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The impact of the National Minimum Wage  
on pay setting since 1994

A report for the  
Low Pay Commission

from  
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This report has been prepared by Incomes Data Services (IDS) for the Low Pay Commission.

This report has been researched and written by:

Alastair Hatchett  
Laura James  
Anna Mayhew  
Ken Mulkearn  
Jack Robertson  
Anna Warberg  
Lois Wiggins  
Louisa Withers

Incomes Data Services  
Finsbury Tower  
103-105 Bunhill Row  
London  
EC1Y 8LZ

Telephone: 0845 077 2911  
Facsimile: 0845 310 5517  
E-mail: [ids@incomesdata.co.uk](mailto:ids@incomesdata.co.uk)  
Website: [www.incomesdata.co.uk](http://www.incomesdata.co.uk)

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## Overview

### **Part One - Pay settlements, minimum wage and recession**

IDS analysis of pay settlements over the last decade shows that pay settlements across the low-paying sectors have been broadly in line with those in the whole economy. Since the onset of recession there has been a significant increase in the level of pay freezes recorded but the proportion has been lower in low-paying sectors than in the economy as a whole. Pay rises in low-paying sectors and the whole economy continued to be made at similar levels in 2009 and 2010. Our findings show that pay settlement levels in the low-paying sectors, like those in the rest of the economy, are more likely to be influenced by RPI inflation and other economic factors, as opposed to being determined solely by the minimum wage increase.

The minimum wage has had an effect on the timing of pay reviews in low-paying sectors. Since 2000 the minimum wage has increased annually from 1 October. Before the introduction of the minimum wage, less than a tenth of low-paying pay settlements were effective from October. However, in 2009 around a fifth of low-paying sector pay settlements were effective from October. The minimum wage has also led to some employers adopting a two-stage approach to the minimum wage uplift in order to manage costs, with the main review taking place early in the financial year followed by a second review in October. This second review usually only applies to the lowest rates of pay or those directly affected by the rise in the minimum wage, and in certain cases to rates higher up the pay structure in order to preserve differentials. However, there have been fewer two-stage reviews more recently.

### **Part Two - Impact of the minimum wage on pay structures**

IDS analysis of the minimum wage's impact on pay structures identifies a number of key trends across four distinct time periods, during which employers made a series of adjustments to pay rates and pay structures as they adapted to the new legislation. Between 1993 and 1997, for example, employers made a number of changes to pay structures in anticipation of a minimum wage and also due to equal pay considerations, including increases to the lowest rates and introducing new grading structures. A number of structural changes were taking place in the economy throughout this period with the expansion of the retail sector and the growth of a part-time workforce, but also in terms of pay bargaining.

The second period, 1997 to 2000, immediately before and after the introduction of the National Minimum Wage, showed that a number of assumptions about its likely impact were unfounded. Most firms were able to accommodate the introduction of the minimum wage

without the need to restructure existing pay systems, due in part to the fact that most major changes had already been implemented in the earlier period.

In the period 2001 to 2006, a distinct shift in the general approach began to emerge, with employers in some sectors increasingly adopting the minimum wage as their lowest rate. This was partly in response to a series of relatively large uplifts in the minimum wage, although there were other factors at play. The extension of Sunday trading and longer opening hours in retailing also had an impact on employers' decisions to look again not only at basic rates of pay, but also at issues such as premium rates for evening, night and Sunday working.

Between 2007 and 2010 increases in the minimum wage were more modest. Many employers were able to adjust pay rates, moving away from paying the minimum wage and, particularly in retailing, restoring differentials for supervisory staff. In this period, other factors also had an impact on pay structures. For example, increased minimum statutory holiday entitlement led to changes in premium payments for bank holiday working.

### **Part Three - Time-series analyses of company pay rates**

The time-series analysis of company pay rates shows a relationship between minimum wage increases and the differential between the minimum wage and 'established' rates in low-paying sectors. In periods of modest upratings of the minimum wage, employers typically increased their established rate by more than the minimum wage increase – leading to a widening of differentials. During years when the minimum wage uplift has been higher, the gap between company pay rates and the national minimum wage has been squeezed. Overall, the differential between the minimum wage and established rates of pay in low-paying sectors has narrowed over time.

A similar pattern emerges when we examine the relationship between increases in the minimum wage and the gap between supervisor rates and established rates, although supervisor differentials have not narrowed by as much. However, the gap between supervisory pay rates and established rates has been maintained at around 7% to 8% since 2005, regardless of the movement in the minimum wage.

## Introduction

Since the introduction of the National Minimum Wage (NMW) in April 1999 the Low Pay Commission (LPC) has had an on-going remit to monitor and assess its impact, and advise Government on subsequent increases in the minimum wage and its application more generally.

### I. Scope of the research

This research has been commissioned by the LPC to examine the relationship between pay settlements and the minimum wage, including the impact of the recession in the most recent period, and the impact of the minimum wage on pay structures. The main objectives of the report are to:

- Test the hypothesis that increases in the minimum wage affect the distribution of pay settlements
- Test the hypothesis that organisations, particularly those in low-paying sectors, have moved settlement dates to match the implementation date of the minimum wage uplifts
- Monitor the effect of the recession on the distribution of pay settlements in both low-paying sectors and the wider economy
- Test the hypothesis that organisations, particularly in low-paying sectors, anticipated the introduction and subsequent uplifts in the National Minimum Wage
- Provide evidence around the introduction of, and subsequent increases in, the minimum wage and the impact on pay structures of individual firms in low-paying sectors
- Explore the relationship between the minimum wage and actual pay rates at the lower end of pay structures, specifically exploring the movement in the lowest rates of pay since the introduction of the NMW.

### II. Methodology

This report is primarily based on the examination of existing data held within IDS. These data cover named organisations in low-paying sectors as well as in other sectors of the economy. All data used in this report have been gathered by IDS researchers through semi-structured interviews, surveys and company visits with HR practitioners. The low-paying sectors covered by this report are retail, hospitality, hotels, children's nurseries and leisure. In preparing this report IDS has adopted a range of methodologies, as outlined below.

#### i. Pay settlements data

The pay settlements data used for this analysis are proprietary IDS data. The analysis is based on a total of 17,153 pay settlements with effective dates between 1 January 1994 and 31 December 2009, which includes a total of 3,414 pay settlements from organisations in low-

paying sectors. The analysis of pay settlements recorded so far for 2010 is based on 312 pay settlements, of which 67 are in low-paying sectors. This includes all pay settlements, as at July 2010, with effective dates between 1 January 2010 and 31 December 2010. A breakdown of the number of settlements IDS has recorded in each year is shown in table i.

Table i: Total number of pay settlements recorded by IDS (as at July 2010)

<b>Year</b>	<b>Total number of pay settlements</b>	<b>Of which are in low-paying sectors</b>
1994	1,118	125
1995	1,080	115
1996	1,224	143
1997	1,166	184
1998	1,169	235
1999	1,235	225
2000	1,126	215
2001	1,110	246
2002	1,000	234
2003	973	248
2004	1,022	279
2005	1,114	300
2006	1,069	286
2007	993	222
2008	884	182
2009	870	175
2010	312	67

#### ii. IDS methodology for recording pay settlements

The IDS methodology for recording pay settlements consists of recording the percentage increase to basic pay. Bonuses or lump-sum payments are not included in the aggregate data. For settlements where the percentage increase varies, IDS records a single figure which is either the average increase (where this is known), or alternatively, the increase received by most employees, or the paybill increase. The findings of the pay settlements analysis are presented in Part One of this report.

#### iii. Bespoke survey of employers

The analysis of any changes in the proportions of staff on the lowest rates combines existing data for the nursery sector (collected via a survey in April 2010) with results of a small bespoke survey of employers across the other low-paying sectors (conducted in June 2010). Employers were contacted via post, email and telephone. The analysis is based on a total sample of 50 employers. The findings of this analysis are presented in Part One of this report.

#### iv. Assessment of changes in pay structures

The narrative assessment of the changes to pay structures at organisations in low-paying sectors between 1994 and 2010 is based on existing data held by IDS. The sources of data are as follows: IDS Pay Report, historical records of company pay, IDSPay.co.uk and other internal editorial databases. The research also draws on previous IDS reports for the LPC. The findings of this analysis are presented in Part Two of this report.

#### v. Analysis of company pay rates

Archive information on company pay rates, as monitored by IDS, has been used to construct a time-series of 'differentials' for a number of organisations, mainly in low-paying sectors but also in financial services and the public sector. This analysis is based on the bottom of the main low-paid grade in 'national' locations i.e. the lowest-paid zone, outside the higher-paying areas of London and the South East. We refer to this grade as the 'established' rate and it varies by sector, as outlined in table ii. In the retail and nursery sectors, this is the established rate/nursery nurse rate since this is the main grade for the lowest-paid staff. In fast food, pubs and restaurants and housing and social care this is the lowest adult rate.

Table ii: Examples of the typical 'established' grade by sector

Sector	Typical 'established' grade
Children's nurseries	Nursery nurse
Fast food, pubs & restaurants	Team member after the probationary period
Financial services	Cashier/customer services advisor
Housing & social care	Unqualified social care assistant
Public sector	Administrative assistant/caretaker
Retail	Customer assistant after the probationary period

The sources of data for the company pay rates are as follows: IDSPay.co.uk, historical records of company pay structures and IDS journals. The list of organisations and the time series are shown in table iii. The findings are presented in Part Three of this report.

Table iii: Overview of time-series pay data for named organisations

Organisation	Time series
Low-paying sectors – fast food, pubs & restaurants	
Greggs	2001 to 2009
KFC	2001 to 2009
Marstons	1998 to 2009
McDonald's	1996 to 2009
Mitchells & Butlers	2000 to 2009
Pret A Manger	2003 to 2009

Table iii: Overview of time-series pay data for named organisations cont'd

<b>Organisation</b>	<b>Time series</b>
<b>Low-paying sectors – retail</b>	
Argos	1995 to 2009
Asda	1990 to 2009
B&Q	2002 to 2007
Blackwells	2004 to 2009
Boots The Chemist	1995 to 2009
C&J Clark	1999 to 2009
Homebase	2994 to 2009
House of Fraser	1998 to 2008
Iceland	2000 to 2007
Makro	1996 to 2009
Marks & Spencer	1997 to 2009
Next	1995 to 2009
Peacocks	2003 to 2009
Sainsbury's	1989 to 2009
Schuh	2003 to 2009
Selfridges	2003 to 2009
Somerfield	1990 to 2009
Tesco	1990 to 2009
Waitrose	2003 to 2009
Waterstone's	1995 to 2009
Wilkinson	1999 to 2009
<b>Private sector – financial services</b>	
Alliance & Leicester	1990 to 2009
Barclays Bank	1997 to 2009
Coventry Building Society	1996 to 2009
First Direct	1998 to 2009
Lloyds TSB	1998 to 2006
Nationwide	2005 to 2009
<b>Public sector</b>	
Foreign & Commonwealth Office	1998 to 2009
Highways Agency	1998 to 2009
Home Office	1998 to 2009
Local Government	1994 to 2009
Ministry of Defence	2002 to 2009
NHS	1993 to 2009
Scottish Prison Service	1998 to 2009

For comparison purposes, differentials between the established rates and the NMW have been calculated for each sector and an overall median for the low-paying sectors is based on the individual sector medians, except in 1999 when it is based solely on the retail differential. The figures used in this analysis for the housing and social care and nursery sectors differ slightly to those for the other low-paying sectors in that they are based on the median starting rate for the established role, as monitored by annual surveys conducted by IDS rather than being drawn from the time-series data. Survey samples vary each year, as shown in table iv.

Table iv: Number of organisations responding to the IDS housing and nursery surveys

Year of survey	Sample size	
	Housing and social care	Children's nurseries
2004/05	69	-
2005/06	123	100
2006/07	86	94
2007/08	56	82
2008/09	65	64
2009/10	74	39

In order to analyse the differential between established rates of pay and those further up the pay structure, IDS has compared established rates and supervisors' pay rates. The panel of supervisory pay rates is constructed of 17 organisations in the retail and fast food, pubs and restaurants sectors, as outlined in table v.

Table v: Organisations included in the panel of supervisory pay rates

Organisation		
Argos	Iceland	Pret A Manger
Asda	KFC	Schuh
B&Q	Marks & Spencer	Somerfield
C&J Clark	McDonald's	Waterstone's
Halfords	Mitchells & Butlers	Wilkinson
Homebase	Next	

## Part One - Pay settlements, minimum wage and recession

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This section of the report provides an in-depth analysis of pay settlements. The analysis is focussed on the period 1994 to 2010 and contrasts pay settlement trends in low-paying sectors with trends in the whole economy. More specifically the research explores:

- Pay settlement levels in low-paying sectors<sup>1</sup> against those in the whole economy, including any changes witnessed since the onset of the 2008 recession
- The distribution of pay settlements in low-paying sectors against those in the whole economy, including any changes witnessed since the onset of the 2008 recession
- The relationship between pay settlement levels in low-paying sectors and upratings of the National Minimum Wage, including any changes in the effective month of pay settlements.

### Key findings:

- Between 1994 and 2006 the median pay settlement in low-paying sectors was broadly in line with the median for the whole economy
- From January 2007 and January 2009 the median pay settlement in low-paying sectors was at around 0.5% behind the whole economy median
- Since the onset of recession, pay settlement levels in low-paying sectors and across the whole economy remained broadly similar. The annual median settlement level for both was 2% in 2009
- However, a lower proportion of pay freezes was monitored in low-paying sectors at 23%, compared to 31% of settlements in the whole economy
- The NMW uplift does not generally determine the overall median pay settlement in low-paying sectors, however it has had an impact on the effective date of pay reviews with around a fifth now effective in October
- There is little variation in median pay settlement levels across the low-paying sectors. However, an analysis of settlements weighted by employees shows slightly more divergence by sector, particularly in the retail sector
- An analysis of the proportions of staff on the lowest pay rates shows very little change over the last year, despite the recession.

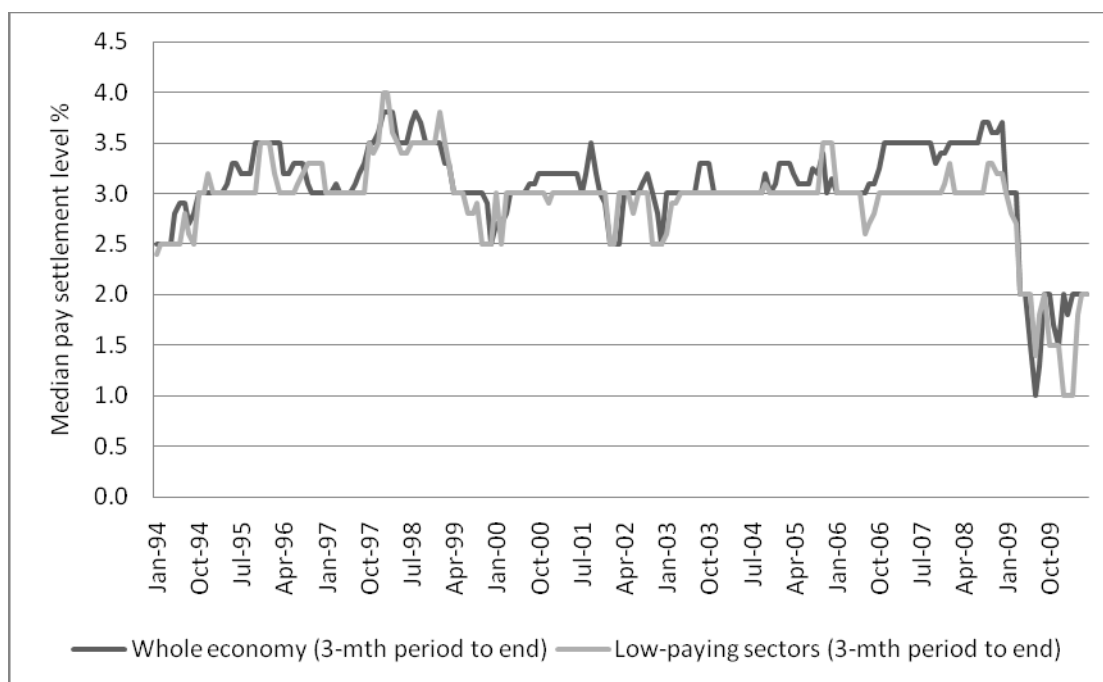
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<sup>1</sup> Low-paying sectors: care services & housing, fast food, pubs & restaurants, hotels, leisure, children's nurseries and retail.

### 1.1. Pay settlement levels between 1994 and 2010

Median pay settlement levels in low-paying sectors broadly followed those in the whole economy throughout the period 1994 to 2006, despite the introduction of the National Minimum Wage. Since the onset of recession in the second quarter of 2008, overall settlement levels have fallen and there has been an increase in the proportion of pay freezes in both low-paying sectors and the whole economy.

Chart 1.1: Median pay settlement levels in the whole economy and low-paying sectors



#### 1.1.1 1994 to 1997

In the period before the minimum wage was introduced, pay settlement levels in the whole economy and across the low-paying sectors were broadly aligned. For most of this period pay settlements were running at around 3% to 3.5%. This broadly reflected RPI inflation which was running at around 3% and was in line with average earnings growth, which ran at around 3.5% throughout the period.

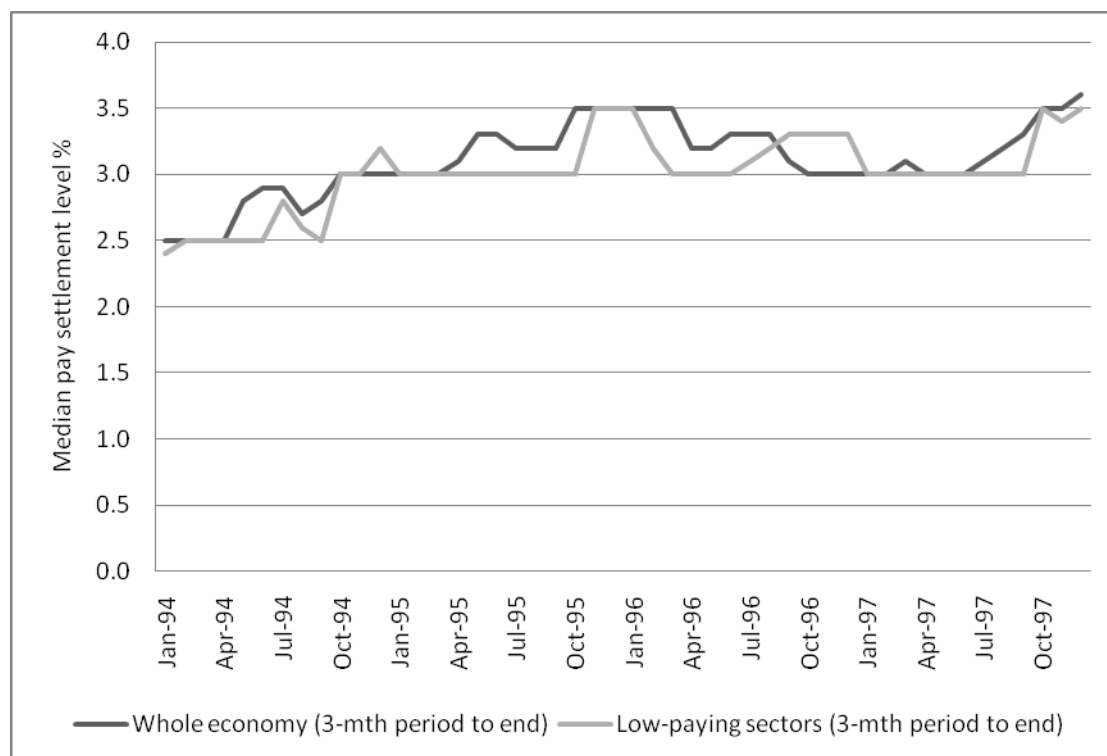
Table 1.1: Distribution of pay settlements between 1994 and 1997

	Proportion of pay settlements (%)											
	Pay freeze		0.1 to 1.9%		2.0 to 2.9%		3.0 to 3.9%		4.0 to 4.9%		+5.0%	
	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE
1994	1.6	3.3	6.4	7.2	49.6	48.3	33.6	30.4	6.4	8.2	2.4	2.5
1995	0.9	0.7	0.9	1.4	19.0	22.4	62.0	54.6	9.0	15.9	9.0	4.9
1996	3.5	1.6	2.8	0.9	18.9	15.8	58.7	59.2	10.5	17.6	5.6	5.0
1997	0.5	0.6	0.5	0.6	24.5	21.9	58.2	55.6	12.0	14.4	4.3	6.9

LP = low-paying sectors; WE = whole economy

A more detailed analysis focussed on the distribution of pay settlements also shows that, in the main, there was not much disparity between low-paying sectors and the wider economy. In 1994 the largest proportion of settlements fell in the 2% to 2.9% range in both the low-paying sectors and the wider economy. Similarly, between 1995 and 1997, the largest proportion of settlements in both the low-paying sectors and the whole economy were worth between 3% and 3.9%.

Chart 1.2: Median pay settlement levels between 1994 and 1997



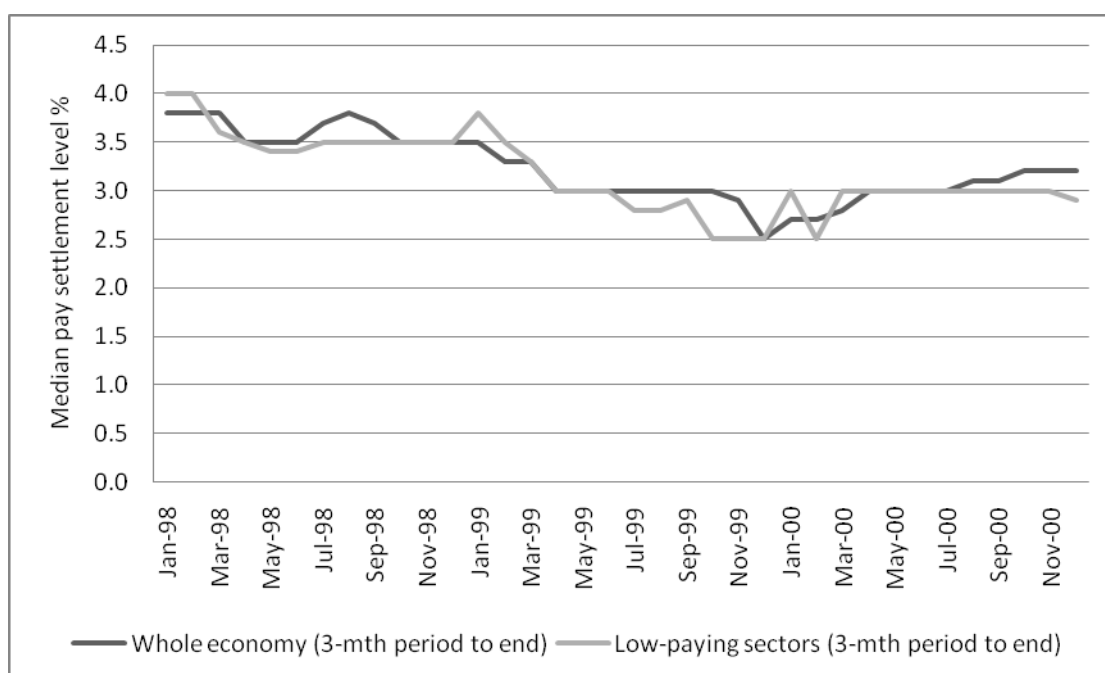
Between 1995 and 1997 there was an increase in the proportion of pay settlements in the 3% to 3.9% range across the whole economy. This proportion increased from around a third of pay settlements in 1994 to around three-fifths between 1995 and 1997. This trend was mirrored in low-paying sectors. Higher pay settlements in 1995 (in comparison to 1994) reflected higher rates of inflation and continuing economic recovery in this post-recessionary period.

### 1.1.2. 1998 to 2000

In the period immediately before and following the introduction of the National Minimum Wage there was little difference between the level of pay settlements across the whole economy and low-paying sectors. At the time when the minimum wage was introduced in April 1999, median pay settlement levels actually fell slightly both across the whole economy and the low-paying sectors. The median pay settlement level in the three months to the end

of March 1999 across the whole economy and the low-paying sectors was 3.3%. By the three months to the end of April 1999, the median in both had fallen slightly to 3%. This coincided with a fall in RPI inflation (from 2.4% in January 1999 to 1.6% in April 1999). RPI had been on a falling trend from a peak of 4.2% in May 1998. When the minimum wage was first updated in October 2000 (by 2.8%), median pay settlements remained at similar levels. In low-paying sectors, pay settlement levels were at 3%, while those across the whole economy were slightly ahead at 3.2%.

Chart 1.3: Median pay settlement levels between 1998 and 2000



In the period 1998 to 2000, the largest proportion of settlements in both low-paying sectors and the whole economy were in the 3% to 3.9% range. However, throughout the period the proportions fell from over half (64% and 53% respectively) in 1998, to just over two-fifths (43%) in both low-paying sectors and whole economy in 2000.

In this period there was also a marked increase in the level of pay settlements in the 2% to 2.9% range. In 1998, just 5% of low-paying sector settlements were between 2% and 2.9% but by 2000, pay settlements in this range were accounting for almost two-fifths of settlements (39%). The proportion for the whole economy increased from 7% to 31%. The proportion of higher-end settlements also declined in both low-paying sectors and whole economy.

Table 1.2: Distribution of pay settlements between 1998 and 2000

	Proportion of pay settlements (%)											
	Pay freeze		0.1 to 1.9%		2.0 to 2.9%		3.0 to 3.9%		4.0 to 4.9%		+5.0%	
	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE
1998	2.1	1.1	0.8	0.4	5.1	6.7	64.1	53.0	20.7	30.5	7.2	8.4
1999	1.3	2.3	2.2	2.8	29.5	23.8	47.6	48.5	11.5	15.7	7.8	7.0
2000	1.4	1.4	5.6	5.1	39.0	31.1	43.0	43.2	4.0	11.1	7.4	8.2

LP = low-paying sectors; WE = whole economy

### 1.1.3. 2001 to 2006

In the period of relatively large rises in the NMW between 2001 and 2006, pay settlement levels across the whole economy and low-paying sectors remained broadly similar. However, in both 2002 and 2006 a higher proportion of pay freezes were recorded across the whole economy than in low-paying sectors. In 2002, this coincided with a slight economic downturn and pay freezes in this year were mostly implemented at manufacturing companies. Similarly, in 2006, there was a moderate rise in the number of pay freezes and again, the majority were implemented in the manufacturing sector.

Median pay settlement levels in low-paying sectors remained below the uplifts in the NMW throughout this period. This is partly linked to the IDS methodology for recording company pay settlements<sup>2</sup>, but also to the fact that employers started adopting new approaches to pay setting. From 2003 onwards, IDS monitored evidence of retailers conducting two-stage pay reviews of the minimum rates in order to comply with the NMW. For example, retailers continued to conduct general pay reviews at the beginning of the year (typically April) and subsequently reviewed rates again in October, increasing minimum rates where necessary in order to comply with the uplift in the minimum wage.

Some employers also applied differentiated rises, with larger increases to those on the lowest rates rather than applying the same increase to all staff across the board. These approaches enabled employers to raise the pay of the lowest paid within a paybill 'envelope' of the main settlement and demonstrated that the relatively large increases in the minimum wage were having an effect on pay setting in low-paying sectors in this period.

<sup>2</sup> IDS records pay settlements as the percentage increase to basic pay, if this varies for different employees the average figure is recorded. If this is not known, the increase received by the most employees, or paybill increase, is recorded.

Chart 1.4: Median pay settlement levels between 2001 and 2006

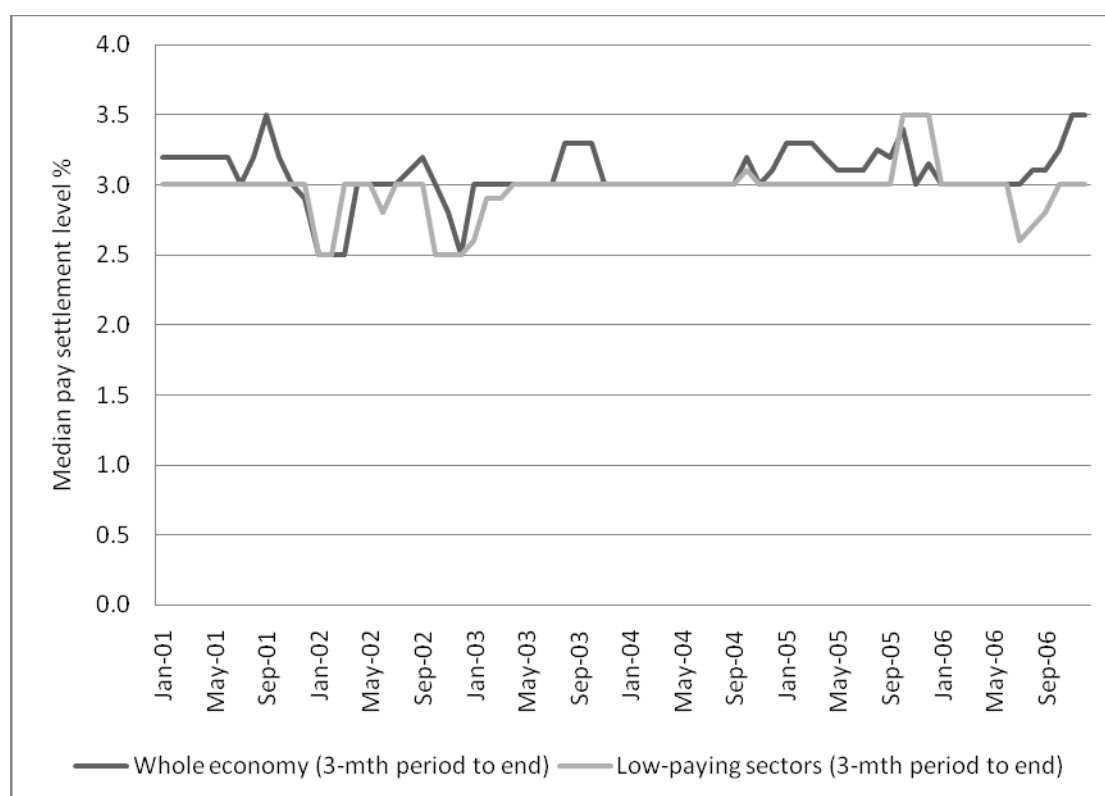


Table 1.3: Distribution of pay settlement between 2001 and 2006

	Proportion of pay settlements (%)											
	Pay freeze		0.1 to 1.9%		2.0 to 2.9%		3.0 to 3.9%		4.0 to 4.9%		+5.0%	
	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE
2001	2.0	3.1	2.0	1.5	30.5	22.6	45.9	51.1	8.1	11.2	11.4	10.5
2002	2.5	6.2	7.7	6.6	40.6	36.5	38.0	33.7	3.9	7.4	7.3	9.6
2003	0.8	2.5	2.0	2.2	31.9	27.5	50.0	49.7	7.3	9.6	8.0	8.5
2004	1.4	1.8	0.4	1.1	31.2	26.1	52.3	53.8	5.7	8.7	7.9	8.5
2005	1.3	1.1	1.0	0.9	26.0	17.7	51.9	59.0	13.7	13.5	6.4	7.9
2006	0.7	1.6	1.1	1.7	42.0	32.6	38.5	47.9	6.6	9.3	11.2	6.9

LP = low-paying sectors; WE = whole economy

#### 1.1.4. 2007 to 2010

From 2007 to the third quarter of 2008, pay settlements across the whole economy and low-paying sectors remained stable, although settlements in low-paying sectors were running around 0.5% behind those for the whole economy. However, from the beginning of 2009, pay settlement levels in both low-paying sectors and the whole economy fell as the recession took hold.

The median pay settlement for the whole economy fell from 3.7% in the three months to the end of December 2008, to 3% in the three months to January 2009. However, the median pay settlement in low-paying sectors did not fall quite as sharply, falling from 3.2% in

December 2008 to 3% in January 2009. An important point here is that although January is generally a busy time of year for pay setting; this is less true in low-paying sectors.

From January 2009 onwards, settlement levels in both the whole economy and low-paying sectors fluctuated. At the beginning of 2010, the period in which pay settlements across the whole economy started showing signs of recovery, pay settlements in low-paying sectors were running at around a percentage point behind those in the rest of the economy, only recovering in the three months to May. However the median settlement level disguises the range of increases that were being set in this relatively quiet time for pay bargaining in low-paying sectors. Pay settlements ranged from pay freezes to 5%, with the relatively higher increases being awarded at children's nurseries.

Chart 1.5: Median pay settlement levels between 2007 and 2010

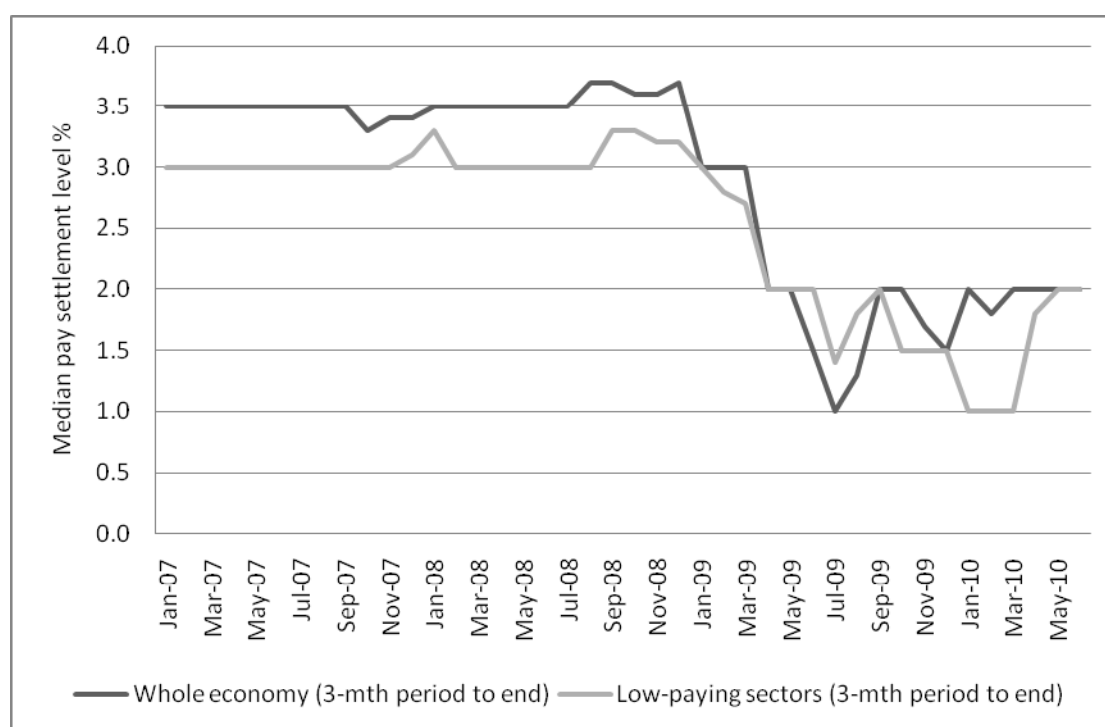


Table 1.4: Distribution of pay settlements between 2007 and 2010

	Proportion of pay settlements (%)											
	Pay freeze		0.1 to 1.9%		2.0 to 2.9%		3.0 to 3.9%		4.0 to 4.9%		+5.0%	
	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE	LP	WE
2007	0.5	0.7	1.4	1.8	23.4	17.0	55.4	47.6	11.3	23.5	8.2	9.4
2008	0.0	1.2	1.1	0.5	28.0	18.0	53.3	43.9	11.0	28.7	6.6	7.7
2009	23.7	30.6	20.3	14.8	35.0	23.5	15.3	20.7	2.8	7.1	2.8	3.2
2010	19.4	24.7	23.9	21.1	40.3	37.8	13.4	11.5	0.0	2.6	3.0	2.2

LP = low-paying sectors; WE = whole economy

## 1.2. Variations in pay settlements at sector level

A closer look at settlement levels within the individual low-paying sectors shows little variation from the all-low-paying sectors median pay settlement level (see table 1.5). The exceptions here are the nursery sector in 2005 and 2006, where pay settlements were marginally higher, and the retail sector in 2010, where the median pay settlement level is comparatively lower.

The variation in median settlement levels between the retail sector and other low-paying sectors in 2009 and 2010 is an indication of how different parts of the retail sector fared during the recession. The median settlement level for the whole retail sector stood at 1.5% in 2009. However, there were variations in the level of pay settlements within the different parts of the retail sector. The food retail sector remained relatively unaffected by the recession and this is reflected in the level of pay settlements recorded. Here, very few pay freezes were recorded and the median pay settlement level stood at 2.0%. Among non-food retailers, meanwhile, there was a wider spread of outcomes with pay settlements ranging from freezes to rises of 4% and the median at 1.2%.

Table 1.5: Median pay settlement levels by sector<sup>3</sup>

	Median pay settlement level (%)					
	Care services & housing	Hotels, restaurants, pubs & leisure	Children's nurseries	Retail	All low-paying sectors	Whole economy
1994	-	3.0	-	2.5	2.7	2.6
1995	3.3	3.1	-	3.0	3.0	3.1
1996	3.0	3.2	-	3.0	3.0	3.3
1997	2.8	3.0	-	3.0	3.0	3.2
1998	3.5	3.5	-	3.5	3.5	3.6
1999	3.0	3.0	-	3.0	3.0	3.0
2000	2.5	3.0	-	3.0	3.0	3.0
2001	3.3	3.0	-	3.0	3.0	3.2
2002	3.0	2.5	-	2.7	2.8	3.0
2003	3.0	3.0	-	3.0	3.0	3.0
2004	3.0	3.0	-	3.0	3.0	3.0
2005	3.0	3.0	4.0	3.0	3.0	3.2
2006	3.0	3.0	4.0	3.0	3.0	3.0
2007	3.0	3.0	3.0	3.0	3.0	3.5
2008	3.0	3.2	3.0	3.0	3.0	3.5
2009	2.0	2.3	3.0	1.9	2.0	2.0
2010	2.0	2.0	2.5	1.5	2.0	2.0
<b>Cumulative increase over the period 1994 to 2010 (%)</b>						
Total	46.4	49.8	-	48.1	49.0	51.2

<sup>3</sup> Cells marked '-' indicate no data available.

### 1.2.1. Employee-weighted analysis

The low-paying sectors are made up of a diverse mix of organisations, from large supermarkets to small owner-managed businesses. In order to gain an understanding of whether or not company size has an influence on pay settlements, IDS has conducted an employee-weighted analysis of settlement levels by sector (see table 1.6). Here pay settlements covering a large number of employees contribute more than other settlements, as opposed to all data points contributing equally.

In the main this analysis shows little difference between the unweighted mean pay settlement and that weighted by the number of employees covered. The exception is the weighted mean pay settlement in the retail sector which is slightly higher in the most recent period than the unweighted mean pay settlement – 2.1% compared to 1.5% in 2010 – suggesting that large employers have paid higher increases during the recession. In fact the largest employers (the supermarkets) continued to pay rises in 2009, while some smaller non-food retailers implemented pay freezes. The variations in mean pay settlement levels in the nursery and hospitality sectors reflect the sizes of organisations covered by IDS monitoring. The nursery sector typically includes smaller employers and the hospitality sector includes a range from large fast-food employers to smaller leisure employers.

Table 1.6: Mean pay settlement levels by sector, unweighted and weighted by employees

	<b>Mean unweighted pay settlement (weighted by employees) (%)</b>					
	Care services & housing	Hotels, restaurants, pubs & leisure	Children's nurseries	Retail	All low-paying sectors	Whole economy
1994	-	2.9 (2.7)	-	2.7 (2.6)	2.8 (2.6)	2.7 (2.8)
1995	3.1 (2.9)	3.3 (3.1)	-	3.0 (3.1)	3.1 (3.1)	3.3 (3.0)
1996	3.1 (3.1)	3.6 (3.9)	-	3.1 (3.3)	3.3 (3.4)	3.4 (3.3)
1997	3.0 (3.0)	3.8 (5.6)	-	3.2 (3.2)	3.3 (3.5)	3.4 (3.2)
1998	3.5 (3.3)	3.7 (4.9)	-	3.5 (3.6)	3.5 (3.9)	3.7 (3.5)
1999	3.2 (3.0)	3.6 (3.9)		3.2 (3.6)	3.3 (3.7)	3.3 (3.9)
2000	2.5 (2.6)	3.1 (3.1)	-	2.9 (2.7)	3.0 (2.8)	3.2 (3.3)
2001	3.2 (3.2)	3.9 (5.7)	-	3.1 (3.1)	3.4 (3.6)	3.4 (3.8)
2002	3.0 (2.8)	2.8 (2.7)	-	2.8 (2.9)	2.9 (2.9)	3.0 (3.8)
2003	3.1 (3.0)	3.6 (4.8)	-	3.1 (3.1)	3.3 (3.3)	3.3 (3.6)
2004	3.4 (3.0)	3.6 (4.5)	-	3.1 (3.5)	3.3 (3.6)	3.4 (3.6)
2005	3.0 (3.0)	3.0 (2.9)	4.4 (3.5)	3.1 (3.6)	3.2 (3.4)	3.5 (3.9)
2006	2.9 (2.9)	3.0 (3.5)	4.8 (4.3)	2.9 (3.2)	3.2 (3.2)	3.2 (3.1)
2007	3.0 (2.8)	3.1 (3.1)	3.8 (3.4)	3.3 (3.3)	3.3 (3.2)	3.6 (2.8)
2008	3.1 (3.0)	3.8 (3.2)	3.1 (3.2)	3.3 (3.5)	3.3 (3.5)	3.6 (3.4)
2009	2.0 (1.7)	2.0 (1.8)	3.1 (2.3)	1.6 (2.1)	1.8 (2.1)	1.9 (1.8)
2010	1.6 (1.8)	1.6 (2.0)	3.0 (2.7)	1.5 (2.1)	1.7 (2.1)	1.7 (2.0)

### 1.3. Pay settlements and the minimum wage

Table 1.7 shows annual median pay settlement levels across the whole economy and low-paying sectors, compared with increases in the NMW each year. The median pay settlement in low-paying sectors broadly mirrors the median for the whole economy, regardless of the size of increase in the minimum wage. For example, in 2004 the relatively large minimum wage increase of 7.8% did not lead to a significant increase low-paying sector pay settlements. The median was 3%, the same as in the whole economy.

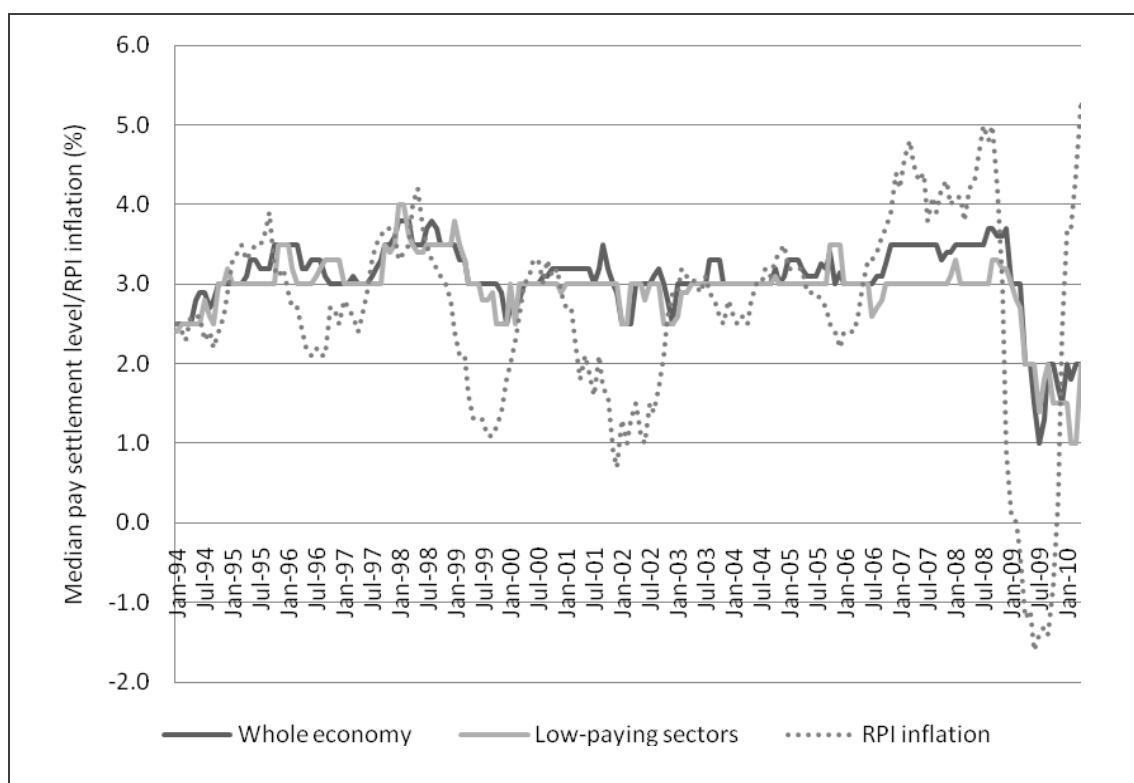
Table 1.7: Median pay settlement levels and headline increases in the minimum wage

	Median pay settlement (%)		Headline increase in the minimum wage (%)
	All low-paying sectors	Whole economy	
1994	2.7	2.6	–
1995	3.0	3.1	–
1996	3.0	3.3	–
1997	3.0	3.2	–
1998	3.5	3.6	–
1999	3.0	3.0	–
2000	3.0	3.0	2.8
2001	3.0	3.2	10.8
2002	2.8	3.0	2.4
2003	3.0	3.0	7.1
2004	3.0	3.0	7.8
2005	3.0	3.2	4.1
2006	3.0	3.0	5.9
2007	3.0	3.5	3.2
2008	3.0	3.5	3.8
2009	2.0	2.0	1.2
2010	2.0	2.0	2.2
<b>Cumulative increase over the period 1999 to 2010</b>			
Total	33.8	35.4	51.3

This indicates that pay settlement levels in low-paying sectors, like those in the rest of the economy, are more likely to be influenced by RPI inflation and other economic factors than be determined solely by the minimum wage increase. To illustrate this point further, chart 1.6 provides the level of RPI inflation tracked against median pay settlement levels for the period January 1994 to June 2010 and shows that the relationship between settlement levels and RPI is retrospective, with settlements broadly following the RPI.

The general decline in pay settlement levels in both the whole economy and low-paying sector witnessed in 1999 (when the minimum wage was introduced) coincided with low rates of RPI inflation (which had fallen from 2.4% in January 1999 to 1.6% in April 1999 and then fell further to 1.1% by September 1999). This provided a downward pressure on pay settlements.

Chart 1.6: Median pay settlement levels and RPI inflation



#### 1.4. October reviews

IDS monitoring of pay settlements shows that the minimum wage has had an impact on the timing of pay reviews across low-paying sectors. A number of organisations have moved their annual salary review to October, in order to align with the annual uprating of the minimum wage. As chart 1.7 shows, the proportion of settlements in low-paying sectors with effective dates in October increased from 7.2% in 1994 to a peak of 25.2% in 2006. In 2009, 19.4% of all pay reviews in low-paying sectors had effective dates in October, covering a third (36%) of the 1.6 million employees in low-paying sectors monitored by IDS that year. October is now a key month for pay setting across low-paying sectors, particularly retail.

Chart 1.7 also shows the proportion of low-paying sector pay reviews with effective dates in October declining more recently, due mainly to sampling variations. However, over the same period the proportion of reviews with effective dates in September has increased marginally from 4.1% in 2007 to 5.1% in 2009. IDS monitoring shows examples of employers moving review dates to October in the last few years, including Morrisons (2008), Halfords (2007) and Next (2010), and the trend in aligning pay reviews to the minimum wage upratings continues. Overall a significant proportion of pay reviews in low-paying sectors have effective dates that broadly align with the annual uprating of the minimum wage, whether at the end of September or between 1 and 31 October (as shown in chart 1.8).

Chart 1.7: Proportion of pay reviews in October

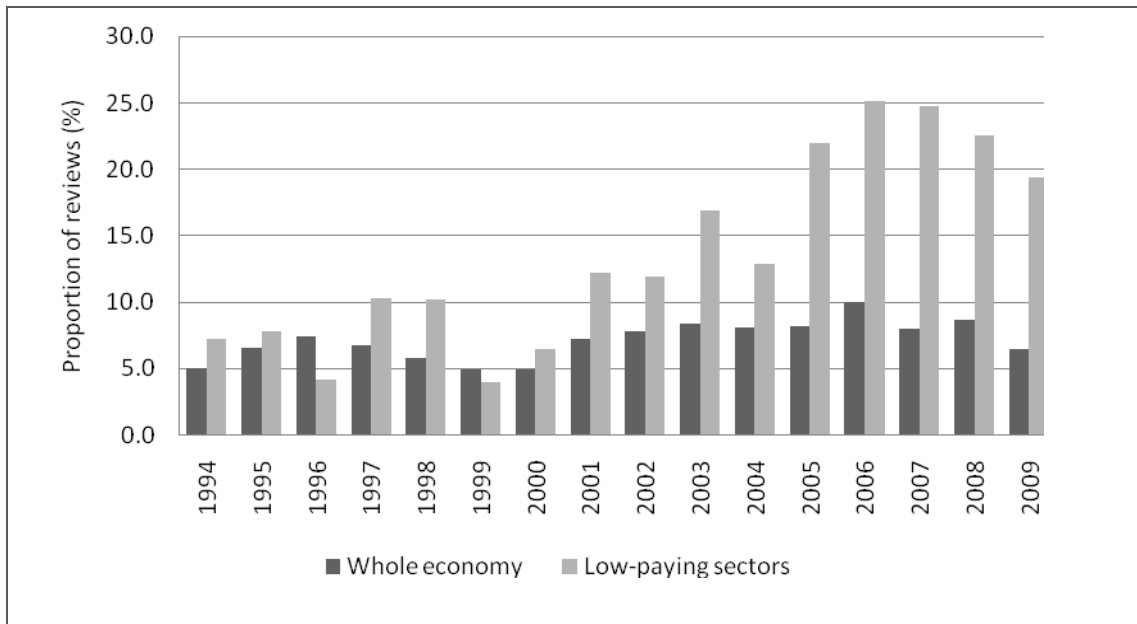
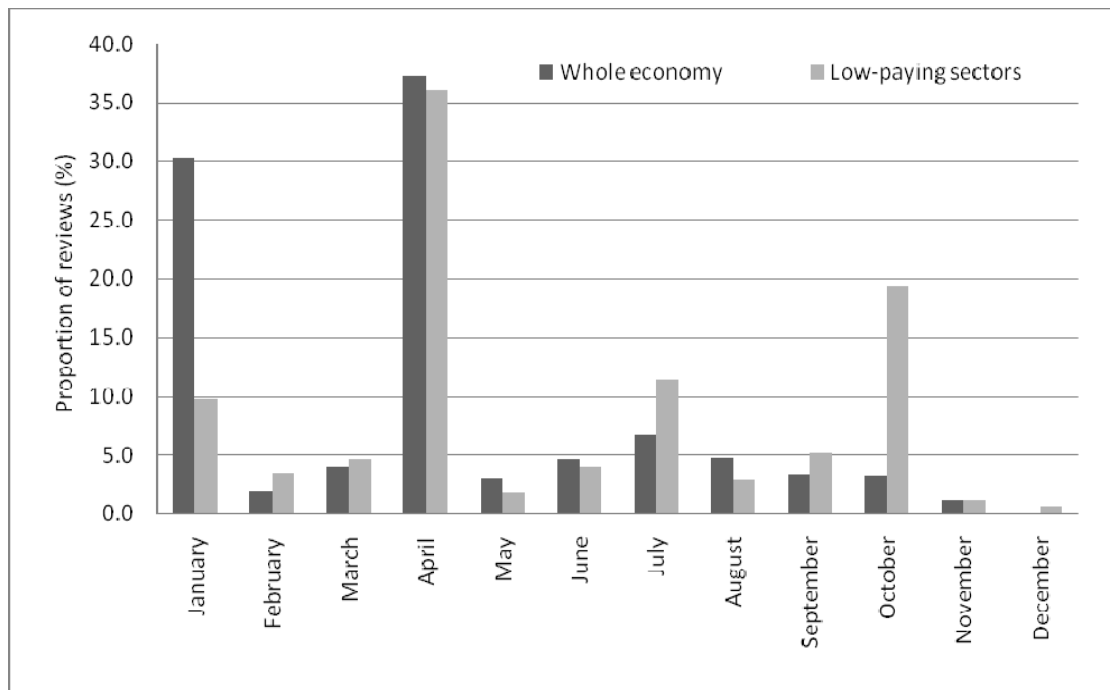


Chart 1.8: Distribution of pay reviews in 2009 by effective month



### 1.4.1. Two-stage approach

Aside from companies moving the month of the annual pay review, some companies in the low-paying sectors, particularly those in the retail sector, have adopted a two-stage approach to the annual salary review. Here organisations raise rates for all eligible employees following the usual annual salary review, typically in April, and then a further increase is applied to coincide with the uplift in the NMW in October. This second review

usually only applies to the lowest rates of pay or those directly affected by the rise in the minimum wage. In some cases rates higher up the pay structure are also increased in order to preserve differentials.

This two-stage approach first started being adopted in 2003, during a period of relatively large increases in the minimum wage. Prior to this employers with April pay reviews moved rates to or above the statutory level in April, rather than applying additional increases to those affected with effect from October. Employers were now waiting to increase rates to this level rather than paying it before they were legally required to. In 2007, IDS monitored a significant reduction in the number of two-stage reviews in the retail sector. This coincided with the month of October becoming increasingly popular for retail pay reviews and a lower increase in the NMW compared with the previous period (2001 to 2006).

#### 1.4.2. Differentiated rises

Aside from two-stage reviews, a number of companies (particularly in the retail sector) award differentiated rises depending on employee group or position in the pay structure. So, for instance, in the event of relatively high rises to the minimum wage, some retailers responded by applying higher increases to their lowest rates of pay – effectively ‘bottom-loading’ pay settlements – while applying a lower across-the-board increase to all other rates.

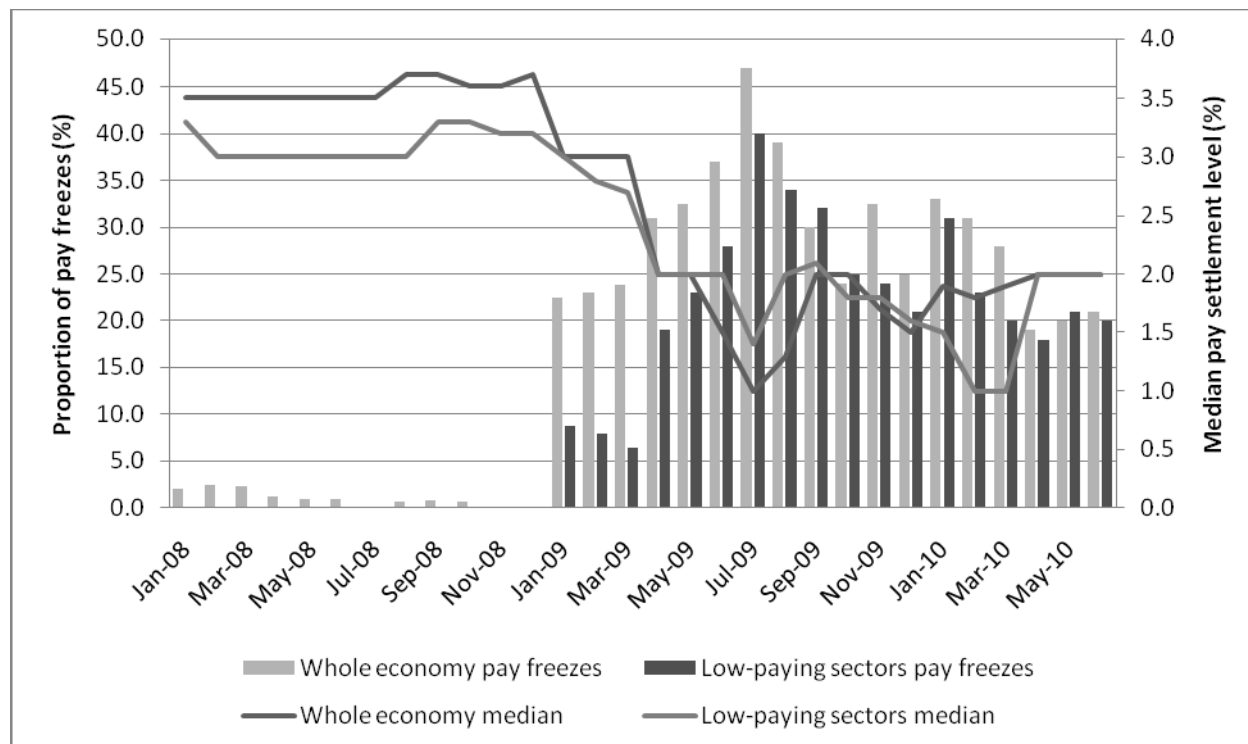
In 2008, around one-in-seven retailers applied higher increases to their lowest rates than to other pay rates. The majority of retailers applied increases of 3.8% (equal to the 2008 minimum wage increase) to their lowest rates of pay and, in some cases, their lowest pay zone. For example, Somerfield increased its lowest rate by 3.8% from September 2008 and applied a lower rise of 3.48% to supervisor rates (the second lowest rate). Other historic examples of retailers applying bottom-weighted increases include Blackwell’s. In 2006 the retailer increased basic pay by 2% but sales staff on the lowest grades received higher increases worth 5.9%.

Retailers also apply differentiated increases to other parts of the pay structure in order to restore differentials, for instance more senior staff including supervisor rates. This tends to be in periods when increases in the minimum wage are modest so that retailers can afford to make adjustments elsewhere in the pay structure, including actioning recruitment or retention strategies. Recent examples include the 2009 pay review at Next where pay rates for store-based staff were increased by 1% from February 2009 while pay rates for store managers were increased by 4% to bring them into line with ‘market rates’.

### 1.5. Impact of recession on settlements

Pay settlement levels in both low-paying sectors and the whole economy have fallen under the impact of recession. Chart 1.9 shows both the median pay settlement and proportion of pay freezes across the low-paying sectors and whole economy.

Chart 1.9: Median pay settlement and freezes as a proportion of all reviews



As chart 1.9 shows, pay settlement levels have fallen and the proportion of pay freezes has increased significantly, particularly from January 2009 – a key month in the pay bargaining calendar. In 2008, IDS recorded just 11 pay freezes across the whole economy (1%), however, by 2009, pay freezes accounted for almost a third of pay settlements (31%). Despite the rapid rise in the number of pay freezes recorded, the median settlement level did not fall to zero – its lowest level was 1% in the three months to July 2009 – since there was a clear split between pay freezes on the one hand and pay rises of around 2% on the other.

Pay settlements also fell in low-paying sectors although the proportion of pay freezes recorded was generally lower than the level recorded across the economy. No pay freezes were monitored in low-paying sectors in 2008. By 2009 pay freezes accounted for a quarter of settlements in low-paying sectors. Throughout 2009 and 2010, lower awards in general were made in low-paying sectors, compared to those set across the wider economy. Also for whole economy awards, while the proportion of pay freezes was relatively high, higher-level awards also continued. For instance in 2009, while almost a third of awards were for pay

freezes, the same proportion (31%) of pay settlements were at or above 3%. In low-paying sectors, just over a fifth of awards (21%) were at or above 3%.

In 2010, the period following the recession and essentially a period of fragile recovery for the economy, the proportion of pay freezes has declined. In low-paying sectors the proportion of pay freezes fell to just under a fifth (19%) of pay settlements, although there are distinct variations by sector (most notably housing and social care). The proportion of pay rises between 0.1% and 2.9% increased in low-paying sectors and the level of higher awards above 3% fell back. Similarly, across the wider economy in 2010, the proportion of pay freezes also fell, from just under a third of settlements to a quarter, and the number of awards in the 0.1% to 2.9% range also increased.

At sector level, the proportion of pay freezes in the housing and social care sector has increased in 2010 compared to 2009. This is driven by Government budget cuts. The slight increase in pay freezes in the hotels, restaurants, pubs and leisure sectors combined is mainly due to sampling variations and the picture may change as more 2010 pay settlements are monitored.

Table 1.8: Pay freezes as a proportion of pay reviews by sector

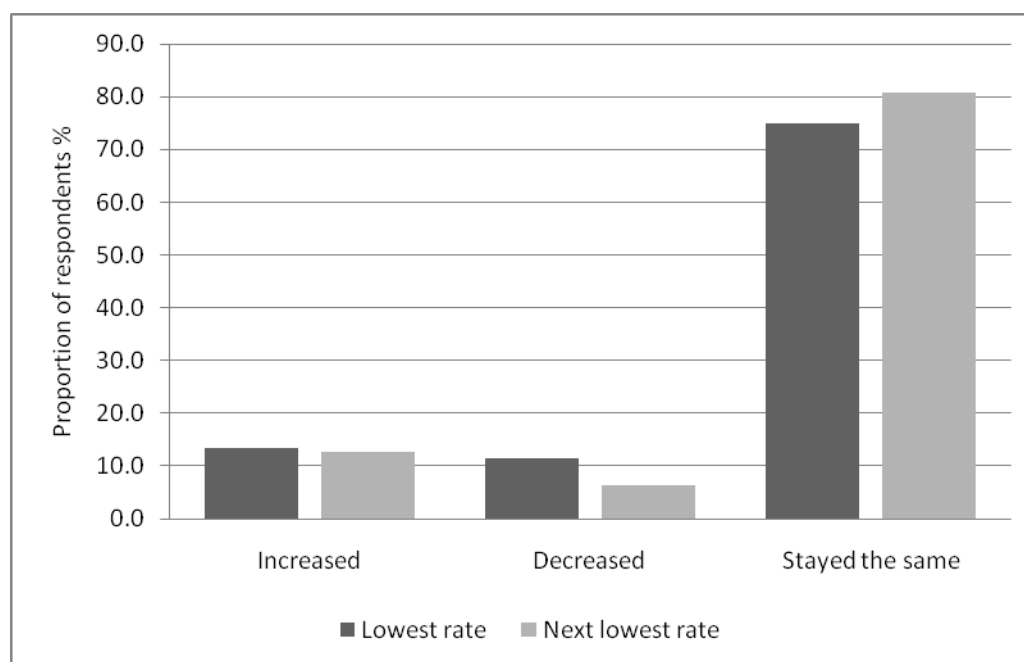
Year	Proportion of pay freezes (%)					
	Care services & housing	Children's nurseries	Hotels, restaurants, pubs & leisure	Retail	All low-paying sectors	Whole economy
2008	0.0	0.0	0.0	0.0	0.0	1.2
2009	23.5	20.0	11.1	24.6	23.7	30.6
2010	37.0	0.0	20.0	5.6	19.4	24.7

### 1.5.1. Recession and earnings

Analysis of the recession's impact on the proportions of staff on the lowest pay rates shows very little change. IDS conducted a survey of employers across low-paying sectors on any changes to the proportions of staff on the lowest and next lowest adult rates in June 2010. The aim of this research was to ascertain whether the recession had led to an increase in the proportion of staff on the lowest rates.

The overwhelming majority of employers said that the proportion had stayed the same, see chart 1.10. Overall 75% (39 of 52 organisations) reported no change in the proportion of staff on the lowest rate, and 81% (38 of 47) reported no change in the proportion of staff on the next lowest rate.

Chart 1.10: Changes in the proportions of staff on the lowest/next lowest rate in 2009/10



As shown in table 1.9, the median proportion of staff on the lowest rate of pay was 10%. The median proportion of staff on the next lowest rate was slightly larger at 12.5%. There were significant variations in both the proportions of staff on the lowest rates and the value at which these rates were set. For example, the proportion of staff on the lowest rate ranged from zero to 90%. This latter figure was at a nursery where the lowest rate of pay is currently £7.65 an hour.

Table 1.9: Lowest and next lowest rates of pay in 2009/10

	Lowest rate		Next lowest rate	
	Proportion (%)	Hourly rate (£)	Proportion (%)	Hourly rate (£)
Median	10.0	5.86	12.5	6.17
Mean	18.8	5.99	16.5	6.32

## Part Two – Impact of the minimum wage on pay structures

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This part of the report examines the impact of the minimum wage on company pay structures. It builds a picture of whether pay structures have changed over time, in order to assess how the minimum wage has affected the way firms shape their pay systems. The evidence is examined in four distinct time periods; 1994 to 1998; 1999 to 2000; 2001 to 2006; and 2007 to 2010. We provide a narrative assessment of how firms have adjusted their pay structures following the introduction of, and subsequent rises in, the minimum wage. We also will address a number of initial assumptions about how the minimum wage could affect pay and provide evidence of the real changes that have taken place.

### Key findings, 1993 to 1997:

- The economy emerges from the early 1990s economic recession
- Labour adopts a minimum wage policy in the 1980s and many firms raise minimum rates in part due to anticipation of a Labour win in the general election of 1992. In the event, the Conservatives were re-elected and held office to 1997
- Between 1992 and 1993 a Conservative government seeks to break up national bargaining through devolved bargaining in the Civil Service, moves to local bargaining in NHS Trusts and the abolition of Wages Councils
- Established in 1909, the Wages Councils were finally abolished in August 1993.
- Wages Councils had only modest regulatory impact and abolition does not produce shock waves. The rise of larger firms across the lower-paying sectors and the influence of their rates of pay is a counter balance to abolition
- Following the abolition of the Wages Councils, some minor industry agreements and the Agricultural Wages Board continue to set minimum rates
- Companies make changes to pay and grading structures in order to tackle low pay and the issue of equal pay for work of equal value.

### 2.1. Changes in the period 1993 to 1997

This section of the report looks at how pay structures changed between the end of 1993 when the Wages Councils were finally abolished and April 1999 when the minimum wage was introduced. The period 1993 to 1997 is sometimes referred to as the 'non-regulatory' period. However, this is perhaps overstating how effectively the Wages Councils had been performing as pay regulators. The scope of the Wages Councils had already been significantly reduced by the Wages Act of 1986 and there was mounting evidence that, far from being an unnecessary burden on business as the Government claimed, with few exceptions the Wages Councils had not effectively fulfilled their function of protecting low-

paid workers in the lowest-paying industries. It also overlooks the fact that some form of pay regulation continued to play an important role in many industries, including agriculture where the Agricultural Wages Board continued to exist, and that company-level bargaining had grown in importance not least due to influential pay deals at the increasingly large supermarket groups.

### 2.1.1. Abolition of the Wages Councils

In the years leading up to the introduction of a National Minimum Wage, a number of low-paying industries were still governed by the terms of the Wages Councils, the first of which had originally been established (as Trade Boards) in 1909. The Wages Councils were abolished by the Conservative government as part of the Trade Union Reform and Employment Rights Act of 1993, which consolidated many of that Government's earlier piecemeal changes to employment legislation as they related to industrial action and the conduct of ballots in trade union elections. The section on Wages Councils was among the first measures in the Act to come into force (on 30 August 1993) and it ended statutory minimum wages protection for around 2.5 million workers in industries such as retailing, hotels and catering, hairdressing, laundry and clothing manufacture.

Abolition of the Wages Councils was predominantly ideologically driven in that it was based on the belief that this form of regulation 'had no permanent place in the labour market', that it distorted labour markets and rates of pay, and that it had an 'inflationary effect' and reduced employment. The Government argued that wage determination was a matter which should be resolved between employer and employee, free from outside interference. Once Wages Councils were abolished, the Government argued, firms would be able to take advantage of the greater flexibility to employ more workers, at lower rates of pay. In the event however, by 1997 it was clear that abolition of the Wages Councils did not necessarily lead to lower nominal wages across low-paying sectors.

Immediately before their abolition, 26 Wages Councils were still in existence (including two which were 'in suspension'). Their main function was to set statutory minimum hourly rates of pay for workers in selected industries, with statutory minimum rates ranging from £2.66 to £3.20 an hour at abolition. Around 2.5 million workers were covered by the Wages Councils at this time, in industries where low pay was predominant. The vast majority of workers who came within the scope of the Wages Councils were women, many of whom worked part-time.

At their peak, in 1953, there had been 66 Wages Councils, but this number had steadily reduced, either because the industries had developed independent bargaining arrangements

– as in Road Haulage, for example – or as a result of the merger of Councils. By far the largest Wages Councils still in operation by 1993 were those covering Licensed Residential and Licensed Non-Residential Establishments and Retail Food and Non-Food. These four Wages Councils accounted for nearly 90% of the workforce governed by various Wages Council minimum rates.

### **2.1.2. Arguments over the Wages Councils**

At the time of their abolition, there was widespread opposition from trade unions, organisations such as the Low Pay Unit and from faith organisations, on the grounds that the Wages Councils' minimum rates afforded an important protection to low-paid workers. There was also opposition from some employers' organisations, mainly smaller ones, who argued that the establishment of minimum rates held wages at an acceptable level and also helped to prevent undercutting by more unscrupulous firms. However, it was also the case that the influence of Wages Councils over firms' pay structures was on the wane by this time, especially in sectors such as retailing.

Many employers – and particularly those in the larger firms such as supermarkets – backed abolition, partly because they regarded the rates set by the Wages Councils as being too low, not too high. When the last ever increase to the minimum rate under the Retail Food and Allied Trades Wages Council was implemented on 5 April 1993, for example, it took the minimum rate for 39 hours to £3.175 an hour, or £123.83 a week. But by this time the minimum rate at one of the largest supermarket chains, Sainsbury's, was already £10 a week a higher, at £3.42 on hour, or £133.38 a week. And at Tesco, the weekly rate was already nearly £16 higher, at £139.76 a week – an hourly rate of £3.83 for a basic 36.5 hour week.

That said, had the minimum rates applicable in the four largest Wages councils immediately before their abolition been uprated in line with RPI inflation, by April 1999 they would have been close to the £3.60 level of the NMW when first introduced.

### **2.1.3. Structural developments**

Aside from the abolition of the Wages Councils, there were also other structural developments which took place in a number of key low-paying sectors during this period which were arguably of as much long-term significance for the low-paid. Not least of these was a major expansion of the service sector and a total transformation of the retail sector. The rapid domination of the High Street by major multiples and the growth in out-of-town shopping which took place from the late 1980s onwards had enormous implications not only for the types of jobs which became available for low-paid workers but also for the

organisation of work, a transformation which was accompanied by a large increase in the participation of women, often working on a part-time basis.

In 1993 we reported: *'There has been considerable focus recently on the spread of part-time employment and the implications this has concerning pay and conditions. Whilst most major retail companies have always employed large numbers of part-time workers, more of them are now shifting the balance of the staff profile towards an even greater proportion of part-timers. The motivations behind this are reduced labour costs and the attainment of a more flexible workforce that can be adapted to suit changing business needs'* (IDS Report 643, June 1993).

#### 2.1.4. Anticipation of a minimum wage

The period prior to 1993 is complicated by employers' anticipation of a Labour victory in 1992. The party's manifesto had committed it to a national minimum wage and by the mid-1990s IDS monitoring picked up on firms already taking measures to enhance the rates paid to employees at the lower end of existing pay structures. In most cases, this had been done with the expectation that a national statutory minimum wage would be introduced if Labour were to win the 1997 General Election, as earlier in advance of the 1992 election. However, there were other contributing factors such as recruitment pressures and trade union/employee aspirations. In some cases, the lowest rates were either merged or abolished altogether. Elsewhere, the approach varied, from additional payments on the lowest rates, to across-the-board or guaranteed minimum increases, or consolidation of bonuses and allowances into basic rates. In a number of deals underpinning increases were agreed that favoured the lowest paid.

Changes to lowest rates were being made in an increasing number of company-level agreements by the late 1990s, with special provisions being made to tackle the issue of low pay, prior to the introduction of a National Minimum Wage. The issue of equal pay for work of equal value, stemming from the Equal Pay legislation amendment in 1984, was also a major factor in encouraging companies to revise their pay and grading structures.

In July 1991 IDS identified more than 120 pay deals which included special measures to address the issue of low pay. Two-thirds of these examples were from company deals, the remainder from public sector or industry-wide agreements. Most of the company examples were, not surprisingly, concentrated in a number of key sectors, where the introduction of a National Minimum Wage was likely to have most relevance. These included retailing and distribution, the textiles, clothing and footwear sectors, hotels and catering, food and drink manufacture and agriculture.

A breakdown of these agreements showed that, while a range of different approaches had been taken in order to raise pay levels for the lowest grades, some clear patterns had emerged. The main approaches fell under the following broad headings:

- Changes to grading structures, including the abolition or merger of grades
- Job evaluation and re-grading exercises (mainly driven by equal pay considerations)
- The payment of percentage increases to the lowest grades, above the level of any general award
- Raising the levels at which company or industry-level minimum rates were set
- The payment of flat-rate, across-the-board or guaranteed minimum increases.

Examples of these approaches in practice are shown in table 2.1; however, it is difficult to disentangle how much of the change was due to the minimum wage and how much was due to the equal pay legislation. Often, these changes boosted pay for women at the bottom end of pay structures, in line with earnings for male workers in better-paid areas such as warehousing.

Table 2.1: Historical examples of enhancements to rates at the lower end of pay structures

Organisation	Details
Halifax Building Society	Abolished age-related pay scales completely in 1990
Ramada Hotels	The 1991 pay review awarded rises of 7% for staff earning more than £8,000 a year, 8.5% for those earning less than this level
Safeway	A job evaluation exercise in April 1990 led to increases of between 6% to 25%, with larger increases for checkout operators and other grades dominated by female workers
TSB Bank	Rises of 8.3% underpinned by £550 minimum increase for staff on the bottom grade and £520 for other staff from April 1990
Tulip International	Minimum rate of £4 an hour introduced in September 1995

The IDS analysis showed that none of the firms which had removed the bottom grade(s) in a pay structure, whether for recruitment reasons, in anticipation of a minimum wage or under trade union pressure, had expressed undue concern in public about the cost of the exercise. We also found that the practice of re-grading and adding new weights to jobs had been common in that period as employers tackled the issue of equal pay, and as a consequence employees were used to certain groups receiving slightly different treatment in pay reviews. In particular, where pay levels at the lower end of structures had been improved, this had frequently been viewed with approval by colleagues rather than seen as a cause for dispute.

Furthermore, much had depended on the size of grade populations at the bottom of pay structures. In some cases these may have been numerous, as in retailing and catering, but in other sectors, very few people may have been at this level. In firms that had 'downsized', for

example, recruitment may well have been frozen, with the result that some lower grades in the pay structure were no longer occupied.

### **2.1.5. Campaigning in the public sector**

Across the public sector efforts were also being made to raise pay at the lowest end of pay structures. By the time the statutory minimum came into force in April 1999, most minimum rates in the public sector were already at least £4 an hour. The minimum rate in local government had moved to £4.47 an hour – the unions having secured a minimum hourly rate of £4 in 1997, which was then updated to £4.12 in 1998 and £4.47 in 1999. Pay deals in the mid to late-1990s in the civil service were characterised by guaranteed minimum rises, benefiting those in the lowest grades most. For example, the 1998 pay deal at the Benefits Agency included a guaranteed minimum rise of £600 to all staff earning less than £9,401 a year.

#### **Key findings, 1998 to 2000:**

- Labour wins the 1997 general election and immediately sets up the Low Pay Commission, with a timeline for the introduction of a minimum wage
- The National Minimum Wage is set at £3.60 from April 1999, not far from a revalorisation of the largest Wages Council rates in 1993
- Most firms appear to be comfortably able to adjust pay rates to the level of the minimum wage given that the most significant changes to pay structures had already taken place in the earlier period
- IDS research showed very few firms reporting serious difficulties adjusting to the National Minimum Wage
- IDS monitoring showed no negative employment effect and no negative effect on differentials for more senior staff, further up the pay structure.

### **2.2. Changes in the period 1998 to 2000**

Our examination of the second period from 1998 to 2000, looks at the way in which employers adjusted to the reality of the NMW, during the period immediately before and after its eventual introduction, in April 1999. At this stage, most firms seemed perfectly able to accommodate the statutory minimum and, if anything, appeared more concerned to keep their lowest rates above the NMW, partly to avoid the unwelcome reputation, as they saw it, of being tagged as ‘minimum wage payers’. This was particularly important during a period when a major expansion of the service sector was continuing apace and there was intense competition on the High Street and beyond for experienced and competent staff, especially in sectors such as retailing, fast food, hospitality and catering.

### 2.2.1. Rise of part-time workers

Throughout this period the shape of the workforce continued to change with a rapid rise in part-time working, particularly among women and student workers. In July 1997 student grants were abolished, and student fees were introduced. This led to an upsurge in the number of students in the labour market, as students took on part-time jobs to help manage these new costs. This, coupled with the continued increase in women's labour market participation and longer store opening hours, changed the balance between full- and part-time workers across the service industries. In evidence to the Education and Employment Committee in 1998, Sainsbury's reported: *'On average our supermarkets are open for 90 hours over seven days per week compared with 74 hours over six days in 1989. The business needs for a flexible, and therefore a predominately part-time workforce, have thus increased. [This means] all our employees are effectively part-time'*.

Table 2.2: Breakdown of Sainsbury's workforce by age and gender in 1998

	Proportion of employees (%)	
	Part time	Full time
All employees		
Women	51.9	12.9
Men	16.9	18.3
Breakdown of employees by age		
Age 16 to 24 - Women	12.6	2.6
Age 16 to 24 - Men	13.2	4.4
Age 25 to 64 - Women	38.8	10.2
Age 25 to 64 - Men	3.3	13.8

### 2.2.2. Assumptions about the minimum wage

A number of common assumptions about the minimum wage turned out to be misguided. The most important example was the number of forecasts predicting dire consequences for jobs. Not only has there been no discernable negative impact on jobs, nor has there been any substantial evidence of the much-vaunted impact on pay differentials.

As we noted at the time, this was remarkable, given the then Employment Minister's (Michael Howard) forecast that the introduction of a minimum wage at the rate of £3.50 an hour would lead to 800,000 job losses and that this figure could rise to 1.5 or even 2 million if pay differentials were restored in full. However, throughout the period 1993 to 1999 pay settlements and average earnings were running at around one to two percentage points ahead of inflation but employment grew by around 3 million. Around the time of the minimum wage's introduction the service sectors continued to expand and a number of firms in the hospitality and retail sectors announced plans for expansion. For example, at the end of 1998 McDonald's announced that it would be opening 100 new restaurants in 1999,

creating a further 5,000 jobs. Similarly, B&Q announced 10 new stores, Pizza Express 40 new restaurants and Burger King 100 new restaurants with a total of around 11,000 new jobs.

The other main argument was that higher-paid employees would seek to restore their differentials. It was believed that if you raised the lowest rates of pay by a percentage more than other staff further up the pay structure, these higher-paid staff would seek to restore their position relative to the lowest paid. IDS monitoring showed many examples of lower-paid employees, in one way or another, gaining higher awards than higher-paid colleagues. These moves did not result in calls for restoration of rates further up the pay structure, partly because they were aimed at tackling equal pay for work of equal value as well as low pay.

Table 2.3: Examples of employer responses on the impact of the minimum wage in 1999

<b>Organisation</b>	<b>Employees paid below NMW level prior to April</b>	<b>Measures taken in anticipation of the NMW</b>	<b>How important is the NMW to your business?</b>
Anchor Trust	1%	Over the last two years we have systematically raised pay for those at the bottom end of the pay scale	Of minor importance
Gleneagles Hotel	0	Introduced a minimum rate of £4 an hour in 1998	Of minor importance
Manchester Care	0	Increased lowest rate to above the anticipated NMW	Fairly important
Warner Village Cinemas	-	Minimum rate outside London & South to be raised from £3.20 to £3.60 from April 1999	Fairly important

### 2.2.3. Impact of the minimum wage

In 1997 Labour won the general election and began to take action on its flagship election policy of establishing a minimum wage. The Low Pay Commission was established and the national minimum wage of £3.60 an hour for adult workers was set for 1 April 1999. The minimum wage was initially estimated to cover around 1.9 million employees, a majority of whom were women. The minimum wage was always intended to have most impact in areas where 'rigid' pay structures were less well established. Generally speaking these tended to be the expanded services industries, with low levels of union membership and where a higher degree of managerial discretion might already be in operation. During this period, larger companies were able to comfortably accommodate the minimum rate of £3.60 an hour, in part because many had revised their pay structures in the previous period.

IDS monitoring showed a prolonged process of adjustments in small steps rather than employers waiting until 31 March 1999 and that the process had been relatively smooth –

although there were of course some exceptions. In March 1999 IDS surveyed employers across the hotels and leisure, agriculture and food processing, textiles, clothing and footwear and voluntary sectors and found that most firms (66%) thought the NMW of minor or no importance compared to other factors affecting their businesses. In a number of cases adjustments needed to comply with the minimum wage had already been made in advance of the legislation coming into force. Furthermore a number of firms had not needed to make any adjustments as they were already paying well above the NMW levels.

#### **2.2.4. Marginal impact on differentials**

The impact on 'differentials' was also not as significant as had been predicted. There was remarkably little evidence to indicate that employees higher up the pay hierarchy were demanding restitution of their rates. Neither had any major union adopted a call for restoration of differentials as a policy initiative. However, a key factor was that the industries most likely to have been affected by disputes over parity and differentials in the past – such as construction, shipbuilding and other parts of engineering – were also the least likely to have been affected by the NMW. This was mainly because their minimum rates were already well above £3.60 an hour, but also because changes which had taken place over the previous two decades meant that strict pay differentials were no longer so prevalent.

Furthermore pay structures in the newer and rapidly expanding services sectors, such as fast food and restaurants, were generally flatter with a large number of staff on one or two grades since this structure was considered to work better given the high incidence of team-working. These structures were thought to be more transparent and not hampered by a tangle of different pay rates.

As part of IDS monitoring of bargaining developments over this period, particular attention was paid to any instance where pay differentials had been mentioned as an issue but found that examples remained few and far between. This not only reinforced the conviction that forecasts of the impact of the NMW on differentials were exaggerated, it also raised the equally intriguing question of why pay structures were so able to withstand the oft-predicted after-effects. The most obvious explanation was that the NMW was initially set at a modest level, quite deliberately. The Annual Report of the Knitting Industries Federation described it as 'well below our industry's worst fears'.

The second was that, though calls for restoration of differentials by other workers were widely predicted and anticipated, none had materialised. No major trade union adopted 'restoration of differentials' as an immediate priority for their own members. On the contrary,

most reports suggested that older workers and other employees on higher rates regarded the introduction of a minimum wage as an overdue safeguard for the lower paid.

It was also the case that, in a number of key industries and companies, pay structures had changed in the previous years and to such an extent those preconceptions of what pay structures looked like could often be quite wide of the mark. For example, the industry with arguably the most controversial history with regard to pay differentials had been engineering. For a period, during the 1960s and 1970s, parts of the sector had gained a reputation for near-continual parity disputes – notably in cars, engineering construction and shipbuilding. But most of these disputes took place at a time when pieceworking was still prevalent in the industry, when the three main categories of skilled, semi-skilled and unskilled labour were rigidly applied and when these fixed relationships were enshrined in the National Engineering Agreement.

In those days, rates of pay for semi-skilled, unskilled and women workers had conventionally been calculated as a percentage of the skilled man's basic rate and these differentials were rigidly administered. By 1999, however, this pattern was no longer typical of the industry. The National Engineering Agreement, which had underpinned the company-level bargaining framework for decades, was dismantled in 1989. By that stage, the concept of rigid differentials was already being undermined by a number of de facto changes in the industry. In most establishments, the populations of unskilled grades had been drastically reduced and many long-standing distinctions between different skilled trades and between white-collar and blue-collar grades were beginning to be eclipsed by a combination of new technology, team-working and harmonisation programmes.

Elsewhere, in sectors where the NMW might have been expected to have more of an impact on differentials, the knock-on effects appear to have been limited for a number of reasons. Not least is the fact that, outside of traditional manufacturing, the concept of differentials is much less recognised. In those parts of the economy with most relevance for the minimum wage (that is, large parts of the service sector) fixed pay differentials did not really exist. In our first interim report to the Low Pay Commission (April 1999) we published the results of a survey we had conducted involving a targeted sample of firms in low-paying sectors such as hotels and leisure; agriculture and food processing; textiles, clothing and footwear; and the voluntary sector, including care homes. A quarter of companies in this sample reported that the minimum wage would squeeze differentials. On further investigation, we discovered that the actual effect would be minimal. At one of the hotels where a problem was reported, it turned out that only three employees out of a workforce of 200 were paid below the NMW.

Similarly, in a major round-up of pay rates in retailing, first published in September 1998, IDS showed that most major high street chains already paid above the level of the minimum wage. Of the 41 companies featured, only seven paid less than £3.60 an hour and, with four of these, the rates below £3.60 only applied for the 18 to 20 age group. The lowest provincial pay rates for sales assistants tended to range from around £3.90 to £4.20 an hour. The equivalent rates in inner London were between £4.50 and £5.50 an hour.

### 2.2.5. Pay structures and differentials

In two important sectors there were other particular reasons why differentials had not proven to be a major issue. One was fast food and the other was retail, where pay structures are typically kept 'flat' mainly in order to encourage a team-working ethos but which also reflected high staff turnover rates. This is because employees in fast food companies normally move fairly rapidly from an entry rate to an experienced rate and the majority of staff are paid at this level, with distinctions not otherwise being made for age or length of service (although, as we shall see, this approach began to change later, when the level of the National Minimum Wage was increased and some firms decided to introduce youth rates). When enhanced rates were paid, they tended to be for the carrying out of supervisory functions or to reward crew members who had performed particularly well. Since there was no extended hierarchy of rates, the question of differentials did not arise, apart from with supervisors.

The same applied, though for different reasons, in parts of financial services, where many employers had adopted 'broad banding' and performance-related pay schemes. One of the purposes of pay systems of this type had been to encourage individual effort and initiative. In theory, a fairly complex pecking order of pay rates might well be created but because the actual diversity of rates was not made transparent, parity claims in practice were few and far between.

Precisely because the number of employees affected by a minimum wage of £3.60 an hour was relatively few, most employers had been able to absorb any additional costs without great difficulty. A substantial number of firms had reported that the onset of the NMW had actually provided a useful stimulus to rethinking their existing approach to recruitment and retention difficulties, indicating that higher rates at the lower end could well work in the employer's favour.

In cases where the NMW had made an impact, it has usually just clipped the bottom end of pay structures. Employers had been reluctant to disturb an entire pay structure when

relatively minor adjustments at the bottom end were sufficient. One or two major firms, notably in the leisure industry and fast food sector, had taken the opportunity to introduce an entirely new pay structure, with a lowest minimum rate at or above the level of the NMW. But most had opted for a range of other measures of the kind we have already identified, such as the abolition or merger of the bottom grades, abolition of induction rates, payment of slightly higher increases to those on the lowest grades or payment of guaranteed minimum increases to the lower grades. None of these methods appears to have had any major implications for disturbance of differentials.

At the time, we noted that some of these factors might help to explain why the onset of the NMW has not produced any obvious negative effect on employment or on inflation, and no marked effect on average earnings. On the other hand, it may simply have been the case that opponents of the NMW had overstated its negative potential and understated the impact of wider market forces. The NMW had no discernable effect on employment growth in the service sector, where the number of jobs increased by a further 300,000 in the 2000s.

For many companies, recruitment and retention pressures exerted more of an upward pressure on pay rates than the NMW. These pressures were intensified because of continuing expansion within the service sector and because competition for the same pool of labour now applied across a broad range of companies. In practice, this meant that, for this layer of the workforce, the option was always open to make a fairly easy transition from High Street bank, building society or travel shop, to a supermarket, DIY store, call centre or theme park. The result was that, barring entry rates, induction rates and some provincial pay rates, most mainstream employers already paid a more advanced minimum rate for trained, full-time staff of at least £4 an hour. At the time a large provincial hotel HR manager told us that she wished the NMW had been set at £4.20 an hour which would have helped to stem the persistent loss of experienced staff to a nearby call centre.

Often, an effective minimum rate of £4 an hour had resulted from specific campaigns by trade unions, aimed at particular sectors. For example, a minimum rate of £4 an hour had by this time become almost universal in local authorities and most other parts of the public sector. After a successful campaign for a minimum rate of £4 an hour in the bus industry, the TGWU (now Unite) had also announced plans for a new target of a minimum £5 an hour.

**Key findings, 2001 to 2006:**

- As no negative employment effect is witnessed, the LPC pushes the minimum wage up strongly to increase its ‘bite’
- October 2001 sees the largest rise in the NMW at 10.8% to £4.10 an hour
- In this period we see changes to pay structures, premiums and the introduction of new contracts across the retail sector
- Some employers begin to re-introduce age-related pay structures
- The NMW sets the pay agenda in low-paying sectors
- Throughout this period industry agreements wither as the NMW takes over the pay component and the minimum wage is increasingly becoming the floor for pay structures
- The minimum wage begins to influence the lowest clerical salaries in banking and the civil service.

**2.3. Changes in the period 2001 to 2006**

The relatively large increases in the minimum wage between 2001 and 2006 led to a number of key changes across low-paying sectors. Employers began to feel the effects of the minimum wage and started to adopt different approaches to pay setting. Employers reacted to the large 10.8% ‘hike’ in the minimum wage in 2001 with new contracts of employment and pay structures with rates specifically linked to age. Later on in this period employers increasingly altered the bargaining timetable with a shift to October as the key month for pay setting. The minimum wage also started to have more of an impact on pay rates at the bottom end of pay structures, either by being adopted by employers as the lowest rate or as a benchmark.

**2.3.1. Increasing the minimum wage’s ‘bite’**

In the first four years of the new decade, the minimum wage rose by an average of 7% a year at a time when the median pay rise across the rest of the economy was nearer to 3%. Having originally set the minimum wage at a fairly modest level, the Low Pay Commission pushed the rate higher so that it would cover more people (as it had previously affected fewer people than had been anticipated). There was no evidence that moving the minimum wage had produced a negative impact on employment. On the contrary, there was considerable evidence that employment had grown in areas such as retail, restaurants, hospitality and leisure. These larger increases in the minimum wage led to increasing evidence that the minimum wage was now having an impact on many more areas of pay determination and the collective bargaining process than had been foreseen at its inception in April 1999. Increasingly it was setting the pay agenda for a wide range of employers and beginning to have a modest impact outside the low-paying sectors. It was changing employers’

approaches to pay and reward and was instrumental in changing the timing of pay reviews, with more review dates in October.

Table 2.4: National Minimum Wage increases and median pay settlement levels

Effective date	Adult minimum hourly wage rate (£)	Minimum wage increase (%)	IDS annual median pay settlement (%)
1 April 1999	3.60	-	3.0
1 October 2000	3.70	2.8	3.0
1 October 2001	4.10	10.8	3.0
1 October 2002	4.20	2.4	3.0
1 October 2003	4.50	7.1	3.0
1 October 2004	4.85	7.8	3.0
1 October 2005	5.05	4.1	3.2
1 October 2006	5.35	5.9	3.0

In 2001 the minimum wage was raised by 10.8% in the first stage of a two-year announcement to raise the minimum wage by 13.2% overall (a 2.4% increase was applied from 1 October 2002). The uplift to £4.10 an hour had more of an effect on many firms than the initial introduction or the previous year's increase. This is partly because the minimum wage had been set at a relatively modest level in 1999 (at £3.60 an hour) and many firms had already adjusted their rates to reach this level in the years preceding its introduction.

Employers adopted a range of approaches to the uprating, including changes to grades, introducing age-related pay rates, and changes to company review dates. During this period a significant number of firms took the decision to move their anniversary pay review dates from earlier in the year to October, so that any uplift which took place would coincide with the annual NMW uprating.

### 2.3.2. Impact on pay rates

As the minimum wage rose, it increasingly became the floor for pay structures, with starting rates typically at this level across low-paying sectors. However ever since the minimum wage came into effect in April 1999, a significant number of organisations have kept their own lowest rates ahead of the NMW to gain some competitive advantage. Given that the NMW set a very firm wages floor, in 1999 we dubbed the next floor up as the 'mezzanine' floor.

The minimum wage's 'bite' increased in 2001 and, for the first time, the impact of the annual uprating was not limited to smaller retailers, with stores like Morrisons, House of Fraser and Safeway all needing to lift their minimum rates to comply with October 2001's minimum wage increase. Retailers dealt with the uplift in a number of ways, with some deferring reviews to October to coincide with the uprating of the minimum wage, and others reviewing

pay on their usual anniversary dates, then applying additional increases later in the year. Some pay reviews resulted in bottom-weighted increases, with grades at the bottom ends of pay structures receiving larger increases than those further away from the NMW. Upward pressure was also put on lower grades in pay structures due to the generally tight state of the labour market, and it was sometimes difficult to tell whether the NMW or the labour market generally was prompting employers' decisions on pay.

The long-standing trend away from paying age-related rates also began to reverse following the 2001 minimum wage increase. Whereas many employers had previously resisted the opportunity to pay different rates to younger workers, a minority began to opt for the introduction of youth rates, especially in the fast food sector. McDonalds's, KFC and Burger King are all examples of firms that introduced age-related pay rates in this period. McDonalds re-introduced an under-18 rate from September 2001. Prior to this it had paid adult rates of pay from age 16, having removed all age discrimination from its pay structure in 1999. KFC also paid adult rates from age 16 until March 2004 when youth rates for under 22s were introduced. Burger King introduced separate rates for younger workers in October 2003, with the adult rate payable from age 19 rather than age 16 as it had been.

Table 2.5: Examples of company moves to implement the 2001 minimum wage uprating

Company	Details
Burger King	Adult rate payable from age 19 rather than 16
Morrisons	Minimum rate moved to £4.02, except for student and temporary workers for whom the statutory minimum applies from age 21
Punch Taverns	Review date changed from April to October
Retail Co-operative	Starter rates abolished from October, bringing lowest grade from £3.96 to £4.19
Woolworths	Minimum rate moved to £4.24; review deferred from August to October

### 2.3.2. Impact on pay structures

The rising minimum wage was also beginning to have a strong impact on the shape of pay structures. In a number of companies the lowest rates had been merged - both the Retail Co-ops and Tesco were examples. Others had abolished their lowest grades and moved the lowest paid to a higher grade. Other firms allowed pay differentials to narrow over this period. Throughout this period IDS monitored increasing evidence of differentials between sales advisors and supervisory grades being squeezed (see Part Three of this report).

Larger increases in the minimum, together with the extension of Sunday trading and the rise in part-time working, led many retailers to adjust their terms and conditions of employment. Indeed, virtually all of the big retailers moved to 'new contracts' which among other things

allowed them to pay lower premium rates for out-of-hours and weekend working during this period.

Table 2.6: Examples of changes to contracts

Company	Details
Greggs	Introduced new contracts for new starters in 2004. Pay rates were 3% higher than those of existing staff, but Sunday premiums were removed and the bank holiday premium was cut from 2T to T+50%
Ikea	In 2002 it announced a decision to buy out the Sunday premium previously paid to retail staff
Marks & Spencer	In 2003 the 'window' for the night premium was reduced from 9pm to 7am to 10pm to 6am for new starters and Sunday premium reduced from 2T to T+50%
MFI	Sunday premium reduced from 2T to plain time for employees recruited after January 2003
Next	Bank holiday premium reduced from 2T to T+50% except for managers from October 2004
Sainsbury's	Introduced new 'rewarding great service' contracts in 2003 for sub-supervisory grades. These replaced flexible working with fixed shifts for each employee. The night shift premium on these contracts remained at T+33%, but the Sunday and Bank Holiday premiums were reduced to T+50%. Existing employees were offered one-off lump sums to move onto the new contracts
Woolworths	Sunday premium abolished in 2001 for employees recruited after February 2002

#### 2.3.4. Industry agreements superseded

There was also increasing evidence that the National Minimum Wage had superseded a number of the industry-wide or multi-employer agreements that had previously set minimum rates of pay. A few multi-employer agreements had been terminated since 1999. The majority that remained in low-paying sectors, such as clothing and textiles, now set a minimum pay rate that was determined by the NMW and minimum terms and conditions. Mostly these minimum rates were used to set overtime calculations, or for periods of waiting time, or machine breakdown. The Agricultural Wages Board also set a rate for 'harvest' workers which was the same as the adult NMW but below the industry rate for a standard worker which was £5.40 from 1 October 2004.

#### 2.3.5. Impact on clerical starting salaries

During this period there were also moves on starting salaries in clerical areas which were designed in part to take salary levels away from the NMW territory. In a two-year deal, the Scottish Executive raised its lowest clerical salary from £10,300 in 2002 to £12,000 from August 2004. In its April 2004 pay review, HSBC raised the minimum salary for clerical staff from £10,000 to £12,250 (a rise of 22.5%). In two pay rises worth a total of 15%, Barclays

raised its minimum salary from £9,100 to £10,500 and guaranteed cashiers a salary of £12,000 once training was completed. In its August 2004 pay review, the Department for Trade and Industry (DTI) increased its lowest pay rate for administrative assistants by 9%, from £11,200 to £12,200 a year. Higher recruitment salaries reflected a buoyancy in the labour market for staff employed on and around the £5 to £6 an hour level.

In the public sector, minimum rates continued to run ahead of the NMW through a combination of Government policy, union pressure and employers' willingness to address low pay. In 2005/06 minimum rates were around the £5.50 an hour level and moving towards £6 an hour. The new three-year Local Government National Joint Council deal set a minimum rate target of £5.80 in 1 April 2006. In the NHS, under Agenda for Change, the lowest rate rose to £5.69 an hour from October 2004, with a further increase to £5.87 in April 2005. The minimum rate for support staff in Further Education rose to £6 an hour from 1 April 2005.

**Key points, 2007 to 2010:**

- More modest rises in the minimum wage gives employers some 'headroom' to move lowest rates ahead of the minimum wage and restore differentials
- There is evidence that the NMW is having less of an impact on pay structures than in the 2001 to 2006 period
- Statutory leave entitlement rises from 20 to 24 days from October 2007, and then to 28 days from April 2009. This leads to removal/reduction of premiums for bank holiday/weekend working, particularly in the fast food, pubs and restaurants sector
- Recruitment and retention pressures become more of an issue than NMW, particularly in the housing and social care and nursery sectors
- The broad trend away from age-related pay structures continues
- Recession sets in during the second quarter of 2008, recovery starts in fourth quarter of 2009.

**2.4. Changes in the period 2007 to 2010**

Finally, we look at what has happened in the last three years, a period during which increases to the NMW have been more modest and we have seen a major recession. Nevertheless, alongside various austerity measures in the new coalition Government's first budget, was confirmation that the LPC's recommendation for a rise of 2.2% in the National Minimum Wage from 1 October 2010 had been accepted. Additionally, in a change that was announced last year, the adult rate of the NMW will be paid at age 21 from October 2010 for the first time. This is an important shift because, since its introduction, the official qualifying age for

the adult rate has been 22, despite successive recommendations from the LPC that lowering the age bar by one year would have no discernible labour market effects. It is also significant that in its Budget the Government announced that the lowest paid in the public sector should receive increases of at least £250 in each year of the public sector pay freeze.

By 2007 the minimum wage and its subsequent upratings had become a recognised part of pay-setting practice across the low-paying sectors. Throughout the period 2007 to 2010 IDS monitored very few significant changes in pay structures. We have seen more 'nudging' of pay rates around the edges rather than a complete overhaul. More moderate rises in the minimum wage have given employers some breathing space to address any squeezing of differentials that took place in the earlier period, particularly in the retail sector. However, employers have had to deal with a host of other pressures, including the changes to the Working Time Regulations, which raised minimum statutory holiday entitlement to 28 days, and the onset of recession in the second quarter of 2008.

#### **2.4.1. Employers gain some 'headroom'**

By 2007 the minimum wage had become increasingly used to determine the floor for pay structures across the low-paying sectors. However, lower rises in the minimum wage in this period have given some 'headroom' for employers to move away from being minimum-wage payers and to restore differentials. In the fast food sector employers continue to use the minimum wage as the floor for pay structures. However, recently there have been some moves to pay above this level. For example, in 2007 McDonald's increased its minimum rate above the statutory minimum for the first time since October 2000. This also coincided with the first non-rounded minimum wage figure of £5.52. At Pret A Manger the team member rate was boosted to £6 an hour in November 2007 and the company told us that it aims to pay as much as it can, rather than as little as it can get away with.

Similarly, lower increases in the NMW over this period meant that a larger number of retailers looked to maintain a gap between their minimum rate and the NMW. In 2007, we found that two-thirds of retailers were paying above the minimum wage at the bottom end of their pay structures. The gap between the median established rate in low-paying sectors and the NMW broadened to 3.7% in 2007, up from 2.6% in 2006 (see Part Three). There was a considerable reduction in the number of retailers making two-stage increases in 2007, down from a third of companies in 2006 to a tenth in 2007. Retailers applied higher increases to minimum rates in order to maintain a gap between their lowest rate and the minimum wage. For example, established sales assistant rates at Marks & Spencer were increased by 6.3% in 2008 to re-establish its rates against its competitors.

Table 2.7: Changes in minimum pay rates between 2006 and 2009

Company	Minimum hourly adult rate <sup>4</sup> (£)			
	2006	2007	2008	2009
C&J Clarks	5.35	5.56	5.73	5.85
Halfords	5.35	5.54	5.75	5.82
Ladbrokes	5.35	5.62	5.79	-
Makro	5.35	5.58	5.74	5.80
McDonald's	5.35	5.55	5.75	5.82
Next	5.35	5.57	5.73	5.80
Pret A Manger	5.35	5.55	6.00	6.00
NMW	5.35	5.52	5.73	5.80

IDS monitoring of pay in hotels in 2009 showed a falling number of employers using the minimum wage as their lowest rate during this period. Hoteliers face issues around recruitment, with higher rates needed to attract staff, especially in London.

Table 2.8: Examples of minimum rates in hotels in 2009

Hotel	Minimum hourly rate for permanent adult employees (£)
BDL Hotels	6.01
The Gleneagles Hotel	5.78
The Lumley Castle Hotel	5.90
Umi Hotel Brighton	6.00

In sectors like children's nurseries and social care, where qualifications and the link between skills and pay are often important, the NMW has played a role in establishing a benchmark minimum as a 'jumping off point' for structures that reward skills acquired with progression in pay terms. In retail and hospitality sectors, the minimum wage is more commonly used to set the lowest adult rate, albeit the rate may be a few pence above. It is important to note that the nursery and social care sectors are very different from other low-paying sectors in that they are subject to a great deal of external scrutiny and regulation. There are rules about staff qualifications and staff-to-client ratios meaning redundancy is not always an option when costs are rising.

IDS research also shows that the broad trend away from age-related pay has continued, with retailers continuing to reduce the age at which adult rates apply or phasing it out altogether. Table 2.9 provides examples of changes to age-related pay that have taken place between 2007 and 2010. On the other hand, age-related pay rates continue to be commonplace in the fast food, pubs and restaurants and childcare sectors which employ large proportions of young people.

<sup>4</sup> The age at which the adult rate takes effects varies by company.

Table 2.9: Examples of changes to age-related pay

Company	Details
Argos	Separate rates for 16 and 17 year-olds are consolidated into a single under-18 rate in April 2007
Boots	Higher rises applied to the under-18 rate in both 2007 and 2008, with the company explaining that the differential between their rates and adult staff was too wide
Marston's	Introduced a youth rate for employees aged under 21 years of age with effect from 1 October 2008
Tesco	In July 2007, junior rates for skilled grades D and E were removed. Age-related pay rates are removed as part of the 2010 review, ending all age-related pay from August 2010
Waitrose	Higher increases to the under-18 rate in 2008 and 2009 in order to narrow the differential with staff aged over 18

#### 2.4.2. Restoring differentials

Lower rises in the minimum wage during this period also sees employers making moves to restore supervisory premiums. In the fast food, pubs and restaurants sector most companies felt pressure on differentials as a result of previous upratings, where the difference between supervisors and team members is important even if the differences in pay levels are not significant in cash terms. Where they could afford to, companies tried to maintain differentials but they did not do this every year for all groups. Not all rates were increased by the same amount. Instead employers pick and choose each year which rates should be increased and by how much. For example, in 2007 McDonald's raised the pay band for shift-running floor managers by a higher amount in order to restore the differential between managers and team members.

Retailers have also looked to restore differentials over the last few years. Some retailers have either paid higher increases to team leader groups as part of the general pay review or introduced skills payments to recognise the responsibilities of these employees. For example, Sainsbury's introduced a skills payment for its fully competent team leaders in 2008 and, in the 2009 pay review, the payment was doubled from 16p to 32p an hour.

Similarly, employers in the nursery sector have tried to maintain differentials. Just under two-thirds of organisations IDS surveyed in March 2007 said that they had to raise the rates of higher-paid staff to maintain pay differentials. In our March 2008 survey, again close to two-thirds of respondents (65%) said they had raised rates of higher-paid staff in order to preserve differentials. In our March 2009 survey, of the 26 organisations that provided information about the effect on pay rates higher up the pay structure, 58% said that they increased the rates of senior staff to preserve differentials. This year around half reported to have increased the rates of more senior staff in order to maintain differentials.

Table 2.10: Examples of retailers restoring differentials

Company	Details
Argos	4.5% increase to team leaders in 2008 to preserve the differential with the NMW. Other staff received 3.5%
Iceland	10% increases for supervisors from 1 April 2008. It said this was intended to reward their commitment, work as a retention incentive, and maintain differentials with sales rates
Morrisons	Supervisors' rates boosted in 2007 to maintain differentials between their rates and those of general store staff. It guaranteed a 50p differential between the sales and supervisor grades
Sainsbury's	Premium paid to team leaders increased by 16p an hour in 2008
Somerfield	Premium paid to duty-manager trained supervisors increased from 10p to 30p an hour in 2008, to recognise the enhanced responsibilities
TK Maxx	TK Maxx paid increases averaging 2.7% in 2007 but specialist sales staff received 4.7% and supervisors 4.3%

Organisations in the housing and social care sector have increasingly taken steps to preserve differentials by either applying the minimum wage increase across-the-board or awarding extra increases to higher-paid staff. Although these employers have also faced pressures due to recruitment and retention difficulties and staff-to-resident ratios (see table 2.11).

Table 2.11: Organisations taking action to preserve differentials, housing and social care

Year	Proportion of organisations taking action (%)	Minimum wage increase (%)
2006	12.0	5.9
2007	17.0	3.2
2008	33.0	3.8
2009	25.0	1.2

#### 2.4.3. Increase in minimum statutory leave entitlement

The Working Time (Amendment) Regulations 2007 increased minimum statutory holiday entitlement from 20 to 28 days a year in two phases. Under these regulations, holiday entitlement in the UK – including the eight public holidays – rose to 24 days' paid holiday for a five-day week from 1 October 2007 and to 28 days from 1 April 2009. The main aim of the legislation was to prevent the practice of including the current eight bank holidays in the minimum annual holiday entitlement, thereby effectively giving employees just 12 days' annual leave, excluding the public holidays.

The change to statutory holiday entitlement had an effect on employers across the low-paying sectors, with our monitoring showing employers in the fast food, leisure, nursery and social care sectors having to increase basic holiday entitlement. The impact in retail and hotels was more varied since many employers already provided 20 days' annual leave, plus paid bank holidays. IDS monitoring also showed a knock-on effect of employers –

particularly in the fast food, pubs and restaurants sector – moving away from paying bank holiday premiums as a way of offsetting increased holiday entitlement.

However, relatively high turnover rates in the fast food sector mean that some staff leave without taking advantage of all accrued holiday. The changes in bank holiday premiums in the retail and catering sectors, coincide with a long-term trend in the retail sector to incorporate premium payments for weekend working and unsocial hours working into basic pay, or to phase them out altogether.

Table 2.12: Examples of changes to premiums following the rise in minimum statutory leave

Company	Details
KFC	Bank-holiday premiums reduced from 2T to T+50% following the October 2007 statutory increase and from 1 April 2009 the company pays bank holidays at normal hourly rates. KFC has also stopped awarding service-related holiday
McDonald's	Moved to pay bank holiday working at normal hourly rates from 1 April 2009, having phased out this premium from September 2008

#### 2.4.4. Scale shortening and underpinning awards in the public sector

In contrast to the low-paying sectors, employers in the public sector have been making significant changes to their pay structures in order to tackle low pay during this period. While our latest analysis of lowest rates in the public sector shows that minimums are typically upwards of £6.50 an hour, low pay remains a key feature in the public sector and is likely to remain so in future years, given the context of public sector pay restraint. In this period 'underpinning', whereby employees on the lowest pay points receive relatively higher increases, has become an increasingly common element of public sector pay awards. Recent examples here include the NHS, local government, universities and government departments. Linked in part to the equal pay challenge, many departments and agencies have also embarked on a programme of scale shortening, boosting pay at the lower end.

#### 2.4.5. Minimum wage and recession

Since the onset of recession the LPC has continued to set modest increases in the minimum wage. In 2009 it rose by 1.2% to £5.80 an hour. Interestingly, the median pay settlement across the low-paying sectors in 2009 was 2% – above the level of the rise in the minimum wage showing that companies set their own agenda, rather than it being determined by the minimum wage. In 2010 the adult minimum wage was increased by 2.2% to £5.93 an hour. The Government also accepted the long-standing recommendation of the Commission for the adult rate to apply at age 21 rather than 22. There is also a new apprentice minimum wage of £2.50 an hour.

IDS monitoring of pay in low-paying sectors so far for 2010 shows a broad trend of employers continuing to focus on pay relativities and restoring differentials. In children's nurseries, the 2010 survey showed fewer employers having to raise their lowest rate in order to comply with the statutory minimum wage, following the relatively small uplift in 2009. Also the gap between the pay rates in this sector and the minimum wage has widened. IDS has also monitored examples of retailers adjusting their rates to maintain or restore differentials for staff at a greater skill or responsibility level. For example, TJ Hughes paid staff rises of 1% from 1 August 2010 but to maintain the premiums paid to level 2 and 3 sales staff (at 10% and 20% above the general sales assistant rate), these staff received a further 1.24% from October 2010. As part of the 2010 pay review, Clarks has moved its lowest adult rate to 10 pence above the current NMW. In 2009 this rate was just 5 pence above the statutory minimum. Tesco has abolished youth rates and introduced a lower 'new starters' premium for working nights.

The exception to this however, is the housing and social care sector, where IDS research shows that employers have narrowed the differentials for care staff over the last year. The sector faces budget cuts and a growing demand for services, pressures which have also led to an increase in the proportion of pay freezes in 2010 while freezes in other parts of the economy have started to come down.

In terms of pay freezes, low-paying sectors have been affected but to a lesser extent than other parts of the economy (see Part One). However, there may be a timing effect here as demonstrated by our 2009 monitoring which showed that those firms who typically review pay in October had yet to see the impact of the recession on pay reviews. Sectors with earlier reviews mirrored the rest of the economy, with a mixture of freezes and rises. So far for 2010, the proportion of pay freezes across the low-paying sectors has come down (except housing and social care), in line with the rest of the economy.

## Part Three - Time-series analyses of company pay rates

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The following section explores the relationship between the level of the National Minimum Wage and actual company pay rates at the bottom end of pay structures, specifically exploring the movement in the lowest rates of pay since the introduction of the minimum wage. In order to do this we have examined changes in the gap between the lowest rates of pay and the minimum wage, as well as the gap between the lowest rate and the supervisor rate, at a range of organisations in low-paying sectors over time.

This analysis is different from that presented in Part One of this report, which looks at pay settlement levels, in that it compares increases in the actual pay levels with increases in the level of the minimum wage, rather than the general uplift applied to all grades following the annual company pay review. The key difference here is that pay settlement levels do not take into account other changes that may have taken place, such as restructuring of grades or larger uplifts for particular grades.

### Key findings:

Relationship between the NMW and established team member pay rates:

- Overall, the gap between the established rate of pay in low-paying sectors and the minimum wage has narrowed from 16.5% in 1999 to 4.3% in 2009
- When there have been larger increases in the minimum wage, the gap between the established rate and the minimum wage has narrowed
- Some employers have adopted a policy of moving their minimum rates towards the level of the minimum wage, rather than maintaining a lead over the statutory minimum.

Relationship between the NMW and minimums in other parts of the economy:

- In the finance sector generally, the trend in the gap between the lowest rate and the minimum wage is similar to that in low-paying sectors, with narrowing between 2007 and 2009. However, here the gap is much wider at around 15% to 20%
- The trend in the public sector is very different to that in the financial services and low-paying sectors. Here we have seen a significant widening of the gap between the minimum wage and lowest grades in recent years as organisations have raised their lowest rates in order to tackle both equal pay for work of equal value and low pay.

Relationship between the NMW and supervisors' pay rates:

- Overall, the gap between supervisory and established rates of pay has narrowed more modestly, from 11.4% in 1999 to 7.8% in 2009
- Since 2004 the differential between established rates and supervisor rates has been maintained at around 7% to 8%.

Movements in pay rates before the minimum wage:

- Since the introduction of the NMW there has been greater variation in increases to established rates than prior to the introduction of the minimum wage, when the trend was for an increase of around 3% in line with the rest of the economy.

### 3.1. Differentials between established rates and the minimum wage

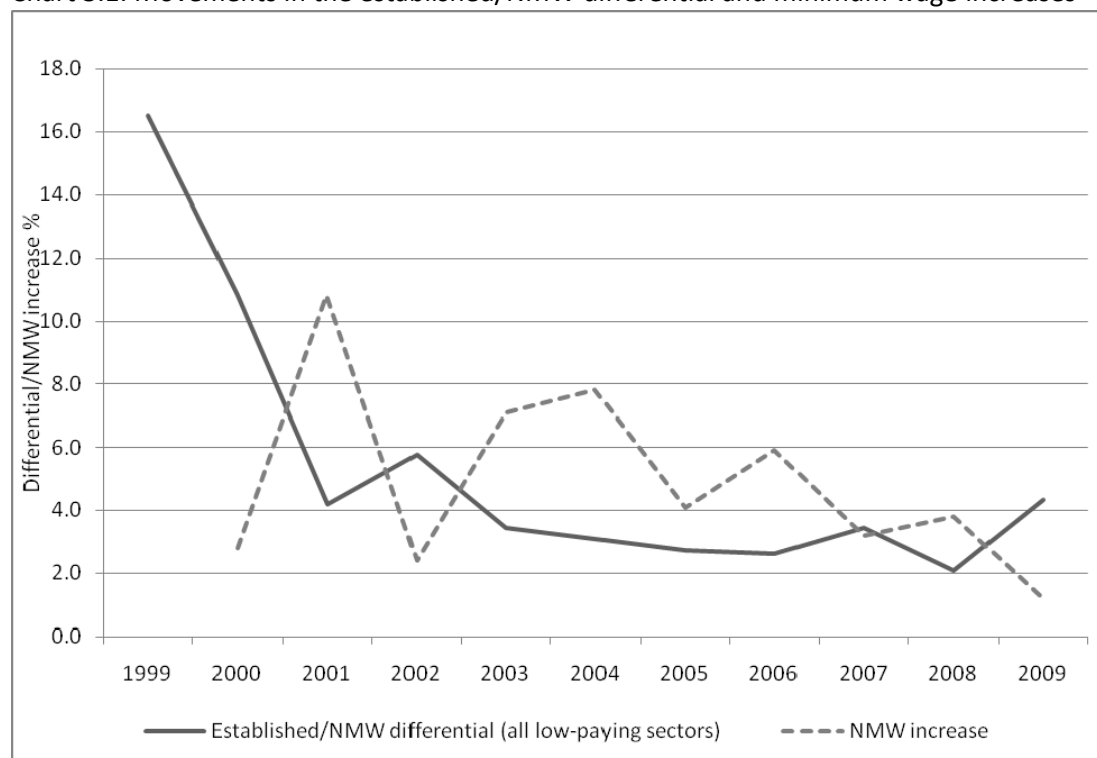
The following section looks at changes since 1999 in the differential between the minimum wage and the established rates at organisations in low-paying sectors. The differential refers to the percentage difference between the established adult rate<sup>5</sup> and the National Minimum Wage (NMW) at a sample of organisations. This is then compared to subsequent increases in the minimum wage since its introduction in 1999.

Chart 3.1 shows the median differential between established rates of pay and the minimum wage over time, referred to as the 'established/NMW differential'. The chart shows that the differential has narrowed from 16.5% in 1999, when the NMW was introduced, to 4.3% in 2009. This reflects the increasing number of employers using the minimum wage to determine the floor for pay structures by either using it directly or as a benchmark to set the lowest rate of pay. During the same period there has also been a range of changes to pay structures, some of which have been identified in Part Two of this report.

Overall the chart shows a relationship between the established differential and the NMW uplift; generally when the uplift is smaller the gap in the established rate over the minimum wage increases and vice versa. In other words, when the increase in the NMW was relatively large, employers did not increase their established rate by as much, but, in years when the NMW percentage uplift was lower, some employers raised rates by more than this percentage.

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<sup>5</sup> Typically, this rate is the bottom of the main low-paid grade in 'national' locations.

Chart 3.1: Movements in the established/NMW differential and minimum wage increases<sup>6</sup>

The period 2001 to 2006 is characterised by relatively high increases in the NMW, following a modest increase in 2000. The peak was the increase of 10.8%, applied to the adult minimum rate in 2001 as part of a front-loaded two-year increase, which also set an increase of 2.4% in 2002. As a result of the large increase in the minimum wage in 2001, the median established/NMW differential fell sharply from 10.8% in 2000, to 4.2% in 2001. However, the differential widened again to 5.8% in 2002, when the second-stage increase in the minimum wage was relatively small.

Between 2003 and 2006 – when the increases to the minimum wage were roughly between 4% and 8% – the median established/NMW differential narrowed to between 2.6% and 3.4%. In summary, a period of relatively high NMW uplifts between 2001 and 2006 led to the differential between established rates and the NMW being around a fifth of what it had been when the NMW was introduced in 1999 and around a third of what it had been in 2000, a year after its introduction.

<sup>6</sup> The 'established/NMW differential' refers to the percentage gap between established rates of pay at organisations included in the panel and the adult national minimum wage.

Table 3.1: Company-specific established/NMW differentials<sup>7</sup>

	Percentage difference between the established rate of pay and the NMW (%)										
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Argos	18.0	17.4	9.2	9.1	4.7	1.0	0.0	0.0	0.0	0.0	0.0
Asda	17.2	17.6	10.0	15.5	12.7	7.8	7.7	6.5	6.5	6.8	7.7
B&Q	-	-	9.8	10.5	6.2	1.4	2.0	1.7	1.6	-	-
Blackwells	-	-	-	-	3.6	2.1	1.0	0.0	0.0	0.0	0.0
Boots The Chemists	14.2	11.1	0.2	10.0	5.8	8.3	7.1	4.1	4.2	4.2	4.0
C&J Clark	8.3	9.2	1.5	1.4	0.0	0.0	0.0	0.0	0.7	0.0	0.9
Greggs	-	16.0	9.0	9.8	6.2	5.2	5.5	-	4.0	6.0	7.9
Halfords	13.3	13.5	5.4	6.2	0.9	0.0	0.0	0.0	0.4	0.4	0.3
Homebase	-	-	-	-	1.3	1.0	1.0	0.0	0.0	0.0	0.0
House of Fraser	9.4	9.2	1.2	1.9	1.3	1.2	1.2	1.1	1.1	1.1	-
Iceland	14.2	13.8	5.4	5.5	0.7	3.1	0.0	0.0	2.4	-	-
KFC	-	2.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Makro	17.8	17.3	6.3	9.8	7.8	3.1	2.2	2.1	3.1	2.3	1.0
Marks & Spencer	-	-	-	11.4	15.1	9.3	12.9	9.4	9.1	11.7	12.6
Marstons	6.9	6.8	6.1	6.0	4.4	3.1	-	-	2.7	-	2.6
McDonald's	0.0	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.5	0.4	0.3
Mitchells & Butlers	-	10.8	3.7	3.6	2.2	2.1	2.0	1.9	1.8	1.8	1.7
Next	15.8	14.9	6.8	6.2	2.0	0.0	0.0	0.0	0.9	0.0	0.0
Peacocks	-	-	-	-	2.2	5.2	5.0	2.8	3.3	2.1	2.1
Pret A Manger	-	-	-	-	15.7	7.2	3.0	2.8	3.3	7.3	6.0
Sainsbury's	21.7	20.8	14.6	14.5	12.2	6.8	6.7	3.7	6.2	6.1	7.4
Schuh	29.4	-	-	-	16.4	11.3	10.1	7.1	6.9	6.1	7.9
Selfridges	-	-	-	-	15.6	10.3	9.1	7.5	7.8	7.3	8.6
Somerfield	3.9	4.1	0.5	2.4	2.2	1.0	0.0	0.0	0.0	0.0	0.7
Tesco	35.3	35.7	26.8	27.1	22.2	16.7	15.6	12.5	13.4	13.4	14.8
Waitrose	-	-	-	-	0.2	0.0	0.0	0.9	1.5	0.9	2.8
Waterstone's	25.3	26.0	13.7	17.6	15.1	10.5	9.3	5.2	4.5	5.8	6.6
Wilkinson	17.8	18.4	10.5	11.4	8.0	7.6	3.4	2.8	2.7	2.1	4.5

<sup>7</sup> Cells marked '-' indicate no data available.

In the later period between 2007 and 2009, increases to the NMW were relatively modest at between 1.2% and 3.8%. During this period employers sometimes increased their established rates by more than the annual NMW uplift and the established/NMW differential widened once again to 4.3%. In 2007, the NMW increase was 3.2% and the differential widened to 3.5%. In 2008 – when the NMW uplift was 3.8% – the differential narrowed to 2.1% and in 2009 – when the NMW increase was only 1.2% – the differential widened again to 4.3%.

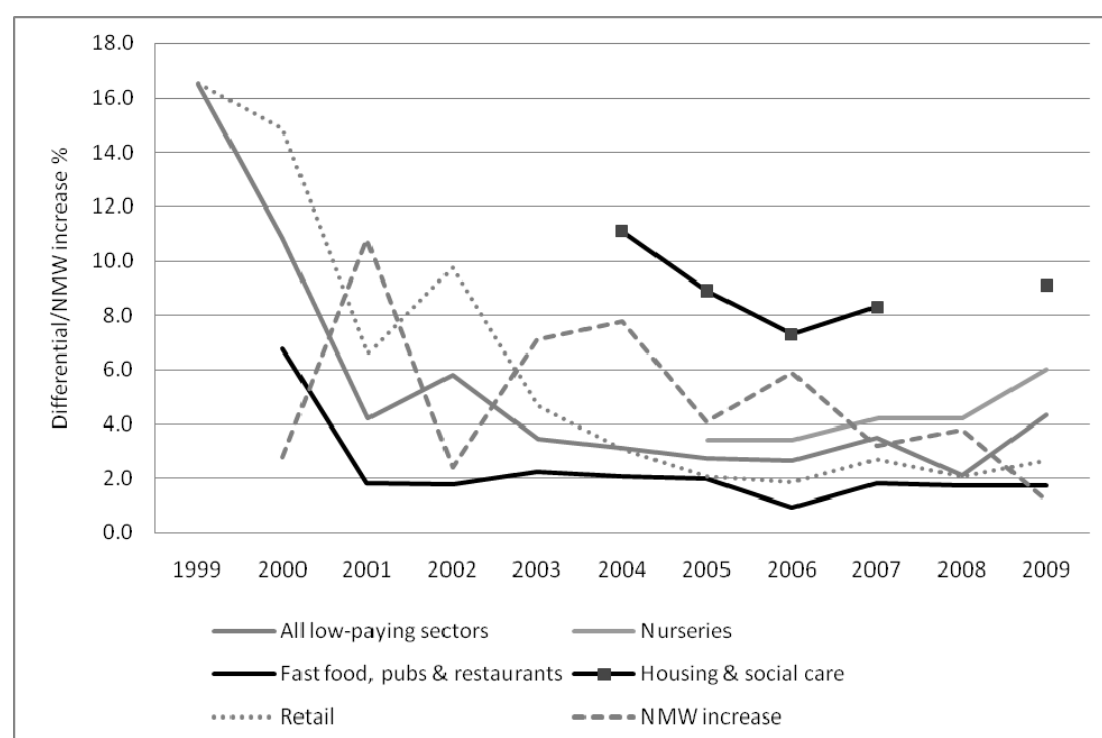
Table 3.1 provides examples of company-specific gaps between established rates of pay and the minimum wage. The table illustrates the two broad trends adopted by employers in managing the introduction of, and subsequent increases in, the minimum wage. Some organisations have moved to adopt the NMW as the floor for pay structures, whereas others have maintained a relatively large gap between the minimum wage and their established pay rate. However, an important caveat here is that these gaps do not take into account other pay and organisational changes that may have taken place at company level during this period (see Part Two).

### 3.2. Differences between low-paying sectors

The gap between established rates of pay and the minimum wage varies within each of the low-paying sectors, as illustrated in chart 3.2. Since 2005, however, the differentials have become more consistent with one another. Overall, the differential is narrowest in the fast food, pubs and restaurants sector and widest in housing and social care reflecting sectoral differences.

As chart 3.2 shows, established rates in the fast food, pubs and restaurants sector have always had the most narrow differential with the NMW. In 2000, the median differential in the sector was 6.8%, but in 2001 it fell sharply to 1.8% and it has stayed at around this level since then. Pay pressures in this sector are weaker, with large numbers of casual workers and relatively high turnover rates.

In the retail sector, differentials have historically been wider than in the fast food sector, but here increases in the minimum wage have had more of an effect. The large minimum wage increase of 10.8% in 2001 led to a sharp drop in the retail differential from 14.9% in 2000 to 6.6% in 2001 (see table 3.2). In 2002, when the NMW uplift was much lower, the retail differential widened again to 9.8%. Since then, however, the median differential in the sector has narrowed significantly, to 4.7% in 2003 and to around 2% from 2005 onwards.

Chart 3.2: Movements in the established/NMW differential by sector<sup>8</sup>Table 3.2: Median established/NMW differentials by sector<sup>9</sup>

Year	Median differential (%)				
	Care & housing services	Fast food, pubs & restaurants	Children's nurseries	Retail	All low-paying sectors
1999	-	-	-	16.5	16.5 <sup>10</sup>
2000	-	6.8	-	14.9	10.8
2001	-	1.8	-	6.6	4.2
2002	-	1.8	-	9.8	5.8
2003	-	2.2	-	4.7	3.4
2004	11.1	2.1	-	3.1	3.1
2005	8.9	2.0	3.4	2.1	2.7
2006	7.3	0.9	3.4	1.9	2.6
2007	8.3	1.8	4.2	2.7	3.6
2008	-	1.8	4.2	2.1	2.1
2009	9.1	1.7	6.0	2.7	4.3

Between 2007 and 2009 – a period of more modest increases in the minimum wage – there was a slight widening in the retail differential to just under 3%. Interestingly, since 2005 there has been very little difference between the differential in the retail sector and that in

<sup>8</sup> The 'established/NMW differential' refers to the percentage gap between established rates of pay at organisations included in the panel and the adult national minimum wage.

<sup>9</sup> Cells marked '-' indicate no data available.

<sup>10</sup> The 'all low-paying sectors median differential' is based on pay rates across low-paying sectors, except in 1999 when it is based on pay rates in the retail sector only.

the fast food, pubs and restaurants sector. However, pay structures in retail are more hierarchical, compared to much flatter structures in the fast food, pubs and restaurants sector and in this same period (from 2007 onwards), we have seen some retailers taking measures to restore differentials between supervisors and established sales assistants, where these had been eroded.

In both the housing and social care and nursery sectors, the profile of employees is different from most other low-paying sectors, and there are minimum requirements for qualifications as well as for staffing levels. They also differ by being quasi-private sector, in that they either receive public funding or the payment of fees are partly subsidised through welfare benefits.

In childcare, the trend since 2005 has followed that in the other low-paying sectors over the same period, with a slight widening of differentials in 2007 and 2009 when the NMW uplifts were relatively low. However, it is worth noting that the differential has tended to be wider than in retail and fast food, and has also tended to have widened more sharply in recent years. This is set against a backdrop of rising recruitment difficulties and qualification requirements, both upward pressures on pay rates.

Housing and social care employers tend to pay spot rates, and typically have an older workforce than the other low-paying sectors – resulting in higher pay rates, even at the unqualified care assistant level. In this sector, the established/NMW differential followed a slightly different trend to the rest of the low-paying sectors. Compared to the other low-paying sectors it has maintained a healthy differential over the minimum wage, possibly a reflection of recent expansion in the workforce and the need to recruit new staff. Between 2007 and 2009 the differential in this sector widened from 8.3% to 9.1%.

### **3.3. Comparing pay differentials by broad sector**

In order to explore the relationship between the NMW and the lowest rates of pay in the wider economy, we have conducted a similar time-series analysis of minimum pay rates for clerical roles in private-sector financial institutions and the lowest grades in the public sector. These data have enabled us to compare trends in low-paying sectors against trends in higher-paid parts of the economy, as shown in table 3.3 and chart 3.3.

The trend in the differential between the minimum clerical pay rate and the minimum wage in the finance sector is similar to that of low-paying sectors. As chart 3.3 shows, there has been a progressive narrowing of the differential over time, followed by a widening in 2009 when the NMW was increased by a relatively small amount. However, differentials in the

finance sector have been maintained at between 15% and 20%, while in low-paying sectors established rates are now less than 5% above the NMW.

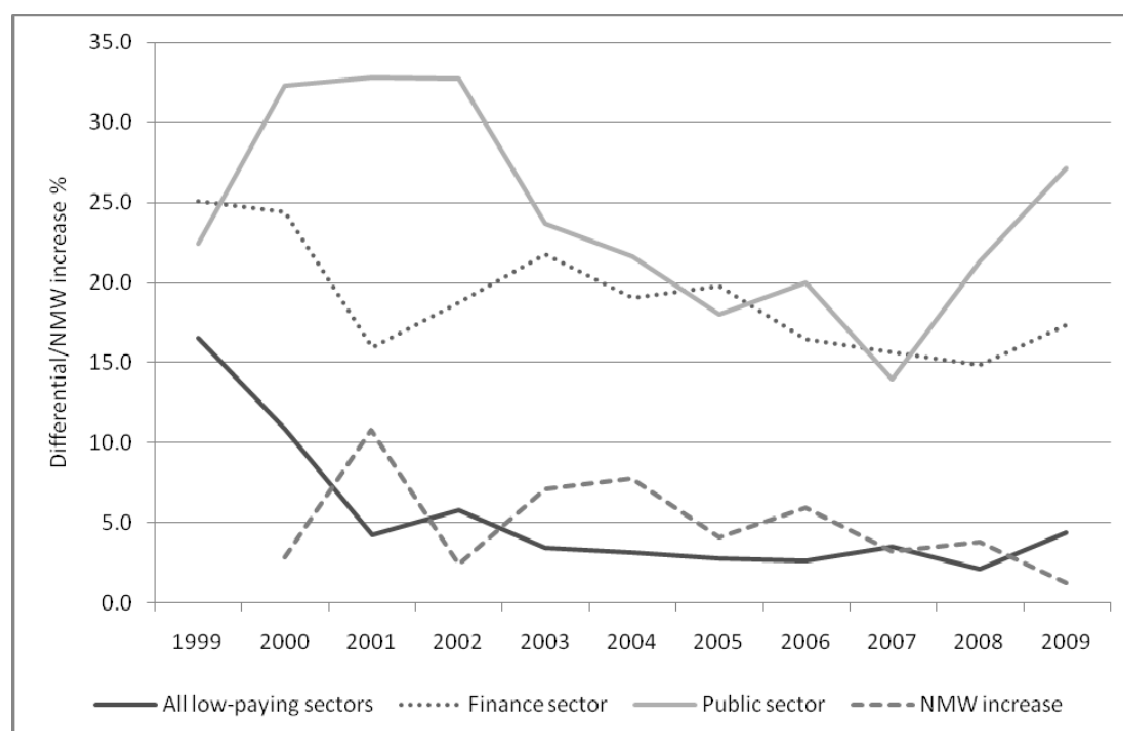
Table 3.3: Median established/NMW differentials by broad sector

Year	Median differential (%)		
	Low-paying sectors	Finance sector	Public sector
1999	16.5 <sup>11</sup>	25.1	22.4
2000	10.8	24.4	32.3
2001	4.2	15.9	32.8
2002	5.8	18.7	32.7
2003	3.4	21.8	23.7
2004	3.1	19.1	21.6
2005	2.7	19.8	18.0
2006	2.6	16.4	20.0
2007	3.6	15.6	14.0
2008	2.3	14.8	21.3
2009	4.3	17.3	27.1

In the public sector, the trend has been different (see chart 3.3). Between 1999 and 2002, public sector employers improved relative pay at the lower end of pay structures and the median differential between the minimum rate and the NMW widened from 22.4% in 1999 to 32.7% in 2002. This is the opposite of what happened in the finance and low-paying sectors. During the period that followed, the Government started bearing down on pay increases in the public sector and the differential between the minimum rate and the NMW narrowed to levels close to those in the financial services sector. The median public sector differential fell to a low point of 14% in 2007, less than half of the peak differential of 32.8% in 2001 (see table 3.3).

From 2007 onwards, during which time we have also witnessed more modest increases in the minimum wage, the differential in the public sector has again widened from 21.3% in 2008 to 27.1% in 2009. However, this widening has taken place against a backdrop of tackling both equal pay for work of equal value and low pay in the public sector. Efforts such as underpinning pay awards for those on the lowest grades, despite modest rises for other groups, and the removal of the lowest spine points have increased the lowest public sector pay rates.

<sup>11</sup> Note: The 'established/NMW differential' is based on pay rates across low-paying sectors, except in 1999 when it is based on pay rates in the retail sector only.

Chart 3.3: Movements in the established/NMW differential by broad sector<sup>12</sup>

### 3.4. Differentials between supervisor and established rates

In order to gauge the relationship between the minimum wage and pay rates further up the structure, we have looked at the gap between pay rates for supervisors and those for less senior staff (e.g. established sales assistants), referred to as the supervisor/established differential.

The differential is the percentage difference between the supervisor and established rates, based on a sample of 17 organisations in the retail and fast food, pubs and restaurants sectors. An important caveat to this analysis is that it does not explore any changes in the organisation of work which may explain some of the changes at company level, such as the introduction of a new tier of management in stores.

The trend in the differential between supervisor and established rates of pay over the period 1999 to 2009 has followed that of the differential between established rates and the minimum wage, but importantly it has not narrowed by as much. Overall, the median supervisor/established differential has narrowed from 11.7% in 2000 to 7.8% in 2009, compared to a fall from 10.8% in 2000 to 4.3% in 2009 in the median established/NMW differential. Another finding is that since around 2004 the gap between rates of pay for

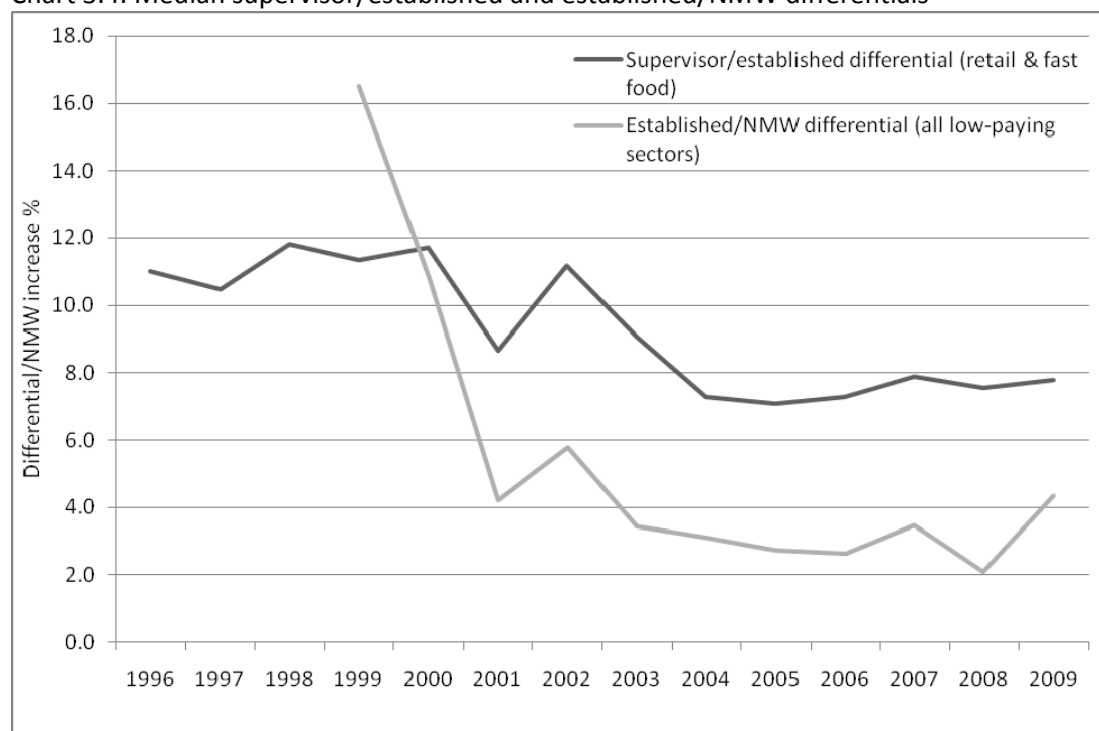
<sup>12</sup> The 'established/NMW differential' refers to the percentage gap between established rates of pay at organisations included in the panel and the adult national minimum wage.

supervisors and those for less senior staff has been maintained at between 7% and 8%. This is despite fluctuations in the level of minimum wage increases and in the established/NMW differential.

Table 3.4: Median supervisor/established differentials and established/NMW differentials

Year	Median differential (%)	
	Gap between supervisor and established rates	Gap between established rates and the minimum wage
1999	11.4	16.5 <sup>13</sup>
2000	11.7	10.8
2001	8.7	4.2
2002	11.2	5.8
2003	9.1	3.4
2004	7.3	3.1
2005	7.1	2.7
2006	7.3	2.6
2007	7.9	3.5
2008	7.6	2.3
2009	7.8	4.3

Chart 3.4: Median supervisor/established and established/NMW differentials<sup>14</sup>



<sup>13</sup> The 'established/NMW differential' is based on pay rates across low-paying sectors, except in 1999 when it is based on pay rates in the retail sector only.

<sup>14</sup> The 'established/NMW differential' refers to the percentage gap between established rates of pay at organisations included in the panel and the adult national minimum wage. The 'supervisor/established differential' refers to the percentage gap between established rates of pay and supervisory rates of pay.

Chart 3.4 illustrates both the trend in the median supervisor/established differential and the median established/NMW differential. At the introduction of the NMW in 1999, the gap between the supervisor rate and the established rate was 11.4%. Following the relatively modest increase in the minimum wage in 2000, the gap widened slightly to 11.7%. This is explained by employers restoring differentials after raising their lowest rates to comply with minimum wage legislation (e.g. the focus had shifted to raising pay rates for supervisors). The differential narrowed to 8.7% in 2001, following the large uplift in the NMW, but then widened again to 11.2% in 2002. This mirrors what happened in the established/NMW differential but less dramatically.

Between 2002 and 2003 the gap between supervisor and established rates narrowed further to 9.1%, again following the trend in the established rate versus the minimum wage. Since 2004, the median differential has been fairly stable at around 7% to 8%, despite movements in the gap between established rates and the minimum wage. In 2009 the gap between established rates and the minimum wage rose from 2.3% to 4.3%, while the gap between established and supervisor rates rose marginally from 7.6% to 7.8%. This indicates a renewed focus in moving away from the minimum wage, while maintaining differentials for supervisory staff at the same level.

### 3.5. Movements in company pay rates

In order to build a picture of company pay decisions in the period prior to and just after the introduction of the NMW, we have plotted actual increases in pay rates over time. Table 3.5 provides details of the actual increase applied to the established rate following the annual pay review from 1994 to 2009 at eight retailers.

Before the introduction of the NMW, there was relatively little change in the annual increase of the established rate from year to year and little variation in the increases applied at individual firms. Between 1994 and 1997, increases in established rates were centred on 3%, with a small variation between just over 2% to just over 4%. Following the announcement of the introduction of the NMW in 1998, established rates were typically increased by between 3% and 4%, whereas in 1999 – when the NMW came into force – established rates rose by around 2.5%. In 2000, when the NMW was increased by 2.8%, retailers typically increased their established rate in line with this. In the years after 2000, the increases in the established rates have been much more varied than in the period prior to the introduction of the NMW. In some years, the increases have mirrored the movement of the increase in the NMW, whereas in other years the increases have been higher or lower than the increase in the NMW.

Table 3.5: Actual increases applied to established rates<sup>15</sup>

	Percentage increase applied to the established rate following the annual pay review (%)								
	Argos	Asda	Boots The Chemist	Next	Sainsbury's	Somerfield	Tesco	Waterstone's	Median
1994	-	3.8	-	-	2.7	2.0	2.5	-	2.6
1995	3.4	3.4	3.3	-	3.2	2.8	3.6	-	3.3
1996	4.1	4.1	3.2	3.3	3.1	3.3	3.0	3.5	3.3
1997	4.2	3.4	3.1	3.2	2.5	2.9	3.6	3.6	3.3
1998	3.0	4.1	3.8	3.3	3.6	3.1	3.9	2.6	3.5
1999	2.8	2.7	0.0	3.5	2.6	2.5	2.7	3.2	2.7
2000	2.3	3.1	0.0	1.9	2.1	2.9	3.1	3.3	2.6
2001	3.0	3.7	0.0	3.1	5.1	7.0	3.6	0.0	3.3
2002	2.3	7.5	12.4	1.8	2.3	4.4	2.7	6.0	3.5
2003	2.8	4.5	3.0	2.9	5.0	7.0	3.0	4.9	3.8
2004	4.0	3.2	10.3	5.7	2.6	6.5	2.9	3.5	3.8
2005	3.1	4.0	3.0	4.1	4.1	3.1	3.2	3.0	3.1
2006	5.9	4.8	3.0	5.9	3.0	5.9	3.1	2.0	3.9
2007	3.2	3.2	3.2	4.1	5.6	3.2	4.0	2.5	3.2
2008	3.8	4.1	3.8	2.9	3.8	3.8	3.8	5.0	3.8
2009	1.2	2.0	1.0	1.2	2.5	1.9	2.4	2.0	1.9

<sup>15</sup> Cells marked '-' indicate no data available.

## Conclusion

This report provides evidence of the way in which the minimum wage and subsequent increases have affected pay setting in low-paying sectors. The main findings are as follows:

- Pay settlements in low-paying sectors, like those in the rest of the economy, are more likely to be influenced by RPI inflation and other economic factors, as opposed to being determined solely by the minimum wage increase
- However, employers approaches to reviewing pay rates have changed, enabling them to raise the rates of the lowest paid within a paybill 'envelope' of the general annual pay review, with differential increases to the lowest paid
- These approaches include: reviewing rates in two stages; applying differentiated rises; or moving review dates to coincide with the minimum wage uplift
- Increases in the minimum wage have had an impact on the effective date of pay reviews, with October becoming more popular for employers in low-paying sectors
- Some major changes to pay structures took place before the introduction of the minimum wage, partly in anticipation of its introduction but also due to equal pay considerations. These reduced the impact of the minimum wage when it was introduced in 1999
- Most employers were comfortably able to adjust pay rates to the level of the minimum wage, with no negative effects on employment or differentials
- However, the larger increases in the minimum wage between 2001 and 2006 were accommodated by employers who adopted new contracts of employment, mainly retailers, and pay structures with rates specifically linked to age, particularly in fast food
- There is an inverse relationship between minimum wage increases and the differentials in low-paying sectors; when increases in the minimum wage are more modest differentials widen and when the increases are larger the gap is squeezed
- The differential between supervisors rates and rates of pay for established staff shows a similar inverse relationship – although overall the gap between supervisors rates and rates for established staff has not narrowed as much as the gap between established rates and the minimum wage.

## Appendix 1

### Company-specific time series data on pay differentials

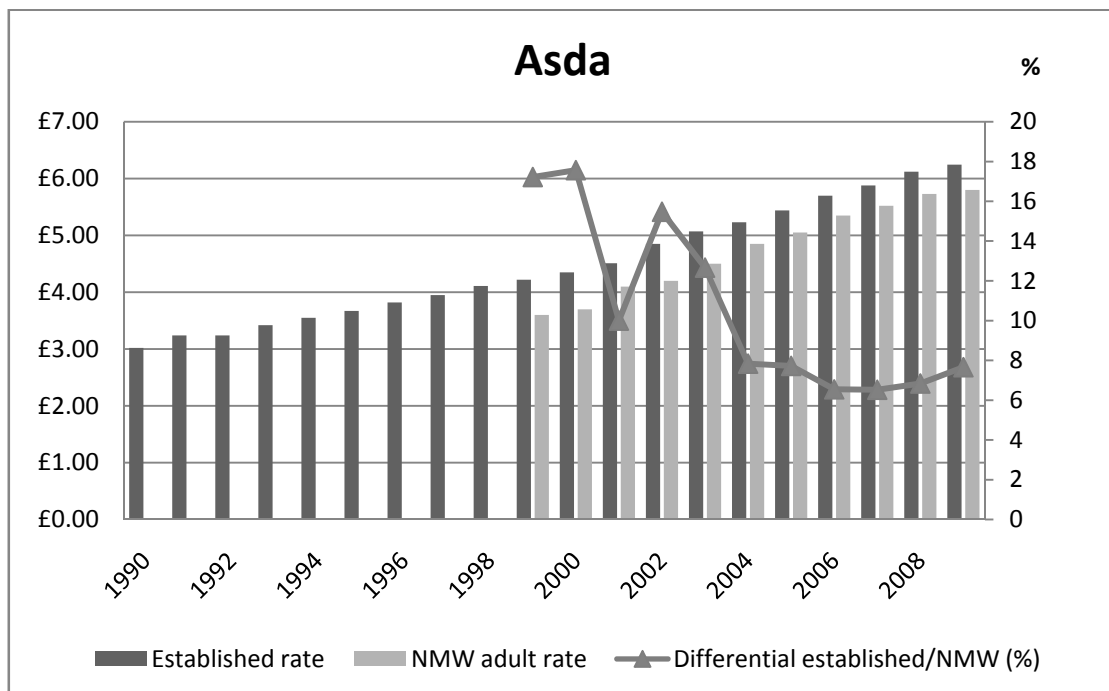
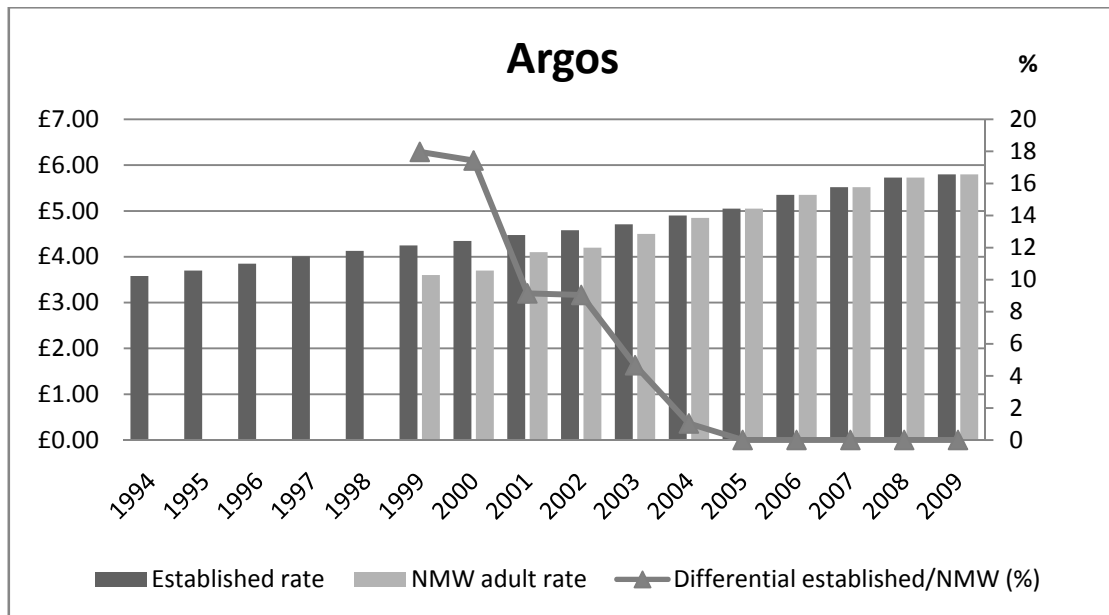
The charts over the following pages plot the difference between company pay rates and National Minimum Wage at the following organisations in the fast food, pubs and restaurants, retail, finance and public sectors as follows:

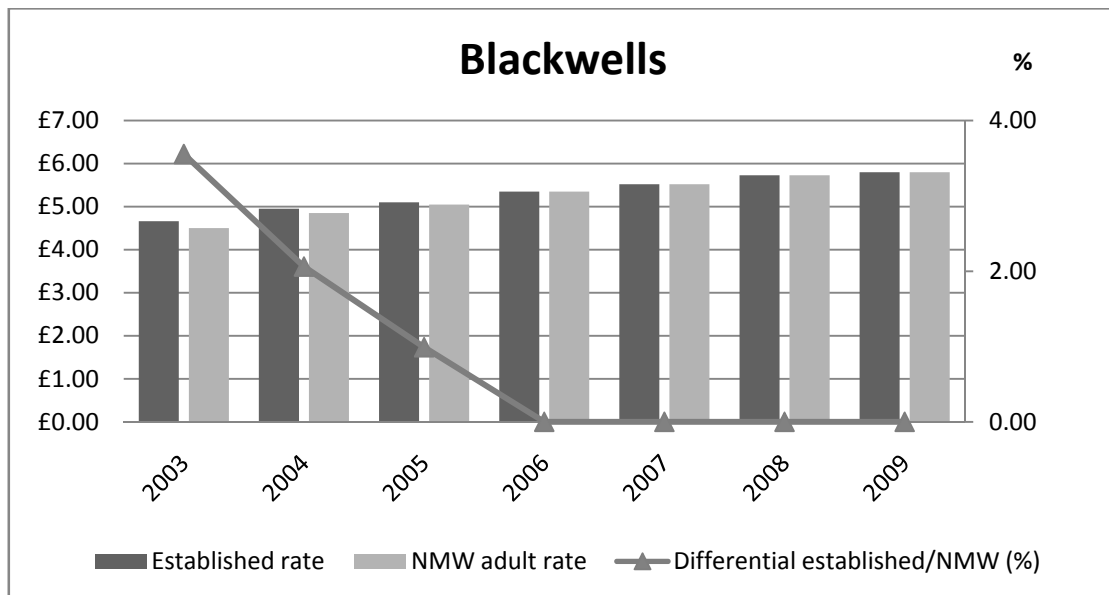
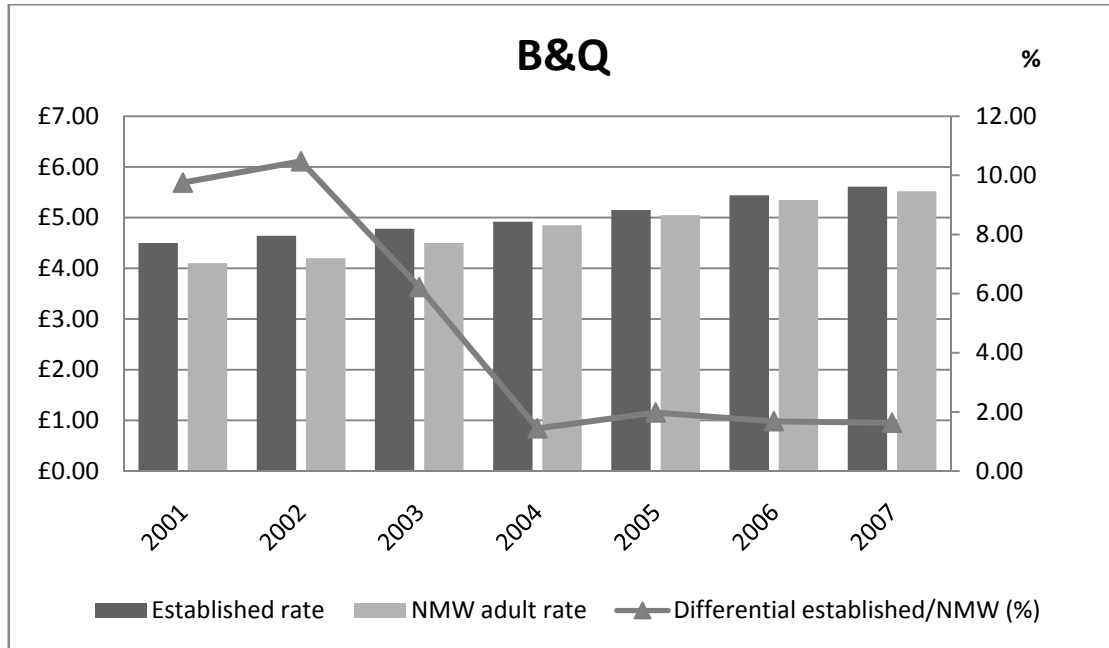
Organisations included in the time-series panel<sup>1</sup>

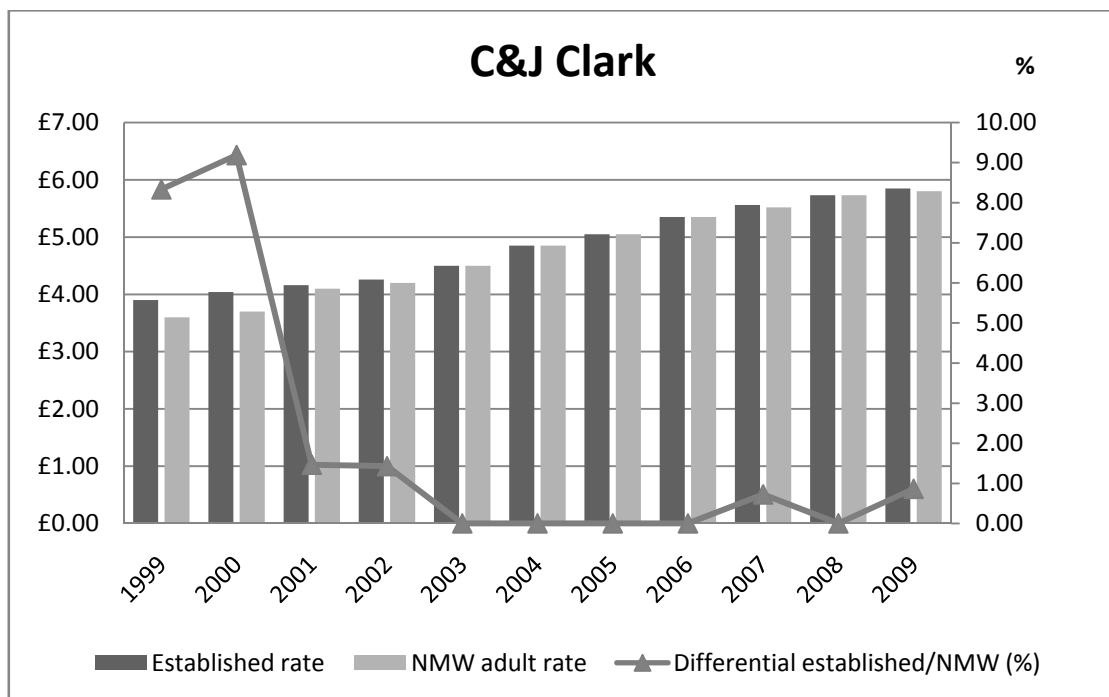
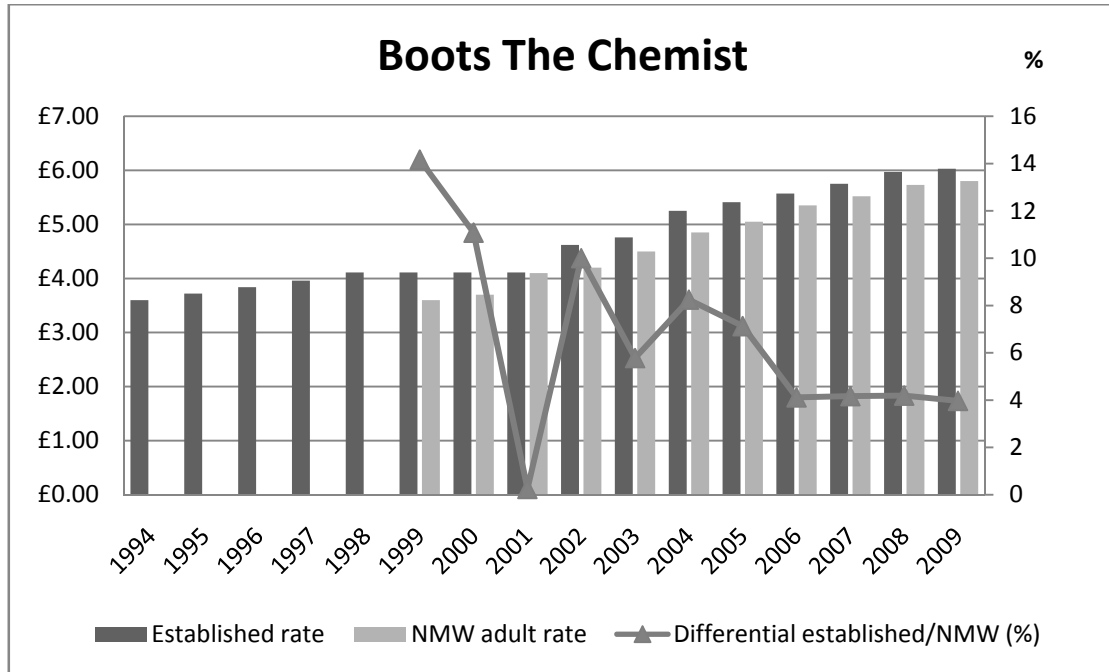
Low-paying sector organisations	
Argos	McDonald's
Asda	Mitchells & Butlers
B&Q	Next
Blackwells	Peacocks
Boots The Chemist	Pret A Manger
C&J Clark	Sainsbury's
Greggs	Schuh
Homebase	Selfridges
House of Fraser	Somerfield
Iceland	Tesco
KFC	Waitrose
Makro	Waterstone's
Marks & Spencer	Wilkinson
Marstons	
Financial services organisations	
Alliance & Leicester	First Direct
Barclays Bank	Lloyds TSB
Coventry Building Society	Nationwide
Public sector organisations	
Foreign & Commonwealth Office	Ministry of Defence
Highways Agency	NHS
Home Office	Scottish Prison Service
Local Government	

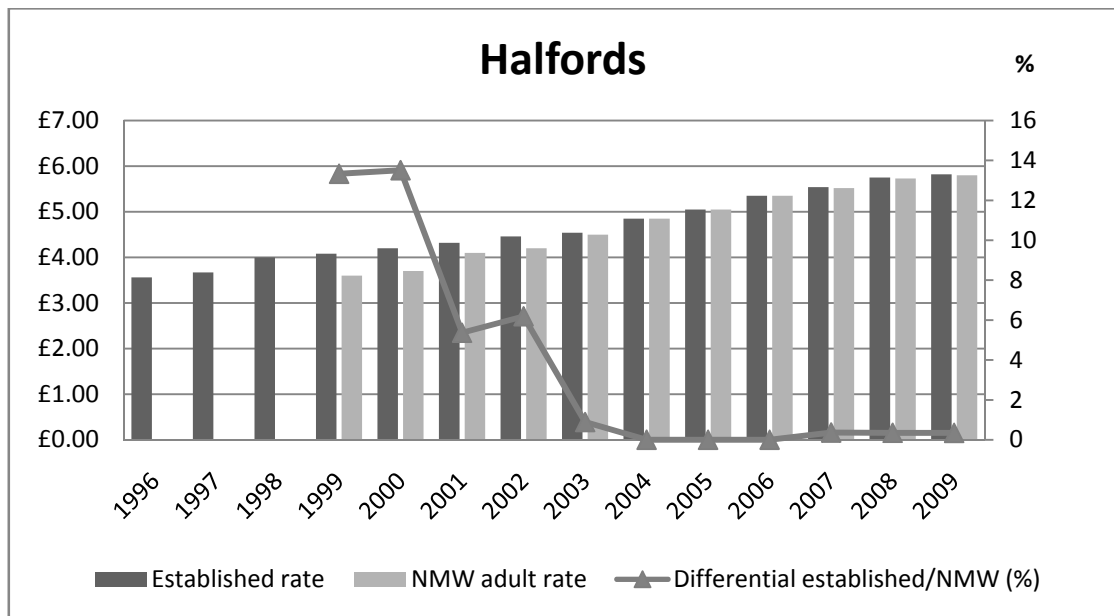
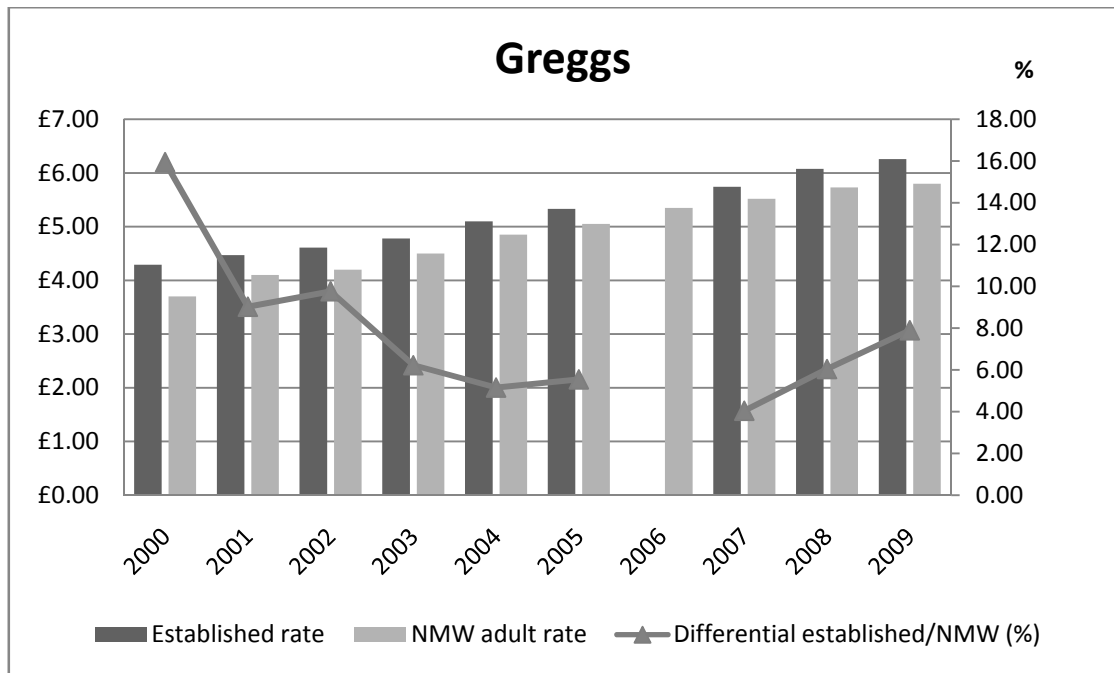
<sup>1</sup> Note: There are a few instances where pay data for the established role was not available.

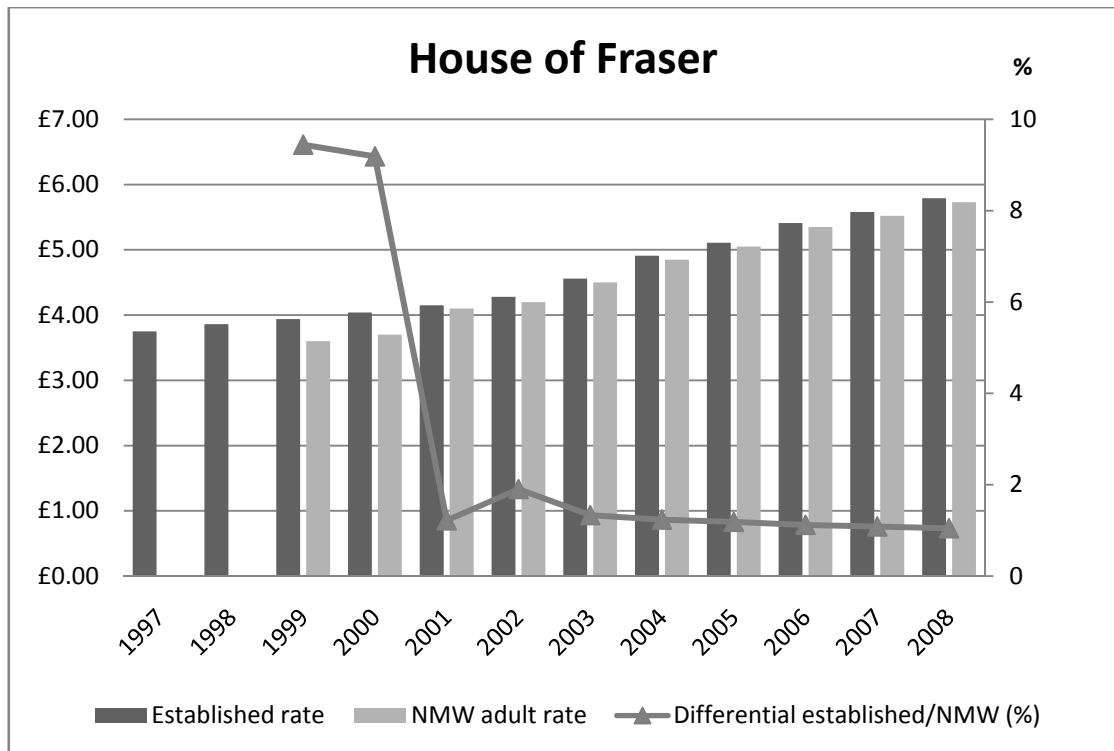
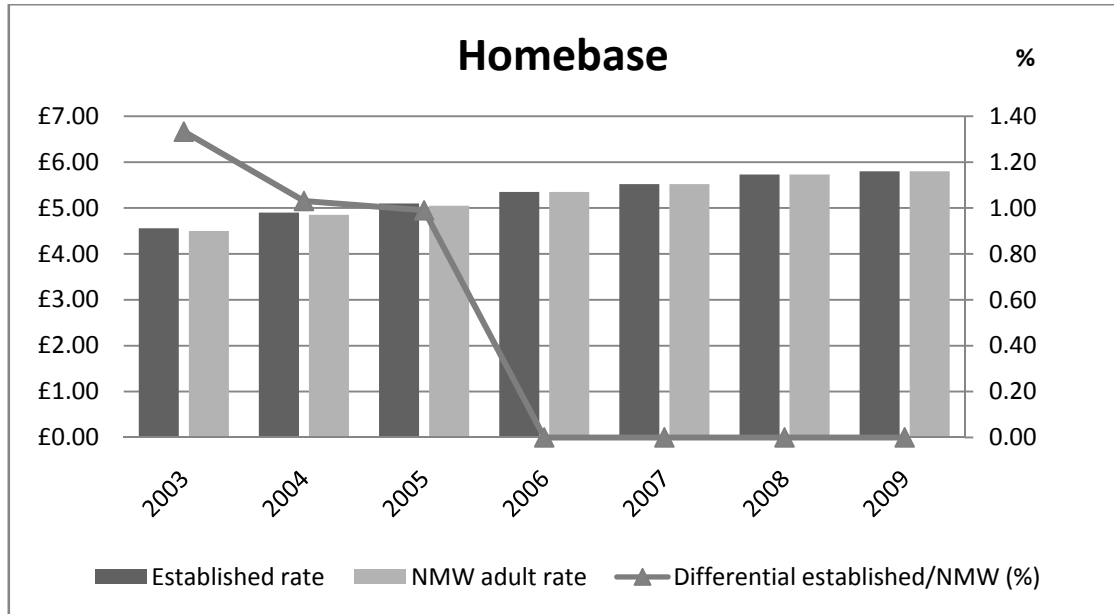
Low-paying sectors

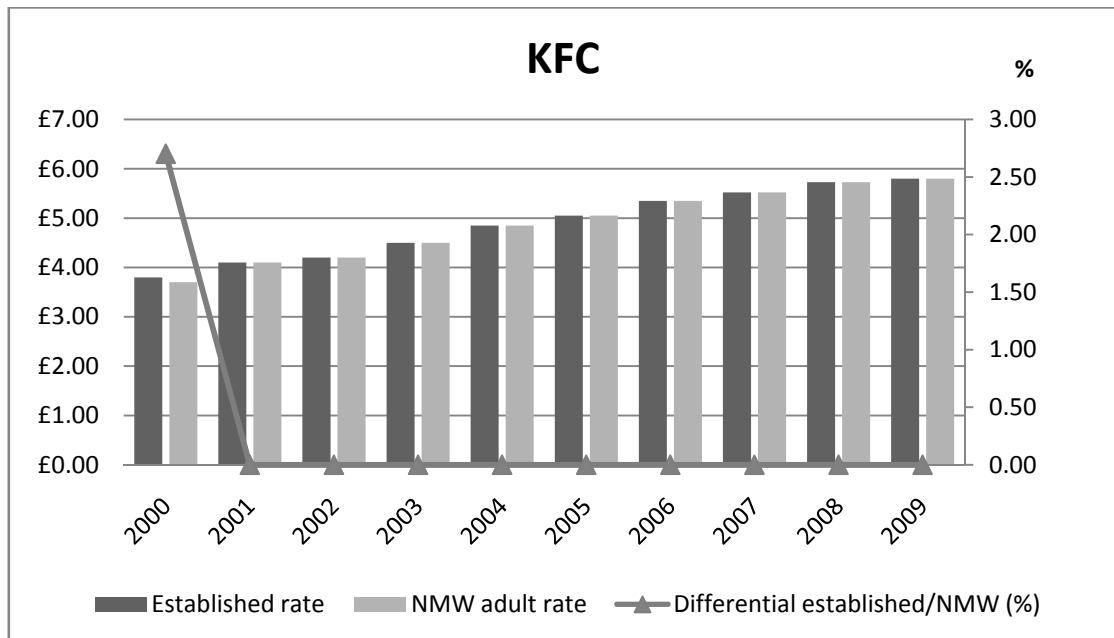
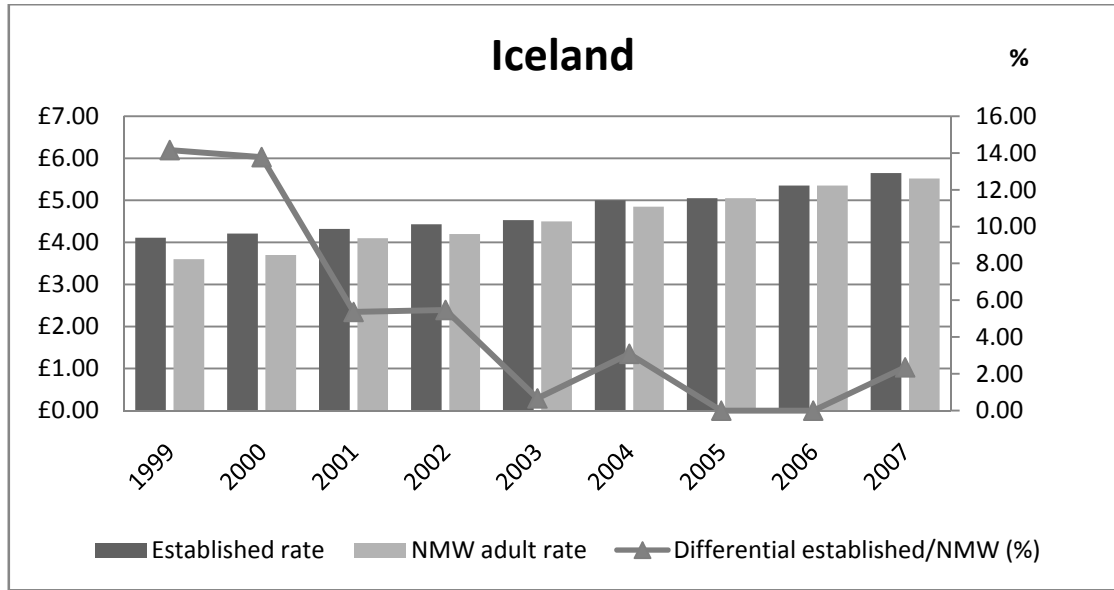


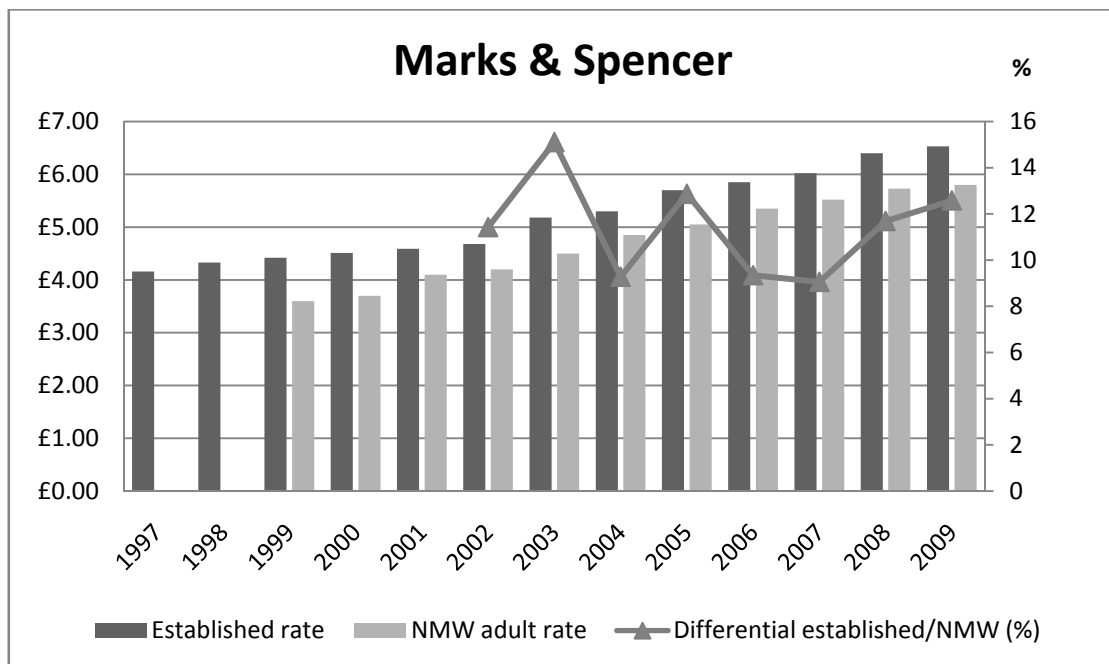
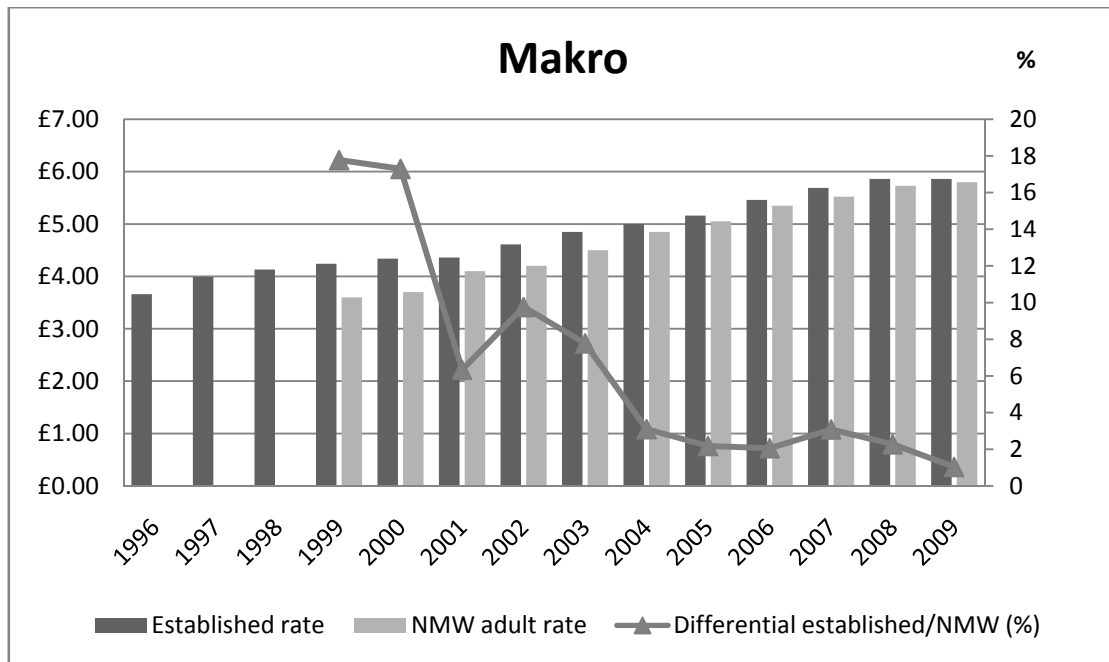


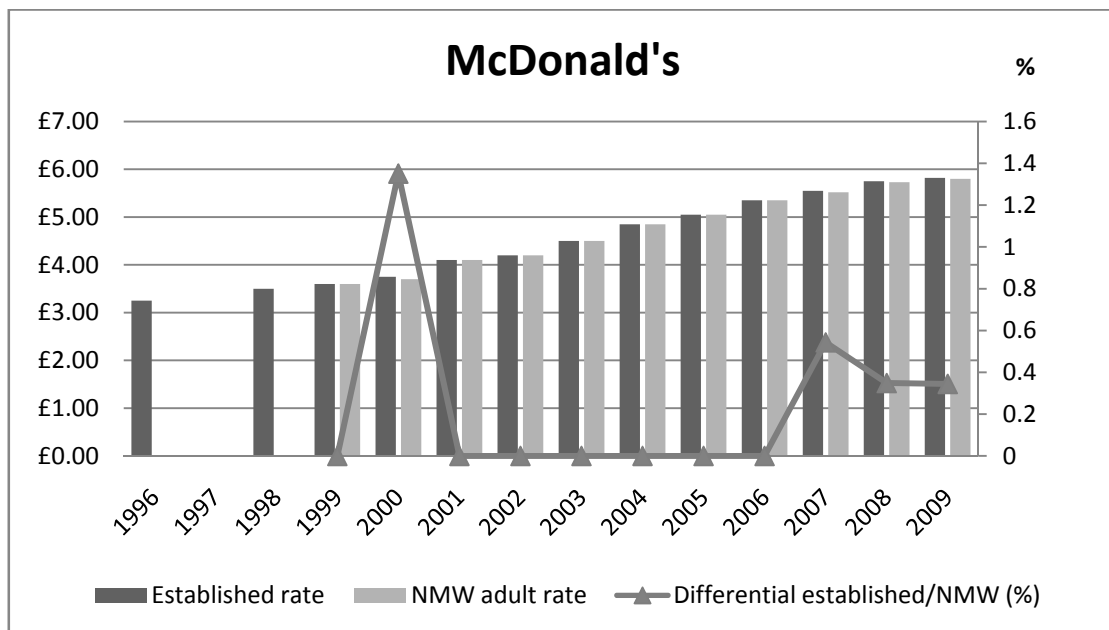
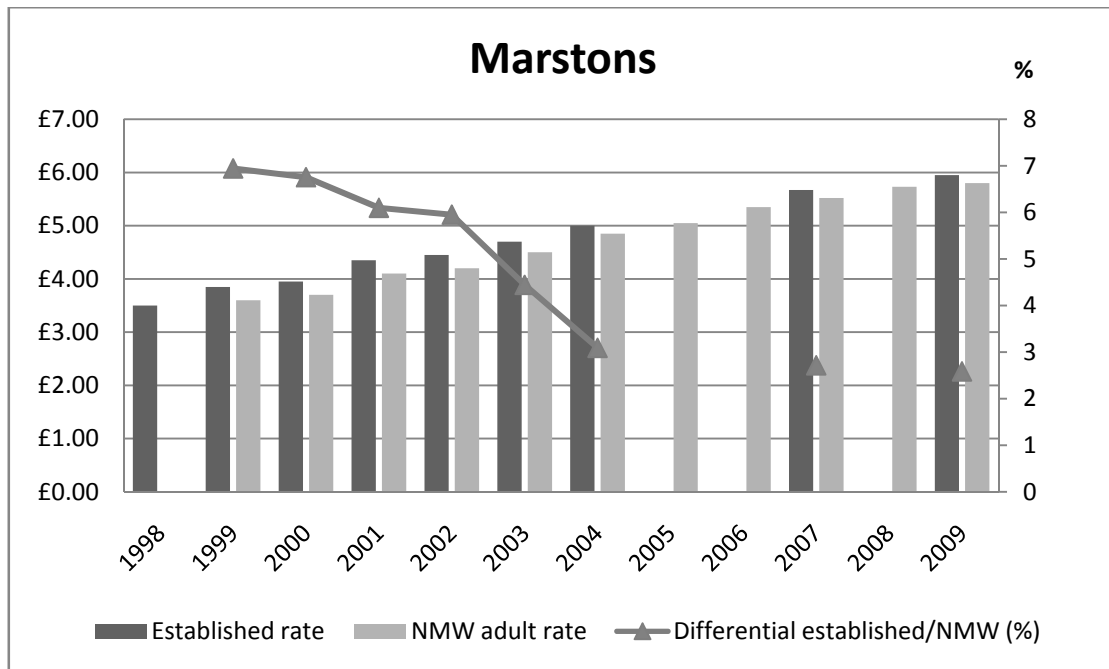


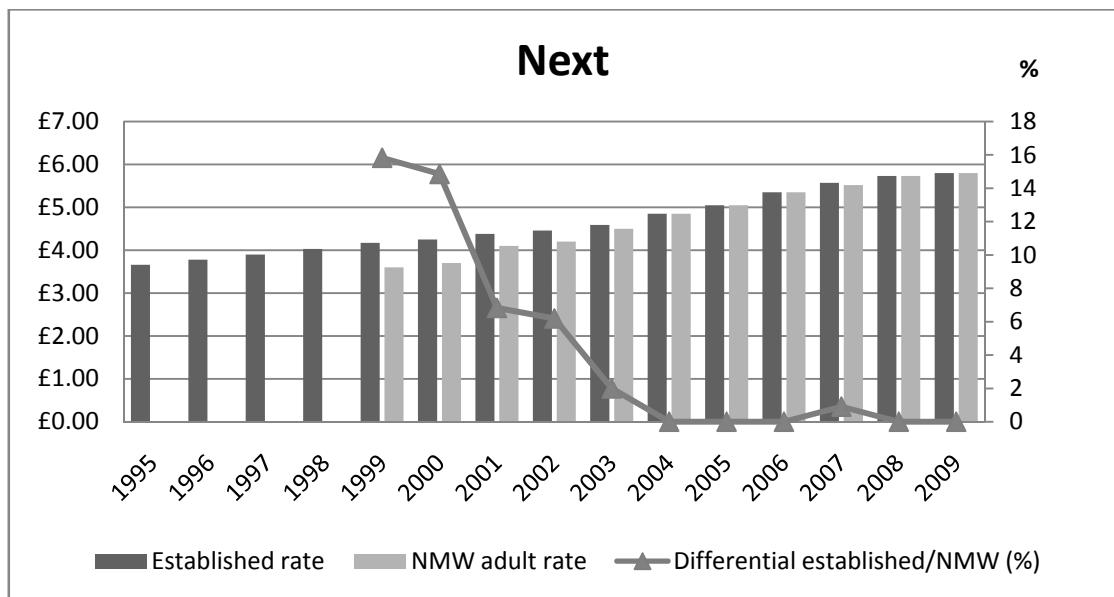
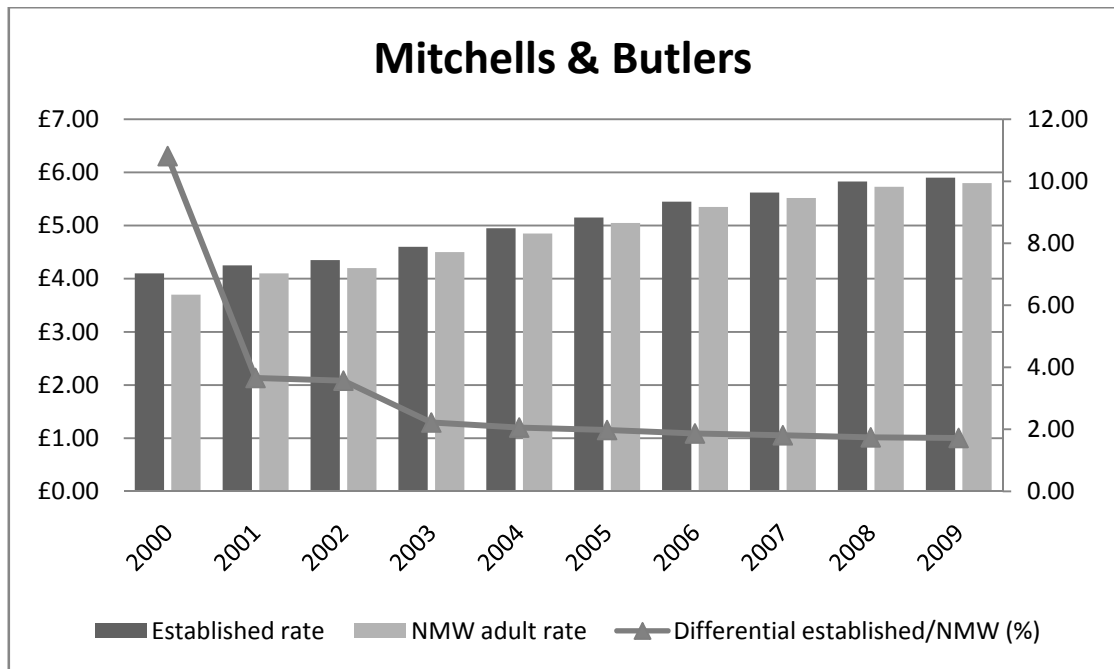


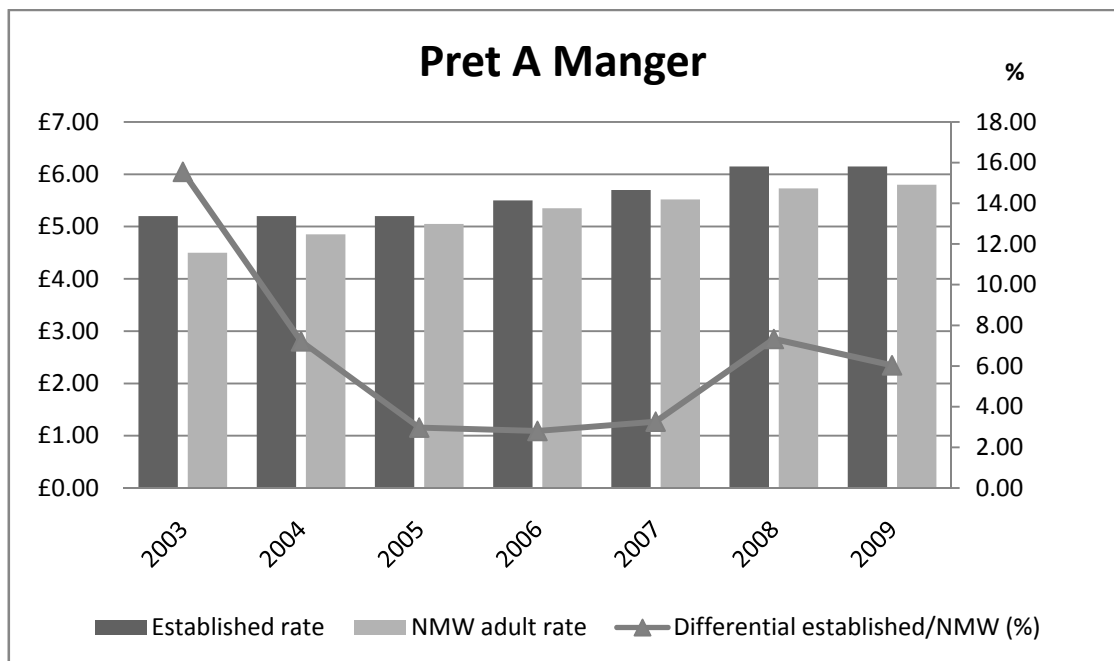
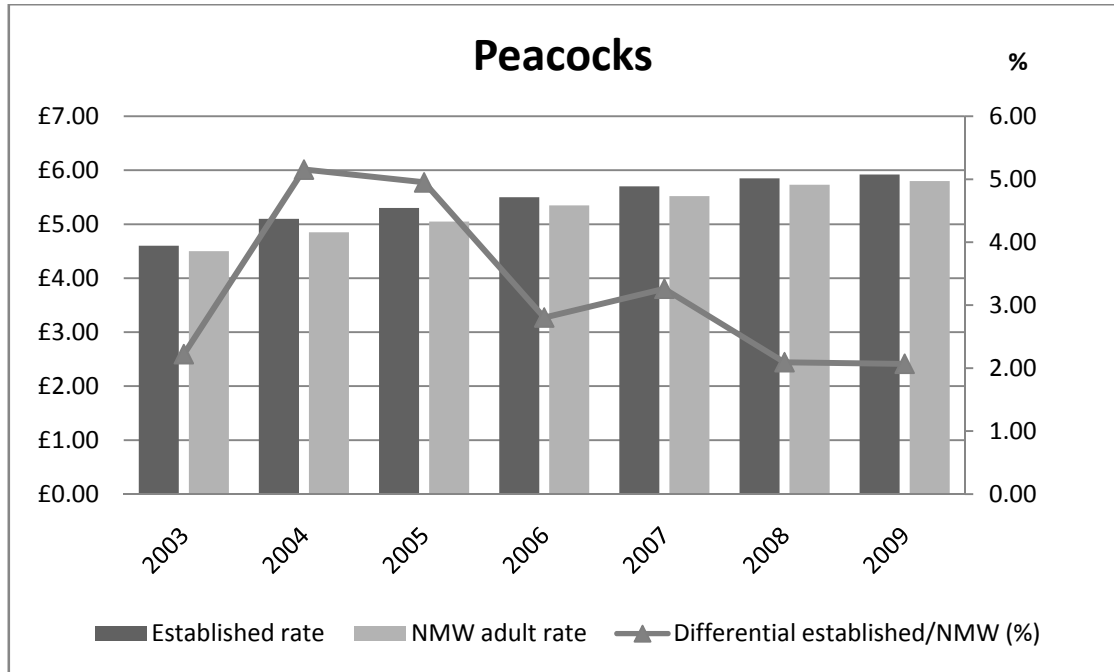


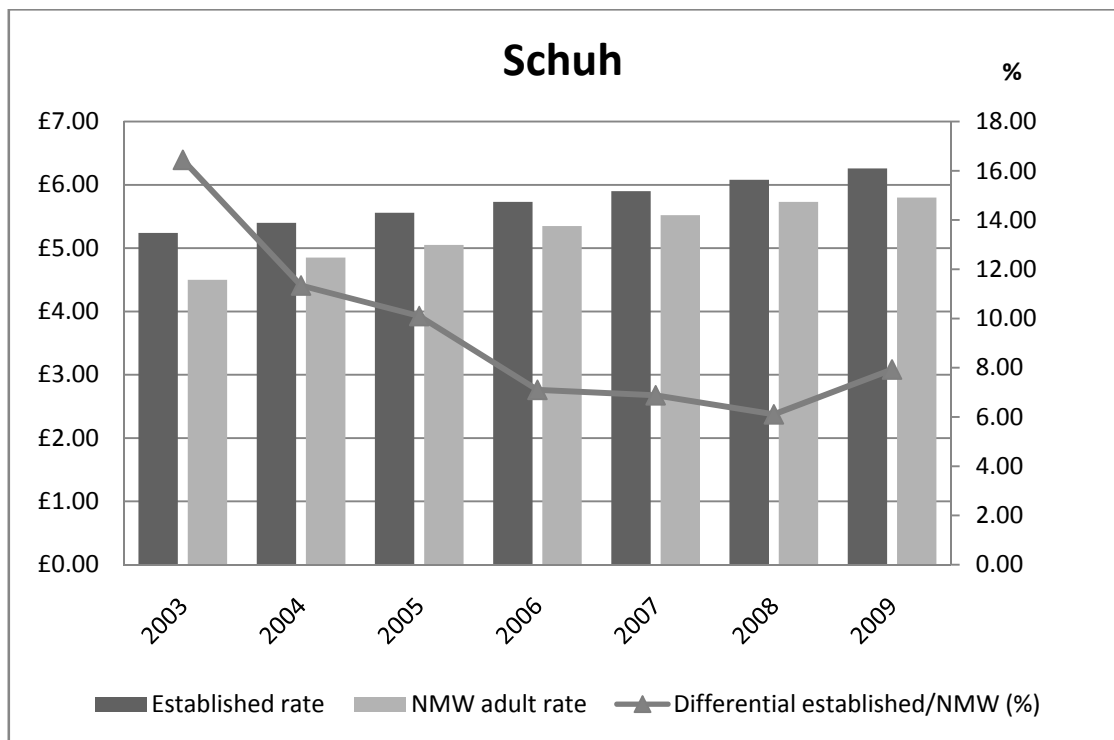
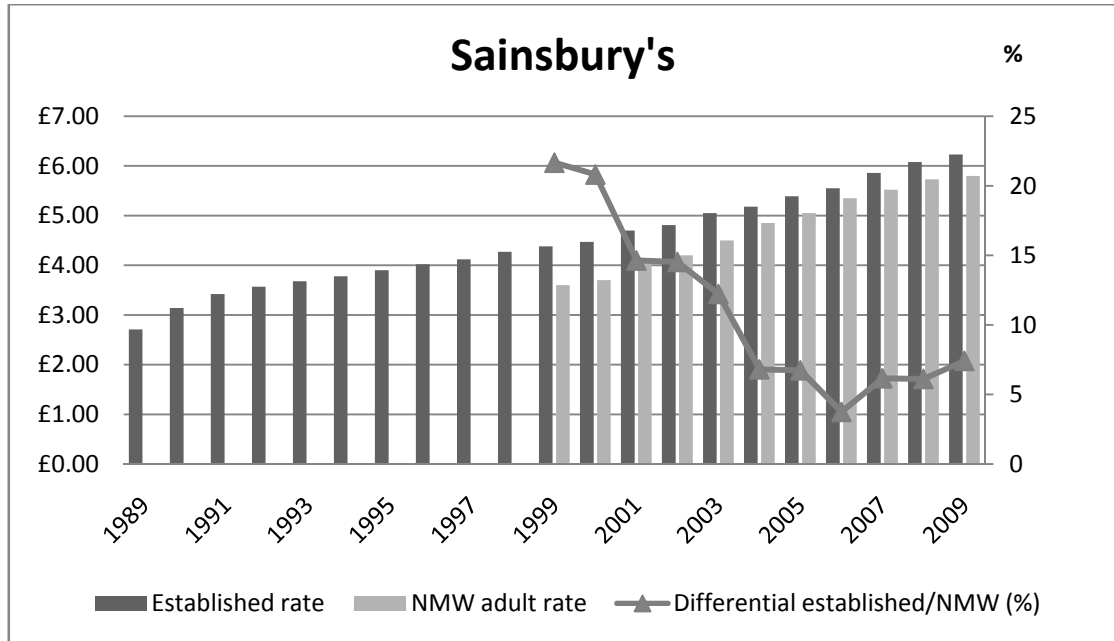


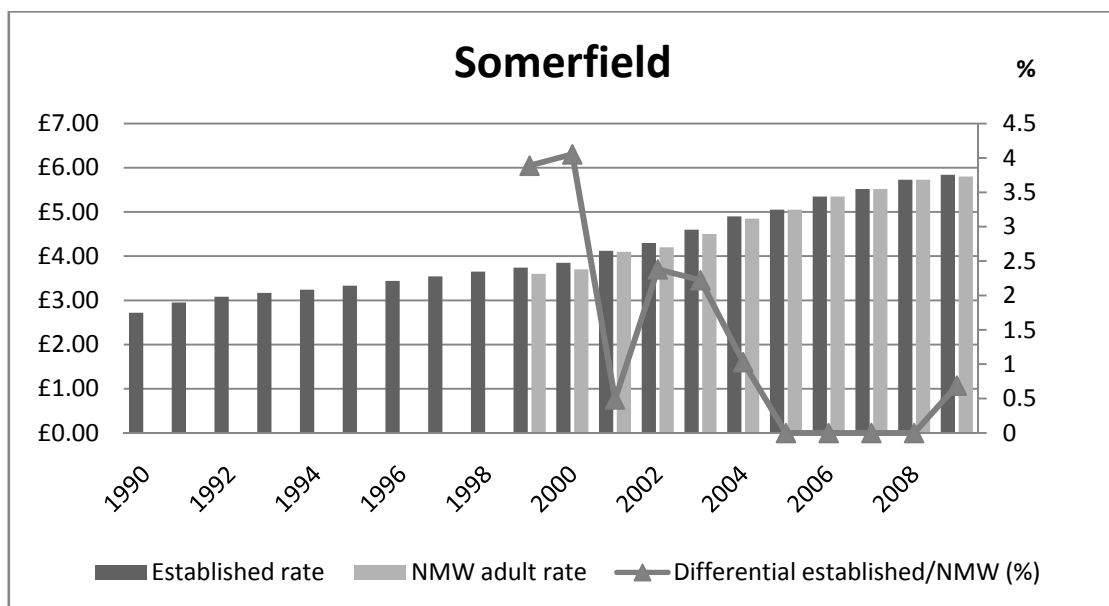
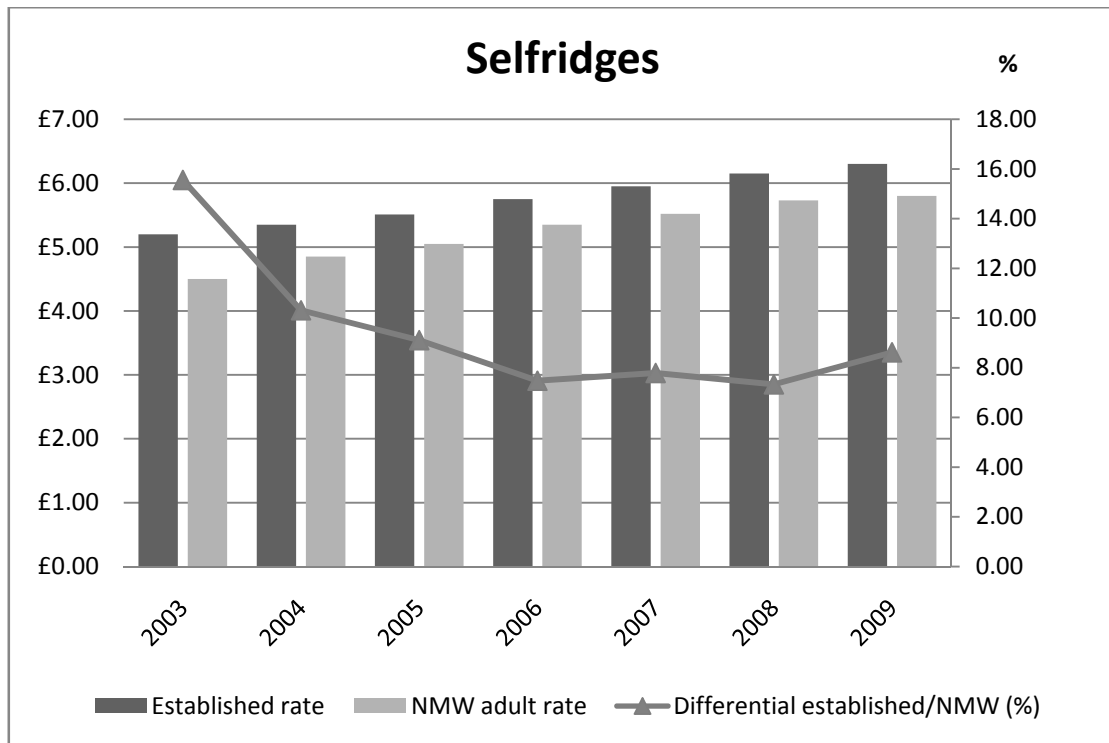


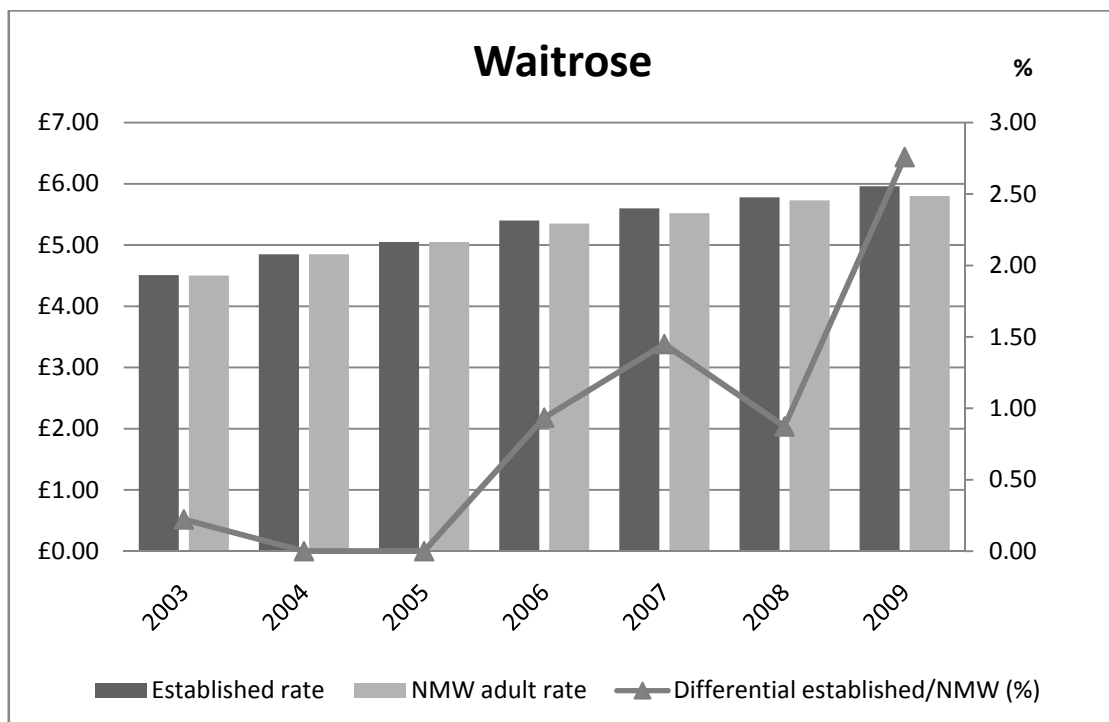
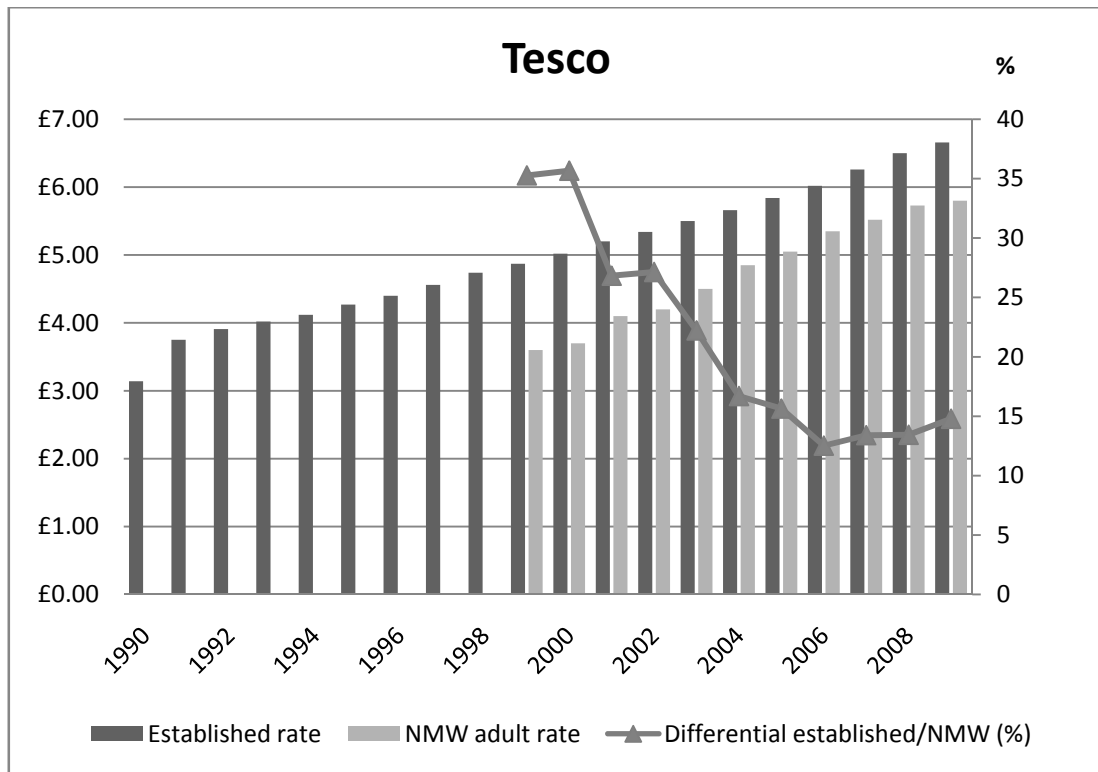


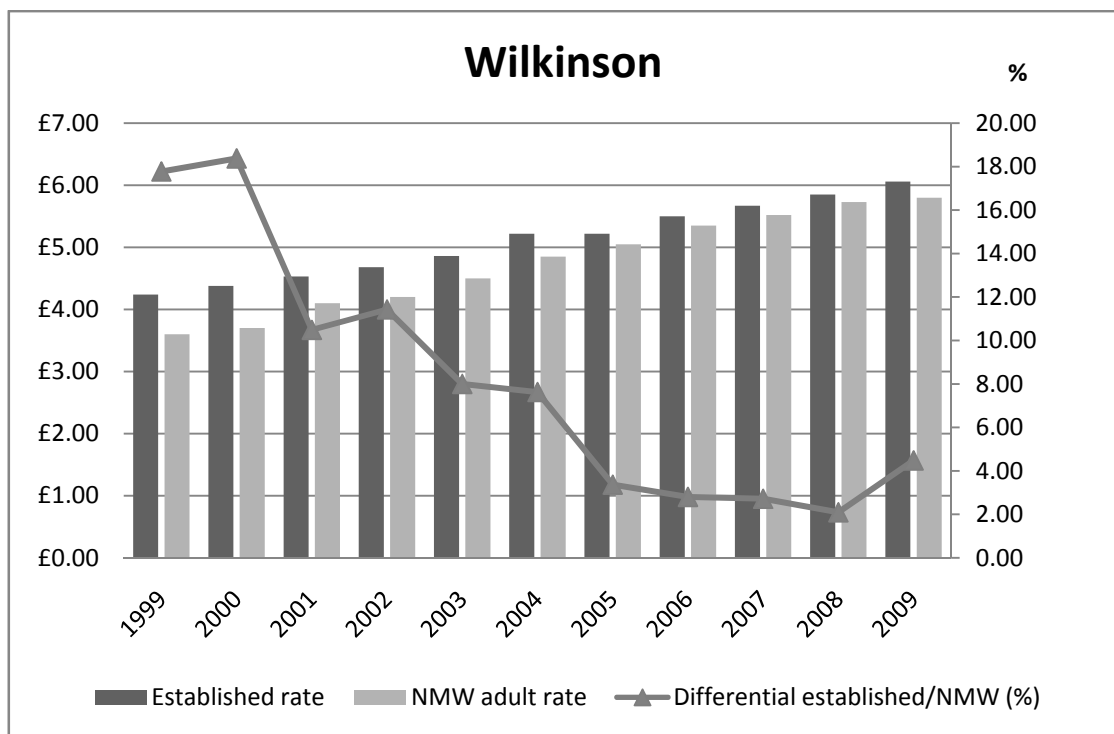
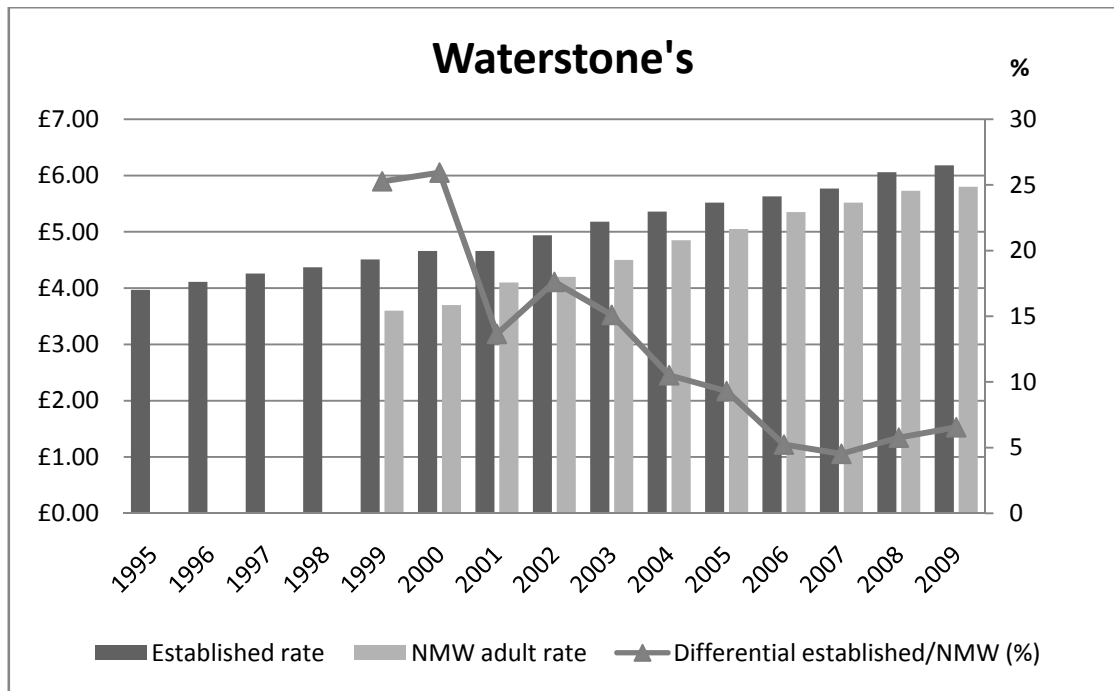




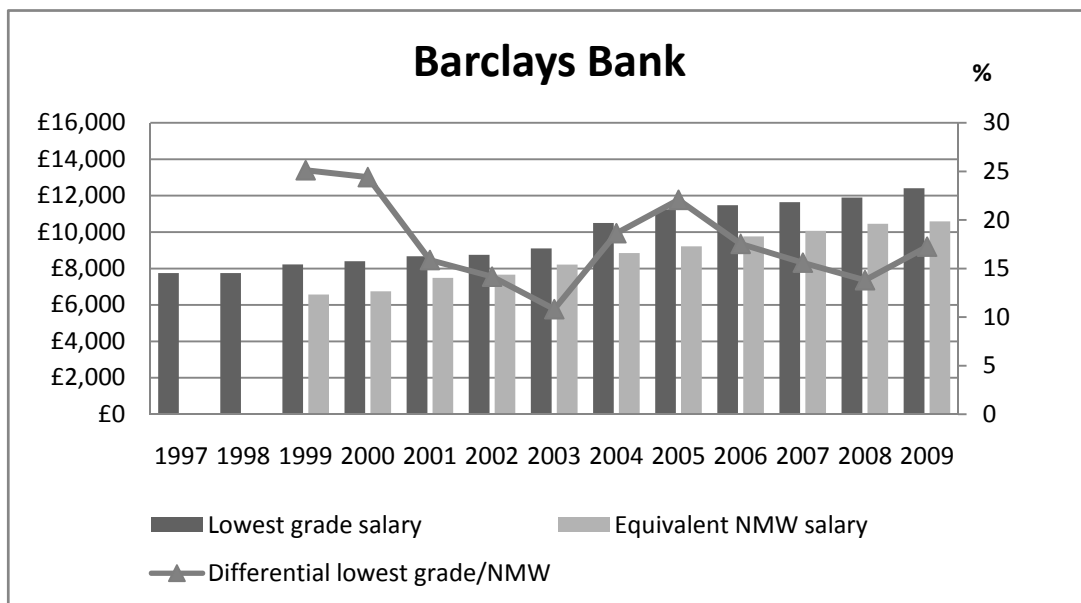
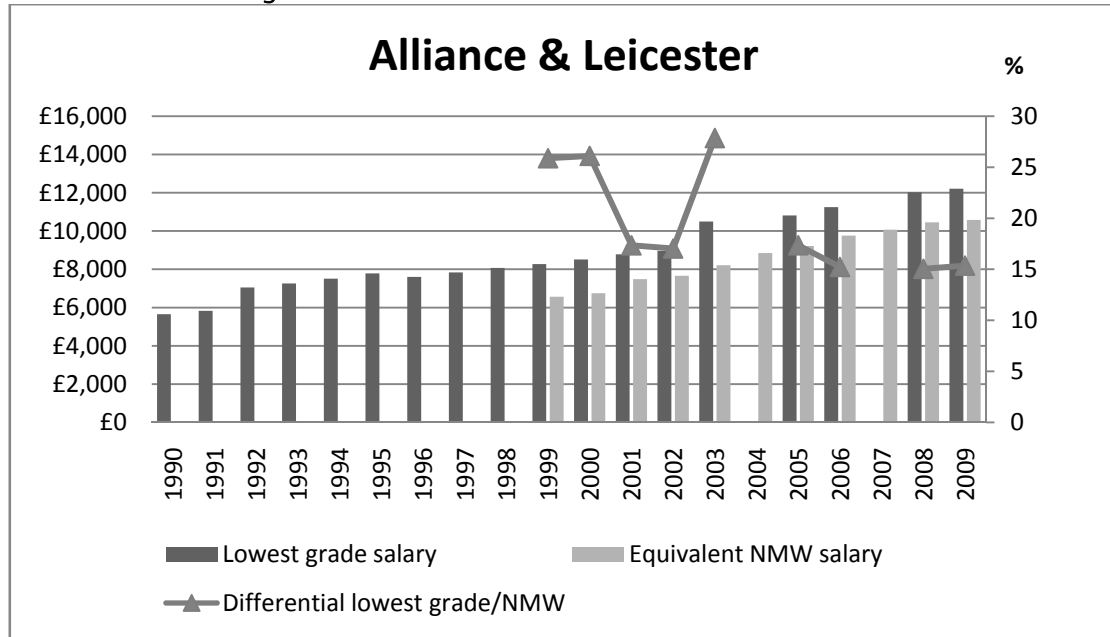


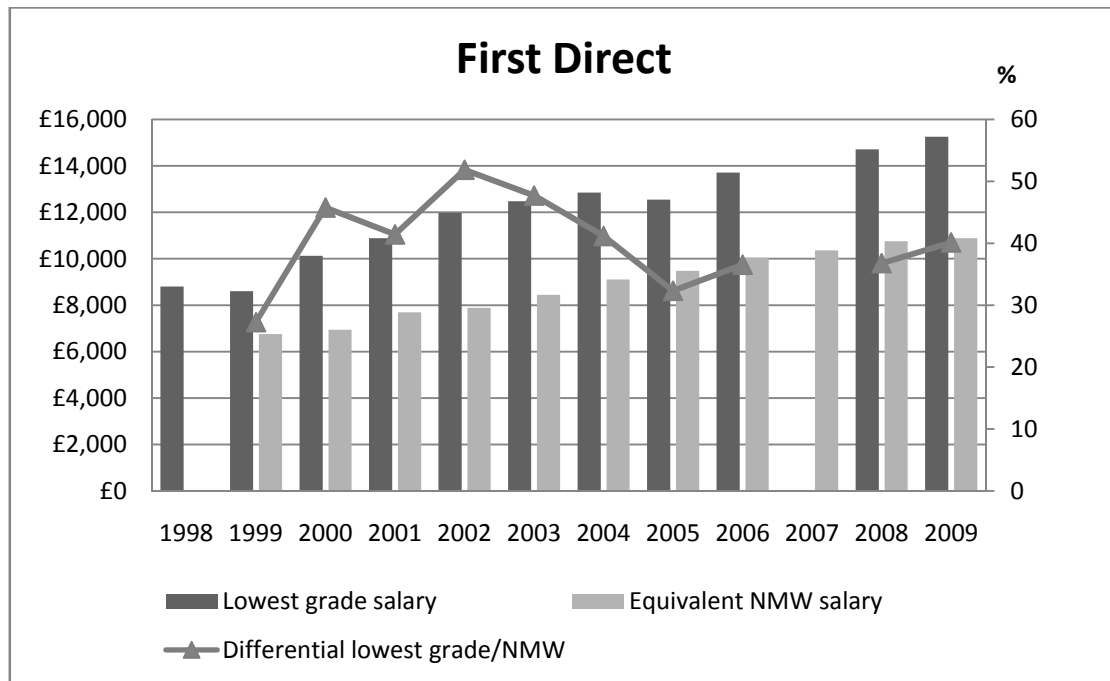
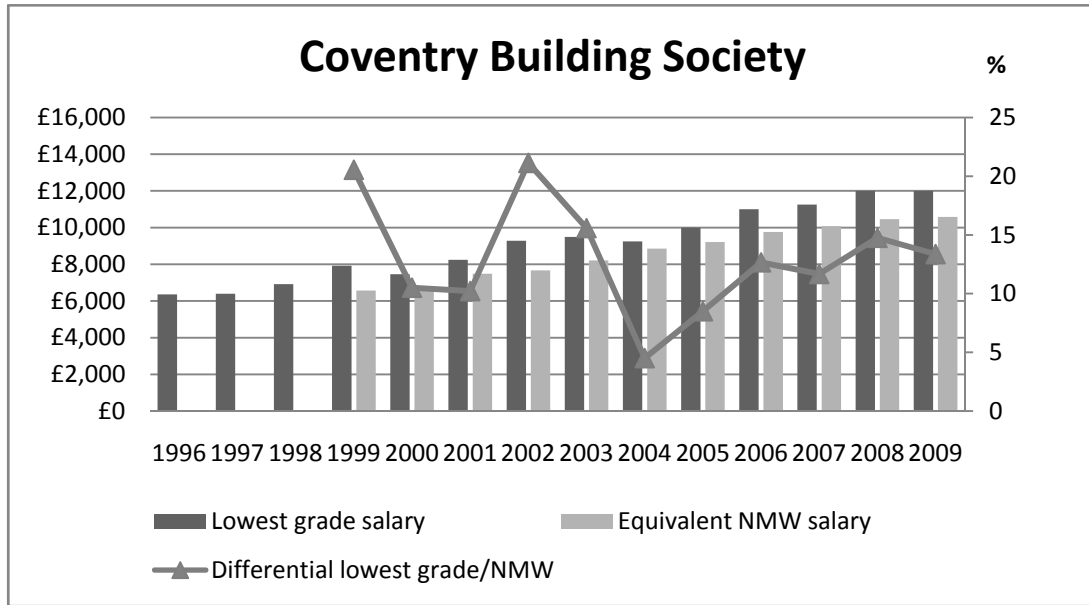


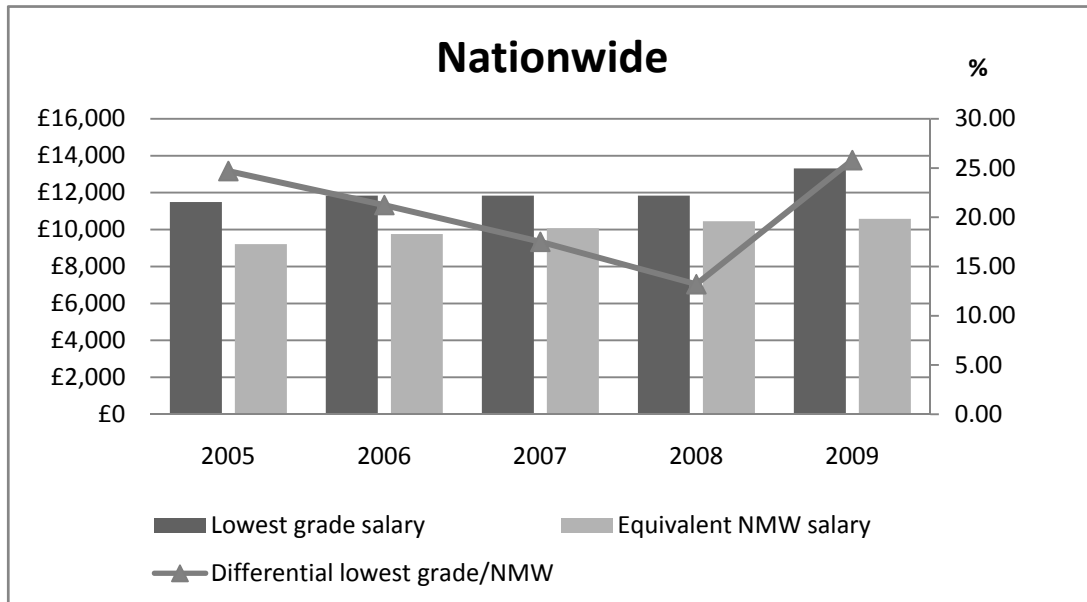
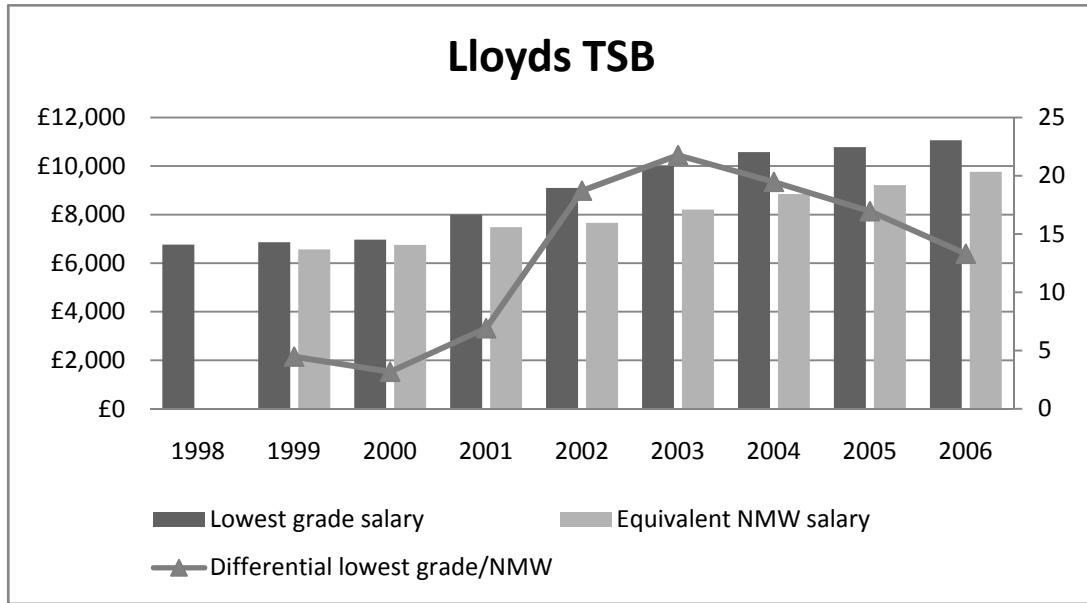




Financial services organisations







Public sector organisations

