



**GOVERNMENT EVIDENCE TO
THE LOW PAY COMMISSION ON
THE NATIONAL MINIMUM WAGE**

NOVEMBER 2005



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Executive summary

It is widely agreed that the National Minimum Wage has been successfully introduced and it is now firmly established as a key element of the UK labour market.

The Government is determined to keep the National Minimum Wage under close review and develop it where possible. The Government welcomes this opportunity to present the Low Pay Commission with its evidence on the National Minimum Wage in its seventh year of operation.

This combined volume contains the Government's 2005 submissions to the Low Pay Commission on both the non-economic and the economic evidence. These submissions were both made in November 2005.

Non-Economic Issues (part 1)

The Government welcomes this opportunity to present the Low Pay Commission with its evidence on the following issues:

- Accommodation offset
- Salary sacrifice schemes
- The older workers development rate
- The apprentice threshold
- Enforcement

This forms the first part of the Government's evidence to the Commission. The Government's evidence on economic issues will be presented to the Commission later this year.

Accommodation offset

The legislation on the accommodation offset has not changed. Accommodation provided by the employer is covered by the rules on the maximum offset that can be counted towards minimum wage pay. The offset is designed to ensure that employers cannot seek to recover the costs of the minimum wage through charges for accommodation.

The offset is not a commodity in the same way that food is, and the Government does not believe it should be treated as such. Nor is the offset intended to be a commercial value. Its purpose is to prevent the exploitation of workers. The Government believes it should be retained for this reason. We would welcome the Commission's view on whether the regulations need amendment to ensure that employers cannot work around the purpose of the offset.

Salary sacrifice schemes

The Government recognises the value of the four main benefits that employers commonly offer to employees through salary sacrifice

schemes arrangements: childcare vouchers, Home Computer Initiative, bicycles and pension contributions.

However, it does not believe that there is a strong enough case for allowing these benefits to count against the minimum wage at the present time. For workers from low to moderate-income families, claiming childcare support through working tax credits is likely to be an equally good or better alternative to sacrificing their salary for the childcare benefit.

While the Government recognises that for a small number of low income workers vouchers would be a better way of funding their childcare, we believe this would complicate the position for workers.

The Government notes that the other schemes are at an early stage in their development. We believe that there is insufficient evidence to justify changing the legislation. We continue to believe that the only benefit in kind which should count towards minimum wage pay is accommodation. This will, importantly, retain the simplicity of the minimum wage and make it easier to enforce. However, we recognise that it may be appropriate to keep the position on these schemes under review.

Older workers development rate

Evidence demonstrates that the take up of the Older Workers Development Rate is very low. The Government does not believe this rate can be justified under the forthcoming age strand of the Employment Directive and believes therefore that the older workers development rate should be abolished from October 2006.

Apprentices' threshold

Apprentices aged 19 to 25 in the first 12 months of their apprenticeship are not entitled to the minimum wage. However all apprentices aged 26 and above must be paid the minimum wage.

In view of the forthcoming age strand of the Employment Directive retaining the 26-year-old threshold would require objective justification. The evidence demonstrates that the number of apprentices aged 26 and above is extremely small. The Government therefore believes that the 12 month exemption should be extended to cover all apprentices aged 19 and over.

Enforcement

While the Government believes that the great majority of employers pay above the minimum wage, we are absolutely determined to tackle difficult employers. The Government have therefore decided to proceed with a new approach called 'targeted enforcement', under which we will target publicity and enforcement at low-paying sectors in turn. For the first year of this programme the hairdressing sector has been chosen. The two key hairdressing employer groups have welcomed this decision. Early discussions with the industry have highlighted the need to clarify

the position of apprentices. Guidance will be sent to all employers and apprentices in the sector later this month and we will begin a proactive enforcement campaign before the end of the year.

The Government has also announced a new criminal investigations strategy, which aims to prosecute a small hard core of employers who regularly or deliberately fail to pay the minimum wage. Her Majesty's Revenue and Customs have now begun identifying suitable employers and we are aiming to identify a first batch of minimum wage employers for prosecution in 2005/06.

Economic Effects of the National Minimum Wage (part 2)

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

It is widely agreed that the National Minimum Wage has been successfully introduced and it is now firmly established as a key element of the UK labour market.

The Government is determined to keep the National Minimum Wage under close review, and has reviewed the developing evidence of its economic impact. The main findings of the Government's assessment on the economic evidence are:

Macroeconomic conditions

UK output growth has slowed over the last year, partly reflecting a fall off in private consumption growth. External forecasters generally expect some pick up in growth next year, albeit remaining below trend. But despite weaker growth the labour market has remained robust, with the employment rate close to its historical peak. External forecasters expect some rise in unemployment next year as more subdued economic growth leads to a slowing in the demand for labour. Earnings growth remains contained, with outside forecasters not expecting much change in 2006.

Aggregate minimum wage impacts

US analysis of the impact of minimum wages is mixed. However studies of the introduction of the UK minimum wage found no significant adverse employment effects. While the minimum wage 'bite' has gradually moved higher, changes in coverage have been more volatile.

Analysis of growth in industry wages and labour demand between 1998 and 2005 finds a generally positive association; low pay industries exhibited no obvious clustering or difference. Moreover, there was no statistically significant difference in the growth of labour demand between low-paying and high paying industries over this period.

Evidence on the distribution of low pay

The national minimum wage 'bite', defined as the value of the minimum wage relative to the average wage, was just over half the median hourly wage in 2005 - the same as in spring 2004. The proposed 5.9 per cent rise in the adult rate in October 2006 is likely to see a modest rise in the bite. The UK level of the 'bite' is around the average for a sample of developed economies which have a minimum wage in place. Looking at pay by age, the point where the minimum wage is closest to the median wage occurs around 18 years old, when the relevant minimum wage switches to the youth development rate. The earnings distribution has become significantly more compressed since the introduction of the minimum wage in 1999, with those at the bottom of the earnings distribution experiencing faster growth than those at the top.

Developments in low-paying industries

Employment in most low-paying industries has increased significantly since the introduction of the minimum wage. Some industries (retail, hotels and restaurants, investigation and security) have seen their share of overall employment grow. Most other low-paying industries have broadly followed national employment trends. The slowdown in private consumption growth has been reflected in the retail sector, which has experienced slower rates of sales growth than in recent years. Wages growth in both retail and hotels and restaurants industries has been below average earnings growth, perhaps reflecting the weakness in these sectors. Looking ahead, external forecasters expect some strengthening in consumption next year.

Developments in the labour market for younger workers

The overall employment rate of 18-21 year olds has fallen back somewhat since its peak in 2000, but the unemployment rate remains lower than at the time of the introduction of the minimum wage. On balance the labour market position of 21 year olds remains closer to younger workers than to workers on the adult rate, although relatively few 21 year olds actually earn below the adult rate of the minimum wage.

Developments affecting 16-17 year olds

So far there has been no discernible adverse impact of the National Minimum Wage on the participation of young people aged 16-17 years in education or training. There has also been no rise in the proportion of 16 and 17 year olds who are not receiving education or training (NET) in recent years. The inactivity rate of 16-17 year olds has been rising, however this reflects higher proportions of 16-17 year olds entering education rather than entering the NET group.



**PART 1:
NON-ECONOMIC ISSUES**

NOVEMBER 2005

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Introduction

The national minimum wage, introduced on 1 April 1999, forms part of the Government's strategy to establish fairness in the workplace and to make work pay, by ensuring that all workers receive at least the minimum hourly rates set.

In July 2005 the Government set out the remit for the Low Pay Commission to report by the end of February 2006 on a range of minimum wage issues, including a review of the 2006 rates. The Commission has asked for evidence to be submitted, on the operation of the accommodation offset and the treatment of salary sacrifice schemes. This paper sets out the Government's views on these issues.

The Government has also been reviewing the position on the Older Workers Development Rate and the way the exemption for apprentices applies to those aged 26 and above, in order to ensure that these issues can be addressed in time for the forthcoming age strand of the Employment Directive. This paper also sets out the Government's views on these issues.

SECTION 1

Accommodation offset

The legislation on the accommodation offset has not changed. Accommodation provided by the employer is covered by the rules on the maximum offset that can be counted towards minimum wage pay. The offset is designed to ensure that employers cannot seek to recover the costs of the minimum wage through charges for accommodation.

The offset is not a commodity in the same way that food is, and the Government does not believe it should be treated as such. Nor is the offset intended to be a commercial value. Its purpose is to prevent the exploitation of workers. The Government believes it should be retained for this reason. We would welcome the Commission's view on whether the regulations need amendment to ensure that employers cannot work around the purpose of the offset.

As part of its remit, the LPC has been asked to review the operation of the accommodation offset, and if appropriate make recommendations for any changes needed to the regulations.

Under the National Minimum Wage Regulations 1999, accommodation is the only benefit in kind that an employer may count towards the minimum wage. This is set out in Statutory Instrument 1999 No 584 – The National Minimum Wage Regulations 1999, as amended.

From 1 October 2005 the amount that can be counted in this way is £3.90 per day (£27.30 per week). If a worker earns exactly the minimum wage, then this is the maximum amount that an employer can charge for accommodation. An employer can charge more than the offset if the worker earns more than the minimum wage, but a worker must never earn less than minimum wage minus the accommodation offset.

In the last year, DTI has been approached by the Association of Labour Providers ("ALP"), a trade association for labour providers. The ALP has raised a number of issues in connection with the way the offset works, and requested clarification on a number of aspects of law. Many of its members provide accommodation to workers, some of whom are recruited from overseas.

The Government believes the sectors most likely to be concerned about the accommodation offset are hospitality, catering, agriculture and food. However, until the representations from the ALP, HM Revenue and Customs had not been aware of any substantial concerns raised by businesses (including hotels and restaurants) regarding the offset. The ALP is the only

representative group to have raised the matter directly with Government recently.

The number of cases progressed by HM Revenue and Customs concerning the accommodation offset remains low. There are around 20 working cases at the moment. In the past year there were approximately 10 direct complaint cases, and a further 45 cases had an offset element when reviewed.

In its representations to Government, the ALP has argued that it is uneconomic to offer accommodation at rates significantly below commercial rates and that the existing level of the offset is too low. It believes that provided workers are free to choose whether to accept or reject the accommodation, labour providers should not be subject to *de facto* restrictions on what they can charge. In this respect, the ALP believes that accommodation should be in line with the provision of commodities, such as food, where there is no offset. Where a worker is free to accept or reject the commodity, such as the provision of a meal, he pays for any such item from his net pay. These deductions do not count towards minimum pay.

A further argument is that in offering accommodation, employers provide a valuable service, free of obligations for the worker, who is not required to provide a deposit or references. Furthermore, the ALP believes that if the offset is maintained, many of its members will either be forced to go out of business, as they will be unable to charge a sufficient amount to cover costs, or they will be forced to evict workers.

Government policy

It has never been the Government's policy intention for the accommodation offset to be a reflection of the commercial value of renting a property. It is widely recognised that accommodation is not a commodity in the same way as food or transport. This is why accommodation is the single exception to the rule about benefits in kind. It accounts for a much larger proportion of an individual's expenditure. By setting a limit, the Government's intention has always been to prevent the exploitation of workers by ensuring that those who are on a minimum wage do not find a significant proportion of their pay being deducted for accommodation.

It has always been Government policy that accommodation provided by the employer must be covered by the rules on the maximum offset that can be counted towards minimum wage pay. Where the accommodation is provided directly by the employer the application of the rules is straightforward. However, there are situations where the worker takes accommodation that is provided to him but the employer is not the same legal entity as the landlord, for example, the accommodation is provided by a company separate to the employing company (but perhaps with the same directors and shareholders). In some of these cases, depending on the precise circumstances, the employer could still be regarded as effectively

providing the accommodation such that the accommodation offset rules should apply. In many cases, however, the offset rules may not apply.

The fundamental question here is whether changes may be needed to the legislation to maintain the policy and to prevent employers from seeking to circumvent the restrictions of the offset by using other vehicles or third parties to provide the accommodation. This is an area that has not been tested by the courts and it seems preferable to ensure that the legislation here is completely clear.

As mentioned, the ALP has suggested that where an employee has voluntarily accepted accommodation, i.e. where workers are free to choose whether to accept or reject accommodation, the offset rules should not apply. Choice is not an issue under the present regulations. However, it will always be difficult to distinguish between those workers who voluntarily accept accommodation offered to them and those who in real terms had little choice.

We are aware that the setting up of the Gangmasters Licensing Authority will require all labour providers to adhere to legal requirements, including payment of minimum wage and the accommodation offset rules, as a condition of their licence. All labour providers will therefore find themselves in the same position, and will either be required to absorb costs or pass them on upwards to those who are purchasing the labour.

The Government does not consider that there should be regional variations for the accommodation offset. This would be complex, cause confusion for workers and create extra enforcement difficulties, for example in relation to where the boundaries are drawn.

We believe that the underlying objective of the accommodation offset is clear but the legislation may be open to misinterpretation. We ask the Commission to consider whether the regulations need amendment to ensure that employers cannot work around the purpose of the offset.

Agricultural Minimum Wage

The application of the accommodation offset for the agricultural sector was reviewed earlier this year. A common approach applies for the agricultural minimum wage and the Department for the Environment and Rural Affairs enforcement practices now mirror those used for national minimum wage purposes. Where the employer provides accommodation, no worker should receive net pay that is less than the national minimum wage less the accommodation offset.

We are aware that some employers are seeking to supplement the accommodation-offset charge by adding charges for accommodation related services such as water and electricity. These cannot count towards the offset and we do not feel that there is a case for allowing them to do so.

The current position

Defra advise that stand-alone agreements for the provision of accommodation by employers are commonplace in agriculture and the allied food-processing sector.

It is estimated that some 40,000 agricultural workers occupy tied cottages supplied by their employer. Many are provided on short-hold tenancies at a market rent. Individuals who rent tied properties, in effect individuals who live in the property as a condition of employment, are excluded from housing benefit.

However where the worker is not tied to the property, he may be eligible to claim housing benefit. Whether someone is entitled to housing benefit is determined by a range of circumstances. Strengthening legislation may result in some workers losing their benefit entitlement and with the employer carrying the cost. It is not possible to ascertain how many may be effected by such a proposal.

There are some 16,250 foreign students working in agriculture under the Home Office Seasonal Agricultural Workers Scheme. This scheme currently allows students to be charged a market rent for accommodation provided by their employer under a stand-alone contract. Rents charged currently average some £30 - £40 per week although a minority of students are charged between £55 and £75 per week. Many of the 8,000 or so accession county nationals working in agriculture and food processing will be treated in the same way.

SECTION 2

Salary sacrifice schemes

The Government recognises the value of the four main benefits that employers commonly offer to employees through salary sacrifice schemes arrangements: childcare vouchers, Home Computer Initiative, bicycles and pension contributions.

However, it does not believe that there is a strong enough case for allowing these benefits to count against the minimum wage at the present time. For workers from low to moderate-income families, claiming childcare support through working tax credits is likely to be an equally good or better alternative to sacrificing their salary for the childcare benefit.

While the Government recognises that for a small number of low income workers vouchers would be a better way of funding their childcare, we believe this would complicate the position for workers.

The Government notes that the other schemes are at an early stage in their development. We believe that there is insufficient evidence to justify changing the legislation. We continue to believe that the only benefit in kind which should count towards minimum wage pay is accommodation. This will, importantly, retain the simplicity of the minimum wage and make it easier to enforce. However, we recognise that it may be appropriate to keep the position on these schemes under review.

A salary sacrifice scheme is a scheme whereby an employee gives up the right to receive part of the cash pay due under their contract of employment. A salary sacrifice is not a deduction or charge from a salary. The employee agrees to a lower amount of cash in return for some form of non-cash benefit. The “sacrifice” is achieved by varying the employee’s terms and conditions relating to pay.

Employers are legally required by the 1999 regulations to pay their employees an hourly rate not less than the national minimum wage. Regulation 9 provides that a workers pay for minimum wage purposes does not include vouchers, stamps or other documents that can be exchanged for money, goods or services. If, therefore, an employee agrees to a salary sacrifice to replace some of their cash earnings with, for example, a childcare voucher, the sacrifice cannot take the employee’s cash pay below the applicable minimum wage rate.

For a salary sacrifice to be effective for tax and National Insurance purposes, the potential remuneration must be given up before it is treated for tax and (NICs) purposes, and the contract must mean the employee is entitled to lower cash remuneration and a benefit in kind.

At present there are four main benefits that employers commonly offer to employees through salary sacrifice arrangements: childcare vouchers, home computers, bicycles and pension contributions. Each of these benefits attracts preferential tax and/or NICs treatment over cash pay, providing an incentive for employers to offer them instead.

To benefit from a salary sacrifice arrangement for any of these benefits, a worker has to be paying tax and National Insurance. They therefore have to earn more than the personal allowance of income tax (£4,895 per year) and primary threshold in NICs (£94/week or £4,888 per year). This means that the *number* of hours they work, and whether this is sustained over the year, is as important as the hourly rate.

As an illustration, anyone working 18 hours per week or less on the minimum wage, at the current adult rate of £5.05, will not be earning enough to pay tax or national insurance. They therefore cannot benefit from *any* salary sacrifice scheme, even if the minimum wage regulations were changed. Someone earning at £6 per hour has to work over 15.7 hours per week to become a taxpayer. Since more than half of low-paid workers work part time, a significant proportion of people affected by the minimum wage could not gain even if the regulations were changed to allow salary sacrifice schemes to count.

Childcare vouchers

The Chancellor announced new tax and NICs exemptions for employer-provided childcare and childcare vouchers in the December 2003 pre-Budget report, to provide an incentive to employers to help their employees to meet their childcare responsibilities. This policy was implemented in April 2005.

Employers may currently issue their employees with childcare vouchers that are then used in direct payment for childcare provision (restricted to registered and approved childcare). Both employees and employers are exempt from paying NICs on the first £50 a week of these childcare vouchers and employees are also exempt from paying tax on the first £50 a week.

Childcare voucher companies have made representations to HMRC that some employers who have considered offering childcare vouchers through salary sacrifice arrangements have been put off as many of their staff, who are paid at or just over the minimum wage, cannot participate. Such employers consider that it would be difficult to offer a scheme to their staff that would effectively only be available to their higher paid employees. They consider that this would be against the spirit of the concession, which requires the benefit to be made available to all staff where it is offered. One

particular supermarket, who employ around 80 per cent of their staff at or just over the minimum wage, has made similar representations to the DTI.

Childcare vouchers and Tax Credits

Working Tax Credit (WTC) provides support with childcare costs for families with low to moderate incomes. To claim the childcare element of WTC a lone parent needs to be working a minimum of 16 hours per week. For a couple one parent must be working at least 16 hours and the combined hours of the household must sum to 30 or more. Once a family qualifies for the childcare element in this way, the additional tax credits are worth 70 per cent of the total cost of childcare up to a maximum of £175 per week for one child and £300 per week for two-or-more children. The amount of help available through the childcare element is increasing from 6 April 2006 to up to 80 per cent of qualifying childcare costs.

Workers who pay only the starting rate of income tax (10 per cent) at the margin are likely to be better off claiming support for their childcare through tax credits rather than sacrificing their salary for the employer provided childcare benefit.

The Government recognises that the decision for workers over whether to use childcare vouchers or tax credits is not a simple one, although for the vast majority of low-paid workers, accepting a childcare benefit from their employer in return for a salary sacrifice will not provide any advantage over claiming the childcare element of WTC.

Further information is set out at Annex A.

Home Computing Initiative

Home Computing Initiative (HCI) schemes are a government-backed effort to increase the use of computers in homes across the UK. The schemes are still relatively new. Although the Finance Act 1999 has allowed for these schemes since 1999, the majority of schemes did not become operational until January 2004.

Under the schemes, businesses can loan computers to employees for personal use at home, free of any tax liability. At the end of the loan the employee can purchase the computer at the going market rate. Around 600 organisations have adopted HCI schemes (50 per cent of which are large companies) and around half a million individuals have taken up the offer.

The incentive for an employer is that any monthly contributions are taken from non-taxable income. An employer can make additional savings in pension and National Insurance contributions. Schemes are liable to the usual scrutiny – HMRC may undertake tax and VAT audits at any time.

HCI schemes vary between employers, but all schemes are first approved by the Office of Fair Trading. However, employers generally use the ‘salary sacrifice mechanism’ to cover the cost of setting up and running the scheme, often spreading the cost for up to 3 years. They also offer a choice

of equipment. In order to ensure that any deductions will not fall foul of minimum wage legislation, most employers allow for a margin of 20 per cent above the minimum wage. It is therefore not available to those being paid around the minimum wage.

The HCI is part of the Government's social inclusion strategy. It is also seen as a vital element in enabling more people to improve the way they work and in leading to personal benefits, including personal education.

Bicycles

The Finance Act 1999 allows employers to loan cycles and cyclists' safety equipment to employees as a tax-free benefit. The exemption removes the tax charge that would otherwise apply, provided certain specified conditions are met. The tax exemption applies when the employee mainly uses the cycle and cyclists' safety equipment for qualifying journeys. An employer may loan to all employees but a salary sacrifice arrangement cannot be used if in doing so the employees' gross pay drops below the minimum wage.

The largest provider of the scheme, Boost, has issued just over 3,000 certificates for new cycles under this scheme. They estimate that next year they will issue at least 30,000 certificates. Halfords, the main other national provider, is expected to issue a similar number of certificates. There are also a number of smaller local providers who offer the scheme. It is estimated that next year there will be almost 100,000 in the scheme.

The Department for Transport has produced guidance and a promotional leaflet is due out shortly. The main policy documents are 'Walking and Cycling: an action plan' published in June 2004 with an action to promote the spread of employer-backed schemes to encourage employees to cycle to work and the Health White Paper, Nov 2004 'Choosing Health - making healthier choices easier' of which the 'cycle to work' scheme is part of the delivery plan.

Pensions

Tax relief for contributions into a tax-approved pension scheme is an important part of the encouragement of pension saving. The tax incentives that the Government offers for pension contributions make pensions a more tax efficient form of remuneration than salary. This has been the case for several decades, and is not the result of any recent initiative.

Tax relief is given on contributions made by the employer as well as the employee. However, employer contributions also receive NICs relief as well as tax relief. This differential is also a long-standing feature of the pension scheme. These incentives exist to encourage firms to run pension schemes for their staff and make contributions to them.

Whether an employer's contribution into an occupational pension scheme is facilitated by a salary sacrifice arrangement is up to the employer. HMRC

rules set a limit on the amount of contributions that can be paid into a pension fund, and contributions are monitored on this basis.

In light of this the evidence that is held by HMRC regarding contributions is limited to the levels of employer and employee contributions into occupational pension schemes over time. HMRC are not able to easily identify those that have switched contributions to salary sacrifice.

The precise design of a pension scheme is a contractual matter between employer and employee. Where firms wish to change this design it is a matter for employment law, not tax law. In complying with employment law, firms should communicate changes with their staff.

Way forward

The Government recognises the value of the benefits that are provided by employers under salary sacrifice arrangements and the opportunities they present to employees. However it does not consider that on balance the advantages of changing the minimum wage regulations to allow these schemes to count would outweigh the costs in terms of complicating the rules and potentially undermining enforcement.

For those minimum wage workers from low to moderate-income families who are eligible for the WTC, claiming childcare support through the WTC is likely to be an equally good or better alternative to sacrificing their salary for the childcare benefit. While the Government recognises the arguments for allowing childcare vouchers to count towards the minimum wage, and accepts that for a small number of minimum wage workers childcare vouchers are a better way of funding their childcare, it believes this would complicate the position for the vast majority of workers.

In the case of the other schemes (home computing, bicycles and pensions), the Government does not believe that there is sufficient evidence to justify any changes to minimum wage legislation.

In particular, the Government believes that allowing these benefits to count towards the minimum wage would detract from the current simplicity and create an unwelcome precedent. It could also create difficulties in terms of enforcement.

The Government will be considering alternative ways to promote salary sacrifice schemes, and will keep the issue of salary sacrifice under review.

SECTION 3

The older workers development rate

Evidence demonstrates that the take up of the Older Workers Development Rate is very low. The Government does not believe this rate can be justified under the forthcoming age strand of the Employment Directive and believes therefore that the older workers development rate should be abolished from October 2006.

In their 2005 report, the LPC provisionally concluded that the older workers development rate should be abolished from October 2006 and that, simultaneously, the 12 months exemption from the minimum wage should be extended to cover all apprentices aged 19 and over.

The Government initially agreed that the Commission should consider these issues as part of their 2006 Report. However the timetable for regulations needed to address the age strand of the Employment Directive meant that the Government has decided to consider this issue first, and to invite the Commissions views on our proposals.

The older workers development rate

The older workers development rate applies for the first six months to workers aged 22 and over that are starting a job with a new employer and doing accredited training. After six months, the worker must be paid at least the minimum wage. Regulation 13 of the 1999 Regulations refers.

The Commission's first report (1998) recommended the creation of the older workers development rate to provide an incentive for employers to recruit unemployed people and those returning to the labour market who need training to reach an acceptable level of performance. The exemption was linked to the introduction of New Deal for workers aged 25 plus.

However, successive reports by the Commission have shown limited take up of the older workers development rate and thrown increasing doubt on the benefits of the exemption.

The Commission's 2005 report states that the take up of the Older Workers Development Rate remains very low. The Commission found it was employed by only 4 per cent of respondents, with greatest use in the hairdressing and childcare sectors (10 per cent and 5 per cent respectively). The Commission found that there is little awareness of its existence and

that the complexity and costs associated with using accredited training schemes also deter use.

We also understand that the Commission met representatives from the National Hairdressers Federation and the Hairdressing Employers Association and were advised that in their view extending the 12-month apprenticeship exemption to cover those aged 26 and over would provide a greater incentive to train older workers than the older workers development rate. We take this as an important indication that the main sector using this rate could accept its abolition.

Department for Education and Skills (DfES) analysis found it difficult to assess the extent of take up of the older workers development rate by employers as the information collected on wage rates does not establish specifically why any worker may be getting less than the minimum wage. About 10,000 individuals a year are receiving below the minimum wage in their first six months with a new job and receiving some kind of accredited training, but these will include many people undertaking apprenticeships. Our best estimate is that no more than half of these will represent employers using this exemption.

The Government have some concerns that in some areas, such as the DfES program, Skills for Life the exemption may even be a deterrent to potential learners. Our conclusion is that the impact of withdrawing this exemption will be limited and in view of the impending age strand of the Employment Directive its retention will be difficult to justify. We therefore propose to abolish the older workers development rate in the forthcoming Employment Directive.

SECTION 4

Apprentices' threshold

Apprentices aged 19 to 25 in the first 12 months of their apprenticeship are not entitled to the minimum wage. However all apprentices aged 26 and above must be paid the minimum wage.

In view of the forthcoming age strand of the Employment Directive retaining the 26-year-old threshold would require objective justification. The evidence demonstrates that the number of apprentices aged 26 and above is extremely small. The Government therefore believes that the 12 month exemption should be extended to cover all apprentices aged 19 and over.

Apprentices are exempt from the minimum wage if they are under 19, or under age 26 and in the first 12 months of an apprenticeship. For the purposes of the minimum wage, apprentices are defined as workers who either have contracts of apprenticeship or are taking part in specified Government training programmes. Regulation 12 of the 1999 Regulations refers.

The Commission's 2005 Report provisionally concluded that the 12 months exemption for apprentices should be extended to cover all apprentices aged 19 and over (in other words, that the 26-years threshold should be removed).

Set out below is a table, drawn from the Labour Force Survey, outlining the number of people in employment and on recognised trade apprenticeships. It shows that the number of people over the age of 25 who are on recognised apprenticeships is low, at less than 10,000 out of a total of about 245,000. We need to stress however that due to the large amount of variability associated with the number, the Office for National Statistics do not consider it to be a reliable estimate.

Table 1. Number of people in employment and on recognised trade apprenticeships by age

Age	Number
16	31000
17	58000
18	47000
19	42000
20	27999
21	12000
22-25	16000
25+	*

Source: Summer 2004-Spring 2005 Labour Force Surveys, not seasonally adjusted

This relates to the number in employment who said they were 'yes-still doing' and apprenticeship when asked 'Are you doing or have you completed a recognised trade apprenticeship'.

Those people who did not answer the questions have been allocated pro-rate across the different response categories 'yes-still doing' or 'no-including apprenticeships begun discontinued'.

*The Sample size is too small to give an accurate estimate for the number of people in this group.

In addition, figures obtained from the Learning and Skills Council suggest that only about 600 apprentices are aged 26 or above, out of a total of 225,000. The second table suggests that only about 50 of these are apprentices in their first year. This suggests that the effect of extending the first year exemption to cover all apprentices aged 19 and over would be minimal.

In addition, it would be difficult to justify the retention of the 26 years threshold under the impending age strand of the Employment Directive. The Government therefore proposes to abolish the threshold in the forthcoming Employment Directive.

Table 2. Average number of apprentices, first 11 months of 2004/05

Age at 31st August 2004	Employed at start of learning				All trainees			
	Started in 2002/03 or before	Started in 2003/04	Started in 2004/05	Total	Started in 2002/03 or before	Started in 2003/04	Started in 2004/05	Total
under 16	0	2	92	94	0	3	136	139
16	4	2326	21369	23,699	6	3998	28176	32,180
17	1349	21782	14606	37,737	2063	27362	18708	48,133
18	9704	15955	14103	39,762	11648	18960	16122	46,730
19	10918	15212	10185	36,315	12608	16721	10974	40,303
20	9403	10785	7013	27,201	10474	11408	7332	29,214
21	7017	8298	5288	20,603	7453	8606	5457	21,516
22-25	12152	17552	9252	38,956	12570	17923	9451	39,944
25+	538	26	36	600	544	27	62	633
Total	51,085	91,938	81,944	224,967	57,366	105,008	96,418	258,792

*Note: The average in learning figures are at learner level. Where a learner is doing more than one programme in a period each programme has equal weight. *Note: The difference in totals is due to rounding.

Table 3. Average number of apprentices, first 11 months of 2005, by age at start

Age at start	Employed at start of learning				All trainees			
	Started in 2002/03 or before	Started in 2003/04	Started in 2004/05	Total	Started in 2002/03 or before	Started in 2003/04	Started in 2004/05	Total
under 16	321	349	131	801	469	578	209	1256
16	12964	17609	18849	49,422	15856	22954	24814	63,624
17	11258	16657	14995	42,910	12817	20405	19468	52,690
18	8841	15249	14100	38,190	9747	17263	16349	43,359
19	5887	12044	10528	28,459	6277	12887	11447	30,611
20	4164	9072	7537	20,773	4350	9488	7898	21,736
21	3093	7054	5610	15,757	3196	7246	5790	16,232
22-25	4554	13894	10158	28,606	4650	14177	10381	29,208
25+	3	9	36	48	3	9	63	75
Total	51,085	91,937	81,944	224,966	57,365	105,007	96,419	258,791

*Note: The average in learning figures are at learner level. Where a learner is doing more than one programme in a period each programme has equal weight. *Note: The difference in totals is due to rounding.

SECTION 5

Enforcement

While the Government believes that the great majority of employers pay above the minimum wage, we are absolutely determined to tackle difficult employers. The Government have therefore decided to proceed with a new approach called 'targeted enforcement', under which we will target publicity and enforcement at low-paying sectors in turn. For the first year of this programme the hairdressing sector has been chosen. The two key hairdressing employer groups have welcomed this decision. Early discussions with the industry have highlighted the need to clarify the position of apprentices. Guidance will be sent to all employers and apprentices in the sector later this month and we will begin a proactive enforcement campaign before the end of the year.

The Government has also announced a new criminal investigations strategy, which aims to prosecute a small hard core of employers who regularly or deliberately fail to pay the minimum wage. Her Majesty's Revenue and Customs have now begun identifying suitable employers and we are aiming to identify a first batch of minimum wage employers for prosecution in 2005/06.

The National Minimum Wage Act 1998 has now been in force for over six years. HMRC has operational responsibility for enforcing the minimum wage through a contract with the DTI.

Key findings in 2004/05

HMRCs target for 2004/2005 was to close 5,200 cases. They closed 5,155. The overall strike rate for this year was 34 per cent, down from 39 per cent last year. In part this was expected because the information on the current tax credit application forms is less useful than that on the previous working families tax credit forms. However, HMRC continue to seek new sources of information. The arrears identified were £3,760,361, up from the total in 2003/04 of £2,558,096. Average arrears per worker for the year were up to £333 from £271 in 2003/04. The number of workers for whom arrears were identified was 11,260, up from 9,428 in 2003/04.

Light touch enforcement

In 2004/05 the Government looked to see whether there were areas where HMRC compliance officers could take a less 'technical' approach to the minimum wage regulations, in order to free up resources so that they could better focus on key areas. Compliance officers found that in a number of

cases workers had been paid below the minimum wage in some pay periods, but were clearly being paid above the minimum wage overall. For example, some workers may be paid weekly and receive basic pay in some weeks below the minimum wage, but in other weeks they earn commission which takes them well above the minimum wage overall.

While strictly speaking this is a breach of the legislation, we believe that cases like these – where workers are earning well above the minimum wage overall – should really not be our main goal. In January 2005 the Government decided not to pursue any more cases of this type, which will help free up resources to tackle seriously non-compliant employers.

Individual workers may still however take their own cases to a tribunal if they wish. HMRC will also reserve their freedom to pursue cases where they believe employers are using this as a loophole to avoid paying the minimum wage – for example, by paying a basic rate below the minimum wage and dismissing workers just before their commission becomes due.

Volunteers and the minimum wage

DTI and HMRC officials have held a number of meetings with the Central Council for Physical Recreation (CCPR) on the subject of the minimum wage and volunteers. The CCPR reported that there may be circumstances in which a sports club believes that a member is acting as a volunteer, but, an entitlement to the minimum wage may arise because a small non-cash benefit or an honorarium is offered. DTI and HMRC have drafted a policy statement which says that HMRC will not undertake pro-active investigations on CCPR Sports Clubs and that certain benefits-in-kind will not be treated as non-cash benefit for minimum wage purposes. The CCPR have responded positively to the policy statement and we hope to announce the statement shortly. The aim here is (again) to help free up resources, to enable us to focus on our main objectives.

Changes for 2005-2006

In April 2005 HMRC introduced a number of changes to improve the quality of their minimum wage enquiries. The key change has been to introduce a new 3-stage quality monitoring system so that Team Leaders have input into a case at set stages throughout an enquiry (not only at the end), with new guidance and procedures linked to the criteria for assessing quality. HMRC will monitor quality scores monthly, look at trends over time and across teams, and aim to have an independent annual audit of the quality scores. HMRC have also introduced mandatory 6 monthly checks to ensure cases are progressed appropriately. Other changes include new procedures to ensure that arrears identified are actually paid and a formal mechanism to trigger repeat enquiries of employers that HMRC suspect may not continue to pay the minimum wage once a case is closed.

On 12 July 2005 the Minister For Employment Relations, Gerry Sutcliffe, outlined two Government initiatives to help further improve the effectiveness of minimum wage enforcement.

Targeted enforcement

Targeted enforcement will allow us to target publicity and enforcement at key low-paying sectors, by meeting the main employer groups in each sector to discuss their concerns about the minimum wage; stress that our purpose is not to tackle the great majority of good employers, but to tackle the minority of bad employers; and issue guidance and publicity aimed at both workers and employers addressing their main concerns. This will then be followed by an enforcement drive, encouraging workers paid below the minimum wage to come forward, and for HMRC minimum wage compliance officers to visit employers where they suspect there may be non-compliance. We believe this approach will enable us to raise the profile of the minimum wage in each sector in turn, address their concerns and improve compliance at the same time.

For the first year of this programme the Government has chosen the hairdressing sector. The two key federations have told us they had no difficulties with being the first selected for targeted enforcement and indeed has welcomed it. In October 2005 the DTI produced two guides related to hairdressing and the minimum wage. A detailed guide with case studies will be sent to all training providers and hairdressing employers, and a short guide will be sent to all hairdressing apprentices. The intention is that this should encourage employers to put their affairs in order and encourage workers to come forward and complain if they think they are being underpaid. From December 2005 HMRC will mount an enforcement drive and begin pro-actively targeting hairdressing employers.

Criminal prosecutions

The great majority of minimum wage cases are settled without the need for any formal enforcement action. However the National Minimum Wage Act 1998 also provides for criminal prosecutions as a long-stop where employers are regularly or deliberately non-compliant. In addition to failure to pay the minimum wage, the criminal offences include obstructing officers, failing to keep adequate records, and producing false records.

To date the Government has not taken forward any criminal investigations, but Ministers now believe there is a case for using this route, particularly where lesser sanctions alone are not producing compliance. DTI have therefore now agreed a criminal investigations strategy in principle with HMRC, and they are looking to identify a small number of employers for prosecution. The intention is to identify a first group of cases for prosecution in this financial year.

Awareness and education

In September/October 2005 the Government ran a nation-wide publicity campaign to coincide with the increases to the adult and development rates; and the rate for 16-17 year olds. The campaign had several objectives: to inform employers and workers of the new increased rates and the rate for 16/17 year olds; to make employers aware of the change in the

law; and to encourage people to call the help-line telephone number to obtain further information and advice.

The campaign was biased towards large circulation national tabloids; supported by adverts in the trade press and selected women's magazines as well as the ethnic press and TV listings. The specific target audience included low-paid workers, young workers, ethnic minority workers and all employers – particularly those in retail, hospitality, social care, hairdressing, security, cleaning and childcare.

The Government will continue to develop their minimum wage publicity strategy to ensure that vulnerable groups like some ethnic minorities and homeworkers are made aware of the minimum wage.

Young workers

In the autumn of both 2004 and 2005, the Government ran an Internet publicity campaign on the new rate for 16-17 year olds. Adverts were specifically designed to appeal to 16-17 year olds on websites popular with this age group.

Research taken after the 2004 campaign showed high awareness of the existence of the new minimum wage rate for 16/17 year olds amongst workers (89 per cent) and employers (100 per cent).

Ethnic minorities

Following research commissioned by the DTI in 2004, we have reviewed our strategy on how best to promote awareness of the minimum wage amongst ethnic minorities. The research findings made clear that the best approach to adopt was to direct mail community networks. In the autumns of 2004 Gerry Sutcliffe, wrote to more than 2,000 ethnic community networks providing details of the increases, offering leaflets in ethnic languages, and explaining the role of the helpline which is able to field calls in many ethnic languages. This exercise was repeated in October 2005 with the Minister writing to more than 7,000 ethnic groups.

ANNEX A

Interaction between tax credits and childcare vouchers

Families can only claim Working Tax Credit (WTC) for childcare costs they incur, and hence cannot claim support through the WTC for childcare provided free by their employer or paid for with a childcare voucher. This means that families can either benefit from tax and NICs savings via the voucher or from tax credit support.

For almost all families, claiming support for childcare through the WTC will be an equally good or better alternative to sacrificing £50 of their salary in return for childcare vouchers.

- 340,000 families were benefiting from the childcare element of Working Tax Credit in July 2004.
- Annual spend on childcare support through childcare element of Working Tax Credit is over £700m (estimated for 2003-04), compared with £350m through its predecessor, Working Families Tax Credit/Disabled Persons Tax Credit and only £50m through Family Credit/Disability Working Allowance.
- On average, families claiming the childcare element of the Working Tax Credit receive £50 extra per week.

In order to help employees, HM Revenue and Customs has now produced guidance for employers and employees to help them decide. Employees can also ring the tax credits helpline for advice on what their tax credit entitlement is, although the helpline cannot give “better off” advice on whether an employee would be better off opting for tax and NICs savings through a salary sacrifice arrangement and reduced tax credits. HMRC does not require employers or employees to report or declare benefits that are not liable for tax or NICs and there are currently no figures available on take-up of childcare vouchers since April 2005. HMRC plans to conduct external research through surveys to evaluate the effect of the tax and NICs changes.

The Government is considering issuing some best practice guidance as part of the detailed guidance on the childcare vouchers. This guidance would set out that:

- Childcare vouchers cannot be counted towards pay for minimum wage purposes.
- For those minimum wage workers who are eligible for the childcare element of the WTC, there is no extra benefit to be gained by sacrificing salary for childcare vouchers.
- Companies may agree with their staff that they will issue childcare vouchers only to those employees who are not eligible for the childcare element of the WTC.



**PART 2:
THE ECONOMIC EFFECTS OF THE
NATIONAL MINIMUM WAGE**

NOVEMBER 2005

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SECTION 1

Macroeconomic conditions

UK output growth has slowed over the last year, partly reflecting a fall off in private consumption growth. External forecasters generally expect some pick up in growth next year, albeit remaining below trend. But despite weaker growth the labour market has remained robust, with the employment rate close to its historical peak. External forecasters expect some rise in unemployment next year as more subdued economic growth leads to a slowing in the demand for labour. Earnings growth remains contained, with outside forecasters not expecting much change in 2006.

Macroeconomic conditions

The Government's latest assessment on the outlook for the UK economy will be published as part of Government's *Pre-Budget Report* in early December. Copies will be provided to the Low Pay Commission on publication.

Economic activity

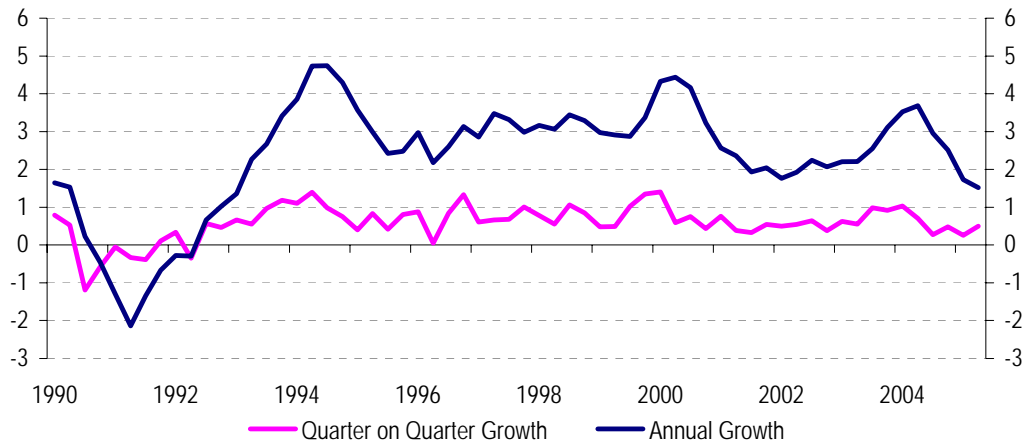
UK output growth has slowed over the past year. Annual growth in GDP peaked at 3.7 per cent in 2004 Q2, before declining to 1.5 per cent in 2005 Q2. ONS' Preliminary Estimate of growth in 2005 Q3 indicates GDP increased by 0.4 per cent on the quarter, 1.6 per cent on a year earlier.

A large part of the decline in overall demand growth has reflected a slowdown in consumer spending, which fell from an annual rate of growth of 3.6 per cent in 2004 to 1.5 per cent in 2005. A key factor that may have played an important part in the slowdown in consumer spending includes the slow down in housing market activity. In the latest data, house price inflation has fallen from its peaks in 2004 to around 3 to 4 per cent in October 2005 on both the Halifax and Nationwide measures. Another related factor in slowing consumption will most likely have been previous interest rate rises in 2004 by the Bank of England feeding through to spending.

Recent monthly data suggests below trend growth may continue into the fourth quarter of 2005. The October 2005 CBI Industrial Trends Survey indicated business optimism remained negative for a fifth successive quarter, although output was expected to rise marginally over the next three months. The Chartered Institute of Purchasing and Supply (CIPS) survey in October also indicated a modest rise in manufacturing output, and

a firmer rate of expansion in the service sector. Consumer spending also appears fairly restrained, with the October CBI Distributive Trades Survey continuing to report weak sales.

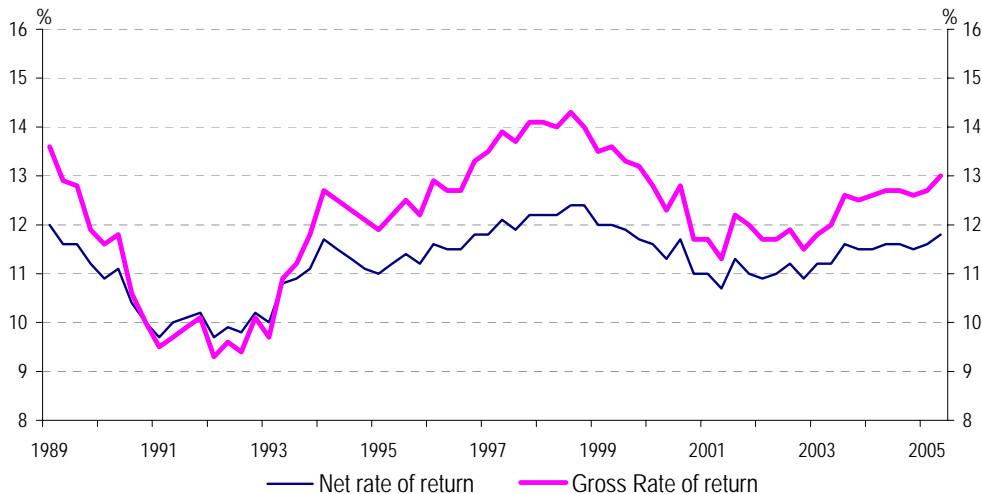
Chart 1. UK GDP growth



Source: ONS

Despite the slowdown in UK output growth, company profitability remains fairly strong. As chart 2 indicates, there was a decline in the gross and net rate of return on UK non-Continental Shelf companies¹ between around 1998 and 2001. In the last few years, however, profitability has recovered somewhat, so that the rates of return in 2005 Q2 stood just above their long-term averages.

Chart 2. UK company profitability (excluding continental shelf companies)



Source: ONS

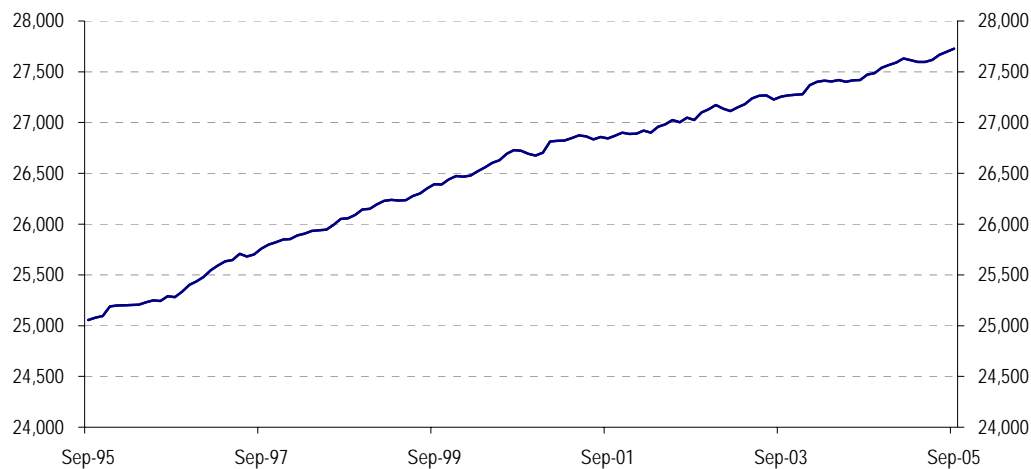
¹ This rate of return data therefore excludes profits made from oil extraction.

Looking ahead, according to the latest HM Treasury's Comparison of Independent Forecasts, external forecasters generally expect some pick up in overall UK output growth with a median forecast of 2.2 per cent for 2006. In part this is driven by expectations that consumption growth will firm up, as the housing market stabilises and lower interest rates feed through to spending.

Employment

Despite the slowing in UK economic growth, the labour market has continued to perform robustly. In the three months to September 2005, a record 28.8 million people were in employment. This represents an increase of 334,000 on a year earlier. Since spring 1997, UK employment has increased by around 2.4 million. Both male and female employment have grown, with male employment rising by around 1.1 million and female employment rising by around 1.2 million.

Chart 3. UK working age employment* ('000s), 1995-2005



Source: Labour Force Survey, ONS, seasonally adjusted

* Women aged 16-59, men aged 16-64

At the macroeconomic level, there is no evidence that the National Minimum Wage has had a significant impact on the level of employment; the level of employment was around 1.7 million higher in the three months to September 2005 than at the time of the minimum wage's introduction in April 1999. Equally, there is no evidence that recent upratings have had an impact. Employment was 262,000 higher in the three months to September 2005 than at the time of the October 2004 uprating, and employment continued to expand in the three months to September 2005 compared to the previous three months.

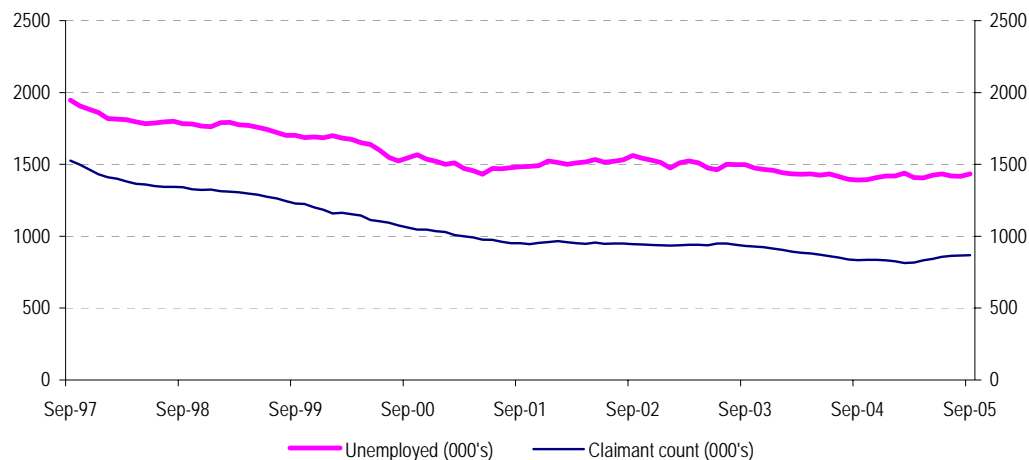
Unemployment

The unemployment rate on both the International Labor Organisation (ILO) and claimant count basis has remained low and stable by historical comparisons.

The ILO unemployment rate in the three months to September 2005 was 4.7 per cent, the lowest rate for 30 years. The claimant count rate of 2.8 per cent in September 2005 also remains close to its lowest rate since 1975. Unemployment has also been very stable in recent years. The ILO unemployment rate has not moved by more than 1 percentage point in either direction over the previous year since the three months to February 1998, the longest such period of stability since the start of the series in the 1970s.

There is no evidence that the National Minimum Wage has had any discernible effect on unemployment rates since its introduction. Between the introduction of the National Minimum Wage in 1999 and the three months to September 2005, the unemployment rate fell by 1.4 percentage points, with the male rate falling by 1.6pp and the female rate by 1.1pp. Since the start of the minimum wage, unemployment on the ILO basis has fallen by around 326,000.

Chart 4. Unemployment* and claimant count levels ('000s)



Source: ONS *Unemployment (ILO basis). Seasonally adjusted series.

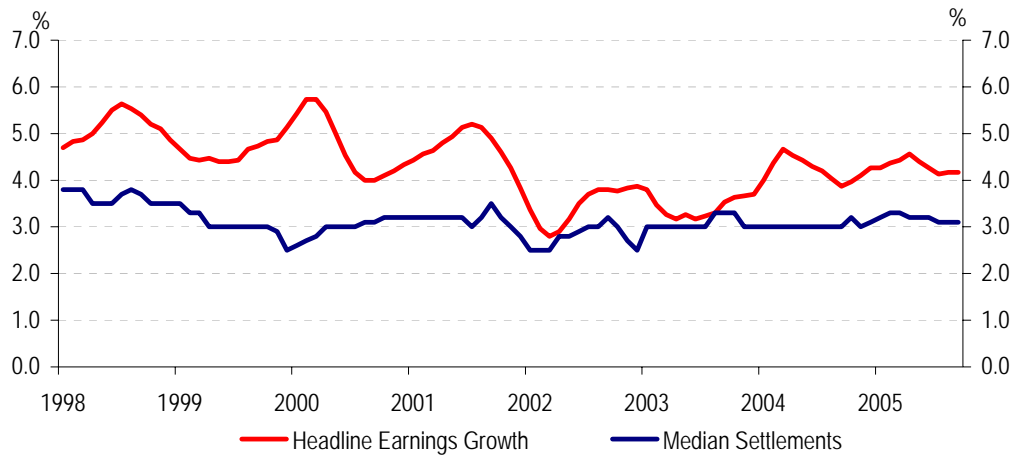
Looking ahead, slower output growth in 2005 and continued below trend growth in 2006 would be consistent with some easing in the rate of employment growth and a modest rise in the level of unemployment over the next few years. However, any rise in unemployment should be fairly modest given that independent forecasters project output growth to remain at rates of growth only just below trend in 2006. The Treasury Comparison of Independent Forecasts indicates that the median external forecast is for a small increase in claimant count unemployment by the end of 2006. Treasury growth forecasts are published with the PBR on 5th December.

Average earnings growth

Nominal earnings growth has remained fairly stable in 2005. The headline rate of annual earnings growth including bonuses was 4.1 per cent in September. For 2005 so far, earnings growth has averaged 4.3 per cent,

unchanged from the average over 2004. Bonuses have generally pushed up on earnings growth in 2005, so that the growth in earnings excluding bonuses in 2005 has averaged 4.0 per cent.

Chart 5. Average earnings growth and median pay settlements 1998-2005



Source: Average Earnings, Great Britain ONS, three-month moving averages. Seasonally adjusted. Median settlement level, Incomes Data Services, three month moving averages.

Looking forward, the Treasury’s Comparison of Independent Forecasts indicates that forecasters expect average earnings growth of 4.2 per cent and 4.1 per cent in 2005 and 2006 (based on median of external forecasters). Earnings growth remains consistent with the Bank of England’s inflation target.

The National Minimum Wage increased faster than average earnings between its introduction in 1999 and October 2004. Average earnings growth for the year to October 2005 is not yet available, but data so far for 2005 suggests that the 4.1 per cent rise in the minimum wage in October 2005 is likely to be broadly in line with average earnings growth.

SECTION 2

Aggregate minimum wage impacts

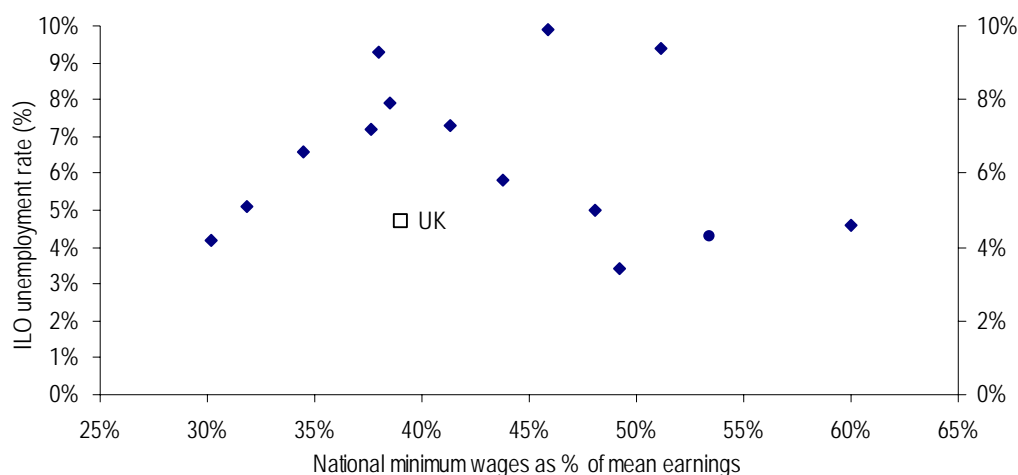
US analysis of the impact of minimum wages is mixed. However studies of the introduction of the UK minimum wage found no significant adverse employment effects. While the minimum wage 'bite' has gradually moved higher, changes in coverage have been more volatile.

Analysis of growth in industry wages and labour demand between 1998 and 2005 finds a generally positive association; low pay industries exhibited no obvious clustering or difference. Moreover, there was no statistically significant difference in the growth of labour demand between low-paying and high paying industries over this period.

The economics of minimum wages

The sections that follow in this submission address the impacts of the National Minimum Wage on specific industries and groups of employees. This section briefly addresses more aggregate economic impacts.

Chart 6. Minimum wages and unemployment rates in OECD economies



Sources: Unemployment rates from Eurostat and OECD. See table C2 in Annex C for minimum wage sources. Slovakia, Poland not shown.

Simple economic models predict that as long as the demand curve for labour is downward sloping – that is, employers demand less labour if its price rises – then an increase in the minimum wage should decrease employment of the affected group. However, if one looks at minimum

wages and unemployment rates across the OECD, only a very weak negative correlation of around -0.1 is found (Chart 6).

Minimum wages, clearly, are only part of the labour market picture – and quite possibly a relatively small part in many economies. Recent research has shown that most OECD countries with high unemployment also have quite restrictive employment protection laws and product market regulation. It is likely to be the interaction between these factors – along with their economic growth performance – that accounts for much of their relatively poor labour market performance.² The United Kingdom, by contrast, has amongst the least restrictive product and labour market regulations in the OECD.

Econometric analysis of the impact of minimum wages is likewise mixed. While most recent US economic studies have not found strong negative employment effects from increases in the adult minimum wage, there is some evidence of minimum wage increases reducing teenage employment.³ Intuitively this makes sense, as youth minimum wage rates are typically higher as a proportion of average youth wages – and cover a greater proportion of this labour pool – than adult minimum wages. This is the case both in the United States and in Britain.

In the United Kingdom, a consistent result from several economic studies of the introduction of the National Minimum Wage in April 1999 was of no significant adverse employment effects – including those on the 18-21 year old development rate.⁴ This is likely to be at least partly due to an initial rate that was not excessive. The robust pace of economic and employment growth during this period would also have helped UK employers to absorb the additional wage costs entailed.

But as the real rate of the NMW has risen at a faster pace than have average earnings since 1999, it is prudent to keep a watchful eye for the emergence of any such adverse impacts.

The overall labour market impact of the NMW

There are many potential ways of assessing the economic impact of the introduction of a minimum wage, and subsequent upratings. One might, for example, look at the ‘spike’ in the earnings distribution. The larger the spike, it is argued, the greater the likely effects.

Useful as this is, we prefer other measures. Two in particular that need to be taken into account are:

- The extent of **coverage** of the minimum wage – what proportion of the labour force receive or benefit from it?
- The so-called earnings **‘bite’** – what the level of the minimum wage is relative to average earnings.

² For a discussion see Nicoletti, et al (2001), OECD (2004) and Nicoletti (2005).

³ See Williams & Mills (2004), Neumark (2001). For the Canadian experience, see Campolieti, Fang and Gunderson (2005).

⁴ See for example Stewart (2004), Metcalf (2004), and Dickens & Manning (2004), along with studies on the Low Pay Commission. A summary of recent research is at Annex E.

Table 1. Employee coverage and 'bite' of the UK National Minimum Wage

Year	Adult NMW rate	Employee coverage ¹	Rate as % median
1999	£3.60	4.8%	45.6%
2000	£3.70	6.3%	45.3%
2001	£4.10	5.0%	48.0%
2002	£4.20	3.8%	47.2%
2003	£4.50	4.2%	48.6%
2004	£4.85	6.7%	50.5%
2005	£5.05	4.9%	50.5%

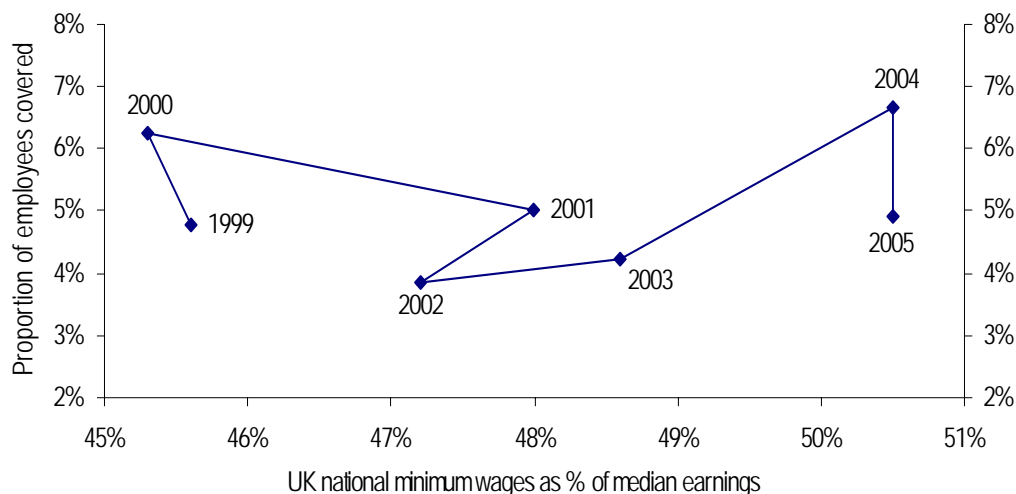
Source: DTI estimates, drawing on the Annual Survey of Hours and Earnings (ASHE) and Labour Force Survey (LFS). Estimates for 1998 to 2003 are based upon the central estimate of the LFS and ASHE. 2004 and 2005 based on ASHE.

¹ Coverage is defined as the % of total employees who stood to benefit from that year's uprating.

Information on these two measures is given in Table 1. One might expect them to be positively correlated. That is, if the minimum wage 'bite' increases, so too would the number of employees covered. However, as Chart 7 shows, that is not necessarily the case.

While the chart clearly shows a gradual movement higher (to the right) in the NMW relative to that of hourly median earnings, changes in coverage have been more volatile. While this may in part reflect employers increasing pay rates ahead of the official date of effect, other factors are no doubt also at work. Nonetheless, as of 2005 around 5 per cent of UK employees were covered by the National Minimum Wage – almost identical to our estimate of the extent of coverage after its introduction in 1999.

Chart 7. Trends in NMW coverage and 'bite' since 1999



Source: See Table 1.

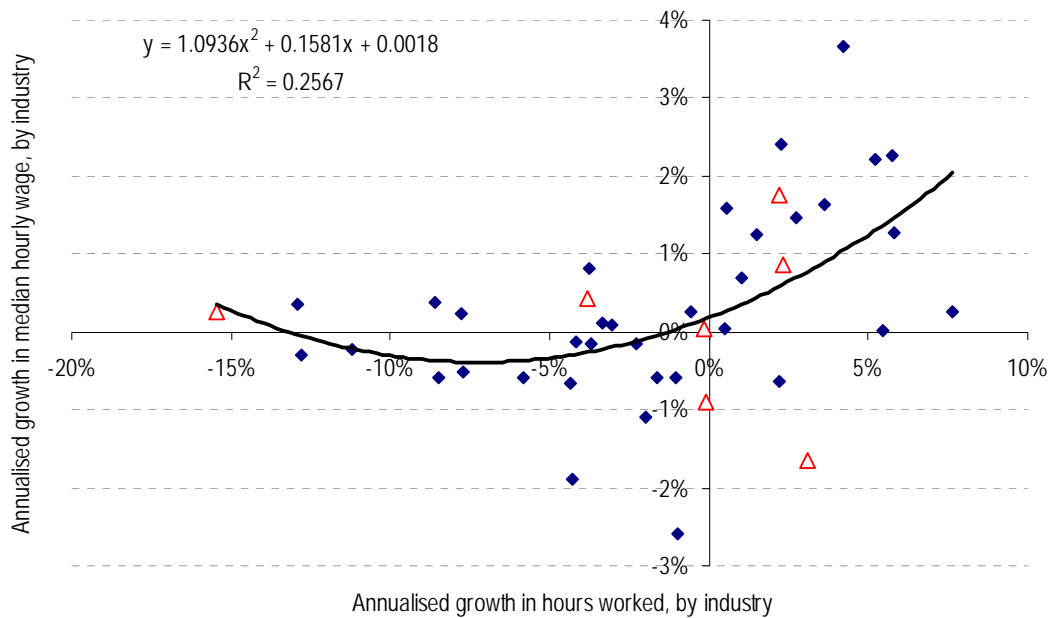
Aggregate wage and employment impacts of the NMW

Another way of looking at the aggregate evidence is to look at growth in wage and labour demand across industries, and to compare the growth rates of industries with a high proportion of low-paid workers with those that rely mostly on better paid employees.

Chart 8 below shows the annualised rate of growth in gross hourly median wages between 1998, before the introduction of the NMW, and 2005 against annualised growth in median hourly wages. We have deducted the national averages for growth in wages and hours worked in order to show the industry deviation from the average. The chart shows, firstly, that there is a positive – though not linear – association between industry wages growth over this period and labour demand (as expressed in total hours worked).

Second, if one compares growth in wages and hours worked amongst the low-paid industries (indicated with a red triangle) with the others, there is no obvious clustering or difference from industries with higher rates of pay. The sole exception is textiles manufacturing, which saw a large annualised fall in employment between 1998 and 2005.

Chart 8. Growth in average hourly wages and hours worked 1998-2005

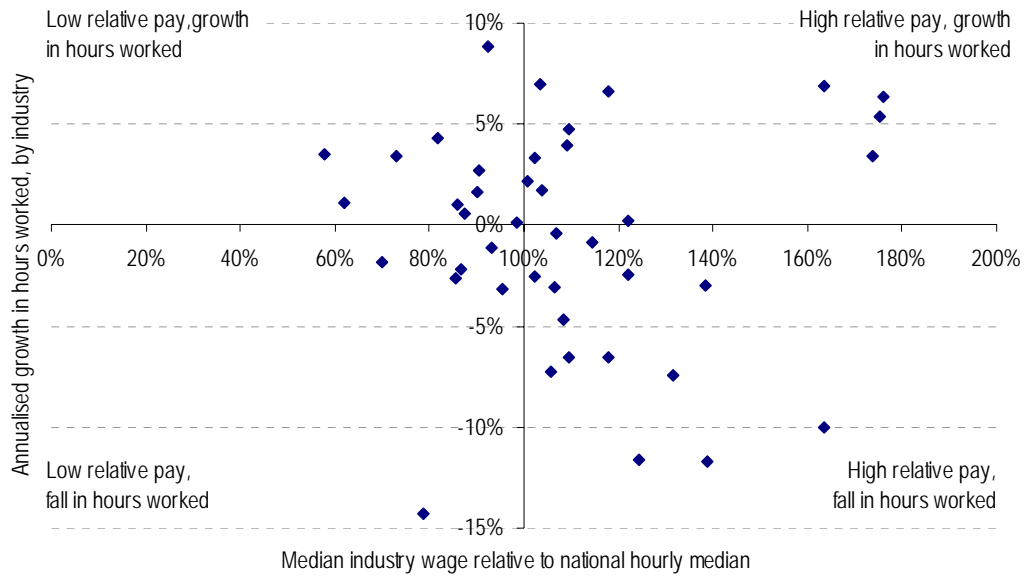


Source: Annual Survey of Hours and Earnings, 1998 and 2005, ONS

* Annualised growth in total basic hours worked. The 'relative industry wage' is the median hourly wage rate excluding overtime for each industry, expressed as a ratio to the national average gross median hourly wage excluding overtime in 2005.

Another way of looking at the data is to examine industries by their pay relative to the national median, and again consider annualised growth in hours worked. In the chart below, however, we have not removed the national average and simply show unadjusted annualised growth.

Chart 9. Growth in total hours worked 1998-2005, by relative industry wage*



Source: Annual Survey of Hours and Earnings, 1998 and 2005, ONS

* Annualised growth in total basic hours worked, by industry, between 1998 and 2005, against the industry median hourly wage rate excluding overtime relative to national hourly rate in 2005

This chart is effectively a random walk. There was no statistically significant difference in the annualised growth of labour demand (as expressed by hours worked) between low-paying and high-paying industries over this period.

In other words, both charts have found negligible sign of any aggregate impact on labour demand from the introduction, or subsequent increases, in the UK National Minimum Wage between 1998 and 2005.

SECTION 3

Evidence on the distribution of low pay

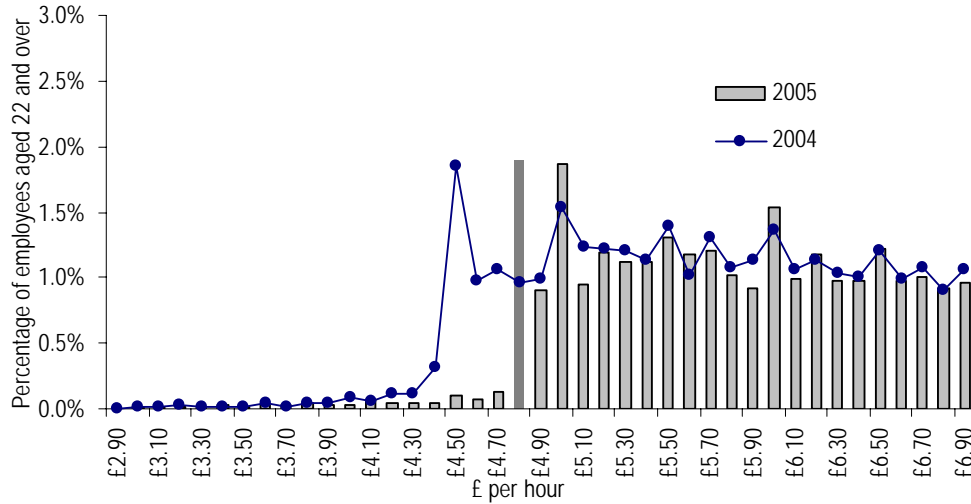
The national minimum wage 'bite', defined as value of the minimum wage to the average wage, was just over half the median hourly wage in 2005 - the same as in spring 2004. The proposed 5.9 per cent rise in the adult rate in October 2006 is likely to see a further modest rise in the bite. The UK level of the 'bite' is around the average for a sample of developed economies which have a national minimum wage in place. Looking at pay by age, the point where the minimum wage is closest to the median wage occurs around 18 years old, when the relevant minimum wage switches to the youth development rate. The earnings distribution has become significantly more compressed since the introduction of the minimum wage in 1999, with those at the bottom of the earnings distribution experiencing faster growth than those at the top.

The wage distribution

The National Minimum Wage will tend to truncate the bottom of the distribution of gross hourly pay. Relatively few employees would be expected to be paid below the relevant minimum wage rate. However there are exemptions for certain groups, some employees may legally be paid below the minimum wage hourly rate, and there may be also some non-compliance. This is discussed in detail below.

Looking at data from the Annual Survey of Hours and Earnings (ASHE) it shows a large jump in the distribution of adult hourly pay at the point where the minimum wage cuts in. As chart 10 illustrates, the uprating of the adult minimum wage from £4.50 to £4.85 in October 2004 resulted in this point moving from the old rate to the new higher rate.

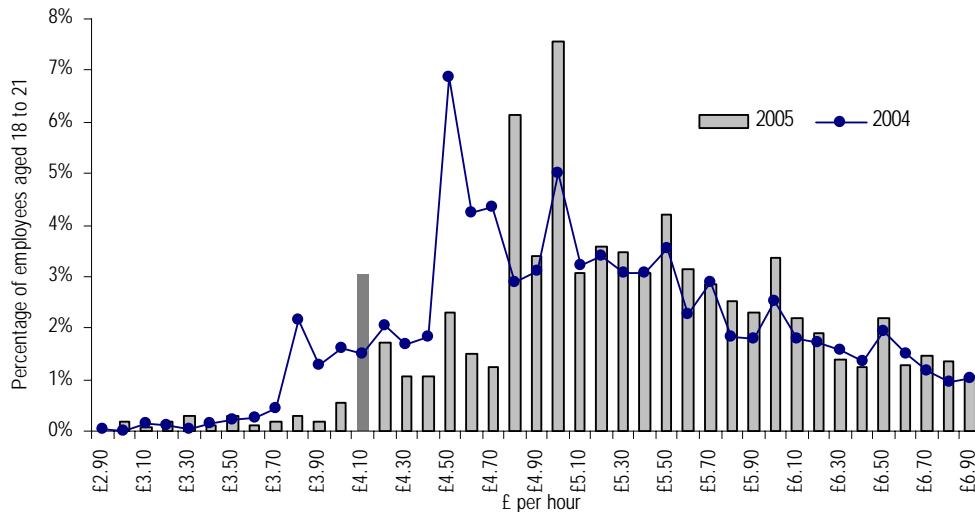
Chart 10: Adult low-paid distribution, April 2005



Source: Annual Survey of Hours and Earnings, ONS

A similar, though less dramatic, effect can be seen for the Development Rate, paid to 18 –21 year olds. Chart 11 shows a spike in the distribution of hourly pay around the Development Rate of £4.10. There is an even larger jump around the adult minimum pay rate of £4.85, reflecting the fact that most employers pay younger workers the full adult rate.

Chart 11. Youth (18-21 year olds) wage distribution, April 2005



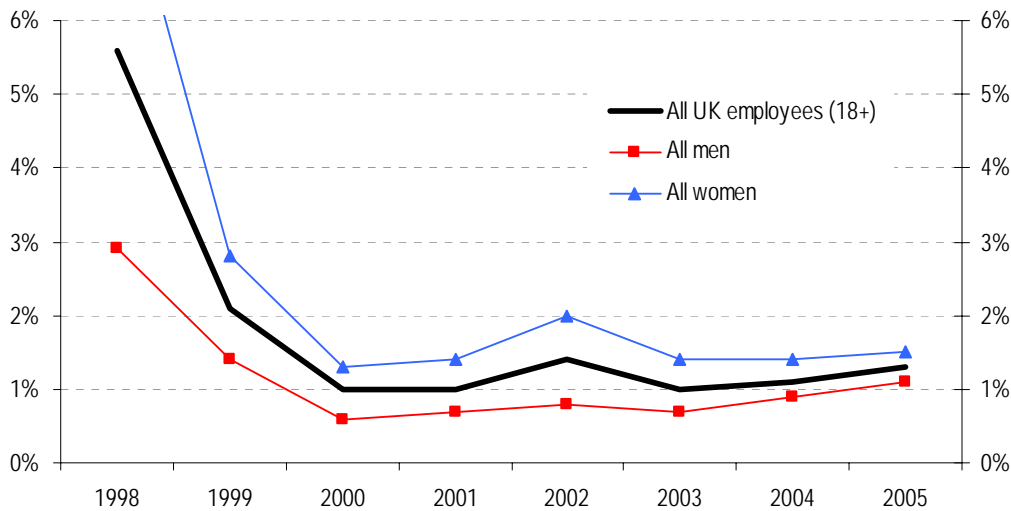
Source: Annual Survey of Hours and Earnings, ONS

Impact of the National Minimum Wage on gender inequality and the part-time pay gap

Evidence from the April 2005 ASHE shows that the National Minimum Wage has continued to help reduce gender inequality in pay rates. Between

1998 and 2005, the number of jobs held by women earning below the National Minimum Wage rate fell from 8.4 per cent of female workers to 1.5 per cent. In comparison, the number of men in jobs earning below the National Minimum Wage fell from 2.9 per cent of male workers to 1.1 per cent.

Chart 12. Female and male jobs earnings less than NMW rates (1998-2005)



Sources: Estimates for 1998 to 2003 are based upon the central estimate of the LFS and ASHE. 2004 and 2005 based on ASHE.

Part-time employees have also benefited substantially. Between 1998 and 2005, the number of jobs held by part-time workers earning below the National Minimum Wage rate fell from 870,000 (14.1 per cent of part-time jobs) to 158,000 (2.3 per cent). This compares with a decline in the number of jobs held by full-time workers earning below the National Minimum Wage rates from 410,000 (2.4 per cent of full-time jobs) to 168,000 (0.9 per cent).

The number of jobs paying less than National Minimum Wage rates

According to the latest Office for National Statistics (ONS) estimates of low pay based on data from the Spring 2005 ASHE survey, there were 327,000 jobs held by people aged 16 or over that paid less than National Minimum Wage rates, equivalent to 1.3 per cent of all UK jobs.

This comprised 249,000 jobs held by those aged 22 and over (1.1 per cent of jobs held by those in this age group), 57,000 jobs held by 18-21 year olds (3.2 per cent of jobs held by those in this age group) and 20,000 jobs held by 16-17 year olds (4.0 per cent of jobs held by those in this age group). The rise in the number of jobs paying below the minimum wage partly reflects the introduction of the new 16-17 year old rate: 20,000 jobs being held by 16-17 year olds are paying less than this new rate.

By comparison, using the ONS' previous methodology of the Central Estimate of the Labour Force Survey (LFS) and the New Earnings Survey (NES), around 1.3 million people (almost 6.0 per cent of employees) in

spring 1998 were in jobs paying below the National Minimum Wage rates that came into effect in April 1999.

Table 2. Number of jobs paid less than the National Minimum Wage¹

Spring quarter	16-17		18-21		22 and over		All jobs	
	'000s	%	'000s	%	'000s	%	'000s	%
1998 ²			110	7.2	1170	5.4	1280	5.6
1999 ³			40	2.4	460	2.1	490	2.1
2000 ³			30	2.2	190	0.9	230	1.0
2001 ⁴			40	2.1	210	0.9	240	1.0
2002 ⁵			50	2.7	290	1.3	340	1.4
2003 ⁶			40	2.3	210	0.9	250	1.0
2004 ⁷			44	2.4	235	1.0	279	1.1
2005 ⁸	20	4	57	3.2	249	1.1	327	1.3

Source: ONS. ¹Estimates for 1998 to 2003 are based on a central estimate of the LFS and ASHE.

²There was no National Minimum Wage in 1998, so figures for spring 1998 are based on 1999 rates i.e. the number of jobs paid at less than £3.00 per hour (aged 18-21) or £3.60 per hour (aged 22 and over). These are the revised estimates based on ASHE methodology.

³Rate is £3.00 per hour (aged 18-21) or £3.60 per hour (aged 22 and over). These are the revised estimates based on ASHE methodology.

⁴Rate is £3.20 per hour (aged 18-21) or £3.70 per hour (aged 22 and over). These are the revised estimates based on ASHE methodology.

⁵Rate is £3.50 per hour (aged 18-21) or £4.10 per hour (aged 22 and over). These are the revised estimates based on ASHE methodology.

⁶Rate is £3.60 per hour (aged 18-21) or £4.20 per hour (aged 22 and over). These are revised estimates based on ASHE methodology.

⁷Rate is £3.80 per hour (aged 18-21) or £4.50 per hour (aged 22 and over). These estimates are based on ASHE.

⁸Rate is £3.00 per hour (aged 16-17), £4.10 per hour (aged 18-21) or £4.85 per hour (aged 22 and over). These estimates are based on ASHE.

The ONS' estimate of the number of jobs paying below National Minimum Wage rates cannot be used as a measure of non-compliance with the National Minimum Wage regulations. There are a number of instances when an individual may legitimately earn less than the appropriate National Minimum Wage rate for their age. First, individuals may be on certain Government training programmes or apprenticeships, in which case they are exempt if aged below 19, and then exempt for the first year up to the age of 26. Estimates for 2004/05 from the LFS suggests that there may be around 240,000 people in this position. Second, employees may not be receiving the National Minimum Wage in cash terms because employers can legitimately reduce rates to take into account the cost of accommodation provided – from October 2004 this amounts to a daily offset of £3.75 leading to a maximum weekly offset of £26.25. Employees over 21 who receive accredited training (such as those doing NVQs) may also be exempted from receiving the full adult National Minimum Wage for the first six months with a new employer. In addition, workers may be exempted if they are members of the family working for the family business and living in the family home or if they live with a family and are treated as members of the family but are not related (such as au pairs).

The 'bite' of the National Minimum Wage

The minimum wage has been increased six times by the Low Pay Commission since its introduction in 1999. These annual increases are shown in table 3 below, alongside the annual growth rates of average earnings and consumer prices over the same period.

Though it commenced in 1999 at a relatively cautious hourly rate of £3.60, the adult National Minimum Wage rate has increased significantly in value

since then, rising by around 40 per cent over the past six years. Given the growth in consumer prices over the same period, that increase amounts to a real rise of 32 per cent, or an average real annual increase of 4.7 per cent.

Table 3. Percentage increases in NMW, earnings and consumer prices

Year	Adult hourly NMW rate	Median hourly earnings*	Avg earnings index ^{1**}	Consumer Price Index ¹	Retail Price Index ¹
2000	2.8%	3.3%	4.5%	0.8%	3.0%
2001	10.8%	4.8%	4.9%	1.2%	1.8%
2002	2.4%	4.1%	4.0%	1.3%	1.7%
2003	7.1%	3.9%	3.6%	1.4%	2.9%
2004	7.8%	3.8%	4.2%	1.3%	3.0%
2005	4.1%	4.2%	3.5% ##	1.9% #	2.5% #
2006	5.9%	-	-	-	-
1999-2005	40.3%	26.6%	27.8%	8.5%	16.0%
Avg annual rise	5.8%	3.8%	4.2%	1.4%	2.5%

Source: Annual Survey of Hours and Earnings, Average Earnings Index, Consumer Price Index, Retail Price Index, ONS.

¹ Annual average growth 2000 to 2004, latest monthly annual rise for 2005.

* Median gross hourly pay (excluding overtime), employees aged 22 and above on adult rates whose pay for the survey pay-period was not affected by absence. April figures.

** Average Earnings Index, all sectors, excluding bonuses # Annual change over the year to October ## Annual change over the year to September

Because the percentage rises in the minimum wage have on average been greater than the rise in 'average' earnings, the so-called 'bite' of the minimum wage has been rising.

The bite is a standard indicator used in the minimum wage literature, defined as the ratio of the nominal value of the minimum wage to the average wage, either mean or median. Usually the median is preferred to the mean as it is less likely to be distorted by changes in earnings dispersion.

The bite provides one measure of the extent to which the minimum wage compresses the wage distribution. As the 'bite' increases wage differentials are compressed at the lower end of the earnings distribution.

Table 4. The UK National Minimum Wage 'bite'

Year	Adult hourly NMW rate ¹	Mean hourly pay rate ²	NMW as % of mean	Median hourly pay rate ²	NMW as % of median
1999	£3.60	£10.08	35.7%	£7.90	45.6%
2000	£3.70	£10.49	35.3%	£8.16	45.3%
2001	£4.10	£11.11	36.9%	£8.55	48.0%
2002	£4.20	£11.70	35.9%	£8.90	47.2%
2003	£4.50	£12.08	37.3%	£9.25	48.6%
2004	£4.85	£12.37	39.2%	£9.60	50.5%
2005	£5.05	£12.96	39.0%	£10.00	50.5%

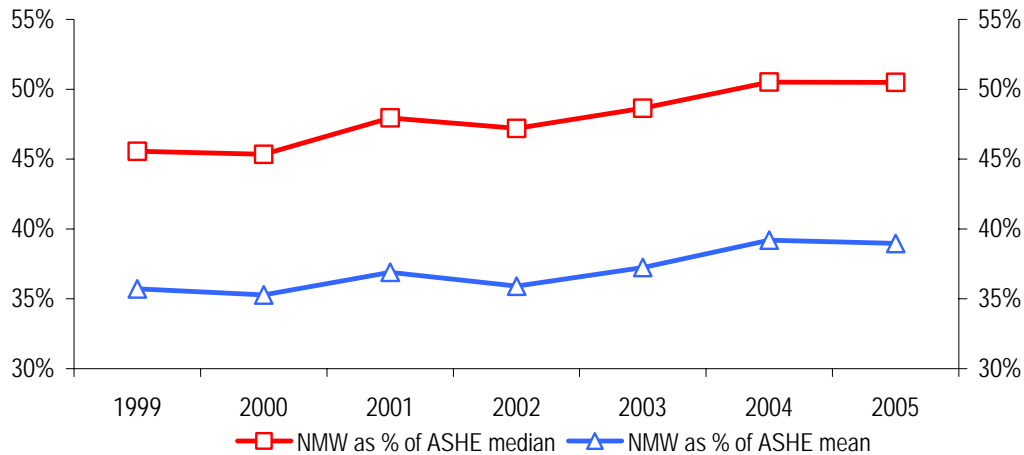
Source: Annual Survey of Hours and Earnings, ONS. Gross hourly pay (excluding overtime), employees aged 22 and above on adult rates whose pay for the survey pay-period was not affected by absence.

¹ October level

² April data

As both table 4 and chart 13 show, using either mean or median hourly earnings, the bite has gradually increased since the introduction of the minimum wage. In the case of the minimum wage relative to the mean, it has risen from a ratio of around 36 per cent to just below 40 per cent over the past six years. Relative to the median, the bite has risen from 45 per cent to 50.5 per cent. In other words, an employee half way up the earnings distribution (on median earnings) earned nearly twice as much per hour as an employee receiving the minimum wage in 2005.

Chart 13. The UK National Minimum Wage 'bite' over time



Source: Annual Survey of Hours and Earnings, ONS. Gross hourly pay rate, employees aged 22 or over. 1998-2003 ASHE excluding supplementary information. 2004-2005 ASHE including supplementary information.

The proposed 5.9 per cent increase in the adult minimum wage rate from October 2006 is likely to be above average wages growth over this period. Hence we would expect to see a modest rise in the minimum wage 'bite' next year.

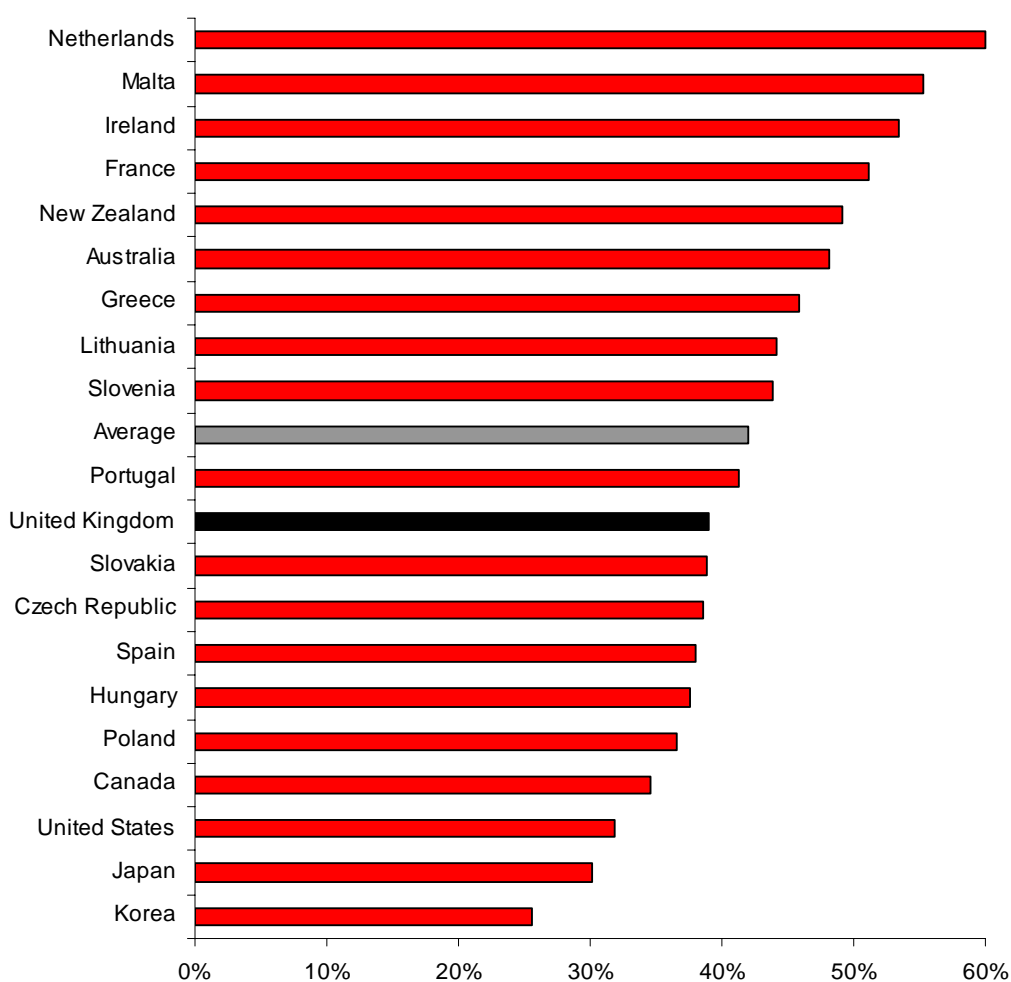
However, as outlined in Section 2, consideration also needs to be given to the extent of coverage of the National Minimum Wage. This is also an important factor in determining its overall economic impact.

International comparisons of the minimum wage 'bite'

A popular approach of comparing minimum wage rates across countries is to measure their relative value to mean or median wage rates. Due to the dispersion of earnings in some countries, using median earnings as the denominator is preferable.

A comparative analysis is provided in Annex C. For countries where the data is available, the ratio of the current minimum wage to mean and median earnings are reported. The mean earnings ratio is summarised below. It was not possible to obtain median earnings for most of the countries.

Chart 14. National Minimum Wage rate as percentage of mean earnings



Sources: Various. Please refer to Table C2, Annex C.

This data shows that the UK bite (39 per cent) is around average for the selected developed countries (42 per cent). Whilst higher than the United

States and Japan, it remains below the ratio for New Zealand, Australia and some European countries, including Ireland and the Netherlands.

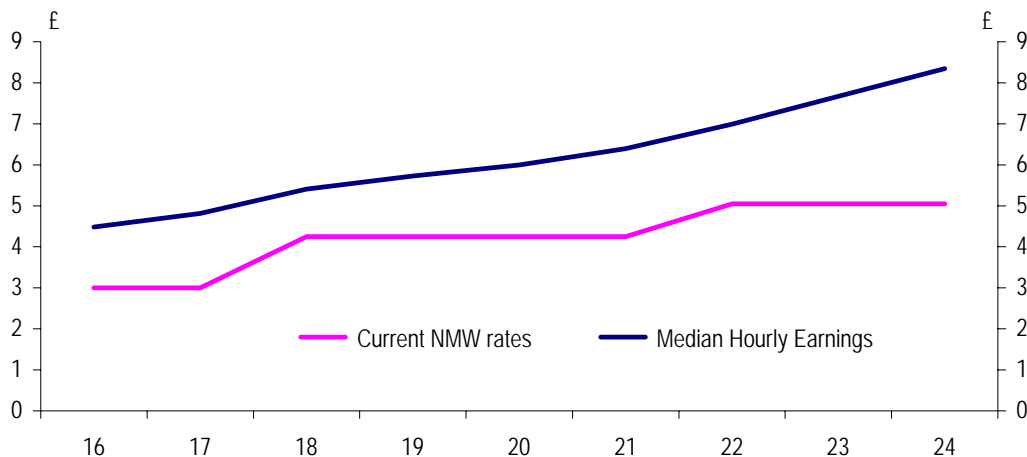
Age related pay and the minimum wage for 16-24 year olds

Median earnings tend to rise steadily by age. One reason for this is that the productivity of workers increases the longer they have been in employment. Furthermore, higher productivity workers who have benefited from Higher Education will tend to be flowing into the labour market as ages rise. Chart 15 shows median hourly earnings for ages 16 to 24 year old. As expected, median gross hourly pay rises across this age range.

The chart also shows the minimum wage level applicable at each age. Median earnings are generally closer to the minimum wage for younger workers than for adult workers. In other words, the 'bite' of the minimum wage is higher for younger workers generally than for the average worker on the adult rate.

The closest point is at 18 years old, where the relevant minimum wage switches to the youth development rate.

Chart 15. Hourly earnings by age, 16-24 (2005)



Source: Annual Survey of Hours and Earnings, ONS

Compression of the earnings distribution

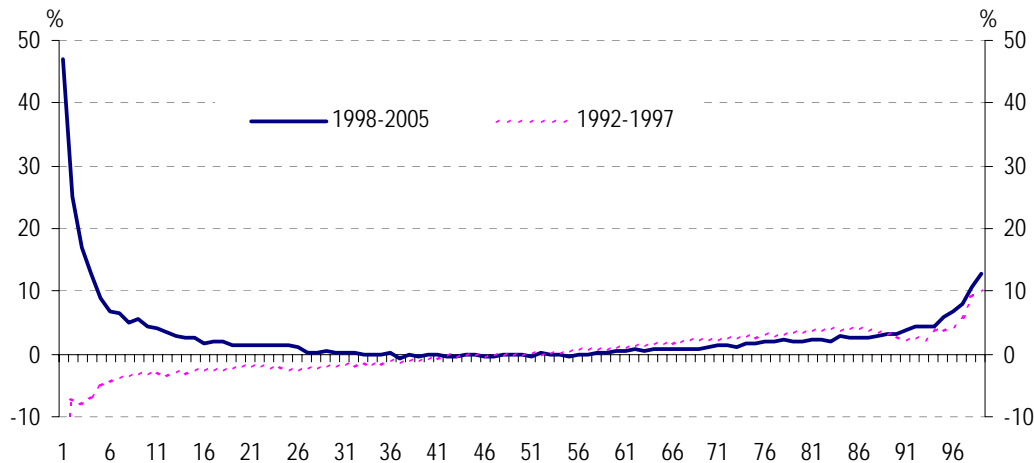
As noted in last year's Government submission and also in a recent *Labour Market Trends* article⁵, since the introduction of the National Minimum Wage the wage distribution has become more compressed, particularly at the lower end of the earnings distribution.

The minimum wage has increased by proportionately more than the median gross hourly wage since its introduction, so those at the bottom of

⁵ 'The hourly earnings distribution before and after the National Minimum Wage', Tim Butcher, *Labour Market Trends* September 2005.

the earnings distribution have experienced faster growth. But there has also been an 'upward ripple' effect reaching further up the earnings distribution, so that hourly pay has increased by more for those on the 10th and 20th percentile than for those at the median.

Chart 16. Cumulative increase in earnings by percentile, 1999-2005*



* Less the median increase for each period.

Source: 1992-1997 New Earnings Survey, 1998 to 2005 Annual Survey of Hours and Earnings, ONS. DTI calculations. There are discontinuities between the ASHE survey before and after 2004, which makes calculation of growth rates across this period subject to uncertainty.

Chart 16 shows the cumulative percentage increase in hourly earnings by percentile for the period 1998-2005 and 1992-1997, stripping out the median increase for each period. Both those near the top and the bottom of the earnings distribution have benefited from above-average increases over recent years. But employees at the lower end of the pay scale have received *larger* percentage increases in their pay than those at the top end since 1998. In contrast, over the period 1992 to 1997, those at the lower end of the income distribution received increases below the median rise. Of course, not all of these gains to workers on lower pay can necessarily be attributed to the National Minimum Wage. It is likely that other trends have also impacted on the distribution over the last few years.

SECTION 4

Developments in low-paying industries

Employment in most low-paying industries has increased significantly since the introduction of the minimum wage. Some industries (retail, hotels and restaurants, investigation and security) have seen their share of overall employment grow. Most other low-paying industries have broadly followed national employment trends. The recent slowdown in private consumption growth has been reflected in the retail sector, which has experienced slower rates of sales growth than in recent years. Wages growth in both retail and hotels and restaurants industries has been below average earnings growth, perhaps reflecting the weakness in these sectors. Looking ahead, external forecasters expect some strengthening in consumption next year.

Employment in low-paying sectors

In its reports, the LPC has identified a number of low-paying sectors that are particularly likely to be affected by the National Minimum Wage. These sectors include retail, hotels and catering, manufacturing of clothing and footwear, and various smaller service-sector industries such as security, cleaning, social work and hairdressing. Of these, the largest sectors are retail, hotels and catering, industrial cleaning and residential social care.

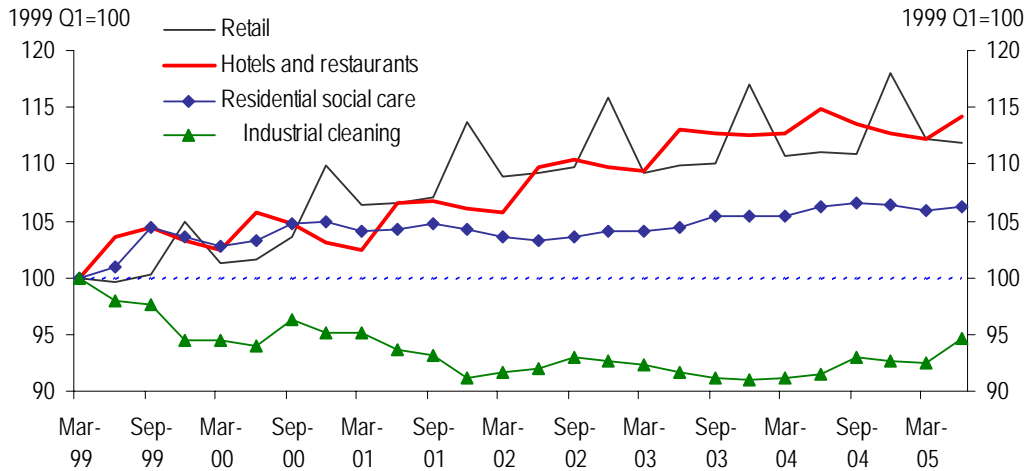
Looking at the Employee Jobs data for the low-paying sectors gives an idea of how these sectors have fared since the introduction of the minimum wage and its subsequent upratings.⁶

Chart 17 shows how the level of Employee Jobs has changed in the largest low-paying sectors since the first quarter of 1999. The number of employees has increased in all the major low-paying sectors since the introduction of the minimum wage, except in industrial cleaning. In fact the percentage increases in employees in retail, hotels and restaurants and residential social care since the first quarter of 1999 have been larger than the increase in employees across all sectors, so that their share of total employees has been rising. Over the year to 2005 Q2, employee jobs increased in retailing and industrial cleaning, were unchanged in residential social care and fell

⁶ For sectoral information, Employee Jobs data is preferred to Labour Force Survey (LFS) data because it is estimated from employer surveys, and employers should have a fairly accurate idea what sector they are in. However, Employee Jobs excludes the self-employed, and this will be important for a few sectors, such as hairdressing.

slightly in hotels and restaurants. Annex A presents further information on these major low-paying sectors, alongside information on the other, smaller sectors.

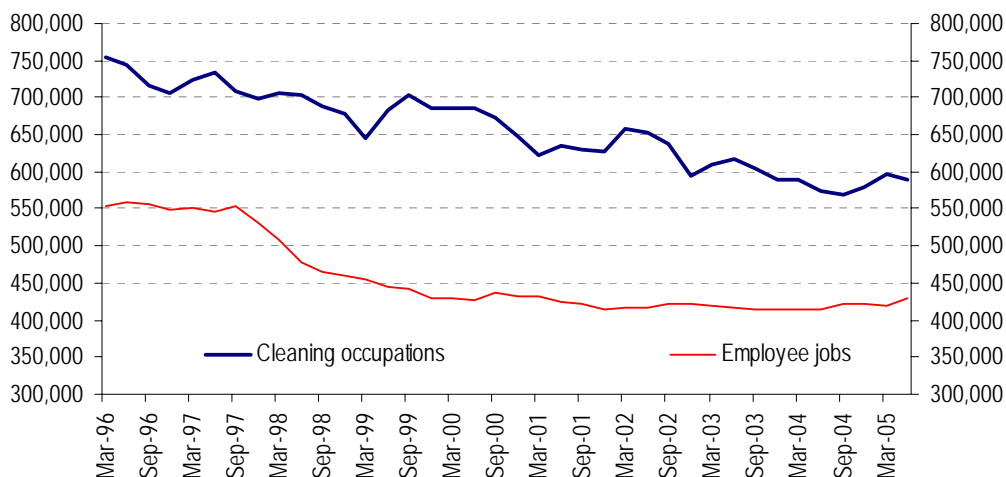
Chart 17. Employment in major low-paying sectors since 1999



Source: Employee jobs series, ONS

Chart 18 shows the number of employees in industrial cleaning has fallen since the introduction of the minimum wage, by around 5 per cent. However, the chart also shows that the fall in employees in industrial cleaning started before the introduction of the minimum wage, and the number of employees in cleaning has stabilised since 2002. Similarly, total employment (including those classified as 'self employed') in cleaning occupations fell but has now stabilised.

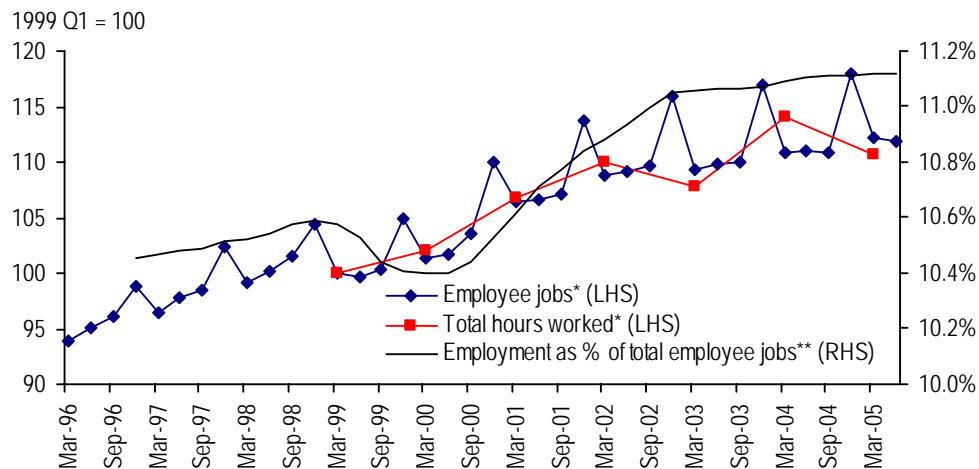
Chart 18. Employment levels in the cleaning industry



Source: Labour Force Survey and Employee jobs series, ONS. Cleaning occupations according to LFS Standard Occupation Classification. The LFS definition of occupations changed in Spring 2001 from SOC 1990 (958 'cleaners, domestics') to SOC 2000 (9233 'cleaners, domestics'). This may introduce a discontinuity into the data.

The number of jobs is one measure of labour input. But changes in the composition of full- and part-time employment and the length of working hours such as overtime may mean that changes in the demand for labour may not immediately be reflected in the number of 'heads' employed. In these circumstances it will also be useful to look at employment in terms of total hours worked. Chart 19 shows the level of employee jobs in the largest low-paying sector, retail, alongside a measure of total hours. It indicates that although the number of employee jobs has risen in the retail sector over the last year, total hours worked appears to have declined, by around 3.0 per cent in the year to Spring 2005. This fall in total hours in retailing may reflect falls in overtime and moves from full-time to more part-time employment in response to slower growth in consumer demand.

Chart 19. Measures of labour input in the retail sector



Source Employee jobs, Annual Survey of Hours and Earnings, ONS. *1999 Q1 = 100. **four quarter moving averages.

Annex A presents further data on employment and total hours worked for the other low-paying industries.

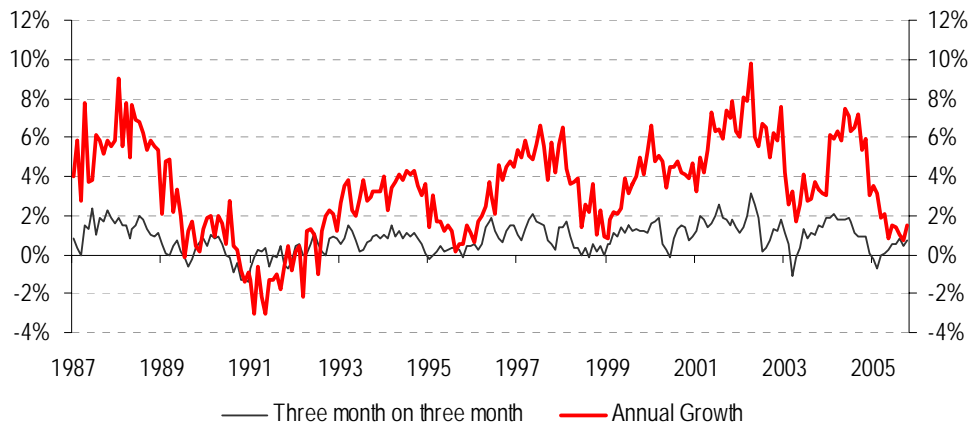
Other developments affecting low-paying industries

An important driver of the overall slowdown in UK GDP growth has been private consumption, which has slowed from an annual growth rate of 3.6 per cent in 2004 to 1.5 per cent in the year to 2005 Q2.

The slowdown in private consumption has also been reflected in slower growth in retail sales, with the volume of retail sales in October 2005 1.5 per cent higher than the same period a year earlier, compared to an annual growth rate in retail sales of 6.1 per cent in 2004. Weaker retail sales have also been reflected in weaker output growth in the retail sector. According to the relevant sub-component of the Index of Distribution, annual growth in Gross Value Added (GVA) in the Retail sector fell to 0.9 per cent in the three months to August 2005. Survey data such as the CBI Distributive

Trades survey have also suggested that the retail sector has been fairly depressed over the first half of 2005.

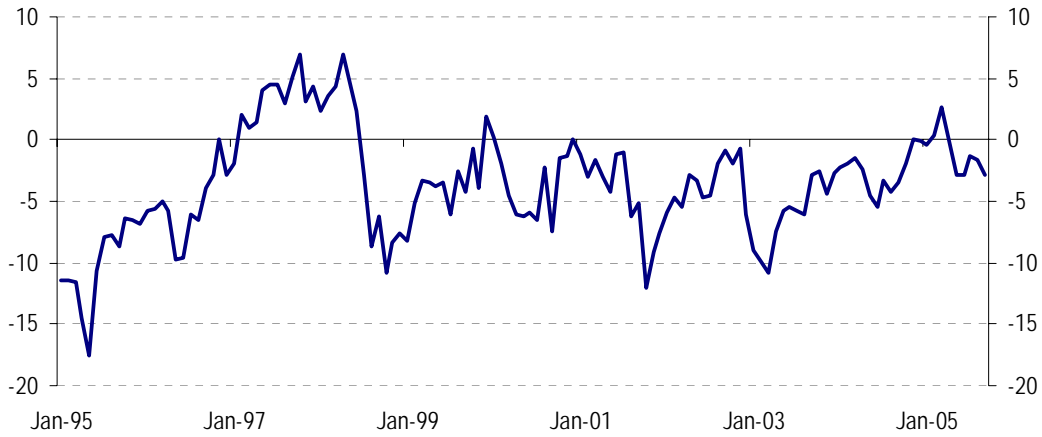
Chart 20: Growth in retail sales volumes (seasonally adjusted)



Source: ONS

There is, however, some evidence that the worst of the slowdown in retail spending may be over, with weak monthly growth around the start of 2005 still having an influence on annual comparisons. The volume of retail sales in the three months to October 2005 was 0.7 per cent higher than the previous three months, significantly greater than the average for the first half of 2005. Similarly, there is some evidence that the worst of the slowdown in output in the retail sector may have occurred earlier in 2005. GVA in the retail sector increased by 0.3 per cent in the three months to August compared to the previous months, compared to a fall of 0.9 per cent in the three months to February. There has also been some indication from the CBI Distributive Trades survey that the rate of decline in sales has slowed. And although consumer confidence has fallen back, it remains at fairly elevated levels by historical standards.

Chart 21. UK consumer Confidence (net balance)

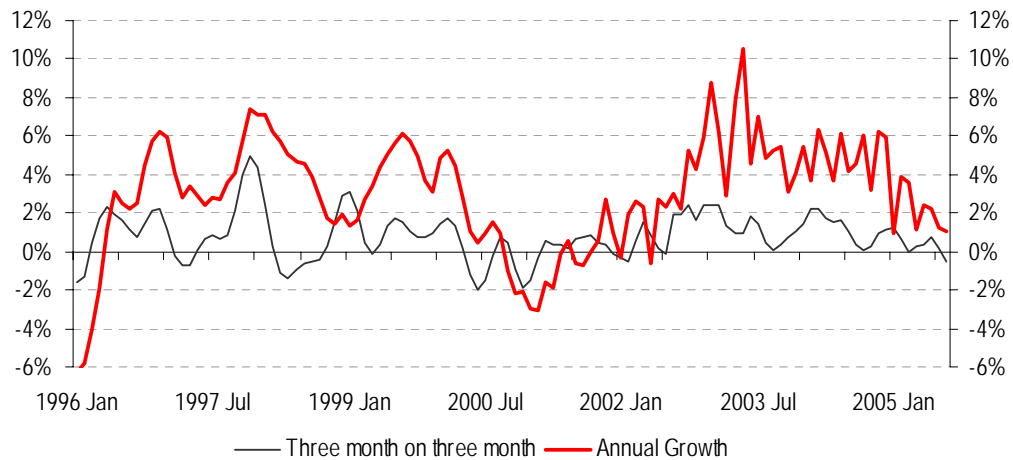


Source: European Commission Survey

The Treasury Comparison of Independent Forecasters suggests that most external forecasters expect some pick-up in annual consumption growth in 2006. In turn, a pick-up in consumption growth should be reflected in stronger retail sales in 2006.

Hotels and restaurants have, in a similar fashion to retailing, seen a decline in activity in 2005. ONS's experimental index of GVA in the hotel and restaurant sector indicates that annual growth in output in this sector fell to 1.0 per cent in August 2005, down from a peak of 6.2 per cent in November 2004. Prospects for this sector should in part be similar to those in retailing, although clearly the hotel sector depends significantly on developments in the global economy, including the number of tourist visits to the UK.

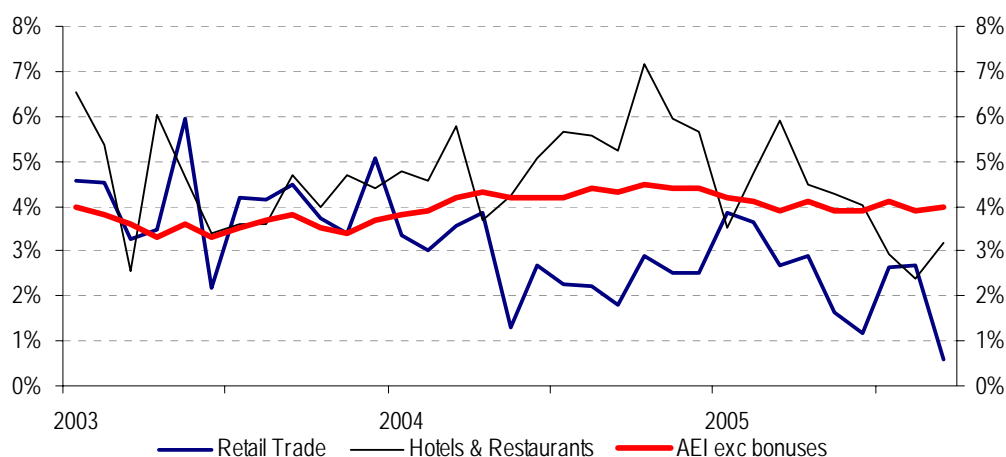
Chart 22. Growth in Gross Value Added in the Hotel and Restaurant Sector



Source: Index of services, ONS

Probably reflecting the proportionately greater slowdown in consumer spending, earnings pressure has been weaker in the retail sector and in hotels and restaurants than in the overall economy. Annual earnings growth excluding bonuses was 0.6 per cent in the retail trade and repairs sector, and 3.2 per cent in the hotels and restaurants sector in September 2005. These figures are somewhat lower than annual growth in average earnings excluding bonuses for the economy as a whole, which stood at 4.0 per cent in the three months to September. Developments in earnings growth in 2006 are most likely to be influenced by the degree to which these sectors experience a bounce-back from weaker output growth in the first half of 2005.

Chart 23. Annual growth in average earnings excluding bonuses



Source: ONS

Regional employment in low-paying sectors

We have also looked at the regional Employee Jobs data for low-paying sectors to see if there has been any deterioration in employment in specific regions following the impact of the minimum wage. However the data is only available up to 2003, which limits the ability to analyse the impact of more recent movements in the minimum wage.

In general, employment in the low-paying sectors at the regional level has followed developments at the national level. In retail, for example, employment has expanded in all regions of Great Britain since 1998.

There are, however, a few examples where this has not been the case. In hairdressing, while employment has generally expanded across the regions since 1998, it fell slightly in the North East, London, the South West and in Wales. The falls in these regions were fairly small in absolute numbers, and it is possible that the fall in employees was offset by a rise in self-employment. Another area to buck the national picture was hospitality in the East Midlands, which saw a fall in employee jobs of 3,000 between 1998 and 2003. Social work in London and the South West also experienced

small falls in the number of employee jobs between 1998 and 2003. On the other hand, employment in industrial cleaning expanded in the North West, South East and the South West while it declined in Great Britain as a whole.

Generally, therefore, the regional picture has resembled the national employment picture for the low-paying sectors since the introduction of the national minimum wage. Where divergences do exist they tend to be small in absolute terms, and probably reflect other factors in the local economies rather than the impact of the minimum wage.

SECTION 5

Developments in the labour market for younger workers

The overall employment rate of 18-21 year olds has fallen back somewhat since its peak in 2000, but the unemployment rate remains lower than at the time of the introduction of the minimum wage. On balance the labour market position of 21 year olds remains closer to younger workers than to workers on the adult rate, although the hourly wages of relatively few 21 year olds (around 8.0 per cent) are below the adult minimum wage rate.

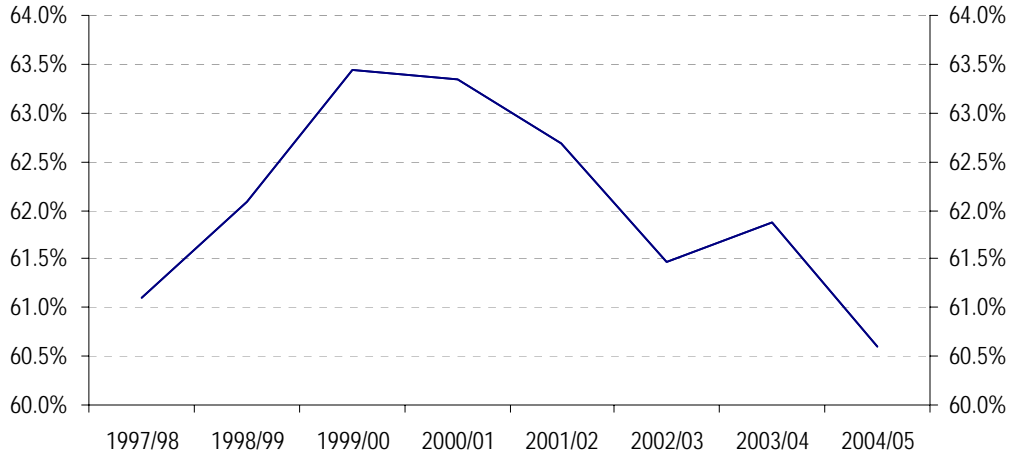
Employment of 18-21 year olds

Younger workers are typically less skilled and productive than older workers. For this reason a lower National Minimum Wage development rate is in place that seeks to help workers aged 18 to 21 years old while not jeopardising their employment prospects.

Since its peak in 2000, the employment rate of 18 to 21 year olds has fallen back. One possible explanation for this fall might be that the proportion of 18 to 21 year olds involved in study has increased, which would tend to push down the employment rate for this age group. But when we look at the employment rate of 18 to 21 year olds excluding students and graduates, there are still signs of a small fall in the employment rate of this age group.

Both men and women aged 18 to 21 have experienced falling employment rates, although over the last year the female employment rate has flattened off, while the male employment rate has continued to fall. However, over the last year the employment rate has risen for females aged 16 upwards, while the male employment rate has declined for this age group. So it is not obvious that the difference between 18 to 21 year old male and female employment rates has an age-specific dimension.

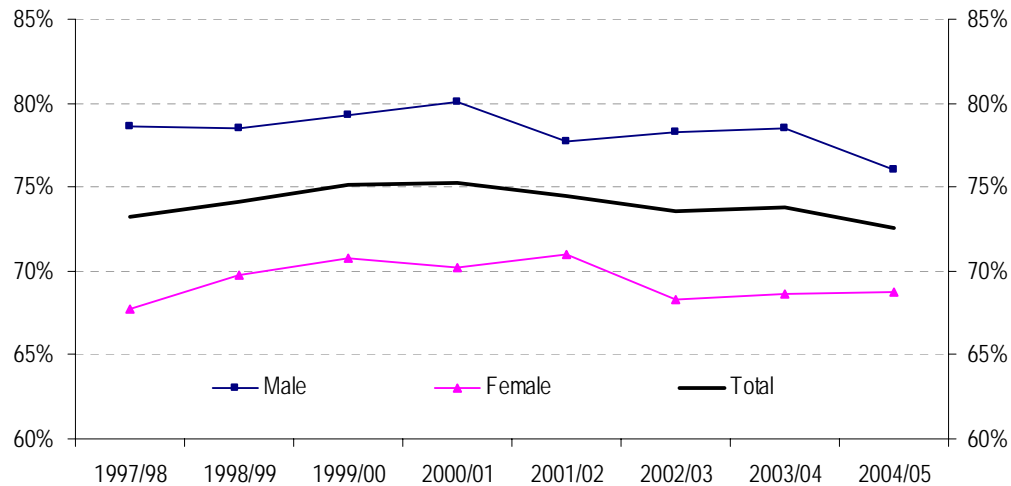
Chart 24. Employment rate of 18-21 year olds, 1997 to 2005¹



Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

Chart 25. Employment rate of 18-21 year olds, 1997 to 2005*¹

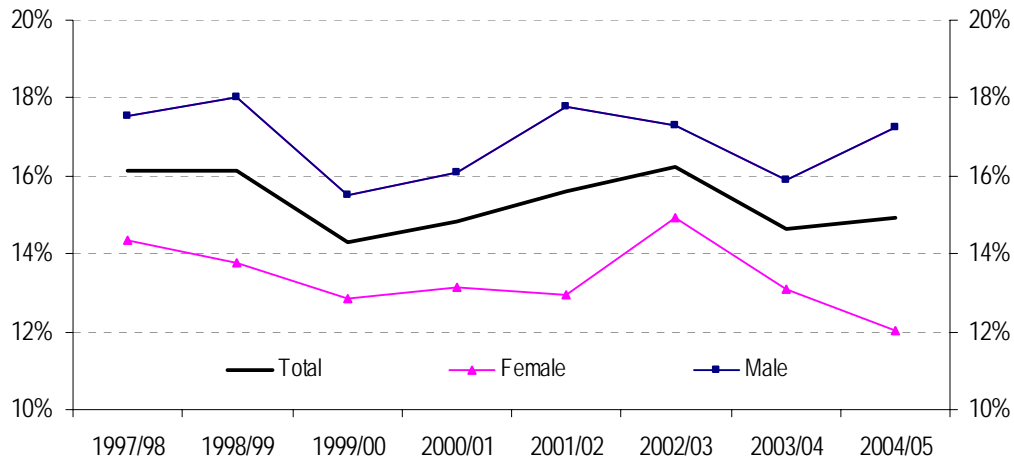


Source: Labour Force Survey, ONS * Excluding students and graduates

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

The fall in the employment rate amongst 18 to 21 year olds has not been matched by a consistent rise in their unemployment rates (see chart 22 below). Instead, the inactivity rate of this age group has increased.

Chart 26. Unemployment rate of 18-21 year olds (Excluding full-time students and graduates), 1997 to 2005¹



Source: Labour Force Survey, ONS

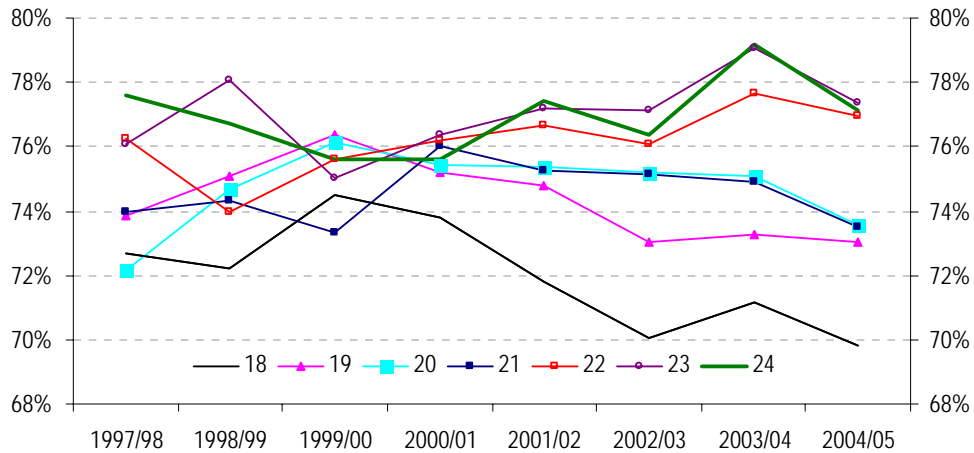
¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

Minimum wage treatment of 21 year olds

Currently 21 year olds are covered by the youth development rate. The Government has previously rejected recommendations from the Low Pay Commission to move 21 year olds onto the adult rate, as it has been felt that the performance of 21 year olds resembles more closely that of 18 to 20 year olds. Younger workers have lower employment and higher unemployment rates than older workers (even when we exclude students and graduates). If 21 year olds were more similar to 19 to 20 year olds than to older workers, moving them to the full adult rate may damage their employment prospects.

Chart 27 plots employment rates excluding students and graduates, by individual age. It suggests that the labour market position of 21 year olds remains more similar to that of 20 year olds than to older workers. The unemployment rate of 21 year olds also remains above that for 22 year olds, as illustrated in Chart 28.

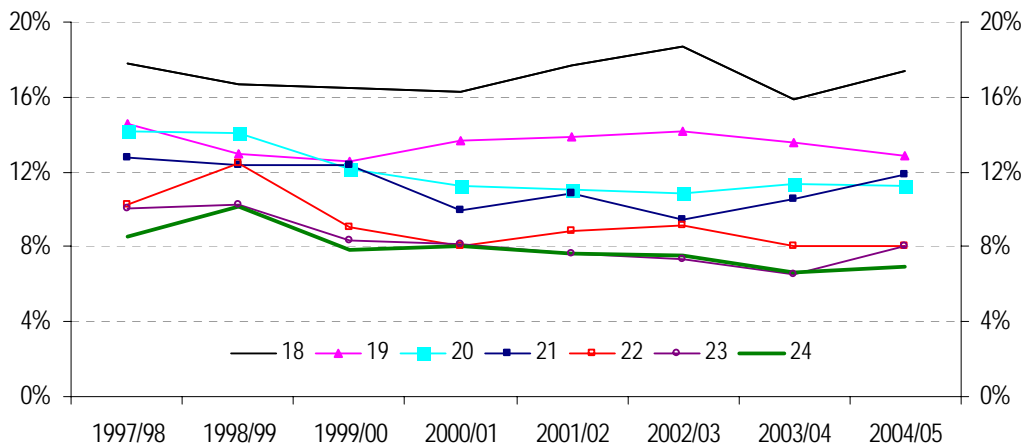
Chart 27. Employment rate of 18-24 year olds (1997 to 2005). Excludes full-time students and graduates¹



Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

Chart 28. Unemployment rate of 18-24 year olds (1997 to 2005). Excludes full-time students and graduates¹

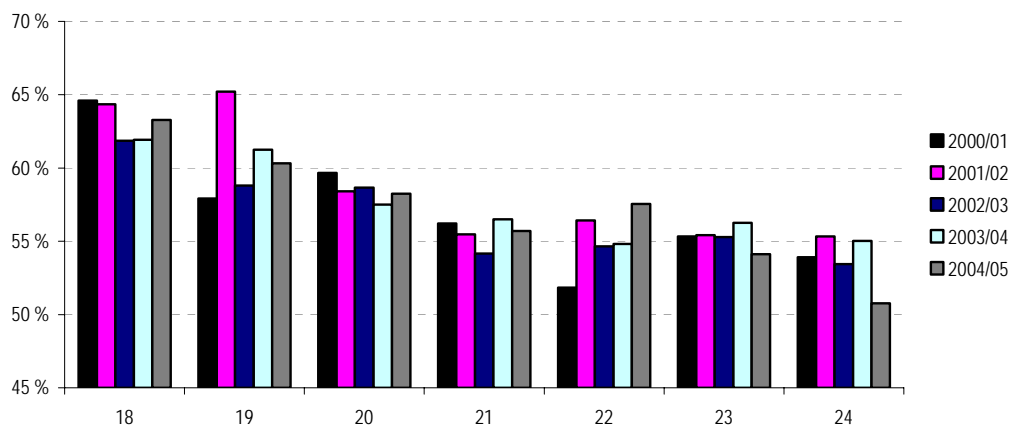


Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

Low-skilled workers are particularly likely to be covered by the minimum wage. In the most recent data the employment rate amongst 21 year old low-skilled females is a little lower than for 20 and 22 year olds. The unemployment rates of 21 year old low-skilled females are similar to 20 year olds.

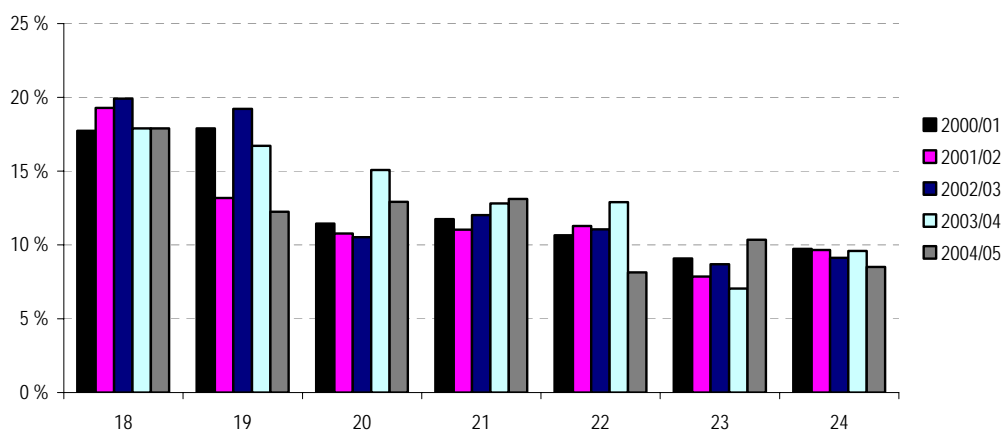
Chart 29. Employment rates of low-skilled, female 18-24 year olds (excluding full-time students)¹



Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

Chart 30. Unemployment rates of low-skilled, female 18-24 year olds (excluding full-time students)¹

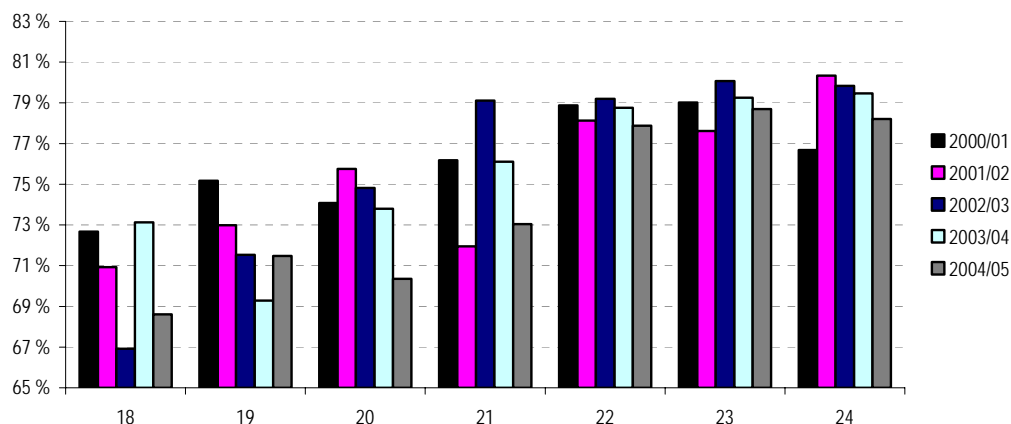


Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

For 21 year old low-skilled males, the employment rate in 2004/05 is lower than that for 22-24 year olds and higher than that for 20 year olds. The unemployment rate of 21 year olds low-skilled males remains well above that for 22 to 24 year olds, and similar to 19 and 20 year olds.

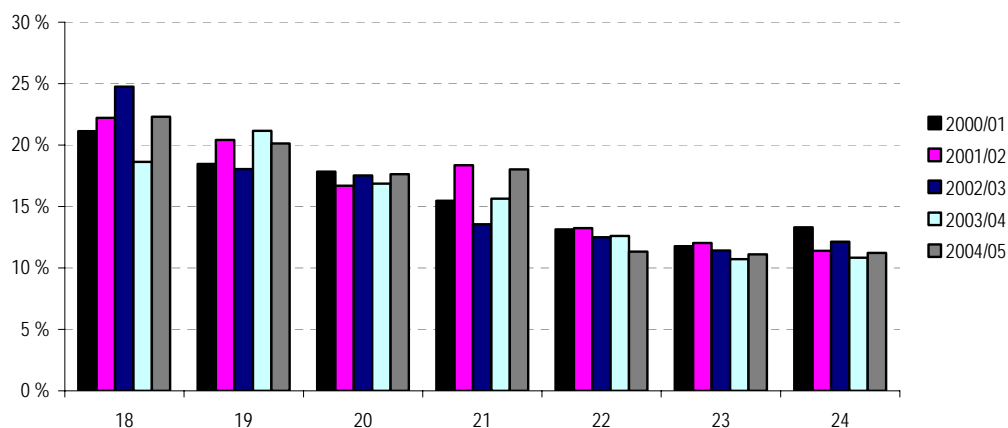
Chart 31. Employment rates of low-skilled, male 18-24 year olds (excluding full-time students)¹



Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

Chart 32. Unemployment rates of low-skilled, male 18-24 year olds (excluding full-time students)¹



Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

On balance the labour market position of 21 year olds remains closer to younger workers than to workers on the adult rate, although the hourly wages of relatively few 21 year olds (around 8.0 per cent) are below the adult minimum wage rate.

Annex D compares employment and unemployment rates by age groups in the UK and selected European countries.

SECTION 6

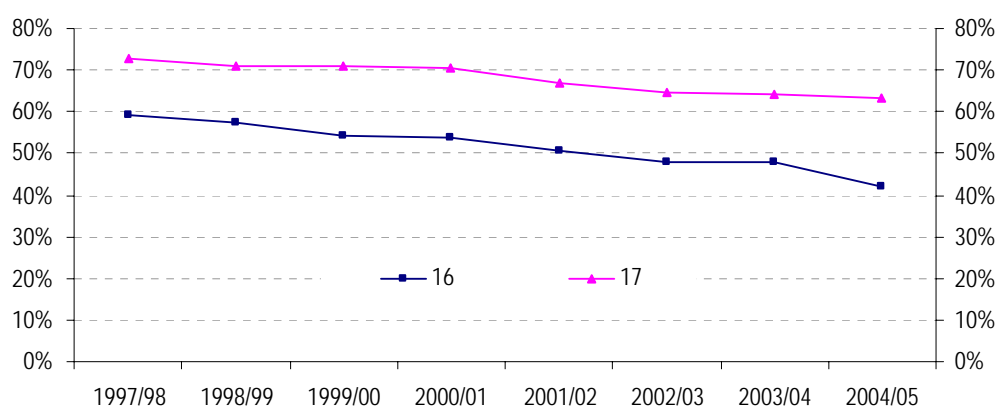
Developments affecting 16-17 year olds

So far there has been no discernible adverse impact of the national minimum wage on the participation of young people aged 16-17 years in education or training. There has also been no rise in the proportion of 16 and 17 year olds who are not receiving education or training (NET) in recent years. The inactivity rate of 16-17 year olds has been rising, however this reflects higher proportions of 16-17 year olds entering education rather than entering the NEET group.

Labour market position of 16-17 year olds

The minimum wage rate for 16-17 year olds was introduced in October 2004, at the same time a number of other policies were implemented. It was set at the lower rate of £3.00. The Government's aim is to afford very young workers some protection from poverty pay, while maintaining the incentives for 16-17 year olds to remain in education or job-related training and build-up their knowledge and future earnings potential. The Government is also concerned that the minimum wage for 16-17 year olds should not discourage firms from taking youngsters on as apprentices, as

Chart 33. 16-17 Employment rates excl. students and graduates (%)¹



Source: Labour Force Survey, ONS

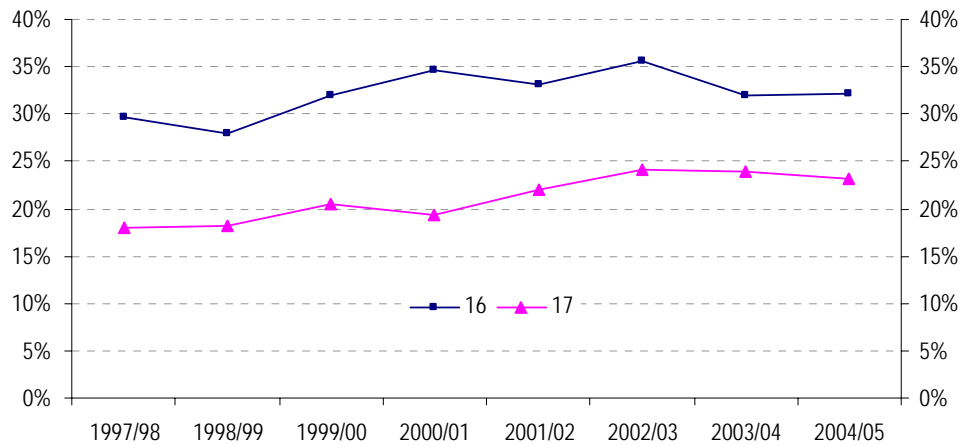
¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

this would inhibit the opportunity for some 16-17 year olds to gain from an important form of training; for this reason, apprentices aged 16-18 are exempt from the minimum wage.

In contrast to the overall population, but similarly to other young workers aged 18-21, the employment rate of young people aged 16 and 17 has declined in recent years.

Alongside the decline in employment rates, there has been a modest rise in the unemployment rate of 17 year olds, with the 16 year old rate remaining broadly flat.

Chart 34. 16-17 Unemployment rates exc students and graduates (%)¹

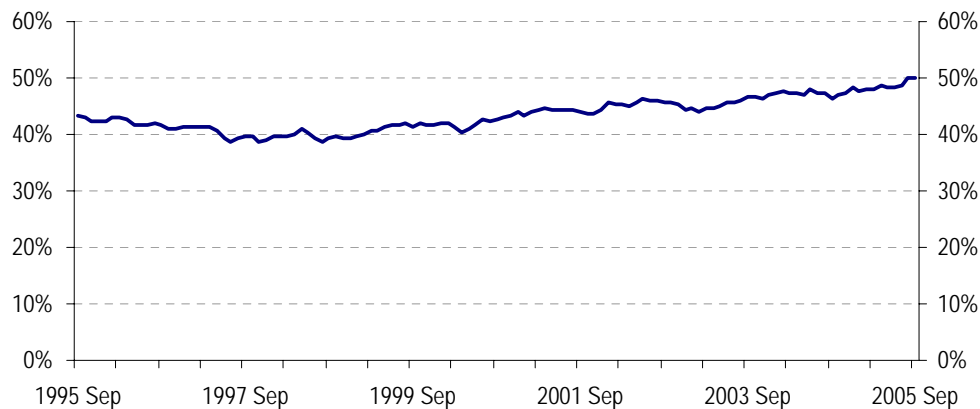


Source: Labour Force Survey, ONS

¹ Annual data includes the most recent June-August seasonal quarter, i.e. 2004/05 covers September-November 2004 to July-August 2005.

The most striking change in economic activity has been the increase in the inactivity rate of 16 and 17 year olds, chart 35. This pattern was not observed elsewhere in the labour market, with the inactivity rate for the rest of the working age population broadly constant.

Chart 35. 16-17 inactivity rates (%)

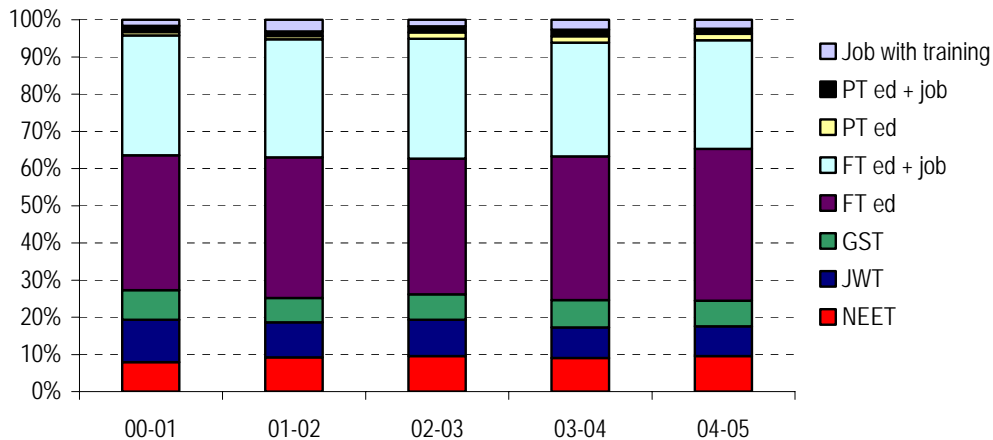


Source: Labour Force Survey, ONS

Detailed breakdown of 16-17 year old economic status⁷

Chart 36 indicates that there has been no discernible impact of the National Minimum Wage on the participation of 16 and 17 year olds in education or training. Participation remained constant at 81 per cent between 2000/01 and 2002/03, increased slightly to 83 per cent in 2003/04, before edging back to 82 per cent in 2004/05.

Chart 36. Economic status of young people aged 16-17

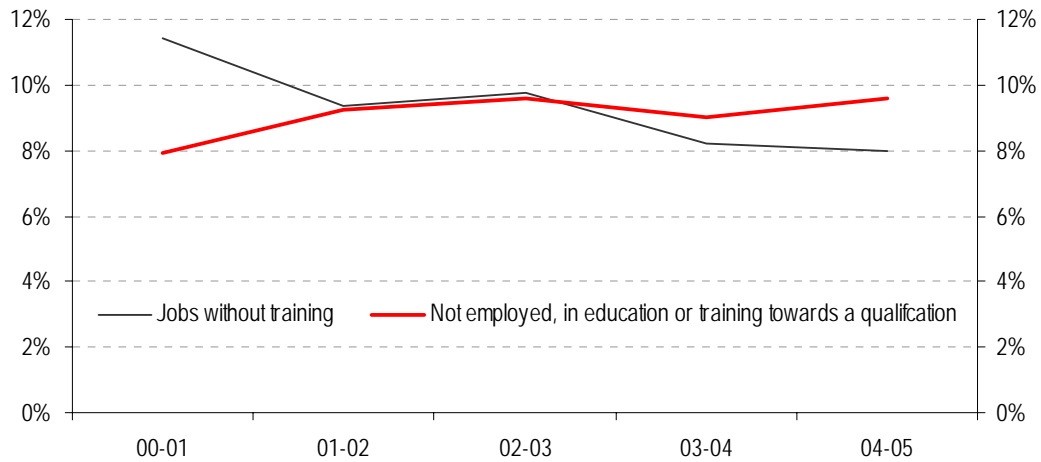


Where: PT ed + job=part-time education and employed; PT ed = part-time education; FT ed + job= full-time education and employed; FT ed=full-time education; GST = Government supported training; JWT = Job with training; NEET = not in employment, education or training.
Source: Labour Force Survey, ONS

Breaking down the form of education, the proportion of 16 and 17 year olds in full-time education without a job has increased in the last few years, from 36 per cent in 2000/01 to 41 per cent in 2004/05. However, the proportion combining full-time education with a job fell over this 5 year period from 32 per cent to 29 per cent, leaving the overall proportion in full-time education (with or without a job) stable at around 70 per cent. The proportion of 16 and 17 year olds in part-time education (with or without a job) has constituted between 2 per cent and 4 per cent of the cohort since 2000/01, again with no discernible trends. The proportion of 16 and 17 year olds undertaking government supported training has remained around 7 per cent across the 5 year period. Similarly, the proportion of 16 and 17 year olds in employment and studying towards a qualification (outside of any government supported training) has been broadly flat, fluctuating between 2 per cent and 3 per cent over the 5 year period.

⁷ The labour market indicators for 16 and 17 year olds reported here from the LFS do not match exactly those reported in the Statistical First Release (SFR): 'Participation in Education, Training and Employment by 16-18 Year Olds in England: 2003 and 2004'. This is due to a number of reasons. For example, the SFR uses academic age to select 16 and 17 year olds (rather than actual age), applies to England only (as opposed to England and Wales) and combines the Winter LFS quarter with other administrative data. Nevertheless, the general trends reported in the analysis above are supported by those in the SFR.

Chart 37. Economic status of 16/17 year olds



Source: Labour Force Survey, ONS

Chart 37 indicates that the proportion of 16 and 17 year olds not in education, employment or training towards a qualification (NEET) has hovered around 9 per cent to 10 per cent over the last 5 years. Similarly, the proportion in jobs without training (JWT) has not displayed a clear trend, remaining at 8 per cent in both 2003/04 and 2004/05. Therefore, the overall proportion of 16 and 17 year olds not receiving education or training (NET) has been broadly flat in recent years, fluctuating around 18 per cent.

The introduction of a national minimum wage of £3.00 for 16 and 17 year olds in October 2004 does not appear to have had an adverse impact on participation in education or training. Whilst employment rates of 16 and 17 year olds have fallen and inactivity rates have risen both before and after the introduction of the minimum wage, this has been associated with a rise in the proportion of young people entering education (rather than becoming NEET). It is not possible of course to isolate the impact of the minimum wage from other policy changes which may be simultaneously implemented. Furthermore, even if there have been no discernible impacts in the period following its implementation, these may take time to feed through to the labour market as the policy beds in.

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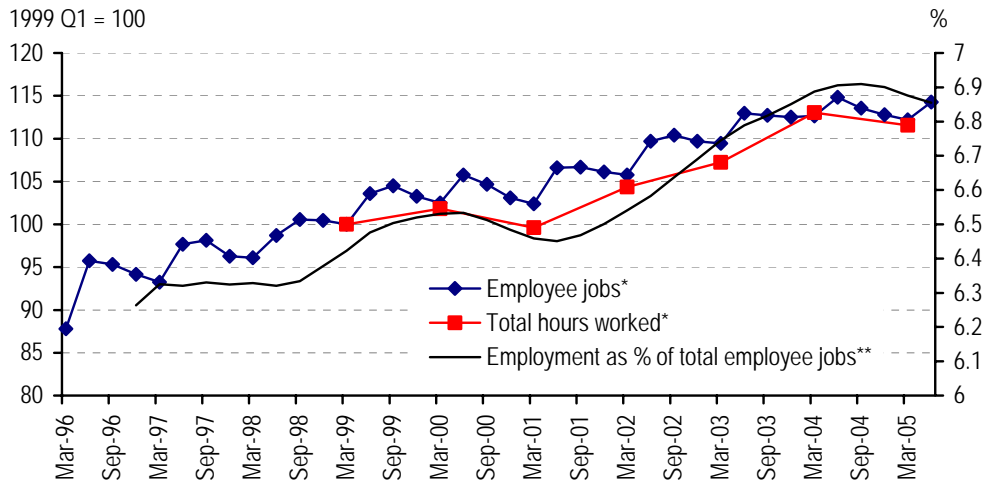
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ANNEX A

Employment data in low-paying industries

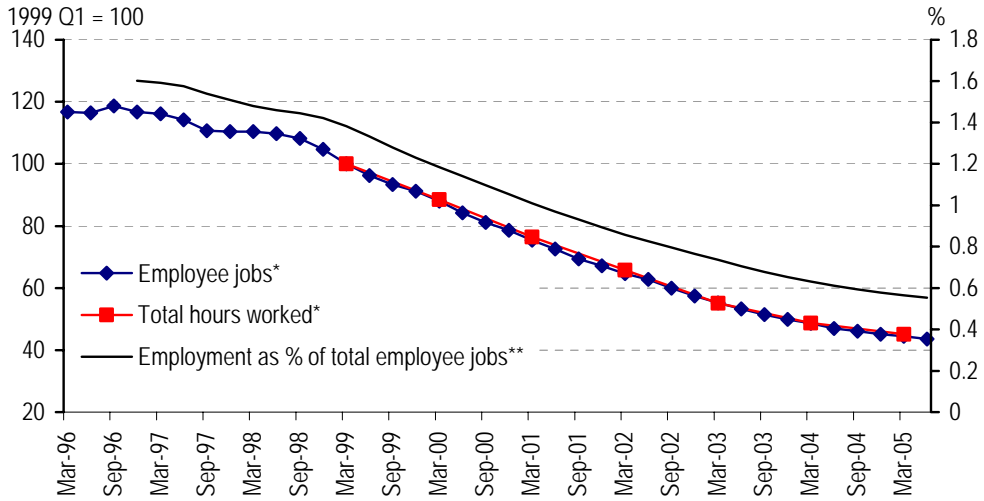
This Annex looks at trends in employee jobs in the following low-paying sectors in the UK economy: hotels and restaurants, textile and footwear manufacture, security, industrial cleaning, hairdressing, residential care and retail. These are the main low-paying sectors in the UK economy and are the sectors that successive Low Pay Commission reports have covered.

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



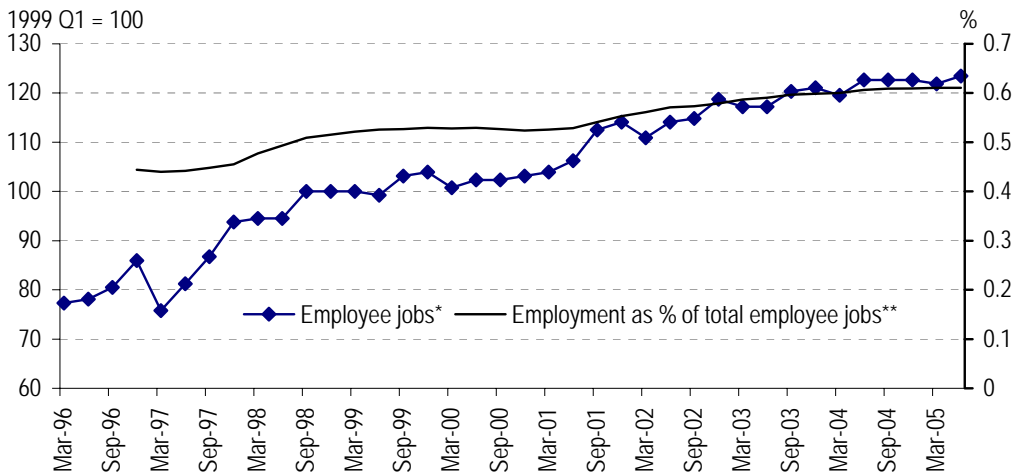
Source: DTI analysis of ONS' Employer Surveys; not seasonally adjusted. *1999 Q1 = 100. **four quarter moving averages. Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A2. Employee jobs and total hours in textiles and footwear manufacture



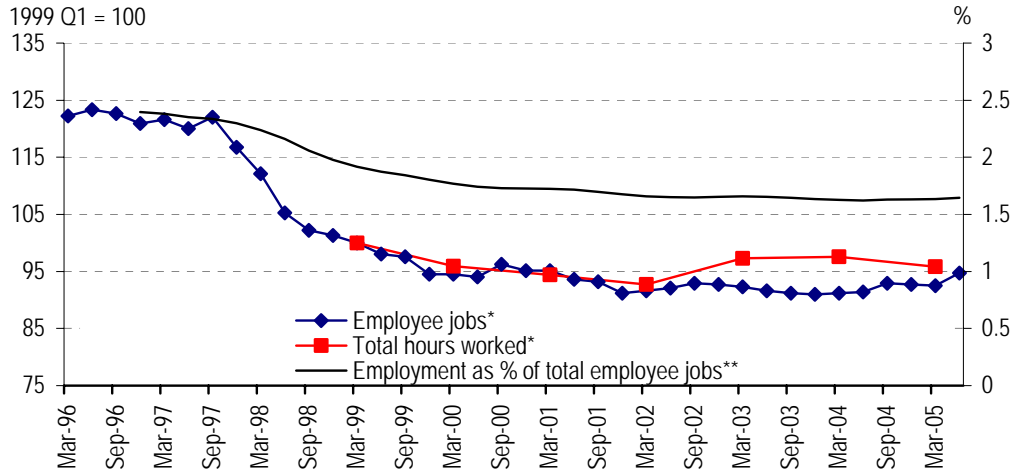
Source: DTI analysis of ONS' Employer Surveys; not seasonally adjusted. *1999 Q1 = 100. **four quarter moving averages. Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A3. Employee jobs in investigation and security activities



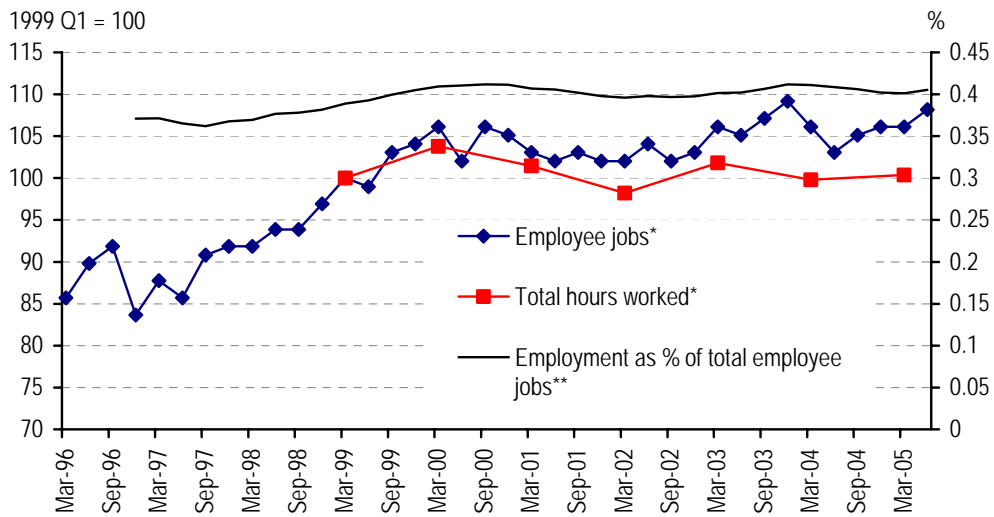
Source: DTI analysis of ONS' Employer Surveys; not seasonally adjusted. *1999 Q1 = 100. **four quarter moving averages. Total hours data not available.

Chart A4. Employee jobs and total hours in industrial cleaning



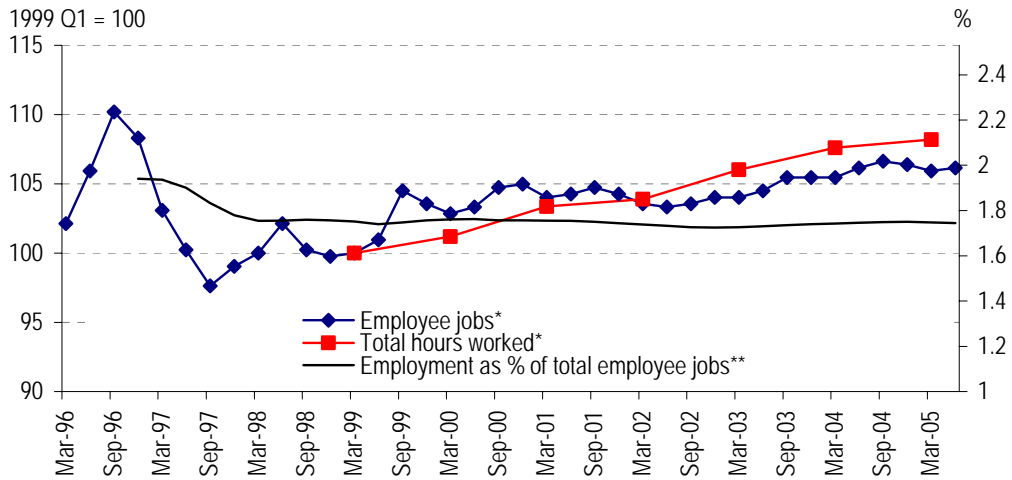
Source: DTI analysis of ONS' Employer Surveys; not seasonally adjusted. *1999 Q1 = 100. **four quarter moving averages. Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A5. Employee jobs and total hours in hairdressing



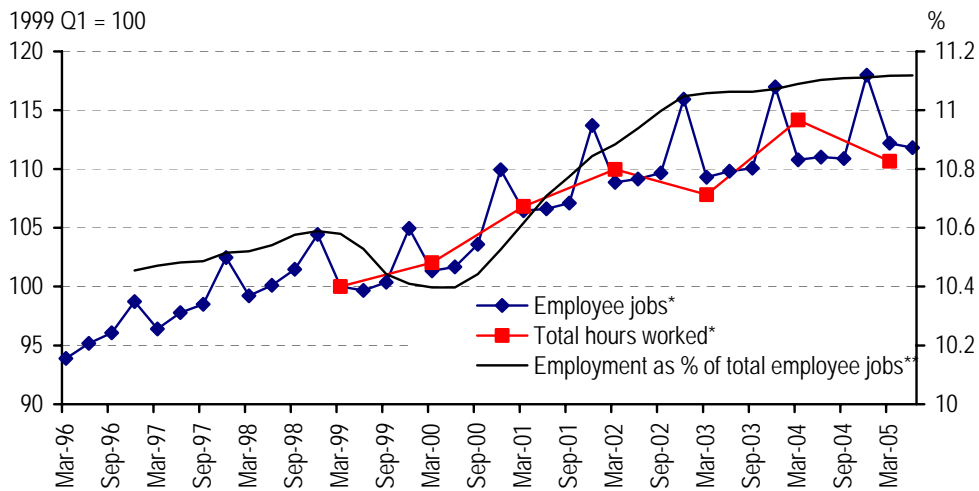
Source: DTI analysis of ONS' Employer Surveys; not seasonally adjusted. *1999 Q1 = 100. **four quarter moving averages. Total hours worked: employee jobs * mean weekly total hours from ASHE.

Chart A6. Employee jobs and total hours in residential social care



Source: DTI analysis of ONS' Employer Surveys; not seasonally adjusted. *1999 Q1 = 100. **four quarter moving averages. Total hours worked: employee jobs * mean weekly total hours from ASHE.

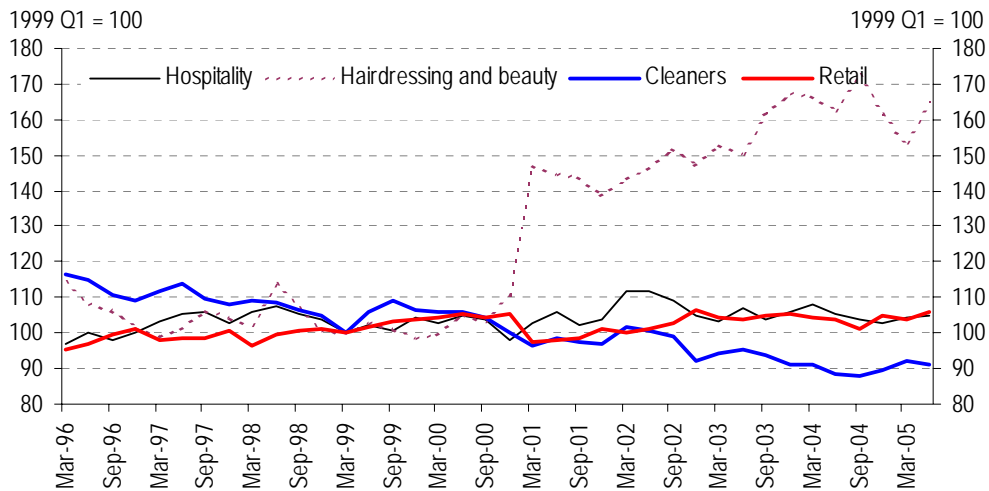
Chart A7. Employee jobs and total hours in retail



Source: DTI analysis of ONS' Employer Surveys; not seasonally adjusted. *1999 Q1 = 100. **four quarter moving averages. Total hours worked: employee jobs * mean weekly total hours from ASHE.

The Labour Force Survey (LFS) also provides data on employment in low-paying occupations. According to the LFS, employment in a selection of low-paying occupations as defined by the Standard Occupational Classifications (SOC) has increased in all but cleaning. This is consistent with employee jobs data. Chart A8 below shows an employment index of LFS occupations, Q1 1999 = 100.

Chart A8. Employment in low pay sectors, by SOC code*



Source: ONS, Labour Force Survey, Seasonal Quarters. * Standard Occupational Classification 2000 (in brackets): Retail - sales assistants (7111) and check out operators (7112). Hospitality - waiters/waitresses (9224), bar staff (9225), hotel porters (9222) kitchen and catering assistants (9223). Hairdressing and beauty- hairdressers and barbers (6221) and beauty (6222). Cleaners - Cleaners and domestics (9233). Before spring 2001, SOC 1990 classifications used. Consequently around 2001 there is a discontinuity in the data.

ANNEX B

Regional employment data in low-paying industries

Table B1. Employee jobs in the low-paying sectors by region (000's)

	North East	North West	Yorkshire & Humber	East Midlands	West Midlands	Eastern	London	South East	South West	Wales	Scotland	Great Britain	Y/Y*
Hairdressing													
1995	3	9	6	5	7	8	15	13	7	4	8	86	
1996	4	10	7	6	8	9	13	15	8	4	8	93	8.5
1997	4	9	7	6	8	8	13	15	8	4	8	88	-5.3
1998	5	10	7	5	8	8	14	14	8	4	9	90	2.2
1999	5	11	7	6	8	9	14	16	8	4	9	97	7.0
2000	4	11	7	6	9	9	14	16	8	5	9	97	0.5
2001	3	10	7	5	8	9	15	16	8	4	9	95	-2.7
2002	4	12	7	6	8	9	13	14	8	4	9	94	-0.3
2003	5	12	8	6	9	10	13	16	8	4	10	100	6.0
Retail													
1995	93	280	200	160	194	225	344	331	199	100	218	2344	
1996	97	288	199	158	200	230	347	349	209	104	220	2401	2.4
1997	97	286	200	163	204	246	356	357	213	107	222	2449	2.0
1998	105	317	228	178	225	257	351	383	235	120	230	2628	7.3
1999	110	325	214	167	223	242	382	391	239	114	229	2636	0.3
2000	110	331	235	183	232	269	378	416	253	121	233	2760	4.7
2001	105	337	240	187	244	276	382	428	258	129	252	2837	2.8
2002	116	348	250	190	243	286	378	443	266	132	261	2914	2.7
2003	112	351	257	204	245	298	373	438	278	140	257	2954	1.4
Hospitality													
1995	51	157	120	88	124	115	224	182	141	65	149	1417	
1996	57	166	128	89	125	116	224	198	143	65	153	1465	3.4
1997	59	178	130	91	115	121	249	202	146	67	150	1508	2.9
1998	60	188	133	99	130	126	245	208	149	70	156	1564	3.7
1999	66	182	129	100	134	126	273	224	143	77	151	1606	2.7
2000	59	183	128	100	129	135	265	232	149	67	165	1611	0.3
2001	60	187	126	103	134	139	278	225	160	75	170	1657	2.8
2002	63	202	129	105	136	137	288	242	163	69	168	1703	2.8
2003	64	208	130	106	134	144	301	247	175	73	169	1750	2.8
Investigation and security activities													
1995	4	12	8	5	10	7	26	13	7	3	9	103	
1996	4	14	9	9	9	6	27	13	6	3	11	112	8.7
1997	7	15	10	7	10	8	28	15	7	4	11	121	8.0
1998	5	16	13	8	9	7	31	17	7	4	10	128	5.9
1999	6	17	11	8	9	7	34	18	6	4	12	133	3.7
2000	6	17	10	7	8	9	33	17	6	4	13	132	-0.6
2001	7	18	9	8	9	9	38	17	8	5	15	143	8.3
2002	6	20	11	11	11	10	39	20	9	5	12	152	6.3
2003	7	20	11	10	11	12	40	18	9	5	13	155	2.1
Industrial cleaning													
1995	15	44	40	22	37	45	95	59	30	20	52	460	
1996	16	49	39	22	38	44	90	55	29	18	45	446	-3.1
1997	16	47	38	24	45	43	84	56	30	17	43	442	-0.8
1998	16	48	41	29	49	46	88	55	28	17	44	460	4.0
1999	13	44	38	23	40	41	88	61	25	16	40	429	-6.8
2000	11	42	39	22	39	44	93	57	27	16	45	435	1.5
2001	13	40	34	19	42	38	87	56	28	11	39	407	-6.5
2002	14	48	35	21	42	40	85	57	29	12	38	421	3.3
2003	13	50	34	15	41	38	81	61	30	12	37	413	-1.9
Social Work Activities**													
1998	41	108	77	62	78	79	119	121	90	47	72	893	
1999	43	118	82	60	83	77	115	127	86	48	81	921	3.0
2000	43	115	78	62	81	79	116	128	87	49	82	920	0.0
2001	46	120	85	66	82	91	118	137	92	52	85	975	5.9
2002	46	120	91	65	82	84	123	137	89	55	94	985	1.1
2003	48	120	92	75	86	83	116	139	89	56	100	1004	1.9

Source: 1995-1997 Annual Employment Survey Rescaled; 1998-2003 Annual Business Inquiry; ONS. *Y/Y shows percentage change of total regional employment from previous year. **Data for 1995-1997 not available.

ANNEX C

International comparison of minimum wage rates

Minimum wages of one form or another exist in 18 of the 30 OECD countries. In Europe there is a national statutory minimum wage in force in Belgium, France, Ireland, the Netherlands, Spain, the United Kingdom and several of the accession states.

Table C1. Current adult minimum wage rates

Country	NMW rate	Last updated	Notes/sources
Australia ^(a)	A\$484.40/wk	Jul-05	Based on statutory 38 hour week
Belgium ^(b)	€1234.20/mth	Aug-04	White collar Rate. Blue collar rate €7.5/hr based on 38hr wk
Canada ^(c)	C\$7.23	n.a.	Average of provincial rates
Czech Republic**	CZK7185/mth	Jan-05	Applicable in 2nd year employment, ages 22+
France**	€1217.88/mth	Jul-05	Based on statutory 35 hour week
Greece ^(d)	€591.18/mth	Sep-05	Unmarried white collar workers only. The terms of this wage order entitles a worker to 13 or 14 monthly payments per year
Hungary ^(e)	HUF57000/mth	Jan-05	
Ireland**	€7.65/hr	May-05	An employee who has any employment in any two years over the age of 18.
Japan ^(f)	Yen664/hr	2002	Weighted average of prefectural minimum wage rates.
Korea ^(g)	Won3100/hr	Sep-05	
Lithuania**	LTL550/mth	Jan-05	
Luxembourg**	€1467/mth	Jan-05	Unskilled workers only
Malta**	MTL241/mth	Jan-05	
Netherlands**	€1265/mth	2003	For employees 18 or over.
New Zealand ^(h)	NZ\$9.50/hr	Mar-05	For employees aged 18 or over
Poland**	PLN849/mth	Jul-05	Jul-05: NMW should increase by forecast inflation plus 2/3 GDP growth rate till reaches 50% of national average wage.
Portugal**	€374.70/mth	Jan-05	This particular wage order entitles a worker to 13 or 14 monthly payments pa.
Slovakia**	SKK6500/mth	Oct-04	
Slovenia**	SIT117500/mth	Aug-05	
Spain**	€599/mth	Jan-05	
United Kingdom ⁽ⁱ⁾	£5.05/hr	Oct-05	
United States ^(j)	\$5.15/hr	Sep-97	Minimum federal rate

Sources: **EUROSTAT (a) Australian Industrial Relations Commission; (b) FCO; (c) Statistics Canada; (d) FCO, Federation of European Employers; (e) FCO; (f) Ministry of Health Labour and Welfare; (g) Korean Labor Ministry (h) New Zealand Department of Labour; (i) DTI; (j) BLS.

Currently, Austria, Denmark, Finland, Germany, Italy and Sweden do not operate a minimum wage, with collective agreements as the main mechanism for regulating low pay for the majority of the working population. A statutory minimum wage is fixed at an hourly, weekly or monthly rate by the government, in most cases in consultation with the social partners. Adjustment may be on an ad-hoc basis, as in the US and Japan, or annually as in Belgium, France and Czech Republic.

Table C2. The national minimum wage 'bite' compared, 2005

Country	NMW rate	Median pay rate	NMW as % of median	Average wage	NMW as % of mean
Korea ^(a)	Won3100/hr	n.a	n.a	Won12160/hr	25.5%
Japan ^(b)	Yen664/hr	n.a	n.a	Yen2200/hr	30.2%
United States ^(c)	\$5.15/hr	\$15.8/hr	32.6%	\$16.18/hr	31.8%
Canada ^(d)	C\$7.23	n.a.	n.a.	C\$20.93	34.5%
Poland ^(e)	PLN849/mth	n.a	n.a	PLN2318.53	36.6%
Hungary ^(f)	HUF57000/mth	n.a	n.a	HUF151,406/mth	37.6%
Spain ^(g)	€599/mth	n.a	n.a	€1575/mth	38%
Czech Republic ^(h)	CZK7185/mth	n.a	n.a	CZK18673/mth	38.5%
Slovakia Republic ⁽ⁱ⁾	SKK6500/mth	n.a	n.a	SKK16,737/mth	38.8%
United Kingdom ^(j)	£5.05/hr	£10.0/hr	50.5%	£12.96/hr	39%
Portugal ^(k)	€374.70/mth	n.a.	n.a.	€906.37/mth	41.3%
Slovenia ^(l)	SIT117500/mth	n.a	n.a	SIT268066/mth	43.8%
Lithuania ^(m)	LTL550/mth	n.a	n.a	LTL1244/mth	44.2%
Greece ⁽ⁿ⁾	€591.18/mth	n.a.	n.a.	€1289/mth	45.9%
Australia ^(o)	A\$484.40/wk	A\$648/wk	74.7%	A\$1008.10/wk	48.1%
New Zealand ^(p)	NZ\$9.50/hr	NZ\$15.31	62.1%	NZ\$19.30/hr	49.2%
France ^(q)	€8.03/hr	€9.59/hr	83.7%	€15.7/hr	51.1%
Ireland ^(r)	€7.65/hr	n.a	n.a	€14.33/hr	53.4%
Malta ^(s)	MTL233/mth	n.a	n.a	MTL437.325/mth	55.3%
Netherlands ^(t)	€1265/mth	n.a	n.a	€2108/mth	60%

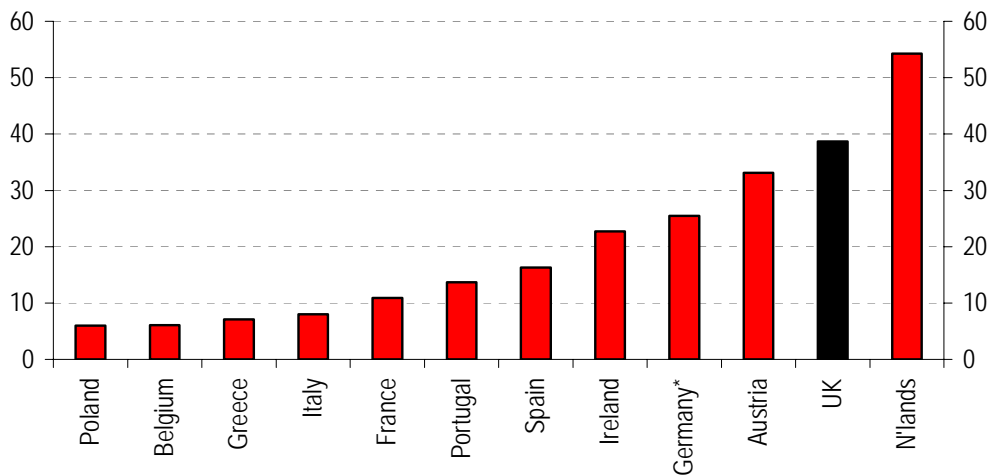
Notes/sources: (a) 2005 NMW and 2005 earnings data, Korea National Statistics Office, based on 49hr week; (b) 2005 NMW and earnings data for 2004, Statistical Handbook of Japan; (c) 2005 NMW and earnings data, BLS, based on 40 hour wk, median pay rate 2004; (d) 2005 NMW and earnings data, Statistics Canada; (e) 2005 NMW and 2005 earnings data, CSO - note that in July 2005 it was decided that the NMW should increase incrementally until it reaches 50% national average wage; (f) 2005 NMW and 2005 earnings data, CSO; (g) 2005 NMW and 2005 earnings data, INEbase; (h) 2005 NMW and 2004 earnings data, Czech Statistical Office 2005; (i) NMW and 2005 earnings data, Slovak Statistics Office; (j) 2005 NMW and earnings data, ASHE; (k) 2005 NMW and 2004 earnings data, EUROSTAT; (l) 2005 NMW and 2004 earnings data, EUROSTAT; (m) 2005 NMW and 2005 earnings data from CSO; (n) 2005 NMW and 2004 earnings data, EIRO; (o) 2005 NMW and earnings data, Australian Bureau of National Statistics, 2003 median pay rate; (p) 2005 NMW and 2005 earnings data, Statistics New Zealand, 2004 median pay rate; (q) 2005 NMW and 2003 earnings data, INSEE, based on 35 hour week; (r) 2005 NMW and 2005 earnings data, CSO; (s) 2005 NMW and 2004 earnings data, EUROSTAT; (t) 2005 NMW and 2003 earnings data, Statistics Netherlands, last NMW uprate 2003.

ANNEX D

European employment and unemployment rates

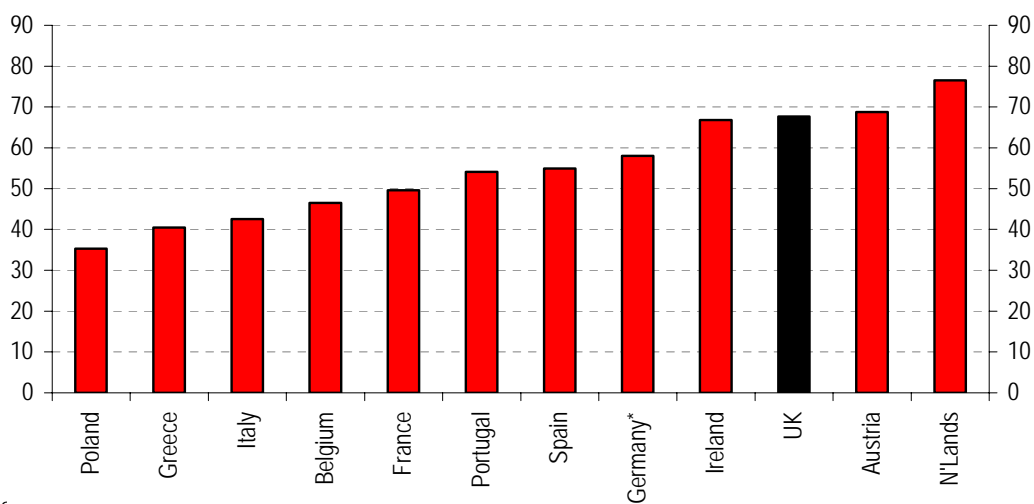
The data below compares UK unemployment and employment rates over several age groups with similar data for other European countries.

Chart D1. Employment rate 16-19 year olds, Q2 2005



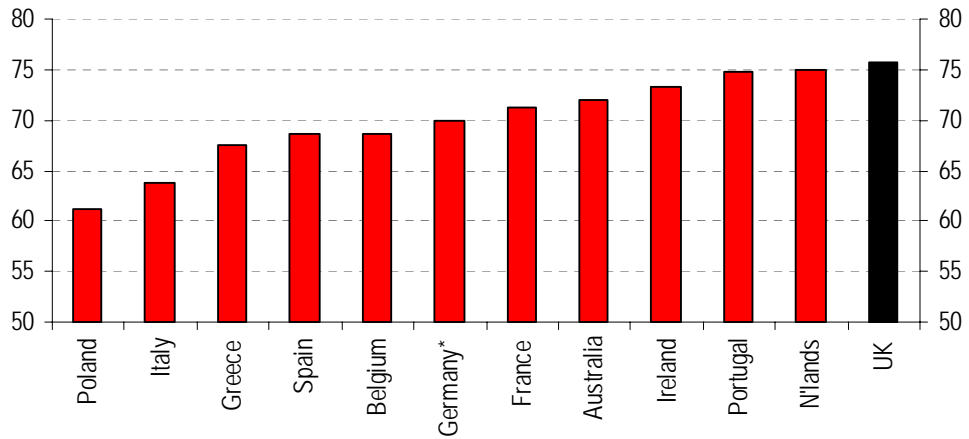
Source: Eurostat. *Germany rate for Q1 2005

Chart D2. Employment rate for 20-24 year olds, Q2 2005



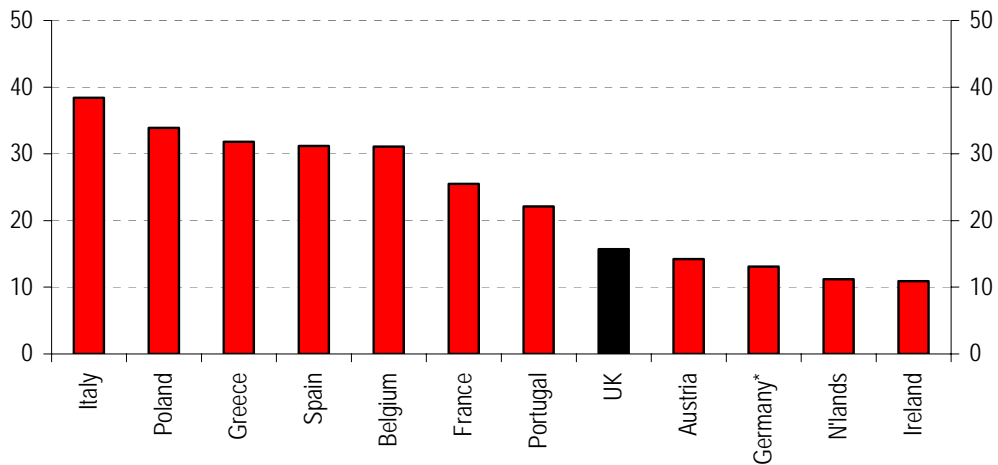
Source: Eurostat. Germany rate for Q1 2005

Chart D3. Employment rate for 25-64 year olds, Q2 2005



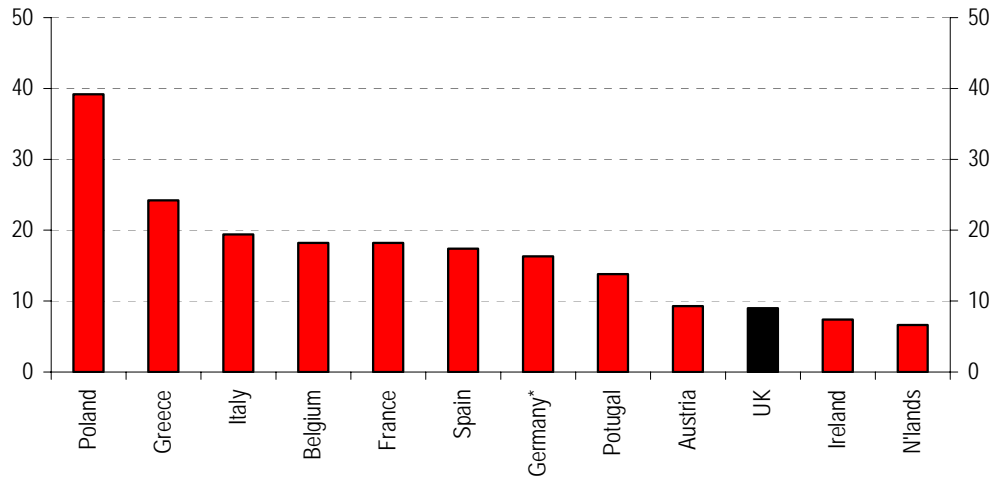
Source: Eurostat. *Germany rate for Q1 2005

Chart D4. Unemployment rate for 15-19 year olds, Q2 2005



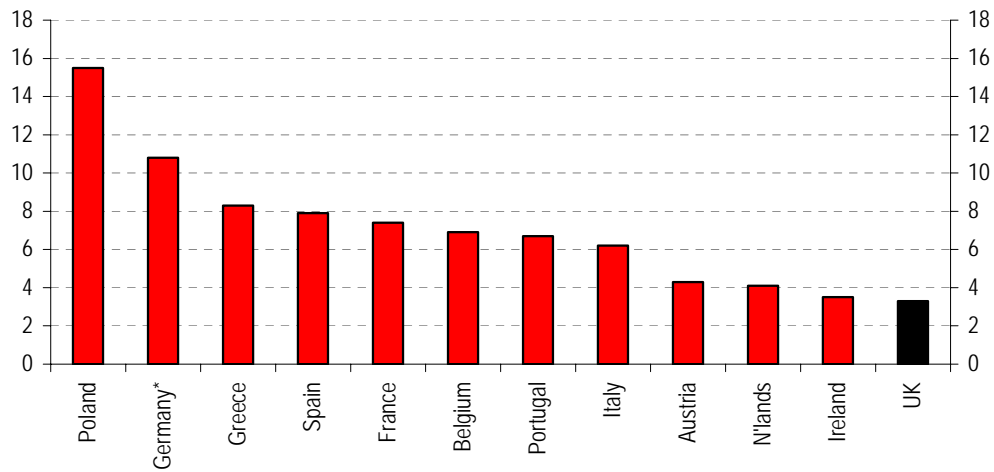
Source: Eurostat. *Germany rate for Q1 2005

Chart D5. Unemployment rate for 20-24 year olds, Q2 2005



Source: Eurostat. *Germany rate for Q1 2005

Chart D6. Unemployment rate for 25-64 year olds, Q2 2005



Source: Eurostat. *Germany rate for Q1 2005

ANNEX E

Review of recent minimum wage research

This short review considers recent academic contributions on the effects of minimum wages. In the UK much of the recent literature has been commissioned by the LPC. For completeness this overview considers this work, alongside other UK and international studies.

Employment effects

In the main the UK academic literature has not found significant evidence of negative employment consequences from the introduction and subsequent upratings of the adult national minimum wage. Stewart (2003) used individual-level longitudinal data to compare the employment experience of individual workers whose pay would have had to be increased to comply with the new minimum, with that of a similar group who were not directly affected. He found little evidence that the introduction of the National Minimum Wage had an adverse impact on the probability of subsequent employment of those affected. There was also little evidence that the 2000 and 2001 upratings had adverse employment consequences. Dickens and Draca (2005) considered the 2003 uprating, finding insignificant disemployment effects.

Some exceptions to the evidence include Galindo-Reuda and Pereira (2005) who, using a matched employer-employee data set, found some evidence that employment growth had been significantly lower in some exposed service sectors around the introduction of the minimum wage. They suggested that the minimum wage might have a slight disemployment effect that could have gone unnoticed (in absolute terms) when the level of the minimum wage was low and economic conditions benign. Machin and Wilson (2004), looking at employment in the UK care homes sector before and after the introduction of the National Minimum Wage, found some evidence of employment reductions, but were unable to detect any effect on home closure.

International evidence on the employment effects on adults also tends to point to these being limited. An OECD study (see Gregg 2000) confirms only small employment effects from increases in the minimum wage. Wolfson and Belman (2004) found that the increases in the US federal minimum wage between 1947 and 1997 raised average wages in many low-paid industries, but the effects on employment were typically mixed

and insignificant.⁸ Similarly, Lemos (2004) finds that minimum wage increases in Brazil have negligible effects on employment.

Effects on working hours

There is some evidence that the introduction of the national minimum wage in the UK may have led to a reduction of working hours. Stewart and Swaffield (2005) found that the introduction of the minimum wage led to a fall in the paid hours of both male and female low-wage workers. Their New Earnings Survey estimates indicated a reduction of between one and two basic hours per week. LFS estimated total effects on basic hours were greater for men and lower for women than the corresponding NES estimates. But no evidence was found of an impact of either the October 2000 or the October 2001 uprating on adult men.

Effects on the distribution of earnings

The academic evidence of the effects of minimum wages on the distribution of earnings tends, on balance, to suggest that there is little evidence for spillovers further up the earnings distribution. This is somewhat at odds with the empirical observation in the UK that the bottom quarter of the earnings distribution has experienced faster growth than the median since the introduction of the minimum wage. But clearly other factors could also have impacted on the distribution over this period, and it is a legitimate area for further research.

Dickens and Manning (2004) investigated the impact of the minimum wage on the distribution of wages in care homes. They concluded that there was virtually no evidence for spillovers from the National Minimum Wage. Metcalf (2004) also finds no evidence for spillovers, with workers in the bottom decile of pay experiencing above average pay rises between 1998 and 2002 and there being no effects further up the wage distribution. Similarly, in the US Neumark, Schweitzer and Wascher (2004) present evidence that increases in the minimum wage are felt by low wage individuals, while individuals higher up the wage distribution are little affected.

Young workers

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

In the UK it is probably too early to draw any firm conclusions on the introduction of the minimum wage for 16-17 year olds, although there are a number of recent studies. Frayne and Goodman (2005) estimated the impact of introducing a National Minimum Wage for 16 and 17 year olds on employment and education outcomes. They found that every 1

⁸ Neumark, Schweitzer and Wascher (2004) do however present evidence that the employment and hours of low-paid workers fall following increases in the minimum wage

per cent increase in the 16–17 year old wage resulted in a 3.6 per cent decrease in employment in hours amongst this group, implying that a minimum wage of £3.00 would reduce employment in hours by around 6 per cent. However, this was an upper bound and if firms are able to absorb even part of the costs of higher wages the effects will be far more moderate. Dickerson and Jones (2004) used the Youth Cohort Study to consider the labour market impact of a minimum wage on 16-17 year olds. They found that the largest single influence on the decision to remain in full-time education at 16 is GCSE attainment. Using GCSE attainment as the indicator of ability suggests that a minimum wage set between £2.50 and £4.00 will have negligible effects on education participation, irrespective of whether or not young people on government-supported training programmes are covered. And Neathey, Ritchie and Silverman (2005) found little evidence in the retail and hospitality sectors of a link between the minimum wage and decisions to employ young workers of various ages.

Several international studies have found evidence that minimum wages can have disemployment effects on the young. Campolieti, Fang and Gunderson compared transitions from employment to non-employment by youths in Canada over the period 1993-99. Using longitudinal data they found that minimum wage increases during the period of interest increased the transitions from employment to non-employment of employed low-wage youths by around 6 percentage points. These disemployment effects in turn implied 'minimum wage' elasticities of about -0.4 (ranging from -0.3 to -0.5). Wessels (2005) found significant negative effects on teenager labour force participation in the US. Looking at quarterly data from the US from 1979-2001 in all states, he found that increases in the national minimum wage had a negative effect on the labour force participation of 16-19 year olds.

Effects on firms

UK research into the impact of the minimum wage on firms has not found strong evidence for negative effects on firms. Machin, Draca and Van Reenen (2005) showed that although profitability fell in firms that were most affected by the introduction of the minimum wage, low wage firms were not forced out of business by the higher wage costs resulting from its introduction. They were also unable to detect evidence of higher wage costs being passed on in terms of higher prices. Forth and O'Mahony (2003) also found no evidence of the minimum wage leading to a general increase in unit labour costs over this period.

ANNEX F

Beneficiaries of the 2005 NMW uprating by sex and region

The DTI estimates that over 900,000 workers stood to benefit from the October 2005 uprating of the National Minimum Wage (NMW). This estimate is based on 1p pay bands from the ONS' Annual Survey of Hours and Earnings (ASHE) 2005, and takes account of average earnings growth and retail price inflation since Spring 2005. Of the estimated 910,000 workers who stood to benefit, 65 per cent were women.

Table F1. Number of workers that stood to benefit from the October 2005 National Minimum Wage uprating by age and sex

	Male	Female	Total
16-17	10,000	10,000	20,000
18-21	60,000	50,000	110,000
22 and over	240,000	540,000	780,000
Total	310,000	600,000	910,000

Source: DTI estimates based on ONS' Annual Survey of Hours and Earnings (ASHE) 2005

Note: These data are based on 1p pay bands from the ONS ASHE and take account of earnings and prices inflation between the period Spring 2005 and October 2005; uprating from £4.10 to £4.25 for 18- 21 year olds and from £4.85 to £5.05 for those 22 and over

Estimates of beneficiaries by country and region are also provided (Table F2).

Table F2. Number of workers that stood to benefit from the October 2005 National Minimum Wage uprating by country and government office region

Country or region	Beneficiaries	% of workers
Wales	50,000	3.8
Scotland	100,000	4.0
Northern Ireland	30,000	4.0
England	730,000	3.7
North-East	60,000	5.2
North-West	120,000	3.6
Yorkshire & Humber	90,000	3.9
East Midlands	70,000	3.5
West Midlands	100,000	3.9
Eastern	70,000	2.6
London	60,000	1.6
South East	80,000	2.0
South West	80,000	3.2
United Kingdom	910,000	3.1

Source: DTI estimates based on ONS' Annual Survey of Hours and Earnings (ASHE) 2005

Note: These data are based on 10p pay bands from the ONS ASHE and take account of earnings and prices inflation between the period Spring 2005 and October 2005; uprating from £4.10 to £4.25 for 18- 21 year olds and from £4.85 to £5.05 for those 22 and over. % of workers calculated using number in employment from October 2005 Labour Force Survey, ONS.

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