per cent had reduced staff hours. SGF told us that "some convenience retailers have reported to us that they have been forced to reduce staff hours" in response to the NLW increase. It shared feedback from one member "that the increase to the NLW this year meant that at least 25 to 50 per cent of staff will have to be let go." Its survey found that shop owners were making up these hours; "over two-thirds of shop owners work more than 65 hours per week and a fifth take no holidays per year."

5.43 The Federation of Wholesale Distributors (FWD) told us that 22 per cent of members stated the NLW increase rates had led to reduced staff employment and 11 per cent said they were likely to have to close their business. The Booksellers Association quoted two members reporting not replacing staff as a result of the rising NLW, while the National Federation of SubPostmasters told us 40 per cent of respondents to an online survey said they had had to let go of staff members due to the increase.

5.44 In a survey carried out by the National Hair and Beauty Federation (NHBF), 19 per cent of respondents said they had reduced the number of staff employed in response to April's NLW increase (compared with 16 per cent in April 2023 and 25 per cent in 2022). Around 22 per cent stated they had reduced staff hours. Its index of recruitment intentions remained negative, with only 16 per cent of respondents likely to take on new staff. It also linked the NLW to the rise in self-employment in the hair and beauty sector, which went in tandem with a decline in employment and apprenticeships. The British Hair Consortium told us that one in five survey respondents said they would consider making redundancies or closing their business.

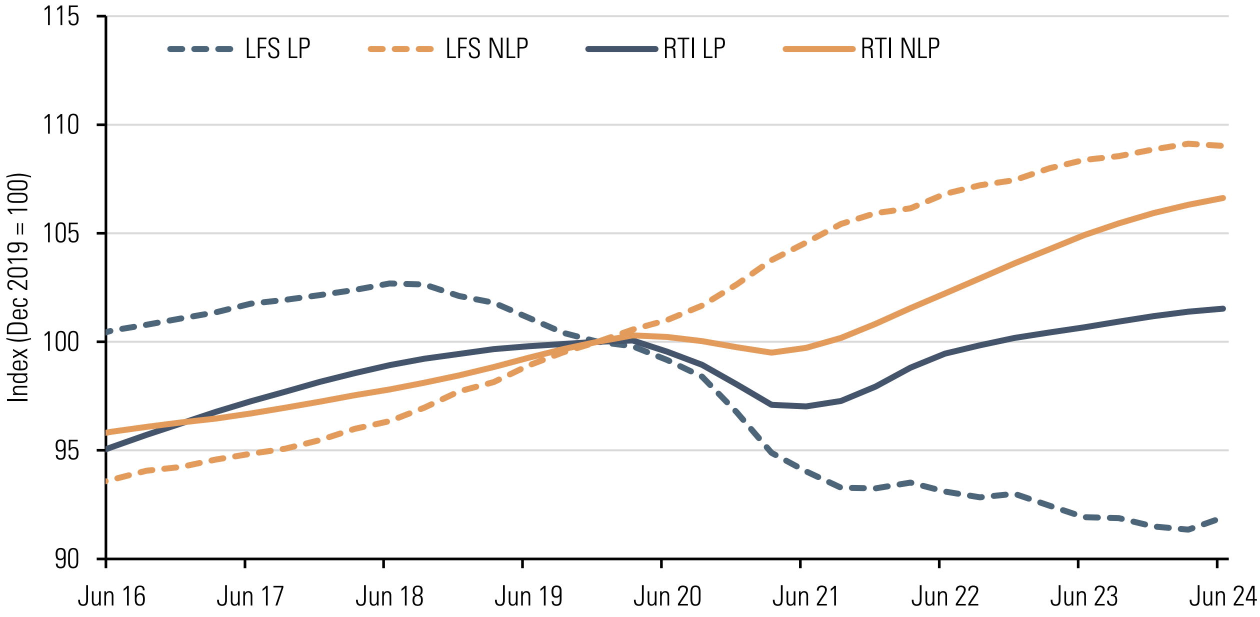
5.45 In the public sector, the LGA told us the NLW increase had resulted in significant financial pressures on councils, potentially leading to job losses and reduced services. It also had an indirect impact on skills shortages across local government which were, in part, caused by the need to cover NLW costs: "there are areas providing much needed services to the public or ensuring proper governance that are functioning while one in four roles are vacant…this is the indirect consequence of funding having to be directed at the NLW and not at other areas of need."

Employment outcomes in low-paying industries have varied

5.46 To understand the impact of the NLW we look at how more NLW-exposed workers, jobs, and regions have fared relative to other less-exposed workers, jobs, and regions. Unfortunately, more granular breakdowns of the different data sources can provide contrasting messages in terms of both magnitude and direction. Given the ongoing issues with the LFS, as with recent years, we put more weight on HMRC's administrative RTI data where they are available.

5.47 We start by looking at employment in low-paying industries. As seen in Figure 5.9, since the pandemic the LFS has persistently overstated the fall in the number of employees in low-paying industries. According to the RTI data, although the number of employees in low-paying sectors has recovered more slowly than in other sectors, it is still higher than it was a year ago and pre-pandemic.

Figure 5.9: Employees by industry type, 21+ population, LFS vs RTI, UK, 2016-2024



Source: LPC analysis of HMRC PAYE RTI data, June 2016-June 2024, seasonally adjusted, 21+ population, UK, 4-quarter rolling average (backward-looking). HMRC PAYE RTI data is as provided to LPC on 9th October 2024. These may differ from revised figures published later. LPC analysis of Labour Force Survey (LFS) microdata, 21+ population, UK, 4-quarter rolling average (backward-looking).

5.48 However, outcomes for low-paying industries have not been the same across all industries. For example, employment in hospitality and wholesale & retail has fallen over the past year by around 3 per cent and almost 1 per cent respectively. At the other end of the spectrum, the RTI data show strong growth in health and social work employment, along with modest job growth in transport and in other service activities (which includes hair and beauty services and goods repair). These broader industry outcomes are consistent with the more detailed, but less reliable, LFS data which suggest that employment has grown over the past year in the social care, transport, cleaning, and hair and beauty industries, but fallen in retail, hospitality and low-paid manufacturing.

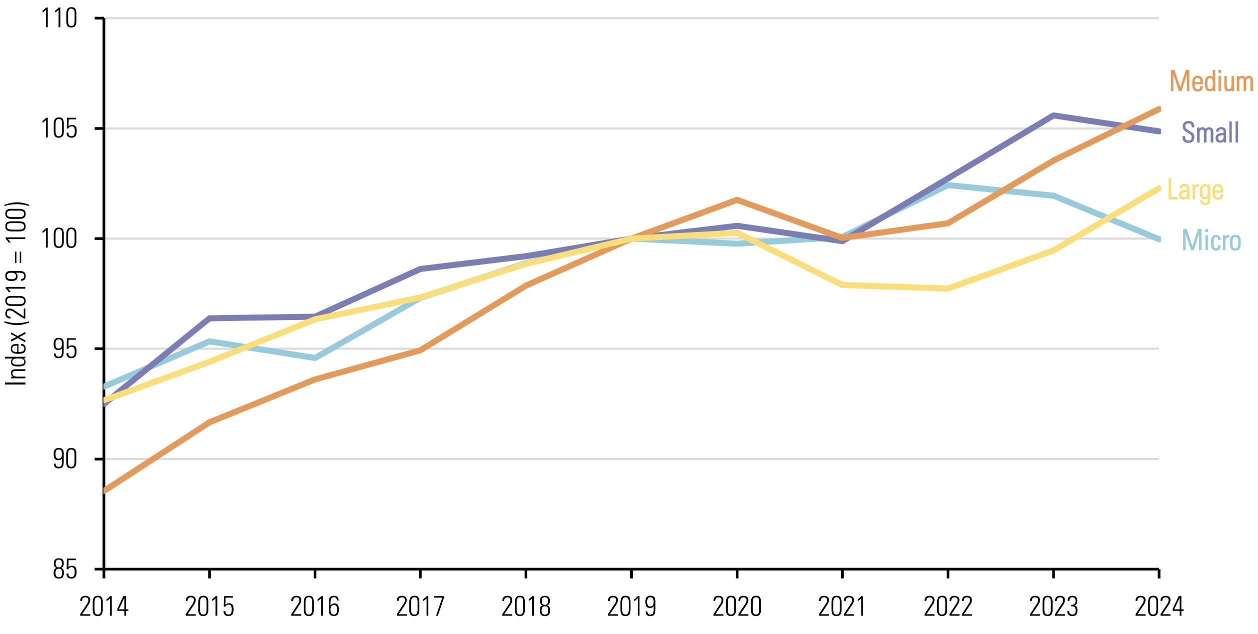
5.49 In interpreting this evidence, we need to be mindful that the NLW is not the sole causal factor. Outcomes at the industry and occupation level reflect broader structural and cyclical shifts in the economy. For example, employment in social care increased substantially after the pandemic, particularly following the introduction of the health and social care visa route, which allowed unmet demand for workers to be filled from abroad. (As discussed in Chapter 2, changes to visa rules introduced in March 2024 have led to a fall in the number of applications for this visa.) In contrast, employment in hospitality and retail has not recovered to pre-pandemic levels as cost of living pressures weigh on demand and the industry shifts away from EU labour. Employment in retail has been in decline for some years, facing competition from online retailers. We need to be aware of these structural and cyclical shifts not only to interpret what has happened, but also to factor into future decision making.

Employment has fallen in smaller firms over the past year

5.50 Micro and small businesses are more likely to employ people at or close to the minimum wage than larger businesses. Over the past year, employment in micro and small businesses has fallen, while increasing in medium and large businesses. Although employment in small businesses remains about 5 per cent higher than in 2019, employment in micro businesses has returned to 2019 levels, having declined in each of the past two years.

5.51 However, it is important to remember that measuring employment growth by size band is tricky. As businesses grow, they cross size thresholds; a micro business becomes a small business, a small business becomes medium-sized and so on. As businesses grow and progress to the next size band, total employment in their previous size band can shrink.

Figure 5.10: Employment by firm size, UK, 2014-2024



Source: LPC analysis of Business Population Estimates 2024, Table 28, UK, 2014-2024.

Employment has decreased for younger NLW-eligible workers, but employment outcomes have improved for other NLW-exposed groups

5.52 If a higher NLW affects demand for workers in low-paying sectors, we would expect it to impact employment for those most likely to work in these industries. Data over the past year have been mixed for different groups of NLW-exposed workers. This can be the result of other structural and cyclical dynamics in the economy, not just the minimum wage, so we need to be careful in interpreting what these outcomes mean in relation to the NLW.

Table 5.1: Employment and coverage rates by personal characteristics, 21+ population, UK, 2019-2024

	Coverage rate (%)[a]		Employment rate (%)[b]						Change in employment rate (ppt)	
	2019 (ASHE)	2019 Q2 (LFS)	2019 Q2	2020 Q2	2021 Q2	2022 Q2	2023 Q2	2024 Q2	2019 Q2-2024 Q2	2023 Q2-2024 Q2
Men	5.0		68.4	68.0	66.5	66.9	66.7	66.1	-2.3	-0.6
Women	8.4		57.7	58.2	57.9	58.0	57.9	58.0	0.3	0.1
No disability		7.6	73.3	73.4	72.1	73.0	73.5	73.6	0.2	0.0
Disability[c]		11.7	33.0	34.3	34.6	35.5	35.6	36.3	3.2	0.7
White		8.5	62.5	62.3	61.2	61.5	61.1	60.7	-1.8	-0.4
Ethnic minority		9.8	66.5	67.9	68.4	68.4	69.2	69.7	3.2	0.5
UK-born		7.9	61.7	61.5	60.5	60.8	60.3	59.9	-1.8	-0.4
Non-UK born		10.1	69.3	70.7	69.9	70.1	70.9	71.1	1.7	0.2
Degree		2.5	75.7	76.5	75.2	74.6	73.7	74.8	-0.9	1.1
No degree		11.7	69.7	69.6	68.0	68.1	67.2	66.9	-2.8	-0.3
21-22[d]	10.9		65.4	63.1	62.4	65.2	62.9	61.4	-4.1	-1.5
23-24[d]	5.2		77.1	77.0	77.1	78.4	77.4	75.2	-1.9	-2.2
25-29	7.4		83.0	84.3	83.5	83.6	83.6	81.9	-1.1	-1.7
30-64	6.3		60.1	60.2	59.2	59.4	59.4	59.5	-0.6	0.1
65+	11.2		10.9	11.0	10.7	11.1	11.2	11.5	0.6	0.3
Total	6.7		62.9	63.0	62.1	62.3	62.1	62.0	-1.0	-0.2

Source: (ASHE coverage rates) LPC analysis of ASHE, low-pay weights, ages 21+, UK, 2019. These figures are chain-linked to account for the change in ASHE methodology in 2021. (LFS coverage rates) LPC analysis of LFS, income weights, ONS imputation method, ages 25+, UK, average of four quarters to 2019 Q2. (Employment rates) LPC analysis of LFS, standard weights, ages 21+, UK, 2019 Q2-2024 Q2 (four quarter average).

Notes:

a. We use ASHE data where available to estimate coverage rates. For characteristics not available in ASHE, we use the LFS to estimate coverage rates. This is a less reliable measure and tends to be higher overall, so the LFS and ASHE figures are not comparable.

b. There is additional uncertainty around these results currently, as they rely on the LFS, which has had issues capturing a representative snapshot of the country since the pandemic (see Chapter 2).

c. We use different definitions of disability in this analysis. We use the DISCURR variable in the LFS for the coverage analysis, whereas for the employment analysis we use the DISEA variable.

d. Coverage rates were lower for 21-24 year olds in 2019 when they were on the 21-24 Year Old Rate. In 2021 23-24 year olds were made eligible for the adult (NLW) rate and coverage rates jumped to 12 per cent. In 2024 21-22 year olds were made eligible for the adult (NLW) rate and coverage rates jumped to 19 per cent.

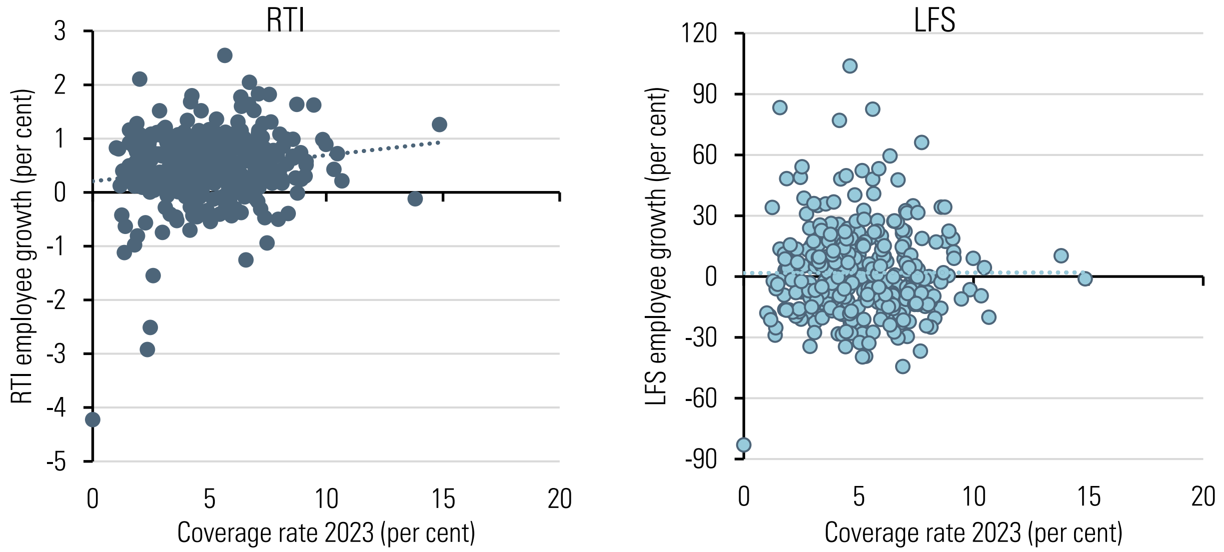
5.53 Employment for workers in their 20s has fallen over the past two years, while employment for those aged 65 and over has increased significantly. Although population dynamics have contributed to these outcomes (the over 65 population has increased, and the 21-24 population has decreased), employment rates for 21-24 year olds have also fallen. Young people are more likely to work in hospitality and retail jobs, two industries facing lower consumer demand. However, much of the fall in employment for younger workers is down to rising inactivity suggesting that other factors are also at work – we discuss the youth labour market in more detail in Chapter 6.

5.54 Other NLW-exposed groups have seen more positive outcomes. Employment outcomes for women have been stronger than for men both over the past year and since the beginning of the pandemic. Similarly, ethnic minorities have experienced better job outcomes than white British and migrants have seen stronger employment growth than the UK-born population. Employment outcomes have also improved for persons with a disability, although the composition of this group is likely to have changed over recent years following a significant increase in the number of people reporting a disability.

Employment has increased by more in higher coverage parts of the country

5.55 Likewise, we would expect those parts of the country most reliant on low-paying jobs to be more affected by NLW rises than those areas which are not. Looking at simple correlations between employment growth and coverage across local authority areas, we see, when using the RTI data, that between April 2023 and April 2024 employment grew by more in local authority areas with higher coverage rates. Using the LFS data we see neither a positive nor negative relationship between employment growth and coverage, but at the local authority level the LFS data are subject to significant variability.

Figure 5.11: Employment growth vs coverage, RTI and LFS, UK, 2023-2024



Source: LPC analysis of ASHE, low-pay weights, UK, all ages, excludes first year apprentices. LPC analysis of RTI employees data all ages, LFS employees data, standard weights, UK, 16+.

Notes:

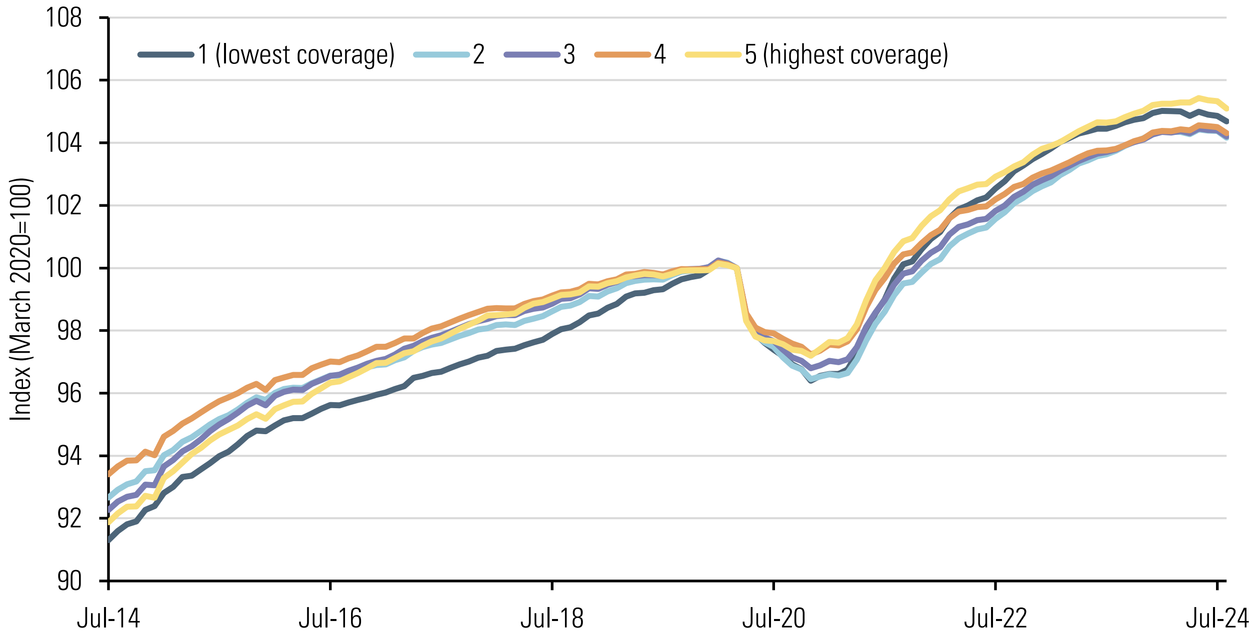
a. Northern Ireland (NI) is included as a single local authority as we don't have detailed data for NI.

b. Excludes Isles of Scilly and City of London.

c. Note the different y-axes for the two graphs.

5.56 Supporting this, we also see that since the beginning of the pandemic employment has recovered the most in the local authority areas that were in the top coverage quintile in 2019 (Figure 5.12). Overall, these data suggest that recent increases in the NLW, while large, have not adversely affected employment in regions with high NLW coverage. Nevertheless, consistent with other broader labour market data, employment growth has slowed in all quintiles over the past year.

Figure 5.12: RTI employment by local authority coverage quintile, UK, 2014-2024



Source: LPC analysis of ASHE 2014-2024 and ONS data. Earnings and employment from Pay As You Earn Real Time Information 2014-2024, total population, UK.

5.57 Despite the difficulties with the data, assessed holistically, outcomes in the low-paid labour market are consistent with broader labour market outcomes. In addition to the employment outcomes just discussed, increased pay compression and reduced progression are indicative of a softening in the low-paid labour market, even if outcomes remain healthy by historical standards. Nevertheless, we are mindful of differential outcomes among sectors and businesses and are conscious of the challenges some key low-paying industries are facing.

Econometric evidence

5.58 We use econometric analysis to supplement our descriptive analysis and stakeholder evidence. When evaluating the employment impacts of the NLW, econometric analysis allows us to make more rigorous comparisons and control for potentially confounding factors, as well as measure the uncertainty around our estimates. In our 2022 NLW Review (Low Pay Commission, 2022), we provided a detailed summary of the evidence up until 2020. We found little evidence to suggest the NLW was reducing employment for all affected workers, although there was some evidence it reduced employment for some subgroups of workers, such as women working part-time.

5.59 Since 2020 it has been more difficult to conduct robust econometric analysis of the employment effects of increases in the NLW. In addition to the confounding impacts of the pandemic and associated policy responses, labour force data have been less reliable than previously.

5.60 This year we commissioned three pieces of external research. Addressing a previously identified research gap, two of these pieces focused on the minimum wage and alternative work arrangements. In the first of these papers, Albagli, Costa and Machin (2024), looking at the introduction of the NLW in 2016, do not find any evidence of a negative employment effect, but do find that the introduction of the NLW increased the use of zero-hour contracts. However, they do not find any evidence to suggest the NLW increased other forms of insecure work, such as involuntary part-time work. In fact, they find that the NLW may have reduced involuntary part-time work.

5.61 The second paper on alternative work arrangements, Giupponi, Ray-Chaudhuri and Xu (2024) assessed how firms changed their pay and contractual practices in response to the introduction of the NLW. The found that the introduction of the NLW was associated with compression of pay differentials within firms. They also found that the introduction of the NLW led more firms to use incentive pay and pay by the hour (as opposed to a salary) to compensate lower-paid workers. The authors did not find any evidence of the NLW leading to increased use of outsourcing.

5.62 The third piece of externally commissioned research, Frontier Economics (2024), looked at how monopsony power within the labour market influences responses to increases in the minimum wage. They found that, following an increase in the minimum wage, employment and total hours increase in areas with higher employer concentration relative to areas of low employer concentration. This finding aligns with previous work, and with the theoretical discussion of the interaction between monopsony power and minimum wage effects.

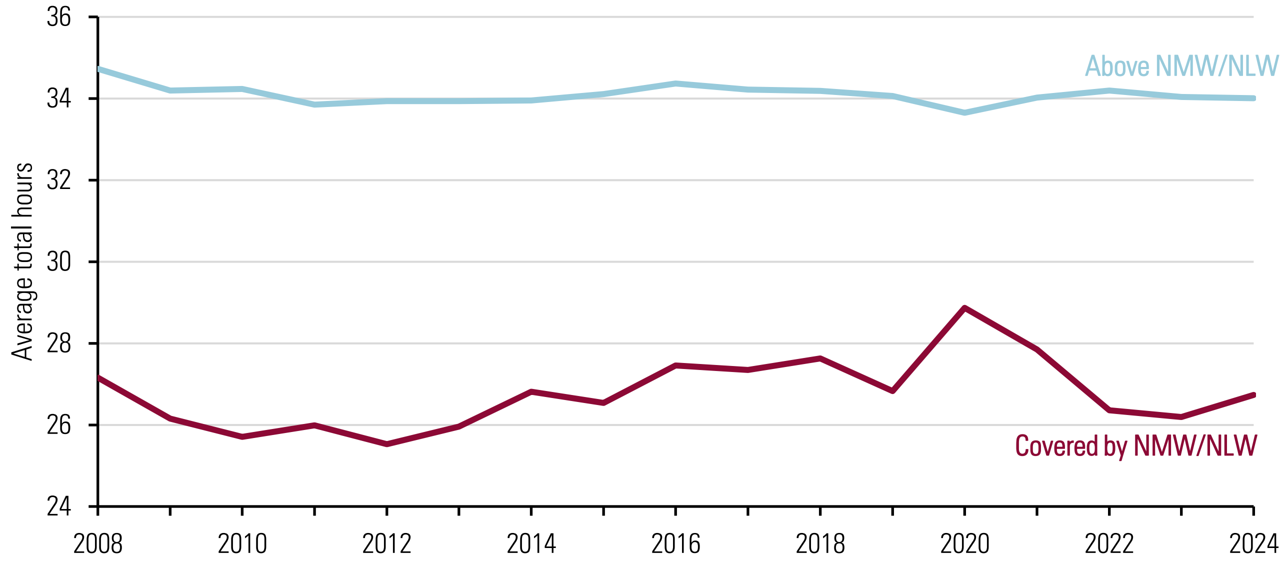
5.63 More details on each of these pieces of research can be found in Appendix 2.

Hours worked and precarious work

5.64 Other than reducing staff levels, employers could also potentially respond to minimum wage increases by reducing workers' hours or by hiring workers on contracts that are more flexible for employers (but considered more precarious for employees). Such contracts include zero-hours contracts (in which an employee is not guaranteed any number of hours) and temporary contracts.

5.65 This year the data suggest that, at least at an aggregate level, employers have not had to resort to these measures. In 2024, after declining in recent years, the average hours worked by NLW workers increased a little, as did hours for those earning just above the NLW. Nevertheless, average hours are still a little lower than they were pre-pandemic, even if the distribution of hours worked for minimum wage employees has remained relatively stable over recent years. Consistent with the increase in average hours, the underemployment rate (the share of workers looking for more hours) also fell over 2024 and remains lower than it did pre-pandemic.

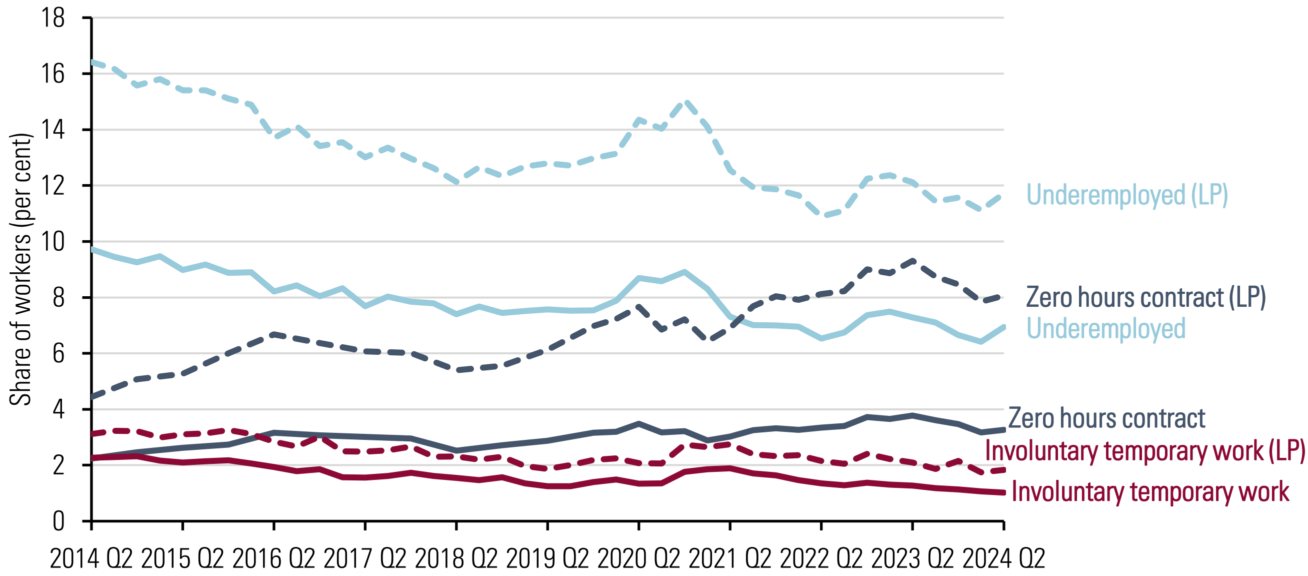
Figure 5.13: Average hours worked by covered status, UK, 2008-2024



Source: LPC analysis of ASHE 2008-2024, low-pay weights, total population, UK.

5.66 Moreover, indicators of precarious work have declined since the middle of 2023. The share of employees on zero-hours contracts fell in low-paying occupations (occupations with high shares of workers paid up to £1.50 above the NLW), although these contracts remain much more common in low-paid occupations than other occupations (Figure 5.14). The share of workers in low-pay occupations in involuntary temporary work (those who are in a temporary job, but would like a permanent position) also declined a little over the year. Similarly, despite a pick up in Q2 2024, underemployment (those who would like to work more hours than they currently do) has fallen since the middle of 2023 both overall and in low-paying occupations.

Figure 5.14: Share of workers in precarious work, low pay occupations and total, UK, 2014-2024



Source: LPC analysis of LFS, standard weights, UK, 2014-2024, figures are not seasonally adjusted. There was a methodology change in the zero-hours contracts measure in 2020 Q2. LP refers to low-paying occupations.

Conclusions

5.67 The 9.8 per cent increase in the NLW this year took the NLW to its highest ever level relative to median pay. As a result, minimum wage and other lower-paid workers received significant increases to both their hourly and weekly pay. At the same time, to date there is little evidence to suggest that the increase in the NLW has caused employment to fall. While employment outcomes in some low-paying industries have weakened, outcomes for many of the most NLW-exposed workers have improved, albeit only modestly.

5.68 Nevertheless, a number of indicators show that while still healthy, the low-paid labour market is softening. In 2024, NLW coverage increased meaningfully for the first time since the introduction of the NLW, and pay differentials in low-paying industries narrowed noticeably. Fewer NLW workers switched jobs in the past year and pay increases for those who did were smaller than they have been in recent years. However, overall, outcomes remain as good as, or better, than they did pre-pandemic, suggesting that the labour market has been able to absorb the increase in the NLW without significant disruption.

Chapter 6

Young people

Key findings

- **Youth employment has weakened, in part due to increased inactivity –** 16-20 year olds' employment rates have likely fallen below pre-pandemic levels. Numbers of young people not in education, employment or training (NEET) have risen, but remain well below levels seen following the financial crisis. Higher inactivity suggests supply issues, such as ill health, could be constraining youth employment, although understanding the youth labour market is limited by the Labour Force Survey issues.
- **Hourly pay growth remains strongest for young workers, suggesting robust demand –** Median hourly pay growth has been stronger for young people than adults over the past year. Large increases to youth minimum wages in April 2024 meant that minimum wage increases have now caught up with median pay growth for young people since 2016. However, the bite of the youth minimum wages (their share of the median wage) remains below the levels seen prior to 2016.
- **Despite large increases in youth minimum wage rates, the share of jobs paid the youth rates has only increased slightly –** The share of 16-20 year olds paid at their youth rates saw a two percentage point increase, with larger increases in coverage for 16-17 year olds than 18-20 year olds. The overall share of 16-20 year olds paid less than the NLW has only increased by one percentage point this year and remains below 2019 levels.
- **However, demand has fallen in the low-paying sectors where young people often work –** Youth employment in hospitality and retail has weakened over the past year. This is consistent with trends in the adult labour market, where strong post-pandemic recruitment in hospitality has unwound. These sectors are the largest employers of young people and are also more likely to use youth rates.
- **The impact from 21-22 year olds becoming entitled to the NLW has been limited –** As expected, the reduction in the age of NLW eligibility from 23 to 21 led to a large increase in the share of 21-22 year olds paid at their minimum wage. However, initial econometric analysis has found no significant impact on employment or hours worked for 21-22 year olds. Employers have reported little impact from the change. However, it was only implemented in April and employers may take time to adjust.
- **Many stakeholders support lowering NLW entitlement further to age 18, but the risks are greater –** Unions and charities support the reduction in NLW entitlement to 18, while employers views are more mixed. 18-20 year olds are more likely to be in education, working part-time, and earning below the NLW than 21-22 year olds were. While we have made progress in narrowing the gap, the increases required to eliminate it are large.

Introduction

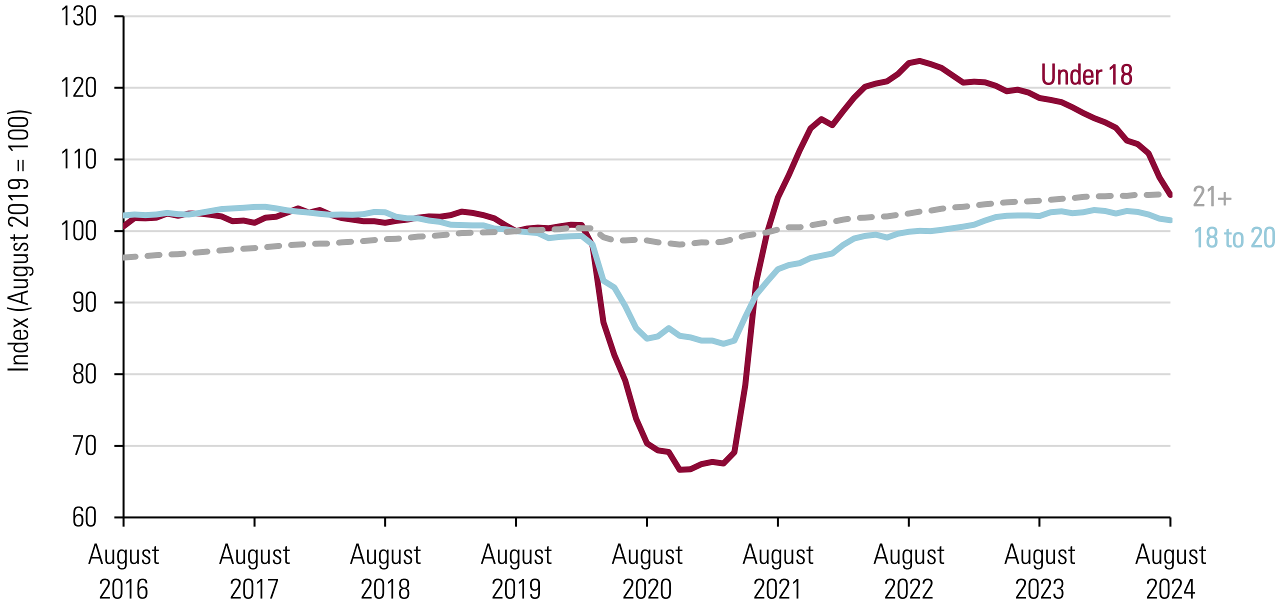
6.1 This chapter looks at the youth labour market and use of the youth minimum wage rates. The Government wants “every adult worker” to benefit from a “genuine living wage” and to lower the NLW age threshold to 18 years of age. Rather than making this change immediately, our remit suggests we should “take steps year by year” and our recommendations for this year should “continue to narrow the gap” between the 18-20 Year Old Rate and the NLW. In making this change, we are asked to take account of the effects on employment of younger workers, incentives for them to remain in training or education and the wider economy. Our remit for the youngest workers, those aged 16 and 17, is to push the minimum wage as high as possible without damaging employment. The Apprentice Rate – which also affects the youth labour market and has been aligned to the 16-17 Year Old Rate since April 2022 – is discussed in Chapter 7.

6.2 We begin by looking at headline pay and employment data for 16-20 year olds. We then break this down, focusing particularly on the sectors where young people are more often employed. The issues with the Labour Force Survey (LFS) discussed in Chapter 2 particularly limit analysis of employment developments for young people, where sample sizes were already small and there has been considerable divergence in estimates of employee numbers for this group compared to other sources (see Appendix 3). While sample sizes are gradually improving and we do continue to use LFS data, we gratefully received additional data from HM Revenue and Customs (HMRC) again this year. This additional Pay As You Earn (PAYE) Real Time Information (RTI) data helped to plug the gaps in our understanding of the youth labour market. We are also able to gain some insights into the state of the youth labour market through changes in the use of the minimum wage and pay. We then analyse the pay and employment outcomes for 21-22 year olds since they became entitled to the NLW in April this year. Finally, we turn to 18-20 year olds and lay out some important considerations for lowering the NLW age to 18.

Youth employment has weakened over the past year

6.3 The number of employees aged under 21 has fallen significantly over the past year but remains above pre-pandemic levels. Figure 6.1 shows that the employment level for 18-20 year olds has performed relatively worse since the pandemic when compared to that for those aged 21 and over, while employment for those aged under 18 is falling rapidly from unusually high levels.

Figure 6.1: Employee numbers compared to August 2019, by age, UK, 2016-2024



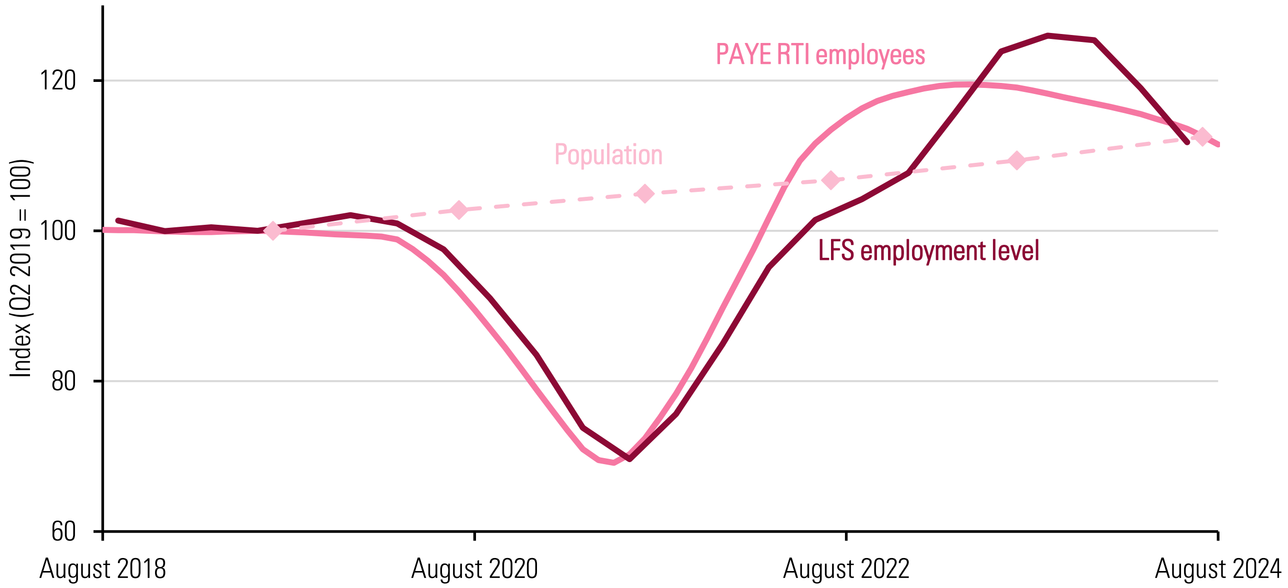
Source: LPC analysis of HMRC PAYE RTI data, seasonally adjusted, UK, August 2016-August 2024. Under-21 and 21+ populations. Data for 18-20 and 21+ groups is as provided to LPC on 7th October 2024 and data for under-18s is from data published on 15th October 2024. These may differ from revised figures published later.

6.4 These employee numbers indicate that there are a declining, but still above pre-pandemic, number of jobs available for young people in the economy. For a fuller picture of how young people are faring, we would usually look at employment numbers in the context of detailed population data, using the LFS. However, small sample sizes and differences in population estimates are a particular problem for the youth age groups, which are already small. HMRC PAYE RTI data do not give us the same level of detail, and we cannot use it to calculate employment rates.[13] We supplement HMRC and LFS data on employment with Office for National Statistics (ONS) population estimates up to 2023 and projections for 2024 (see Appendix 3 for further details).

6.5 For context, we can look at the projected change in the youth population from the ONS in combination with HMRC and LFS estimates of the employment level over the same period, shown in Figures 6.2 and 6.3. These projections give a broad indication that the growth in employee numbers since 2019 has likely been more than offset by population growth. This means that the employment rate – defined as the employment to population ratio – is likely at or below pre-pandemic levels. However, population projections are annual and based on past population estimates, so are not directly comparable to the HMRC employee numbers.

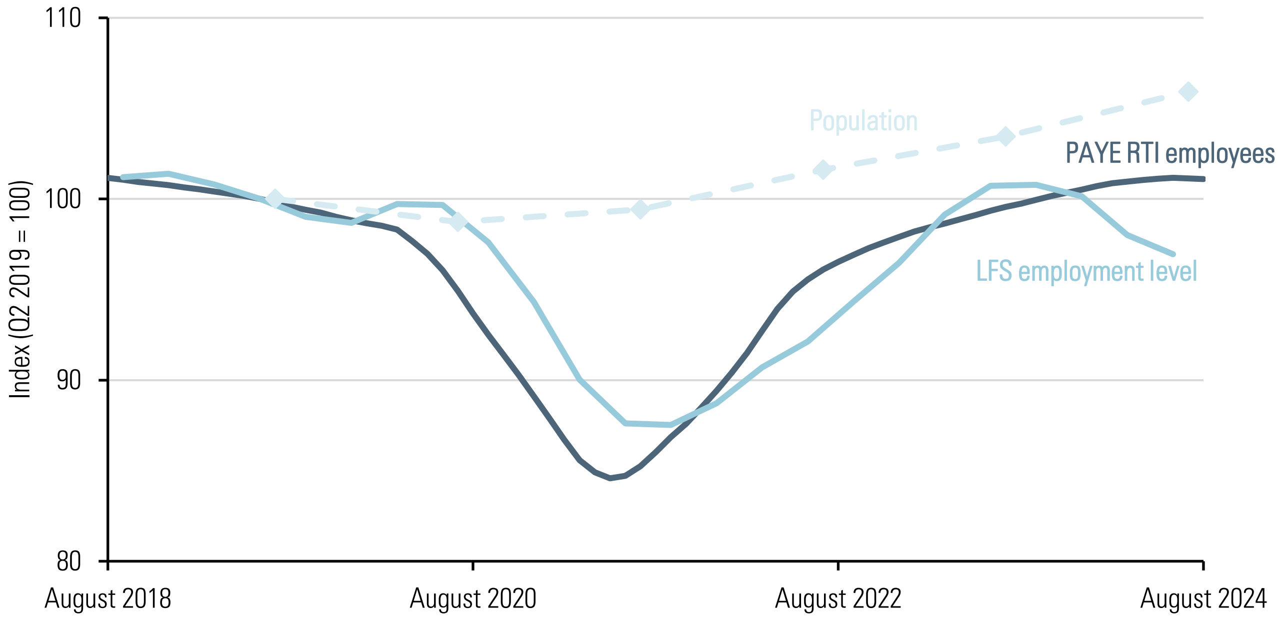
[13] There are differences between the employee population captured by HMRC's PAYE data and the definition of the employed as used in the LFS and internationally, e.g. the PAYE data does not include the self-employed. See Appendix 3 for further information.

Figure 6.2: Projected change in population compared to PAYE RTI employee and LFS employment levels, 16-17 year olds, UK, 2018-2024



Source: LPC analysis of HMRC PAYE RTI data, under-18 population, not seasonally adjusted, UK, August 2018-August 2024, 12-month averages (backward-looking), indexed to June 2019; LFS, UK, Q3 2018 – Q2 2024, 16-17 population, 4-quarter averages (backward-looking), indexed to Q2 2019; ONS mid-year population estimates, UK, 2019-2023; and ONS 2021-based interim population projections, UK, 2024. PAYE data for under-18s is from data published on 15th October 2024. These may differ from revised figures published later.

Figure 6.3: Projected change in population compared to PAYE RTI employee and LFS employment levels, 18-20 year olds, UK, 2018-2024



Source: LPC analysis of HMRC PAYE RTI data, 18-20 population, not seasonally adjusted, UK, August 2018-August 2024, 12-month averages (backward-looking), indexed to June 2019; LFS, UK, Q3 2018 – Q2 2024, 16-17 population, 4-quarter averages (backward-looking), indexed to Q2 2019; ONS mid-year population estimates, UK, 2019-2023; and ONS 2021-based interim population projections, UK, 2024. PAYE data for 18-20s is as provided to LPC on 7 October 2024. These may differ from revised figures published later.

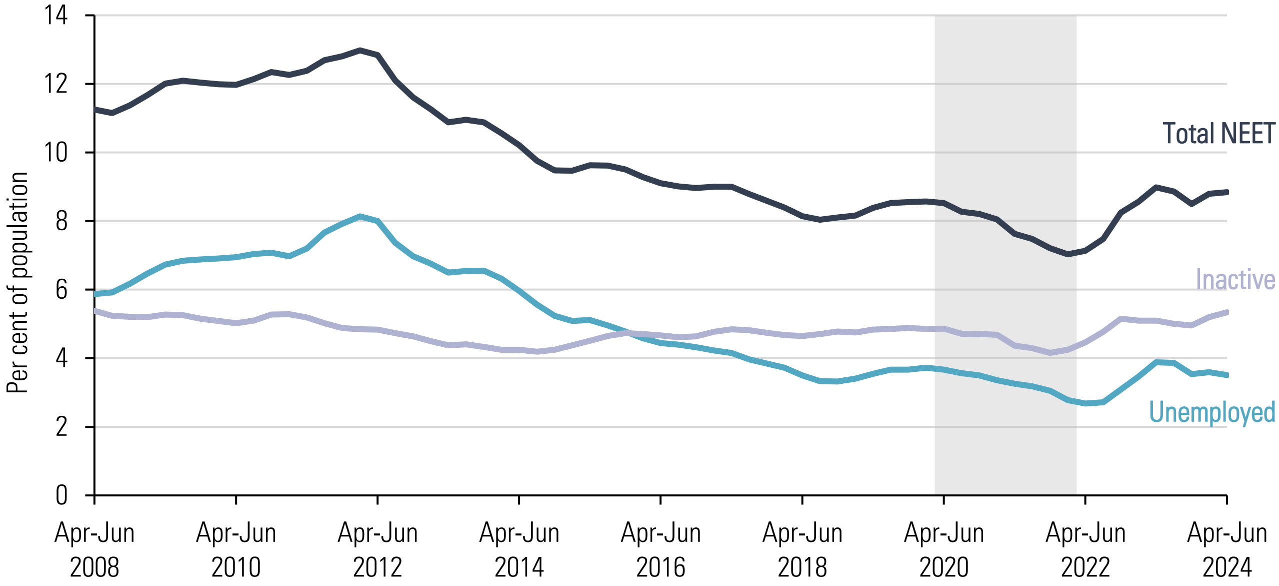
6.6 Stakeholder evidence told a mixed story of the labour market for young people. UNISON took a long-term view that "unemployment rates for 18-24 year olds and 16-17 year olds have been running among their lowest levels in many years" despite the recent downturn in employment rates. On the other hand, Youth Employment UK noted that youth unemployment and the number of young people not in employment, education or training (NEET) were rising. UKHospitality (UKH) noted a "move away from inexperienced, unskilled young staff because you have to pay them the same level as somebody who has got a bit more experience". The British Hair Consortium (BHC) told us that youth employment opportunities were declining, both for apprentices (see Chapter 7) and newly qualified workers. Many young, newly qualified workers were "unable to gain employment as employers cannot afford to recruit young people since NMW increases have overtaken consumer pricing behaviours".

Youth inactivity has increased

6.7 Another important indicator for the youth labour market is the share of the population not in any kind of education, employment, or training (NEET). The NEET rate is often preferred to the youth unemployment rate as a measure of how difficult it is for young people to find employment. This is because the unemployment rate removes those who are in education from the calculation, which can make the unemployment rate appear higher when more young people stay in education. The NEET rate is taken as a proportion of the whole youth population, which means increased numbers of students do not increase the NEET rate.

6.8 As NEET data also come from the LFS, we have less confidence in these estimates for recent years. However, the estimated share of 16-20 year olds who were NEET in the second quarter of 2024 was similar to pre-pandemic levels – at an annual average of 8.8 per cent of the population. The increase in NEET rates over the past two years is due to increases in both unemployment and inactivity. However, the NEET and unemployed rate has increased from historic lows while the NEET and economically inactive rate has reached its highest level since 2011 at 5.3 per cent. The number of 16-20 year olds citing long-term sickness as their reason for inactivity doubled from 40,000 to 80,000 between the second quarter of 2019 and 2024. If the LFS data are accurate, they suggest that more young people are finding themselves detached from the labour market, partly due to an increase in ill-health.

Figure 6.4: NEET rates for 16-20 year olds, UK, 2008-2024



Source: LPC analysis of ONS NEET data, 16-20 population, UK, 4-quarter average (backward-looking), not seasonally adjusted, UK, 2008 Q2 – 2024 Q2. The shaded area indicates the period affected by the pandemic.

High costs and a lack of support have made it harder for young people to access the labour market

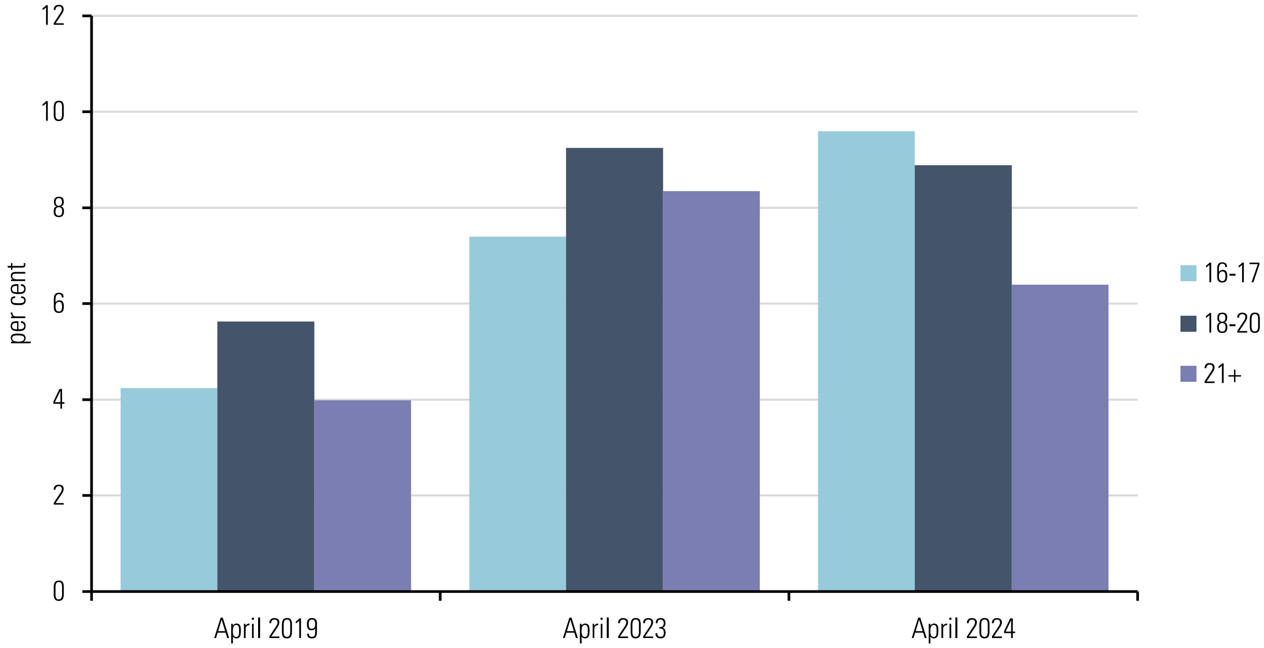
6.9 The King's Trust (formerly the Prince's Trust) 2024 Annual Youth Index found that "one in ten NEET young people have turned down a job because they could not afford the costs associated with it – likely to include, travel, clothing, or childcare". In a meeting convened by the End Child Poverty Coalition, we spoke to one young worker who wanted to get a job, but whose transport costs meant it wouldn't be feasible to work in a role which paid the youth rates. Living in a rural location meant "I would only be able to work on the weekends and the amount that I get paid because I'm under 18 would mean that I'm working over an hour for free … the cost of lunch on top would mean I pretty much spend half my wages." The worker thought that the costs associated with employment meant that "it's just not sustainable … you're not coming away with enough to make it worthwhile."

6.10 Youth Employment UK told us that unemployment and inactivity were driven by a range of issues including disruption from the pandemic, the fragmentation of the education system, health, levels of pay and low confidence. It tended to hear from families that there was a "really linear route" up to 16, after which it became "difficult to navigate that there are so many different opportunities for our young people". It noted that young people "don't know the skills employers are looking for" and "aren't confident with the entire [hiring] process". Young people, it argued, feel like "there's not quality work opportunities for them and they just can't navigate the system." In turn, employers "need more support to enable them to [..] provide support to our young people". Employers often "will not want to employ young people because they see that additional cost" in terms of health issues, investment in upskilling and investment in training.

Young people have seen sustained hourly pay growth

6.11 Hourly pay growth has been strong in the labour market between April 2023 and April 2024, but it has been particularly strong for younger workers. In April 2024, 16-17 year olds saw the strongest growth in median hourly pay of any age group (Figure 6.5). Hourly wage growth was slightly lower for 18-20 year olds, but still above growth for those aged 21 and over. This is likely to be a function of the strength of hourly pay growth in low-paying sectors (see Chapter 2), where young people are more likely to work.

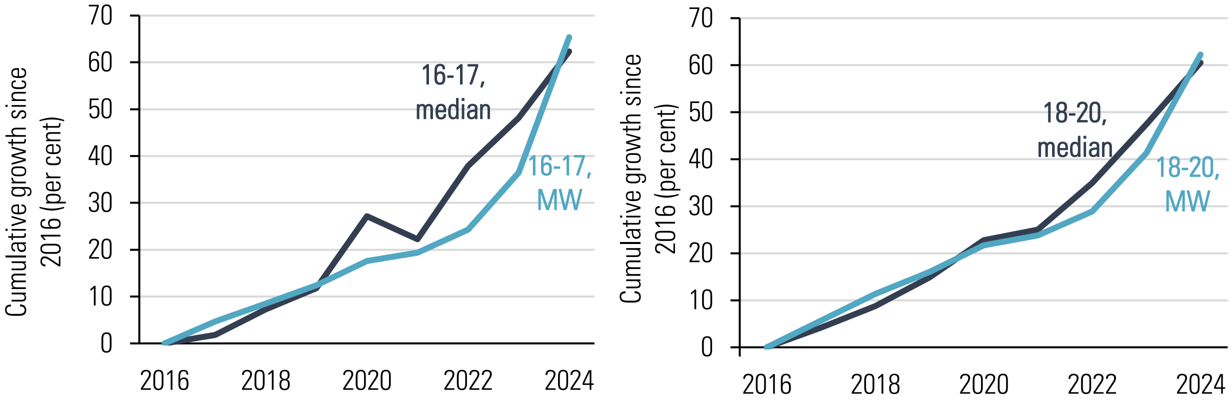
Figure 6.5: Annual growth in median hourly wages, by NMW rate population, UK, 2019, 2023 and 2024



Source: LPC analysis of ASHE, standard weights, UK, 2019-2024. 16+ population, excluding those eligible for the Apprentice Rate. Estimates are chain-linked to adjust for a methodology change in 2021, see Appendix 3 for details. Annual growth is measured from April of the given year compared to April of the previous year.

6.12 April's large youth minimum wage increases helped to regain the ground lost against average wages of younger workers since April 2016. Figure 6.6 shows minimum wage rises falling behind median wage growth in the post-pandemic period, before growing more rapidly than the median in the most recent year. This contrasts with the adult labour market where the minimum wage has consistently risen by more than median wages since 2016.

Figure 6.6: Cumulative nominal growth in median and minimum wages, 16-17 year olds (LHS) and 18-20 year olds (RHS), UK, 2016-2024



Source: LPC historic minimum wage data and LPC analysis of ASHE, standard weights, UK, 2016-2024. 16-20 population, excluding those eligible for the Apprentice Rate. Median estimates are chain-linked to account for the methodology change in 2021.

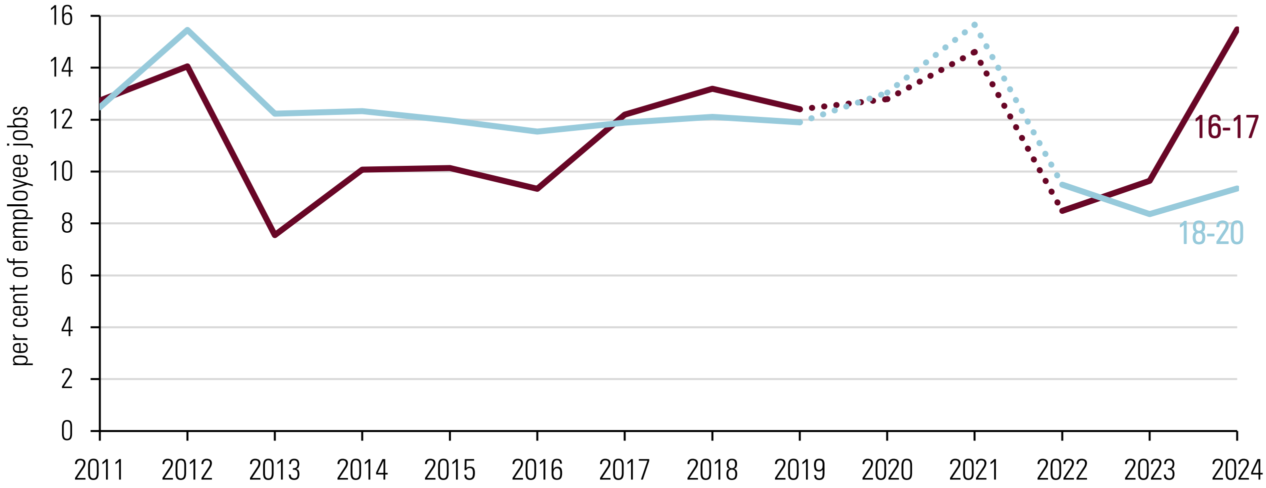
6.13 With the minimum wage growing faster than median pay, the bite of the minimum wage increases. The bite of the 16-17 Year Old Rate reached 72 per cent in 2024, returning the bite level to its pre-pandemic average. The bite of the 18-20 Year Old Rate reached 74 per cent in 2024, which is still below historic levels of bite for 18-20 year olds.

6.14 The youth minimum wages have also grown in real terms. Between April 2016 and March 2024, youth minimum wages grew by more than the CPI and CPIH measures of inflation, but by less than RPI. The large increase in April 2024 has meant that the growth in youth minimum wages since April 2016 has exceeded the growth in prices over the period according to all three measures of inflation (CPI, CPIH and RPI).

Use of youth rates has increased slightly over the past year

6.15 We define the coverage rate as the share of workers paid up to 5 pence above their minimum wage. After a £1.12 (21.2 per cent) increase in their minimum wage, the coverage rate for 16-17 year olds rose by 5.8 percentage points to reach its highest ever level (see Figure 6.7). However, this only represents 17,000 more jobs being covered by the 16-17 Year Old Rate because the number of 16-17 year old workers is very small compared to other groups. For example, the NLW coverage rate rose by 1.4 percentage points, but this represents an additional 454,000 jobs. Despite a £1.11 (14.8 per cent) increase for 18-20 year olds, the coverage rate for this group only rose by one percentage point (7,000 jobs). Overall, the coverage rate for 16-20 year olds increased by 2.2 percentage points.

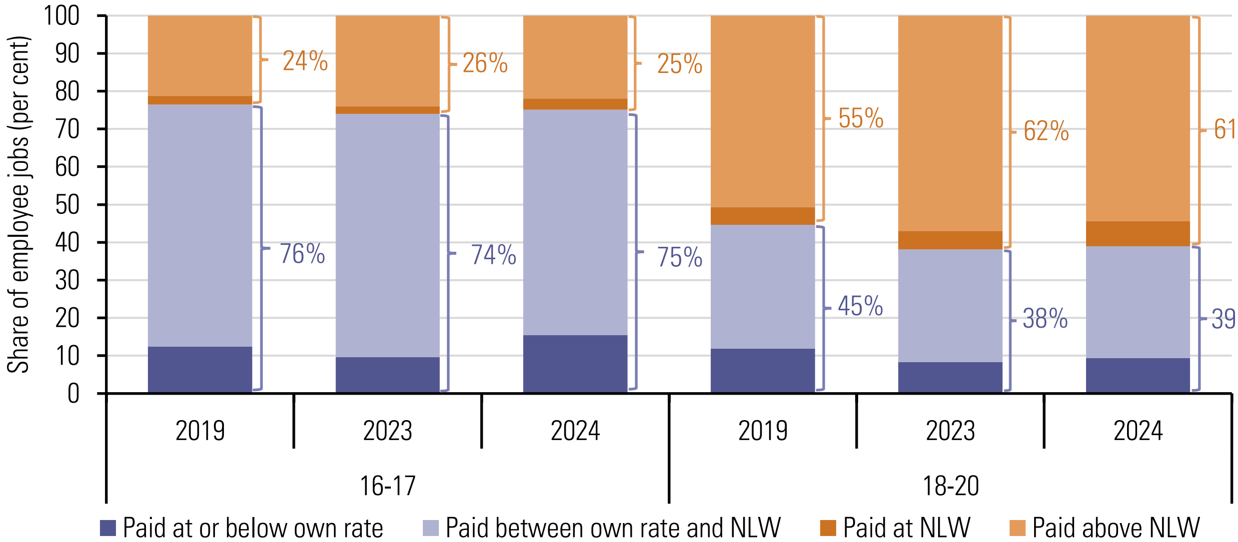
Figure 6.7: Coverage rates of youth minimum wages, UK, 2011-2024



Source: LPC analysis of ASHE, low pay weights, UK, 2011-2024. 16-20 population, excluding those eligible for the Apprentice Rate. Estimates are chain-linked to account for the methodology change in 2021. Dashed lines indicate the period affected by the pandemic.

6.16 There is some nuance to the use of the youth rates. While only 15 per cent of workers aged 16-17 are paid at their minimum wage rate, 75 per cent are paid less than the NLW (Figure 6.8). This means that three-quarters are 'effectively covered' by youth rates; their employer is making use of the availability of youth rates by paying less than the NLW. In some cases, this may reflect employers choosing to pay above the age-related minimum wage rate to avoid the risk of non-compliance. However, of those paid between their own rate and the NLW, the majority are paid more than 50 pence above their age-related rate, suggesting that other factors – such as competition between employers, or concerns over fairness – also play a role.

Figure 6.8: Coverage of own minimum wage rates and NLW, 16-20 year olds, UK, 2019, 2023 and 2024



Source: LPC analysis of ASHE, low pay weights, UK, 2019-2024. 16-20 population, excluding those eligible for the Apprentice Rate. Estimates are not chain-linked to account for the methodology change in 2021.

6.17 Far fewer 18-20 year olds are effectively covered by the youth rates (just under 40 per cent). However, this still represents a sizeable portion of young workers and more than might be expected given stakeholder feedback. Despite large increases to the youth rates in 2024, the share of 16-20 year olds paid below the NLW only increased by one percentage point and remains below 2019 levels (Figure 6.8).

In some sectors, the youth rates are rarely used

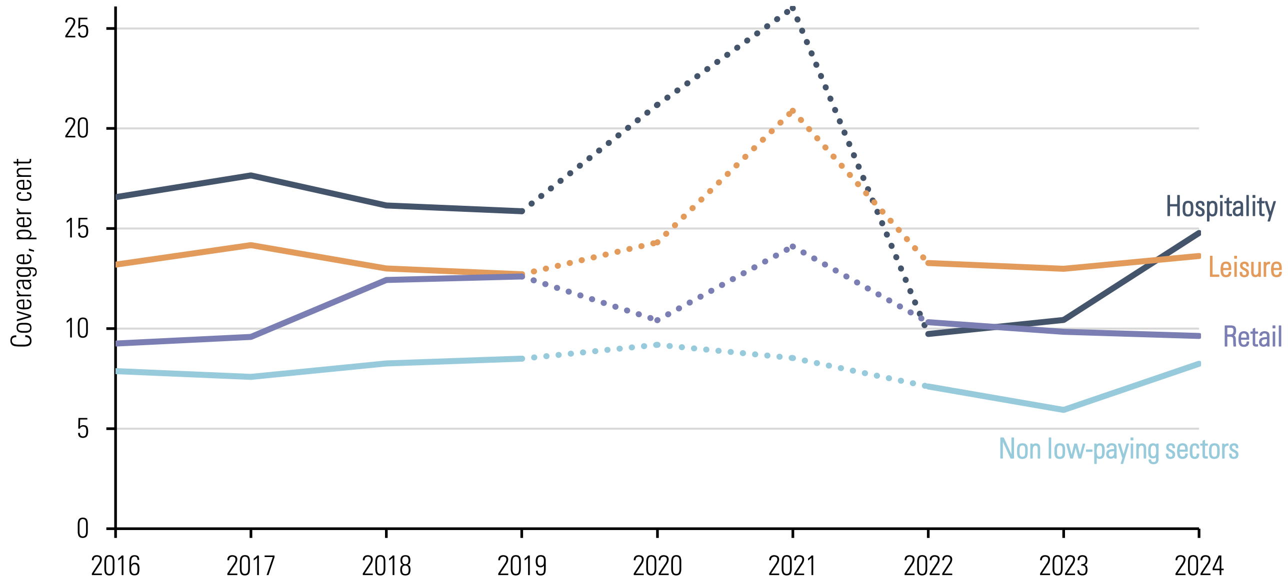
6.18 Care England and the Homecare Association (HCA) both told us that the sector employs an older workforce, with an average age of 44 due to struggles employing younger people and making social care an attractive career. The sector does not differentiate pay based on age, and pays a standard rate for each care worker. The Chartered Institute for Payroll Professionals (CIPP) reported that a significant proportion of its members "pay based on job role rather than age". This most often reflected "an ethical standpoint" and recognition that young workers may be living independently; another rationale was "to reduce the administration burden of changing rates when employees move between brackets".

6.19 Make UK told us its members rarely used youth rates, preferring to pay according to skills, experience and value added to the business. It stated the tight labour market had further reduced the use of youth rates, as offering the lowest wage often resulted in low or no applications. For some Horticultural Trades Association (HTA) members, "the minimum rate for 16-17 year olds is not used, with some businesses opting to pay the same wage rate for those doing the same job regardless of their age." The National Farmers' Union (NFU) also told us that "workers in the horticulture sector are in the main paid according to job performed rather than by age." However, this is not true for other parts of the farming sector where youth rates are used more extensively. As one poultry farmer told us, "We do have rates for 16 to 17 [and] 18 to 20. We certainly do, because to pay a 16-17 year old the same as you pay somebody who's been in the business for 30 years, that's not right."

Other sectors use youth rates more extensively

6.20 Coverage of youth rates is higher in low-paying sectors such as hospitality, retail and leisure (Figure 6.9). Following the large increases in youth rates this year, coverage in hospitality and non-low paying sectors increased significantly while coverage in retail fell slightly.

Figure 6.9: Coverage by industry group, 16-20 year olds, UK, 2016-2024



Source: LPC analysis of ASHE, low pay weights, UK, 2011-2024. 16-20 population, excluding those eligible for the Apprentice Rate. Estimates are chain-linked to account for the methodology change in 2021. Dashed lines indicate period affected by the pandemic.

6.21 In hospitality, the British Beer and Pub Association (BBPA) reported that around 60 per cent of members used the youth rates and coverage had increased due to the size of recent increases. It quoted one member: "A large proportion of our workforce are aged under 25 so it added a significant cost to our business. This affects our long-term profitability and therefore our future investment back into the company." UKH told us about 44 per cent of its members used the youth rates. UKH's survey found that members used youth rates primarily "to manage costs, maintain operational flexibility, and recruit and train young workers effectively – as well as reflecting levels of experience and regulatory constraints".

6.22 In retail, the British Retail Consortium (BRC) reported that fewer than 4 per cent of retailers paid less than the NLW, down from 6 per cent of retailers last year. The BRC told us that "the only time [retailers] use [youth rates] and do say that they are useful is for newer members of staff who may be being effectively trained up." Usdaw stated that "many companies which employ significant numbers of young people, especially across the retail sector, are able to do so whilst paying the full adult rate." We spoke to one young worker in Northern Ireland who worked for a large retail chain and earned less than the NLW, but most retail workers we spoke to earned at least the NLW. Among smaller retailers, there was a more mixed picture. The Association of Convenience Stores (ACS) told us the use of age rates among its members was quite low as it was difficult to argue a case for paying less for performing the same role. On the other hand, representatives from both National Craft Butchers and the Farm Retail Association told us that youth rates were important in their sectors, particularly when it came to new entrants and ensuring pay differentials for more experienced staff.

6.23 Some other smaller sectors rely more heavily on youth rates. The National Hair and Beauty Federation (NHBF) told us its members used youth rates for a range of reasons, including cost management, the ability to invest in training and development, greater ability to create entry-level positions and to maintain competitive pricing. The British Beauty Council (BBC) told us its members made full use of the age rates to reduce salary costs. A survey by the Equestrian Employers Association

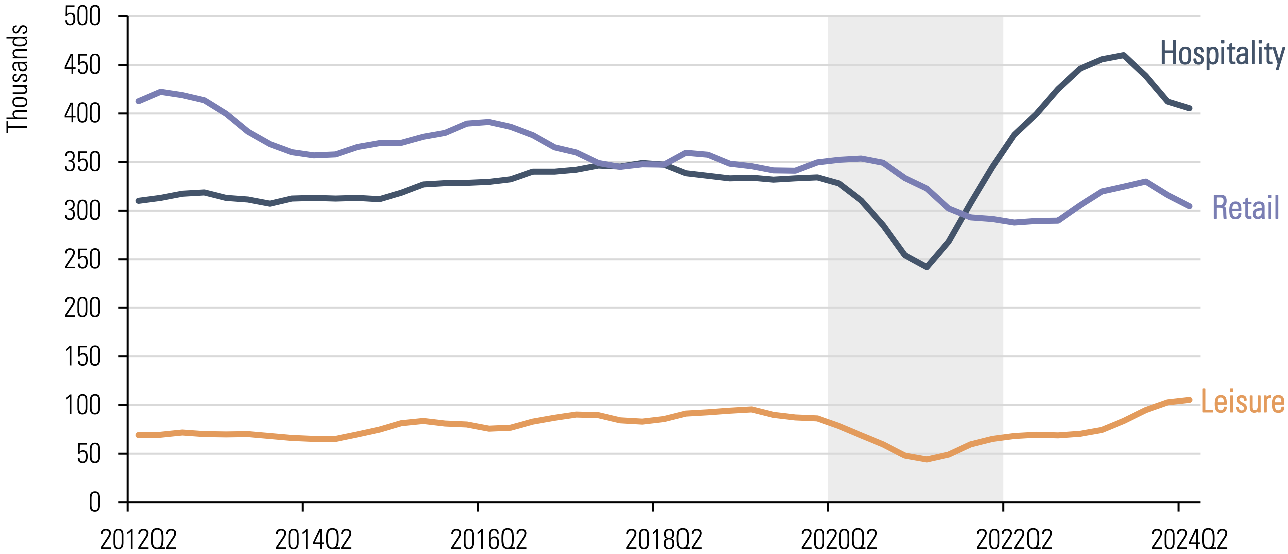
(EEA) found that 50 per cent of respondents used the youth rates and around a third of survey respondents reported they could not afford to recruit people eligible for the NLW.

6.24 Smaller firms are also more likely to use youth rates. Around a quarter (24 per cent) of 16-20 year olds working in small and micro businesses were covered by youth rates, compared with only 4 per cent of 16-20 year old employees in large businesses. The Federation of Small Businesses (FSB) told us that around three in ten of its survey respondents reported using the youth rates either for 18-20 year olds or 16-17 year olds. But larger shares (42 and 63 per cent respectively) reported paying young workers a rate somewhere between the NMW rate and the NLW.

Demand has weakened in the low-paying sectors where young people work

6.25 For 16-20 year olds, low-paying sectors make up the bulk of their employment, particularly the hospitality and retail sectors that together account for roughly half of all employment for those aged under 21. LFS data show that youth employment has weakened over the past year in these sectors (Figure 6.10).

Figure 6.10: Number of workers under 21, by largest low-paying sectors, UK, 2012-2024



Source: LPC analysis of LFS, population weights, UK, Q2 2011 – Q2 2024, Standard Occupational Classification (SOC 2020), 16-20 population, 4-quarter averages (backward-looking).

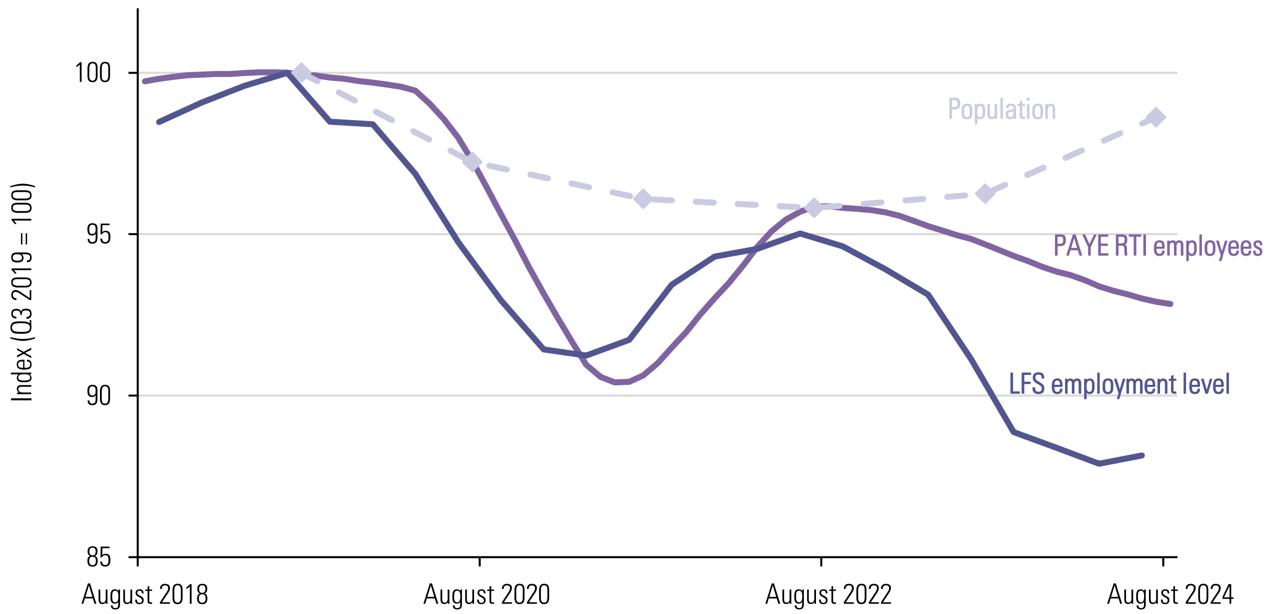
6.26 In hospitality, total employment has declined by around 3 per cent over the past year. Last year, hospitality employers told us recruitment difficulties meant that employers were recruiting more young workers. UKH told us the state of the labour market for younger workers has been more challenging this year, with significant practical barriers against people without higher education qualifications starting and building careers. They described a "move away from inexperienced unskilled young staff because you have to pay them the same level as somebody who has got a bit more experience". They argued that while a "small proportion" of the hospitality workforce was aged 16-18, "it is a really important proportion for those bits of the sector that use [youth rates]," with significant employment of under-18s for seasonal and temporary work. The BBPA reported that 18 per cent of its members' pub workforce were aged 18-20 and 4 per cent were aged 16-17.

6.27 In retail, the decline in youth employment is consistent with the long-term decline in overall employment in the sector described in Chapter 5. The BRC told us that "labour demand has pulled off quite considerably" in the sector as a whole, with employment on "a steady downward trend since 2016".

The impact of lowering the NLW age threshold to 21 has been limited

6.28 In April 2024, 21-22 year olds became eligible for the NLW, increasing their minimum wage from £10.18 to £11.44 (12.4 per cent). Following this, the share of 21-22 year olds covered by their minimum wage rose sharply to reach 19 per cent in April 2024 (see Chapter 5 for further detail). 21-22 year old employment has performed poorly over the past few years, with both PAYE RTI and LFS data showing that employment levels for 21-22 year olds never fully recovered from the pandemic (Figure 6.11). The employment rate improved between 2021 and 2022 but has fallen over the past two years (although as discussed above, the population projections used are not directly comparable with the RTI employee numbers). However, median hourly pay growth has been strong, suggesting robust demand for workers of this age (7.5 per cent in the year to April 2024, compared with 6.3 per cent for those aged 23 and over, excluding those eligible for the Apprentice Rate).

Figure 6.11: Projected change in population compared to PAYE RTI employee and LFS employment levels, 21-22 year olds, UK, 2018-2024



Source: LPC analysis of HMRC PAYE RTI data, 21-22 population, not seasonally adjusted, UK, August 2018-August 2024, 12-month averages (backward-looking), indexed to August 2019; LFS, UK, Q3 2018 – Q2 2024, 21-22 population, 4-quarter averages (backward-looking), indexed to Q2 2019; ONS mid-year population estimates, UK, 2019-2023; and ONS 2021-based interim population projections, UK, 2024. 2021-based population projection year-on-year growth rates have been applied to 2023 estimates to estimate 2024 population due to a discrepancy between the 2021-based projections and the mid-2023 estimates. PAYE data for 21-22s is as provided to LPC on 7th October 2024. These may differ from revised figures published later.

6.29 We are also reassured by the econometric evidence: we have replicated the research carried out by London Economics on 23-24 year olds (London Economics, 2022) and applied it to 21-22 year olds. We find no evidence of employment effects, but this research uses LFS data and so there may be quality concerns (see Appendix 3). However, using ASHE data, we also find no effect of the change on hours worked. It is too soon for us to evaluate the full impact of bringing 21-22 year olds into the NLW on employment outcomes. As more ASHE and LFS data becomes available, we will conduct an in-depth evaluation.

Employers have felt little impact from lowering the NLW threshold to 21

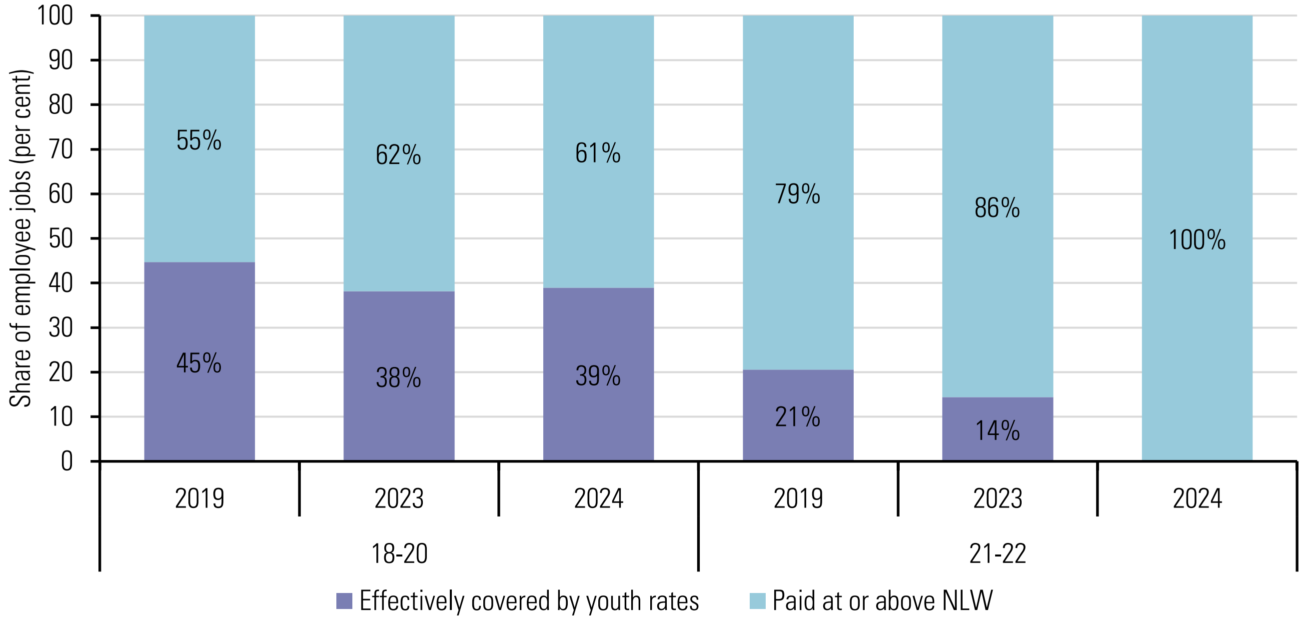
6.30 Most employers reported minimal impact from lowering the NLW threshold to 21 as most already paid 21-22 year olds at or above the adult rate. For example, Make UK told us that youth rates were considered too low to attract young people into manufacturing. The Food and Drink Federation (FDF) told us most members already pay above the 21-22 Year Old Rate. The NFU told us about industry-wide audit requirements that workers' pay is determined by the job performed and not age. The British Beauty Council (BBC) supported the reduction to age 21, recognising that higher pay for young people made them more likely to remain in the sector and benefit from in-house training. However, they stressed that lowering of age thresholds for wage rates should be balanced against government support measures that ease the pressure on businesses, otherwise it would largely be untenable for many SMEs. UKH told us that "the great majority of our members paid the NLW from 21" and so had not been affected by the move from 23 to 21; in addition, "this change in eligibility had been flagged well in advance so this aided the management of the transition." In the BBPA's member survey, around two-thirds of respondents had seen no impact as 21-22 year old employees were already being paid at the NLW rate or above. For the remaining third, however, there had been an increase in operating costs which was in some cases significant.

6.31 The Intergenerational Foundation (IF) told us it was pleased with the lowering of the NLW threshold to 21: "IF believes that the newly lowered NLW age threshold will be an important lifeline for young people. Lower minimum wage rates for young people are sometimes justified based on the assumption that young people live with their parents or are in part-time education, but 40 per cent of those aged between 20 and 22 are living on their own and therefore likely to face high, and rapidly increasing, housing costs associated with the private rental market."

The risks are greater for lowering NLW entitlement to age 18

6.32 More 18-20 year olds would be affected by a move onto the NLW than 21-22 year olds were this year. Around one in seven (14 per cent) 21-22 year olds (121,000 employees) earned less than the NLW in April 2023, whereas over 39 per cent of 18-20 year olds (368,000 employees) earned less than the NLW this year (Figure 6.12). Nearly half (46 per cent) of all 18-20 year old workers would earn the NLW if they were currently eligible. The bite of the NLW – the ratio of the NLW to median wages for this age group - is also higher for 18-20 year olds. The NLW bite for 21-22 year olds was 92 per cent in April 2024, whereas it would have been 99 per cent for 18-20 year olds.

Figure 6.12: Share of employee jobs effectively covered by youth rates, 18-22 year olds, UK, 2019, 2023 and 2024



Source: LPC analysis of ASHE, low pay weights, UK, 2019-2024. 18-22 population, excluding those eligible for the Apprentice Rate. Estimates are not chain-linked to account for the methodology change in 2021. The 2024 shares do not account for any NLW underpayment of 21-22 year olds.

6.33 Unions support the removal of youth rates. The Trades Union Congress (TUC) supported the goal of "expanding the NLW to cover workers of all ages as quickly as the evidence allows". GMB argued that low coverage and strong employment showed the youth rates were not needed. It pointed to other countries which have removed the youth rates, such as Australia and Canada, "where nearly all provinces have no youth rates of pay," as well as Ireland, where the Irish Low Pay Commission has recommended their removal. UNISON also stated its opposition to youth rates, which "remain a fundamentally unfair and discriminatory feature of the minimum wage system" and "an unacceptable injustice in the workplace". It argued that low coverage rates showed the "great majority of employers [recognise this and] accordingly waive the youth rates."

6.34 Some employer groups accepted the proposal to lower NLW eligibility to 18 but called for it to be implemented gradually. The Confederation of British Industry (CBI) noted that the path to an NLW for 18 year olds was more challenging than the changes made thus far, and with compulsory education up to 18, would mean there would be no such thing as a "new entrants' rate" in the labour market. It called for a policy response (beyond pay) to the gradual increase in youth unemployment and inactivity "to make sure that we're not losing young people in their transitions into the labour market and making that any harder than it already is". Make UK suggested its members would accept changes to the NLW age threshold with some reservations. It quoted one member: "[I have] no concerns with 18-20s getting the same minimum rate as older workers if expectations are the same and they are doing the same job." It recommended staggering the implementation over several years to give employers visibility of the changes, and also argued that "to balance the lowering threshold, the increase in [the NLW] should not be as high as it has been in previous years." The FDF urged the LPC and the Government to consider phasing in a lower age threshold over a number of years.

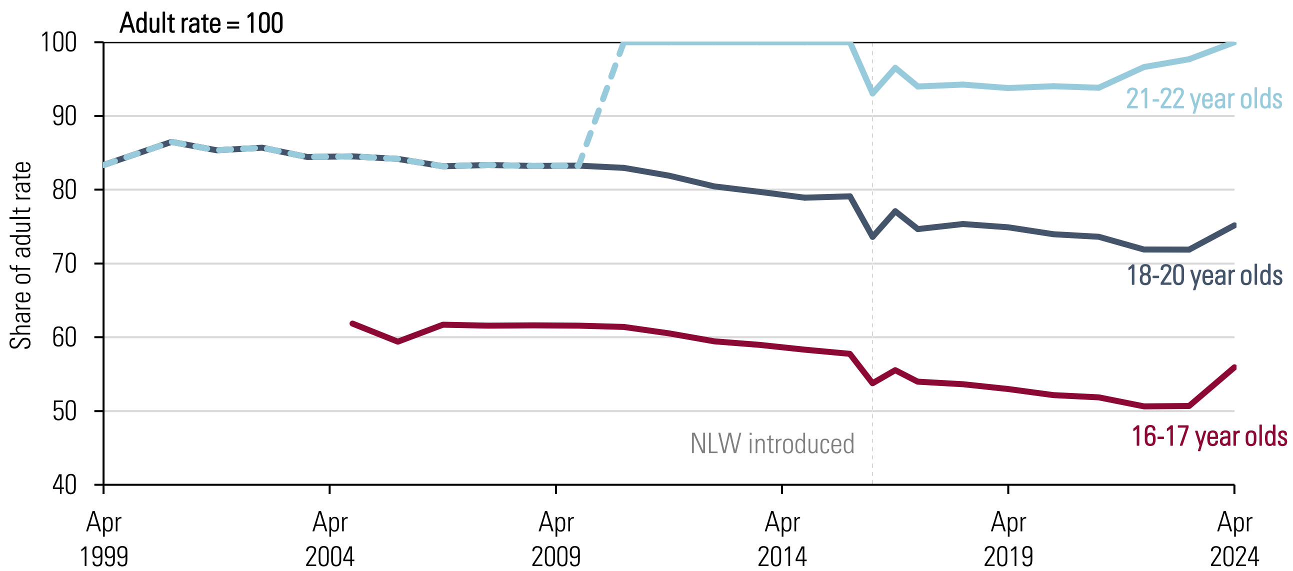
6.35 The FSB's survey found that of those businesses which employed 18-20 year olds, only 16 per cent said that lowering the threshold would have no impact. Nearly half (44 per cent) said they would recruit fewer workers in this age range; the same proportion said they would raise prices. The Recruitment and Employment Confederation (REC) said that as youth rates drew closer to the NLW, businesses were less inclined to hire young people due to the lack of experience compared to other candidates.

6.36 The British Chambers of Commerce (BCC) recommended that the youth rates "should rise in proportion to the NLW (i.e. there should be no widening or further closure of the gap)," arguing that a higher youth minimum wage could discourage employers from hiring younger workers. Employers, it told us, reported that young workers are often less productive and more costly to employ, for example requiring extra training. The National Farmers' Union Scotland (NFUS) argued that young, inexperienced workers needed training and time to develop, at a cost to their employer, and it was "absurd" to expect employers to pay them the same as skilled and experienced workers. The EEA thought the consequences for its sector would be serious, quoting one member: "Our total wage bill has gone up 18.4 per cent this year and 13-18 yr olds wages have gone up 48 per cent since April 2021. If this lower age band increases again, we will have to close our business."

The gap between the 18-20 Year Old Rate and the NLW remains large

6.37 The gap between the 18-20 Year Old Rate and the NLW is much greater than was the case for the 21-22 Year Old Rate before it was subsumed into the NLW. The 21-22 Year Old Rate remained above 90 per cent of the adult rate while the 18-20 Year Old Rate was 72 per cent of the adult rate before we began to close the gap in April 2024 (Figure 6.13). We began to narrow the gap between the NLW and the 18-20 Year Old Rate this year, bringing the 18-20 Year Old Rate to 75 per cent of the adult rate in April 2024. The gap between the 16-17 Year Old Rate and the NLW also remains large, with the 16-17 Year Old Rate at 56 per cent of the adult rate in April 2024.

Figure 6.13: Youth rates as a proportion of adult rate, 1999-2024



Source: LPC historic minimum wage data. Prior to October 2010, there was an 18-21 Year Old Rate (Youth Development Rate) and workers aged 22 and over were eligible for the adult rate.

18-20 year olds are more likely to be students working part-time

6.38 18-20 year olds also have different non-pay characteristics to 21-22 year olds. Around three in five 21-22 year old employees work at least 32 hours a week, compared to just over a third (34 per cent) of 18-20 year olds. Around two in five (41 per cent) 18-20 year old workers are in full-time education while fewer than one in five (18 per cent) 21-22 year old workers are in full-time education.

6.39 The effect of youth minimum wages on incentives to remain in education or training is ambiguous. A higher minimum wage can increase the relative value of working compared to staying in education, but it could also reduce the number of employment opportunities available for young people. Bowyer, Cerqua, Pietro, Gorman and Urwin (2019) found that there was limited scope for youth minimum wages to affect educational decisions for 17-19 year olds in the UK.

6.40 We received a submission from a research team led by Dr Kim Allen at the University of Leeds on young women's labour market transitions. The submission noted that for many young people, education and employment are combined. The respondents noted that one common justification for youth rates "is that lower wages operate as an important incentive for young people to stay in education". However, they told us that many young people work not only to support themselves "but also as contributors to their wider family due to the impact of the cost-of-living crisis". They quoted one participant: "with my parents, like my mum in particular, she used to tell me to like not have a job and study, but the way our family was I had no choice but to work...So I was just like, you are saying this, but we are not millionaires; I have to work." They also noted evidence that "earnings from paid work now comprise over a quarter of average full-time student income." The response went on to argue that raising youth rates can have a positive impact on education outcomes. A higher minimum wage for young workers "is needed to enable young people to stay in education and complete their studies; improving their job prospects in the longer-term as well as their present quality of living". The King's Trust also argued that "Differential pay rates for younger adult workers … does not reflect the reality that some will be living independently or supporting families themselves. With the increasing cost of living, lower wage rates for young people risks pushing them into financial difficulty."

6.41 Youth Employment UK argued that real-terms cuts to student finance support had increased students' reliance on working while studying to cover essential costs. Its submission quoted one young person: "many young people, myself included, barely make enough via student finance to cover rent and expenses whilst studying. This means many of us are required to work long hours alongside our studies which can hinder our academic performance. Part time jobs for young people are no longer just to buy new clothes or go out with friends, they are being used to survive and should reflect the amount needed to do so in the respective area they live in."

6.42 Youth ambassadors working with the End Child Poverty Coalition were aggrieved that students cannot claim Universal Credit: "it means that you have to work and you can't get any kind of extra support. And in theory your bursary should cover your university costs, but it doesn't." In addition, they noted that Universal Credit paid less for those aged under 25; "There is a real misconception about the people who are claiming Universal Credit who are young. It seemed to be justified that you can pay young people less, almost like they have some family somewhere to fall back on. But if you're claiming Universal Credit, you don't." The End Child Poverty Coalition told us that between the ages of 16 and 19, 30 per cent of young people were living in relative poverty after housing costs.

6.43 Money Advice Scotland argued that young adults can incur the same costs as their older peers, especially students. It cited research showing that a greater proportion of people aged 18-24 have recently sought debt advice: "the biggest factor that differentiated between people in this age group needing debt advice or not was the type of work they do, with those with lower and less reliable earnings needing debt advice more."

6.44 The Equality Trust also highlighted a range of cost pressures young people face: unaffordable housing costs, a lower rate of Universal Credit for those aged under 25 and student loan repayments. Youth Employment UK called for higher youth rates to allow young people to cover living costs. The Intergenerational Foundation wanted the LPC to remove age-related criteria for the NLW altogether, to "combat the cost-of-living crisis, which affects younger and poorer people the greatest" It claimed that lower first job earnings increase the likelihood of staying in low-wage jobs and that lower rates discriminate against younger people based on age.

Young workers often perceive age-related pay as unfair

6.45 During our Glasgow visit, Unite members working in hospitality reflected on the unfairness of lower pay for young workers. Several participants thought their past or present employers over-recruited young people because they could pay them less regardless of experience. One participant judged that for his role in a hotel restaurant where the 18-20 Year Old Rate was used, the job was "just not worth it for the pay if you're not over 21". One participant argued: "If an employer can prove that an 18 year old costs them £2 per hour", then they could justify differential pay, "but if the value they're creating is the same value – it's crazy to not pay the same amount". On the same visit, a convenience store manager argued that the young workers she employed "are doing as much work as full-time staff … It'd be unfair to say just because you're younger you should be paid less." Younger staff had the same responsibilities as their older counterparts (keyholding and locking up). She paid young workers the full NLW.

6.46 Young people working with the End Child Poverty Coalition also told us about the unfairness of age-related pay in their workplaces. One 20 year old hospitality worker was paid less than her less experienced colleagues, which made her feel her circumstances were "belittled". She disagreed with the premise that someone who's older has "more to think about, more to care about … Why should I be paid pounds less than someone when most of the time I feel like I'm doing more work than they are?"

6.47 The submission by researchers at the University of Leeds, City St George's, University of London and the University of Manchester reported that young workers felt youth rates were unfair. Participants in the study "felt that relatively lower NMW rates were unjust, and some participants reported a sense of unfairness that they were working the same jobs as their older counterparts, for lower pay." Participants also felt "that employers specifically sought out younger workers in order to access the lower rate of NMW". The End Child Poverty Coalition's youth ambassadors also disagreed that age correlated with experience and that if rates were equal, employers would prefer to employ older workers. As one participant summed up: "Many of the jobs we are doing, they'll struggle to fill the spaces. I don't think more older workers will be willing to undergo the levels of exploitation that we currently do. I personally can't see many older people willing to do the hours or the work that we do in nightclubs, for example."

6.48 Young retail workers we spoke to in Northern Ireland generally perceived youth rates as fair. One 20 year old worker told us: "I don't have anyone dependent on me to pay bills or anything or take care of … it makes sense that generally younger people will be getting paid less than someone who has a family or is in their mid-40s." Another worker said that "you have less outgoings and you're not exactly renting someplace in most circumstances, at the age of 16, so you have less money… it does mean that you can get a job easier than someone that would be paid the full rate, because they're going to likely choose people that they're paying less."

Conclusion

6.49 While data issues have limited our analysis of the youth labour market, high hourly pay growth and weakening, but still robust, employment levels give us confidence that 16-20 year olds remain in a reasonable labour market position. While minimum wages have caught up with the growth in median wages, the gap between the youth and adult rates is still large. The evidence, including bites and effective coverage rates below historic levels, suggests scope for increases to the youth rates. We discuss the data on apprenticeships – which have important interactions with the youth labour market – in the next chapter.

6.50 Initial evidence suggests that moving 21-22 year olds to the NLW has not affected the employment prospects for this group, but we will continue to monitor the impact as more data becomes available. The risks are greater for lowering NLW eligibility to 18, but many stakeholders, including unions, charities and some employers, support the change. We discuss potential approaches for closing the gap between the 18-20 Year Old Rate and NLW in Chapter 11.

Chapter 7

Apprentices

Key findings

- **There has been a long-term decline in low-paying apprenticeships –** Total apprenticeship starts in the 2023/24 academic year were consistent with the previous year, but the long-term trend in England remains one of declining starts for those apprentices most likely to be paid the Apprentice Rate. We have not seen declines to the same extent in the devolved administrations, where there has been a much smaller degree of policy change.
- **We do not yet know the full impact of the large increase to the Apprentice Rate in April 2024 –** At the time of our recommendations, we did not have data on apprentice starts in the first quarter of the 2024/25 academic year (August to October), when the largest share of annual starts take place. Apprenticeship vacancies have declined over the year and are now below their pre-pandemic level.
- **Apprentice pay growth weakened in the year to April 2024 –** We do not have our preferred source of apprentice pay data – although for 2023, median pay for apprentices in the Annual Survey of Hours and Earnings (ASHE) was similar to the Apprenticeship Evaluation Survey (AEvS). For most apprentices, ASHE shows weaker pay growth in the year to April 2024 than in the preceding year. This is despite the large increase in the Apprentice Rate in April 2024. Pay growth varies erratically between different age groups.
- **Most stakeholders tell us they do not use the Apprentice Rate but ASHE pay data shows the rate is widely used –** Coverage is highest for under-19s and has jumped in the past year. In addition, "effective coverage" is high across all age bands, showing that employers pay eligible apprentices aged 18 and older less than their NMW age rate. Indeed, apprentices have lower average pay and higher coverage than non-apprentice peers. We intend to investigate further the disparity between stakeholder evidence and the pay data.
- **Changes to the apprenticeship system and youth rates will have implications for the Apprentice Rate –** At the start of 2024 we proposed significant changes to the Apprentice Rate, although we said these should be subordinated to wider changes to the NMW youth rates. Since then, the incoming Government has announced its intention to substantially reform the apprenticeship system in England. We will pay careful attention to the detail of these reforms, once available, and their implications for the treatment of apprentices who are paid less than the NMW.
- **We recommend keeping the Apprentice Rate aligned with the 16-17 Year Old Rate in the interim –** Our recommendations on the Apprentice Rate have been linked to the 16-17 Year Old Rate since April 2022. By measures such as bite and coverage, apprentices are more exposed to changes in the minimum wage than 16-17 year old non-apprentices. Despite this, we continue to think it is right to hold these two rates together, in part for reasons we set out in our advice earlier in 2024.

Introduction

7.1 This chapter focuses on apprentices, the smallest group for whom we recommend a separate minimum wage. The Apprentice Rate is the minimum wage for all apprentices aged 16-18 years old, and for older apprentices in the first year of their apprenticeship only. The Apprentice Rate was introduced in 2010 as the lowest of the NMW rates (and before this, apprentices were not entitled to a minimum wage), in recognition of employers' investment in apprentices' training costs. Since April 2022, we have aligned the Apprentice Rate with the 16-17 Year Old Rate. In April 2024, the rate increased by 21.2 per cent from £5.28 to £6.40, the largest increase in its history in both cash and percentage terms.

7.2 Last year, we reviewed the Apprentice Rate. Our annual report explained the rationale for the rate applying from April 2024, while our separate advice to the Government on the National Minimum Wage Beyond 2024 (2024b) considered the case for removing the rate entirely. For our detailed considerations of the Apprentice Rate and its relationship with outcomes for apprentices, we encourage those interested to read this latter publication.

7.3 We concluded that there were grounds to remove the Apprentice Rate, but doing this at the same time as reducing the gap between the youth and adult non-apprentice rates brought considerable risk. In the context of our recommendations on 18-20 year olds, we stated that reducing the gap between youth and adult rates should be prioritised over changes to the treatment of apprentices. This is because differential minimum wages are more justified on the basis of training than on age. To that end we recommended that we keep an Apprentice Rate but that, for those aged 18 and over, it should change to a simple discount on the appropriate age rate during the apprentice's first year.

7.4 As set out in Chapters 6 and 10, the Government's ambition is to extend the National Living Wage (NLW) to 18-20 year olds. The Government has not responded to our recommendation on the Apprentice Rate, but the rate's future is closely linked to what happens to the NMW youth rates, as well as the Government's plans for reform of the apprenticeship system. The Government has announced plans for the transformation of the Apprenticeship Levy into a new Growth and Skills Levy, a reconsideration of the training which qualifies for funding through this levy and a refocusing of funding towards the youngest apprentices (Department for Education 2024a).

7.5 We think these reforms are likely to have significant implications for apprentices' pay, employment and their minimum wage, although the full detail is not likely to be available for some time. We continue to support the recommendations we made at the start of 2024 but appreciate the need for a joined-up view of reform. In the meantime, this chapter considers the evidence around the Apprentice Rate as it currently exists.

Groups working with young people recommended removing the rate

7.6 In our evidence-gathering this year, many stakeholders continued to argue for the removal of separate treatment of apprentices, on the basis that it harmed their outcomes. Youth Employment UK shared views from a roundtable with young workers where "there was consensus that apprentices should not be paid a lower rate than the NMW, since they contribute to the workforce." Young people valued apprenticeships but felt "the apprenticeship wage is not a fair representation of their efforts." The low Apprentice Rate, Youth Employment UK argued, may deter young people from taking up an apprenticeship. In their Youth Voice survey, they found that "most young people (83 per cent) felt that apprenticeship rates are too low", particularly for those without additional financial support: "more needs to be done to ensure apprenticeships are an attractive option to young people."

7.7 The King's Trust (formerly the Prince's Trust) argued the Apprentice Rate was a barrier to entry for those from disadvantaged backgrounds. Recent increases had been welcome, but "Low pay rates for apprentices – and often just the perception of low pay – can act as a barrier for those from disadvantaged backgrounds who cannot rely on family support, closing off this route for this group. As the cost-of-living limits household finances, the number of families able to act as safety nets for young people pursuing this route could see a decline." They argued that an increase to the rate could improve social mobility and address skills shortages. The End Child Poverty Coalition echoed these views. A survey conducted by Organise showed that 85 per cent of respondents think the Government should scrap the lower rate for apprentices.

7.8 The King's Trust suggested the Apprentice Rate should be 80 per cent of the NLW for adults. This would "acknowledge the non-productive time that apprentices spend on off-the-job training, while still fairly recognising their contribution" and ensuring that apprenticeships remain accessible to all.

7.9 The National Society of Apprentices told us that most of the young people they spoke to put apprentice pay as their "absolutely top priority" to fix. They argued there was a link between low pay and inadequate training provision: "The Apprentice Rate is currently used, to be charitable, not by our blue chip apprenticeship provision … There's a correlation between apprentices who don't receive their 20 per cent off the job training and pay levels." They noted the gender disparity in apprentice pay: "We see broadly that women's work is underpaid and boys' jobs get good wages." They also pointed out the disparity in benefit treatment between apprentices and those on T-levels; apprentices' families would lose their child benefit, whereas those on the T-level ("exactly the same work and standard, delivered full time") continued to be eligible: "that's absolutely, utterly bonkers".

7.10 Unions tended to call for the removal of the rate. The Trades Union Congress (TUC) argued the Apprentice Rate should be equalised with the main rates, stating: "The current set-up has risked encouraging exploitative employers to deliver poor quality apprenticeships in order to access cheap labour. Unite described the rate as "tantamount to exploitation," calling for it to be set level with NMW age rates "as a bare minimum." Good employers, they argued, "are being undercut by unscrupulous bosses who are exploiting the apprenticeship system."

7.11 The British Beer & Pub Association (BBPA) said they would be supportive of the move to a simple discount for apprentices of the kind proposed by the LPC, subject to the level of the discount. They welcomed the simplification and felt that improving the Apprentice Rate could act as an incentive to new recruits. However, there was a caveat that this supportive view was contingent on future increases in NMW rates. The Chartered Institute of Payroll Professionals (CIPP) were in favour of the LPC's proposal on the grounds of simplification: "Currently during onboarding payroll departments need to be aware of commencement dates and apprenticeship start dates, this can cause confusion and miscommunication, leading to errors." They noted that caution needed to be applied in calculating the right discount rate.

7.12 The British Chambers of Commerce (BCC) stated the Apprentice Rate should be set at a level that is attractive to young people; while some members use the rate, many others pay the age-appropriate rate in order to attract and retain good quality candidates.

Some employer groups opposed the removal of the rate

7.13 The Federation of Small Businesses (FSB) advised us to evaluate recent large increases before any further significant changes. "The Apprentice Rate increased substantially in April 2024. We would suggest that a proper evaluation of the impact this has had on apprenticeship starts among young people and SMEs is conducted before any further significant increase." The FSB tempered their previous support for increases; "it is a fine balance to be struck in ensuring that the supply of employers willing to hire apprentices is not hamstrung by it becoming overly expensive to hire."

7.14 The National Hair & Beauty Federation (NHBF) oppose the rate's removal, because of the low revenues that apprentices initially bring to a business. They quoted one member: "I've now got somebody on say £11.44 an hour that's going to bring not a penny into my business as it takes them a year to 18 months to grow a clientele because our frequency of visits has dropped ….and so it's two year apprenticeship and then it's at least a year, if not two, before we get them to a break-even point."

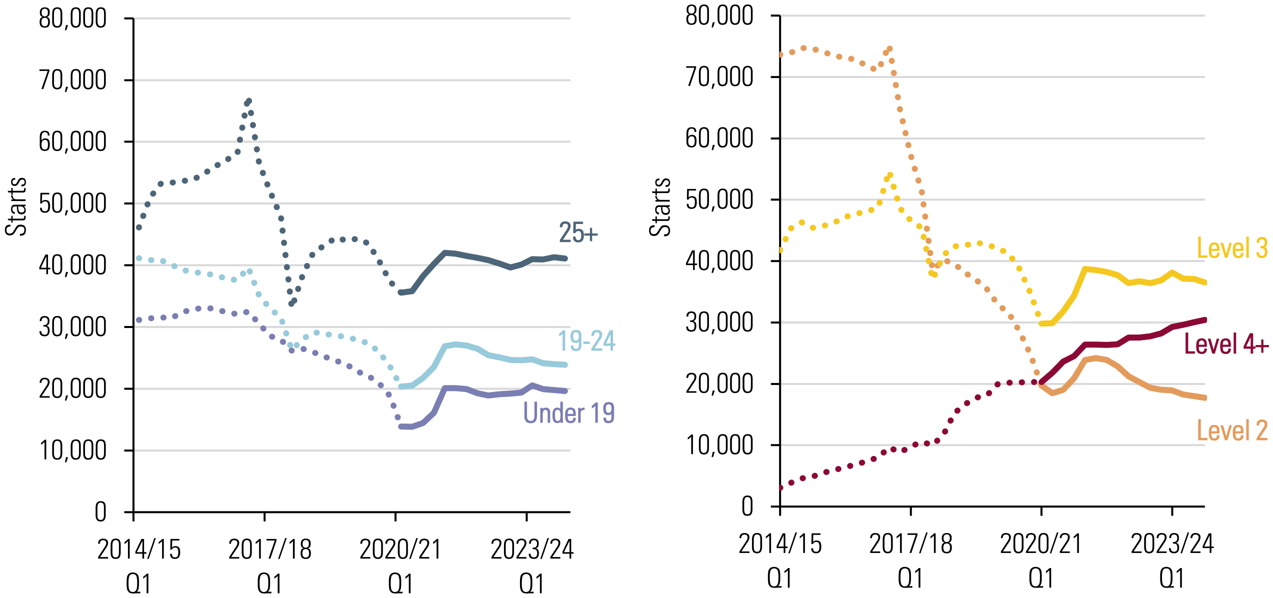
7.15 The Equestrian Employers Association (EEA) said that there was "huge concern amongst employers" at the prospect of the rate's removal, 69 per cent of whom said this would result in fewer apprenticeships being available. A similar share expressed concern over the effect on staff morale if more experienced staff were being paid equal to apprentices. The greatest concern reported was that there would be no incentive for employers to recruit apprentices if they could get higher-skilled workers for the same cost, with 77 per cent saying this was a worry for them.

Apprenticeship starts

7.16 We look at apprenticeship starts to assess what's happening to apprentice employment. Employers' decisions on apprentices are driven by a wide range of policy and funding decisions; the minimum wage is only one of these, and it is difficult to separate the impacts. Apprenticeship policy is devolved across the UK; funding arrangements vary between the four nations and each publishes separate statistics.

7.17 Apprenticeship starts in England have been stable over the past year, with a provisional total of 338,640 starts in the 2023/24 academic year (August to July), 0.6 per cent higher than the previous year. The introduction of the Apprenticeship Levy and other associated reforms in 2017 were a major upheaval to apprenticeships in England. Under these reforms, employers with a payroll over £3m pay a levy worth 0.5 per cent of their annual pay bill; these funds go into an account which they can then use to fund apprenticeships. Smaller employers do not pay the levy; they can access funding for their apprentice training costs, but have to make a contribution of 5 per cent. Following the levy's introduction, starts at Level 2 (equivalent to GCSEs) and among younger apprentices declined sharply. Although the composition of starts by age has not changed significantly in recent years, the composition by level has continued to shift, with starts at Level 4 and above (equivalent to degree-level or higher) continuing to rise and Level 2 to decline to new lows.

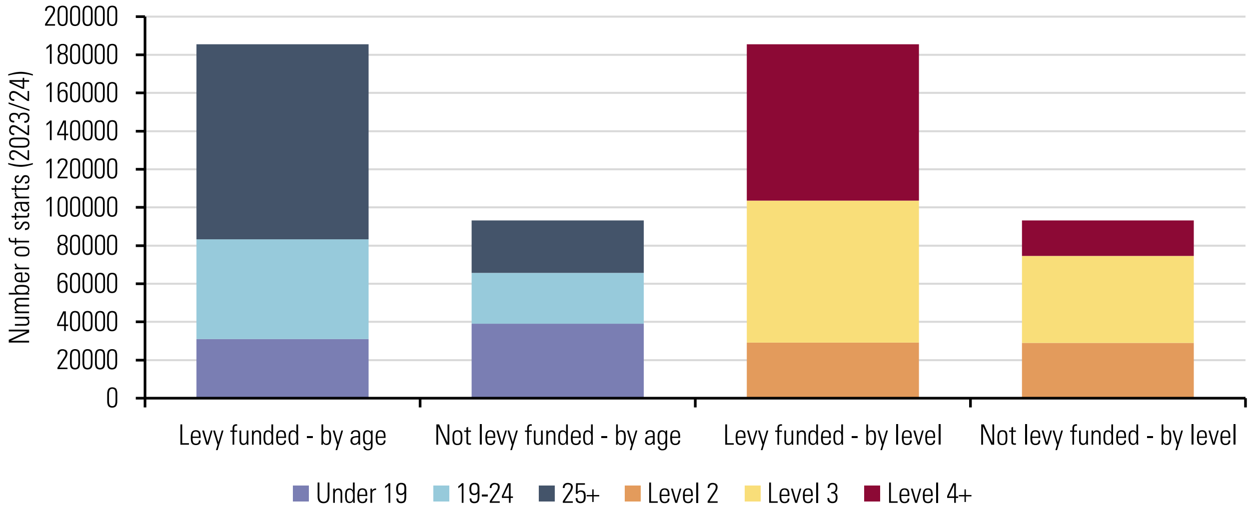
Figure 7.1: Apprenticeship starts, England, by age (LHS) and level (RHS), Q1 2014/15-Q4 2023/24



Source: LPC analysis of DfE, Explore Education Statistics (October 2024), England, Q1 2013/14– Q4 2023/24. 4-quarter rolling averages. Data is organised by academic year (Aug-Jul). Dotted lines indicate final full-year data (historical series). Solid lines indicate provisional full-year data as at October of each year (which are comparable with the latest data we have for 2023/24). There are not usually significant changes between provisional and final full year data.

7.18 The introduction of the Apprenticeship Levy shifted the composition of apprenticeships. Around two in three apprenticeship starts in England in 2023/24 were funded by the levy (that is, they took place in or were otherwise funded by larger employers with a pay bill over the £3m threshold). These larger employers are much more likely to fund higher level apprenticeships and courses for older individuals than smaller firms. The majority of starts for under-19s are in smaller employers who do not pay the levy; this group are also much more likely to take on apprentices on Level 2 courses.

Figure 7.2: Apprenticeship starts, England, by age, level and levy status, 2023/24

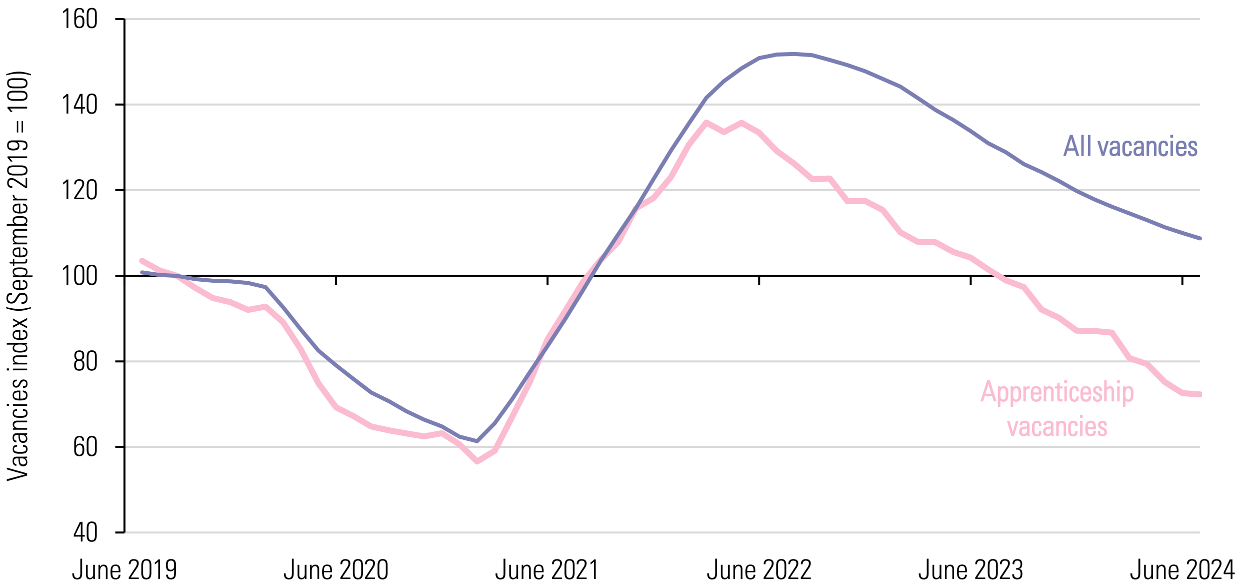


Source: LPC analysis of DfE, Explore Education Statistics (October 2024), England, 2023/24 academic year.

7.19 The starts data available at the time of our decision in October only extended to July 2024, the final month of the 2023/24 academic year. The busiest period for apprentice starts each year is the first quarter of the academic year and September in particular; in 2023/24, more than one in five starts were in September 2023. The lack of starts data for the beginning of the 2024/25 academic year limits our ability to really assess the strength of the apprentice labour market in the wake of this April's uprating.

7.20 One forward indicator we can access is the vacancy figures drawn from DfE's Find an Apprenticeship site. Here we see that vacancies have declined steadily from their post-pandemic highs. To an extent, this reflects broader trends in the economy, where all vacancy measures have moved down as the labour market has loosened. The apprentice vacancies measured by the DfE, however, have fallen faster relative to their pre-pandemic level, and are now lower than in 2019.

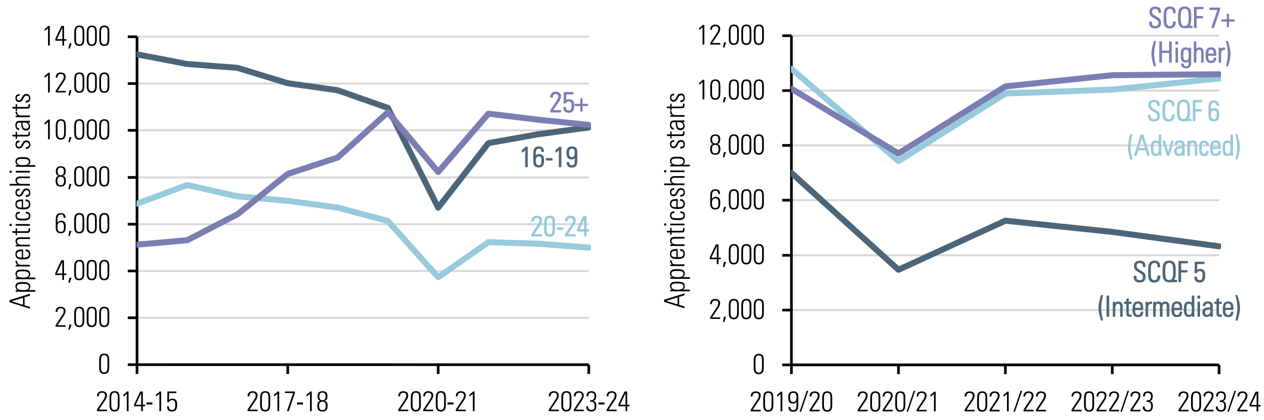
Figure 7.3: Apprenticeship and total vacancies relative to September 2019, 2019-2024



Source: LPC analysis of ONS Vacancy Survey (VACS01), UK, June 2019 - September 2024. 12-month average (backward-looking) relative to September 2019, for 'All vacancies'. DfE Apprenticeships and traineeships statistics: vacancies as reported on the Find an Apprenticeship website, England, June 2019 – September 2024. 12-month average (backward-looking) relative to September 2019, for 'Apprenticeship vacancies'.

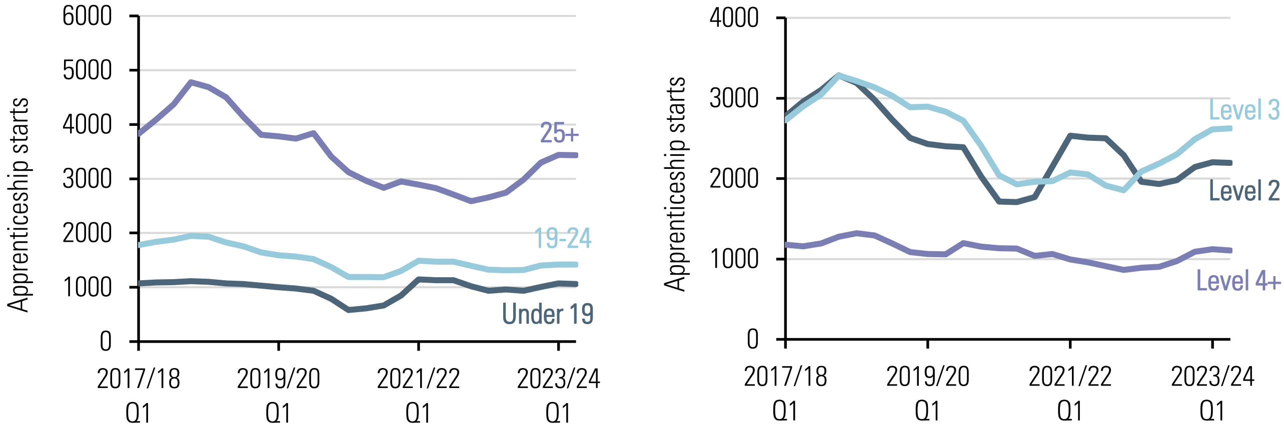
7.21 Compared with England, the composition of apprentices is different in the devolved administrations. On an age breakdown, Wales is most similar to England, with over-25s predominating. In Scotland, numbers of 16-19 and 25+ year olds are roughly equal. In Northern Ireland, 16-19 year olds are the largest group, although starts among 25+ year olds have shot up in the latest data in response to changes in funding policy (Department for the Economy, 2023). Also notable is the greater stability in overall numbers. In Wales, overall apprentice numbers have declined since 2017/18, but unlike England this has not been concentrated among the youngest apprentices or at the lowest levels. In Scotland and Northern Ireland apprenticeship starts have been much more consistent from year to year. These differences reflect the varying policy contexts and funding mechanisms between nations (the Apprenticeship Levy only applies in England and apprenticeships are publicly funded in the other nations). It also suggests that the minimum wage is of secondary importance for starts compared with other aspects of Government policy.

Figure 7.4: Apprenticeship starts, Scotland, by age (LHS) and level (RHS), 2014/15-2023/24



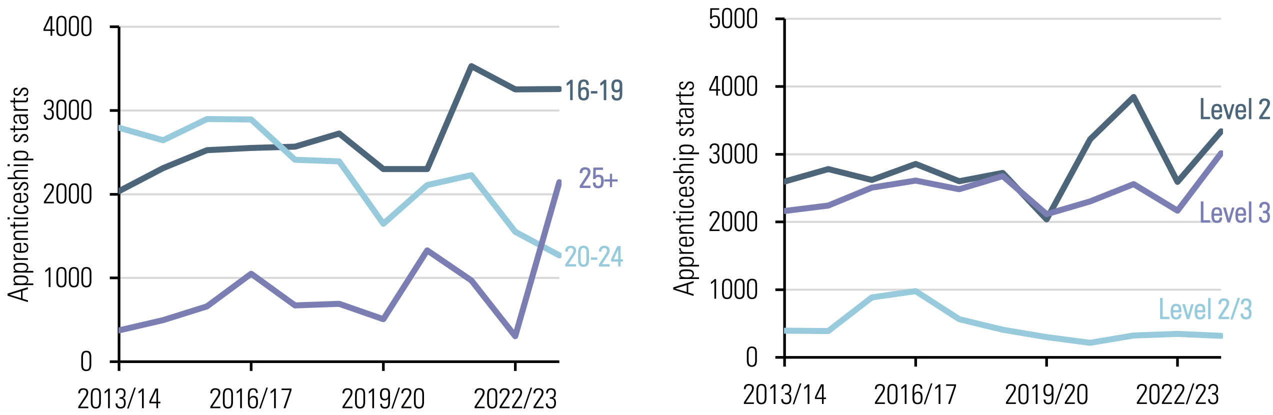
Source: LPC analysis of Skills Development Scotland Modern Apprenticeship Statistics (May 2024 edition), Scotland, 2014/15-2023/24. Data for Scotland are organised by financial year (April to March).

Figure 7.5: Apprenticeship starts, Wales, by age (LHS) and level (RHS), 2017/18 Q1 – 2023/24 Q2



Source: LPC analysis of StatsWales Apprenticeship learning programmes started by quarter (August 2023 edition), Wales, academic years 2017/18 Q1-2023/24 Q2. Four-quarter average (backward-looking).

Figure 7.6: Apprenticeship starts, Northern Ireland, by age (LHS) and level (RHS), 2013/14 – 2023/24



Source: LPC analysis of Northern Ireland Department for the Economy ApprenticeshipsNI Statistical Bulletin, Northern Ireland, August 2017 to April 2024. 2023/24 academic year figures are for August to April only.

Many stakeholders report a steep decline in apprenticeship starts due to funding issues and inflexibility in the Apprenticeship Levy

7.22 Several respondents to this year's consultation lamented declines in apprenticeship starts. Most respondents identified the funding system as the main cause. Make UK told us that although apprentices were critical for their sector's growth, apprenticeship starts had fallen by around 41 per cent since the introduction of the Apprenticeship Levy. They argued the lack of sustainable funding and flexibility in the levy were key factors in this decline. The Food and Drink Federation (FDF) described the outlook for apprentice recruitment in their sector as challenging, with difficulties due to the high number of experienced workers retiring and limited interest from new entrants. Food and drink manufacturers had worked to develop standards for their sector but the uptake of these programmes have flatlined or fallen since 2020.

7.23 NHBF reported that apprenticeships in their sector were in decline, due to a combination of "the shift to self-employment, lower levels of funding and young people staying on in education." Their April 2024 survey found that recruitment intentions for apprentices were negative, with 14 per cent certain or likely to take on apprentices in the next three months, compared with 30 per cent saying it was unlikely and just over half that they definitely would not. NHBF's submission referenced a 2022 survey which identified the lack of financial support from the Government as the biggest threat to apprenticeships in the sector. NHBF argued for greater redistribution of levy funds to small businesses in the form of employment incentives. When we spoke to NHBF members in Portsmouth, they saw the collapse of apprenticeships as a systemic risk for the industry. One salon owner remembered: "they used to queue out the door then, right? I mean, we used to have like 300 applicants for a hairdressing apprenticeship." The British Beauty Council thought that improved incentives for employers to take on apprentices would help the sector.

7.24 BCC told us that small and medium employers advertising apprenticeships at the Apprentice Rate reported a shortage of candidates applying, as young people could earn more in a job that offered no learning opportunities. Families also lost child benefit and other allowances when a young person began a job with training. The BCC noted many businesses were unable to invest in training and supported proposals to incentivise this. UKHospitality (UKH) told us there were a number of issues holding back the uptake of apprentices but pay was less significant than the structure of the system.

7.25 The Papworth Trust reported that increasingly line managers were not keen to hire apprentices due to poor support from training providers (the third parties who provide off-the-job training to apprentices). "We have mixed experience from apprenticeship providers who provide an inconsistent level of support and the quality of that support is also varied." Employer members of the Hampshire Chamber of Commerce complained that the Apprentice Rate did not act as an incentive to employ apprentices, but the increase in wages after the first year was a disincentive to keeping them on. One employer told us this increased their staff costs by £12,000; others agreed this change had a cost impact. "We can't show their increased productivity within that time because they're still just coming out of training. […] An unscrupulous employer could almost get rid of those employees and employ another apprentice for what it's going to cost you."

7.26 The Local Government Association (LGA) were rare in painting a positive picture of apprenticeship starts. The average annual number of starts created by the local government sector (14,100) was more than double the annual average before the levy was introduced (6,000), and all delivered at a time of significant financial constraint. However, they also pointed to frustrations with the way the apprenticeship levy worked for their sector, which was preventing them from doing more in this space.

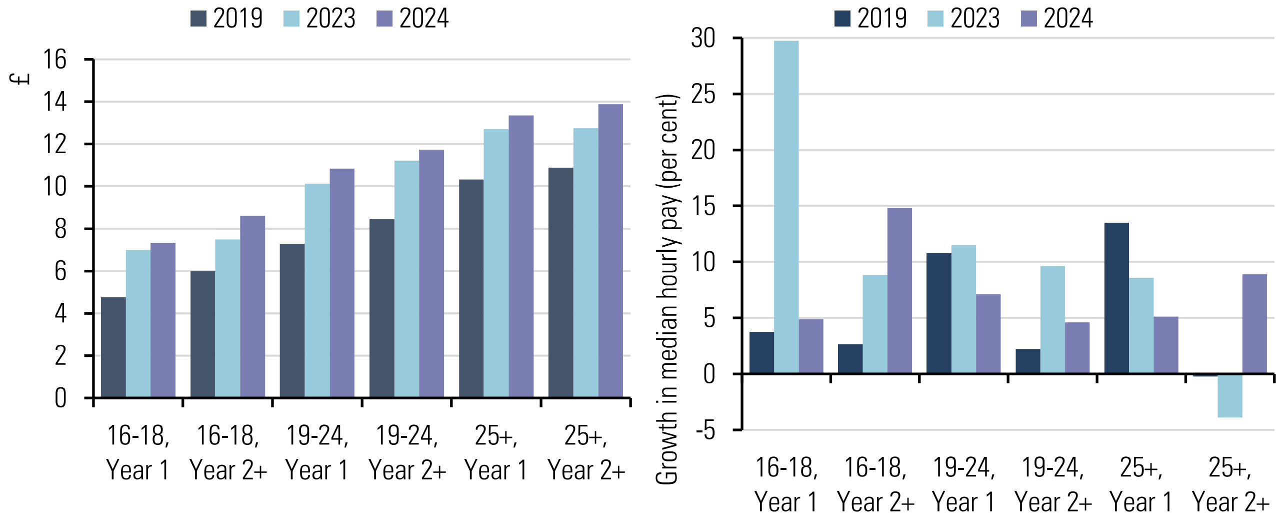
7.27 The Scottish Women's Convention (SWC) noted that women face barriers to accessing and progressing in apprenticeships. SWC argue that the "engrained misogyny at play across sectors, such as construction, contribute to [women's] continued disengagement in apprenticeships." Undertaking an apprenticeship "can be intimidating due to a lack of women colleagues and teachers, as well as a 'boys' club' mentality which can make working environments uncomfortable."

Apprentices' pay

7.28 We use the Annual Survey of Hours and Earnings (ASHE) to look at apprentices' pay. In previous reports, we have noted ASHE's shortcomings when it comes to apprentice pay; the principal problem is that it undercounts the number of apprentices in the workforce (Low Pay Commission, 2020). A related issue is that it may have a particular weakness in identifying apprentices on low earnings. Our preferred data sources on apprentice pay are the direct surveys of apprentices; formerly this was the biennial Apprentice Pay Survey, carried out by predecessors of the Department for Business and Trade and last held in 2019; in 2021 and 2023, pay questions were included in the Department for Education's Apprentice Evaluation Survey (AEvS). We do not have access to any new AEvS data this year, although in our analysis of the 2023 survey we found that its estimates of median apprentice pay matched reasonably closely with those observed in ASHE.

7.29 As we have seen in previous years, apprentice pay increases with age and length of time in post. In April 2024, median pay for 16-18 year olds in their first year was £7.33, rising to £8.60 in their second year. For most age groups, growth in median pay slowed between April 2023 and April 2024 compared with the previous year. According to ASHE, median apprentice pay for 16-18 year olds in their first year grew by only 4.9 per cent, despite the 21.2 per cent increase in the Apprentice Rate minimum wage over this period

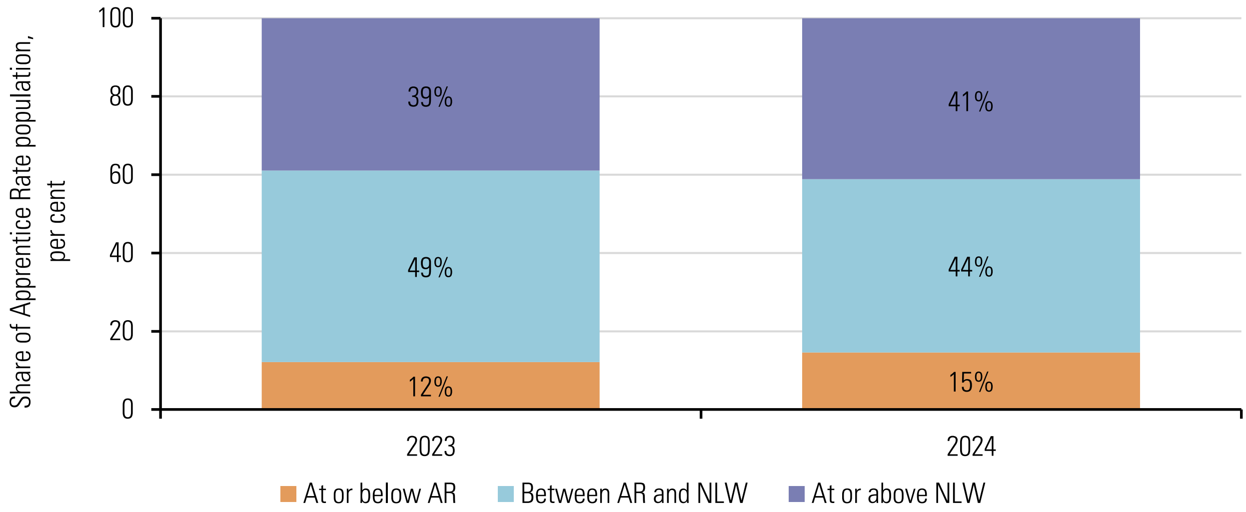
Figure 7.7: Apprentice median hourly wages (LHS) and growth in median hourly pay (RHS), by age and year of apprenticeship, UK, 2024



Source: LPC analysis of ASHE, standard weights, UK, 2019-2024. 16+ population eligible for the Apprentice Rate.

7.30 Although median hourly pay for most groups is well above the Apprentice Rate of £6.40, 15 per cent of the eligible apprentice population earn at or below the Apprentice Rate. As Figure 7.8 shows, though, a large number of apprentices have pay rates between the Apprentice Rate and the NLW, or at the NLW or above.

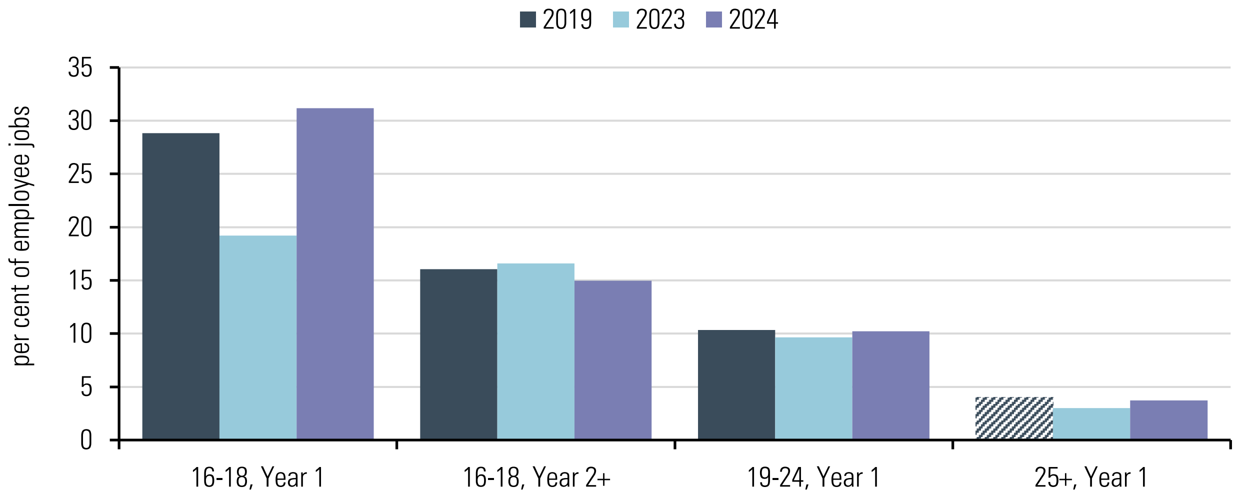
Figure 7.8: Distribution of hourly pay, Apprentice Rate population, UK, 2023-2024



Source: LPC analysis of ASHE, standard weights, UK, 2023-2024. 16+ population eligible for the Apprentice Rate.

7.31 As Figure 7.8 shows, the overall coverage rate rose slightly between 2023 and 2024. Figure 7.9 shows this was driven by a jump in coverage among 16-18 year olds in their first year. Following the large increase in the rate in April, just over three in ten under-19s are paid at the Apprentice Rate, compared with one in ten in the 19-24 age group and less than one in twenty among the 25+ population.

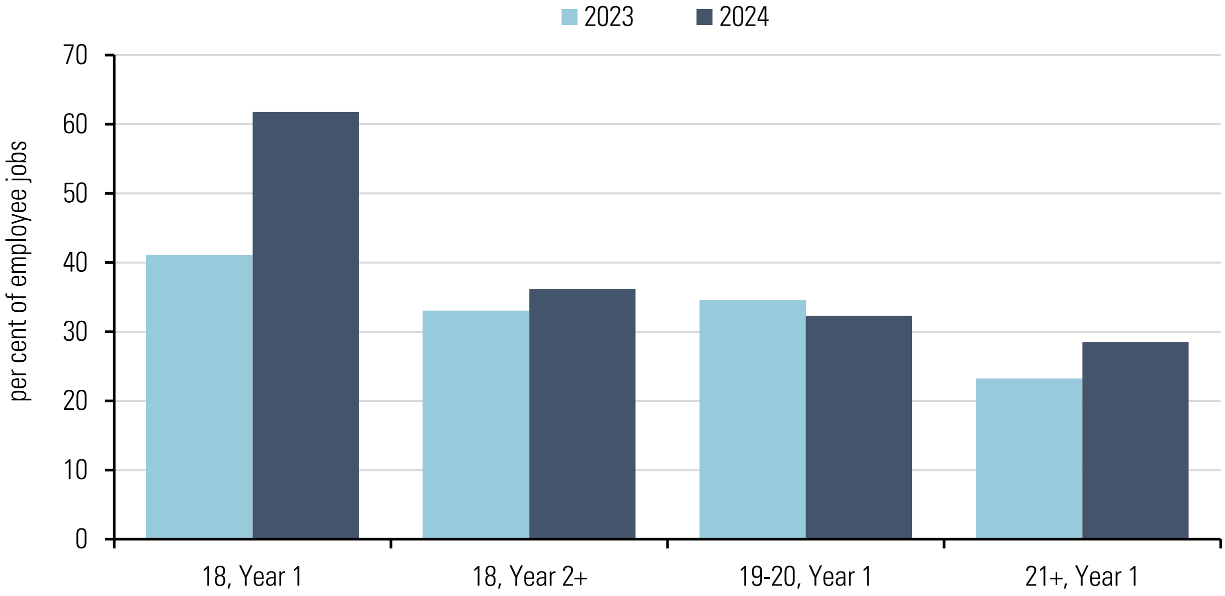
Figure 7.9: Apprentice coverage by age and year of apprenticeship, UK, 2019-2024



Source: LPC analysis of ASHE, low pay weights, UK, 2019-2024. 16+ population eligible for the Apprentice Rate. True value for 25+ first year apprentices in 2019 is suppressed due to insufficient sample size.

7.32 Even if apprentices are not covered by the Apprentice Rate, for those aged 18 or over, employers can still take advantage of the flexibility afforded by the rate's existence by paying less than the relevant NMW rate for their age. (This option is not available for 16-17 year olds, given the alignment of the Apprentice Rate with the 16-17 Year Old Rate.) As Figure 7.10 shows, while real coverage decreases with age, "effective coverage" (that is, the number of apprentices paid between the Apprentice Rate and the relevant NMW rate for their age) is more consistent. Around one in three 19-20 year old apprentices earn less than the 18-20 Year Old Rate, and a similar proportion of the 21+ population earn below the NLW.

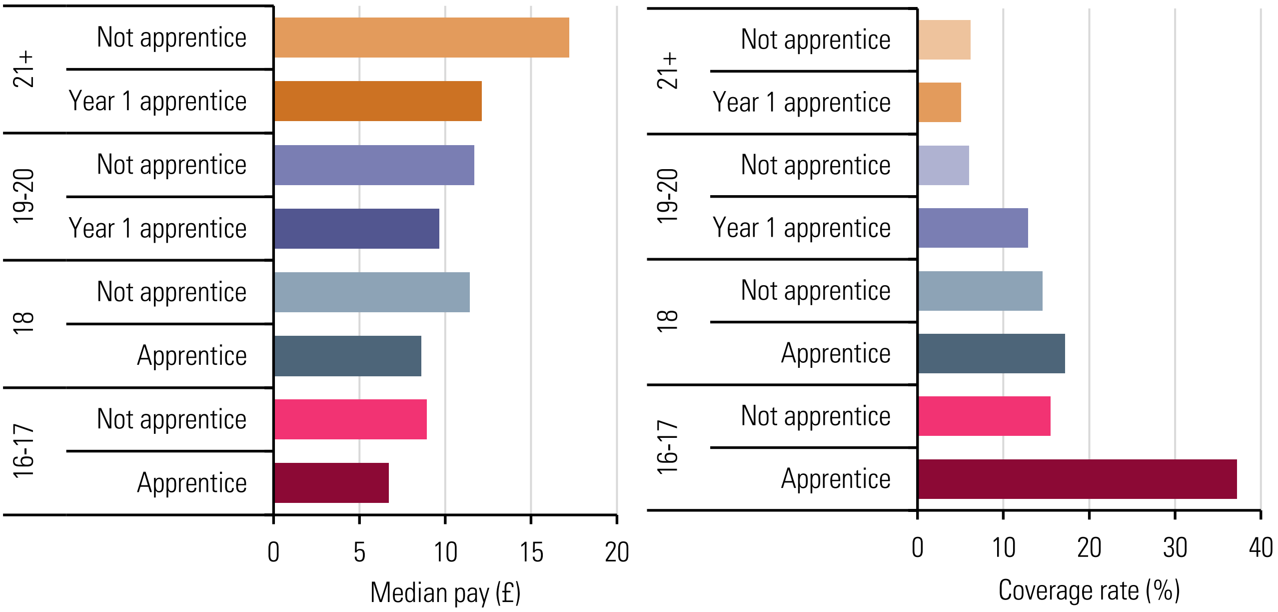
Figure 7.10: Share of apprentices paid below their age-related rate, UK, 2023-2024



Source: LPC analysis of ASHE, low pay weights, UK, 2023-2024. 18+ population eligible for the Apprentice Rate. The age-related rate for 21-22 year olds changes from the 21-22 Year Old Rate in 2023 to the NLW in 2024. The total shares for 21+ incorporate this change.

7.33 This points to the fact that apprentices have lower pay and higher coverage than their non-apprentice peers. Figure 7.11 compares median pay and coverage rates between these two groups, showing the discount apprentices are expected to take. The disparity in the coverage rates of 16-17 year olds is striking, where apprentices were more than twice as likely to be paid at £6.40 than their non-apprentice peers. Many employers we meet tell us they are content to pay apprentices "the rate for the job," the same as non-apprentice staff. Despite this, there is a clear pattern in the data whereby employers expect to pay apprentices less.

Figure 7.11: Median pay (LHS) and coverage rate (RHS) by apprenticeship status and age, UK, 2024



Source: LPC analysis of ASHE, standard weights for median pay and low pay weights for coverage, UK, 2024. 16+ population.

7.34 Overall, this year's ASHE data suggest successive large increases have led to coverage of the Apprentice Rate increasing, in particular for the 16-18 year olds in their first year who have seen relatively weak pay growth.

A number of industries continue to use the Apprentice Rate

7.35 The LGA noted that pay policies varied from council to council across local authorities, with some paying apprentices the Living Wage Foundation's 'real living wage' rates to apprentices while others used the Apprentice Rate. The LGA told us there was anecdotal evidence that more councils local authorities may be using the rate than did so previously to help offer apprenticeship opportunities despite further pressures on their budgets. They told us maintained schools were more likely to use this rate due to their own budgetary pressures and their tendency to favour more apprenticeships at levels 2 and 3. Many authorities base pay on the age, level and experience of an apprentice and whether they are an existing staff member or a new starter.

7.36 Make UK told us that the Apprentice Rate was relatively well used by manufacturers, with one in four employing apprentices on the minimum wage for their age. One manufacturer we met gave us an example of their apprentice pay structure; they used the Apprentice Rate for the first year; in the second year, under 18s would continue at the Apprentice Rate, but managers could approve an increase to £8.60. (Apprentices aged 19 and over would become entitled to the 18-20 Year Old Rate or NLW in their second year.) Apprentices received the NLW in the third year. Existing workers starting an apprenticeship stayed on their existing wage.

7.37 In the National Farmers' Union's (NFU) survey, 30 per cent of respondents who employed an apprentice stated that apprentices were paid at the Apprentice Rate. In EEA's survey, just under half of respondents employed apprentices; the large majority of this group used the Apprentice Rate, with only 5 per cent of the entire sample paying above this.

7.38 The NHBF's survey found that 17 per cent of respondents said changes to the Apprentice Rate would have the most impact on their business. They called for future increases to the rate to "be balanced and supported by government incentives to employers to encourage businesses to keep on and take on new apprentices."

7.39 The Papworth Trust told us they paid apprentices £7.50 in their first year: "We feel this is a fair level and reflects that we do not expect them to be a fully paid member of staff. We also recognise that the role will take them out of the workplace one day a week (at college) and requires intensive training/support from their line managers and supporting team."

7.40 USDAW told us they were aware of the Apprentice Rate being used in non-unionised retail workplaces: "There appear to be no clear pathways for progression in such instances."

Conclusions

7.41 The apprenticeship system appears stable, but there are signs of weakness in the data. Apprenticeship starts around the UK have been consistent with previous years, but vacancies have fallen below their pre-pandemic levels and we do not have data showing the start of the new academic year. Apprentice pay growth has weakened. We often hear that employers are reluctant to pay at the Apprentice Rate, but coverage is high for 16-17 year olds and a significant share of apprentices continue to be paid below the NMW age rate to which they would otherwise be entitled.

7.42 We recommended large changes to the Apprentice Rate in our NMW Beyond 2024 report published in March 2024. Since then, there has been a general election and there are substantial changes to apprenticeships planned. It will be important to consider the detail of these reforms before making decisions on the future of the rate, which for now remains aligned with the 16-17 Year Old Rate.

Chapter 8

Employer responses to the minimum wage

Key findings

- **The most common ways employers adapt to NLW increases are by absorbing it through reduced profits or passing it on via price increases** – These have consistently been the leading responses across multiple employer surveys and this year is no different. There is evidence that recent increases are affecting more employers, though.
- **There are signs that price pass-through has become less common in the past year** – as inflation has eased. Employers in some sectors feel they are reaching the limit of what they can pass through. However, it remains one of the most common responses to minimum wage increases.
- **We estimate that the NLW has only a limited effect on the overall rate of inflation** – Minimum wage workers account for around 3 per cent of the overall wage bill; this figure increases to around 12 per cent when using a generous assumption about the indirect effects of NLW increases through wage spillovers. If the coverage of the NLW increases, the impact on prices is also likely to increase.
- **We hear mixed evidence about the minimum wage's effects on employers' productivity** – We meet employers who have made significant investments to automate processes and save labour; while others argue that NLW increases have squeezed the money available for investment, particularly for small employers. In some sectors employers tell us the productivity options available to them are limited.
- **Some employers are intensifying work by asking staff to worker harder and more flexibly –** Survey evidence finds that attempts to raise productivity in response to the NLW by work intensification are slightly more common than those associated with investment and automation – although this latter group have become more common in the past year.
- **The effects of the rising NLW are particularly acute in a number of sectors which rely on public funding –** Social care is the most prominent among these, but we also heard representations from employers in local government, childcare, leisure and the voluntary sector. In all these areas funding has not increased at the same rate as labour costs, and respondents worried that continuing financial pressure was leading to the erosion of services for users, especially affecting the least well-off.

8.1 This chapter gives an overview of the ways in which employers respond to the rising minimum wage. Chapters 5, 6 and 7 have considered the minimum wage's impacts on employment, pay and the wage distribution. The broad conclusion is that there is little evidence of minimum wage rates affecting employment. This raises the question as to how employers are responding adjusting to the increase in their labour costs. As this chapter shows, employers take a range of options to manage the cost of minimum wage increases. This chapter also looks in depth at the situations of employers and workers in low-paying sectors which rely primarily on public funding: these include local government, social care, childcare, education and leisure and culture. In these sectors, employers face particular constraints in how they can manage minimum wage costs, often with implications for how important public services are delivered.

Overall trends in employer surveys

More firms' wage bills may be affected by the NLW

8.2 Employer representatives told us that the 2024 increase affected a greater share of businesses than previous upratings. The Chartered Institute of Personnel and Development's (CIPD) Labour Market Outlook survey found that the share of businesses affected by the NLW increase had risen. 48 per cent of employers said the uprating had increased their wage bill to some or large extent, compared with 43 per cent in 2023 and 39 per cent in 2022. In total, 64 per cent of respondents stated their wage bill had increased as a result of the uprating. Hospitality was the sector most affected, with 39 per cent of respondents reporting being affected to a large extent, a significantly greater proportion than any other sector.

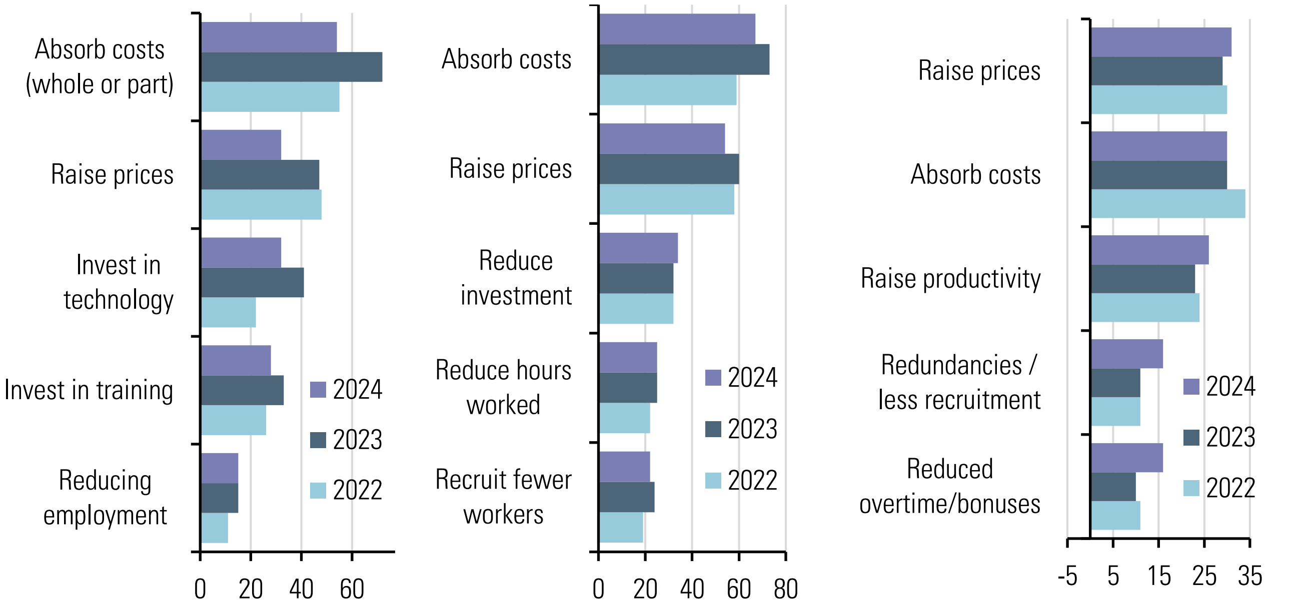
8.3 The Federation of Small Businesses' (FSB) survey found that 16 per cent of respondents were paying all staff less than the 2024 NLW rate of £11.44 before the most recent increase immediately prior to the uprating, the highest such percentage since FSB started regularly surveying on the topic in 2017. 36 per cent of businesses were already paying all employees at or above the incoming NLW rate, compared with 54 per cent in April 2022.

Passing on through prices or absorbing the cost remain the most common responses

8.4 For an overview of how employers respond to minimum wage increases, we use employer surveys, carried out by representative bodies. These reveal a consistent pattern over time, albeit with some variations by group of employers and sector. The most common response is simply to absorb increases via reduced profits. The next is to pass NLW increases on via higher output prices – a response which became much more common with the surge in inflation from 2022 onwards, and which may now have fallen back in the past year.

8.5 Alternatively, employers can adjust to the NLW by making their business more productive, and there are varying ways to achieve this which we discuss below (paras 8.24-8.36). Another way employers adjust to a higher minimum wage is by reducing wage differentials, as discussed in Chapter 5. More rarely, employers might make changes to their non-pay reward package, cut back on training, recruit more young workers or apprentices rather than (more expensive) older workers or change the types of employment contracts they give to workers.

Figure 8.1: Responses to NLW increases among surveyed employers, CBI (left), FSB (centre), CIPD (right), 2022-2024



Source: LPC analysis of surveys by the Confederation of Business and Industry's Employment Trends Survey, 2022, 2023 and 2024; surveys by the Federation of Small Businesses carried out for their submissions to LPC consultations in 2022, 2023 and 2024; and the Chartered Institute of Personnel and Development's Summer Labour Market Outlook surveys, 2022, 2023 and 2024.

Notes:

a. Charts show most common responses rather than all responses. Responses are abbreviated or summarised where necessary. See accompanying data tables for original wording.

b. Responses to the CBI's survey are to the question: 'How has your company already responded to the introduction of the NLW?'

c. Responses to the FSB's survey are to the question: 'You've said that the National Living Wage has increased your organisation's wage bill. How is your organisation managing these additional wage costs?'

d. Responses to the CIPD's surveys are to the question: 'You've said that the National Living Wage and the National Minimum Wage has increased your organisation's wage bill since April 2016. How has your organisation been managing these additional wage costs?'

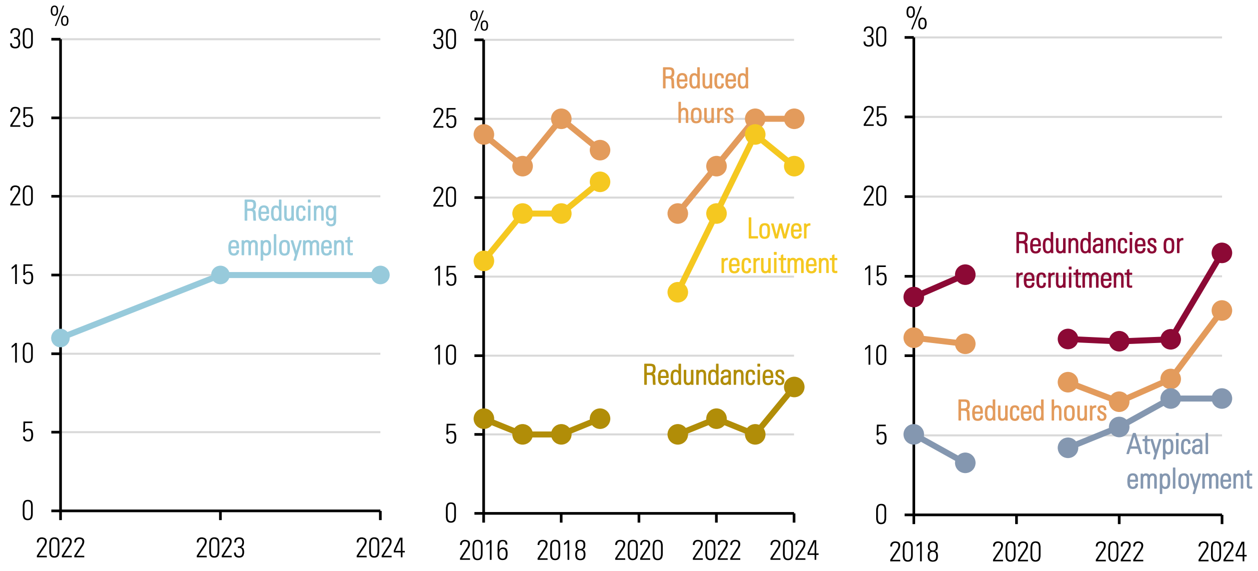
e. In all cases, respondents are able to select multiple responses and so totals will not sum to 100 per cent.

Minorities of employers say they are reducing employment, hours or recruitment, but this share may be growing

8.6 Reductions in employment are relatively less frequent, but some surveys say more employers are doing this in 2024. We used reduced employment to refer to a range of outcomes, including redundancies, reductions in recruitment, reduced hours of work and switches from permanent to atypical employment.

8.7 Figure 8.2 sets out how these responses have appeared in different stakeholder surveys over time. 15 per cent of respondents to the Confederation of British Industry's (CBI) Employment Trends Survey said they had reduced employment in response to NLW increases, the same share as in 2023. In the FSB's survey, 8 per cent of respondents affected by the NLW said they had made redundancies, up from 5 per cent in 2023. It was more common for respondents to say they had reduced recruitment, with 22 per cent saying they had done this (down from 24 per cent in 2023). In the CIPD's survey, 16 per cent of respondents said they had made redundancies or reduced recruitment, up from 11 per cent in 2023. We do not know the relative share of redundancies and slower recruitment within this block. The British Chamber of Commerce's (BCC) survey (not shown) found that 6 per cent of employers surveyed had made redundancies in response to the NLW increase. A survey by UKHospitality (UKH) found that just under 30 per cent of respondents had decreased employment "somewhat" in response to the NLW increase, while an additional 7 per cent had done so "significantly."

Figure 8.2: Prevalence of employment responses among surveyed employers, CBI (left), FSB (centre), CIPD (right), 2018-2024



Source: Source: LPC analysis of surveys by the Confederation of Business and Industry's Employment Trends Survey, 2022, 2023 and 2024; surveys by the Federation of Small Businesses carried out for their submissions to LPC consultations from 2016 to 2024; and the Chartered Institute of Personnel and Development's Summer Labour Market Outlook surveys from 2018 to 2024.

Notes:

a. Responses to the CBI's survey are to the question: 'How has your company already responded to the introduction of the NLW?'
b. Responses to the FSB's survey are to the question: 'You've said that the National Living Wage has increased your organisation's wage bill. How is your organisation managing these additional wage costs?'
c. Responses to the CIPD's surveys are to the question: 'You've said that the National Living Wage and the National Minimum Wage has increased your organisation's wage bill since April 2016. How has your organisation been managing these additional wage costs?'
d. In all cases, respondents are able to select multiple responses.

Raising prices

Passing on NLW increases to consumers by raising output prices was again a leading response

8.8 As set out above, employer survey evidence suggested that the share of employers passing on rising NLW costs via price increases fell slightly this year, while remaining a leading response. More than half of FSB members affected by the NLW (54 per cent) had raised prices, slightly down on 2023 (60 per cent) but above the 2019 figure (45 per cent). In the CBI's survey, those passing NLW costs onto consumers fell from 47 per cent in 2023 to 32 per cent in 2024. Their written submission argued that the NLW "has so far created inflation over productivity".

8.9 The BCC's survey found that 31 per cent of businesses had raised prices in response to the NLW increase, down from 48 per cent in 2022 but it was still the most frequent survey response. Among consumer-facing businesses, the share who had passed the cost through was 47 per cent. The

Federation of Wholesale Distributors (FWD) told us that 55 per cent of their members thought the proposed NLW increase would result in increased prices for consumers. The Early Years Alliance (EYA) reported that eight in ten members planned to increase fees to mitigate the rising NLW, while just over half intend to introduce or increase optional charges such as trips, meals and snacks.

8.10 78 per cent of surveyed British Beer and Pubs Association (BBPA) members had increased their prices in response to the rising NLW. In UKH's survey, over 55 per cent of employers said they had increased their prices "somewhat" in response to the rising NLW, while nearly 23 per cent said they had increased them "significantly."

8.11 Just over half of British Hair Consortium (BHC) members said they would increase prices in response to the NLW, despite fears of losing business to "cheaper business model alternatives." The BHC argued cost increases were accelerating the shift to alternative employment models in the hair and beauty sector: "With consumers unwilling to pay more, the result is often job losses or a shift to non-tax-paying business models." One hair salon owner told us they had increased prices by 7 per cent last year and 5 per cent this year; this had initially led to the salon losing customers, although many had returned after using alternative salons.

8.12 One convenience store owner told us they had covered most of the cost of NLW increases via price increases to goods for home deliveries. This was done via "subtle increases", for example 10 or 15p on the price of cigarettes: "not like putting a pound or anything like that on it … So people won't look at our online menu and go, 'oh god, that's extortionate' … but it's still making an impact."

8.13 Some employer representatives noted that the ability to pass higher costs on through prices varied across the UK, which meant the NLW's effects varied by region. UKH told us the NLW had a greater impact in areas where average spend per head was consistently lower. The BCC's survey found regional variation in responses, with 42 per cent of firms in the Midlands raising their prices compared with 33 per cent in the north of England and 26 per cent in the south. The BHC remarked that "pricing is very much dependent on business geography." NLW increases "in the north is just not sustainable which is why we have seen so many under 21s jobs lost."

Employer representatives across many sectors were concerned about their (in)ability to pass through costs, with consequences for their profits

8.14 Manufacturers were foremost among these: a submission by one manufacturing employer remarked that cost increases could not be passed on due to international competition. The manufacturer's customer base was outside the UK, "with competition predominantly from lower waged economies being India/China." Another large manufacturer described the same situation, whereby international competition, a low inflation environment and fixed price contracts limited their ability to pass through costs. "You're already in a fairly tight margin space, you're competing against competitors mostly sourcing products from the Far East."

8.15 Despite the frequency of pass-through as a response in surveys by UKH and the BBPA, hospitality business owners we met often told us they were unable to pass through costs in full. Employers in Glasgow told us that to preserve their customer base they had only passed on a portion of the higher costs. One hotel owner noted that in the last four years they had only managed to increase sale prices by 6 per cent, while the NLW has gone up 24 per cent: "it should be £10 for a pint - but no one will pay that." One hotel owner told us that, rather than pass on costs, the NLW had led to a tightening of margins. "Payroll's gone up by another couple of per cent compared to our turnover because we haven't been able to increase the turnover pro rata to maintain the payroll percentage that we tried to budget". The increases have "ultimately absorbed our bottom line, our profit."

8.16 Pub owners in Northern Ireland remarked that there had been "a perfect storm of costs combined with a ceiling of achievable sale price". Hospitality businesses were "really struggling with price points", especially in rural areas. One, who ran a rural business, told us that "we can't increase our price point because the guys on the street can't afford it". For example, he felt his pubs couldn't increase the price of a pint of beer beyond £4.50.

8.17 The National Council of Voluntary Organisations (NCVO) told us voluntary organisations had limited scope to put up prices. "Where organisations do have this option, they are mindful not to pass on increased costs to the people they work with, many of whom have low or no incomes." The Community Transport Association told us that without increased funding their members were forced to pass on increases to customers (often vulnerable or excluded individuals) as a "last resort."

8.18 A salon owner from the National Hair and Beauty Federation (NHBF) calculated that "we would have to put up prices 35 per cent to get ourselves in line with what we should be charging … and the consumer of course isn't prepared to pay that just now, especially when they can go down the road or [to a salon using a self-employment, 'chair rental' model] that is already 20 per cent cheaper than me."

8.19 In the National Farmers' Union's (NFU) survey, reduction in profits (89 per cent) was the top impact of the 2024 increase in the NLW, while an increase in prices (50 per cent) was fourth. Around 60 per cent of NFU Scotland members who responded to its survey stated that the increase had caused a significant decrease in profits. "The cost of inputs for farmers have skyrocketed over the last few years". They argued that farmers were price takers, and therefore could not reflect increasing input costs onto the end customer, especially in a situation where supermarkets were giving a two per cent increase on produce, nowhere near sufficient to meet cost increases. Further increases, they told us, unless passed onto supermarkets or consumers, would take labour intensive businesses out of production.

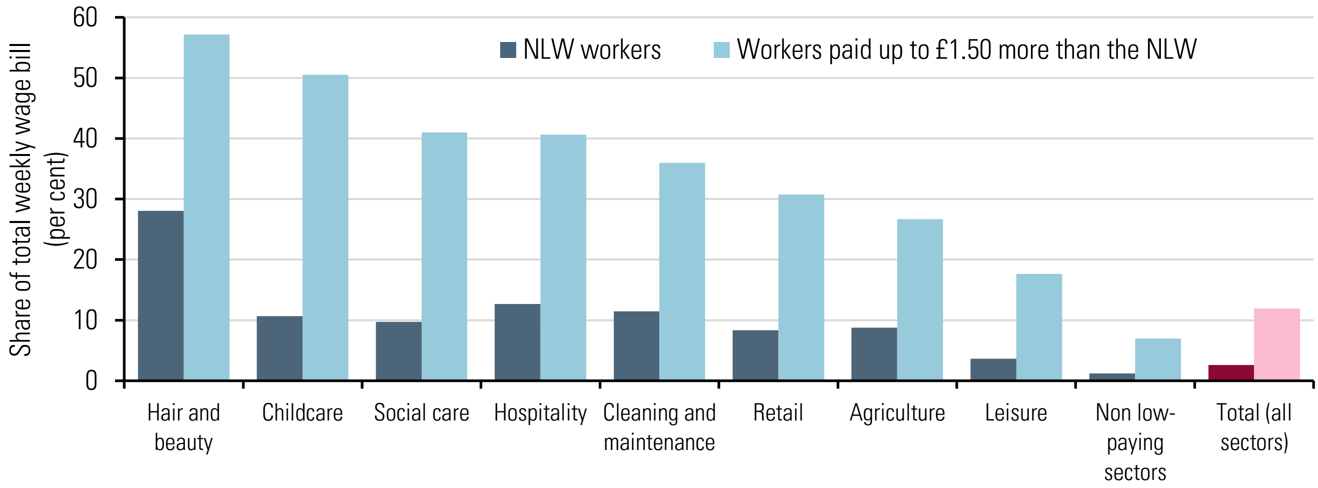
Analysis of price data shows limited impact of the NMW/NLW on headline inflation

8.20 Our analysis suggests that price increases resulting from the NLW have only a small impact on the overall inflation rate. NLW employment makes up around 3 per cent of the UK-wide wage bill, despite covering around 6 per cent of jobs. However, the NLW also has spillovers higher up the wage distribution (Cribb, Giupponi, Joyce, Lindner, Waters, Wernham, and Xu (2021)). Even once we account for equivalent percentage wage increases for all workers paid up to £1.50 above the NLW, the cost of employing NLW workers accounts for only around 12 per cent of the total wage costs faced by employers. As spillovers diminish moving up the pay scale, this is likely an overestimate. For example, hourly wages at the 30th percentile of the wage distribution (£1.37 above the NLW in April 2023) saw a 7.2 percent increase between April 2023 and April 2024, which is less than the 9.8 per cent increase in the NLW.

8.21 The impact of the NLW on headline inflation is also limited by the fact that some items are not domestically produced, and labour is not the only production cost. Following from this, we find that even if all affected firms passed on 100 per cent of the cost of NLW increases and spillovers of up to £1.50 – an improbable scenario – a 10 per cent increase in the NLW could increase the CPI inflation rate by up to 0.3 percentage points. This means that the upper bound of our estimates, under the most generous assumptions, is a 0.3 percentage points increase in the inflation rate. The true value is likely to be much lower and will depend on a number of factors, including changes in the coverage of the NLW and underlying wage growth in the absence of the NLW.

8.22 However, Figure 8.3 shows that the NLW wage bill varies significantly between sectors. In non-low paying sectors, NLW workers account for only one per cent of employers' wage bills on average, but 28 per cent in hair and beauty. This means that the NLW may be more likely to raise prices in these sectors – for example, the price of a haircut or nursery fees – than in other sectors. However, even if firms are highly affected by the NLW, they may not be able to increase prices if their customers are particularly price sensitive.

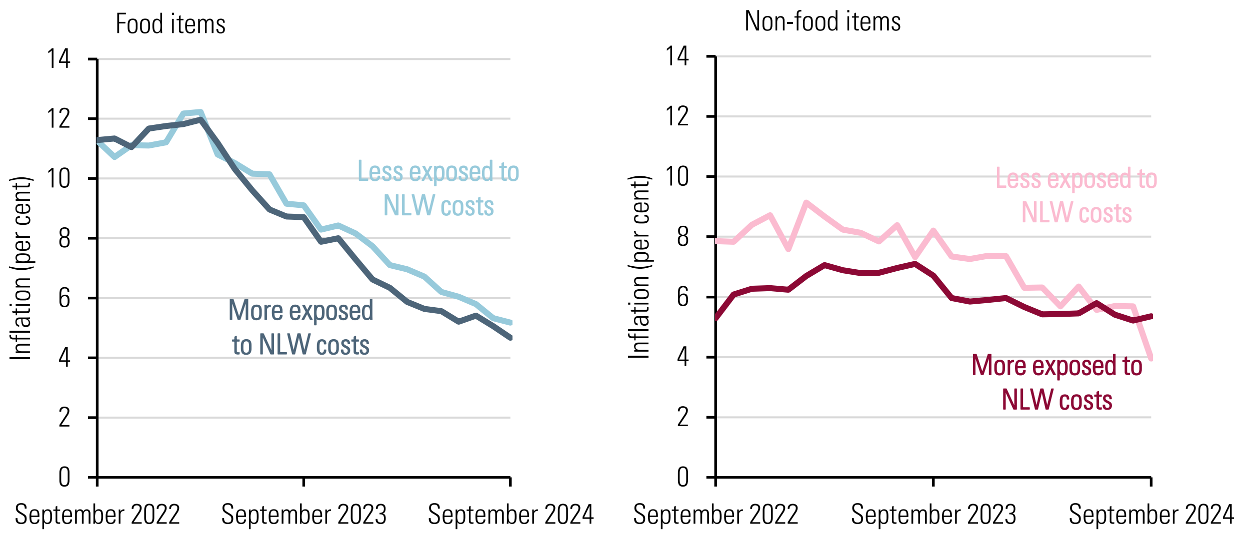
Figure 8.3: Share of wage bill for NLW jobs and jobs paid within £1.50 of NLW by low-paying industry, UK, 2024



Source: LPC analysis of ASHE, low pay weights, UK, 2024. 21+ population, excluding those eligible for the Apprentice Rate. Not all low-paying industries are shown.

8.23 Previous research we commissioned on the inflationary impacts of the NLW (Wilson, 2020) suggests that, even in those sectors most affected by the NLW, firms typically pass on only a small share of any NLW increase through higher prices. This is echoed when we compare price increases for goods and services where the NLW makes up a large share of the costs ('more exposed to the NLW') to those where it makes up a lower share of costs ('less exposed to the NLW'). Figure 8.4 shows that inflation was similar for items more exposed to the NLW between 2022 and 2024. However, this compares a diverse range of products, and so may reflect an imbalance in the cost of other inputs, such as energy, between more and less exposed items, rather than the absence of an impact from increased NLW costs.

Figure 8.4: Annual inflation of food and non-food items by exposure to the minimum wage, UK, 2022-2024



Source: LPC analysis of ONS price microdata, CPI weights, UK, September 2022 – September 2024. Non-tradeable items only. List of sectors and goods/services most exposed to the minimum wage is taken from Wilson (2020). Items with missing observations over the period are excluded, so additions to the CPI basket of goods are not considered. Only non-tradeable items that can be mapped to sectors and prices that can be mapped to regions are considered, so the CPI weighted average of items considered does not equal headline CPI.

Productivity and investment

8.24 One of the ways that firms try to respond to minimum wage increases is by improving productivity. This could take the form of increased investment in technology and automation that makes workers more productive, improved training to improve workers' skills, or by developing new products and services. While many firms note that NLW increases had incentivised new investment, others claim that higher labour costs limit their budget for investment. At an aggregate level, previous analysis we have done provides no evidence that the NLW has improved or worsened economy-wide productivity (Latimer, 2022).

8.25 The best overview of employers' productivity responses comes from the CIPD's Labour Market Outlook survey. Figure 8.5 compares their 2023 and 2024 results when asking employers how they had improved productivity in response to the NLW. The most common responses are general ones, improving productivity via seeking to improve "staff morale and motivations" and "improved general practice" e.g. quality control, supply-chain management, monitoring of business processes. Just under a quarter of respondents indicate that they have not taken actions to improve productivity.

Some employers are intensifying work by asking staff to work harder or more flexibly in response to the NLW

8.26 The next most common responses involve intensification of work and greater expectations of flexibility among staff. A quarter of respondents affected by the NLW in 2024 said they were allocating staff more tasks, 19 per cent that they were demanding a higher pace of work and 18 per cent that they were requiring more flexibility from staff in their hours of work. The share of respondents investing in automation and technology is lower than those asking staff to work harder, but both categories grew this year. The falls in employers increasing training or recruiting more skilled workers are small but notable.

8.27 Intensification was a feature of other stakeholder responses. The CBI said that hospitality firms have told them that "*the only available to way to increase the productivity of waiters is to ensure they wait more tables – something that is generally only possible through placing greater demands on them within the confines of health and safety considerations.*" Likewise, the BRC said *"working harder remained one of the key actions retailers have taken and plan to take in response to increases".*

Figure 8.5: CIPD findings on employer actions to improve productivity in response to the NLW, 2023 and 2024

Source: LPC analysis of the CIPD's summer Labour Market Outlook survey, 2023 and 2024.
Note: Employers are asked to identify 'Actions taken to improve productivity in response to NLW increases.' Base is all firms affected by NLW increases. The response on Generative AI was not in the survey in 2023, hence the zero figure for that year.

Unions are also concerned about work intensification, and believe recruitment difficulties or short staffing are the cause

8.28 Unite told us "Our 2024 survey of hospitality workers earning the minimum wage reveals concerns over work intensification resulting from deliberate short-staffing. Work intensification is also an issue commonly cited by our officers with some reporting that with each increase (in NMW/NLW) they are seeing less staff being recruited leading to additional pressures at work for existing workers." Usdaw's response showed how technology is used to intensify work: "The increasing use of technology, data surveillance and AI continues to have a marked impact on retail job roles…. alongside decreasing store headcounts in some places. Workers are now routinely expected to manage several tills at once, including ID checks, removing security tags and minimising thefts whilst prioritising service, alongside other duties…. A recurring theme from our members is the sense of injustice that they are working harder and doing more, whilst seeing their wages becoming less and less valuable."

Large and small firms differ in how they respond to the NLW

8.29 There are clear differences between the approaches of large and small employers in the CIPD's survey. Around 32 per cent of employers with fewer than 250 employees said they had not tried to increase productivity in response to the NLW, compared with 20 per cent of larger firms. Larger firms are more likely to have tried nearly every productivity-enhancing option more than smaller ones. The gap is widest when it comes to automation and investment. Around a quarter of larger firms said they had automated tasks or invested in machinery, equipment or technology, compared with only 10 per cent of smaller firms.

A range of employer representatives told us the NLW was a factor in low or declining investment

8.30 Several employers and representative bodies told us the rising NLW had led to reduced investment. The CBI told us that increases were squeezing the money available for this: "investment in alternatives to labour provides a route out of this catch-22 [i.e. labour shortages] for some but requires relief from the high labour costs squeezing budgets." The constraints created on investment, the CBI argued, made work intensification more likely: employers "have a need to get more from workers – if they don't have a way to do it, it just materialises as more pressure to do more."

8.31 The share of FSB members reducing investment in their surveys has risen steadily. More than a quarter of 2024 respondents said they had reduced investment in response to NLW increases, up from 10 per cent in 2021. As well as costs, they argued that information constraints and a lack of expertise could be obstacles to automation. The Association of Convenience Stores (ACS) told us that half of survey respondents said the latest uprating would result in reduced investment, up from 33 per cent in 2022.

8.32 The NFU reported that reductions in investment were the second most common (66 per cent) result of the rising NLW. The Horticultural Trade Association (HTA) noted that cost rises meant less money left for investment – "wider input cost increases have built over recent months and years, leading to a reduction in the ability to invest in technology, compounded impacts of hikes in global trade costs and border impacts, and ability to invest in the transition to peat-free." The Federation of Wholesale Distributors told us that half of their members stated that the proposed NLW increase would have a negative impact on investment.

8.33 Hospitality employers tended to tell us that automation was challenging due to customers' expectations of service levels. In the CIPD's survey, only 5 per cent of respondents in the hospitality sector had invested in technology or equipment while 11 per cent had automated tasks. A manager at one large hotel chain told us that although they were "very keen to look at automation and technology and find ways where we can try and minimize [labour costs] … the reality is our hotels are four-star full-service hotels. People that come here, they want they want that engagement with people."

8.34 Hotels told us that a tight labour market for skilled staff was also a drag on productivity. Brexit and the end of freedom of movement had cut hotels off from skilled labour. As a result, they were employing more lower-skilled workers; headcounts had risen and productivity was down. One hotel owner summarised for us: "we used to run the hotel with 35 people, we now probably have closer to 50 people in one hotel … The payroll is probably 30 per cent more than before, but the turnover is probably only about 15 per cent more than before."

Some employers had increased investment to improve automation and productivity

8.35 A number of employers and employer representatives in the retail sector told us they had invested in additional resources. The British Retail Consortium (BRC) told us the NLW and the rising cost of employment continued to contribute to a shift towards technology adoption and automation in some parts of the retail industry. Around two-thirds of respondents (68 per cent) indicated they had already invested in technology to increase automation as a result of the NLW – the leading response in the BRC's survey.

8.36 One large manufacturer told us that, as a result of NLW increases, they "have had to automate the factory extensively", reducing headcount in their business. "We're putting millions frankly into automation to reduce the labour content … Anything that's voluminous and repetitive we're looking at getting rid of." Over 28 per cent of manufacturers from Make UK indicated a focus on productivity improvements, with many investing in automation to offset the costs associated with higher wages for lower-paid staff. This had contributed to maintaining profit margins despite the wage increases. Around 36 per cent of Food and Drink Federation (FDF) survey respondents reported an uptake of automation to tackle labour shortages.

Evidence on publicly funded sectors

8.37 A large share of the evidence we hear each year comes from low-paying sectors which are to varying extents reliant on public funding. These sectors are often constrained in their ability to absorb the NLW in profits or pass on higher costs via price increases. This section considers evidence we have heard on the pressures created by the NLW in these sectors and its consequences for employers, workers and the delivery of services.

Social care continues to face a critical funding squeeze

8.38 Social care is a large sector with heavy use of the minimum wage. Skills for Care estimated that this April's NLW increase directly affected around 760,000 care sector roles and that around 60 per cent of workers in the sector were paid less than the incoming rate of £11.44. They noted that many of the remaining 40 per cent of posts would also receive a pay rise to maintain differentials. As of December 2023, they estimated around 94 per cent of adult social care providers in the independent sector were paying at least some of their workers below £11.44.

Funding remains the critical issue in the care sector

8.39 The National Care Forum (NCF) outlined the cumulative pressures faced by the sector: "more generous one-off local government uplifts or grants from government are unable to make a dent in the funding gap providers are faced with following years of underfunding." This funding gap contributes to an estimated 36 per cent pay gap between care workers and their NHS counterparts, and leads to high vacancy levels and declining availability of care.

8.40 Care England told us that the average fee rates paid by local authorities had increased by circa 6 per cent; however, this may not necessarily reflect the average uplift which providers had received, with many reporting minimal, if any, uplifts. The Home Care Association (HCA) described local authorities commissioning homecare for rates as low as £14 per hour – less than half the HCA's published minimum sustainable rate of £28.53. A 2023 FOI request asked commissioners of homecare for hourly fee rates and found only 5 per cent paying the calculated minimum price. Unison described poor quality commissioning practices as "an elephant in the room" when it comes to non-compliance in care, with the potential to "increase the likelihood of care workers being paid below the NMW."

8.41 The Association of Directors of Adult Social Services (ADASS) noted the NLW was consistently in the top five greatest concerns for councils in terms of financial pressures. They estimated that the April 2023 NLW increase cost councils approximately £1.02bn in direct costs (council run services), and £774m in indirect costs (independent sector provision purchased by councils), representing approximately a third of upward cost pressures for councils in 2023/24. Increases to the NLW, they argued, should be accompanied by support for councils to meet the additional costs, otherwise there would be adverse consequences for care services and people with care needs.

8.42 We heard several examples of the funding squeeze leading care providers to cross-subsidise publicly and privately funded parts of their service. One large care provider told us they were passing increased wage costs onto residents but "did not receive a single complaint" as clients understood the effects of inflation. One care homeowner told us they were subsidising a home in a less affluent area (nearly all publicly funded) from others in wealthier parts of the county (not publicly funded) and other businesses. His costs had increased by 5.4 per cent last year, but local authority fees had increased by only 4 per cent; his private fees had increased by 9 per cent to cover the shortfall.

8.43 Despite funding shortfalls, some providers can make substantial profits. At oral evidence, Unison said "the kinds of profit-taking that we've seen … we find hugely problematic … the way in which some of the big players in social care have used tax havens or taken massive profits out of the sector." They recognise "it's a very fragmented sector … we don't want to disregard those who are struggling. But the big players are making quite a lot of money[14]." GMB described seeing "lots of financial engineering" and confusing corporate structures in care: "we don't know who to go to for bargaining … You don't even know who your own employer is."

Recruitment and retention remain significant challenges in the care sector

8.44 Various respondents discussed the care sector's high vacancy rate. The HCA described recruitment as a key challenge, with 'low fee areas' facing more difficulties and changes to immigration policy threatening an important route into the sector. Recruitment challenges, Care England argued,

[14] To back up this point, Unison shared reports with us from Warwick Business School, the Centre for Health and the Public Interest, the Centre for International Corporate Tax Accountability and Research, and the Centre for Understanding of Sustainable Prosperity. Published between 2019 and 2023, the six reports shared look at evidence on profitability and ownership structures in the social care sector.

would persist until the sector could match the pay of competitors including the NHS, retail and hospitality. ADASS argued that significant staff shortages worsened the quality and choice of care: their 2023 survey found that "Between January and March 2023, 564,584 homecare hours could not be delivered due to lack of staff."

8.45 Comparisons were frequently made with employment in the NHS. Care England complained about the lack of clear pay scales for staff to progress and lamented that Department of Health and Social Care's (DHSC) proposed £500m investment to create new training routes (announced in April 2022) had been cut in half (in a white paper published in April 2023). The NCF noted the very low pay premium received by experienced care workers, referencing Skills for Care findings that "on average, care workers with five year's (or more) experience in the sector are only paid 7p per hour more than a care worker with less than one year experience." The Royal Mencap Society argued that starting wages in care should at a minimum be equivalent to NHS band 3 roles. Separately we heard from Unison members in Wales that many care workers looking after patients at home carried out many more duties than their NHS equivalents for far less pay.

8.46 The NCF told that the restrictions on the Health and Care visa since 2023 (in particular the ban on dependents joining workers) threatened to cut off a source of labour care employers relied on. They argued the result would be "a serious contraction in the number of care workers and …the services available to people over the next few years." ADASS suggested the Government's modelling underestimated the effects of these changes: the Government had modelled a 22 per cent reduction in care and senior care worker oversees arrivals, equating to 20,000 fewer overseas workers, whereas applications for the relevant visa had actually dropped by 76 per cent between Jan-April 2023 and Jan-April 2024. HCA members on the Glasgow visit summed up the situation: "we're dying of thirst up here while someone's turning off the tap down there."

Work in care is insecure with variable hours and poor working conditions contributing to high staff turnover

8.47 Unions and employers alike shared evidence on the nature of work in social care and how it was affected by the wider issues in the sector. Working hours and flexibility were central to this. HCA noted that 2022/23 Skills for Care estimates showed 23 per cent of the adult social care workforce were on zero hours contracts. A Unison survey found that three-quarters of care workers said their hours varied from week to week, with 77 per cent saying they'd take more hours if they could get them.

8.48 For Unison, poor employment conditions were associated with higher turnover. They referenced Living Wage Foundation findings that "around one in seven insecure jobs in the UK are in the health and social care sector." They used Skills for Care data showing that "Where care workers were paid more than the minimum wage, were not on a zero-hours contract, were able to work full time, had access to training and held a relevant qualification, the turnover rate was less than half that of staff where none of the five factors applied." GMB pointed to Skills for Care data showing care workers with better employment conditions were more likely to remain in their jobs. ADASS cited evidence (Allan and Vadean, 2023) showing that higher wages were "positively associated with improved outcomes for people drawing on care in long-term residential settings."

8.49 The WRC noted the general inadequacy of wages for workers: "In our experience many migrant care workers opt to work for the additional 20 hours a week that is permitted under the HCW (Health and Care Worker) visa to supplement their income, and many often need their partner's income to match the cost of living in the UK." The WRC's submission similarly found a widespread lack of stability "owing to constant shifting of rotas." They also reported that "bullying and harassment were noted as a frequent occurrence, with migrant workers being on the receiving end of verbal abuse and shouting, belittling conduct and even racism." In general, they found that "workers preferred to have a contract with fixed hours, allowing them to plan their personal and working arrangements ahead of time."

8.50 Several respondents reflected on experience with the "real living wage" in care. The submission from Public Health Wales stated that social workers have likely benefited from the implementation of the Living Wage Foundation's "real living wage" in social care by the Welsh Government, with an independent evaluation of outcomes underway. Care workers we met in Cardiff complained the additional money Welsh government provided to councils and employers to boost hourly pay to the level of the real living wage, had not been passed on to all care workers and some said they had yet to receive any uplift, although Unison officials noted that a new commissioning framework would make it easier for councils to ensure providers were complying. Royal Mencap Society called for this to be extended to colleagues in England and Northern Ireland; currently some local authority contracts were funded solely to meet the NLW while others enabled them to pay higher. One London-based provider told us the decision to pay the London Living Wage (LLW) had not made a difference to recruitment or retention, and that even though staff received the LLW, they were still desperate to get overtime hours: "we're not dropping behind, but we're running to stand still."

Migrant care workers are at particular risk of exploitation

8.51 WRC's submission set out evidence that migrant workers on the Health and Care Visa faced a number of forms of exploitation. WRC identified the most common issues as the payment of illegal recruitment fees, the enforcement of repayment clauses if a worker left an employer and issues around payment of travel time and fuel allowance. Recruitment fees, they argued, effectively created conditions of debt bondage for some care workers. Although repayment clauses are legal, their use should conform with a code of practice and workers' only recourse against their improper use is via an Employment Tribunal. A lack of pay for travel time "can mean that migrant workers can spend the whole day 'working', but only receive a few hours of pay due to limited contact time with clients. For example, one respondent noted that they could only earn around £30 on a 'bad day' where travel reduces contact time with clients."

8.52 A group of migrant care workers told us that new arrivals to the UK were being charged excessive visa and sponsorship fees, both by the intermediary agencies who recruit them and their employers in the UK. Workers alleged that sponsoring companies then failed to provide them with the full-time work specified in their contract of employment. The workers we spoke to struggled to earn a liveable wage, and certainly earned less than they had expected to when travelling to the UK. They were unable to move to another employer because of the difficulty of finding a new sponsor under the Health and Care Visa. Although it is impossible to know how representative a single meeting with workers is, the WRC told us that they were contacted by several dozen workers in the first half of 2024 alleging they had been provided less than contractual or no hours by their visa sponsor. Unison officials in Cardiff also told us they were receiving more requests for representation from migrant workers, who were often unaware of their rights.

8.53 Migrant workers in the domiciliary care sector also faced more familiar problems with the non-payment of travel time by their employers. One estimated that he earned just £8 per hour once time spent driving between appointments was accounted for. The issue of underpayment related to care workers' travel time has been widely reported in the past and is discussed in Chapter 9 of this report.

Several stakeholders called for action on sleep-ins and investment in care more generally

8.54 Several submissions called specifically for action on the continuing problems associated with pay for sleep-in shifts. These are shifts, common in the care sector, where workers are expected to remain on premises overnight; while they may sleep, they are expected to make themselves available to work should they be needed. Workers on these shifts are not currently entitled to the minimum wage, following the Supreme Court's 2021 ruling in the case of Royal Mencap Society v Tomlinson-Blake. Unison called on Government to "remedy the injustice that sleep-in care workers have been experiencing for years and deliver meaningful legislative reform on this issue." They asked the LPC to "[add] its voice to the need for adequately funded legislative reform on the issue of sleep-in shifts as loudly and forcibly as possible." Professor Deirdre McCann of Durham University argued the treatment of these shifts "remains a significant challenge to decent work." She recommended the LPC call for urgent legislative reform to give workers entitlement to the NMW for all working hours in sleep-in shifts. "This principle is essential to a sustainable social care system and, more broadly, ensures a coherent and universal legal framework of worker protection." We collected a few examples of how employers treated sleep-in shifts, which reinforced the diversity of practices in this area. A Unite rep based in Northern Ireland cited a case of adult care workers being paid £6 per hour to cover overnight shifts. On the Dover visit, one care provider told us they paid £80 a night for sleepovers.

8.55 We feel that this long-standing issue merits a fundamental review. **We recommend that the Government ensures the question of sleep-in shifts' entitlement to the minimum wage is addressed in the planned Fair Pay Agreement for the social care sector.**

The NLW and increased service demands are pushing local councils into a funding crisis

8.56 The funding crisis in social care itself stems from funding issues faced by local government. In their written evidence, the Local Government Association (LGA) told us that councils had been given access to an additional £3.6 billion in core spending power (which includes council tax rises) in 2024/25, of which an estimated £1.6 billion would go solely to fund cost increases in commissioned adult social care due to the NLW increase. At the same time, we heard councils were facing substantial increases in demand across a range of service areas. LGA estimated that by 2024/25 cost and demand pressures will have added £15 billion (or 28.6 per cent) to the cost of delivering council services since 2021/22. Key areas of financial pressure include both children's and adults' social care, escalating costs of home to school transport for children with special educational needs and disabilities and increasing costs of homelessness services.

8.57 In addition, the increase in the NLW to £11.44 had placed upward pressure on local government pay spines, requiring adjustments to maintain differentials and competitiveness. The LGA estimated that the 2024 pay negotiations would leave little space between the lowest pay point and the NLW. The final offer to trade unions from the National Employers for local government amounted to a 4.03 per cent increase to the national pay bill with a cash equivalent cost of over £730 million, which would take the lowest pay point to £12.26 per hour. The likely forecast for the NLW in April 2025 was key to the National Employers' deliberations.

8.58 The LGA told us financial pressures from recent pay decisions would lead to job losses and reduced services. They argued that substantial skills shortages across local government were, in part, caused in part by the need to cover NLW costs: "there are areas providing much needed services to the public or ensuring proper governance that are functioning while one in four roles are vacant…this is the indirect consequence of funding having to be directed at the NLW and not at other areas of need." They gave examples of key areas of difficulty, including children's social workers, environmental health officers, building control and housing officers and planning officers. They stated "with certainty that without additional funding for employers in sectors covered by the LGA, implementing the increases in NLW in 2025 will lead to job losses and/or service reductions due to issues of affordability."

Childcare providers warned that rising wage costs, recruitment struggles, and higher fees risked deepening inequalities in access

8.59 The picture painted by childcare organisations was again comparable to social care; a tight funding settlement meant providers struggled to absorb NLW increases and had limited scope to pass these on. (Childcare providers are required to offer a set amount of free hours to parents, which the Government ultimately funds at a fixed rate.) This, combined with other stress factors, created recruitment and retention problems and ultimately threatened the provision of services.

8.60 Both the Early Years Alliance (EYA) and the National Day Nurseries Association (NDNA) estimated the proportion of NLW workers in the sector at around 60 per cent. With wages accounting for around three-quarters of provider costs, EYA told us the increase of the NLW to £11.44 had significantly affected early years providers. In their member surveys, 86 per cent of nurseries and pre-schools said the April 2024 increase would have a 'somewhat negative' (28 per cent) or 'very negative' (58 per cent) impact on their setting finances. Of those, eight in ten planned to increase fees to mitigate this, while just over half intended to introduce or increase optional charges such as trips, meals and snacks. The NDNA told us their members' wage bills had risen by an average of 14 per cent following the recent increase, while the average fee increase for parents had been 8.5 per cent.

8.61 Both bodies agreed current levels of pay in the sector were too low and this had an impact on recruitment. EYA gave an example from their own organisation of a teaching post remaining vacant for eight months. Their surveys had found that 84 per cent of settings found it difficult to recruit suitable staff. Low pay and undervaluation are primary causes, affecting accessibility and availability of early years providers.

8.62 EYA argued that the childcare sector would remain vulnerable without additional help from the government. They foresaw an increasing divide between more and less affluent areas, with the sustainability of settings in the latter areas in doubt as families would be hesitant to pay for extra hours above the free limit.

The voluntary sector is seeing the impacts of constrained funding

8.63 Shedding light on an area we receive relatively little evidence from, a joint submission from the National Council of Voluntary Organisations (NCVO) and the Community Transport Association (CTA) set out how public funding to the voluntary sector was failing to keep pace with the NLW. With Government providing 30 per cent of the voluntary sector's income, NCVO and CTA report that the cost of the minimum wage increasingly had to be met from charitable rather than public funding. "It is unacceptable for public bodies to not, as a bare minimum, ensure that their grants and contracts meet the cost of paying the minimum wage." The respondents reported that members from a wide range of subsectors were finding it more difficult to pay the NLW because of underfunding: "Low pay is driven in part by a competitive approach to commissioning public services, which prioritises low cost over quality and seeks to drive down cost year-on-year."

8.64 NCVO and CTA noted the Government's estimate in its impact assessments that the 2024 NLW increase would cost the voluntary sector at least £200m over the next six years. They argued this estimate was too low, and shared estimates from four large charities that the increase would cost them an additional £14m this financial year. Other charities, they reported, estimated the costs from the increase to represent between 2 and 5 per cent of their annual income.

8.65 NCVO and CTA stated that voluntary organisations had limited scope to put up prices: "Where organisations do have this option, they are mindful not to pass on increased costs to the people they work with, many of whom have low or no incomes." Community transport organisations without increased funding may be forced to pass on increases to customers (often vulnerable or excluded individuals) as a "last resort." As a result of this funding gap, the NCVO gave examples of charities cutting services, staff and hours of work to afford NLW increases.

Education

8.66 This year, we received more evidence on low-paid work in the education sector than in previous years, meeting with workers in Further Education (FE) colleges, school support staff and university staff. For staff In FE colleges, the differential from the wage premium above the NLW had been eroded and they were struggling to get by: "You can't survive on what we're getting, I think, and live at the same time – you have to have other circumstances around you to be able to do that." Similarly, we heard from Unite members that the lowest-paid workers at one university earned approximately £12 per hour. The university, they told us "still [has] workers who are using food banks" and "choosing between heating their homes and eating".

8.67 School support staff told us pay was low and there was little opportunity for progression. GMB estimated the average annual salary for teaching assistants was just £15,476 in 2023. One participant thought her pay was around the minimum wage; another was on a higher pay band (around £1400 monthly) but noted that staff were employed on term-time contracts, so their gross pay was generally lower than the headline (hourly) rate would make it seem. GMB's written evidence argued that low pay among school support staff was an under-recognised problem.

8.68 Staff in all these areas felt undervalued, especially relative to their level of responsibility. One FE worker complained that his learning support role was "pivotal," but that wasn't recognised by senior management. GMB's written evidence argued that staff looking after vulnerable and disadvantaged children "do it without training … without standards of pay that reflect the responsibility, duty of care, and professionalism that we must display in schools every day". They quoted one member: "I hear daily stories from GMB members who are beyond despair, working in unsafe environments for both children and staff. They are consistently asked to take on more and more work for no more pay and offered no opportunities for the future." Recognition and respect were important asks from school support staff.

Community leisure providers warned of service cutbacks, higher prices and a weakening of their charitable mission

8.69 The community leisure sector, largely reliant on local authority funding and made up of charitable and not-for-profit providers, reported similar concerns to counterparts in the voluntary and care sectors. Community Leisure UK (CLUK) told us the outlook for public sector organisations dependent on local government support was very uncertain and likely to get tougher. Two-thirds of councils, they told us, had warned of cutbacks to local neighbourhood services including leisure. In a survey, over half of their members stated the NLW had impacted profits in the last year, and reduced profits meant reduced investment to improve services. Wage costs also had a direct impact on prices, although this conflicted with leisure trusts' general aim to remain affordable and accessible, and some members believed they were nearing a tipping point where increased prices would result in customers stopping using services and cancelling memberships.

8.70 Leisure trusts also worried about the impact funding constraints were having on their charitable mission. The leader of one trust in the North West shared concerns that financial pressure, including from the NLW, was diluting leisure trusts' charitable reach, by forcing them to look hard at what services they can offer. "We're a lot more brutal on individual areas of the business – anything that doesn't wash its face, we can't do it anymore." This had led to a gradual eroding of charitable outcomes. Another trust reflected they felt under pressure to provide more "value added" activities such as swimming lessons that they could charge for – "but those aren't the services we want to provide and they don't reflect our charitable objectives."

Unions argue that public sector outsourcing is closely linked to low pay

8.71 Unison's submission argued that low pay in the public sector was closely linked to the privatisation and subcontracting of public services. They pointed to social care as the most salient example of this, citing Skills for Care data on employment, pay and working conditions in the sector. GMB discussed their recent experience of campaigning for "insourcing" in NHS hospitals, where their members had campaigned "to be valued in the same way as direct NHS employees." They gave the example of one hospital where outsourced cleaners had been excluded from a Covid bonus given to other staff. GMB challenged this and won the right to have a restorative pay award. They stated that "companies will wait and wait until we have to get members out on strike … often because parent companies aren't providing money – they see companies as revenue generators."

8.72 GMB's submission also discussed the situation of security staff employed by outsourcing companies in Job Centres run by the Department for Work and Pensions, whose pay differential above the NLW had fallen over time, with supervisors now receiving a differential of just 1p above the NLW. GMB argued that the large multinational employers in this sector "do not take their obligations seriously to adequately pay these workers for the skilled and dangerous jobs they do in service of the public" and that the job was becoming "deskilled" as a result. GMB's analysis showed "security guards and related workers were £1.40 an hour worse off in real terms in 2023 than they were nearly twenty years prior (a real terms cut of over 11 per cent)." Low pay, they argued, was a leading barrier to recruitment and retention in the sector and GMB members working at Job Centres were preparing to take strike action.

8.73 RMT's submission reflected on low-paid outsourced workers in the rail sector. Low pay, they told us, principally affects rail workers in outsourced "ancillary" services such as "cleaning, catering, security and some station staff roles like 'gateline' workers." RMT estimated there could be as many as 10,000 such workers, often on precarious contracts and with a very low level of sick pay and pension entitlement. An RMT survey of outsourced cleaners found 80 per cent saying they sometimes or regularly struggle to make ends meet and 90 per cent worried about paying their bills every month. They gave an example of a contract offered by one rail company to "gateline" workers, which guarantees only 336[15] hours per year (or six per week), whereas in reality staff work up to 60 hours per week.

Conclusions

8.74 The evidence suggests that employers adapt to the increase in the NLW by covering the extra costs from their profits or passing it on via higher prices rather than reducing employment. Despite the prevalence of price pass-through, we estimate that the NLW has only a limited effect on the overall rate of inflation. Employer surveys suggest that more employers were affected by last April's uprating than in previous years, but the overall pattern of responses did not differ significantly. The minimum wage's effect on productivity remains unclear, with different options available between sectors and to large and small employers. Productivity measures associated with intensification appear to be slightly more common than those associated with investment and automation.

8.75 Sectors which rely on public funding are more constrained in their ability to deal with the rising minimum wage. We heard evidence this year that the pressure created by the rising pay floor and squeezed funding is affecting service delivery across a range of sectors.

[15] 336 hours is regarded as a notional 1 day a week in employment contracts.

Chapter 9

Compliance, enforcement and the Accommodation Offset

Key findings

- **We estimate around 370,000 workers were paid less than the minimum wage rate for their age in April 2024** – This is around 20,000 higher than the previous year, but is still below pre-pandemic levels. Because overall coverage jumped, underpayment as a share of coverage fell.
- **We have continued to hear examples of non-compliance across several sectors** – The care sector was the most salient of these, with Unison's evidence critical of governmental "inaction and indifference" towards care workers.
- **Some employer representatives thought the National Minimum Wage guidance was inadequate and enforcement by HM Revenue & Customs (HMRC) unhelpful** – Some stakeholders contrasted the relative leniency of the NMW penalty enforcement regime with tax law or immigration checks.
- **Several years delay between underpayment and being named for non-compliance means employers can more easily dismiss being named as 'historic'** – Some respondents told us the long delays in naming employers for underpayment meant this sanction had lost its deterrent effect.
- **Workers are worried about losing their jobs and livelihoods so are reluctant to complain, and some, particularly migrant workers, don't know how to complain** – Stakeholders suggested separation of migration and NMW enforcement, changes in the way payslips are enforced and greater penalties for non-compliant employers, particularly where non-compliance is shown to be deliberate. Unions asked for a greater role in the enforcement process.
- **Employers' attitudes to the Accommodation Offset were dependent on their sector and the kind of accommodation they offered** – Some suggested the gap between the offset and the NLW should close, although very few indicated the level of the offset was a factor in their decisions on accommodation. Agriculture workers we spoke to thought the offset at its current level was a bad deal for them, given the size and quality of the accommodation they were living in.
- **There was broad support among stakeholders for our 2022 recommendations on the offset** – but frustration that these had not been taken forwards by the Government.

9.1 This chapter covers evidence related to underpayment, compliance and enforcement of the National Minimum Wage (NMW), as well as the Accommodation Offset. The Offset caps the deductions employers may charge minimum wage workers for their accommodation. Compliance and enforcement are not part of our formal remit but are an important element of the evidence we hear each year from workers, employers and other bodies. We consider it important to present this evidence and, more generally, to offer views and recommendations on the NMW enforcement system where appropriate. The enforcement system is an essential guarantor of workers' rights to the NMW and of a level playing field for employers. The evidence in this chapter dovetails with the recent standalone report on compliance and enforcement which we published in December 2024 (2024f).

Headline underpayment levels of the National Minimum Wage have risen but fallen as a share of coverage

9.2 Table 9.1 compares the latest 2024 underpayment data with revised 2023 estimates and pre-pandemic levels from 2019 using the Annual Survey of Hours and Earnings (ASHE), our main source of pay information. It shows that total estimated underpayment increased from 351,000 in 2023 to 371,000 in 2024 with the rise driven by older workers. This is likely to be a result of the large increase in the number of workers that became covered by the minimum wage following the 2024 upratings - something we discussed earlier in Chapter 3. This substantial jump in coverage meant that, despite underpayment levels increasing, underpayment as a share of coverage fell to 19.4 per cent from 23 per cent in 2023. The 2024 share was also lower than in 2019.

Table 9.1: Number of employee jobs paid below[a] the minimum wage, minimum wage coverage and underpayment as a share of coverage, by rate population, UK, 2019, 2023 and 2024

	Underpayment			Coverage			Underpayment as a share of coverage		
MW rate	2019	2023	2024	2019	2023	2024	2019	2023	2024
	Thousands			Thousands			Per cent		
AR	9	6	8	31	24	27	29.7	26.1	31.5
16-17	3	3	4	36	34	51	9.4	10.0	8.0
18-20	19	14	14	116	82	88	16.3	17.2	15.9
21-22[b]	20	26	31	98	93	147	20.9	27.5	21.2
23-24[c]	12	23	21	57	89	107	21.6	25.5	19.8
25+	364	279	292	1,649	1,204	1,494	22.1	23.1	19.5
Total	**428**	**351**	**371**	**1,987**	**1,527**	**1,914**	**21.6**	**23.0**	**19.4**
NLW[d]	*364*	*301*	*344*	*1,649*	*1,294*	*1,748*	*22.1*	*23.3*	*19.7*

Source: LPC analysis of ASHE, low-pay weights, chain linked, UK, 2019-2024.
Notes:
a. Underpayment is measured as anyone paid below the rate for the relevant minimum wage population.
b. 21-22 year olds received their own new rate in 2021. Prior to this they were eligible for the 21-24 Year Old Rate.
c. 23-24 year olds became entitled to the NLW in 2021. Prior to this they were eligible for the 21-24 Year Old Rate.
d. NLW was for those aged 25 and above from introduction in 2016 until the addition of 23-24 year olds in 2021, 2022 and 2023. 21-22 year olds became entitled to the NLW in 2024.
e. Figures may not sum due to rounding.

How we estimate underpayment

We use the Annual Survey of Hours and Earnings (ASHE) to estimate underpayment. This is a survey of employers based on a one per cent sample of employee jobs taken from HM Revenue and Customs' (HMRC) Pay As You Earn (PAYE) records. ASHE provides the best available estimate of underpayment, but comes with a number of caveats. In some cases, it is likely to record legitimate practices as underpayment (for example, if accommodation charges are deducted from workers); in others, underpayment will go unrecorded (for example, if an employer doesn't accurately log working hours for payroll). Because it is based on PAYE, it will not capture any underpayment in the informal economy, where a lot of underpayment is likely to take place. In addition, the prevalence of underpayment changes over the year, with its highest point in April, immediately after new rates have come into force.

We heard examples of non-compliance across several sectors

9.3 In our discussions with stakeholders, we are much more likely to hear about underpayment in certain sectors. Social care is chief among these. Unison's submission again discussed at length non-compliance and enforcement in the care sector. They described the non-payment of care workers' travel time as "still appalling". They characterised the Government's response to non-compliance in the care sector as "inaction and indifference", arguing the Government "has completely given up on tackling non-payment of the minimum wage in the care sector, indeed if it actually had any interest in doing so in the first place."

9.4 They shared recent FOI responses showing HMRC officials had not met with the Department for Health and Social Care (DHSC), other departments or local authorities to discuss care-related compliance issues and commissioning practices. They also showed that the Government had not prosecuted any care employers for failure to keep records. The failure to engage with DHSC "displays a complete dereliction of duty from the Government in trying to address a profound problem for tens of thousands of social care workers across the UK." They shared evidence showing that in 2023/24 average arrears per care worker recouped by HMRC came to just £123.63, and 73 per cent of all arrears were awarded via self-correction. In comparison, they gave the example of a recent tribunal case for nine home carers. Respondents had failed to disclose pay records so members spent a lot of time calculating their working hours. The case took four years to conclude and ended with a total award of around £100,000.

9.5 The Home Care Association (HCA) acknowledged that compliance is a challenge for providers reliant on public funding from local authorities or clinical commissioning groups, as they often purchase care by the minute for contact time only. Many do not pay extra for travel or waiting time between clients. HCA stated that these public organisations pay significantly below the rate the HCA calculate is necessary to deliver care. Unison described poor quality commissioning practices as "an elephant in the room" when it comes to non-compliance in care, which "can increase the likelihood of care workers being paid below the national minimum wage."

9.6 In agriculture, the submission from the Association of Labour Providers (ALP) argued that the rising NLW incentivised 'rogue operators' to cut corners. They shared evidence from an April 2024 survey of their members on supply chain practices. Nearly three quarters have seen competitors "offering unsustainably low charge rates" and nearly half "have walked away from business due to unfair procurement practices." They argue that compliant businesses are "priced out by those who are prepared to cut corners and exploit workers." Research by the National Farmers' Union (NFU) found that the main reasons for non-compliance among their members were confusion about the relationship between basic pay and overtime and productivity payments, and the interactions between the minimum 32-hour paid employment rule for seasonal workers and NMW pay rules.

9.7 The submission from the Equestrian Employers' Association (EEA) again recognised that failure to pay NMW/NLW rates exists within the equestrian industry and employers were fearful of enforcement: "They would be reluctant to report any failings they identify themselves or ask for support due to concern that they would be issued with crippling fines forcing their business to close."

9.8 The submission from the British Hair Consortium (BHC) described the hair and beauty sector as "the wild west," stating there are "no employment checks, no understanding of basic employment law or checks by HMRC or any other agencies." Rather than NMW underpayment, their main concern was the rise of (bogus) self-employment models, which they argued was effectively pushing the sector into "the hidden economy." Competition from bogus self-employment and cash in hand businesses, they argued, undermines businesses with conventional employment models and makes it harder to raise prices to cover cost increases. "Employers need incentives and grants to drive growth. Alarmingly, only 35 per cent of our sector is employed, which should raise serious concerns about the industry's sustainability." The British Beauty Council (BBC) agreed that "greater HMRC resource needs to be placed into addressing those operating within the black economy and not declaring their full income."

9.9 Trades Union Congress (TUC) research published in August found that major job boards were advertising dozens of salaried jobs at below the minimum wage (Trades Union Congress, 2024b). Unite members in Northern Ireland told us that unpaid overtime put many hospitality and retail workers into underpayment: "You have folks that are formally hired on a 30, 35, 40 hour contract and when you translate the salary, it's maybe just slightly above the NMW, but the amount of hours that they're working in unpaid overtime puts them below the minimum wage."

9.10 The TUC argued that enforcement was failing seafarers. Despite the extension of NMW rights to greater numbers of seafarers, "over the last 14 years we are only aware of one maritime employer that has been found to have underpaid seafarers and that offence was committed before the 2020 regulations came into force." They noted that implementation of the Seafarers Wages Act remained incomplete, and the scope of the act would not rule out actions such as those taken by P&O Ferries in 2022, while proper enforcement of the act would require resourcing and training for Maritime and Coastguard Agency staff. Similarly, the RMT saw little evidence of enforcement for seafarers, with notional rights remaining unenforced. The application of the NMW to seafarers is discussed further at the end of this chapter.

Stakeholders want the Government to look at the entitlement to and enforcement of the NMW for seafarers

9.11 The RMT told us the Seafarers Wages Act left significant holes in coverage and enforcement. The RMT provided extensive evidence on the operation of the Act, which provides for seafarers who don't qualify for the UK NMW but do work in UK waters to be paid at a wage equivalent to the NMW. They note the Act's limitations in preventing a repeat of P&O's mass sacking of seafarers. RMT's preferred option is the adoption of the voluntary Seafarers' Charter as a mandatory set of employment conditions. To date, though, no employer has completed the verification process to obtain charter status.

9.12 The RMT also argued that the separate extension of the NMW to seafarers in October 2020 had been partial and incomplete. The regulations that extended the NMW to seafarers working in UK waters omitted those working in the offshore wind or offshore renewables supply chain beyond the 12-mile territorial water limit. The offshore renewables sector was expected to grow considerably in the coming years, and the shortcomings of the legislation created the risk that "the offshore renewable sector supply chain will see rates of pay below the legal minimum wage." RMT argued that this lack of foresight risked storing up problems with pay and employment conditions in the future. They stated there was already evidence that operators in the sector were using agency seafarers paid below the NMW. Even with current legislation, they described low pay as 'ingrained' among seafarers and referenced evidence from P&O to the DBT select committee "that some seafarers on their short sea international routes from the UK are paid as little as £4.87 per hour for tours of 17 weeks." **We recommend the Government look more widely at the entitlement to and enforcement of the NMW for seafarers, including via full implementation of the Seafarers Wages Act.**

There were mixed views on the enforcement system

Employers had negative views of HMRC's enforcement

Employer representatives complained of HMRC's approach and performance

9.13 Various stakeholders had comments on HMRC's enforcement of the NMW. Some employer representatives objected to the lack of any distinction between deliberate and inadvertent non-compliance, as well as the time and resource demands NMW investigations created. The Confederation of British Industry (CBI) argued that the rising NLW increased the need for reform of the enforcement system: "long-standing business concerns about the opaque legal enforcement of the NLW could also be made worse if a higher bite were to lead to higher coverage. Employers are still concerned about technical and deliberate non-compliance being treated by HMRC as if it is the same, and if coverage rises, more may be brought into scope of the enforcement regime. A single enforcement body capable of providing proactive, clear advice to employers is needed to reduce accidental non-compliance."

9.14 The ALP's submission argued that HMRC's case closure rates show "staggering underperformance," and picked out the 2022 figures showing only seven cases closed per HMRC NMW staff member. They repeated their previous call for a National Audit Office review of HMRC's work and for the LPC and Director of Labour Market Enforcement to work "to develop appropriate outcome and impact based key performance indicators aligned with the Regulators' Code."

Employers tell us complying with investigations creates significant burdens

9.15 The HCA told us their members complained of HMRC making high demands for documentation and the inspection process taking a long time. Members felt HMRC did not always understand how to interpret the regulations with respect to the delivery of homecare, and there could be inconsistency across inspectors. Members wanted inspections to do more to highlight systemic issues with non-compliance resulting from local authority fee rates and commissioning approaches rather than focusing on individual providers.

9.16 The British Retail Consortium (BRC) told us their members faced "an uphill task" in compliance and enforcement and found it extremely difficult to engage with HMRC. The Scottish Grocers'

Federation (SGF) told us "it is important that HMRC can distinguish between genuine businesses who may have made genuine errors and those rogue businesses that deliberately break their responsibilities and duties as required under employment law."

9.17 In hospitality, the British Beer and Pub Association (BBPA) told us experiences with HMRC were generally not positive. Themes that emerged from their survey of members were a lack of clarity and transparency, inconsistency (notably in terms of the HMRC staff allocated to cases), the length of time taken for investigations and the prioritisation and proportionality of investigations. Hospitality Ulster described HMRC enforcement as "pedantic and unhelpful", and argued there should be a "more holistic approach to look at the quality of the employment". They argued that too much depended on interpretation of rules around things like uniforms, and inspections are perceived as unnecessarily obstructive; "they want to catch people out as opposed to help people comply." UK Hospitality's (UKH) survey found half of respondents said they had no experience of enforcement. Of those that had, just over half felt the experience was 'standard' with a third saying it was poor, and a sixth saying it was good.

9.18 The Federation of Wholesale Distributors (FWD) were more positive: "Over 55 per cent of respondents agree that HMRC's enforcement of NLW and the guidance they make available to employers helps to increase compliance." The NFU also expressed their approval of the "supportive and educational" approach HMRC had taken to promoting compliance.

Some respondents argued enforcement was too lenient

9.19 In contrast, the Work Rights Centre's (WRC) submission argued that enforcement culture was too lenient. HMRC operated, they argued, using a "presumption that most firms want to comply with relevant legislation," and this affects how they deal with non-compliance once discovered. They compared this with tax law and immigration right to work checks; "this leniency is not replicated in other areas where employers have serious legal responsibilities." In addition, factors such as visa sponsorship rules and a lack of reporting channels "have meant that some sponsors can act with impunity and get away with flouting minimum wage requirements." They agreed with past LPC comments on the length of the enforcement process: "if 40% of HMRC's caseload takes between 120-365 days to close, this may come too late for workers who become undocumented or who end up returning home and are no longer within reach."

9.20 Unison shared their concerns about how strong and active HMRC investigations are, as well as the self-correction process: "it's how deep they're prepared to dig, and whether they take what employer tells them at face value." While they acknowledged there could be a role for self-correction in cases where underpayment affected only one worker, any instance involving more employees should be treated as a red flag requiring investigation. Overall, "the whole process needs to be more transparent."

9.21 The Recruitment and Employment Confederation (REC) told us they would support more substantial penalties for NMW non-compliance, including a warning system and harsher penalties for persistent breaches. They compared the NMW enforcement process with Right to Work checks – where their members were "terrified" because penalties were so strict (for example, employers face penalties of up to £60,000 for each illegal worker they employ). WRC highlighted previous Resolution Foundation work on the level of NMW penalties and the insufficient deterrent effect they offer (Judge and Slaughter, 2023). They noted penalties in the UK are low compared with other countries and recommended increasing fines and having more regular naming rounds.

9.22 Unison told us that poor quality payslips and record-keeping were prevalent in the care sector, but shared Freedom of Information requests revealing that no care providers had been prosecuted for failure to keep records: "the difficulty is that complete lack of transparency when it comes to pay and the average worker being unable to decide for what they have been paid." They urged the LPC to consider recommendations about record-keeping, making a specific suggestion that Government could bring section 12 of the NMW Act into force, which would require employers to provide an NMW statement so workers can check they have been paid. "If there was a statutory obligation on employers to provide a statement … there would be a more level-playing field."

Employers feel NMW guidance is inadequate

9.23 Unison told us that "employers are crying out for clearer guidance," and many employers agreed. Chartered Institute of Payroll Professionals (CIPP) members felt guidance was inadequate, with one complaining of "some very ambiguous/vague areas which feel like they are designed to trip you up." The CIPP argued that "Some of the confusion around NMW compliance seems to stem from the split of duties between HMRC and the Department for Business and Trade (DBT). A more joined up approach to compliance is needed to provide employers with the clarity they need to follow the rules accurately."

9.24 The Federation of Small Businesses (FSB) noted that "Understanding employment law can be particularly challenging for small businesses who do not have a HR or legal department. With small businesses being such a wide and disparate group, promoting awareness of rights and responsibilities can be a challenge." The NFU called for an improvement in awareness and guidance and suggested three changes: greater use of worked examples; the inclusion of scenarios specific to agriculture and horticulture, including the application of the accommodation offset; and a suite of frequently asked questions. UKH told us that, concerned by "the seemingly random interpretation of some of the rules used under NMW enforcement," the hospitality sector had, for many years, requested sector-specific guidance that clarifies how officers interpret policies on uniforms, time required to be ready for work and other issues but there has been a lack of sector-specific guidance.

9.25 REC told us that current NMW guidance "fails to adequately address the complexities of temporary work. This guidance relies on traditional full-time employment models and outdated legislation, which do not reflect modern practices such as the rise in temporary work and the gig economy … This lack of clarity can lead to accidental non-compliance by employers who are confused about the correct practices for temporary workers."

9.26 A specific area where we heard about problems with NMW guidance was the rules around work type. When measuring working time for NMW purposes, working arrangements are divided into four categories: salaried hours work, time work, output work and unmeasured work. These categories and their implications for working time and underpayment – are complex, and we have heard from both employers and advisory bodies that they are routinely misunderstood. This is particularly true when it comes to salaried work and unmeasured work. In our recent report on compliance and enforcement, we recommended that Government look at improving the guidance on work type and the differences in calculating working time between salaried and unmeasured work.

Naming rounds are no longer an effective sanction

9.27 REC shared their concerns over the effectiveness of naming rounds. The long wait between offences first being identified and companies being named meant that by the time of naming "companies have often taken steps to correct whatever led to the breach occurring." Naming then "becomes little more than an act on a company's brand and reputation despite the issue having long been resolved." One advisory firm also thought the time between naming and the actual underpayment was now so long that firms could write the naming off as "historic" or "under previous ownership".

9.28 The Chartered Institute of Personnel and Development (CIPD) requested more educational information in naming and shaming rounds to feed back to their members. The CIPP also thought it would be beneficial to see more information about how non-compliance came about, whether by process errors, clerical errors or fraud.

Unions called for a more central role in the enforcement process

9.29 Unite called for the enforcement agencies to collaborate more with unions: "Enforcement agencies alone cannot effectively 'police' against labour abuses." GMB too wanted to see "more proactive work between enforcement agencies and trade unions, including a widely trusted third-party complaints system and providing unions with more information and oversight on non-compliance in the sectors they represent workers in." More feedback from HMRC would help, as would rights of access to workplaces: "All this would mean a lower cost of enforcement for the state." Similarly, Unite argued unions should be able to bring collective grievances. Under the current rules, workers "are left in the vulnerable position of being forced to individualise every complaint. Unite would like to see a situation whereby a trade union can make a representative action on behalf of a group of workers to an employment tribunal."

Stakeholders told us workers are not confident in reporting underpayment and worried about losing their jobs

9.30 Some respondents reflected on the incentives for workers to make complaints. Citizens Advice on the Isle of Wight told us that when one group of workers from a specific employer had come to them reporting minimum wage underpayment, they had been reluctant to complain "because they're worried about losing their jobs". This was still the case when advisors offered to complain anonymously on their behalf: "the employer knows who they're underpaying, don't they? So there there's a small pool of people that could have made that complaint." A Unite rep in Northern Ireland told us that "when workers do report minimum wage issues, they're getting a very, very slow response time". There was also "a huge burden of evidence [for] those workers who are making these reports," which was particularly difficult for migrant workers.

9.31 WRC's submission referenced Defra survey findings on the seasonal agricultural workers scheme "that nearly 30 per cent of workers do not know how to raise a complaint when one arises. Of those that had submitted a complaint in the past, 42 per cent reported their complaints not being followed up." In Northern Ireland, Unite agreed that awareness of both the NLW and the agricultural wages board was "unfortunately low" in rural areas, with poor awareness especially of rules around deductions for accommodation and food.

9.32 WRC expanded on the lack of safe reporting channels for migrant workers. While other countries "have recognised that preventing information from being shared about a worker's immigration status is key to identifying and preventing abuse," the WRC argue that in the UK data-sharing between police, labour inspectorates and immigration enforcement is common. They stated: "a lack of safe reporting channels is the most pressing reason that enforcement bodies have lacked 'upstream' intelligence from migrant workers in recent years … migrant workers are simply not incentivised to report their circumstances." They also described how the work-sponsorship model reinforces this problem – workers worry that by complaining, their employer might lose their sponsor status, meaning both the worker and their colleagues would lose their jobs. The WRC recommended a range of measures to end data sharing and joint working between labour and immigration enforcement teams, and to build trust with migrant communities. Submissions from GMB and TUC also argued for a firewall between immigration enforcement and labour enforcement.

9.33 Some respondents supported previous LPC recommendations on third-party complaints. WRC noted that HMRC's NMW enforcement was key for their client base of migrant workers as Employment Tribunals were in most cases not a practical option. They told us they would benefit from several changes suggested in past LPC reports: sharing of non-disclosive information on activity in certain sectors; some examples of actionable intelligence and how it can be used; and prompt and regular feedback to third parties, to help inform their own activity. For seafarers, RMT supported reform of the third-party complaints process, stating "it is arguable that there is a serious lack of understanding of NMW rights for seafarers because of the significant differences between seafarers' and land based workers' employment rights." They saw reforms of the third party complaints process (and greater involvement for unions in the process) as one way to address this and to strengthen workers' rights, "especially those of non-EEA seafarers who are reluctant to engage with UK state regulators."

Employers are frustrated with salary sacrifice rules

9.34 The interaction between NMW rules and salary sacrifice schemes has been an increasingly prominent theme in evidence we've received in recent years. Like other deductions, if salary sacrifice schemes reduce workers' pay below the NMW this is underpayment. Although not a new issue, increases in the NLW mean a wider swathe of workers – including those paid significantly above the NLW before any salary sacrifice – are potentially caught by this effect. We have received submissions from employers in recent years who have ceased to offer salary sacrifice schemes to some or all of their workforce because of this. We covered some of the detail of this area in our recent standalone report on compliance and enforcement.

Box: What is salary sacrifice?

Salary sacrifice refers to an arrangement whereby a worker agrees to "sacrifice" part of their contractual entitlement to pay in exchange for another, usually non-cash benefit. The term is not used in NMW legislation. Salary sacrifice arrangements result in a reduction in the workers contractual pay, and it is this new (lower) amount that is considered as the starting point for NMW calculations. If the benefits the worker receives under a salary sacrifice scheme are not liable to tax and/or National Insurance contributions (NICs) then they could be in a better position overall than if they had merely purchased the benefit from their net (after tax and NICs) pay independently. The employer also avoids paying employer NICs on the cash amount given up for any pay above the NICs Secondary threshold of £175 a week (15.3 hours on the NLW).

The category of non-taxable benefits includes pension contributions, travel schemes (for example cycle to work or vehicle lease schemes) and childcare vouchers (which have been closed to new entrants since 2018).

9.35 For low earners - especially part-time workers on the minimum wage – the advantages of salary sacrifice arrangements can be limited. If a worker normally earns employment income between the lower earnings limit (£123 per week, or just under 11 hours at the £11.44 NLW) and the earnings threshold (£242 per week, or just over 21 hours at the £11.44 NLW), they do not pay class 1 (employee) NICs, so there is no saving from switching from cash to a non-cash benefit. If salary sacrifice reduces earnings below the lower earnings limit the worker will not pay class 1 NICs and may lose entitlement to contributory benefits and the state pension. NICs thresholds have been frozen in recent years while the NLW has risen significantly, lessening this risk.

9.36 At our request, the CIPD included questions on salary sacrifice in their summer Labour Market Outlook survey, a representative survey of over 2,000 senior HR professionals and decision-makers. This represents our best data on the provision of salary sacrifice arrangements and their interaction with the NMW. Just over half of survey respondents offered their workers salary sacrifice; 39 per cent offer salary sacrifice to the whole workforce, while another 14 per cent offer it just to some. Public sector employers are more likely to make it available than private sector ones (60 versus 52 per cent), and it was more likely to be on offer in larger organisations (71 per cent of employers with over 1,000 employees make it available). Pension and travel schemes were the most common kinds of benefit available via salary sacrifice. 77 per cent of employers offering salary sacrifice offered it for pension contributions; 70 per cent for travel schemes such as vehicle lease or cycle to work.

9.37 Less than 10 per cent of employers in the survey had withdrawn salary sacrifice as a result of the NLW. 2 per cent had withdrawn it for all eligible workers, and 7 per cent for some eligible workers. Among employers with 250 or more employees, 14 per cent had withdrawn salary sacrifice schemes from some of their workforce and 4 per cent had withdrawn them totally. The effect was greater in certain sectors (with the caveat that sample sizes are smaller when looking at individual sectors): in manufacturing, 29 per cent withdrew it for some of their workers and 2 per cent for all; in construction these figures were 28 per cent and 1 per cent respectively; in healthcare 10 and 7 per cent. Among employers who did not offer salary sacrifice schemes, three-quarters said the NLW was not a factor at all in this decision. Lower-paid workers are more likely to be affected by the withdrawal of salary sacrifice schemes. Beyond salary sacrifice, 14 per cent of employers have either taken away or never offered other (non-salary sacrifice) benefits to staff on or just above the NLW.

9.38 Other employer representatives noted the withdrawal of salary sacrifice schemes. The BRC argued that "the current design of the system is detrimental to those who need it the most, as it excludes colleagues in lower incomes. These constraints also have an impact on the cost of governing salary sacrifice schemes, that can become prohibitively high." They called for a review of the rules around these schemes. The CIPP's submission stated that "salary sacrifice arrangements have been heavily impacted by large rises in NMW rates … employees who had headroom to sacrifice salary no longer do and must be removed from the schemes". Employers, they told us, were concerned about the fairness of such decisions. The CBI also noted a trend for employers to withdraw salary sacrifice. The Food and Drink Federation (FDF) recommended allowing the inclusion of salary sacrifice in the NMW calculation.

9.39 Pension contributions were the most frequently identified and discussed benefit. The BRC told us its members "believe this area needs to be reviewed in order to further encourage individuals to participate in pensions and save in the most tax efficient way for their future." The CIPP's submission outlined how ending salary sacrifice for pension schemes could leave employees worse off: "When an employee is removed from a salary sacrifice arrangement, they will be put onto a relief at source or net pay scheme, neither of these schemes give the National Insurance relief that a salary sacrifice scheme would. The result is that an employee contributes the same amount to a pension scheme but sees a reduction in the take home pay they receive. This can cost an individual around £100 over the tax year in relief lost."

9.40 The main policy proposal suggested was to allow salary sacrifice to take workers below the NMW, whether for certain benefits only (e.g. pension contributions) or for a wider range of benefits. The CIPP acknowledged this would require "long and thoughtful" consideration, to protect those on low incomes. "It is understood that NMW regulations are there to protect the lowest paid and most vulnerable, therefore we do not propose that salary sacrifice should be allowed to bring a worker below NMW in all situations." Some members argued that "such allowances could only be made for OpRA (Optional Remuneration Arrangement) exempt items, such as pension contributions and cycle-to-work schemes." Other members called for "all salary sacrifice arrangements to not impact the calculation of NMW" although CIPP recognise this approach "would require sufficient safeguards to allow freedom to sacrifice salary without unscrupulous employers from engaging in fraudulent deductions."

Unions accept some workers are losing out, but do not favour a change to the rules

9.41 Some unions acknowledged that salary sacrifice schemes were being withdrawn, but their views on the appropriate remedy tended to differ from those of employers. GMB told us that low-paid health workers had been excluded from salary sacrifice schemes (specifically, schemes for car lease arrangements). They saw this as a consequence of the lowest pay rates falling so close to the NLW. Usdaw also recognised that salary sacrifice schemes were not offered to low-paid workers in case they fell below the NMW, with employers not wanting to risk naming by HMRC. When prompted on whether the rules needed changing, an Usdaw representative told us: "I don't know what the perfect solution is. I think allowing people to be paid below the minimum wage opens up a whole can of worms. And you've got to end up trying to judge what the benefits of the salary sacrifice arrangements are." For Unison, "you can understand the arguments … our concern is about keeping the minimum wage as simple as possible to enforce … the weight of the argument for us is about keeping it simple and not allowing employers the wiggle room to get out of paying the minimum wage."

9.42 The TUC told us they "would approach any proposal [to allow sub-NMW pay via salary sacrifice] with a very high level of suspicion because of all the implications of … changing somebody's contractual pay rate." These included "the risk of going below the lower earnings limit and then finding eligibility to benefits like statutory maternity pay or sick pay or the risk of pension contributions going down," as well as "the implications for somebody of having a lower reported pay rate for their wider abilities to borrow or to access finance, and for what that might mean for future pay awards." They argued that "if an employer wants to provide such a benefit, do it at a rate that's sufficiently high that it doesn't take someone below the minimum wage."

Worker representatives are concerned that the minimum wage is not sufficient to save for a pension

9.43 The TUC's submission discussed the NLW's interaction with auto-enrolment thresholds and the effects of this for low-paid workers. As the NLW rises, the TUC point out that a greater proportion of low-paid workers are brought into auto-enrolment (the threshold for which has been frozen for some time). The TUC argued the cost of pensions contributions should be taken into account in setting the NLW, and also recommended the LPC should "consider what level of pay is needed to save enough for a decent retirement income."

The emergent "elective deduction model" risks workers losing out on the pay or holiday they are entitled to

9.44 A submission from the Low Incomes Tax Reform Group (LITRG) raised two emergent areas where they saw risks of underpayment. The first was around workers incorrectly described as self-employed because of an "elective deduction model … aimed at low paid agency workers in the temporary labour market." Under this model, workers are paid via an umbrella company, which deducts employer NICs and its own margin, and pays the worker their gross pay. The arrangement is premised on the individual being classed as employed for tax purposes but self-employed for the purposes of employment rights (indeed, their contract states this). LITRG argue that "this worker's 'self-employed' label doesn't reflect the reality of the working arrangements and the nature of the relationship between the parties involved." The gross pay the individual receives does not account for the holiday entitlement to which they are entitled (owing to their having 'worker' status). "Depending which way you look at it, they are being incorrectly denied holiday pay (as a minimum) - or they are being underpaid the NMW." LITRG also pointed to status issues in the care sector specifically: "there seems to be an increasing number of self-employed workers in the care sector, many of whom appear to be falsely self-employed."

9.45 LITRG believed HMRC would not identify this issue: "we do not know whether HMRC officers really consider digging into status to be part of their NMW enforcement role or whether they would be more inclined to accept a self-employed status on face value." They called on the LPC to engage with HMRC, to "ensure, as far as possible, that HMRC officers understand Elective Deduction Model (EDM) and are not strict or sparing in their approach to it. Instead, they should be helpful, holistic and see the potential role that they could play in making engagement models such as EDM ineffective."

Salary advance schemes also present risks of underpayment

9.46 The second area identified by the LITRG relates to salary advance schemes. These schemes allow employers to move from a weekly to a monthly payroll system (which is less administratively burdensome), while workers continue to be paid on a weekly basis. The schemes are operated by third party providers, which collect a fee for the service. "The issue here is that rather than being used in an emergency, we think the schemes are being used by employees to simulate being paid weekly." LITRG saw a risk that the fees charged by the provider could be seen as reducing pay for NMW purposes, and thought guidance on the use of such schemes and their interaction with the NMW was inadequate. They "urge the commissioners to undertake a review of the salary advance market so as to better understand the nature and scale of scheme use, and to recommend a tweak to the law if deemed necessary to protect low paid employees."

Some stakeholders believe firms can "phoenix" to avoid paying wages too easily

9.47 The WRC's submission laid out the ways in which employers who underpay workers can get away with phoenixing. WRC stated that their Service Provision team persistently encounter phoenixing, where "those flouting minimum wage regulations and other employment obligations … simply disappear once a complaint is raised, leaving workers without money and without access to redress." Despite recent legislation giving Companies House new powers, there is still a lack of practical means to hold individuals to account. WRC noted that "the Insolvency Service considers the non-payment of an employee's wages "an individual commercial dispute." They argued that "this messaging does little to instil confidence that enforcement of the minimum wage is seen not only as an individual good, but a 'public' good that benefits other employees and compliant businesses alike." They recommended that "workers should be able to sue individual directors at the Employment Tribunal," which is often prevented currently, and that the UK could follow the example of Brazil "where the state maintains a list that sanctions individuals who are engaged in exploitative practices, rather than companies themselves."

Accommodation Offset

9.48 In addition to recommending minimum wage rates, the LPC is responsible for recommending the Accommodation Offset rate, which caps the deductions employers may charge minimum wage workers for their accommodation. The offset is distinct from other NMW rates, both in the paucity of quantitative data on its use and effects, and in the lack of a clear direction in our remit on how to set it. Our 2022 Report contained a detailed review of the offset and made a number of recommendations. The main recommendation concerned future changes to the level of the offset; we stated that the value of the offset as a proportion of the NLW would not increase significantly until we had assurance that robust minimum standards for accommodation quality were in place and enforced. Stakeholder evidence this year concerned both the level of the offset and our 2022 recommendations.

Employers are not satisfied with the level of the offset…

9.49 There were some variations in employers' views on the level of the offset by sector. In agriculture, the NFU noted the offset did not cover the costs of the provision but described it as "useful in allowing some costs to be recovered. The recent increases, although not sufficient to fully cover the cost of provision, are welcome." One NFU Scotland member on the Glasgow visit (a labour provider) told us the businesses he worked with found the offset to be "workable … there hasn't been too many issues with it." Another farmer was more ambivalent, and stressed it was important to find the right balance in setting the offset: "maybe there needs to be a better balance … just to keep it viable. Of course it has to work for the staff as well, I absolutely understand that. But it has to work for us as well as employers." On our Dover visit, AC Hulme, a large fruit grower, told us the offset was too low: "There needs to be some catching-up," and increases "should never be less than [increases in] the NLW … for it to be less is not equitable to the provider."

9.50 In hospitality, UKH argued the level of the offset was too low: "the change in the level of the offset exacerbated this, by not keeping pace with wage rates." Anecdotally, they reported, this was leading businesses to look at removing worker accommodation. "This would be detrimental for workers and employers but would be a logical step as rooms can be let out at much higher rates.

Accommodation now typically tends to be provided to managerial or experienced members of staff for whom the offset is either irrelevant or minimal. The effect of the offset is that additional accommodation is not being provided for those on lower wages who are being disadvantaged by having to pay market rents in addition to transport costs." The BBPA told us there was a concern among members that an increasing need to provide accommodation for staff would, over time, mean that the significance of the offset may increase for the sector. For those who did provide accommodation, the general view was that the increase had a negligible impact on employers' decisions.

9.51 In care, the HCA told us they had seen an increase in the provision of accommodation arising from increased overseas workers. They felt the offset had not increased enough to reduce the potential for non-compliance. They were also unsure if employers were properly accounting for the costs to ensure compliance.

9.52 REC told us they believed "the Offset should continue to rise in line with the adult rate, as it is a valuable tool for firms in hospitality and agriculture." The British Chambers of Commerce (BCC) told us that while the offset was only used by a small number of our members "it seems to be working well for employers where used."

...but workers thought the offset did not represent good value

9.53 The TUC called for employers to bear as great a share of accommodation costs as possible: "Employers gain significant benefit from the provision of accommodation, which gives them immediate access to their workforce on site … Where the job is only possible while living in tied accommodation, the offset should not be used at all." The WRC's submission similarly argued that: "the Accommodation Offset can and often is used to suppress workers' earnings. Under the SWS [seasonal workers scheme], the accommodation offset represents yet another cost/deduction/financial burden that encumbers workers."

9.54 Migrant workers we spoke to in a focus group organised by the WRC uniformly felt they were getting a bad deal for their accommodation and that the current offset level of nearly £70 per week was too expensive. Workers described their caravans as in a poor condition, too small for sharing with up to five other workers and thought the accommodation charge was too high for what they were provided with. In some cases, views on the cost of accommodation were linked to views on charges for utilities and other services, which were often additional to the basic rent covered by the offset. One worker told us that workers on his site were charged £2 to wash clothes and the same again to dry them, and because of the nature of their work were having to wash their clothes nearly every day. Another worker had been charged £5 per day for travel costs from his place of accommodation to the farm (although this ceased following a Home Office inspection of the provider). Another worker had calculated that for the equivalent sum to the offset, given the number of people living in the caravan she occupied, they could be renting privately somewhere much nicer.

The kinds of accommodation covered by the offset vary significantly

9.55 AC Hulme spoke to us about the investment they had made in on-site accommodation. Caravans were purchased from commercial holiday sites. Their lifespan on the farm "depends on how much abuse they get" but was no more than five years. They had invested in the site as part of a joint venture with a large labour provider (so workers accommodated on their site also worked at other farms in the region). This agreement had helped maximise occupancy and helped drive forward standards at the campsite. "There's been a rapid realization within our industry that your staff will be more loyal to if you look after them." As they summarised "we need to provide this accommodation … if we didn't provide it, they wouldn't come here." Having good occupancy throughout the site made it easier to make significant investments.

9.56 Other farmers we met through the year described the importance of tied accommodation. An NFU member we met on a visit to Coventry and Wolverhampton argued "there is a distinction to be drawn between horticulture, with a large seasonal migrant seasonal worker population, and other sectors which will offer tied accommodation as part of an overall employment package." Another NFU member at the same meeting told us: "we couldn't recruit without some tied accommodation in places. […] It's not close the shop at five o'clock and come back on Monday morning. And so if the cattle suddenly get out at 2:00 AM on a Sunday morning, God forbid, you want someone on site."

9.57 A farmer we spoke to in Northern Ireland provided accommodation in four brick-and-mortar houses that he owned in the local town. He did this because his business was his home and he "would really like people off site whenever it's not working times." He thought accommodation quality was important and wanted "really good accommodation that people want to come back to", which he thought increased the number of older, returnee workers. The farmer did not deduct the accommodation offset from payslips (he was "not looking to make money out of [his] accommodation") but did charge workers rent of £55 per week including bills and transport to work (below the offset rate).

9.58 On our Glasgow visit, hoteliers told us the offset was "broken as a system," summing it up as "caravans versus Ritz Carltons." Hotels felt aggrieved that their expensive and high-quality accommodation was subject to the same treatment as caravans provided in agriculture. One emphasised the substantial investment they'd made: "we had to pay £25k to upgrade the wifi so the staff can play Call of Duty after work. People won't work for you now without single rooms, en suite…"

The offset creates compliance risks for employers

9.59 Employers and their representatives often saw the offset as a difficult area for compliance. The ALP's submission provided an annex listing 38 areas, directly or indirectly connected to the offset and the provision of accommodation, where there was ambiguity over the application of NMW guidance. These ranged from key deposits to bedding, payments for washing machines or showers to purchases from on-site shops. More generally, they call for DBT's guidance to be made more accessible (it "is inadequate in supporting industry in correct and consistent application of the law"). The CIPP's submission noted that the views of its members on the offset varied significantly, and "it may be worth reviewing what the offset seeks to achieve, assess the practicalities of its administration and seek simplification in the process." One hotel on our Glasgow visit noted that some establishments were misleading potential recruits with job adverts promising "free accommodation", which "is not possible as you'll get P11D'd" (whereby HMRC treats a benefit in kind as taxable).

9.60 The specific area employers worried about most were utilities – whether and how much it was permissible to charge workers for them. As an NFU member on the Coventry and Wolverhampton visit stated, "the area which causes the most difficulty and where people slip up more often is … what can and cannot be included in that in that offset, especially when it comes to the provision of utilities. […] There is a desire perhaps for a bit more sector-specific guidance". NFU Scotland told us that not being able to charge for gas, electricity and other utilities was a growing concern and left employers out of pocket. Employers, they stated, would rather charge less rent and allow the worker to cover their own utility costs. NFU Scotland members in Glasgow similarly felt that the cost of electricity had gone up substantially and "the workers are using more electricity, I guess because they're not paying for it." Another member worried that "where they're not getting charged for it directly, then you know, is there any incentive for them to not leave heaters on? … we try and monitor it, but it becomes another job and that's where it can become very, very costly."

There is general support for previous LPC recommendations on the offset

In our review of the Accommodation Offset in 2022, we made three recommendations:

- The value of the Accommodation Offset as a proportion of the NLW will not significantly increase until we have some assurance that there are robust minimum standards in place for accommodation and that these are enforced.
- We recommend a minimum hours requirement before accommodation costs can be deducted, for workers at risk of no or very low pay as a result of accommodation charges.
- We recommend that seafarers be exempt from the Accommodation Offset while on board ship.

At the time of writing, the Government has yet to respond to these recommendations. We continue to stand behind the recommendations we previously made and urge the Government to consider and respond to them formally.

Stakeholders recognise the case for quality standards and want to see these implemented

9.61 The TUC stated their support for the LPC's 2022 recommendations on quality standards: "The quality of accommodation should be monitored by enforcement agencies and no offset deductions should be taken for poor quality accommodation." They noted evidence from the Seasonal Workers Pilot review (Defra and Home Office, 2019) that "15 per cent of workers said their accommodation was neither safe, comfortable, hygienic nor warm and 10 per cent said their accommodation had no bathroom, no running water, and no kitchen."

9.62 The WRC also support these recommendations, reporting they received frequent complaints from workers "of being placed in poorly insulated caravans which are cold and far away from kitchen and toilet facilities. Safeguarding issues have also arisen in some cases, including women being placed in male-only caravans." They noted the vagueness of Home Office guidance to scheme operators. While the Home Office assign responsibility for oversight to local government, they had found limited evidence of this being exercised. A WRC FOI request found that no local authority in England or Wales had applied for approval to licence caravan sites for agricultural workers. "The Commission's conclusions around accommodation standards are therefore highly relevant in tackling what is effectively an unregulated area."

9.63 The ALP proposed trial implementation of accommodation standards in agriculture. Along with the Fresh Produce Consortium, they told us they had produced their own guidance on temporary accommodation for seasonal workers. "ALP recommend that a pilot with appropriate funding is developed within the Seasonal Workers' visa route which can be used as a template for roll out to other sectors."

9.64 UKH similarly welcomed the LPC's recommendation ("a positive step for employers who provide good accommodation to their workers, and it will disadvantage those that provide sub-standard living standards") but were concerned that delays in any regime coming into force would mean investment was deferred. "The longer this is delayed, the more likely it is that existing accommodation will be converted for commercial use and that investment in live-in accommodation will be delayed." Their proposal was for the LPC to work with their sector to create and pilot a model for evaluation and enforcement, with an eventual view to a higher offset rate for accommodation which is recognised as high quality.

9.65 The BBPA told us that where members provided accommodation, the general view was that this was already of a good standard and the LPC's proposed change would have minimal impacts. They expressed "a note of caution at introducing a new level of regulation and administration that potentially duplicated existing requirements" and added to costs.

Employers have concerns over the application of a minimum hours requirement

9.66 The WRC supported our recommendation on a minimum hours requirement. Even though the seasonal workers visa in agriculture now provided for a minimum of 32 hours of work, WRC still thought implementation of the LPC's recommendation would be "a welcome guarantee of [workers'] rights." They noted the importance of enforcing any such change. Even if the change would leave farms at risk of providing accommodation to some workers for free, WRC argue "this is currently a fair compromise for the financial risk that workers on the [seasonal worker visa] otherwise take on when working in the UK."

9.67 The ALP told us they supported a minimum hours requirement but suggested the proposal needed more thought: "ALP will provide further evidence should this proposal develop." The NFU told us about members' concerns about the existing visa rules guaranteeing 32 hours: because of weather and crop conditions, "agriculture is inherently uncertain and it is not possible to guarantee on a week-by-week basis that work will always be available … Often a week or more of low activity can be followed by a period or periods of intense activity." In respect of the LPC's recommendation, their ask was for "an appropriate reference period which is fair both to employers and workers." NFU Scotland had similar concerns, asking that "considerations should be made to averaging out the minimum hours over a monthly basis, for all types of pay systems."

9.68 The BBPA told us that members were concerned that a minimum hours requirement "would add another level of bureaucracy into administrative systems." They quoted one member sceptical of our proposal: "Clearly, any team member having the accommodation offset deducted needs to work enough hours to ensure that they still have enough residual income to live off and where necessary commute to work. If they don't, they will simply leave and as we only provide accommodation to attract staff in the first place, any failure to provide sufficient remuneration for an employee using company accommodation would be fundamentally counterproductive. As such we are not persuaded that any minimum hours restrictions are really needed." Where a minimum number of hours was specifically mentioned, 20 hours was typically suggested as a minimum.

9.69 The EEA told us that "any minimum hours requirement in the equestrian industry may prove detrimental to part-time positions being offered. This is already a challenge within the industry as is the ability to work flexibly in general. Alternatively, it may lead to further non-compliance with NMW legislation where unlawful deductions are being made to cover the employer's accommodation costs."

There has been little progress on removing seafarers from the offset

9.70 The RMT noted the failure to enact our recommendations on the accommodation offset in maritime sector. They stated that "Worryingly, the employers' organisation UK Chamber of Shipping has objected to the LPC's recommendation … on the grounds that it is 'unfair.'"

The situation of domestic workers still requires attention

9.71 The WRC's submission noted that issues persist with the treatment of domestic workers, despite the removal of the family worker exemption, effective from 1 April 2024. The exemption stated that workers did not need to be paid the minimum wage if they lived with their employer and were treated as part of the family. It was originally introduced to facilitate au pair arrangements, but in light of extensive evidence that it provided a loophole for exploitation of live-in domestic workers, we recommended its removal in our 2021 Report (Low Pay Commission, 2021).

9.72 The delay in legislating to remove the exemption, the WRC argued, "by a simple statutory instrument no less, is an unfortunate reflection of the wider deprioritisation of the circumstances facing migrant domestic workers in the UK." WRC note that approximately 20,000 workers continue to arrive each year under the Overseas Domestic Worker visa, but although these workers are now entitled to the NMW, features of the visa and shortcomings in the wider employment law framework mean they continue to face exploitation. "Despite sustained calls for reform over a number of years, the government has not made any fundamental reforms to the structure of the ODW visa to address the exploitation that domestic workers face."

Conclusions

9.73 The number of underpaid workers rose in 2024. We estimate around 370,000 workers were paid less than the minimum wage in April 2024 – an increase of around 20,000 on the previous year although still below pre-pandemic levels. Because overall coverage jumped, underpayment as a share of coverage fell.

9.74 Stakeholders have suggested a wide range of ways to improve the NMW regulations and enforcement system. Employers most commonly complain about the lack of distinction between deliberate and inadvertent non-compliance, as well as the time and resource demands of NMW investigations. Unions call for a more central role in the enforcement process and note workers' lack of confidence in reporting underpayment. We note that the planned creation of the Fair Work Agency as a single enforcement body for employment rights represents an important opportunity to respond to the concerns of both workers and employers.

9.75 Linked to the growing number of salaried workers affected by the NLW, we have heard examples of employers preventing low-paid workers from using salary sacrifice schemes. Employers see this as an unintended consequence of the NMW rules. Worker representatives tend to view it more as a necessary protection against exploitation of workers. Survey evidence from the Chartered Institute of Personnel and Development showed that just over half of employers offer salary sacrifice, and just under 10 per cent had withdrawn it as a result of the NLW.

9.76 Our recommendations on the Accommodation Offset continue to be guided by the conclusions of our 2022 review. While many employers are dissatisfied with the current level of the offset, it is only a direct driver of their decisions in a minority of cases and workers argue the offset does not represent good value. We await responses from the Government to the recommendations we made in 2022.

Chapter 10

Looking forwards

Key findings

- **Future prices and wages are now key for our recommendations** – Our remit for 2025 says our NLW recommendations should take account of economic conditions; not allow the NLW to fall below two-thirds of median hourly earnings for those aged 21 and over; and take account of the cost of living (including expected inflation up to March 2026). Earlier chapters discuss economic conditions. This chapter shows how we've used forecasts to inform the other two aspects.
- **Multiple factors have raised our projection of median earnings in October 2025 –** So far in 2024 wage growth has been higher than forecast. This prompted forecasters to revise up their forecasts for 2024 as a whole and 2025. In addition, the ONS revised its method for estimating the distribution of wages in its Annual Survey of Hours and Earnings. This meant our estimate of the median hourly wage in 2023 was revised upwards, and the median for 2024 was higher than previously projected.
- **Our current central projection is that the NLW will need to rise to £12.21 in 2025 to be at two-thirds of median hourly earnings in October 2025 –** This forecast has increased from £11.84 in October 2023, £11.89 in March 2024, and £12.10 in August 2024.
- **An NLW of £12 in April 2025 should be enough to stay ahead of forecast growth in living costs –** We estimate that the NLW would need to increase to £11.95-£12.00 in April 2025 to maintain its April 2024 real value up to March 2026 – and £11.90-£11.96 to maintain its July 2024 real value, when the Government published its new remit for the LPC.
- **Our remit also includes taking steps to reduce the age of entitlement for the NLW to 18 years** – There are two ways of achieving this: increasing the 18-20 Year Old Rate until it aligns with the NLW; or gradually reducing the age of entitlement until everyone 18 and over is covered. We will consult on the appropriate way forward in early 2025.
- **There is scope to achieve this aim, but risks and trade-offs remain** – Even if we assume that the NLW remains at two-thirds of median earnings and there is a long transition period, the upratings required are historically large. This is because there is a large gap between the 18-20 Year Old Rate and the NLW (£2.84 in April 2024). There are greater risks in bringing 18-20 year olds into the NLW as they are more likely to be paid less than the NLW than those aged 21-22 were before they became eligible. The LPC remains of the view that there is scope to lower the age threshold to 18, but this should be done with caution, monitoring the impacts along the way.
- **The quality of the evidence base is a substantial problem –** The quality of the Labour Force Survey (LFS) makes it extremely difficult to evaluate NLW and NMW upratings with confidence. We recommend the Government improves our access to the RTI dataset alongside ongoing efforts to improve the LFS.

Future wages and prices are key for our NLW recommendations

10.1 Alongside economic conditions, our remit for the National Living Wage (NLW) in 2025 is to ensure it does not fall below two-thirds of median hourly earnings for those aged 21 and over, and to take account of the cost of living (including expected inflation up to March 2026). This latter part of the remit is part of the Government's ambitions for a genuine living wage.

10.2 In September we published a statement explaining how we would respond to the living costs aspect, which is new to the LPC's remit (Low Pay Commission, 2024c). In essence, the requirements to take account of living costs and not fall below two thirds of median pay act like "floors" to our recommendations. There is scope to recommend increases above the "floor" if the economic evidence supports this, and we would only recommend an NLW below the "floor" if this was necessary to avoid substantial negative outcomes. However, focussing on living costs is new for our remit and so our thinking may evolve over time.

10.3 To fulfil this part of our remit – i.e. to take account of living costs and stay above two thirds of median pay – we need to estimate what price levels and wages will be in the future. This chapter shows how we have done this.

Projecting median hourly earnings

10.4 From the day it comes into effect the NLW is fixed for 12 months, but median hourly earnings for the economy as a whole tend to continue growing. This means the bite (the value of the NLW relative to median earnings) peaks when a new rate is implemented on 1 April. But it then falls throughout the year as median earnings grow, reaching its lowest on 31 March each year. To avoid only hitting the target for a matter of days or weeks we have always aimed to hit the target threshold in each October. This means we include an extra 6 months of wage growth and so each April the bite is higher than the target and drifts down toward it by October. Doing this means the average bite of the NLW over the NLW year (1 April to 31 March) should be roughly equal to the target value.

Estimating the baseline

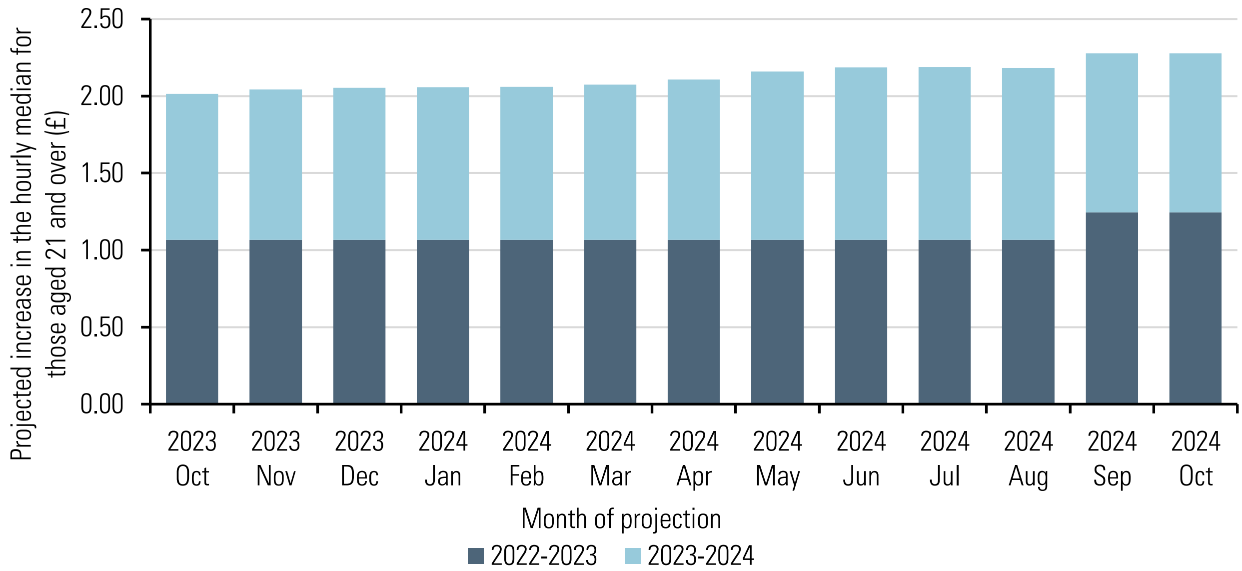
10.5 Our projection for what median earnings will be in October 2025 depends on two elements: our best estimate of the current median (the baseline); and wage growth between the baseline and the target date. The baseline estimate comes from the Annual Survey of Hours and Earnings (ASHE), the best measure of hourly earnings available. Our baseline is the median of gross hourly earnings, excluding overtime and any premia (for example, for shifts and unsocial hours) for those in the relevant age group. Since April 2024, the relevant age group is those aged 21 and over. In April 2024, the latest ASHE data available, we estimate the median for those aged 21 and over to be £17.19 an hour.

10.6 The Office for National Statistics (ONS) changed its ASHE methodology this year. First, it updated its population weights (which had a downward impact on the estimated median for 2023). Second, it addressed the issue of ASHE under-estimating the number of higher earners in the labour market, which was first noted by Henry and Joyce (2024). This had an upward and greater impact on the estimated median for 2023. The net effect of these revisions was to increase the ASHE estimate of median hourly earnings in 2023 for those aged 21 and over from £15.98 to £16.16. Figure 10.1 shows the impact of that revision with the median increasing by £1.25 (8.3 per cent) instead of £1.07 (7.1 per cent) between April 2022 and April 2023.

10.7 In October 2023, we expected median hourly earnings to increase by 5.9 per cent (95 pence), between April 2023 and April 2024. In August 2024, ahead of the publication of ASHE 2024, we revised this up to 7.0 per cent (£1.12) because wage growth turned out to be higher than expected. The out-turn was a little lower – the provisional data for ASHE 2024 show a £1.03 (6.4 per cent) increase in the median.

10.8 Taken together over the two years, the latest estimates from the ASHE data suggest a much stronger increase in the median between April 2022 and April 2024 (£2.28) than in any of our projections (£2.01 in October 2023, £2.07 in March 2024 and £2.18 in August 2024). That is, the baseline for our latest projections was significantly higher than we had previously forecast.

Figure 10.1: Projected change in median pay in ASHE, UK, 2022-2023 and 2023-2024



Source: LPC projections using ONS data and forecasts from the HM Treasury panel of independent forecasters and the Bank of England. Median of hourly earnings for those aged 21 and over, ASHE, annual, UK, April 2022-April 2024; Average weekly earnings total pay (KAB9), monthly, GB, May 2022-August 2024; Median of average wage growth forecasts from HM Treasury panel of independent forecasters, monthly, October 2023-October 2024, and conditioning assumptions on average wage growth from the Bank of England Monetary Policy Reports, quarterly, August 2023-August 2024.
Note: From August 2024, the Bank of England has used private sector instead of whole economy average wage growth.

Projecting future wage growth

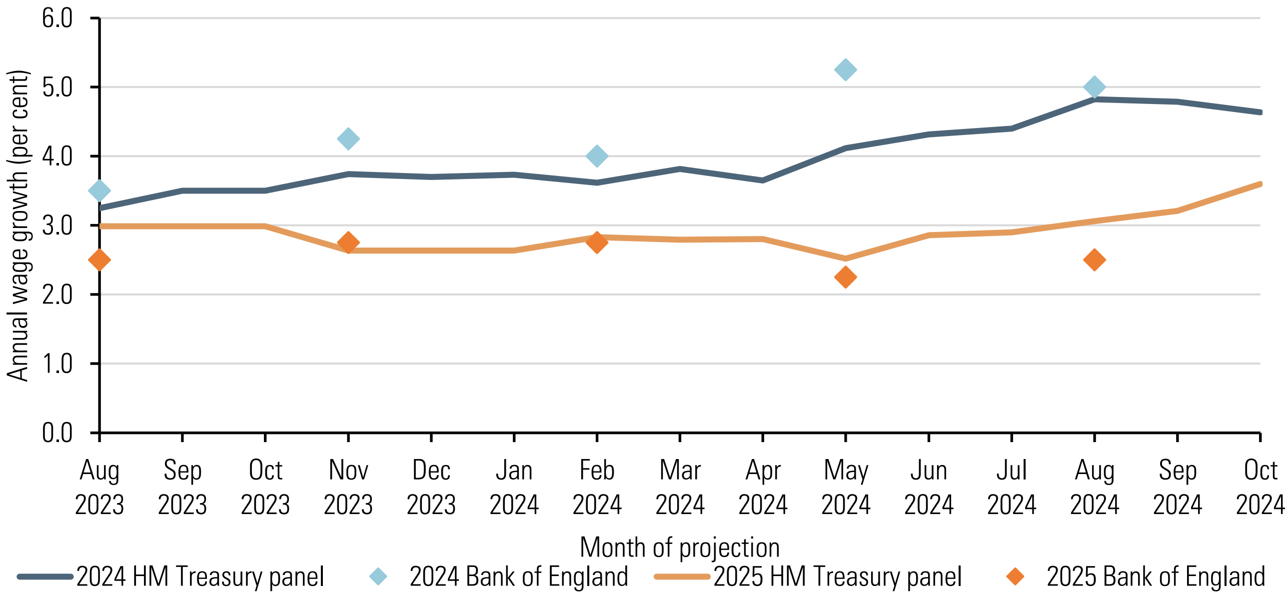
10.9 From our baseline in April 2024, we then project forward to the target date in two sequential periods: first, from April to August 2024 using Average Weekly Earnings (AWE) and second, forecast wage growth from August 2024 to October 2025. AWE is timelier and, in normal economic times, tends to move in line with ASHE. However, unlike our baseline median, it measures weekly, not hourly pay; covers all employees on the payroll irrespective of age and only covers Great Britain. We average the level over 12 months to remove some of the volatility around the timing of bonuses.

10.10 For the second part of our projection, we use forecasts of AWE wage growth to project median pay estimates forward from the latest available wage growth data (August 2024) until the target date (in this case, October 2025 or the fourth quarter of 2025). We combine forecasts from the monthly HM Treasury panel of independent forecasters with those from the most recent Bank of England Monetary Policy Report. The Office for Budget Responsibility (OBR) produce forecasts to coincide with fiscal events and so timely OBR forecasts are not available to us at the time we calculate the path.

10.11 The HM Treasury panel forecasts annual average (mean) weekly earnings growth to the fourth quarter of each year. This is a proxy – there is no forecast produced for median hourly pay. However, this forecast is consistent with the AWE measure we use in the model. We use the median of those forecasts made in the last three months. The median forecast of annual average wage growth available in October 2024 for 2024 Q4 was 4.6 per cent, slowing to 3.6 per cent in 2025 Q4, as shown in Figure 10.2. However, the range of forecasts had narrowed compared with the considerable uncertainty of the previous two years – down to a range from 4.0 to 5.3 per cent in 2024 and 2.6 per cent to 4.3 per cent in 2025.

10.12 Figure 10.2 shows how the forecasts for annual wage growth to Q4 2024 (blue line) and Q4 2025 (orange line) have evolved over the last 18 months or so. In October 2023, when we last made our recommendations, average wages were forecast to grow by 3.5 per cent to the end of 2024 and 3 per cent in 2025. Over the following six months the forecasts changed little. However, since the spring of 2024, they have been revised up. By October 2024, annual average wage growth was expected to be 4.6 per cent in the fourth quarter of 2024 and 3.6 per cent in the fourth quarter of 2025.

Figure 10.2: Annual average wage growth forecasts in Q4 2024 and Q4 2025 by month of forecast, UK, August 2023-October 2024



Source: LPC analysis using forecasts from the HM Treasury panel of independent forecasters and the Bank of England. Median of average wage growth (Tables 2 and 5) from the HM Treasury panel of independent forecasters, monthly, August 2023-October 2024 and the conditioning assumptions on average wage growth from the Bank of England (Monetary Policy Reports, August 2023, November 2023, February 2024, May 2024 and August 2024).
Note: From August 2024, the Bank of England has used private sector instead of whole economy average wage growth.

10.13 Compared with the forecasts available last autumn (October 2023), the variation in forecasts around the median has reduced but, as shown in Table 10.1, it was still greater than in the forecasts available pre-pandemic. This autumn, the forecasts for wage growth in the fourth quarter of 2024 ranged from 4.0 per cent to 5.3 per cent. That range (of 1.3 percentage points) was lower than for 2023 in autumn 2023 (2.8 per centage points) but still higher than observed pre-pandemic (0.5 percentage points in 2018 and 0.9 percentage points in 2019). This also held for the wage forecasts for 2025.

Table 10.1: Wage growth forecasts, UK, 2018-2025

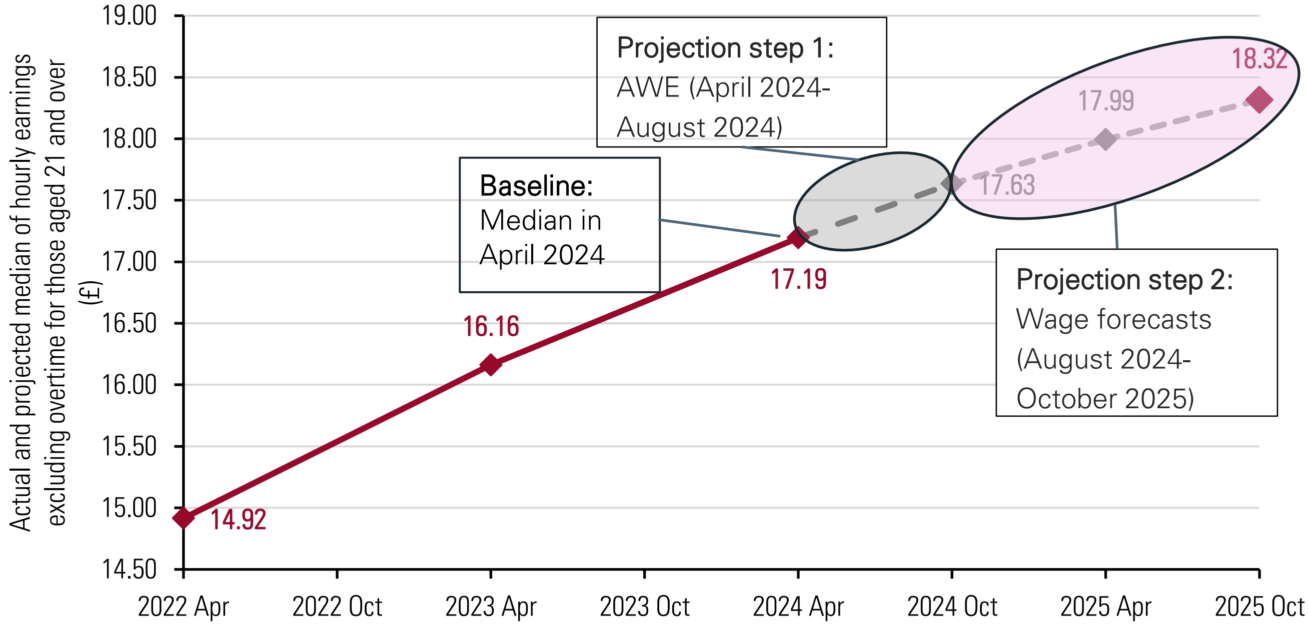
	Pre-pandemic				Post-pandemic			
HM Treasury panel and Bank of England (average wage forecasts)	HM Treasury and Bank forecasts (autumn 2018)		HM Treasury and Bank forecasts (autumn 2019)		HM Treasury and Bank forecasts (autumn 2023)		HM Treasury and Bank forecasts (autumn 2024)	
	2018	2019	2019	2020	2023	2024	2024	2025
Median	2.7	3.0	3.6	3.2	6.6	3.5	4.6	3.6
Mean	2.7	2.9	3.1	2.9	6.4	3.6	4.7	3.5
Minimum	2.4	2.0	2.9	2.6	4.9	2.1	4.0	2.6
Maximum	2.9	3.3	3.8	4.1	7.7	5.8	5.3	4.3
Range	0.5	1.3	0.9	1.5	2.8	3.7	1.3	1.7
Lower quartile	2.6	2.8	3.4	3.1	5.5	3.0	4.4	2.9
Upper quartile	2.7	3.1	3.7	3.5	6.9	4.3	5.0	4.0
Interquartile range	0.1	0.3	0.3	0.4	1.4	1.3	0.6	1.1
Bank of England (only)	2.5	3.3	3.0	3.3	6.0	3.5	5.0	2.5

Source: LPC analysis using average wage forecasts from the HM Treasury panel of independent forecasters (2018, 2019, 2023 and 2024 October) and the Bank of England (2018, 2019, 2023 and 2024 August).
Note: From August 2024, the Bank of England has used private sector instead of whole economy average wage growth.

10.14 Figure 10.3 plots the three stages discussed above. It shows that we currently project median hourly earnings for those aged 21 and over to increase from £17.19 an hour in April 2024 to £17.63 in October 2024, £17.99 in April 2025 and to £18.32 in October 2025. Two-thirds of the projected median in October 2025 is £12.21.

10.15 Two-thirds of the median in October 2024 is now projected to have been £11.76 (the latest observed median earnings data is from April 2024). That is 32 pence higher than the level of the NLW (£11.44) that we judged in October 2023 would meet that target. Around half of that difference was due to the revision in the ASHE 2023 data with the other half the result of stronger wage growth than forecast and upward revisions to the forecasts.

Figure 10.3: Actual and projected median hourly earnings for those aged 21 and over, UK, 2022-2025

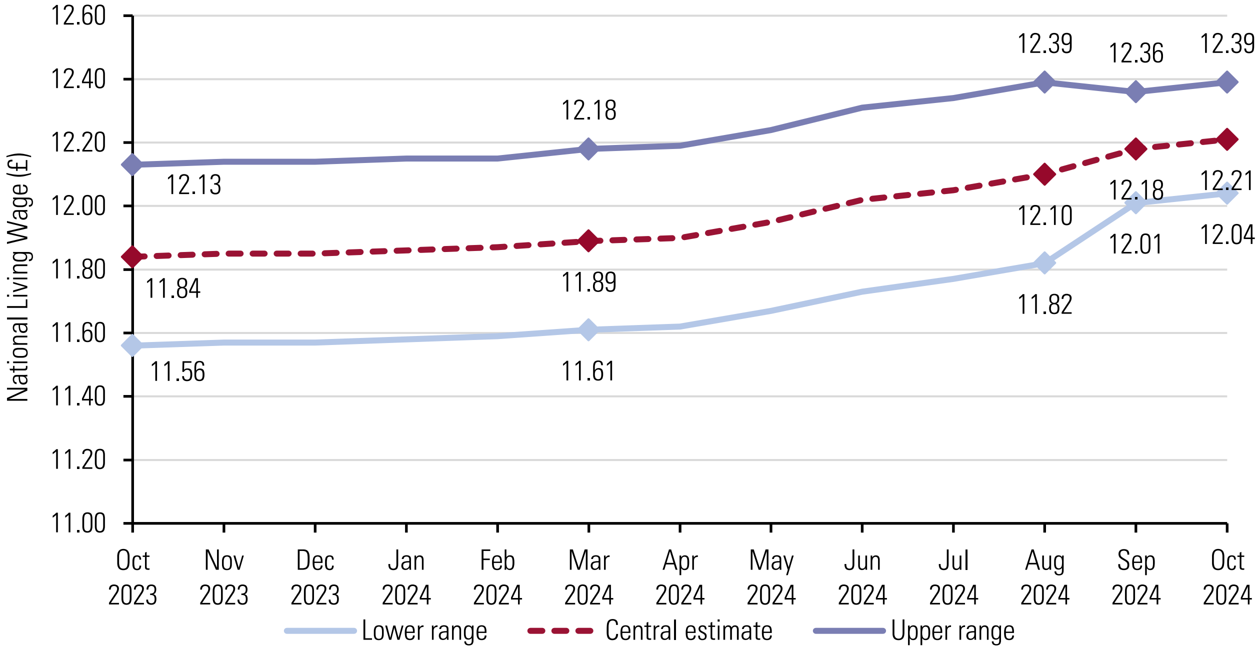


Source: LPC projections using ONS data and forecasts from the HM Treasury panel of independent forecasters and the Bank of England. Median hourly wage excluding overtime from the Annual Survey of Hours and Earnings for April 2022 (final), April 2023 (final) and April 2024 (provisional), standard weights, UK, 2022-2024; Annual wage growth derived from Average Weekly Earnings total pay (KAB9), seasonally adjusted, monthly, GB, April 2022-August 2024; Median of average wage growth (Tables 2 and 5) from the HM Treasury panel of independent forecasters, October 2024 and the conditioning assumptions on private sector average wage growth from the Bank of England (Monetary Policy Reports, August 2024).
Note: Projected wages use estimated median from ASHE (April 2024) as the baseline, then AWE wage growth (April-August 2024) and forecasts (August 2024-October 2025). For more information on projection methodology see Appendix 3.

10.16 Figure 10.4 plots our estimate of the value of the NLW needed to hit two-thirds median hourly earnings in October 2025 over time and therefore shows how it has responded to changes in data and forecasts. In October 2023, we projected that the NLW would need to be £11.84 in 2025. Reflecting the uncertainty, we calculated a range from £11.56 to £12.13 around this figure. We did this by allowing forecast wage growth to be ±1 percentage point higher or lower each year. Allowing wage growth to differ by ±1 percentage point to reflect the uncertainty in the forecasts, we obtained a range of £11.56 to £12.13 for our NLW estimate. One percentage point is greater than the usual difference between the forecast and outcome. We used 0.5 percentage points pre-pandemic, but uncertainty has greatly increased since then, particularly following the recent inflation shock.

10.17 Figure 10.4 also shows how the projected NLW needed to meet that two-thirds target has changed each month since last October. Wage data turned out stronger than forecast, and forecasts were revised up (as shown in Figure 10.2). As a result, our central projection increased in each of the last twelve months. We received pre-release access to the ASHE data in September, when the projection is revised up by 8 pence but the range narrows (as we no longer need to estimate wage growth from April 2023 to April 2024). In October 2024, it had reached £12.21 within a range of £12.04 to £12.39 using the ±1 percentage point approach.

Figure 10.4: Projected NLW in 2025 for those aged 21 and over, UK, 2023-2024



Source: LPC projections using ONS data (ASHE and AWE) and forecasts from the HM Treasury panel of independent forecasters and the Bank of England. Median of hourly earnings for those aged 21 over, ASHE, annual, UK, April 2022-April 2024; Average weekly earnings total pay (KAB9), monthly, GB, September 2021-August 2024; Median of average wage growth forecasts from HM Treasury panel of independent forecasters, (Tables 2 and 5), October 2023-October 2024, and the conditioning assumptions on average wage growth from the Bank of England, August 2023-August 2024.
Note: From August 2024, the Bank of England has used private sector instead of whole economy average wage growth.

Taking account of future inflation

10.18 Having considered the two-thirds floor, we now look at the implications of the second part of the remit for this year: taking account of the cost of living, including expected inflation up to March 2026. To do this, we need to use forecasts of consumer price inflation. To project to March 2026, we need quarterly forecasts of all the main official inflation measures discussed in Chapter 4. Unfortunately, of all the main official inflation measures discussed in Chapter 4, the only timely quarterly inflation forecasts are from the Bank of England and those are just for the Consumer Prices Index (CPI). The Office for Budget Responsibility produces forecasts for a range of quarterly inflation measures including CPI and the Retail Prices Index (RPI) but these are only published twice a year, with the latest available at the time of our recommendations dating from March 2024.[16]

10.19 The short-term forecast of CPI and RPI in the HM Treasury panel are only made from fourth quarter to fourth quarter of each year, while the medium-term forecasts are for the whole year. This requires us to make assumptions about the trajectory of those forecasts through the year to calculate price change to (any) March. To broaden our pool of quarterly forecasts, we wrote to each of the HM Treasury panel members. Nine gave us their CPI forecasts, but only seven went up to March 2026. This subset had a median that matched those in the HM Treasury panel for the appropriate quarters. We

[16] The OBR published new forecasts on 30 October, after we had submitted recommendations to the Government.

received just two that did the same for RPI – these produced a median that was slightly higher than that for the whole HM Treasury panel. As with RPI in general, we placed less weight on these given the small number of responses.

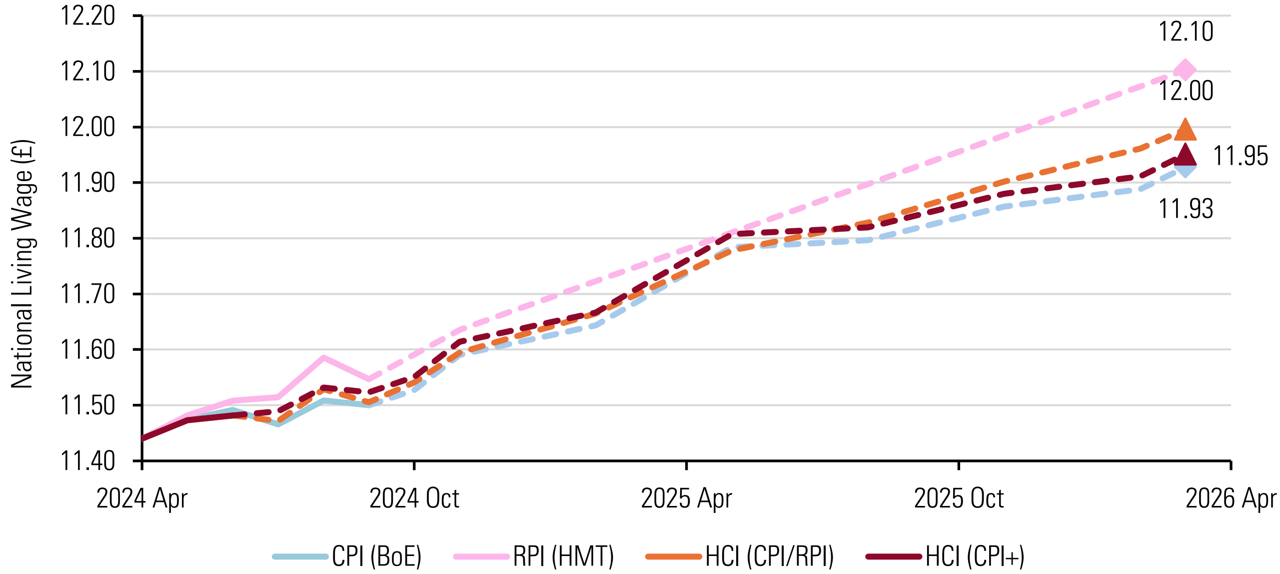
10.20 Unfortunately, there are currently no forecasts for the Household Costs Indices (HCI). However, we make use of the available CPI and RPI forecasts to project three different scenarios. The first is that HCI will increase in line with the CPI forecasts, the second is that it will increase midway between the CPI and RPI forecasts, and third that it will increase in line with its historic relationship with CPI (just a little faster than CPI).

10.21 We showed in Chapter 4 that the NLW had more than kept pace with the increase in inflation since 2019, including the energy price driven spike from April 2021. The remit asked us to at least maintain the real value of the NLW up to March 2026. Using our historic comparison of HCI and CPI as our forecast, we show that to maintain its April 2024 real value to March 2026, the NLW would need to increase to £11.95 in April 2025 (Figure 10.5). If HCI increased in line with the average of the CPI and RPI forecasts, then the NLW would need to be £12.00. The NLW would need to be £11.93 if using the Bank of England's CPI forecasts, but £12.10 if using RPI from the HM Treasury panel.

10.22 The actual remit notes that it should at least maintain its real value from the time we received our remit (July). In which case, the required NLW needed to maintain its real value by March 2026 would be slightly lower: £11.90-£11.96 for the HCI (depending on the approach used); £11.90 for CPI and £12.02 for RPI.

10.23 In conclusion, the NLW required to maintain its real value is less, on all measures of inflation considered here, than that required to ensure that it is no lower than two-thirds median hourly earnings.

Figure 10.5: Actual and projected real values of the 2024 NLW, UK 2024-2026



Source: LPC estimates using data from ONS and forecasts from the Bank of England and the HM Treasury panel of independent forecasters. Consumer price index (D7BT), retail price index (CHAW), monthly, April 2024-September 2024; Household costs index for all households (Table 23, Household Costs Indices for all households), monthly, April 2024-June 2024; CPI forecasts from Bank of England Monetary Policy Report August 2024 (market median from MPC forecasts of annual CPI inflation) and HM Treasury panel of independent forecasts (median from Tables 2 and 5 from August 2024 and Table M3 from October 2024); RPI forecasts from HM Treasury panel of independent forecasts (median from Tables 2 and 5 from August 2024 and Table M3 from October 2024).

Note: CPI (BoE) uses Bank of England market median to project the CPI path. RPI (HMT) uses the HM Treasury panel to project the RPI path. HCI (CPI+) projects HCI such that it grows in line with the historic relationship between HCI and CPI. HCI (CPI/RPI) projects HCI so that it grows in line with the average of the CPI and RPI projections.

Stakeholder views on the 2025 rate for the NLW

10.24 The majority of our evidence-gathering took place before the General Election on 4 July and before the new Government's publication of an updated remit on 30 July. Many of the submissions we received and the discussions we held with stakeholders were based on a different remit, published by the previous Government in March. We continued to meet with stakeholders from July onwards, and indeed our discussions from 22 May onwards were held in knowledge of the approaching election and the possibility of a change to our remit. This section on stakeholder views should be read with this background in mind.

10.25 We launched our call for written evidence in April. At this time, our central projection of two-thirds of median hourly earnings for October 2025 was £11.89, in a range of £11.61 and £12.18. We published an updated range in August, with a central projection of £12.10, in a range of £11.82 to £12.39.

Employers argued for a cautious approach

10.26 A range of employer representatives supported the on-course rate of £11.89. Many recognised the importance of the NLW (at least) keeping pace with inflation. The CBI stated that "from 2025, the NLW should be held, in the long run, at two-thirds of median income, with flexibility in the short term to respond to economic challenges and shield its real value from inflation." UKH supported the stance on two-thirds median earnings as "the right target … Now at this target, it is understandable that it should be maintained." Nevertheless, they told us that £11.89 "will likely lead to further price increases, and there is concern that it may lead to a decline in employment." Make UK noted that £11.89 reflected current pay growth across manufacturing and was significantly lower than increases in recent years. The FSB, FDF and BBPA each accepted that £11.89 was appropriate. The NFU supported the policy of keeping the NLW at two-thirds of median earnings, but argued the need for flexibility to take account of impacts on business. It noted that £11.89 "will be challenging for many businesses if increases in employment costs cannot be passed on through increased farmgate prices."

10.27 Other employers called for a slower or a cautious approach to increasing next year's NLW. The BCC stated its members needed breathing space to adjust to cost pressures, and recommended the NLW should rise in line with CPI, which it estimated would result in a rate of £11.68 in April 2025 and £11.93 in 2026. It argued this would demonstrate a prudent approach alongside a commitment to addressing income inequality and promoting fair wages while mitigating potential adverse effects on businesses, allowing firms to plan ahead. At oral evidence, REC argued that future NLW increases should allow employers "breathing room" or risk small employers failing to survive. Recent increases, it argued, had compounded businesses' struggles with other cost increases, especially in high coverage sectors like hospitality: "anxious is probably the word I would describe our members as being … The fear is that … margins won't be thin anymore, margins will be non-existent." It called for an increase at the lower end of the projected range published in March 2024.

10.28 ACS did not recommend a specific level for the NLW, but suggested a cautious approach would be welcome and advocated a principled approach rather than another target. The Scottish Grocers'

Federation (SGF) stated that "Wage costs are a large proportion of shop costs and substantial increases impact profitability, employment sustainability and business survival." They referred to the latest iteration of their "Real Cost of Employment" research, which estimates the total hourly cost of paying at the NLW as £15.39. They stated this work "is intended to show that the headline rate is one element, but there is a related, cascading cost increase to the business of the headline rate setting. These costs are unavoidable for the business but rarely receive a mention." SGF also mentioned a range of other costs in addition to the NLW ("energy, business rates and investing in regulatory changes") which were affecting the profitability and viability of businesses.

10.29 The NHBF urged caution and argued that rising minimum wages should be offset by Government support. The policy to keep the NLW at two-thirds of median earnings "should be monitored, evidence based and counterbalanced by further targeted support for employers."

10.30 One small cinema operator told us that the NLW was threatening its business viability. The recent increase had increased the wage bill for each site by around £200 per week; "now with the generous increase in the minimum wage taking money that we do not have, it really is very difficult to break even." Feedback from the UK Cinema Association was similar – trade was "still around 30 per cent down on pre-pandemic levels, and … significantly increased operating charges across a range of areas including utilities and staffing are calling into question the viability of an increasing number of cinema sites."

10.31 One large farming business told us that "When the NLW was introduced, I thought that was the end of our businesses, and that hasn't been the case – we've thrived, moved forward and become more productive." But at this point "there is no more productivity" and "our costs of production have clearly risen as a result of the NLW." They added "We really can't cope with it continuing as it is… the higher NLW than indicated this year has really seriously hurt us."

10.32 More than half of EEA employers responded to say that they would like to see the NLW remain at £11.44 per hour. NFU Scotland does not believe the NLW should increase at all in April 2025. It argued that for agricultural employers, there needs to be a similar uplift to the NLW in the price offered by supermarkets and consumers before any further wage increase will be viable.

10.33 The CBI argued for a broader range of NLW impacts to be considered as the labour market will remain tight for the time being. The CBI's submission argued that in recommending rates, the LPC should in the future focus on a greater range of risks and indicators, in recognition of "the new realities of the labour market". It advocated a "shift of focus … to formally include the range of economic implications of the NLW beyond unemployment … These include the demographic trends that will continue to squeeze labour supply and the pressing need to allow businesses the capacity to invest in the productivity growth that can drive real wages." This refocusing reflected the CBI's view that unemployment was unlikely to be a primary concern in the future: "The value of calibrating the trajectory of the minimum wage by the extent to which displaced workers become unemployed or find other jobs has been significantly weakened by the UK's demographic challenge. For the foreseeable future the demand for workers is likely to exceed supply." As such, the LPC should focus on other concerns, taking a holistic view of "the extent to which all policies, including the minimum wage, support or frustrate a transition to a higher-investment model for productivity-based growth – the difference between higher inflation and higher living standards." Given that "the levers to raise living standards sit elsewhere across government policy," the CBI argued the main priority should be "the need for government to support businesses in securing greater private investment."

Employee representatives and other stakeholders argued for ambitious increases

10.34 In contrast, unions argued for a steep increase to make up for the loss of real earnings. The TUC argued that falling NLW coverage showed there was scope for a higher rate, and that there was "no evidence that firms cannot afford higher minimum wage rates." It told us the two-thirds remit was not ambitious enough: "At the very least, we urge the LPC to make recommendations at the top of its forecast range. If wage growth turns out stronger than the central estimate implies, and the LPC is cautious in its recommendations, the bite of the minimum wage will fall. This would be unacceptable." The LPC should instead be asked "to make recommendations that raise the bite of the minimum wage as quickly as the evidence allows." In the longer term, the LPC "should be set a more ambitious remit so that we reach a £15 minimum wage as soon as possible." The TUC estimated this could be achieved by 2028, via a 75 per cent bite target. "The next increase in April 2025 must deliver a large real terms increase to ensure low-paid workers share the benefits of economic recovery."

10.35 Usdaw argued the NLW should be raised to £12 per hour as soon as possible, as a step towards a long-term ambition of £15. UNISON told us that sticking at two-thirds would be a "travesty," adding that "A minimum wage increase that merely tracked average earnings would condemn the UK's lowest-paid workers to likely further real terms cut in the value of their wages. Such an outcome would represent a travesty for a body designed to protect minimum wage workers' interests." UNISON recommended applying "the higher growth rate out of average earnings and cost of living as measured by the Retail Prices Index." The SWC advocated that "the NLW rate should be increased to the highest possible amount … This higher level would assist women working within low-paid sectors, allowing them increased access to better quality lives."

10.36 GMB called for the LPC to set out a pathway to a rate of at least £15 applicable to workers of all ages. Remaining at two-thirds median earnings "shows not only a lack of ambition but a lack of care for low-paid workers." It argued the LPC should also "account for historical and current changes to workers' living standards when setting a target pathway for minimum wage rates after 2025, in addition to average earnings and economic factors." Unite again referenced the report by Landman Economics submitted in 2022, setting out the benefits of a £15 per hour minimum wage. It argued this could be delivered without job losses, with substantial exchequer benefits as well as impacts on gender and racial equality. Unite reiterated that Landman Economics confirmed with them that "this analysis still holds and that there is still a powerful economic case for an increase in the National Living Wage to £15 per hour as soon as possible."

10.37 The Equality Trust argued that "increasing the NLW to £15 per hour would compensate low-paid workers who have suffered a lost decade and a half of real-terms wage increases." Respondents raised the impact of NLW increases on the public sector. Around 91 per cent of survey respondents from Organise believe the NMW should be £15 per hour. This was echoed by a retail worker we met in Glasgow who claimed, "£12 is nowhere near what it should be. To not worry, you need £15 per hour … You just can't afford to live now." Although some prices and bills were falling, he noted "they're not falling fast enough."

Reducing the NLW age from 21 to 18

10.38 In our remit, the Government told us that it was "committed to ensuring that every adult worker benefits from [a] genuine living wage" and that we should recommend "steps year by year in order to achieve a single adult rate". There are two main methods for reducing the NLW age of eligibility: lowering eligibility by one age year band at a time until reaching 18 years or increasing the 18-20 Year Old Rate until it aligns with the NLW.

10.39 Unions and charities have told us that they support a reduction in NLW entitlement to age 18, while the views of employers were more mixed. However, we have heard limited stakeholder views on how to make this change. We will consult stakeholders in early 2025 next year on the appropriate pace and approach to achieving this outcome.

10.40 There are some additional policy considerations that could impact our recommendations for 18-20 year olds in the coming years. In Chapter 6, we discussed the characteristics of 18-20 year olds that increase the risk of bringing them into the NLW when compared to 21-22 year olds. Other government policies could increase or reduce this risk. These policies include the level of ambition for the NLW and the Government's 'Youth Guarantee'.

Stakeholder views

10.41 Unions and charities have told us that they support a quick, evidence-based move to age 18. The Prince's Trust said that "The next step is for the NLW to cover all adults over the age of 18 where evidence allows, and we believe should happen as soon as economically suitable." Similarly, the Trades Union Congress (TUC) supports the goal of "expanding the NLW to cover workers of all ages as quickly as the evidence allows." The TUC said this could be done by "following the established pattern of extending the main rate down incrementally, and by recommending large increases to any remaining youth rates so they converge on the headline rate."

10.42 Employers' views on the change are more mixed. Make UK supports the change but told us that we should "consider staggering the implementation of a lower age threshold over a number of years. This could be reducing the threshold by one year every year, i.e. reaching 18 by 2027, to give employers visibility of the upcoming change." One large hospitality employer told us that while their organisation already paid the NLW regardless of age, the move to 18 "will detrimentally impact those smaller organisations if this comes as a fast, flat increase to the age [of eligibility]." The Federation of Small Businesses (FSB) said that lowering the age threshold to 18 would have a "fairly significant" impact on small businesses, with 44 per cent of small businesses that currently employ 18 to 20 year olds, or 28 per cent of all survey respondents, saying they would recruit fewer 18-20 year olds as a result of the change.

There are risks and trade-offs with lowering the NLW threshold

10.43 In our Beyond 2024 Report (Low Pay Commission, 2024b), we said that there is scope to reduce the age of eligibility for the NLW to age 18, but this should be done with caution. We remain of this view. However, even if we assume the NLW bite does not rise above two thirds of median pay and a long transition period, the increases required are substantial. Chapter 6 explains that the characteristics of 18-20 year olds mean the risks are greater than they were for lowering the age to 21. 18-20 year olds have lower median earnings and more of them are paid less than the NLW; they are more likely to be part-time student workers, and the required increases in their wage floor are far higher than was required for 21-22 year olds.

10.44 The level of the NLW affects the path to reducing the age of eligibility to 18. A more ambitious NLW will increase the ground to make up and the bite of the NLW for 18-20 year olds. Similarly, any significant increase in inflation could also mean that cost of living considerations lead to the headline NLW rising faster than expected.

10.45 These issues highlight the importance of the evidence base. Currently our understanding of the youth labour market is limited by the issues with the Labour Force Survey. In Chapter 11 we make recommendations on how the evidence base could be improved to help us provide robust advice to inform this policy.

10.46 Should the Government opt for another bite target as part of its approach to the genuine living wage, the interactions with the youth rates would need to be considered. Each younger age group that is included in the NLW lowers the median pay reference level, and therefore the level of the NLW required to hit the target. For example, projected median hourly pay in October 2025 is £18.32 for those aged 21+ and £17.96 for ages 18+. This means that a lower NLW age threshold in 2025 would have reduced the NLW rate required to reach two-thirds of median earnings by 24 pence (from £12.21 to £11.97).

Other policy changes will affect the ease of this transition

10.47 The Government has said that it intends to introduce a Youth Guarantee for 18-21 year olds that will provide opportunities to access training, an apprenticeship, or help to find work. Additional subsidy or support for employers to hire young workers could improve labour market outcomes for this group, making it easier for us to recommend increases to their minimum wage. We will pay careful attention to the detail of these and any other relevant policy changes once available, and their implications for the youth labour market and the transition of the NLW age threshold down to 18.

Conclusion

10.48 This chapter has considered the implications of the remit for the real and relative values of the National Living Wage. A range of factors led us to revise up our estimate of the NLW needed to hit two-thirds of median earnings for those aged 21 and over in 2025. These factors were stronger wage growth than forecast, which in turn led to forecasts themselves being revised up, combined with a methodological change to the wage data. Our central estimate is now £12.21 an hour within a range from £12.04 to £12.39.

10.49 Our remit also asked us to take into account the real value of the NLW up to March 2026. Using the available forecasts, we judge that an NLW of over £12.10 an hour would be more than sufficient to maintain its real value by March 2026.

10.50 After the large increases in the NLW in 2023 and 2024, employers generally argued for a more cautious approach to rate increases this year. In contrast, unions and employee groups saw scope for further increases to make up for the increase in prices in recent years. Opinions on reducing the age of entitlement to 18 were more mixed. Unions were unanimously in favour of doing so quickly, whereas there was a divergence of opinion among employers. However, even employers who supported the change thought it should be implemented gradually.

There are risks and trade-offs involved in lowering the NLW eligibility age down to 18. To achieve this by the end of the Parliament, historically large minimum wage increases are needed for 18-20 year olds. Doing this carries risks as this age group is more likely to be paid less than the NLW than those aged 21-22 were before they became eligible for the NLW. Including younger workers in the NLW also lowers the median wage and therefore the level of the NLW required to meet any bite target. However, the policy landscape, such as a Youth Guarantee for 18-21 year olds, could mitigate some of this risk.

10.51 The LPC remains of the view that there is scope to lower the age threshold to 18, but this should be done with caution, monitoring the impacts along the way. However, issues with the Labour Force Survey (LFS) make it difficult for us to identify the impacts. We recommend that HMRC provides more timely access to HMRC RTI micro data and implements its planned changes to employee hours data collection. This would allow us to better evaluate the impact of our recommended changes. Next year, we will consult on how best to lower the threshold and consider how the changing policy landscape affects the transition down to 18.

Chapter 11

Recommendations

Key findings

- **We recommend a National Living Wage (NLW) of £12.21 to apply from April 2025 –** Our new remit asks us to take account of workers' living costs, employers' trading conditions and the Government's aim for the NLW not to fall below two-thirds of median hourly earnings. Having done so, we recommend an NLW of £12.21 an hour should apply to those aged 21 and above (an increase of 77 pence or 6.7 per cent).
- **This is the rate required to meet the Government's ambition not to fall below two-thirds of median hourly earnings in 2025 –** In October 2023, when we made our recommendation of £11.44 for the NLW from April 2024, we expected that it would meet two-thirds of median hourly earnings in 2024. However, the combination of wage growth outstripping forecasts and the Office for National Statistics (ONS) changing the Annual Survey of Hours and Earnings methodology – our key data source on pay – meant that £11.44 fell short of this target.
- **We believe this rate is also high enough to take account of inflation up to March 2026 –** Because of the welcome return of real wage growth and forecasters' expectations that this will continue, we believe our recommended rate is sufficient to stay ahead of expected inflation on a range of measures up to March 2026.
- **We believe this NLW increase is consistent with the state of the labour market and the wider economy –** The labour market has loosened, but demand remains robust. And while some business conditions have deteriorated – with more firms worried about cash, debt and insolvency – others have improved. Labour shortages have reduced, and the growth in input costs has slowed. If interest rates fall in response to lower inflation, then this may further bolster economic growth, which is expected to be greater in 2025 than it was in 2024.
- **We recommend an 18-20 Year Old Rate of £10 an hour to apply from April 2025 –** Despite the large increase in the 18-20 Year Old Rate in April 2024, coverage for workers in this age group increased only slightly. Combined with strong wage growth, this suggests continuing healthy demand for this age group. Our recommended increase of £1.40 (16.3 per cent) is large enough to reduce the gap with the NLW, as specified in our remit.
- **We recommend the Apprentice Rate and 16-17 Year Old Rate to be £7.55 an hour from April 2025 –** These rates have been aligned for several years and we see no reason to decouple them at this time. The increase in the 16-17 Year Old Rate restores its value relative to the adult rate when it was introduced.
- **We recommend the Accommodation Offset rises to £10.66 per day from April 2025 –** This increase of 6.7 per cent, the same percentage as the NLW, is in line with the conclusion of our review of the offset in 2022, where we stated that "The value of the offset as a proportion of the NLW will not

increase significantly until we have some assurance that there are robust minimum standards in place for accommodation quality and that these are enforced. ”

- **Without improvements to the evidence base, our ability to give the Government the best advice we can is compromised –** Throughout this report we have highlighted problems with the data on which our advice is based. These problems make our job more difficult and our advice less credible. We make several recommendations on improving the Labour Force Survey (LFS); improving access to Real Time Information (RTI) employment data; introducing forecasts for the Household Cost Indices (HCI); and communicating further changes in evidence-gathering methodologies.
- **We recommend that the Government ensures the question of sleep-in shifts' entitlement to the minimum wage is addressed in the planned Fair Pay Agreement for the social care sector –** Care workers are not currently entitled to the minimum wage for these shifts, although there is a wide variety of practice. If there is to be a broader review of pay and employment conditions for care workers, this long-standing issue should be included.
- **We reiterate our previous recommendation that the Accommodation Offset should not apply to seafarers. We also recommend the Government look more widely at the entitlement to and enforcement of the National Minimum Wage (NMW) for seafarers.** This should include via full implementation of the Seafarers Wages Act.

The Low Pay Commission remit in 2024

11.1 The election of a new Government in July 2024 brought with it a new remit for the Low Pay Commission (Department for Business and Trade, 2024a). For the National Living Wage (NLW), there were three parts to this. We are asked to ensure that the NLW did not fall below two-thirds of median hourly earnings; to take account of the cost of living, including inflation to March 2026; and to take account of the impacts on businesses, competitiveness of the labour market and wider economy.

11.2 For those aged 18-20 we are tasked with narrowing the gap between their rate and the NLW, a process we began with last year's recommendations. The Government has also made plain its ambitions for the genuine living wage to cover all adults, which means the 18-20 Year Old Rate must eventually go. However, the Government has also asked us to consider the potential effects of such a change on young people's employment and their incentives to remain in education.

11.3 For those aged 16-17 and for apprentices, the remit remains the same as in previous years – to raise rates as high as possible without damaging employment.

Our recommendations

National Living Wage

11.4 In considering economic conditions we noted that GDP growth, while improved, is still fairly weak by historic and international standards and productivity growth remains subdued. At the time (October 2023) we made our recommendations for April 2024, the economy was expected to grow weakly in 2024 (around 0.4 per cent). However, growth in the first half of the year comfortably beat these projections. This led forecasters to more than double their growth estimates for 2024. They also expect growth to be higher still in 2025.

11.5 Despite this improved macroeconomic picture, the labour market has continued to loosen, with vacancies falling for the last two years and nominal earnings growth coming down from its high point in summer 2023. However, we believe this largely reflects an unwinding of the exceptionally strong levels of recruitment seen post-pandemic. Levels of vacancies and the vacancy rate remain similar to 2019, which itself was a period of tight labour markets when both measures were at or close to historic highs. In line with this, forecasters expect unemployment (on its International Labour Organisation definition) to remain at its historic low levels, albeit increasing slightly.

11.6 The low-paid labour market is in a similar position. April 2024 saw a second successive substantial increase in the NLW and the share of jobs covered by the NLW increased for the first time since it was introduced in 2016. However, coverage remains below pre-pandemic levels, despite the lowering of the age of eligibility to include 21-22 year olds from April 2024. The rate at which NLW workers moved into higher-paying employment, and the wage premium for doing so, both fell, but, again, remained above pre-pandemic levels. This suggests that the low-paid labour market has loosened to an extent, but remains robust.

11.7 However, this does not mean that employers, especially small businesses, have found it easy to respond to this large NLW increase. Employers in low-paying sectors are more worried about their cash reserves, debt obligations and risk of insolvency than those in other sectors. Few of them, though, are planning redundancies, and growth in input costs has slowed.

11.8 Employers are also concerned about pay differentials – the difference in pay between those on the wage floor and those just above them in the pay distribution, including their managers and supervisors. Differentials have been compressed in the low-paying industries and becoming increasingly so. Employers worry it is harming staff retention, recruitment and morale. Some workers have also told us that the reduction in differentials has reduced their incentives to progress.

11.9 Passing on the costs of the NLW increase to customers through price increases remained a common response among employers. Some, though, continued to say that there is a limit to how long this can go on, particularly as general inflation itself wanes. Some sectors remain constrained in their ability to pass on cost increases. Firms who compete internationally, and publicly-funded sectors like social care, local government, and childcare are less able to increase prices. While retail and hospitality sectors had been able to pass on costs through prices, they say their ability to do so now has diminished.

11.10 While inflation has slowed, workers and employers are keen to remind us that this just means that prices are now growing more slowly. It does not reverse the damage done to living standards in recent years. While energy prices have fallen, they are far higher than prior to the recent spike in inflation, as are the prices of food and other essentials. However, we are pleased to note that the NLW has increased in real terms since 2019.

11.11 Workers told us they are still suffering from the recent dramatic increases in the cost of living and have seen their spending power and living standards decline in recent years. While NLW upratings are appreciated they are seen as a partial mitigation at best. We also heard that insecure work is common and that it exacerbates this financial insecurity. Many workers told us about the difficulty of securing sufficient working hours.

11.12 Measures that the LPC recommended in 2018 (Low Pay Commission, 2018) may help with insecure and unpredictable hours of work. We recommended a right to an employment contract that reflects usual hours of work, to reasonable notice of work schedules and to compensation if a shift is cancelled or curtailed at short notice. So, it is gratifying to see these measures being taken forward through the Employment Rights Bill.

11.13 Our new remit asks us to balance the living standards of workers, business conditions for employers and the Government's aim for the NLW not to fall below two-thirds of median hourly pay. Taking all of this into account, **we recommend an NLW of £12.21 that should apply to those aged 21 and above (an increase of 77 pence or 6.7 per cent)**.

11.14 This (£12.21) is the level required to meet the Government's aim not to fall below two-thirds of median earnings. In October 2023, when we made our recommendation of £11.44 for the NLW in April 2024, we expected that it would meet two-thirds of median earnings in 2024. However, the combination of wage growth outstripping forecasts and methodology changes to the Annual Survey of Hours and Earnings (ASHE) by the Office for National Statistics (ONS) meant that £11.44 fell short of this target. As a result, there is ground to make up to reach this threshold in 2025, and an increase of 6.7 per cent is required to achieve two-thirds of median earnings in 2025. The combination of the larger than expected increase necessary to meet the Government's threshold and evidence of business conditions weakening in some sectors has led us not to recommend an NLW rate above two-thirds of median hourly earnings.

11.15 Because of the welcome return of real wage growth and forecasters' expectations that this will continue, we believe our recommended rate is sufficient to stay ahead of expected inflation on a range of measures up to March 2026 (see paragraph 11.34 and Figure 11.2). The labour market has loosened, but demand remains robust. And while some business conditions have deteriorated – with more firms worried about cash, debt and insolvency – others have improved. Labour shortages have reduced, and the growth in input costs has slowed. If interest rates fall in response to lower inflation, then this may further bolster economic growth, which is expected to be greater in 2025 than it was in 2024. We believe this increase is consistent with the state of the labour market and the wider economy.

Youth rates of the National Minimum Wage

11.16 The Government wants "every adult worker" to benefit from a "genuine living wage" and to lower the NLW age threshold to 18 years of age. Rather than make this change straight away, the remit suggests we should "take steps year by year" and in 2025 we should "continue to narrow the gap" between the 18-20 Year Old Rate and the NLW. In making this change, we are asked to take account of the effects on employment of younger workers, incentives for them to remain in training or education and the wider economy. Our remit for the youngest workers, those aged 16 and 17, is different again. Here we still have our traditional remit of pushing the wage as high as possible without damaging employment.

11.17 Last year we recommended ambitious increases for young people and apprentices and acknowledged some risk in doing so. However, while the labour market has softened for young people there is no robust evidence to suggest that last year's large increases have caused harm.

11.18 The increase for 18-20 year olds in April 2024 was the highest ever (£1.11 or 14.8 per cent) and has already started to close the gap with the NLW. With such a large increase we would expect coverage (the share of eligible jobs paid the rate) to increase in tandem, but it only increased very slightly. Also, effective coverage – those paid between their age rate and the NLW – has remained below pre-pandemic levels. Wage growth among this age group was strong. All of this is consistent with healthy demand for 18-20 year old workers so **we recommend an increase that continues to narrow the gap with the NLW, with a recommended rate of £10 an hour for 18-20 year olds (an increase of £1.40 or 16.3 per cent)**. We will consult next year on the appropriate pace and approach to eliminating the remaining gap, whether by raising the level of the 18-20 rate, lowering the age threshold or a combination of the two.

11.19 Following a substantial increase in the wage floor for 16-17 year olds (£1.12 or 21.2 per cent) in April 2024, coverage rates for this group rose to their highest ever level, though they remain below those for some apprentices and 21-22 year olds. Also, as wages more generally have been growing rapidly for these workers, the very large increase in their wage floor has only returned the bite (the ratio of the minimum wage to the median wage) to its pre-pandemic levels. **We recommend a rate of £7.55 an hour (an increase of £1.15 or 18 per cent)** that restores the 16-17 Year Old Rate to the relativity it had with the adult rate when it was introduced.

Apprentices

11.20 In our advice on the National Minimum Wage Beyond 2024 (2024b), we recommended that, in the long term, the Apprentice Rate changes to a simple discount of the appropriate age rate for apprentices aged 18 or over. However, we said that this should not happen at the same time as major changes to the youth rates. We also note the Government's intention to change policy on apprenticeships and the levy, which will have implications for the system in England. As such, we don't recommend significant change at this stage and the Apprentice Rate should stay aligned with the 16-17 Year Old Rate, so **we recommend a rate of £7.55 an hour for them also (an increase of £1.15 or 18 per cent)**.

Accommodation Offset

11.21 **We recommend increasing the Accommodation Offset in line with the NLW, to £10.66 a day (an increase of 67 pence or 6.7 per cent)**. This is in line with the conclusion of our review of the offset in 2022, where we stated that "*The value of the offset as a proportion of the NLW will not increase significantly until we have some assurance that there are robust minimum standards in place for accommodation quality and that these are enforced.*" In this context, we note the Government's announcement that they will consult on a new Decent Homes Standard for the rented sectors; we wait to see the details of whether this applies to the accommodation affected by the offset and our recommendations.

11.22 In 2022, we recommended that the Accommodation Offset should not apply to seafarers, noting their particular situation of being confined to their work premises which also happens to be their only available accommodation. We reiterate this recommendation. **We also recommend the Government look more widely at the entitlement to and enforcement of the National Minimum Wage (NMW) for seafarers, including via full implementation of the Seafarers Wages Act.** In particular, we note stakeholder representations on the situation of workers in the offshore renewables sector, who they tell us are currently excluded from the NMW.

Sleep-in shifts in social care

11.23 As discussed in Chapter 8, we feel the long-standing issue of care workers' entitlement to the NMW for sleep-in shifts deserves a fundamental review. **We recommend that the Government ensures the question of sleep-in shifts' entitlement to the minimum wage is addressed in the planned Fair Pay Agreement for the social care sector**.

Recommendations on the evidence base

11.24 Throughout this report we have highlighted problems with the data on which our advice is based. These problems make our job more difficult and our advice less credible. This is particularly important as we enter an important phase in the life of the minimum wage. We are closing the gap between the rates for 18-20 year olds and the NLW, a change that carries risk and so each step must be monitored and evaluated to avoid causing harm. The Government also has an ambition to create a genuine living wage. This too needs to be informed by the best evidence and advice.

11.25 Without improvements to the evidence base, our ability to give the Government the best advice we can is compromised. Equally, where the Government or the ONS are planning to improve sources of evidence, these must be communicated well in advance with those who make decisions based on that data. This will make it easier to plan for these changes and understand their potential impacts ahead of time.

11.26 To that end, **we recommend the following**:

- We recommend that the ONS work with all parts of Government that use the Annual Survey of Hours and Earnings to inform policy decisions, to ensure that they have advance notice of further methodological changes and the opportunity to agree the most appropriate time to make these changes.

- We urge the Government do all it can to enable the ONS to improve the Labour Force Survey as soon as possible and successfully transition to the Transformed Labour Force Survey.

- Robust econometric analysis is not possible with the Labour Force Survey in its current state. This means we cannot rigorously assess the impacts of changes to the minimum wage rates on employment and hours. Improved access to HMRC's Real Time Information could provide a partial alternative:

    i) We recommend that the Government provides us with an ongoing RTI dataset that covers all employment by minimum wage age group and low-paying sector for each local authority area in the UK since RTI data became available in 2014.

    ii) We recommend that the Government provide access to far more timely RTI micro-data through the HMRC Datalab and ultimately through the Integrated Data Service being established by ONS.

- The Government's focus on living standards has shown the need for improved forecasts of living costs. At the moment, we are not aware of any reputable forecasts for the Household Cost Indices (HCI). We recommend that the HM Treasury asks the OBR and its panel of forecasters to begin forecasting HCI inflation, particularly for lower income households.

Implications of the rates

The bite of the NLW should meet the two-thirds floor

11.27 We estimate that the bite of the NLW (the ratio of the NLW to median hourly earnings) will be 67.9 per cent when it comes into effect in April 2025. This is a 1.4 percentage point increase on April 2024. The increase in bite is a consequence of growth in the NLW (6.7 per cent) exceeding expected growth in median hourly earnings (4.6 per cent) between April 2024 and April 2025) (calculated as explained in Chapter 10). Over the course of the year, the bite of the NLW will decline as wages grow, reaching approximately two-thirds of median hourly earnings in October (the midpoint of the NLW year).

11.28 We also expect the bite of the youth rates to rise next year because of the significant increases in those rates. However, the projections in Table 11.1 are likely to overstate the increase in the bite for these rates. They assume that median pay grows by 4.6 per cent for every rate population. This is a reasonable assumption for the adult population (those aged 21 and over), but based on recent trends, it is likely to underestimate median pay growth for younger workers and apprentices. Since the pandemic, median pay has grown faster for younger workers than older workers. It is likely that median pay will again grow faster for younger workers and apprentices; however, we do not produce (or know of any other organisation that produces) an age-specific median wage forecast.

Table 11.1: Median hourly pay and bite projections, UK, 2024-2025

	April 2024			April 2025		
National Minimum Wage Rate	Rate	Median	Bite	Rate	Median	Bite
NLW (21+)	£11.44	£17.19	66.5%	£12.21	£17.99	67.9%
18-20	£8.60	£11.56	74.4%	£10.00	£12.09	82.7%
16-17	£6.40	£8.93	71.7%	£7.55	£9.34	80.8%
Apprenticeship rate	£6.40	£10.26	62.4%	£7.55	£10.73	70.4%

Source: LPC analysis of ASHE, standard weights, UK, Average Weekly Earnings and HMT panel of forecasts.

Notes:

a. This table shows projected medians and bite values for April 2025. The target for the NLW to hit two-thirds of median earnings refers to October 2025. We expect the bite of the NLW to fall back between April 2025 and October 2025 as median pay grows and the NLW rate stays unchanged.

b. This table shows our central projections of the median in April 2025. As discussed in Chapter 10 there is significant uncertainty around this projection.

We expect coverage to increase further over the next year

11.29 We expect the increase in bite to result in a further increase in the number and share of jobs paid up to 5 pence above the minimum wage, what we term coverage. These estimates are in Table 11.2.

11.30 We use two methods to forecast coverage. Under the first method, we assume that all workers' pay increases by 4.6 per cent (our projected increase in median pay outlined in Chapter 10). We then count how many jobs would be paid less than 5 pence above the relevant minimum wage. This method implicitly assumes that the increase in the minimum wage does not generate spillovers for other low-paid workers. As such we regard this estimate as an upper bound on the number of minimum wage jobs. Using this method, we estimate that coverage of the NLW could increase from 6.2 per cent this year to 9.8 per cent in 2025 – an increase of almost 1 million jobs. However, this is unlikely – by neglecting spillovers this method has consistently overestimated coverage.

11.31 The second method forecasts coverage based on the historic relationship between bite and coverage. We consider this method to provide a better indication of what coverage will be next year. It allows for spillover effects and doesn't require assumptions about the distribution of pay growth. However, it does assume that the relationship between bite and coverage is the same as it has been since 1999.

11.32 Historically bite and coverage increased together, but following the introduction of the NLW and again following the pandemic the relationship looked to have changed. After an initial jump in coverage that came with the introduction of NLW, coverage remained relatively stable despite ongoing increases in the bite. Following the pandemic, coverage fell despite significant increases in the bite. This was likely because of the tightness of the labour market, which resulted in stronger pay growth for low-paid jobs. This year, as a result of the increase in bite and with a loosening labour market, coverage increased in a way that was consistent with the historical relationship between coverage and bite. As a result, last year's estimate of the number of covered jobs using this method was accurate to within 20,000 workers. The second method projects the coverage rate of the NLW to increase to 6.9 per cent and the number of NLW jobs to increase to 1.92 million.

11.33 Similarly, we expect coverage under the youth rates to increase, although once again the estimates in Table 11.2 are likely to overestimate coverage in younger age groups. Like our bite projections, our coverage estimates rely on wages growing at the same rate on average in the younger rate populations as in the NLW population. In the recent past, hourly pay has grown faster among younger workers. We have not found a reasonable alternative way of forecasting coverage for these groups. We therefore use these forecasts as indicative numbers, but it should be noted they are likely overestimates.

Table 11.2: Projections for the number and share of jobs covered, UK, 2024-2025

	April 2024		April 2025: Method 1		April 2025: Method 2	
Rate	Share of jobs (%)	Number of jobs ('000s)	Share of jobs (%)	Number of jobs ('000s)	Share of jobs (%)	Number of jobs ('000s)
NLW (21+)	6.2	1,748	9.8	2,741	6.9	1,923
18-20	9.4	88	19.2	182	12.8	121
16-17	15.5	51	27.8	91	24.8	81
Apprenticeship	14.6	27	22.7	41	17.2	31
Total	6.5	1,914	10.4	3,055	7.3	2,156

Source: LPC analysis of ASHE, UK, 1997-2023. For more detail on projection method 2, see Low Pay Commission (2022) Chapter 10. This year we have updated our youth rates projections to use data on bite and coverage for each rate population between 2013 and 2024.

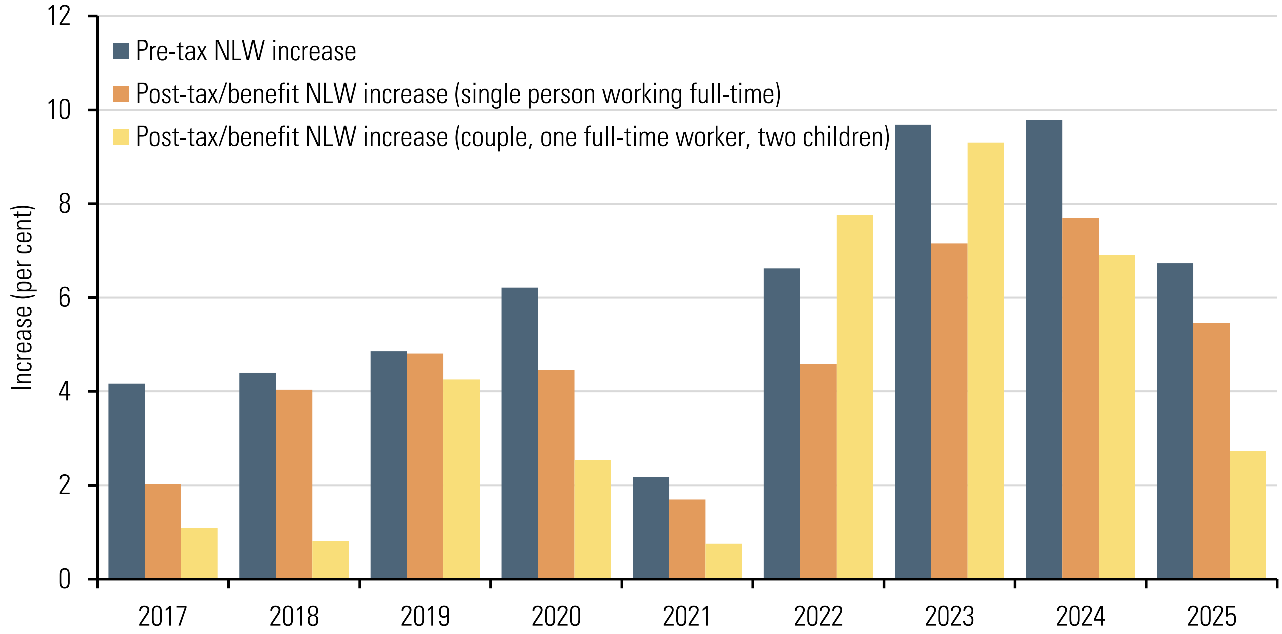
Note: This analysis assumes the total number of jobs remains the same between April 2024 and April 2025. It uses estimated job counts from ASHE, which may differ from other sources. Appendix 3 discusses our data sources in detail.

Implications for household income

Minimum wage rises will translate to increases in take-home pay

11.34 Although minimum wage workers will receive a 6.7 per cent increase in their hourly pay from April 2025, most minimum wage workers will see a smaller increase in their take-home pay. As shown in Figure 11.1 this is common in most years. This is because, generally speaking, as workers' incomes increase, their average tax rate increases and their benefits taper.

Figure 11.1: Projected pre-tax/benefit and post-tax/benefit increases in the NLW, England, 2017-2025



Source: LPC estimates using HM Revenue and Customs information on thresholds and rates.
Note: The analysis has been conducted for England. Income tax rates and thresholds vary in Scotland and Wales. Excludes auto-enrolment.

11.35 Table 11.3 sets out the earnings and household incomes for two example households with one full-time NLW worker. Although their earnings grow in line with the NLW (6.7 per cent), their take-home incomes only grow by 5.3 per cent and 2.7 per cent respectively. The precise outcomes for any particular household will depend on their circumstances, including whether they receive benefits, what benefit components they receive, how many members of the household work, and the number of hours they work.

Table 11.3: Household incomes for two examples households with a NLW worker, 2024/25-2025/26

25+ worker, 35 hour week on NLW	Level (pounds)		Change	
	2024/25	2025/26	Pounds	Per cent
Pre-tax hourly rate	11.44	12.21	0.77	6.7
Gross annual pay	20,878.00	22,283.25	1,405.25	6.7
Gross weekly pay	400.40	427.35	26.95	6.7
Single, working on NLW, no children				
Weekly deductions				
Auto enrolment contribution	14.04	15.38	1.35	9.6
National insurance contribution	12.67	14.83	2.16	17.0
Income tax	29.06	34.18	5.12	17.6
Weekly benefits	0.00	0.00	0.00	na
Net weekly income	344.63	362.96	18.33	5.3
Weekly post-tax/benefit change	-55.77	-64.39	-8.62	15.5
Hourly rate post-taxes/benefits	9.85	10.37	0.52	5.3
Couple, one working on NLW, 2 children				
Weekly deductions				
Auto enrolment contribution	14.04	15.38	1.35	9.6
National insurance contribution	12.67	14.83	2.16	17.0
Income tax	24.23	29.35	5.12	21.1
Weekly benefits	220.63	217.54	-3.09	-1.4
Net weekly income	570.10	585.34	15.24	2.7
Weekly post-tax/benefit change	169.70	157.99	-11.71	-6.9
Hourly rate post-taxes/benefits	16.29	16.72	0.44	2.7

Source: HM Treasury analysis, December 2024.

Notes:

a. Estimates that the household is in receipt of Universal Credit with no housing costs.

b. Estimates exclude Council Tax Support

c. "Average hourly rate" refers to the hourly rate when working 35 hours. This rate decreases as hours worked increases.

d. The 2024/25 scenarios are based on current policy as of Autumn Statement 2024.

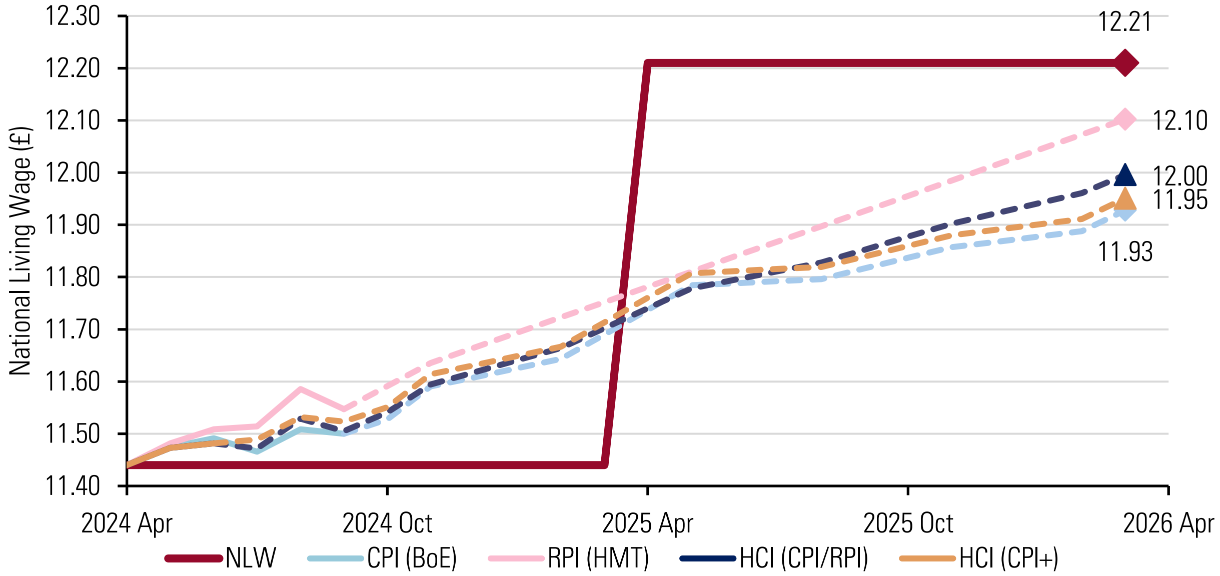
e. Estimates assume the couple in the examples are of the same age. In families with two children, the children are assumed to be aged 5 and 14. Child benefit is included in the calculations for families with children. It assumes the couple is married.

g. After-tax and benefit hourly rate is weekly household income after tax and benefits divided by hours worked.

Implications in real terms

11.36 In Chapter 4 we showed that the NLW had, so far, kept pace or exceeded a range of metrics of living costs. In particular, the NLW has risen faster than inflation since 2019. Using forecasts to roll this forward, we estimate that the NLW of £12.21 should stay ahead of predicted inflation up to March 2026, as per our remit. Figure 11.2 compares the nominal value of the NLW to what it would be in March 2026 if it was instead uprated by forecast inflation (see Chapter 10 for more detail on this). This chart shows that any NLW rate above £12.10 would be sufficient to keep ahead of a variety of inflation forecasts. The rate of £12.21 is more than sufficient. As the other rates of the minimum wage saw larger percentage increases than the NLW, they too will likely stay ahead of predicted inflation.

Figure 11.2: NLW uprated in line with various forecast inflation measures, April 2024-March 2026



Source: LPC estimates using data from ONS and forecasts from the Bank of England and the HM Treasury panel of independent forecasters. Consumer price index (D7BT), retail price index (CHAW), monthly, April 2024-September 2024; Household costs index for all households (Table 23, Household Costs Indices for all households), monthly, April 2024-June 2024; CPI forecasts from Bank of England Monetary Policy Report August 2024 (market median from MPC forecasts of annual CPI inflation) and HM Treasury panel of independent forecasts (median from Tables 2 and 5 from August 2024 and Table M3 from October 2024); RPI forecasts from HM Treasury panel of independent forecasts (median from Tables 2 and 5 from August 2024 and Table M3 from October 2024).
Note: CPI (BoE) uses Bank of England market median to project the CPI path. RPI (HMT) uses the HM Treasury panel to project the RPI path. HCI (CPI+) projects HCI such that it grows in line with the historic relationship between HCI and CPI. HCI (CPI/RPI) projects HCI so that it grows in line with the average of the CPI and RPI projections.

Conclusions

11.37 The labour market has loosened, but demand remains robust. And while some business conditions have deteriorated – with more firms worried about cash, debt and insolvency – others have improved. Labour shortages have reduced, and the growth in input costs has slowed. If monetary policy loosens and interest rates fall in response to lower inflation, then this may further bolster economic growth, which is expected to be greater in 2025 than it was in 2024.

11.38 Therefore, we recommend an NLW of £12.21 that should apply to those aged 21 and above (an increase of 77 pence or 6.7 per cent). This is the rate required to meet the Government's ambition not to fall below two-thirds of median earnings. Because of the welcome return of real wage growth and forecasters' expectations that this will continue, we believe our recommended rate is sufficient to stay ahead of expected inflation on a range of measures up to March 2026. We believe this increase is consistent with the state of the labour market and the wider economy.

11.39 We believe labour market conditions for young people were consistent with fulfilling the remit aim to reduce the gap between the NLW and the 18-20 Year Old Rate, and for us to return the 16-17

Year Old Rate back to the relative value it had to the NLW when it was introduced. Further, we saw no need to decouple of the Apprentice Rate from this rate.

11.40 In short, these recommendations meet all aspects of the remit and should deliver gains relative to the cost of living for all minimum wage groups.

Appendix 1
Consultation respondents

A1.1 We are grateful to all those people and organisations that contributed to the preparation of this report. We would like to thank, in particular those who provided evidence, either written or oral, and those who organised or participated in Low Pay Commission visits and meetings. All such individuals and organisations are listed below, unless they expressed a wish to remain unacknowledged.

ACH Farming

Association of Colleges

Association of Convenience Stores

Association of Directors of Adult Social Services

Association of Labour Providers

Avante Care & Support Ltd

Avondale Care Home

Baby Box IOW

Booksellers Association

British Beauty Council

British Beer & Pub Association

British Chambers of Commerce

British Hair Consortium

British Printing Industries Federation

British Retail Consortium

Card Factory plc

Cardiff Council

Care England

CBI

Centre on Household Assets and Savings Management (CHASM), University of Birmingham

The Chartered Institute of Payroll Professionals (CIPP)

Chartered Institute of Personnel and Development (CIPD)

Christians Against Poverty

Citizens Advice Isle of Wight

Community Leisure UK

Community Trade Union

Community Transport Association

Deloitte LLP

Denroy Group Limited

Donna Ankers

Dover Big Local

Dunelm

Early Years Alliance

East Midlands Chamber

Edinburgh Living Wage City Action Group

End Child Poverty Coalition

Equality Trust

Equestrian Employers Association

Federation of Small Businesses

Federation of Wholesale Distributors

Focus on Labour Exploitation (FLEX)

Food and Drink Federation

GMB Union

GoI Centres Ltd

Greggs Plc

The Hair & Barber Council

Hampshire Chamber of Commerce

Henry Scrope

HM Government

Homecare Association

Horticultural Trades Association

Hospitality Ulster

Incomes Data Research

Independent Retailers Confederation

Institute for Fiscal Studies

Intergenerational Foundation

Joseph Rowntree Foundation

K2 Architects

Kent Invicta Chamber of Commerce

The King's Trust

Labour Research Department

Leaf Hotels Group

Living at Home UK

Living Wage Foundation

Local Government Association

Low Incomes Tax Reform Group

Make UK

McMullen & Sons

Michael Nisbet

Money Advice Scotland

National Care Forum

National Council for Voluntary Organisations

National Day Nurseries Association

National Farmers' Union

National Fast Food Association

National Federation of SubPostmasters

National Hair & Beauty Federation

National Institute of Economic and Social Research

National Union of Rail, Maritime and Transport Workers

NFU Scotland

Nicola Alison

One Stop Dumbarton Road, Glasgow

One Stop Stores Limited

Organise

Papworth Trust

Professor Deirdre McCann, Durham Law School, Durham University

Public Health Wales

PureCyber Limited

Recruitment & Employment Confederation

Red Hen Cookery

Resolution Foundation

Royal Mencap Society

Scottish Grocers' Federation

Scottish Women's Convention

Shaw Healthcare

Skills for Care

Sutcliffe

Tees Active Limited

The People Director Partnership

Tony Catherall

Trades Union Congress

UK Cinema Association

UKHospitality

Ulster Farmers' Union

Union of Shop, Distributive and Allied Workers

UNISON

Unite the Union

The University of Leeds

White Horse Child Care Ltd

Wm Morrison Supermarkets Limited

Women's Budget Group

Work Rights Centre

XpertHR

Young Women's Trust

Youth Employment UK

Zell

Appendix 2

Research evidence

A2.1 The pandemic and its consequences, alongside ongoing issues with data quality continue to affect our ability to assess the impact of recent minimum wage increases in the UK, particularly on earnings, employment and hours. Policies to control the pandemic, such as furlough and the restrictions imposed on businesses, affected estimates of earnings and employment. They also made it almost impossible to distinguish the impacts of increasing the minimum wage from those resulting from the pandemic (and measures to control it). Many of the most affected businesses were also ones with a greater share of minimum wage workers. Lockdown measures were gradually eased after the spring of 2021 with the Coronavirus Job Retention Scheme (or furlough) officially ending on 30 September 2021. This not only affected the data up to that date, it also directly affects pay and job growth data up to November 2022 (official headline pay and job growth estimates are derived using three month averages on the year before). Thereafter, concerns about earnings and employment estimates should have resolved.

A2.2 However, these issues have been compounded by the deterioration in the quality of our main data sources on pay and employment. Response rates to the Labour Force Survey were already causing concerns prior to the pandemic but these fell further as the method of collection moved away from face-to-face interviews to telephone interviews. Sample sizes, particular for certain groups, such as young people, made it increasingly difficult to conduct robust analysis. Indeed, these concerns came to the fore when the Labour Force Survey (LFS) data were not released in the third quarter of 2023. ONS has since implemented measures to boost response rates and increase sample sizes. However, despite these improvements, there are still concerns about the quality of the findings produced and our ability to use these in our research.

A2.3 Data quality concerns have also affected our main source of information on earnings – the Annual Survey of Hours and Earnings (ASHE). Although response rates have improved, they remain below what they were pre-pandemic. Two main issues have been highlighted by research findings – biases from firm non-response; and the underestimation of high-earners. In a series of papers, the Wages and Employment Dynamics project (2021, 2022a, 2022b, 2022c, and 2023b) looked at the implications of the response biases on estimates of pay and minimum wage coverage. Henry and Joyce (2024) highlighted issues with ASHE sampling of higher earners since the pandemic and the resultant underestimation of pay growth. The latter issue was addressed by ONS in a partial review of its methodology this year. This resulted in large revisions to the ASHE earnings data in 2023 and 2024. A full review of the methodology, that will also address some of the issues raised about non-response bias, is ongoing but we do not expect any findings to be implemented from that before 2026. The issues with the data are described in more detail in Appendix 3.

A2.4 Although new data sources, such as HMRC Real Time Information (RTI) and the Business Insights and Conditions Survey (BICS) from the Office for National Statistics (ONS), have been developed and provide timely new information and useful insights, they are not replacements for the detail contained in the LFS and ASHE required for our econometric analysis.

Commissioned research

A2.5 For this report, we commissioned three external research projects which all used data prior to the pandemic: Frontier Economics looked at minimum wages and monopsony in the UK labour market; London School of Economics investigated the impact of minimum wages on alternative work arrangements; and the Institute for Fiscal Studies assessed the impact of the introduction of the NLW on firms' wage distributions, pay practices and use of alternative contractual arrangements. In addition, we have also undertaken some econometric analysis in-house to look at the initial impact of the most recent uprating in April 2024. The data sources, methodology and key findings of these three projects are summarised in Table A2.1.

Monopsony, minimum wages and the UK labour market

A2.6 In a perfectly competitive market, the elasticity of labour supply facing individual firms (workers' responsiveness to a change in wages) is infinite (in other words, even a slight reduction in wages will cause all of its workers to leave to work for other employers) and the wage equals the marginal product of labour. Under these conditions, classical labour theory predicts that, as long as the minimum wage is binding, any increases in the minimum wage should unambiguously lead to a negative effect on employment and total hours worked.

A2.7 Previous empirical work on the employment effects of increases in minimum wages has tended to show negligible or null impact on employment levels and some modest impact on total hours worked (Manning (2021a), Clemens (2021), Jardim, Long, Plotnick, van Inwegen, Vigdor, and Wething (2018), Dube, Lester and Reich (2010), Dickens and Draca (2005), and Card and Krueger (1993)). Various explanations have been offered for this, including that the minimum wage level has not been binding, or that businesses adjusted to NLW increases through other channels.

A2.8 One explanation for the elusive employment effects of minimum wage increases has been the role of monopsony power in labour markets. Manning (2021b) found strong evidence that the labour market in developed countries deviates from a simple perfectly competitive framework and that there is substantial variation across industries, occupations and geographical regions. Bell and Tomlinson (2018) examined product and labour market concentration in the UK since the early 2000s. They found that labour market concentration was substantially higher in low-paying sectors and for low-paid workers compared with the rest of the UK economy. This suggested that labour market concentration, characterised by limited employment options may disproportionately affect low-paid workers. Araki, Bassanini, Green, and Marcolin (2023) in their study of OECD countries estimated that rural labour markets were more concentrated than urban ones in the UK. However, they also found that the UK labour market overall was less concentrated than the OECD average.

A2.9 Recent studies in the US (such as Munguia-Corella, 2020, and Azar, Berry, and Marinescu, 2022) have explored the relationship between minimum wages and measures of employment concentration as a proxy for monopsony power. They found that increases in the minimum wage significantly decreased employment in low concentration markets but become less negative (and even positive) as labour market concentration increases. Studies in the UK (such as Manning and Petrongolo, 2022, Abel, Tenreyno, and Thwaites 2018, Manning and Petrongolo, 2017) have tended to focus on the measurement of monopsony power in the labour market and its impact on average wages rather than minimum wages.

A2.10 In more recent research in the UK, the Competition and Markets Authority (2024) analysed labour market concentration in the UK economy, and explored the relationship between employer power, labour market institutions and outcomes. It found no evidence of increased employer market power or labour market concentration in the UK over the last twenty years. However, it identified large and persistent differences in both measures across regions, occupations, and firms. It found some evidence that monopsony power played a role, as workers in more concentrated labour markets tended to earn lower pay. Additionally, in high concentration (less competitive) labour markets, employment appeared less sensitive to minimum wage increases. Datta (2024) looked more generally at monopsony in the UK labour market. He found that commutes generated considerable spatial heterogeneity in monopsony power, accounting for approximately a third of the total wage markdown. He estimated that a minimum wage worker would require an extra £0.37 per hour for an increase in commuting time by five minutes. He also demonstrated that around 40 per cent of spatial variation in monopsony power was within Travel-To-Work-Areas (TTWAs), highlighting the importance of spatial definitions for measures of concentration.

A2.11 Frontier Economics (2024) explored role that imperfect competition in the labour market can play in explaining employment effects (or lack thereof) associated with minimum wage increases. In particular, it investigated the link between different degrees of market concentration and minimum wage effects on the number of workers in low pay employment, total weekly hours worked among low pay workers, average hours per worker among low pay workers, and base hourly wages among low pay workers.

A2.12 It estimated its labour market concentration measure using data on employment, geography and industry from the Business Structure Database (BSD) – an annual abstract from the Inter-departmental Business Register (IDBR), which covers VAT and PAYE-registered firms (around 96 per cent of all firms in the UK). The BSD has information at the workplace (local unit) and firm (enterprise unit) level. The Annual Survey of Hours and Earnings (ASHE) was used to estimate various measures of pay, hours worked and employee numbers. These measures were derived for each TTWA in England and Wales between 2015 and 2019. The researchers also added an industrial dimension, using 4-digit Standard Industrial Classification (SIC) codes, to their definition of local labour markets. A methodological contribution of this study was to use a novel data-driven sectoral definition of low-pay labour markets, which grouped sectors together based on the volume of low-pay job switches/moves across sectors. This analysis identified nine industry clusters. The data for 2020 and 2021 are affected by the furlough schemes that operated to support incomes during the pandemic.

A2.13 The study found evidence that, following an increase in the minimum wage, employment and total hours increase in high employer concentration areas relative to in low concentration areas. This finding aligns with previous work, and with the theoretical discussion of the interaction between monopsony and minimum wage effects. However, the magnitude and statistical significance of the results are sensitive to the model specification. This is likely due to the generally low employer concentration in low-pay labour markets, on its measure of concentration.

A2.14 The research found no clear pattern in hours worked per low-paid worker and in base wages across sectors with respect to monopsony and minimum wage effects. However, it provided robust evidence that the introduction of the NLW increased hourly wages for low-paid workers in both high and low concentration labour markets.

A2.15 Its findings show that the results are sensitive to geographic definitions of local labour markets. The researchers concluded that monopsony likely interacts with minimum wage effects differently across different sectors and occupations, due to differences in public sector employment, in the elasticity of hours per worker, in the geographic distribution of different sectors, and other factors.

A2.16 The finding of low-employer concentration in most sectors of the low pay labour market suggested that future work on monopsony effects could usefully focus on sectors or local areas with higher-employer concentration. We noted that the extent of monopsony might not be picked up by the data available as even TTWA may not be disaggregated enough. Datta (2024) has explored different spatial definitions. Further, research by YouGov (2023) suggested that there are reasons other than concentration of employers that prevent workers from moving jobs and thus enabling some degree of monopsonistic power to employers even in low concentration areas.

A2.17 Having considered the impact of the minimum wage across geographies, we now look at research that also makes use of geography to assess the impact of the NLW on work arrangements.

Minimum wages and alternative work arrangements

A2.18 Empirical study of minimum wages has evolved in recent years to consider margins of adjustment that go beyond the employment effects that the majority of research traditionally studied. However, there is a limited literature on the use of alternative work arrangements (such as variable hours and zero hours contracts, temporary or work agency contracts, involuntary part-time work and solo self-employment) as methods of adjustment. Boeri, Giupponi, Krueger and Machin (2020) reported that the use of these types of alternative work arrangements had been rising across the OECD in recent years. Low-paid workers were shown by Cominetti, Costa, Datta, and Odamtten (2022) to be more likely to be employed through these alternative work arrangements, and that such contracts were heavily characterised by job insecurity and hours insufficiency. However, there has been little research into whether increases in the NLW have incentivised the use of self-employment or had an impact on the type of work arrangements used by employers.

A2.19 We commissioned two research projects for this report that address that evidence gap. The first, Albagli, Costa, and Machin (2024), looked at how labour market dynamics and alternative work arrangements feature in these different margins of adjustment that can impact workers and firms. The study primarily focused on the introduction of the National Living Wage in April 2016 in the UK and exploited variation in pre-policy exposure to minimum wages across different regions and ages, in a similar vein to Manning (2016), Dube (2019), and Butcher and Dickens (2023), as a means to estimate the causal effects.

A2.20 The study began by confirming the significant wage effects from the NLW that feature in earlier research. Wage boosts from the minimum wage were found, especially for workers in low-paying industries. While there is no overall negative employment effect from the NLW introduction, there are some negative and positive estimated effects on the net stock change of unemployed and inactive individuals.

A2.21 One key part of the report delves into the effects on labour market flows. The finding of a decrease in the probability of being unemployed is primarily driven by increased job retention, marked by substantially lower flows to unemployment, predominantly fuelled by a decrease in involuntary separations (i.e. layoffs). This decrease in layoff probabilities is notably pronounced among those facing job loss after the termination of a temporary contract. The reduction in layoff probabilities aligns with the findings of Brochu and Green (2013) in Canada and Dube, Lester and Reich (2016) in the US, but there is no evidence of significant reductions in voluntary separations or job-to-job transitions.

A2.22 Additionally, there is no evidence of changes in on-the-job search. Furthermore, it turns out that a substantial part of the employment retention effect is observed among those on full-time contracts. At the same time, in line with a strong income effect occurring among those remaining in part-time employment, positive effects are estimated in both the probability of reporting voluntary part-time and the probability of transitioning from voluntary to involuntary part-time without an increase in hours worked.

A2.23 Consistent with these findings of altered transitions for full-time and part-time workers, the chances of a worker reporting to be underemployed fell as a result of the policy sustained by reduced flows from non-underemployment to underemployment and non-employment. Additionally, modest effects of workers moving from variable to fixed-hour contracts are also seen.

A2.24 The other major part of the report focuses on other job attributes and contract features to provide an understanding of adjustment margins related to alternative work arrangements. Whilst there is no evidence of minimum wage policy pushing workers into self-employment, the incidence of zero-hour contracts increased among those most exposed to the minimum wage, a finding consistent with the earlier work of Datta, Giupponi and Machin (2019).

A2.25 Overall, the combined effects of increased flows from variable to fixed hours, temporary to permanent positions, and enhanced job retention of full-time workers result in an overall reduction in what the OECD classifies as non-standard work arrangements. The researchers concluded that these potentially favourable effects for hours sufficiency and job security primarily benefited low-tenured incumbents, raising questions about the net benefits for firms' productivity, profitability, and workers' career progression opportunities, which they argued required further evaluation.

A2.26 Our final research project also investigated some aspects of the impact of minimum wages on alternative contractual arrangements, as well as assessing the impact of the introduction of the NLW on firms' wage distributions and pay practices.

Minimum wages, firms' wage distributions, pay practices and alternative contractual arrangements

A2.27 As we noted above, most minimum wage research has focused on the impact on wages and employment. In general, this research has found that minimum wages increase wages with limited effects on employment. But much less is known about how firms adjust their organisational and pay structures in response to the minimum wage. Qualitative evidence suggests that employers are worried about the NLW narrowing pay differentials between low-paid workers, or having to incur significant additional costs to maintain current differentials (Low Pay Commission, 2024a). The extent to which firms adjust their pay and organisational structures will play an important role in determining the outcomes of those earning at or near to the minimum wage. Giupponi, Ray-Chaudhuri and Xu (2024) provided an assessment of how firms changed their pay and contractual practices in response to the higher wage bills and pay compression generated by the introduction of the NLW in 2016.

A2.28 First, they documented the extent to which the NLW affected the distribution of wages within firms. They then examined whether firms adjusted their occupational structure in response, by looking at the prevalence of high and low-paid occupations. They next considered the extent to which firms made use of payment by the hour and incentive pay in order to incentivise workers. They also looked at whether firms changed their use of alternative contractual arrangements, agency workers and subcontractors, in response to the rise in the minimum wage. Finally, they examined whether the NLW had impacts on firm-level employment or the likelihood of a firm closing.

A2.29 There is an established international literature on the effect of minimum wages on the wage distribution, such as Autor, Manning and Smith (2016); and Cengiz, Dube, Lindner, and Zipperer (2019). Increases in the minimum wage not only raised the wages of directly affected workers but led to 'spillovers' (increases in wages for workers earning slightly higher wages). For the UK, Giupponi, Joyce, Lindner, Waters, Wernham, and Xu (2024) found spillover effects up to £1.50 per hour above the new minimum when the NLW was introduced.

A2.30 These findings suggest that employers' responses to minimum wages, in particular how they set wages of workers earning above the minimum, can have important implications for the overall impact of the policy on top of the direct effect. Despite this, there has been little research to date on the extent to which minimum wages affect the distribution of wages within firms. Forsythe (2023) and Gopalan, Hamilton, Kalda, and Sovich (2021) found that increases in the minimum wage in US states led firms to increase wages for workers earning above the minimum, while Giupponi and Machin (2023) found that the NLW generated spillovers in the residential care home sector. Giupponi, Ray-Chaudhuri and Xu (2024) sheds light on the impact of the NLW on the wage distribution of large firms, covering the majority of UK employees.

A2.31 As well as adjusting wages, firms might respond to higher minimum wages through other adjustment channels, such as prices (Aaronson and French, 2007; Harasztosi and Lindner, 2019), profitability (Draca, Machin and van Reenen, 2011), and productivity (Riley and Bondibene, 2017; Mayneris, Poncet and Zhang, 2018). The evidence on firms using pay and contractual arrangements is more limited. Datta, Giupponi and Machin (2019) found that the NLW increased usage of zero-hours contracts in the adult social care sector. A novelty of this research is that it also covers the impact of minimum wages on incentive pay, and the use of agency workers and subcontractors.

A2.32 This research utilised three data sources – the Annual Survey of Hours and Earnings (ASHE), the Annual Business Survey (ABS) and the Business Structure Database (BSD) – to analyse the period from 2012 to 2019. That was after the labour market had stabilised following the global financial crisis in 2007–2008 but before the onset of the pandemic.

A2.33 Their basic econometric approach involved using a difference-in-differences framework – comparing changes in outcomes before and after the introduction of the NLW between firms that were more affected by the NLW and those less affected. They also adopted an event study approach, which plotted the differences each year rather than just pre or post-introduction of the NLW.

A2.34 They used ASHE to calculate an NLW exposure measure for large firms (those with at least 20 observations in the sample – firms with over 2,000 employees) using the firm-level coverage of the NLW in 2015. They then adopt a novel approach to impute firm-level coverage for a much larger set of firms. The ASHE-derived coverage was then related to the characteristics of those firms that are observed in the ABS such as average pay, industry and employment. A least absolute shrinkage and selection operator (LASSO) regression was then used to select the most relevant predictors. These were used to predict firm-level coverage for all firms in the ABS.

A2.35 They found declines in the ratio of high pay to low pay (the 90:10 ratio) and median pay to low pay (the 50:10 ratio) for less-exposed (those with minimum wage coverage of 5-20 per cent) and moderately-exposed firms (those with 20-40 per cent coverage) but not for highly exposed firms (those with more than 40 per cent coverage). The latter firms have little scope to reduce differentials but there was evidence of a fall in the 90:50 wage ratio for these firms, suggesting that effects can extend far up the wage distribution in firms with many minimum-wage workers.

A2.36 They concluded that the NLW led to significant pay compression, with small spillovers up to £2 per hour above the minimum level, across all types of firms considered. Incumbent workers (tenure of at least one year) were more likely to benefit from spillovers than new starters. Spillovers were smaller in firms with the highest shares of workers earning the minimum wage, and larger in public-sector firms. These ‘spillovers’ suggested that firms also raised wages for workers not directly affected by the NLW, partly maintaining pay differentials between workers. Similar to the findings for US firms by Forsythe (2023), they found no effect on firms’ occupational structures, suggesting that any changes in firms’ job ladders must be subtle enough not to be detected by their occupation-based measure.

A2.37 They do, however, find evidence of a change in pay practices. Preserving pay differentials in response to minimum wage increases can be costly and we have seen that firms have only partly maintained these differentials. But narrowing pay differentials might reduce incentives for low-paid workers to progress, or lower morale among higher-paid workers. Thus, firms might try to address this by changing the employment contracts offered or by making more use of incentive pay or paying workers by the hour. In 2015, incentive pay was more likely to be used in firms with smaller shares of minimum wage workers but the reverse was true for the use of hourly pay. Within firms, low-paid workers were more likely to be paid by the hour.

A2.38 They found that, among all workers, the introduction of the NLW did not lead to a significant increase in the share of workers receiving incentive pay, the amount of incentive pay received, or the share of workers being paid by the hour. But there were differences between firms that already used these practices and those that had not. Comparing firms heavily exposed to the NLW with those less exposed, they found that firms that were already using incentive pay or payment by the hour did not change their use of these when the NLW was introduced. This was consistent with such firms having little room to increase their usage.

A2.39 However, they did find that the NLW caused firms not already using incentive pay and payment by the hour to implement these methods to compensate low-wage workers, resulting in an increase of 3.4 percentage points in the probability of workers in these firms receiving incentive pay and an increase in incentive pay as a share of total pay of 0.3 percentage points. The researchers argued that this was consistent with attempts to mitigate weakening incentives to progress caused by pay compression. Further, they did not find any significant changes for higher earners in incentive pay among firms not already using these practices, suggesting that firms adopted these practices as a way to deal with wage compression among low-paid workers.

A2.40 The introduction of the NLW also led to a 9.1 percentage point increase in the share of workers paid by the hour in firms that had previously not paid workers on that basis. In contrast to the findings on incentive pay, they also found a large and significant increase in payment by the hour for high earners. They suggested that these wanted the ability to have more control on hours worked across the whole workforce.

A2.41 Another option for firms to cope with minimum wage increases is to make use of alternative contractual arrangements, and to outsource tasks to workers outside the firm. Employing agency workers, who can be hired on a temporary basis, allows firms to avoid committing in advance to paying employees for a certain number of hours each week or month at the minimum wage. Using subcontractors instead of hiring employees potentially allows firms to bypass paying the minimum wage altogether, because subcontractors may be classed as self-employed workers and thus not covered by minimum-wage legislation. Giupponi, Ray-Chaudhuri and Xu (2024) employed novel ABS data on firms' spending on agency workers and subcontractors together with measures of NLW coverage (either using the ASHE or imputed) to explore the extent to which this happened in response to the NLW.

A2.42 They did not find any effect of the NLW introduction on firms' use of agency workers or subcontractors, even among firms that might be most able to use them. In fact, the share of large firms' employment costs spent on outsourcing – agency workers and subcontractors – did not change dramatically between 2012 and 2019. However, the researchers noted that the analysis was based on large firms (generally those with at least 250 employees). Consequently, the findings may only be relevant for these types of firms, although these firms do account for the majority of UK employment. While they did not find any statistically significant effects, the estimates were not highly precise. They suggested improvements required to address these issues. More detailed data on firms' wage structures would enable more precise estimates of minimum-wage coverage and give greater confidence to any conclusions, while improved sample coverage of smaller firms will be necessary to assess potential impacts on these types of firms.

A2.43 The research had focused on how existing firms responded to changes in the minimum wage. But one potential outcome of a significant increase in the National Minimum Wage is that firms are forced to close because of the higher costs. This could affect their results, because their estimates of outcomes in the years after the NLW introduction are based on a sample consisting only of firms that remained open. If the firms that closed were systemically different to those that remained open, then their estimates could be picking up compositional changes in the sample of firms, rather than firm responses to the change in the minimum wage. A similar issue could arise when we look at worker-level outcomes if firms made large changes to the size of their workforce. In response to these concerns, Giupponi, Ray-Chaudhuri and Xu (2024) tested what impact the NLW had on firm survival and firm-level employment in large firms. They draw on the administrative information on firms and their employment in the BSD, for those firms for which there were measures of NLW coverage.

A2.44 Including controls for firm age, industry and employment, they found that there were persistent differences in the probability of being open between high- and low-coverage firms prior to the introduction of the NLW (high-coverage firms were more likely to close). These differences continue after the introduction of the NLW but are suggestive of a slightly increased likelihood that firms close although not significant. They also looked at the probability of a firm closing in any given year. For both high- and low-coverage firms, the rate of closure was roughly the same each year between 2012 and 2019, even though that rate was higher for high-coverage firms than low-coverage firms. They concluded that, taking both pieces of evidence into account, it did not seem that the NLW has had significant impacts on the rates of survival of the large firms analysed in their research.

A2.45 They used a similar sample to explore whether the NLW led to any changes in firm-level employment. Having established that the NLW had not led to higher numbers of closures, they restricted their sample to those large firms that were open throughout the period of interest, 2012 to 2019. The estimates show a downward trend between 2012 and 2019, reflecting the fact that employment was falling by more among high-coverage firms than among low-coverage firms. But there did not seem to be any differences between the trend before and after the introduction of the NLW. This suggested that the NLW did not lead to significant changes in firm-level employment among large firms.

A2.46 They noted that the analysis in this report had concentrated on the impacts of large firms – those with more than 250 employees. They concluded that the introduction of the NLW had not led to changes in firm survival or employment, suggesting that their methodology of looking at existing firms' responses to the introduction of the NLW was likely to capture the majority of the impact of the NLW through changes to pay and contractual arrangements, at least for this set of firms.

A2.47 They concluded that while the analysis here sheds light on wider firm responses to minimum wages, the paucity of data in this area still presents a challenge to researchers. Analysis of the impact on UK firms' wage distributions can only be done for large firms, and while our imputation allows us to expand the sample for analysing pay practices and outsourcing, it is still mostly limited to firms with more than 250 employees. Although our sample of large firms is representative of the firms that hire the majority of UK workers, smaller firms may be less able to deal with the effects of the minimum wage, and so the null results presented here may not extend to them.

Annual Research Workshop and the Twelfth Annual Research Symposium 2024

A2.48 As part of our research programme, we hold two research events a year. The first, usually in April, is a half-day workshop that generally focuses on the data sources and methodology to be used by the researchers in newly commissioned research. The second, in September, is a research symposium that showcases the findings of that research but also covers relevant recent external research.

April research workshop

A2.49 This year, our event in April contained more complete research. There were three sessions: Impact of the minimum wage; non-compliance; and monopsony in the UK labour market.

Impact of the minimum wage

A2.50 The workshop started with a presentation from one of our three commissioned projects. Sam Ray-Chaudhuri (Institute for Fiscal Studies) and Giulia Giupponi (Bocconi University, Milan) discussed the findings they had made so far in their research on identifying minimum wage firms and the impact on firms' contractual arrangements. They explained the methodology and data used to estimate firm exposure to the NLW, and discussed some caveats to this approach (in particular extrapolation to small firms and sampling errors in the data). The presentation then focused on using this approach to look at the impact of the National Living Wage on outsourcing, agency work and contracting work. They concluded that their new coverage measure was an improvement on other measures (use of average wages or wage bills) of identifying minimum wage firms. They also found some evidence, albeit not statistically significant, of an uptick in use of outsourcing in high-bite firms relative to low-bite firms post-NLW. Rui Costa (London School of Economics) acted as the discussant. He flagged concerns with the extrapolation approach – an unbalanced panel and the rotational aspect of small firm sampling in the Annual Business Survey (ABS) – but noted it worked well for 2015 and suggested an alternative data source. He also suggested an alternative approach to identifying the impact of the NLW on contractual arrangements.

Non-compliance

A2.51 The next session focussed on non-compliance. It was chaired by Margaret Beels, the Director of Labour Market Enforcement, with Carlos Vacas (Eurofound) giving a presentation that summarised his organisation's recent publications on non-compliance and enforcement across EU Member States. The research was in two parts. The first used analysis of the European Union Statistics on Income and Living Conditions (EU-SILC) and the Structure of Earnings Survey (SES) to provide a comprehensive quantification of non-compliance with minimum wages. It defined non-compliance as pay below 95 per cent of the minimum wage and covered 20-65 year olds. The second part provided a mapping and assessment of the institutional set-up for the enforcement of minimum wage.

A2.52 The research had found that non-compliance was difficult to measure, with the two data sources giving different findings. The average non-compliance across the EU was 8.1 per cent, ranging from 1 per cent in the Slovak Republic, Czechia and Belgium to over 14 per cent in Italy according to EU-SILC. In contrast, the SES measures of non-compliance were much lower, averaging 1.8 per cent and ranging from close to zero in Belgium, Poland, Lithuania and Malta to 6 per cent in Cyprus.

A2.53 Enforcement mechanisms differed across the EU, although 19 countries had generalist labour inspectorates as the main enforcement body, often managed centrally and accountable to central government. Data collection and monitoring systems on the enforcement of minimum wages across the EU was generally poor. Only Belgium, Croatia, Poland and Portugal had specific data collection for minimum wage enforcement.

A2.54 The discussant was Chris Warhurst (University of Warwick). He appreciated the transparency on the limitations of its research. Measuring non-compliance was difficult as it relied on modelling assumptions and some types of firms were excluded from the analysis. However, clear patterns of non-compliance did emerge across Europe by types of country and types of worker. There are different patterns of enforcement across Europe but they are typically under resourced; enforcement is weak and even absent in some countries. Deterrence and prevention are key, but detection and punishment require resources.

Monopsony in the UK labour market

A2.55 The final session focused on monopsony in the UK labour market and the implications for the minimum wage. The first presentation was from Dan Popov (Frontier Economics), who presented research commissioned by the LPC and discussed above in paragraphs A2.6-A2.16.

A2.56 Nikhil Datta (University of Warwick) was the discussant. He welcomed the use of flow data to construct better outside options using industries. He highlighted a potential mismatch between the empirical framework and the results, questioning the use of current 'bite' rather than lagged 'bite'. He noted that travel-to-work areas were very large and that low-pay workers generally commuted less than 20 minutes. He questioned the use of the concentration measure (the Herfindahl-Hirschman index (HHI)). He suggested an alternative approach using a measure of employer concentration based on observed worker mobility patterns (Nimczik, 2018) but recognised the time constraints for such modelling.

A2.57 Joel Kariel (Competition and Markets Authority) gave the final presentation. The Competition and Markets Authority (2024) also used the HHI to measure labour market concentration and assess how employment was distributed among employers in local labour markets. The local labour market area was defined using travel-to-work areas and occupations. The research used ASHE (2002-2022) to define concentration among existing jobs and Lightcast data (2012-2023) on advertised vacancies as an alternative.

A2.58 The research found that labour market concentration, measured by employment, had generally been falling over the last two decades but had increased during the pandemic back to pre-financial crisis levels. However, using vacancies, concentration was little changed over the last decade. The was a great deal of geographic variation in the measure of concentration. The researchers used production data from the Annual Business Survey to estimate wage markdowns (defined as the difference between the wage and the marginal revenue product of labour). They found that these were stable or falling with workers taking home around 55-75 per cent of their marginal revenue product of labour.

A2.59 They found that workers in more concentrated labour markets tended to have lower pay but that was mitigated to some extent by collective bargaining. They also found that employment was less sensitive to minimum wage increases in high concentration (or less competitive) labour markets, suggesting that monopsony is playing a role. They also found evidence that non-compete clauses were common across the economy and that there was a u-shaped relationship between their use and incomes. Low-pay jobs were more likely to have these clauses than middle-pay jobs, although they were much more common among high-paid ones.

A2.60 Philip Schnattinger (Bank of England) was the discussant. He noted that the counter-cyclicality suggested employer market power rose in recessions; but that falling mark-ups/mark-downs suggested a stronger transmission over time of fundamental shocks into wages and prices. He added that these might be mitigated on the downside by higher competition implying higher values to a job to an employer reducing extensive margin (layoffs). He wondered about the impact of increased working at home on the extent of monopsony. He concluded by noting that concentration along the job ladder might be important (workers did not always search where the vacancies are) for improvements to productivity.

September research symposium

A2.61 The second event, held on 5 September 2024, was our twelfth annual research symposium.

Data developments

A2.62 The event began with a presentation on the latest developments in UK labour market data from David Freeman (ONS). He discussed data concerns and planned improvements to the labour market data. ONS had responded to falling LFS response rates by returning to face-to-face interviews, improving incentives and boosting the sample. This had helped but responses were still well below pre-pandemic levels. He then outlined next steps: the sample boost would continue to work through the LFS (and will be fully implemented by March 2025); and a reweighting would be implemented in the December labour market publication with LFS person data revised back to 2019.

A2.63 He then discussed the Transformed LFS – the project to replace the LFS with an online survey, with a view to achieving a larger overall sample size, more robust processing systems, and greater flexibility in the survey. It was due to replace the LFS in 2024 but there were concerns about the data collected. In response, ONS decided to continue with the dual running of the LFS and TLFS, initiated an academic review, and set up a stakeholder panel. Further improvements will be tested in early 2025 before a decision is made on the future timetable.

A2.64 He concluded by looking at the earnings data provided by ONS. He noted that Average Weekly Earnings (AWE) and HMRC’s Real Time Information RTI showed a similar pattern of wage growth since the end of the pandemic but that the Annual Survey of Hours and Earnings (ASHE) had shown a different pattern (with lower wage growth). ONS had allocated more resources to this area with a focus methods, processing and analysis. Areas for development and analysis in ASHE and AWE had been identified and some would be implemented in the 2024 ASHE.

A2.65 Van Phan (University of the West of England) then gave an overview of the Wages and Employment project. The aim of the project is to improve the data available to researchers for labour market analysis. The programme has consisted of improved documentation and quality assurance for ASHE; improving the consistency of ASHE over time; linking ASHE with the 2011 Census; and linking ASHE with HMRC pay data on workers (Pay-As-You-Earn) and the self-employed (Self Assessment). These linked data sets are now ready for research purposes. The project will next look to link with the Migrant Worker Scan (in 2025) and the 2021/2022 Census (in 2025/2026).

A2.66 The enhanced ASHE is a high-quality data set with additional variables to the main ASHE data (for example, minimum wages, survey dates, consistent definitions and some additional longitudinal variables from the ONS archives) and new weights. Van highlighted some of the methodological and analytical research that had been undertaken using these data, much of which is relevant to the Low Pay Commission. She concluded by encouraging researchers to use this resource.

Women in the labour market

A2.67 The Young Women's Trust presented the findings of three different pieces of research conducted in the past year: its annual survey; a piece on gender income gaps; and another piece on progression. Christal Kihm, Kate Nightingale, Elspeth Oakley and Becky Sibson gave the presentation.

A2.68 The income gap research used data from the UK LFS 2023 to explore the relative contribution that different characteristics make to the overall gender pay gap. They found that, on average, a young woman will earn a fifth less each year than a young man of the same age (equating to around £4,000 a year). For some groups of young women, such as those from ethnic minority communities, or with disabilities, the income gap is even larger. They divided the income gap into five contributing factors finding that higher concentration of women in low-paying industries had the largest impact, followed by tenure (men's pay grew faster with length of tenure at the same employer), children and age. In contrast, education reduced the income gap as women were more likely to have higher education outcomes.

A2.69 Its annual survey, conducted in July 2024, produced a sample of 3,926 young women, 1,051 young men and 917 HR Managers. It found that discrimination, childcare challenges, the cost of living, lack of skills development opportunities and lack of networks can trap young women in low pay. More than a fifth (22 per cent) of young women said that they have been paid less than the minimum wage they were entitled to (it was 20 per cent for young men). This was higher for young women with care responsibilities and working in certain industries such as hospitality (29 per cent), the arts, entertainment and recreation (26 per cent) and health and social care (25 per cent). Young women felt less able than young men to challenge pay inequality at work, and challenge or report discrimination.

A2.70 The research into progression at work was a qualitative study that consisted of interviews and creative methods with 58 young women. The data was collected in March 2024. They cited young women who reported that low pay prevented them taking opportunities to progress and that the Universal Credit system did not aid taking risks. The presentation concluded with three requests. First, to lower the age band for the NLW and ensure that it meets the cost of living. Second, the NLW and other employment rights needed to be properly enforced, and support provided for workers to know their rights and stand up for them. Finally, employers should be required to have clear and transparent progression pathways to ensure equal access to promotion for all workers.

A2.71 Joanna Crossfield (Ipsos) was the discussant. She noted that women were more likely to be lone parents and that heightened the importance of childcare costs and need for flexibility. Young women were discriminated most for pregnancy, parental leave or caring responsibilities. She also noted that while young women and men are equally likely to work for an employer not paying minimum wage, women were less likely to challenge and be more likely to be negatively affected.

A2.72 She asked how we might build capacity and resilience among younger women to better equip them to avoid the low pay trap. Becky Sibson responded that this needed to be addressed by policymakers, employers and in education. It needed to be comprehensive and not put the onus on young women. Joanna added that shifting childcare towards greater shared parental responsibility could have a significant impact on women. Ipsos research had found that awareness of Universal Credit Childcare support was very low. She then asked about why women were drawn to certain (low-paying) occupations. Becky responded that it was for several reasons: cultural/social norms of male and female jobs; traditionally considered 'female' sectors, such as social care and childcare, are undervalued; and certain sectors offered greater flexibility. Becky also thought that the Government's Make Work Pay strategy would address many of the issues that prevented young women from progressing.

Impact of the minimum wage on work arrangements

A2.73 Two of our commissioned research projects were presented in the next session that focused on the impact of the minimum wage on pay and work arrangements. Xiaowei Xu (Institute for Fiscal Studies) presented the IFS's research on the impact of the minimum wage on firms' pay and contractual arrangements. She highlighted the methods and the main findings. Further detail is given above in #paragraphs A2.26-A2.45.

A2.74 Steve Machin (London School of Economics) was the discussant. He thought it was a good piece of work and welcomed the use of firm-level data. He noted that other countries had better employer-employee matched data but that this research was what could be done with the limitations of the available data. Most minimum wage research had focused on employment and hours effects. He welcomed the focus on other forms of adjustment. However, he suggested that these data could be used to assess employment dynamics, as well as subsequent NLW upratings. He wondered about the imputation procedure and how firm size might affect the results and interpretation. Large firms tended to pay more but there was also dispersion of pay policies among large firms. He suggested a robustness check using the whole sample.

A2.75 Overall, his main take from the research was that there are effects on contracts and pay policies but these are fairly modest. Thus, it seems that firms are able to make small adjustments and cope with large minimum wage increases. It results in more pay compression but firms seem able to cope. There are no exit effects. It would be useful to put these in a context of other adjustments including prices, profits and productivity.

A2.76 Rui Costa (London School of Economics) presented the findings of the second commissioned project. This also looked at the impact of minimum wages on alternative work arrangements, but used a different approach and data source. His key findings were: the introduction of NLW resulted in increased job retention by lowering involuntary job separations while leaving search behaviour on and off the job relatively unchanged; minimum wage changes can result in shifts in types of contracts, with most of the adjustment being concentrated among incumbents; and although the magnitude of the effects on labour market transitions are not negligible, the size of the causal effects on contract types are relatively small.

A2.77 Mark Williams (Queen Mary University of London) was the discussant. He thought the research paper was very comprehensive and addressed an evidence gap, as adjustments to firms' employment structures had not been properly investigated by evaluation studies. This study found that job security had improved – the introduction of the NLW had reduced layoffs and termination of temporary contracts, and increased job tenure.

A2.78 It also found that the NLW may have improved work-life balance (hours had become more aligned with preferences and there had been an increase in fixed hours making life easier to organise). However, there had been an increase in zero hours contracts. These are not intrinsically bad – it is the poor job quality that is usually associated with them. But this increase is set against no changes in hours, more fixed hours, hours better matched to preferences, better job security, and higher wages. He wondered how these findings could be reconciled. Had improvements for one group (NLW workers) been offset by changes to other workers? He concluded that this study was a welcome contribution to our understanding of how regulatory changes can transform non-pay job quality.

Labour market mobility

A2.79 John Forth (City University) presented the findings of the Wage and Employment Dynamics project on the impact of a rising wage floor on labour mobility across firms. The researchers used linked employer-employee data (ASHE) with a difference-in-difference (DiD) estimator to evaluate the impact of the introduction of the NLW on job mobility among workers aged 25 and over in the UK. They examined the sensitivity of results to various re-specifications of treatment and control groups (e.g. accounting for the possibility of spillovers). They found no evidence that the increase in the wage floor changed rates of job-to-job mobility among low-paid workers, on average. They concluded that this provides further evidence of the seemingly benign effects of minimum wage policy on employment dynamics in the UK.

A2.80 The discussant was Abigail McKnight (London School of Economics). She noted that a higher minimum wage could lead to increased mobility (as employees moved to more productive jobs as their jobs were no longer viable); increased churn (job moves may be separated by unobserved periods out of work); or reduce incentives to move to another firm (as wages became more compressed). It was therefore an empirical issue, which this research addressed in aggregate. She noted that given firm-to-firm job moves were important drivers of wage growth and progression, it would be helpful to know more about what happened beneath the aggregate trends.

A2.81 The next presentation was given by Nikhil Datta (University of Warwick) who considered local monopsony power. With minimum wage employment effects remaining elusive, more focus has been put on monopsony as a potential explanation. Much of the previous research had not considered the drivers of monopsony. He developed a theoretical job search model that incorporated distaste of commuting. He found that distaste for commuting increased monopsony power but did so heterogeneously across space, suggesting that denser areas were more competitive. He added that coarsely discretising space can be problematic as commutes within spatial labour markets are not costless and there is large heterogeneity in monopsony power even within these markets. He showed why continuous labour markets more precisely identified labour market concentration than travel-to-work areas.

A2.82 He used a firm data set (on vacancies and applicants) with 350 establishments across the UK and identified two sources of exogenous wage variation (the Living Wage and wage saliency) that validated his model. He showed that there was no firm or worker mobility response to spatial minimum wage exposure. He estimated that the application elasticity would be about 65-80 per cent higher without commutes. Distaste for commuting was therefore responsible for around 1/3 of the wage markdown.

A2.79 Jakob Schneebacher (Competition and Markets Authority) was the discussant. He viewed the model as highlighting the importance of the distribution of workers (as well as firms), and unlocking important substantive research questions through the novel concentration measure. He noted that there was quasi-random variation in the wage, but not in the commuting disutility. Commuting distance may be correlated with other features (search frictions, job amenities). He suggested two avenues to explore: use the information in HR dataset to test alternative theories directly; and be more explicit about the commuting term in context of the search friction/product characteristics literature. Although workers and existing firms do not move a lot, there may be other ways that sorting takes place: new firms, new workers (for example, migrants), jobs (working from home), and input substitution.

Wage volatility

A2.80 The fifth session considered wage volatility. Nye Cominetti (Resolution Foundation) presented his work with Mike Brewer (Resolution Foundation) and Stephen Jenkins (London School of Economics) on measuring earnings volatility with ASHE-PAYE dataset. The study utilises the WED project that links HMRC's payslip data with ASHE. The research has focused so far on month-to-month earnings volatility (including workers paid weekly and fortnightly). The ASHE-PAYE dataset contains data for all of the ASHE sample from 2014-2019, whether their employers responded or not to the ASHE questionnaire. That covers around 289,000 workers with around 5.8 million payslips each year. Nye highlighted some of the issues with the dataset.

A2.81 They distinguish between what they define as 'labour market volatility' and 'earnings volatility'. The former is larger and includes zero pay periods, the latter excludes them. They found that volatility was seasonal, peaking in April and at its lowest in November for monthly-paid workers. For weekly-paid, the seasonality is less pronounced. But volatility was higher for those paid weekly rather than monthly. There was a small gender difference. There were much larger differences by age, with young workers (aged 20-25) having the highest volatility and older workers (those over 50) the least. Volatility was also greater for those paid hourly, those in low-paying industries, those in temporary jobs, and those in multiple jobs. Although volatility was highest for low-paid workers, it was also high for the highest paid (as bonuses appeared to play a roll around April each year).

A2.82 Eduin Latimer (Institute for Fiscal Studies) was the discussant. He highlighted the main findings as: earnings volatility is persistently high for employees in the UK; most volatility in pay is due to volatility within a spell of employment; and earnings volatility is higher for certain groups of workers. Eduin suggested it would be worth separating out different types of volatility, as they will likely have different effects. Identifying bonuses separately may help better distinguish between volatility caused by uncertain hours and that caused by one-off annual payments. It also might be useful to differentiate between downside and upside volatility, as there may be asymmetric consequences.

A2.83 He concluded by suggesting some areas for future research. The role of firms and whether volatility varies by size of firm and across individual firms within an industry. In the HMRC datalab, it may be possible to identify firm effects for all firms. The introduction of the National Living Wage (NLW) and its subsequent increases may have affected volatility in pay. Some employers say they responded to the NLW through increased use of flexible/zero hours contracts (and there is some academic evidence for this (Datta, Giupponi and Machin (2019) and Albagli, Machin and Vieira-Marques (2024)). The difference-in-difference design could be applied with the linked PAYE-ASHE data.

A2.84 Marsha Wood (University of Bath) then presented her qualitative research with Rita Griffiths (University of Bath) on the Universal Credit (UC) system of monthly assessment. The study looks at how monthly assessment periods affect the income volatility and financial well-being of working households. UC is assessed and paid monthly in arrears, which means that UC can rise and fall each month in response to changes in reported earnings. The study conducted interviews with 37 households and collected monthly data for 13 months on their earnings, income, and UC payments, as well as additional qualitative evidence on the issues they faced.

A2.85 Most of the households experienced significant volatility in their monthly incomes, primarily due to earnings variability. They found that 28 of the 37 households (76 per cent) had incomes that varied by £500 or more from one month to the next at some point during the study. Monthly earnings varied for a range of reasons including unemployment, changes in hours, sick leave, backdated pay awards, and performance bonuses. However, the study also found that reported earnings often varied significantly without underlying changes to earnings. This was primarily due to the workers' pay frequency, with workers who were paid weekly, fortnightly and four-weekly having a varying number of pay packets captured within the UC assessment period each month. This meant that the UC monthly assessment system often exacerbated rather than dampened income volatility. For 20 of the 37 households (54 per cent) UC payments varied by £400 or more at some point during the study period.

A2.86 Households in the study also generally had income that was too low to put aside savings buffers, which made it difficult to manage the income volatility. 32 of the 37 households (86 per cent) had average incomes below the Minimum Income Standard (MIS) and three-quarters of the households had no savings. Finally, the study also found that the UC monthly assessment and high withdrawal rate appeared to have weakened, rather than strengthened, work incentives.

A2.87 The discussant was Susan Harkness (Bristol University). She emphasised the importance of this research in providing evidence on the link between the labour market and Universal Credit. She noted that while UC aims to replicate the labour market with the monthly payments in arrears, workers receiving UC are more likely to work in risky jobs that are paid weekly or fortnightly and have irregular hours. The study highlights earnings volatility as a new risk and raises questions about the role of welfare state in reducing this risk.

A2.88 She also emphasised that individual earnings are not the only type of risk. Family events, such as childbirth and gaining or losing a partner, are major sources of risk to incomes. Families are also able to provide security by compensating for changes in partner's earnings. Employer engagement on UC was also a key takeaway. She said it is important for employers to understand the impact of bonuses and pay awards on UC payments.

Government contracting and living wages

A2.89 Steve Machin (London School of Economics) presented his joint work with Nikhil Datta (University of Warwick). The research explores the impact of living wage clauses in local procurement contracts. It does so by utilising a rich worker-firm dataset where establishments are exogenously subjected to living wages. It studies a set of adjustment margins for workers in establishments that get treated by living wages as compared to control establishments.

A2.90 The dataset is derived from HR records on workers in all establishments of The Company for the period of 2011-2019. The Company consists of over three hundred establishments operating in the UK service sector. The data covers wages, hours, tenure and demographic characteristics of workers. There is detailed information on job role, pay scales, within-firm job moves, pay points, employment composition and contract type. Alongside the HR data, the researchers have collected data on establishment exit, output prices and quality ratings.

A2.91 They found that the introduction of the Living Wage in the environmental, social and corporate governance framework of local government contracts had a strong positive impact on low-wage workers. Earnings increased by around 3 per cent in London and 5 per cent in the rest of the UK. They found no negative aggregate labour demand effects at establishment level, nor an adverse impact on firm performance. But there were winners and losers within establishments as The Company adjusted to higher living wages through labour-labour substitution (in ways consistent with monopsony power and low substitutability) and by changing their pay policies. The introduction of the voluntary Living Wage reduced internal wage inequalities through these modes of adjustment.

A2.92 Max Mosley (National Institute for Economic and Social Research) was the discussant. He commended the identification of this natural experiment. After highlighting the main results he raised several issues about long-run effects and whether this reduction in within-firm wage inequality was positive. He also raised the issue of whether there was an optimal strategy that policymakers wanted in the trade-offs of adjustment mechanisms. He concluded by noting there was such a strong body of evidence that the introduction or rise in the minimum wage had a positive effect on workers' wages and little to no employment effect as firms absorbed associated costs. This now appears to hold with the higher more generous Living Wage.

A2.93 We would also like to thank all of those who acted as discussants or chairs at our research events: Nicola Allison (Office of Manpower Economics), Margaret Beels (Director of Labour Market Enforcement), Rui Costa (London School of Economics), Joanna Crossfield (Ipsos), Nikhil Datta (University of Warwick), Susan Harkness (Bristol University), Eduin Latimer (Institute for Fiscal Studies), Steve Machin (London School of Economics), Abigail McKnight (London School of Economics), Max Mosley (NIESR), Philip Schnattinger (Bank of England), Jakob Schneebacher (Competition and Mergers Authority), Chris Warhurst (University of Warwick) and Mark Williams (Queen Mary University of London). We would also like to thank all those that took part. The comments and suggestions have contributed to the development of our research programme.

Conclusion

A2.94 The research continues to generally find that the introduction of the National Living Wage and subsequent upratings have significantly increased the earnings of the lowest paid but that, to date, there has been no strong evidence of any negative employment effect in aggregate over the whole period. However, nearly all of the econometric analysis has been limited to the period prior to the pandemic and thus does not look at the impact of the large increases in the National Living Wage since 2020.

A2.95 However, from the commissioned research, it seems that firms have been able to cope with the large minimum wage increases by making a variety of small adjustments to contracts and pay policies. It appears that firms have been able to manage more pay compression. There have so far been no effects on exits. It would be useful to put these in a context of other adjustments as we know from previous research that firms have used other adjustment channels, such as prices, profits and productivity.

Table A2.1: Research for the 2024 Report

Project title and researchers	Aims and methodology	Key Findings
Monopsony, minimum wages and the UK labour market **Maria Guijon, Katharine Lauderdale,** and **Dan Popov** (Frontier Economics)	Frontier Economics (2024) investigated the link between different degrees of labour market concentration and minimum wage effects on number of workers in low pay employment, total weekly hours worked among low pay workers, average hours per worker among low pay workers, and base hourly wages among low pay workers. A methodological contribution of this study was to use a novel data-driven sectoral definition of low-pay labour markets, which grouped sectors together based on the volume of low-paid job switches across sectors. The study derived its labour market concentration measure using data on employment, geography and industry from the Business Structure Database (BSD). The Annual Survey of Hours and Earnings (ASHE) was used to estimate various measures of pay, hours worked and employee numbers. These pay, hours and concentration measures were derived for each Travel-to-Work Area in England and Wales between 2015 and 2019. The researchers also added an industrial dimension, using 4-digit Standard Industrial Classification (SIC) codes, to their definition of local labour markets. They used analysis of job moves to identify nine industry clusters. Their unit of analysis was an industry cluster within a local area for instance, retail in Chelmsford. The study examined the association between changes in the minimum wage and labour market outcomes (employment, hours, hours per worker, wages). The analysis took into account firm exposure to minimum wage increases in local areas, and different levels of market concentration.	The main findings were: • There was robust evidence that the introduction of the NLW increased the hourly wages of the low-paid across all labour market areas (those with both low and high labour market concentration). • In line with previous work, there was some evidence that, following an increase in the minimum wage, employment and total hours increased in high-employer concentration areas relative to low-employer concentration areas. • This is also in line with the theoretical model of monopsony that allows for the possibility that increases in minimum wages can lead to increases in employment and hours. • They also found some evidence that minimum wage increases exert downward pressure on the wages of higher income workers in markets with high concentration. • However, as noted by the authors, the magnitude and statistical significance of the results are sensitive to the specification of the model. That may in part be due to the fact that they found labour market concentration is generally low in low-paying labour markets. • The researchers concluded that monopsony likely interacts with minimum wage effects differently across different sectors and occupations, due to differences in public sector employment, in the elasticity of hours per worker, in the geographic distribution of different sectors, and other factors. • The finding of low-employer concentration in most sectors of the low-paying labour market suggested that future work on monopsony effects could usefully focus on sectors or local areas with higher-employer concentration.

Project title and researchers	Aims and methodology	Key Findings
Minimum Wage Effects: Adjustment Through Labour Market Dynamics and Alternative Work Arrangements **Pinjas Albagli, Rui Costa** and **Steve Machin** (London School of Economics)	The aim of this report was to understand potential impacts of minimum wage changes on margins such as contract types and job attributes related to hours volatility and work security. The study primarily focused on the introduction of the National Living Wage in April 2016 in the UK and exploited the variation in pre-policy exposure to minimum wages across different regions and ages, in a similar vein to Manning (2016), Dube (2019), and Butcher and Dickens (2023), as a means to estimate the causal effects. Albagli, Costa and Machin (2023) use the Quarterly Labour Force Survey (QLFS) as the main data source. The QLFS contains unique information on most types of contracts of interest to the Low Pay Commission. It also covers a long period of time enabling the study of heterogeneity over the scale of NMW upratings and changes in age bands of NMW. However, sample sizes can be small for particularly detailed socio-demographic groups. Robustness was conducted using the Annual Population Survey (APS). They used a difference-in-difference model and an event study model to derive their results. They pool the data for 16-65 year olds from the second quarter of 2014 to the second quarter of 2017. They derived 96 age-region cells (from 8 age groups and the 12 standard regions). They used two measures of exposure to the minimum wage (bite and coverage) to assess the impact of the introduction of the NLW on the incidence of various contract types and self-employment. They did this by comparing the outcomes up to the first quarter of 2016 and afterwards. In the event analysis, they track these changes each quarter for a panel of age-region cells before and after the first quarter of 2016.	The main findings were: • In line with previous research, there were significant wage effects from the introduction of the NLW, especially for workers in low-paying industries. • Whilst there was no overall negative employment effect from the introduction of the NLW, there were some negative estimated effects on unemployment with positive effects on inactivity. • The negative impact on the probability of being unemployed was primarily driven by increased job retention, marked by substantially lower flows to unemployment, predominantly fuelled by a decrease in involuntary separations (i.e. layoffs). • This decrease in layoff probabilities was notably pronounced among those facing job loss after the ending of a temporary contract. • The reduction in layoff probabilities is consistent with the findings of Brochu and Green (2013) and Dube, Lester and Reich (2016) in the US and Canada. • There was no evidence of significant reductions in voluntary separations or job-to-job transitions. Nor was there evidence of changes in on-the-job search. • A substantial part of the employment retention effect was observed among those on full-time contracts. • The chances of a worker reporting to be underemployed fell – sustained by reduced flows from non-underemployment to underemployment and non-employment. • Modest effects of workers moving from variable to fixed-hour contracts were also found. • There was no evidence that the NLW had pushed workers into self-employment, but the incidence of zero-hour contracts increased among those most exposed to the NLW • Overall, the combined effects of increased flows from variable to fixed hours, temporary to permanent positions, and enhanced job retention of full-time workers resulted in an overall reduction in what the OECD classifies as non-standard work arrangements.

Project title and researchers	Aims and methodology	Key Findings
The impact of the National Living Wage introduction on firms' pay and contractual arrangements **Giulia Giupponi, Sam Ray-Chaudhuri** and **Xiaowei Xi** (Institute for Fiscal Studies and Bocconi University, Milan)	The aim of this research was to assess the impact of the introduction of the National Living Wage (NLW) in 2016 – a new and higher minimum wage for workers aged 25 and over in the UK – on firms' wage distributions, pay practices and use of alternative contractual arrangements. The research: • documented the extent to which the NLW affected the distribution of wages within firms; • examined whether firms adjusted their occupational structure in response, by looking at the prevalence of high- and low-paid occupations; • considered the extent to which firms made use of payment by the hour and incentive pay in order to incentivise workers; • looked at whether firms changed their use of alternative contractual arrangements, agency workers and subcontractors, in response to the rise in the minimum wage; and • examined whether the NLW had impacts on firm-level employment or the likelihood of a firm closing. They used three data sources covering the period from 2012-2019: the Annual Survey of Hours and Earnings (ASHE), the Annual Business Survey (ABS) and the Business Structure Database (BSD). Their basic approach involved using a difference-in-differences framework – comparing changes in outcomes before and after the introduction of the NLW between firms that were more affected by the NLW and those less affected. They also adopted an event study approach, which plotted the differences each year rather than just pre- or post-introduction of the NLW.	The main findings were: • The NLW raised the overall wage bill • The NLW led to wage increases for low-paid workers, up to £2 per hour above the minimum level. • These 'spillovers' suggest that firms raised wages for workers not directly affected by the NLW, partly maintaining pay differentials between workers. • Workers in post for at least one year were more likely to benefit from spillovers than new starters. • Spillovers were smaller in firms with the highest shares of minimum wage workers, and larger in public-sector firms. • The NLW led to pay compression among low-wage workers. Despite this, there was no evidence that large firms adjusted their organisational structure (measured in terms of the mix of occupations) in response to the higher minimum wage. • There was evidence of a change in pay practices. Comparing firms more or less exposed to the NLW, the NLW induced firms not already using incentive pay to introduce incentive pay and payment by the hour. • No effect of the NLW introduction was found on firms' use of agency workers or subcontractors, even among firms that might be most able to use them. In fact, the share of large firms' employment costs spent on outsourcing – agency workers and subcontractors – did not change dramatically between 2012 and 2019. • No effects were found on the survival rates of large firms, or on firm-level employment.

Appendix 3

Data sources

A3.1 In this appendix, we outline the main data sources that we have used in our analyses, including any major changes that have occurred since our 2023 Report. We also provide further detail on some of our methodology and definitions. Table A3.2 provides a list of low-paying occupations and industries as defined by the LPC.

Data Sources

A3.2 We use four main sources of data to measure earnings in this report: the Annual Survey of Hours and Earnings (ASHE), Average Weekly Earnings (AWE), HMRC Pay As You Earn (PAYE) administrative data and the Labour Force Survey (LFS). Our headline measure of hourly earnings comes from ASHE.

A3.3 We use three main sources to understand employment: the LFS, HMRC PAYE data and the ONS Workforce Jobs series (WJ). The LFS captures information about all employment; the PAYE series measures the number of employees (registered on the PAYE system) in the UK, and WJ gives an estimate of the total number of jobs. There are some significant differences between these definitions, most notably that the PAYE series excludes the self-employed.

A3.4 All of the data sources mentioned above are published by the Office for National Statistics (ONS), although the PAYE series is collected by HMRC. The ONS provides detailed quality and methodology information for each dataset on its website, as well as a comparison between different sources of data for earnings and employment (ONS, 2022c).

A3.5 In addition to employment and earnings data, we also look at a wide range of macroeconomic data and statistics. This appendix outlines the main macroeconomic series on inflation and gross domestic product (GDP) used in our analyses, as well as summarising any revisions over the last year that ONS has made to its GDP estimates.

A3.6 In 2020 and 2021 there were significant limitations across several of the datasets we use due to the impact of the pandemic. Data from 2022 onwards are largely free from the direct impact of pandemic restrictions, although some impacts on data collection have persisted and our estimates of annual changes in 2022 are affected by using data collected during the pandemic as a base. For this reason, throughout the report we also compare the latest data with 2019 or pre-pandemic averages where relevant.

Annual Survey of Hours and Earnings (ASHE)

A3.7 The Annual Survey of Hours and Earnings (ASHE) is our main source for analysis of the structure and distribution of earnings in the UK and is regarded by the ONS as the best source of earnings information for cross-sectional analysis. It provides information on the level, distribution, and composition of earnings, as well as information on hours worked, gender, age, geography, occupation and industry. It is a survey of employees completed by employers and conducted in April each year. The reference date for the 2024 survey was the pay period that included 17 April 2024. The sampling frame consists of a one per cent sample of employee jobs in PAYE income tax schemes obtained from HM Revenue & Customs (HMRC). It is weighted to be representative of the population of employees in the UK by gender, broad age group, region and occupation.

A3.8 As ASHE surveys only employee jobs paid through PAYE, some workers are excluded: it will not capture the self-employed or workers who are not paid through PAYE. This latter group could include workers in the 'gig economy' who retain the rights of workers – including to the minimum wage – but are not classed as employees and may not appear on a company payroll. It could also include a small number of employees who earn less than the limit at which their employers are required to pay them through PAYE (currently £123 a week) – although in most cases, employees are paid through PAYE regardless of their earnings.

A3.9 In our analysis of the earnings effects of the minimum wage, our main measure of hourly pay using ASHE excludes overtime pay and shift premiums. We do this to make our measure of pay as close as possible to the legal definition used in minimum wage legislation.

A3.10 ASHE data for the latest year used in our report is always provisional and therefore subject to revision. Final data is received a year later and used in subsequent reports: thus, for this report we received 2023 final data at the same time as receiving provisional data for 2024. We are grateful to ONS for allowing us pre-release access to enable us to give timely statistical advice to Commissioners.

Changes to ASHE methodology in 2024

A3.11 As we have noted in previous reports, the distribution of earnings growth since 2019 is different between ASHE and other sources, such as the HMRC PAYE administrative data. The ASHE data tend to show stronger pay growth at the bottom of the distribution relative to the PAYE data and weaker growth at the top. There are a number of factors which could be driving this difference, some of which are inherent to the different data sources, while others indicate issues with the representativeness of ASHE data. For example, Work and Employment Dynamics (2022b, 2022c and 2023b) find that the ASHE weights – which use worker, not firm characteristics – underweight certain types of businesses.

A3.12 The ONS has been investigating the differences between ASHE and other sources of earnings data. This year, they made some changes to the processing of ASHE returns, resulting in more high earners being included in the final data. This methodology change affects the 2023 (final) and 2024 (provisional) data. It leads to a significant increase in our revised estimate of median hourly earnings for 2023, as well as contributing to our estimate of median hourly earnings in 2024 being higher than expected. It also leads to a break in the series between 2022 and 2023.

A3.13 We are currently working with the ONS to develop consistent estimates for years prior to 2023. In the meantime, we have not adjusted past data to account for this methodology change and estimates of changes between 2022 and 2023 should be treated with caution.

Changes to the Standard Occupational Classification used in ASHE

A3.14 ASHE data is weighted based on classes defined by occupation, region, age and sex. In occupation, it follows the UK's Standard Occupational Classification (SOC), which is periodically updated to reflect changes in the labour market.

A3.15 Since 2021 (final data), ASHE has coded occupations using SOC 2020. This leads to a break in the ASHE series, where 2021 final data are not comparable with those of previous years. This affects all estimates using ASHE via the change in weighting. It also leads directly to a break in the series by occupation, including our analysis of low-paying occupations (see Table A3.2). A similar break occurs in 2011 with the shift to SOC 2010, and with further methodological breaks (for other reasons) in 2006 and 2004. For each break, ONS provides two datasets for the year of the change, one using the old methodology and one the new.

A3.16 To adjust for these breaks in the series, we 'chain link' certain estimates. That is, we estimate the impact of the methodology change in the year it is made (by comparing the same dataset before and after the change), and adjust all previous estimates by the same factor as follows:

$$Chain - linking\ factor(CLF)_X = \frac{X_t^{New}}{X_t^{Old}}$$
$$X_{t-1}^{New} = CLF_X * X_{t-1}^{Old}$$

A3.17 Chain linking can mean that estimates published in previous reports are later adjusted for consistency with the most recent data.

A3.18 Where pre-2011 data is used, we chain link all estimates to adjust for the changes in 2004, 2006 and 2011. In 2021, there were significant data limitations due to the pandemic. Sample sizes – particularly for young people – were low compared with the pre-pandemic average. The labour market was also different to its pre-pandemic state. This means that there are some disadvantages to using 2021 as a link year (and assuming that the impact of the change is the same in 2021 as it would have been in previous years). Therefore, while we consistently chain link estimates of the median for all groups in 2021, we retain non-chain-linked estimates in other areas, particularly when looking at the youth and apprentice rate populations. The notes accompanying each chart or table specify whether estimates are chain linked in 2021. Our 2022 Report (Low Pay Commission, 2023a) provides a detailed explanation of our use of chain linking, along with tables comparing chain-linked and non-chain-linked estimates of median hourly pay, coverage and underpayment. The differences between chain-linked and non-chain-linked values are small.

Other issues relating to ASHE

A3.19 In 2024, there were 173,000 responses to ASHE. This is the highest achieved sample size since 2019, although remains slightly lower than the pre-pandemic average, which was around 180,000.

A3.20 While the reduction in sample size was less severe than for household surveys such as the Labour Force Survey, it does cause two issues for our analysis, particularly for estimates for 2020 to 2022. First, the reduced sample sizes mean that there is more uncertainty over our results, especially for smaller subgroups (such as groups within the younger rate populations). Second, if the employers who no longer respond are not representative of the wider employer population, the reduction in sample size might bias the results from the survey. For instance, if the ONS stopped receiving as many responses from high-paying firms, this could bias the estimates of average pay down. ONS weight the survey to population totals from the Labour Force Survey in order to make it representative of the workforce. This should help to mitigate this risk, but it is possible that the changing pattern of non-response has had an effect on pay estimates. However, there are also concerns about the population weights used in the LFS. We discuss the recent issues with the LFS later in this appendix.

A3.21 In 2020 and 2021, estimates of pay from ASHE data were affected by furlough. Where we refer to the 2020 and 2021 ASHE data in this report, we use our central estimate of workers' pay unless otherwise stated. This is adjusted to remove the effect of reduced payments due to furlough. We use additional questions asked in ASHE 2021 to determine the ratio between measured pay and normal pay for each job and adjust upwards accordingly. In cases where these questions were not answered, we use the median ratio to adjust their pay, and we limit the ratio to a range between 80 and 100 per cent. This is discussed in detail in Appendix 3 of our 2021 Report (Low Pay Commission, 2021). Figures in this report may vary from central estimates reported in Low Pay Commission (2021) due to the SOC update, although the methodology used is the same. By the ASHE reference date in 2022, no workers were on furlough and questions relating to furlough were removed from the survey. However, growth comparisons will be affected by furlough effects and how they were measured in 2020 and 2021.

A3.22 The introduction of the National Living Wage (NLW) in 2016 had important implications for our analysis and interpretation of ASHE data. A key change is that the NLW was introduced in April, coinciding with the ASHE data collection period. Previously, new minimum wage rates were introduced in October, with measurement of earnings, the bite and underpayment occurring six months after implementation of the new rates. Both the bite of the minimum wage, and measured underpayment, are at their highest upon introduction and correspondingly lower when measured six months after implementation. All the other minimum wage rates were uprated in April 2017 to ensure alignment with the NLW uprating date. This introduced a break in the time series, with a step change in estimates of both the bite and underpayment.

A3.23 ASHE is not our preferred source of pay data for workers eligible for the Apprentice Rate. Estimates of the total number of apprentices are lower in ASHE than in administrative data, suggesting that some apprentices are not identified as such by employers responding to the survey. Previous research commissioned by the LPC (Drew, Ritchie and Veliziotis, 2016) has suggested that lower-level apprenticeships in small firms are likely to be underrepresented. Recently, we have also seen indications that apprenticeships done by older workers – often at the higher end of the pay distribution – are underrepresented. The impact of these issues is reduced when we look at individual age groups, however this does leave us with small samples where indicators are often volatile.

Average Weekly Earnings

A3.24 Average Weekly Earnings (AWE) is the lead monthly measure of the level of mean weekly earnings per employee in Great Britain. It is based on data from the Monthly Wages and Salaries Survey, which samples around 9,000 employers (excluding small businesses employing fewer than 20 people) covering 12.8 million employees. AWE provides a monthly measure of regular pay, bonus pay and total pay. It replaced the previous measure of short-term changes in earnings, the Average Earnings Index (AEI) in January 2010. AWE uses current industry weights that are updated each month to take account of the distribution of jobs across sectors. The ONS also produces a decomposition of the growth rates to show how much growth is due to wage growth, and how much growth results from changes in employment across sectors. The AWE estimates do not just measure pay, but also reflect industry-based compositional changes within the workforce (but not job-type or occupation-based changes within industries).

A3.25 The ONS publishes three AWE historic time series, all of which are monthly in frequency and include bonus payments: the whole economy series runs from January 1963 to December 1999, while public and private sector series are available from January 1990 to December 1999. The method used to compile these time series takes into account the observed relationship between AEI and AWE, in particular that AWE increased faster than AEI for most of the period between January 2000 and July 2010 (when both measures were available). The difference between the AEI and AWE wage growth should not be over-interpreted, as there is considerable uncertainty introduced by the estimation process. As these historic time series are now only available up to 1999, even though the AEI was not discontinued until 2010, there is no fully consistent complete time series for these data sets up to the present time.

A3.26 AWE revisions were carried out in 2017 and 2019 following regular reviews of the methodology used to calculate estimates of earnings of employees in small businesses. Businesses with fewer than 20 employees are excluded from the Monthly Wages and Salaries Survey, which is largely used for the calculation of the AWE. To compensate for this omission, pay is estimated using a factor derived from ASHE, which does cover small businesses. Changes were announced that aim to better reflect earnings of employees in small businesses as well as reflecting improvements to the coverage of small businesses on the main sampling frame, the Inter-Departmental Business Register. Details of the findings of the most recent review and revisions made as a result can be found in Office for National Statistics (2019).

A3.27 In April 2020, lockdown measures and furloughing led to significant changes in employee pay, making it necessary to change the way that AWE data were processed. Normally, when companies do not respond their employee and pay information is imputed based on their most recent previous response. But in a period where there had been substantial pay changes, this imputation may not always be accurate. The ONS therefore increased the level of data validation over this period. Response rates were 84 per cent by August 2023, close to pre-pandemic levels. As a result, AWE validation is back to normal.

Average earnings forecasts and projection of the path of the minimum wage

A3.28 We project the path for the minimum wage using three data sources. First, we calculate a baseline estimate of median hourly earnings. We do this using the ASHE data. This estimate is based on the eligible population for the NLW. It excludes overtime and shift premia and excludes workers with less pay than normal due to sickness or absence (based on the "lop" loss of pay variable in the ASHE dataset). We also exclude workers where their hourly pay estimate is zero or the low-pay weight is missing.

A3.29 Second, we use the 12-month smoothed growth rate of AWE total pay (ONS Code: KAB9) to project the growth rate of median hourly earnings in each month between the latest ASHE data and the latest available AWE data.

A3.30 If there are more than 6 months of AWE data since the latest ASHE publication, we calculate the smoothed AWE growth rate for the relevant 6 month period and use it in our projections. We then use the latest AWE data for any remaining months of available AWE data. For instance, if the latest AWE data relates to December and the latest ASHE data relates to April, we would apply the 12-month smoothed October AWE growth rate to the six months between April and October and then the 12-month smoothed December AWE growth rate for the remaining months between October and December.

A3.31 Finally, we use forecasts for average earnings to project the growth of median hourly earnings for periods where no AWE or ASHE data are available. We take these forecasts from the HM Treasury panel of independent forecasts (Table 2 and Table 5 from HM Treasury (2024j) and Table M6 from HM Treasury, 2024h). The Bank of England (2024c) conditioning assumptions on average wage growth are added to the panel and included in those medians. Since August 2024, the Bank of England (2024c) has only published these for private sector AWE growth.

A3.32 We assume that pay grows at the same rate each month within the year in our projection. For instance, if the forecast growth rate for pay in a given year is 5 per cent (and we only have forecast data for that year), we would assume that each month pay grows by 0.4 per cent month-on-month as growth at this rate compounds over 12 months to equal 5 per cent.

A3.33 Projections for median pay in the future are inherently uncertain. Moreover, since the pandemic pay forecasts have become a less reliable guide to future pay. To reflect these uncertainties, we project a range around our central estimate for the on-course rate. This lower end of the range assumes pay grows 1 percentage point a year slower than in our central projection and the higher end of the range assumes pay grows 1 percentage point a year faster than in our central projection. This is not a formal confidence interval, it is based on judgement and an assessment of previous forecast errors.

Labour Force Survey

A3.34 The Labour Force Survey (LFS) is the official data source used to measure employment and unemployment. It is a quarterly survey of around 60,000 UK households conducted on a rolling monthly basis and provides information on: employment, unemployment, earnings, and personal and socio-economic characteristics, including gender, ethnicity and disability.

A3.35 Analyses of aggregate employment, unemployment and hours worked use seasonally adjusted monthly and quarterly LFS data published by ONS using the latest population weights. For detailed analyses of the labour market by age, ethnicity, disability and other personal characteristics, we conduct analyses using the non-seasonally adjusted quarterly LFS microdata. We generally use the four-quarter moving average of these outputs to take some account of seasonality, which is different to the seasonal adjustment method used by ONS.

A3.36 The pandemic introduced a number of issues for surveys. Lockdown meant a move to telephone-only interviewing but a side effect of this was the introduction of additional non-response bias to the survey. ONS introduced a number of temporary measures to address this: for example, housing tenure-based weights were used to produce revised datasets in October 2020. In July 2021, ONS also introduced the use of HMRC RTI data to improve the population weights used to produce labour market estimates.

A3.37 This report uses the LFS microdata published in August 2024, and aggregate data published in October 2024. These have been reweighted based on the 2022 mid-year population estimates. Revised data using the latest weights are only available back to the July-September 2022 data, introducing a break in the series.

A3.38 As with the ASHE data, the LFS has transitioned from coding occupations on a SOC 2010 basis to a SOC 2020 basis but SOC codes for both systems continue to be provided.

Falling LFS response rates

A3.39 A major concern in recent years has been the reduction in survey response rates. While they had been steadily decreasing since 2015, the issue was accelerated by the pandemic. In July 2020 ONS responded by doubling the issued sample but this was then reduced back to 160 per cent in May 2021 when ONS rolled out a Knock to Nudge programme to improve response rates. The issued sample was reduced further to 150 per cent of pre-pandemic levels in November 2021, before rising slightly to 155 per cent in January 2022.

A3.40 In March 2022 ONS announced (ONS, 2022b) plans to move to the Transformed Labour Force Survey (TLFS). The online-first successor to the LFS would deliver increased coverage and make the survey more representative of the population as a whole. ONS also planned to make more use of administrative data. As part of the complex transformation of the TLFS a period of dual running alongside the LFS was proposed to identify differences in findings.

A3.41 Response rates for the LFS continued to fall, however. Smaller samples mean there is a greater chance the data is not representative and is less likely to accurately reflect the true number of people who are employed, unemployed, or economically inactive. There is also greater variability from quarter to quarter, making the data less reliable. In July 2023, the LFS sample was reduced back to pre-pandemic levels – the result was a reduction in the overall response rate to just 15 per cent. Several organisations, including the Resolution Foundation, the Financial Times and the Institute for Employment Studies voiced concerns over the reliability of the LFS data. The ONS paused publication of LFS estimates in October 2023.

A3.42 Since the final quarter of 2024, the ONS has introduced several measures to increase the achieved sample, including increasing the planned sample from Q1 2024. Since February 2024, it has resumed publication of LFS estimates, but they remain 'official statistics in development'. The move to using the TLFS as the main source of labour market data has also been delayed.

PAYE Real Time Information

A3.43 An additional data source that allows us to understand trends in the number of employees and their earnings is from HMRC's Real Time Information (RTI) administrative data derived from Pay As You

Earn (PAYE) records. We refer to these data as the PAYE data. Rather than using a sample, as with the other data sources discussed above, PAYE data covers the whole population of employees paid through PAYE. Monthly statistics are produced on the number of employees and the distribution of pay for the population of nearly all employees in the UK. The data are available by age, industry and region, but they are not available by gender. The data do not include the number of hours worked, and so cannot be used to estimate hourly pay, but the data provide information on median and mean monthly pay and the median of pay growth.

A3.44 Where we use PAYE data, this provides information on the number of employees, not the employment rate. This means that rises and falls can also be related to changes in the total population, due, for example, to shifts in migration patterns or the changing age profile of the population. Although these changes usually occur over an extended period, the pandemic precipitated dramatic changes in migration. This is most likely to affect workers in their mid-20s and 30s. Demographic changes will also be more pronounced for the under 18 and 18-24 age groups as they are smaller age groups.

Differences between PAYE and other data sources

A3.45 Administrative data sources cannot be directly compared with estimates from surveys where the administrative system is measuring a different concept to the survey, or where the population coverage is different. Statistics derived from PAYE administrative data are not directly comparable with statistics from AWE, ASHE and LFS because of differences in measurement and coverage.

A3.46 The number of people receiving pay from PAYE employment is higher than in the LFS employee series. This is likely to be because RTI covers a different population to the LFS. PAYE administrative data includes all individuals who are employed in a PAYE scheme and who were paid in the reference period, while the LFS sample has no coverage of those aged under 16 or temporary residents in the UK, but has a stronger coverage of people who are in work but not being paid. A further difference arises because PAYE administrative data classifies any person receiving pay through a company payroll as being an employee, while the LFS only classifies a person as an employee if the interviewee describes themselves as an employee in their main job.

A3.47 Statistics on pay are also not directly comparable with AWE or ASHE. As well as published administrative PAYE pay measures being on a monthly basis, PAYE estimates include earnings of employees whose pay was reduced for any reason and do not distinguish between full- and part-time work. PAYE estimates are calculated on a person basis, including all jobs for which an individual is paid through the Pay as you Earn tax system, while AWE and ASHE estimates are calculated on a job basis. This difference causes RTI estimates to be higher than AWE estimates. PAYE estimates also include redundancy payments paid through payroll.

Inflation and price data

A3.48 We discuss the range of consumer inflation data available in Chapter 4. We also use a range of inflation measures that reflect price changes for business, including the Services Producer Price Index (SPPI), Producer Price Indices (PPI), as well as the broad GDP deflator.

A3.49 Of the ONS' consumer price statistics, each measure uses the same basic price data, but there are differences in the basket of goods and services used to calculate overall inflation, the way spending is weighted across different parts of the population, and some of the calculations used to aggregate the prices. The CPI (which follows international definitions) excludes Council Tax and a number of housing costs faced by homeowners that are included in the RPI and CPIH. The RPI is never revised and the CPI, although revisable in theory, has never been revised. CPIH includes costs associated with owning, maintaining and living in one's own home (known as owner occupiers housing costs) along with Council Tax, which are excluded from CPI. It has been revised twice when a new method was introduced. The first revision was on 24 March 2015, which incorporated improvements to the measurement of owner occupiers' housing costs. The second was on 21 March 2017, incorporating council tax and revised weights for owner occupiers' housing costs. In both cases, the full back series was revised. ONS does not intend to make any further revisions.

A3.50 This year, we have also made use of the Household Cost Indices (HCI). These measure the inflation experienced by different types of households. Different indices are constructed for households that have children and those that do not; retiree and non-retiree households; by home ownership status; and for each household income decile. In addition to the headline HCI measure we focus on the indices constructed for low-income households as these are likely to better reflect the experience of minimum wage workers.

A3.51 There are some important differences the CPI and HCI. Whereas CPI weights reflect total expenditure shares by households in the economy, HCI weights are based the average household's expenditure shares. Because of this HCI is better able to captures the experience of a typical household. Further, HCI attempts to capture the change in prices of goods and services as households pay for them, rather than at the time they were acquired (the approach used to construct CPI and CPIH). This includes changes in the cost of repaying interest on debt, as well as payments that households make to own and live in their own home, such as mortgage interest payments, stamp duty, and the costs of major repairs and maintenance.

A3.52 The Services Producer Price Index (SPPI), Producer Price Indices (PPI) and the GDP deflator focus more on the costs for businesses. Producer price inflation, derived from the PPIs, measures changes in the prices of goods bought and sold by UK manufacturers, including price indices of materials and fuels purchased (input prices) and factory gate prices (output prices). The input price measures the price of materials and fuels bought by UK manufacturers for processing. It includes materials and fuels that are both imported or sourced within the domestic market. It is not limited to materials used in the final product but includes what is required by businesses in their normal day-to-day running, such as fuels. The factory gate price (output price) is the amount received by UK producers for the goods that they sell to the domestic market. It includes the margin that businesses make on goods, in addition to costs such as labour, raw materials and energy, as well as interest on loans, site or building maintenance, or rent. The input and output producer prices are published monthly.

A3.53 In July 2022, ONS extended the back series by making historical data readily available and revising the index to 2015=100. The headline PPI output series (GB7S) now goes back to January 1957. The headline input series (GHIP) now includes a back series to January 1984. Unlike the headline output index, the input headline was first introduced in the early 1990s. The addition of these back series does not affect the methodology used to calculate the previous ONS data to 1973. For the periods January 1957 to December 1972, ONS rescaled data from a number of historical rebased series to make these comparable with previously published data.

A3.54 The SPPI provides quarterly estimates of inflation in services bought and sold by UK businesses. There has been no change to the methodology since January 2021, when the SPPI was produced with an annual weight update using the annual chain-linking method recommended by Eurostat. Previous SPPIs had their weights updated every five years using the rebasing method.

A3.55 The GDP deflator represents the broadest measure of inflation in the domestic economy, reflecting changes in the price of all goods and services that comprise GDP. It is important to note that the GDP deflator covers the whole of the economy, not just consumer spending. Movements in the implied GDP deflator in 2020, 2021 and 2022 have been largely affected by the Government consumption deflator, which is the expenditure that is incurred by the Government in producing non-market goods and services, such as health and education. The volume of government activity fell while at the same time government expenditure increased in nominal terms, reflecting how ONS record volume estimates of education and health.

Measuring price changes for items 'more exposed to the minimum wage'

A3.56 We also use the price microdata underlying these price indices and other ONS price statistics. These data have been made available by ONS since 2017 for research purposes only. They include the individual price quotes from which the ONS calculate its price indices and pre-calculated indices for the individual items that form part of the basket of goods used to measure inflation.

A3.57 Data are available for 2010 onwards for price quotes and 2005 onwards for item indices; however, during the pandemic there was serious disruption to price collections. For sectors that were shut down, prices could not be collected at all, and in-person price collection of other items could not take place in some months, leading to large reductions in sample size. In its item indices, the ONS imputed values for each item where there were gaps. This was typically done in such a way as to minimise the impact on the overall price index, and so imputed indices should not be used for comparing price changes of individual items. Price quotes data have not been imputed. In order to avoid the impact of these data collection issues, we avoid using price data for individual items during the period of disruption.

A3.58 When comparing price changes between items and sectors most exposed to the minimum wage and others, we follow the method used by Wilson (2020) for compiling item-region indices. We then weight these indices using each item's CPI item weight as a share of the total CPI weight of exposed and less exposed items respectively. This approach helps to control for the fact that some sectors have many more items assigned to them than others and so would otherwise be disproportionately represented in the overall index. However, this should be considered a 'naïve' approach to weighting, as we have not adjusted the CPI weights to reflect the varying contribution of different regions to overall inflation. For example, the hourly rate for a domestic cleaner in Wales will receive the same weight as the hourly rate for a domestic cleaner in London. Similarly, weights do not reflect different patterns of expenditure in different regions.

A3.59 Our classification of those products most exposed to the minimum wage and our mapping of items to sectors are taken from the data published in Wilson (2020) and Frontier Economics (2020). These studies used data on wages and turnover from 2015-2018 to calculate exposure at the sector and region level. Due to data availability, we were not able to update these calculations this year, although we will look to do this once sufficient data beyond the pandemic is available. Our estimates only include those items which appear in the basket of goods across the whole period we examine. This is unlikely to have a noticeable effect on our estimates: the vast majority of items added each year are tradeable items, which we exclude to limit the effects of international price movements on the analysis.

Gross Domestic Product

A3.60 GDP provides a measure of total economic activity. It is often referred to as one of the main 'summary indicators' of economic activity and is used to measure growth in the economy. In 2018, the ONS introduced a new publication model for GDP, reducing the number of published estimates of quarterly GDP from three to two. It sought to balance timeliness with accuracy of GDP estimates, with the aim of reducing the likelihood and frequency of revisions. It also enabled the publication of monthly estimates of GDP.

A3.61 Quarterly GDP: The first quarterly estimate of GDP is published 40 days after the quarter to which it refers. This is two weeks after the previous model's preliminary estimate (but in line with other G7 release schedules) and so will contain higher quality output data. It also contains information from the income and expenditure approaches two weeks earlier than in the previous model although the data content will be less than in the previous second estimate. A comprehensive (second) estimate of GDP continues to be released as part of the Quarterly National Accounts, available 85 days after the end of the reference quarter as previous.

A3.62 Monthly GDP: the ONS brought forward the Index of Services release by two weeks, which, alongside the Index of Production and the Index of Construction allow production of a combined monthly estimate of GDP using the output measure, the timeliest of the three GDP measures, and the only one available on a monthly basis.

Blue Book 2024 changes

A3.63 The Blue Book, published annually by ONS, presents a full set of economic accounts for the UK. It outlines any methodological changes made to the National Accounts in addition to the normal quarterly process of incorporating new information into its estimates of economic activity. The 2024 Annual National Accounts, also known as Blue Book 2024, incorporated a small number of improvements to sources and methods (ONS, 2023 and 2024). These include the implementation of outstanding classification decisions affecting the public sector, improvements to healthcare volumes to use more comprehensive data sources and updates to the UK trade gas exports deflator. The base year for chained volume estimates of GDP has now been moved on to 2022, after several publications using 2019 as the base year to avoid using years affected by the pandemic. These changes primarily affect the years from 2020 onwards.

Business Insights and Conditions Survey

A3.64 In March 2020, ONS introduced a new fortnightly business survey to understand how firms have been affected by the pandemic and lockdown measures. It captures firm-level data on how their turnover, workforce, prices, trade and business resilience have been affected in the two-week reference period. Each two-week period is referred to as a “Wave”. Prior to Wave 7, results were unweighted but apportioned by responding business employment size. From Wave 7 onwards results were weighted by employment for industries sampled in the survey.

A3.65 In November 2020, the Business Impact of Coronavirus (Covid-19) Survey was superseded by the Business Insights and Conditions Survey (BICS). At this time (Wave 17) the survey increased its representative sample to 39,000 businesses with a response rate around 25 per cent. The published data continue to provide weighted estimates from businesses on financial performance, workforce, prices, trade and business resilience. The latest data available were from Wave 116 (Wave 115 for microdata), covering the reference period from 1-31 August 2024.

A3.66 Over time ONS has dropped survey questions that are no longer applicable, replacing them with more relevant questions. These are documented in their published spreadsheets each Wave. To reduce the burden on firms the frequency of some questions has also extended from every survey to every other or even every four surveys. In February 2024 (Wave 102) following stakeholder engagement BICS moved to two publications a month as opposed to every two weeks.

A3.67 For this report we have made greater use of this firm level resource by analysing the BICS microdata through the ONS' Secure Research Service. As part of this analysis we combined the data with our definition of low-paying sectors to allow us to compare responses from firms operating in low-paying sectors with those in non-low paying sectors.

A3.68 This analysis uses statistical data from ONS which is subject to Crown Copyright. The use of the ONS statistical data in this work does not imply the endorsement of the ONS in relation to the interpretation or analysis of the statistical data. This work uses research datasets which may not exactly reproduce National Statistics aggregates. The analysis was carried out in the Secure Research Service, part of the Office for National Statistics.

Family Resources Survey

A3.69 The Family Resources Survey (FRS) is a continuous household survey published by the Department for Work and Pensions. It collects detailed information on the financial situation of private households, along with information on their living circumstances, such as housing tenure. Data is collected throughout the relevant financial year. We use FRS data to look at households with one or more NLW workers, and to understand the different roles NLW workers play within their households.

A3.70 We define NLW jobs in the FRS broadly as we do within ASHE: any job with hourly pay less than the prevailing rate of the NLW plus 5 pence. We calculate this using stated hourly pay where available and a derived measure using usual weekly pay and hours if not. Note that this can include overtime, which differs from the definition used in ASHE (as does the use of stated hourly pay). An NLW worker is defined as any worker with an NLW job (regardless of whether they have other, non-NLW jobs or income sources) and an NLW household is defined as any household with at least one NLW worker.

A3.71 As we would expect from survey data collected directly from households, estimates of hourly pay tend to be lower than ASHE (where data is collected from employers) and by extension estimates of coverage are higher. This means that the number and share of 'NLW households' is not directly comparable with our headline estimate of job-level coverage from ASHE.

A3.72 Where using FRS data, we generally report estimates for all workers covered by (or paid less than) the NLW, regardless of age. We do this to reflect the full range of households where a member's income is likely to be affected by changes in the NLW, as well as for simplicity. The relevant population is reported in the notes below each figure or table.

A3.73 Some of our FRS analysis splits workers by their role within the household. It is not possible to perfectly separate the different roles as there is often overlap between them (e.g. someone may be both living with their parents and the highest earner in the household). Judgment is needed to decide how to deal with the range of household structures and income sources households may have. We tend to be most interested in earnings from work, as this is where the direct impact of the NLW is felt. The definitions (and hierarchy of assignment) that we use are detailed in Table A3.1.

Table A3.1: Definition of NLW worker roles within the household

Role	Definition
Living with parents	Child (including step- or adopted children) or grandchild of the Household Reference Person (HRP). This category is assigned fist, and regardless of earnings, so takes precedent over 'highest earner'.
Highest earner	The individual with the highest **total weekly earnings from work** in the household, excluding those who (a) are not related to the HRP; (b) reported that they live in a shared household, or (c) are already assigned to 'living with parents'. It is possible to have two highest earners in a household if they both earn exactly the same amount. For NLW workers, it is possible that their total earnings include both NLW and non-NLW jobs. Other household members may have higher incomes if these come from non-work sources. This category is assigned second and so takes precedent over those below.
Secondary earner	This includes spouses, cohabitees or civil partners of the highest earner or HRP; parents or grandparents of the HRP and others who don't fall under the other definitions.
Shared household or lodger	This includes (a) all members of households that report they are 'shared households'; (b) individuals not related to the household reference person; (c) the household includes one or more groups of unrelated individuals, no dependent children and the individual is not the spouse, parent or child of the HRP.

Youth population estimates

A3.74 In Chapter 6, we compare the youth population to the RTI employment level. The youth population is calculated using mid-2023 UK population estimates for 2019 to 2013 (released October

2024) and 2021-based interim UK population projections for 2024 population figures (released January 2024).

A3.75 These population figures differ from the population estimates used in the Labour Force Survey (LFS). At the time of analysis, the LFS had been reweighted based on the mid-2022 population estimates (see previous section on the Labour Force Survey).

Low-paying industries and occupations

A3.76 Last year, we reviewed our definitions of low-paying industries and occupations. These are the industries and the occupations which are most exposed to minimum wage rises. The table below sets out which industries and occupations are included within our updated definitions. A detailed discussion of the review and detailed mapping tables are available on our website (Low Pay Commission, 2023b)

Table A3.2: Low-paying industries and occupation definition

Low-paying industry/occupation	Current industry definition (SIC 2007)	Current occupation definition (SOC 2020)
Retail	45, 47, 77.2, 95.2	3553, 3555, 5443, 7111, 7112, 7114, 7115, 7121, 7123-7132, 7219, 9241, 9249
Hospitality	55, 56	5434-5436, 9261,9263–9266
Social care	86.102, 87, 88.1	6135-6137
Employment agencies	78.1, 78.2	-
Cleaning and maintenance	81, 96.01	6231,6232, 6240, 9131,9221-9229
Leisure	59.14,79, 92, 93, 96.09	3413, 3431-3433, 6129, 6211, 6212, 6219, 9267, 9269
Food processing	10.1-10.3, 10.7-10.8	5431-5433, 8111, 9132
Wholesale food incl. agents	46.2, 46.3,52.1	-
Childcare	85.1, 88.91	3232, 6111, 6114, 6117, 9232
Agriculture	01,03,75,	5112-5114,9111- 9119
Security and enforcement	80.1	6312, 7122, 9231
Textiles and clothing	13, 14, 15	5411-5413, 5419, 8112, 8146
Hair and Beauty	96.02, 96.04	6221,6222
Office work	-	4131,4152,4159, 4212,4214, 4216,4217, 7212, 9219
Non-food processing	20.4, 22.2,23.4,23.7, 27.3, 32.1-32.4,	5422, 5423, 5442, 8114, 8119, 8131, 8135, 8139, 8141, 8144, 8149, 9129, 9139
Storage	-	9252-9259
Transport	49.32,49.39,53.2,	8145, 8213, 8214, 8219, 8239

Low-paying industry/occupation	Current industry definition (SIC 2007)	Current occupation definition (SOC 2020)
Call centres	82.2	7113, 7211
Activities of other membership organisiations	94.9	-
Education	-	4135, 4213, 6112-6113, 9233
Healthcare	-	6131, 6133, 9262

Appendix 4

International evidence

International developments in minimum wages

A4.1 To inform our recommendations on National Minimum Wage (NMW) rates in the UK, we monitor developments in other countries' minimum wages and maintain relationships with counterpart bodies around the world.

A4.2 In light of the inclusion of living costs in our remit, we were particularly interested this year in how other countries approach the question of minimum wages and living standards. One of the most common factors driving different countries' minimum wage policies in recent years has been the surge in inflation since the pandemic, putting pressure on both real average wages and the real value of minimum wages. Eurofound (2024) in its annual review of minimum wages noted that minimum wages in most member states had increased in real terms in 2024. This reversed the loss of purchasing power experienced by minimum wage workers in many countries between 2021 and 2023. Eurofound (2024) offers a survey of the different criteria countries use in setting minimum wages. It identified 14 countries which use inflation rates and eight which use a target a value relative to average wages. Other lesser used criteria included gross domestic product, unemployment and employment levels and labour productivity.

A4.3 At the European level, the European Commission's directive on adequate minimum wages, adopted in 2020, has continued to shape policy in EU member states. The directive requires member states to demonstrate the "adequacy" of minimum wages in two dimensions: i) if they are fair in relation to the wage distribution in the relevant member state and ii) if they provide a decent standard of living for a full-time worker. The deadline for transposition of the directive was November 2024, with national policy still to be determined in some countries. Eurofound told us that it was more common for member states to define adequacy on the basis of the first dimension, fairness in relation to the wage distribution, than in relation to workers' living standards.

A4.4 In March 2024, the International Labour Organization (ILO) adopted a tripartite agreement on wage policies, including living wages (ILO, 2024). The ILO's agreement set out some common principles to be used in estimating living wages. These principles include evidence-based methodologies to estimate the needs of workers and their families; consultation with social partners; and the use of transparent, robust and timely data. The ILO's conclusions note that the implementation of living wages needs to reflect national circumstances and take account of various factors.

Needs-based approaches

A4.1 As discussed in Chapter 4, the European Union's (EU) adopted a directive on adequate minimum wages, adopted in 2020, states that minimum wages are considered to be adequate if "they are fair in relation to the wage distribution in the relevant Member State and if they provide a decent standard of living for workers based on a full-time employment relationship". Most EU countries have focused on the former rather than the latter. Only two EU countries – Romania and Slovenia have passed laws to introduce a statutory living wage.

A4.2 In Romania, Law 174/2020 provides a method for estimating the living wage at a national level and stipulates that the minimum wage should be set while considering this estimate. It also stipulates that the National Institute of Statistics should calculate and officially publish the living wage estimate periodically. It has not yet done so, claiming technical errors in the text of the law prevent it from doing so. Government officials have thus ignored this law when setting the minimum wage.

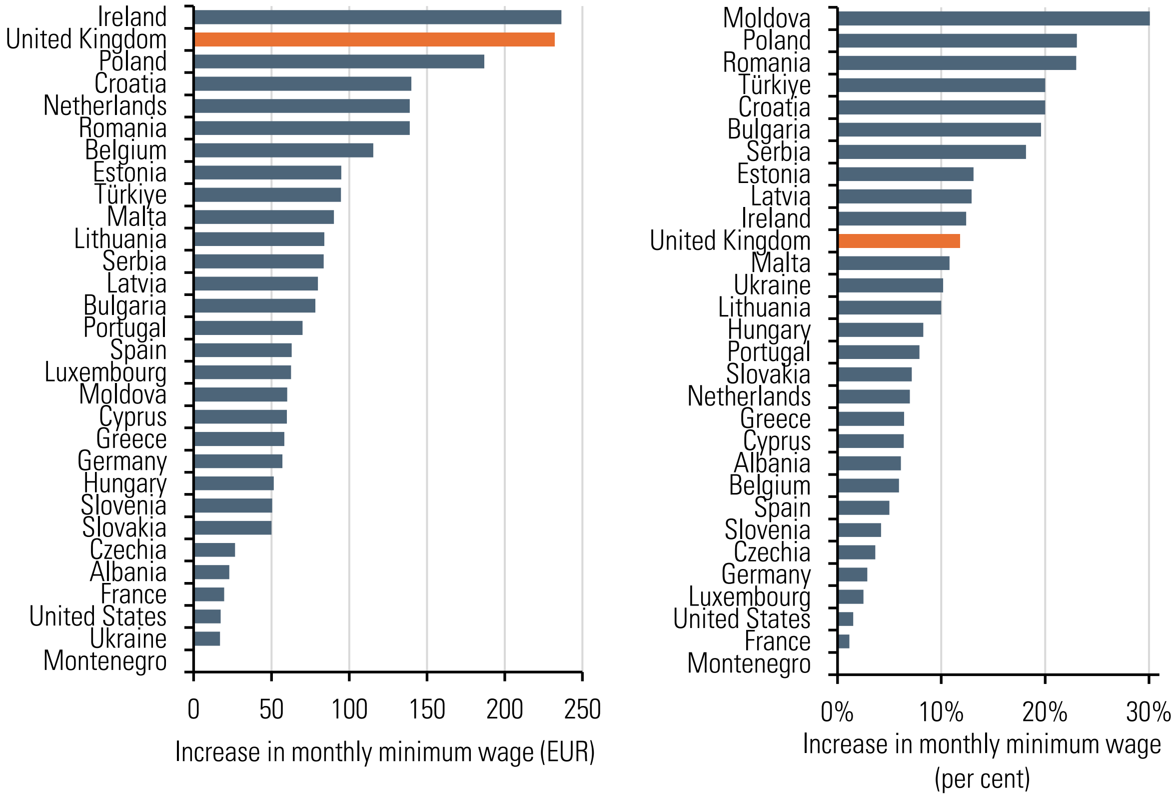
A4.3 Slovenia has a statutory minimum wage which is governed by the Minimum Wage Act. According to the Slovenian Minimum Wage Act, social partners (employers' organizations and trade unions) must be consulted prior to setting the amount of the minimum wage and its yearly indexation. The calculation of the minimum wage is based on a formula which takes into account the minimum costs of living. The act stipulates that the net minimum wage has to be set between 120 per cent and 140 per cent of the minimum living costs, which are calculated every six years. The latest calculation of the minimum living costs was carried out in October 2022. The formula also states that the minimum wage should be adjusted at least by the level of inflation. Therefore, in addition to the yearly adjustment by the consumer prices, the minimum wage is also increased every six years to adhere to the minimum living costs criteria.

Comparing minimum wage upratings between countries

A4.4 It is challenging to compare minimum wages between countries. The same nominal wage may go further in one country than another. Tax and social security systems vary hugely, as do other non-wage benefits available to workers. In addition to this, countries uprate their minimum wages at different points in the year.

A4.5 Figure A4.1 uses data from Eurostat to compare increases between 2023 and 2024 in a number of European countries and the United States. Eurostat's data use monthly values, converted into Euros. On this basis, the UK's April 2024 uprating was the second highest in this period among the countries surveyed; in percentage terms, several Eastern European countries implemented larger increases.

Figure A4.1: Increases in monthly minimum wages, by country, H2 2023-H2 2024



Source: LPC estimates based on data from Eurostat. Minimum wages (Online data code: tps00155), half-yearly, 2023 H2-2024 H2.
Note: Minimum wage changes are between the applicable rates in July 2023 and July 2024.

A4.6 Our annual international workshop was held in September 2024 and attended by representatives from the bodies setting minimum wages in France, Germany, Ireland, the Netherlands, and Spain, as well as representatives from Sweden, the ILO, the Organisation for Economic Cooperation and Development (OECD) and Eurofound. We also received updates from counterparts in Australia and New Zealand. At the time of our recommendations, we had several examples of other countries' recent and forthcoming recommendations for minimum wage increases. In general, countries with similar profiles to the UK have generally announced lower increases for 2025 than implemented in 2023 or 2024.

A4.7 In Australia, the National Minimum Wage sets a pay floor but is overlaid by a wide range of sectoral awards which set minimum pay rates and working conditions in different sectors. The Fair Work Commission makes recommendations on both the minimum wage and the award minimum rates. This year it recommended an increase in the National Minimum Wage of 3.75 per cent, which was implemented in July. The same increase applied to its award minimum rates. This compared with an increase of 5.75 per cent in 2023 and 5.2 per cent in 2022. Following a 7.1 per cent increase in April 2023, the New Zealand Government implemented an increase of 2 per cent in April 2024.

A4.8 The Netherlands increased its minimum wage by 3.1 per cent to €13.68 in July from €13.27 in January (and from €12.12 in July 2023 – an annual increase of 12.9 per cent on the year). Increases to the minimum wage in the Netherlands involve both an indexation mechanism and political choices following consultation with social partners. In January 2024, the Dutch minimum wage became an hourly minimum wage. There is no longer a monthly, weekly or daily minimum wage. The minimum wage will increase again in January 2025.

A4.9 In Germany, minimum wage upratings usually follow a two-yearly cycle. The minimum wage will increase by 3.5 per cent in January 2025, from €12.41 to €12.84. This is the second part of a recommendation made by the German Minimum Wage Commission and follows an increase of 3.4 per cent in January 2024. This in turn followed a large uprating of around 15 per cent to €12 in October 2022, upon the appointment of a new Government.

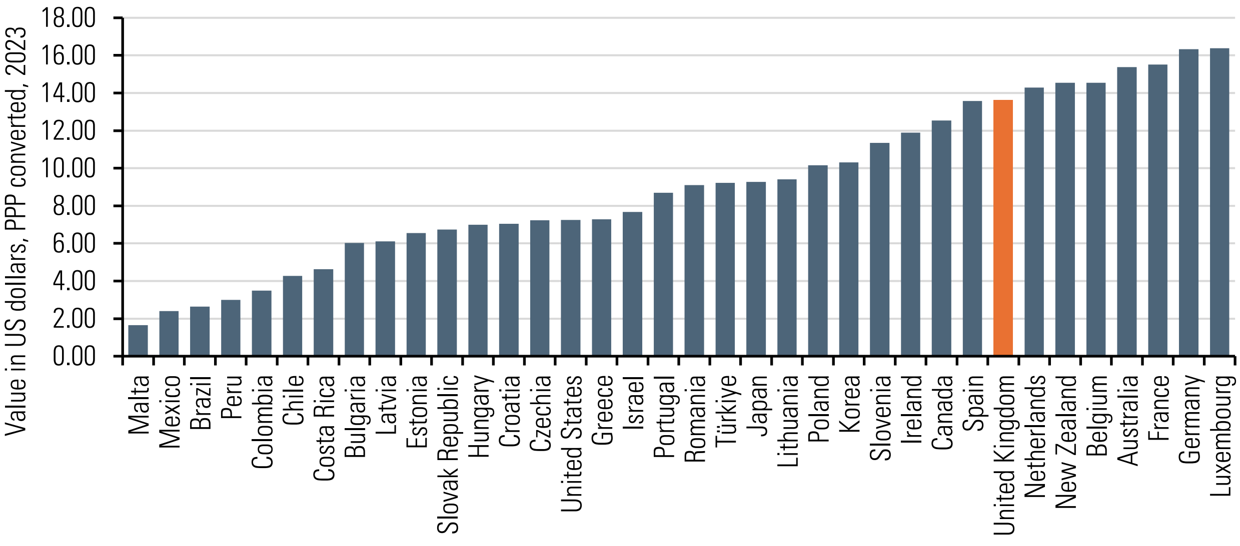
A4.10 In Ireland, the minimum will increase by 6.3 per cent to €13.50 in January 2025, as part of a commitment to reach 60 per cent of median earnings by 2026. That followed an increase of 12.4 per cent from €11.40 to €12.70 in January 2024.

A4.11 On 23 October, the French Government announced a special minimum wage increase of 2 per cent would be implemented on 1 November 2024, driven by CPI indexation, taking the hourly minimum from €11.65 to €11.88. This brought forward the increase that was expected in January 2025.

Comparing minimum wage levels between countries

A4.12 To more fairly compare minimum wages between countries, we need to adjust for purchasing power – that is, we need to take account of what a worker on the minimum wage can purchase in different countries. The OECD produce comparisons of different national minimum wages adjusted for purchasing power parity (PPP). The latest available data reflect minimum wages in 2023 (so before the uprating of the National Living Wage to £11.44) and they use an average value calculated across the whole calendar year. As Figure A4.2 shows, the UK sits comfortably in the upper half of the OECD's rankings, although PPP-adjusted minimum wages are still higher in several neighbouring West European countries as well as Australia and New Zealand.

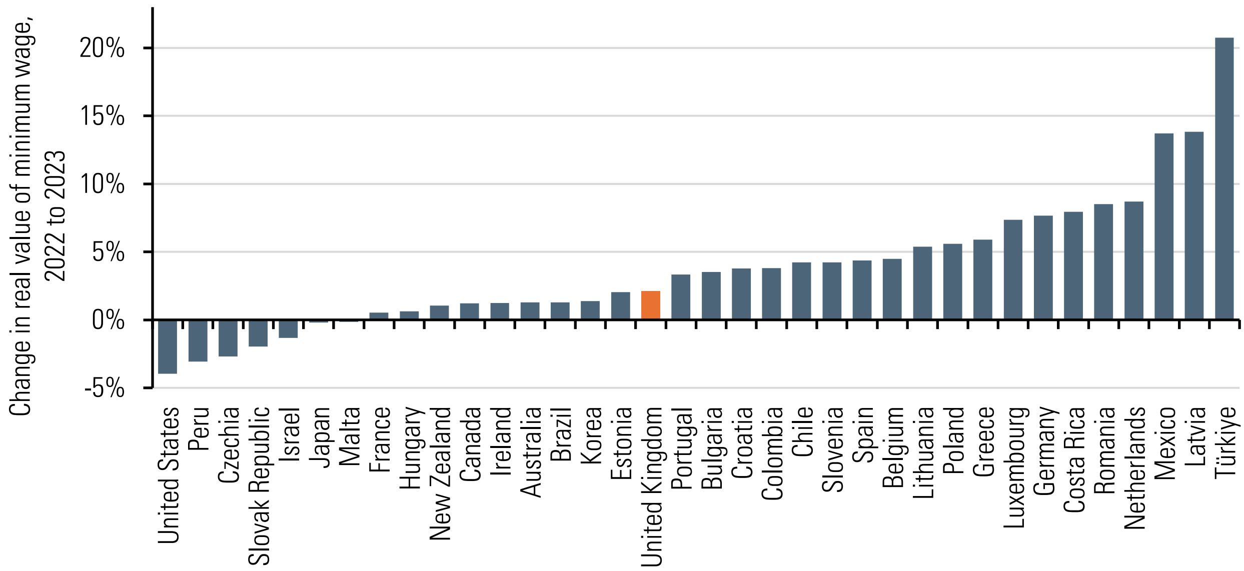
Figure A4.2: Comparison of international minimum wages adjusted for purchasing power parity, OECD countries, 2023



Source: LPC estimates based on OECD data. OECD Data Explorer. Real minimum wage data in 2023 constant prices at 2023 US$ purchasing power parities, OECD countries. (Real minimum wages at constant prices, hourly, US$, PPP converted, 2023).
Note: Minimum wages are converted by OECD to an annual value to enable comparison across the whole of 2023.

A4.13 Figure A4.3 compares the real increases in minimum wages between 2022 and 2023. The real value of the NLW did increase in this period, but the surge in inflation meant this real increase was substantially less than the 9.7 per cent nominal increase when the rate rose from £9.50 to £10.44. Most – but not all – countries in the OECD's rankings implemented a real-terms increase. The UK sits around the middle of the pack.

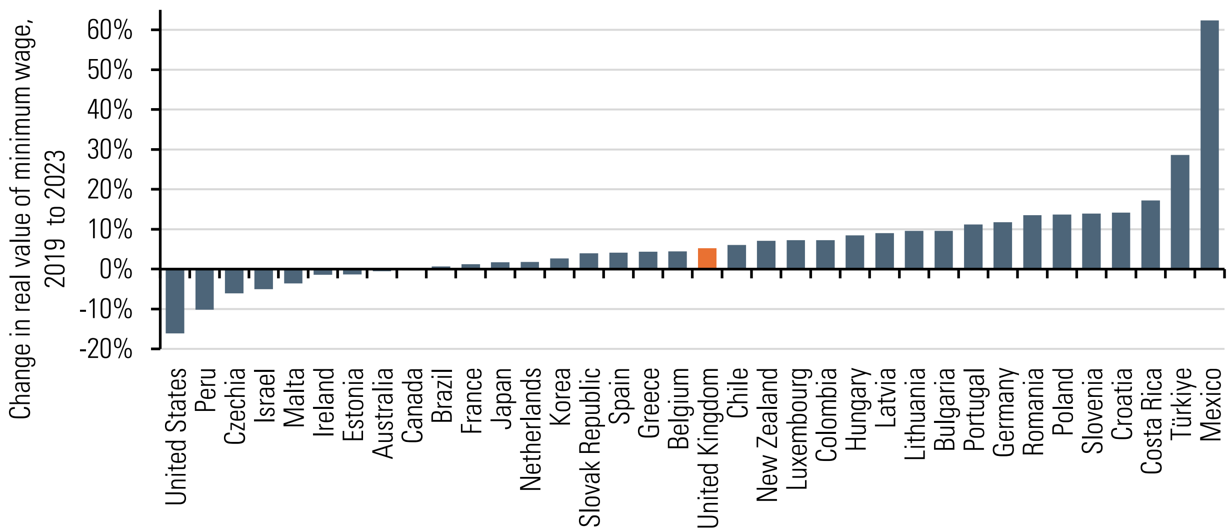
Figure A4.3: Change in the real value of minimum wages, OECD countries, 2022-2023



Source: LPC estimates based on OECD data. OECD Data Explorer. Real minimum wage data in 2023 constant prices at 2023 US$ purchasing power parities, OECD countries. (Real minimum wages at constant prices, hourly, US$, PPP converted, 2022-2023).
Note: Minimum wages are converted by OECD to an annual value to enable comparison across the whole of the year in question.

A4.14 The same is broadly true when looking at a longer time period, from 2019 to 2023. Many of the countries which have implemented large real increases over this period started from a low base and have a PPP-adjusted minimum wage in the lower half of the OECD's rankings.

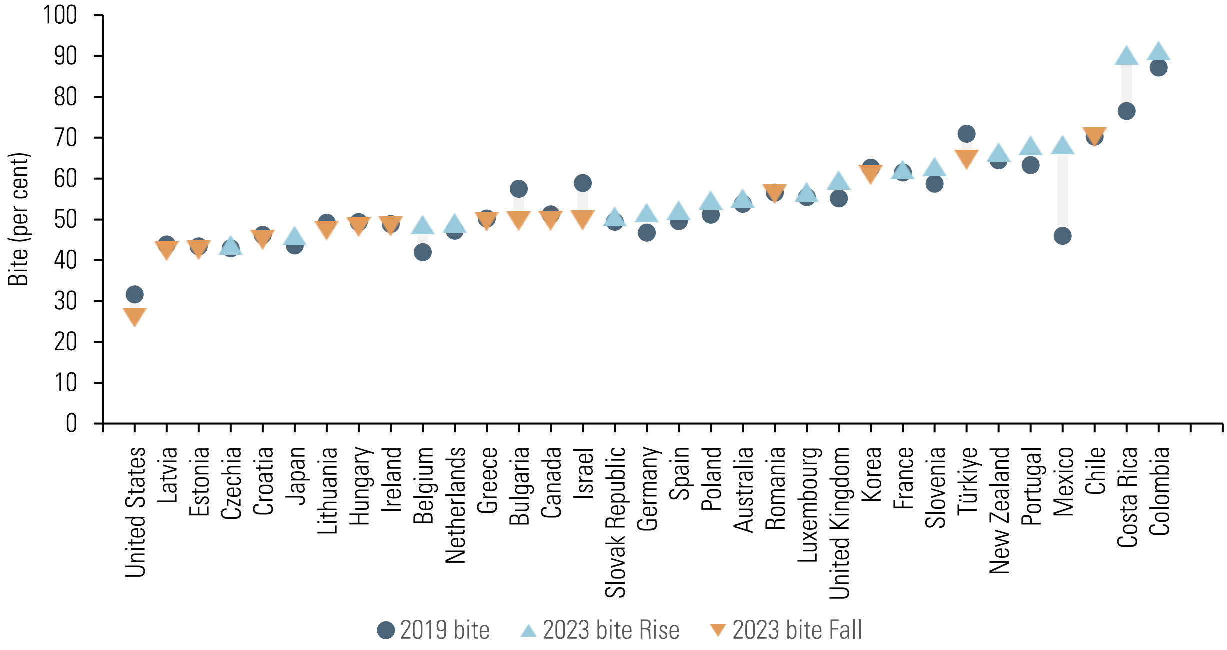
Figure A4.4: Change in the real value of minimum wages, OECD countries, 2019-2023



Source: LPC estimates based on OECD data. OECD Data Explorer. Real minimum wage data in 2023 constant prices at 2023 US$ purchasing power parities, OECD countries. (Real minimum wages at constant prices, hourly, US$, PPP converted, 2019-2023).
Note: Minimum wages are converted by OECD to an annual value to enable comparison across the whole of the year in question.

A4.15 The OECD data also allows for a comparison of the bite of the minimum wage between different countries. Figure A4.5 shows the OECD's calculation of the change in the bite of different countries' minimum wages between 2019 and 2023. As this is calculated on the basis of full-time workers only, it differs from our own calculations of the NLW's bite. On this basis, the bite of the minimum wage in the UK is in the upper half of the distribution, higher than most of the high minimum wage countries in Figure A4.2 but below France and New Zealand.

Figure A4.5: Comparison of international minimum wages relative to median wages of full-time workers, OECD countries, 2019-2023

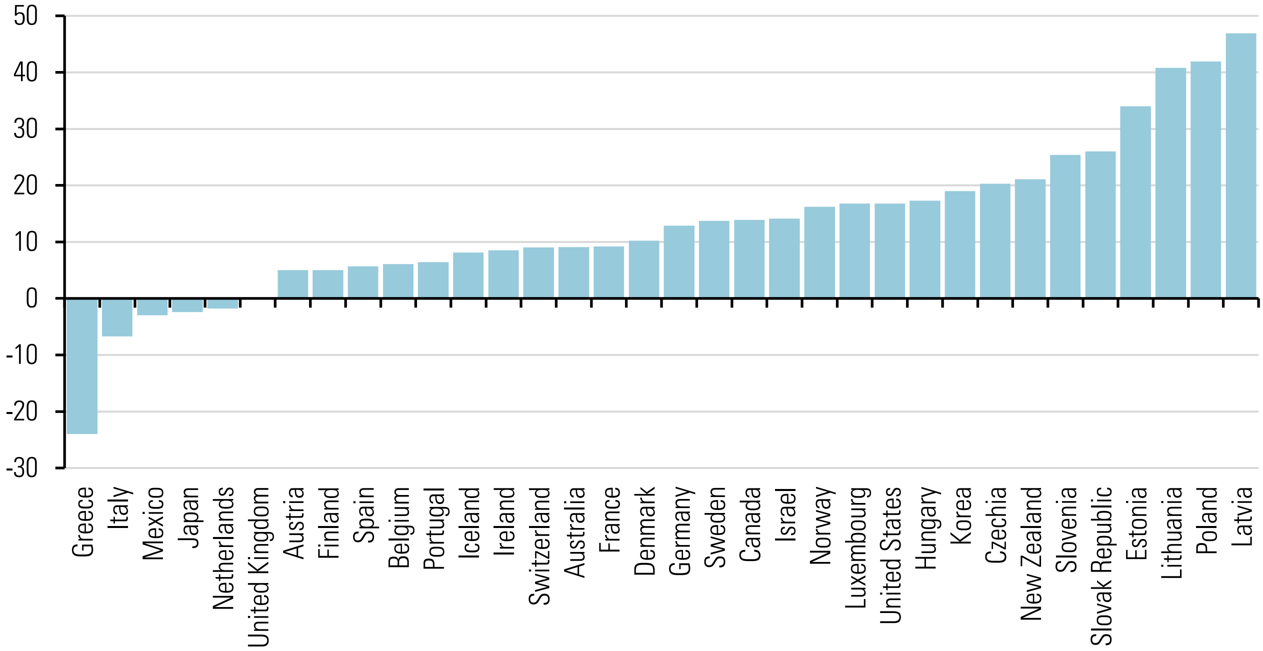


Source: LPC estimates based on OECD data. OECD Data Explorer. Minimum relative to average wages of full-time workers. Minimum wage relative to the median wage of full-time workers, OECD countries, 2019-2023.
Note: Minimum wages are converted by OECD to an annual value to enable comparison across the whole of the year in question.

Comparing real wage growth between countries

A4.16 Chapter 4 looked at the relationship between minimum wages and living standards in the UK. We noted that a key aspect of the living standards situation is the long running squeeze in real wages, with little net growth since the financial crisis of 2008. This lack of real wage growth is rare by international standards. Figure A4.6 compares the change in average annual wages per full time equivalent employee in 2022 constant prices between 2007 and 2023. The UK is part of a small group of countries (6 of 33) where real wages have been static or fallen, including Greece, Italy, Japan, Mexico and the Netherlands. Other G7 countries like France (9 per cent), Germany (13 per cent), Canada (14 per cent) and the USA (17 per cent) have all seen much stronger wage growth.

Figure A4.6: Total change in real average annual full-time wages, 2007-2023



Source: LPC estimates based on OECD data. OECD Data Explorer. Average annual wages. Average annual real full-time wages in 2023 constant prices at 2023 US$ purchasing power parities, OECD countries, annual, 2007-2023.

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