

**QUALITATIVE RESEARCH ON FIRMS'
ADJUSTMENTS TO THE MINIMUM WAGE:
FINAL REPORT**

to the

Low Pay Commission

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The logo for 'irs research' features the letters 'irs' in a bold, red, lowercase serif font, followed by the word 'research' in a grey, lowercase sans-serif font. A thin black diagonal line is positioned above the 'i' in 'irs'.

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EXECUTIVE SUMMARY

In December 2003 IRS Research was commissioned by the Low Pay Commission (LPC) to undertake a qualitative study of firms affected by the national minimum wage (NMW). The research was conducted prior to the October 2004 upratings and the introduction of the rate for those aged under 18 but above compulsory school age.

The research was conducted among smaller businesses because recent work by IRS on the NMW, both before it was launched and since its introduction, has shown that larger firms are having relatively few problems dealing with the minimum wage or increases to it. IRS therefore conducted in-depth, face-to-face interviews with four employers' associations and the TUC, as well as 53 interviews with employers.

The research is designed to assess how firms have responded to, and coped with, recent increases in the minimum wage and provides a detailed picture of the actions firms have taken and plan to take as a result of increases to the minimum wage, covering the effect on their:

- Pricing decisions;
- Levels of profitability;
- Staffing and workforce planning;
- Productivity; and
- Training.

Methodology

The core sampling framework for this project was derived from the need to gather data with sufficient validity within the initial project parameters. Following a review of past research and associated literature, IRS selected industrial sector, region and company size as the three factors that warranted specific inclusion within the sampling schedule.

Industrial sectors initially selected for inclusion within this study were:

- Cleaning/facilities management;
- Catering/food processing;

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- Security;
 - Packing/distribution;
 - Hospitality;
 - Hairdressing;
 - Construction;
 - Retail; and
 - Small office based companies.

IRS used a three-stage process to ensure an effective sample of employers was obtained for this project:

- Face-to-face, in-depth interviews with four employer associations and the TUC;
- Mailing 4,000 short questionnaires to small business, seeking their views of the NMW and its impact on their business; and
- Semi-structured, face-to-face, depth interviews with employers.

Findings from the employer survey

IRS Research surveyed 4,000 small businesses in the UK. This aspect of the fieldwork was designed to assess the extent to which sectoral and regional factors were impacting on firms' assessment of the NMW. In addition, the survey was also used as the basis for identifying possible organisations to interview for the main part of this study.

The questionnaire asked employers if the NMW had affected pay, profits, employment and training, by stating 'Yes', 'No' or 'Don't know'. In addition, the questionnaire gave employers the opportunity to give some qualitative feedback of their experiences of the NMW.

In total, IRS Research received 265 responses to the questionnaire. Almost three in five employers (58.5 per cent) reported that the NMW had affected pay levels, with a similar figure (54.3 per cent) reporting an effect on profits. A smaller proportion reported that the NMW had impacted on their firm's employment levels (35.8 per cent) and training (22.6 per cent).

Findings from the face-to-face interviews

The employers interviewed for this project were generally positive about the introduction and need for a national minimum wage. Respondents spoke of it being fair that people should receive a 'decent wage' and remarked that it had helped to deal with 'rogue' employers.

A number of employers noted that the NMW had formalised the employment arrangements and wages in their locality and sector and some respondents reported that the practice of paying 'cash-in-hand' had decreased since the introduction of the NMW.

However, many employers were critical of the government's intervention in the labour market by setting wage levels. Those employers felt that they should be allowed the freedom to set wages that were commensurate to their employees' 'worth'. In addition, employers felt the NMW did not take into account regional, sub-regional or even sectoral factors.

Knowledge of rates

Overall, the vast majority of employers knew the current adult rate, as well as the planned increase in October 2004. However, employers' knowledge of development rates, how and when they could be used and the 16- to 17-year-old rate planned for 2004 was somewhat limited.

Finding out about the national minimum wage

Employers received information on the minimum wage and a range of other employment issues (such as changes to maternity and paternity rights, and entitlement to paid holidays) from a number of sources. Typically, respondents were finding this information out for themselves from their professional and trade bodies, the Inland Revenue, the national press, sector-specific publications or their accountants or bank.

The research highlighted that some employers would prefer to be formally notified of changes to the NMW directly from a government source – for example, an Inland Revenue flyer giving the rates and implementation dates as soon as these had been decided.

Increases to the NMW

Despite the largely positive view taken by employers of the NMW, a large proportion were unhappy with what they saw as arbitrary and substantial upratings to the rate in 2003, as well as that due in October 2004.

Employers mentioned that the increase to the rate outstripped inflation and average earnings increases, as well as the increases they could make to the prices they charged for their products and services. As a result, these employers reported that NMW increases were seriously damaging the profitability of their business. These employers were also concerned that another increase in 2005 similar to that planned for October 2004 (ie of 35p per hour) would be difficult to accommodate.

Notice of upratings to the NMW

Employers were generally happy with the amount of notice they received of planned increases to the minimum wage. The advance notice of upratings was considered useful, as it allowed businesses to plan budgets and prices well in advance of the changes in pay rates.

Working Tax Credits

About ten employers mentioned encountering problems with the Working Tax Credits (WTC). Where this occurred, staff were refusing to work extra hours. However, the extent to which this was a WTC–benefits issue, or a work-life balance or home responsibilities issue, was difficult for some employers to ascertain.

Employers' coping strategies

Employers reported using a variety of different ways to cope with the increases to the national minimum wage and other changes to employment legislation that had impacted on their businesses.

However, employers were unable categorically to state that their actions or 'coping strategies' were as a direct result of the NMW. Employers found it difficult to take the NMW in isolation, given that

legal changes in the past five years – such as entitlement to paid holidays, improved maternity and paternity rights and increases to NI contributions – had also impacted on their businesses at the same time.

Some employers had tried a number of different ways of dealing with the NMW and reducing their costs by looking at productivity, changing suppliers or diversifying into new areas. However, for the most part, the employers in this study spoke of operating with the minimum number of staff they possibly could or said that because of the nature of the work carried out by their staff productivity could not be improved by investing in new machine or changing working practices.

Changes to wages and pay structures

The introduction of the NMW impacted on all but six businesses interviewed for this research – a construction company in the South East, a specialist cleaning company in the North West, a business travel agency in the North East, a high street travel agency in the North East, a training company in Scotland and a food processing company in Wales.

Ten employers reported paying in excess of the NMW for all staff when it was introduced and 17 now paid in excess of the current rate to all staff. Where this was occurring, these employers were typically using wages as a means of tackling staff shortages or of attracting what they described as 'better-quality' staff.

Six employers made changes to their pay scales and structures – for example, consolidating bonuses into hourly rates, reducing the number of pay scales or introducing a flat rate for all staff of a certain type.

The introduction of the NMW in 1999 had a limited impact on pay differentials in the organisations involved in this study. However, recent upgrades to the rate, as well as that proposed for October 2004 are causing employers concern.

In total, 12 employers reported that the NMW had impacted on their organisation's pay differentials in recent years. Employers reported that staff being paid well above the minimum wage when it was introduced in 1999 were now beginning to see their differentials eroded by either lower-skilled or less experienced staff.

Reducing hours

Nine employers reported that they had cut the number of hours their staff were working. This typically involved employers in the hospitality sector letting staff leave early if there was no work for them to do during less busy periods.

Increasing prices

The ability of businesses in this study to increase their prices to offset the introduction of, and increases to the NMW was limited by some sectoral, regional or competitive factors. Fourteen employers had increased their prices over the past two to three years, but this was not a 'coping strategy' in dealing with the NMW or other business pressures, but an annual activity to cover some of the increase in input costs to the businesses.

However, employers reported that where they were able to increase prices, this did not cover the full costs of increases caused by the NMW and other legislation.

A small number of employers, typically those in the business-to-business sector, were not able to pass on any increased costs – be they wage or other input costs, such as raw materials – to their customers. As a result, these employers were expected to absorb the costs of the NMW and other employment legislation.

Reducing profits

The increases to labour costs as a result of changes in the NMW and other employment legislation, as well as the inability of employers to recover the full costs of the increases, gave them only a few other options for coping with the NMW.

Twenty employers spoke of the direct impact the NMW has had on their organisation's profits. These firms tended to be larger employers – typically employing 40 or more staff.

Reducing employment levels

Ten organisations interviewed had reduced staffing levels as a result of the NMW and other changes to employment law. Where employers were operating with fewer staff, this typically occurred where

employees left the firm and were not replaced. In one sector in particular, hairdressing, respondents were either reluctant to hire young staff or trainees overall, or had cut down on the numbers of trainees they had taken on in recent years. This trend was also seen, to a lesser extent, within the travel sector.

Conclusions

Organisation variables, such as ownership structure or size did not impact on employers' coping strategies or their ability to deal with the NMW or increases to the rates in this study. In addition, regional factors had little impact on employers' coping strategies. However, sub-regional factors, particularly the extent to which firms in urban and/or metropolitan areas were better placed to deal with the NMW, were reported by employers as having an effect.

The majority of firms in this study that were encountering difficulties with the NMW and had made changes to how their business operated revealed that they could not operate with fewer staff or introduce any mechanisation that could further improve productivity. The coping options available to these firms when dealing with the NMW were to increase prices to recoup some of the costs of the NMW and/or to accept reductions in their organisation's levels of profitability.

There was some evidence that sectoral factors affected employers' views and coping strategies when dealing with the NMW in the hairdressing and travel sectors (by reducing the number and age of trainees it was employing). However, there were no other common sectoral coping strategies used by the employers in this study. It is noticeable that the hairdressing sector is reacting to the NMW by reducing the number of trainees it is prepared to hire, as well as limiting these training opportunities typically to 16- and 17-year-olds only.

While employers expect that the NMW will continue to increase year on year, many suggested that future increases to the rate should be linked to inflation. Given that a high proportion of employers were increasing their prices each year to cover inflation, it is likely that future increases to the NMW at this rate would be less likely to harm these employers' profitability in the future.

The environment into which the NMW has been introduced is important. Since 1999, the UK economy has continued to perform well. Economic growth has ranged between 1.8 per cent and 3.9 per cent of GDP per year (1999 - 2003) despite the significant changes seen globally in that same time period. The unemployment rate now stands at 4.7 per cent - down from 6.1 per cent in 1999 – low by the standards of the preceding two decades. It is in this overall economic environment within which the effects of the NMW on businesses has to be judged.

This is perhaps particularly relevant to the low-paying sectors chosen for this study. It is likely that the majority of the firms interviewed for this research were, prior to the introduction of the NMW, operating low-cost low-wage business models (prior to the introduction of the NMW, only ten employers reported that they were paying above the NMW in 1999). While some commentators suggest it is important that the UK economy is based on high-wage high-skill jobs, and that the NMW could be increased in order to force low-skill low-pay organisations into higher-paid higher-skilled sectors, the sudden removal of low-paying occupations and sectors could have a dramatic effect on the low-skilled, deprived communities and ultimately the tax and benefits system.

1. LITERATURE REVIEW

Since its introduction in April 1999, the national minimum wage (NMW) has rapidly established itself within the economy. The concept and operation of the minimum wage is now broadly accepted by employers, employees, trade unions and most other interested parties. A 2002 IRS survey found that around four-fifths of employers now support the idea of the national minimum wage.¹ Accordingly, the debate has moved on to consider how the NMW should evolve. Increases in minimum rates of pay, age restrictions, accommodation offsets and enforcement have been brought to the fore by new government regulations and judicial decisions. Underlying all of these developments is a consensus that future changes to the national minimum wage must be based on a solid understanding of its operation and impact.

The environment into which the NMW has been introduced is important. Since 1999, the UK economy has continued to perform well. Economic growth has ranged between 1.8 per cent and 3.9 per cent of GDP per year (1999 - 2003) despite the significant changes seen globally in that same time period². This performance is all the more impressive when measured against many of the UK's international competitors. Employment has also held up well in the UK. The unemployment rate now stands at 4.7 per cent - down from 6.1 per cent in 1999. This rate of unemployment is low by the standards of the preceding two decades. It is in this overall economic environment within which the effects of the NMW on businesses has to be judged.

The impact of the NMW on small businesses is of particular concern to the government, employers' organisations and academics. For the UK private sector including public corporations and nationalised bodies, two in five employees (41.7 per cent) work in organisations with fewer than 100 people (excluding those with no employees). Combined, small and medium sized businesses account for more than two fifths of turnover (41.7 per cent) and over half of employment (51.4 per cent) in the private sector.³

¹ IRS (2002). 'Floor covering: the minimum wage survey', IRS Employment Review 750.

² HM Treasury. Pocket Databank, 7th September 2004.

³ Small Business Service (2004). SME Statistics UK 2003.

Indeed, in 2001 the government specifically asked the Low Pay Commission to commission rolling research on the impact of the minimum wage, and the various increases to the rate, on business as a whole and on small businesses in particular.

The review set out below attempts to summarise the state of research, and viewpoints expressed, concerning small businesses and the NMW.

At present, the NMW adult rate stands at £4.50 per hour for employees aged 22 and over. At the time of introduction in 1999 the NMW adult rate was £3.60. Although the initial rate managed to raise the wages of 1.3 million workers⁴, it was at the lower end of expectations. Consequently, a lot of the initial research now requires reassessment. As the LPC summarises in its fourth report, “Our consultation suggests that some employers found the 2001 increases harder to accommodate than the initial introduction.” It was initially predicted that the minimum wage would eventually benefit 1.7 million to 2.5 million workers by October 2004.⁵

Of the studies considering small businesses and the NMW five stand out: Arrowsmith et al (2003); Adam-Smith et al (2003); Machin et al (2002); Heyes & Gray (2001); and Undy et al (2002). These studies used a variety of research techniques (longitudinal studies, interviews, case studies, labour market analysis etc) and the focus of analysis differs whether that be industry (textiles, catering, retail, childcare or hairdressing etc.) or ownership structure (family run, ethnically denominated, sole trader etc).

The studies mentioned present a range of findings but all generally conclude that the NMW has increased the wages of workers within small businesses although this has caused problems for some employers. Very occasionally, companies have had to close. Others have changed their workforce profile to take account of lower minimum wage rates for those under 22 and those in training. A few have sought to evade the minimum wage altogether. The conclusion of Arrowsmith et al (2003) is that ‘informality’ and business sector are significant mitigating factors in determining the company’s response to the NMW. In general, firms were found simply to absorb the extra cost. Moreover, due to the nature of employee–employer relations in small businesses, an increase in pay at the lowest level did not cause

⁴ Low Pay Commission (2001). *The National Minimum Wage: Making a Difference*, Third Report of the Low Pay Commission, vol 1.

⁵ IRS (2003). ‘Minimum wage to rise to £4.85 an hour’, *IRS Employment Review* 773.

other workers to demand the restoration of differentials. Similarly, the empirical research on residential care homes carried out by Machin et al (2002) concluded that the NMW has minimal impact on long-term levels of employment.⁶

Many of the sectors studied to date were characterised by their piecework and ad hoc payment systems. It is in this area that significant consequences of the NMW have been detected. Small businesses appear to have changed to paying hourly rates in order to make the administration of the NMW easier and more transparent. Both Arrowsmith et al (2003) and Undy et al (2002) report this adverse affect on the piecework system.

In general, studies and anecdotal evidence have not linked the minimum wage with any changes in productivity or employment levels. Some cost-substitution models may have predicted a positive impact but this is yet to emerge.

While the Confederation of British Industry (CBI) has now expressed its support for the NMW (after initially opposing its introduction) it retains many of its original reservations. The evidence the CBI submitted to the LPC in 2002 included a survey claiming, "At £4.70 an hour, 21 per cent [of firms] would cut jobs while 34 per cent would reduce hours".⁷ Their current position is that the minimum wage, when introduced, was prudently priced but is now being raised to levels unsupported by economic growth and harmful to employment levels.

Surprisingly little has been written on the NMW from an employee's perspective. Often news reports have used trade unions as a proxy voice. Several studies have interviewed employees benefiting from the NMW as part of their research programmes, but the overriding focus is on business impact and aggregate employment levels. The experience of individual, low-paid, employees in the small business sector has been touched on only briefly by most pieces of research.

The eventual rise in the NMW to £4.85 (£4.10 for the development rate) per hour in October 2004 is still short of the £5 or even £6 per hour lobbied for by trade unions.⁸ Additionally, the TUC call for the extension of the NMW to cover 16- and 17-year-olds has now been accepted. From October 2004 16- and 17-year-olds above

⁶ Machin S, Manning A, Rahman L, (2002). 'Where the minimum wage bites hard: the introduction of the UK national minimum wage to a low wage sector', London School of Economics and Political Science, Centre for Economic Performance.

⁷ Confederation of British Industry. Press release, 18 October 2002

⁸ IRS (2003). 'Minimum wage to rise to £4.85 an hour', IRS Employment Review 773

compulsory school age will be entitled to a minimum wage of £3.00 per hour.⁹

As the fourth LPC report makes clear (2004), low rates of pay are associated as much with certain social groups as with certain industries. Part-time workers, young people, some ethnic groups and women have all benefited disproportionately from the NMW.

The employment of workers aged under 18 has been a particular area for concern. Several studies were commissioned by the Low Pay Commission in 2003 to investigate the possible effects of introducing a minimum rate of pay for 16- and 17-year-olds. Although research by the Warwick Institute for Employment Research¹⁰ predicted that a minimum wage for this age group would have little effect on educational participation, the situation regarding levels of employment is more uncertain.

Gender has been a significant factor in determining an individual's pay. National Statistics estimates that 170,000 women were paid below the NMW in 2003, compared with just 90,000 men¹¹. The gender disparity is even starker when only part-time working is considered. Homeworking, for example, is recognised to be an extremely low-paying economic activity and is dominated by women (92 per cent of workers) and ethnic minorities (50 per cent). Legally, homeworkers' employers may only pay four-fifths of the NMW¹² although this will change from October 2004.

While support for the concept of a minimum wage is high, even among sectors identified as low paid and predominantly casual, support for further rises is less clear-cut. An IRS survey conducted in 2002 detected small but significant inter-sectoral differences of opinion over the desirable level of NMW.¹³ At that time, 30 per cent of retail and hospitality businesses surveyed thought that the minimum wage should be at or below £4.10 (the NMW adult rate prevailing at the time) compared with 20 per cent of the total sample. Given government emphasis on tackling poverty and 'making work pay', it is likely that future developments could well prove more contentious than they have been to date.

⁹ TUC. Press release, 24 November 2003

¹⁰ Dickerson A, Jones P, (2004). 'Estimating the impact of a minimum wage on the labour market behaviour of 16- and 17-year-olds', Warwick Institute for Employment Research, Report to the Low Pay Commission.

¹¹ National Statistics (2003). 'Low pay estimates: Spring 2003', Office for National Statistics.

¹² IRS (2004). 'Minimum wage protections for homeworkers', Equal Opportunities Review 128.

¹³ IRS (2002). 'Floor covering: the minimum wage survey', IRS Employment Review 750.

Despite well over a million people benefiting from the introduction of the minimum wage, the effects of the regulation have not been as expected. Far fewer workers had their wages raised than originally predicted. It is possible that only with the recent and forthcoming uplifting of the minimum wage will any significant effects emerge within the small business sector. Until now, the largest general changes noted have been the organisational developments introduced to deal with the administration of the minimum wage. A recent IRS report¹⁴ into retail sector pay noted that some employers have now introduced additional pay reviews in October to deal with increases in the national minimum wage.

Any conclusive, national-level, positive or negative effects on employment levels, productivity or growth have yet to emerge. However, this is not to say that particular industries or businesses have been unaffected by the national minimum wage.

¹⁴ IRS (2004). 'Retailers spend on pay to keep pace with the economy', IRS Employment Review 806.

2. METHODOLOGY

In December 2003 IRS Research was commissioned by the Low Pay Commission (LPC) to undertake a qualitative study of firms affected by the minimum wage.

The research is designed to report on the variety of ways in which firms have responded to, and coped with, recent increases in the minimum wage, in particular those affected by the increase in October 2003, and those that might be affected by the increases due from October 2004. The research for this report was conducted before the October 2004 minimum wage uprating.

IRS Research conducted this study among smaller businesses, as recent work by IRS on the NMW, both before it was launched and since its introduction, showed that larger firms (those employing more than 250 employees) were having relatively few problems dealing with the minimum wage or increases to it.¹⁵ By contrast, research by IRS for the LPC reported that smaller firms – typically those employing fewer than 100 staff – were finding the NMW impacting on a number of different areas of their business.¹⁶

IRS Research aimed to conduct in-depth, face-to-face interviews with trade union/employer association representatives and businesses employing up to 100 staff. The study did not seek to research the actions of a representative sample of small businesses throughout the UK. Rather, it aimed to present the common actions and the variety of actions employers took when dealing with the NMW.

The research looks at how different firms have been affected by the minimum wage and increases to the minimum wage, as well as how they will react to further increases to the NMW, in the following areas:

- Pricing decisions;
- Levels of profitability;
- Staffing and workforce planning;
- Productivity; and
- Training.

¹⁵ IRS (2002). 'Floor covering: the minimum wage survey', IRS Employment Review 750.

¹⁶ Miller, L., J. Hurstfield and N. Stratton (2002). The National Minimum Wage and Employers' Training Decisions. Research Report for the Low Pay Commission.

Sampling

The core sampling framework for this project was derived from the need to gather data with sufficient validity within the initial project parameters. Following a review of past research and associated literature, IRS selected industrial sector, region and company size as the three factors that warranted specific inclusion within the sampling schedule.

Industrial sector

In order to effectively investigate the impact of the national minimum wage, several sectors were excluded from the sampling framework. Where possible, sectors that were not in a period of considerable structural change were selected to enhance the focus on the specific innovations in employment legislation under consideration. Sectors judged to have been particularly affected by overseas competition were also excluded. For corresponding reasons, several contracted-out service areas were also selected for inclusion owing to their geographically defined and apparently stable industry structures.

Industrial sectors initially selected for inclusion within this study were:

- Cleaning/facilities;
- Catering/food processing;
- Security;
- Packing/distribution;
- Hospitality;
- Hairdressing;
- Construction (casual site staff);
- Retail; and
- Small office-based companies.

Using the estimates provided by the Small Business Service and National Statistics, the sectors selected provide employment for approximately three million people in the UK.¹⁷ Of these employees, 1,711,000 are based in *micro to medium* (employing 1 to 249 members of staff) sized companies. These smaller companies account for an estimated 240,510 enterprises with a turnover of £142.6 billion. Owing to the problems associated with gathering

statistics on small businesses, the sectors covered by the statistics above extend beyond those within the sampling schedule. However, they do provide an indication of the relevance of small employers within these sectors to the UK economy as a whole.

Non-public enterprises, employment and turnover within selected industrial sectors (broad definition)

Business size	Number		
	Enterprises	Employment (000's)	Turnover (£000,000's)
Micro (1 - 9 employees)	209,720	761	62,445
Small (10 - 49 employees)	26,410	511	42,153
Medium (50 - 249 employees)	4,380	439	38,014
Large (250 or more employees)	1,185	1,331	120,971
All employers	241,685	3,230	269,704

Notes: Standard Industrial Classification groups (3-digit SIC codes) included:
153, 158, 452, 522, 551, 555, 632, 633, 634, 672, 746, 747, 748 and 930.

Source: SME Statistics 2003.

Based on the results of our screening questionnaire and one test interview, the construction sector was removed from the sampling framework. Travel agencies were also selected in place of the more general 'small office-based companies' category. And retail was redefined into retail food business.

Company size

Prior investigations into the impact of the national minimum wage had concluded that larger companies were unlikely to be particularly affected by the legislation. The importance of the small businesses to the UK economy should not be underestimated. By one estimate, more than 99 per cent of all UK private sector businesses (including public corporations and nationalised bodies) have fewer than 100 employees and account for 51 per cent of private sector employment.¹⁸ IRS accordingly selected companies with fewer than 100 employees for inclusion within the study.

¹⁷ Small Business Service (2004). SME Statistics 2003.

¹⁸ Small Business Service (2004). SME Statistics 2003.

Given the importance of company size in defining labour relations, internal organisation and patterns of business, the following approximate sampling schedule for company size was derived:

- 10 employers with 10 to 19 employees;
- 15 employers with 20 to 49 employees;
- 15 employers with 50 to 74 employees; and
- 10 employers with 75 to 100 employees.

Geographic location

A minimum number of three interviews were conducted in Northern Ireland, Scotland, Wales and each of the nine English government office regions set to ensure national coverage of the research. This accounted for 36 of the 50 planned interviews. The remaining 14 interviews were allocated according to the initial result of the preceding interviews. For example, additional interviews were conducted in rural areas to gain an appropriate urban/rural split.

Obtaining interviews

IRS Research used a three-stage process to ensure that an effective sample of employers was obtained for this project. The first stage involved interviews with employer association representatives in four sectors as well as the TUC. The main aim of these interviews was to ascertain the key issues for businesses when dealing with the national minimum wage. The interview schedule for this fieldwork is presented in Appendix 6.

The second stage involved mailing 4,000 short questionnaires (see Appendix 3) to small business using the above dimensions of sector, location and company size to create the mailing list. IRS requested a random sample of named managerial-level contacts in 4,000 UK organisations from Yell.co.uk – the business-listing service formally called ‘Yellow Pages’ and now part of ‘Experian’. The results of this brief survey can be found in Appendix 1.

A shortlist of employers to approach for interviews was drawn up from the 265 valid questionnaire responses received. Individual businesses were then approached via the telephone and interview appointments arranged accordingly. In the later stages of the project, additional

organisations, from the initial mailing list but which did not respond to the survey, were approached in order to gain an appropriate match with the sampling schedule. This procedure also served as a further check to eliminate the inbuilt self-selection bias generated from using self-completion postal questionnaires as the primary method for approaching organisations.

Conducting interviews

Interviews were semi-structured and conducted in person with employers. A topic guide was produced to ensure that all employers were interviewed consistently. The guide contained the following sections (see Appendix 4 for more):

- General information
- Views and impact of the national minimum wage
- Organisation coping strategies, and
- Additional comments and future expectations.

Initial piloting of the pro-forma was conducted with three small businesses and refined prior to the main bulk of the research interviews that were conducted between April and August 2004.

In response to a request from the Low Pay Commission, employers were also asked whether they had noticed any relationship between the national minimum wage and the Working Tax Credit in terms of staff being unwilling to work beyond a certain number of hours. Additionally, a supplementary interview questionnaire was used in the latter stages of the fieldwork to gather information on pay rates, turnover, costs and profits (see Appendix 5). This questionnaire served to streamline interviews and to provide supporting quantitative information.

In total, IRS Research conducted and analysed interviews with 53 businesses in the following regions, sectors and size bands:

- East Midlands – 7
- East of England – 5
- London – 4
- North East – 4
- North West – 5
- Northern Ireland – 3
- Scotland – 4
- South East – 4
- South West – 5
- Wales – 4
- West Midlands – 4
- Yorkshire and the Humber – 4

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- Cleaning/facilities management – 7
 - Construction – 1
 - Hairdressing – 8
 - Hotel – 8
 - Packing – 6
 - Security – 5
 - Cafes/catering – 8
 - Food distribution/processing – 5
 - Office-based – 5
-
- Fewer than 19 employees – 19
 - 20 to 49 employees – 15
 - 50 to 74 employees – 6
 - 75 or more employees – 13.

Only in company size (as represented by employee numbers) did the final allocation of interviews differ from the original sampling schedule. This was a result of a several factors, including a primary interest in representing business sectors and the dynamic nature of some small businesses.

Analytical approach

Employer interviews were recorded and then reviewed. Summaries were made of each interview in order to synthesise the large amount of qualitative data gathered. These summaries, and the original data, were reviewed in the middle of the project and an initial analysis performed. The results of this analysis were fed into the interview arrangement process in the later stages of the fieldwork to enable testing and further investigation of preliminary findings.

Interviews and summaries were further examined upon completion of the fieldwork stage of the project. Through investigation of the data, comments were drawn up on the initial research questions that were posed. Emergent themes were further scrutinised and any resulting schemas were reported.

3. INTERVIEWED ORGANISATIONS

This section provides a brief summary of the companies interviewed in this study. Overall, 53 companies employing 2,675 employees were interviewed with the median number of employees in each company being 38. The large majority of companies detailed below were limited companies, with only three organisations operating as a partnership.

Outlined below is a summary of the companies interviewed for this research on a sector-by-sector basis.

Cafes and caterers

Eight companies in Greater Manchester, Kent, Leicestershire, London, Scotland and Wiltshire, employing 292 staff in total, were interviewed. The employee numbers ranged between 10 and 90. Reported gross hourly pay (where information was provided, across all ages) ranged from £4.00 to £8.00. Where reported, wages as a percentage of costs were estimated as between 22 per cent and 40 per cent. The following organisations were interviewed:

- Family owned café and sandwich shop based in the North West employing 10 staff that was established in 1990.
- Scottish catering company employing 65 members of staff and established in 1994.
- A London based catering and bakery company established 30 years ago. The company employs 90 people.
- A café/restaurant based in a city in South West England employing 15 people. The company was established in 1985.
- A Kent based café interviewed as part of this study employed 17 people – 10 of them on a temporary basis. Established in 1996.
- A family owned café and coffee shop in rural South West England employing approximately 10 people and established in 1990.

- An East Midlands based company with several café related sites/businesses. Employing 65 members of staff, the company was originally established more than 50 years ago.
- A South West based café and lorry divers facilities company with 20 employees. The company was established in 1987.

Selected pay rates for cafes and catering organisations

Generic job title	No. of companies	Rate
Students	2	£4.00 - £4.60
Part-time employee	3	£4.50 - £5.00
Catering assistant	7	£4.90 - £5.85
Supervisor/cashier	2	£5.45 - £5.75
Skilled baker/chef	3	£6.50 - £7.90
Manager	2	£5.60 - £8.00

Note: The use of separate pay rates for part-time and full-time staff, doing the same work, is contrary to current employment law.

Food processing and distribution

Five companies in Fife, Herefordshire, London, Northern Ireland and West Glamorgan, employing 197 staff in total, were interviewed. The number of employees ranged between 17 and 65. Reported gross hourly pay (where information was provided, across all ages) ranged from £5.00 to £9.50. Where reported, wages as a percentage of costs were estimated as between 12 per cent and 70 per cent.

The following firms were interviewed:

- A food processing company in Wales employing 35 full-time workers. The business was originally incorporated in 1989.
- A West Midlands based food processing company employing 38 people (25 of whom were temporary workers).
- A London based food processing company established in 1965. The company had 65 employees.
- A Scottish food distribution company employing 42 permanent members of staff. The company was originally established more than 40 years ago.

- A food distribution company based in Northern Ireland employing 17 people. The company was originally established more than 30 years ago.

Selected pay rates for food distribution and food processing organisations

Generic job title	No. of companies	Rate
Line workers	2	£5.00
Office based employee	3	£5.00 - £5.75
Supervisor	1	£6.50
Driver	1	£6.53
Manager	1	£9.50

Cleaning and facilities management

Seven cleaning/facilities management companies in Cheshire, Derbyshire, Essex, Lancashire, Wiltshire and Yorkshire, employing 382 staff in total, were interviewed. The number of employees ranged from 14 to 123. Reported gross hourly pay (where information was provided, across all ages) ranged from £4.50 to £11.00. Where reported, wages as a percentage of costs were estimated as between 47 per cent and 75 per cent.

The following firms were interviewed:

- An East Midlands-based firm employing 75 members of staff. The company was originally established more than 50 years ago.
- A cleaning company in Yorkshire employing 31 members of staff. The company is family owned and was established in 1974.
- A family owned, North West based, specialist cleaning company established in 1984. The company has 53 permanent employees.
- Cleaning company in the East of England employing 46 permanent members of staff. The company was established in 1994.

- A North West specialist cleaning company established in 1975. The company employs 14 people.
- A cleaning and facilities management company in the South West employing over 100 members of staff. The company was established in 1988 and has been diversifying its businesses for over 10 years.
- A North West cleaning company employing 53 people. The company was incorporated in 1991.

Selected pay rates for cleaning organisations

Generic job title	No. of companies	Rate
Cleaner	12	£4.50 - £6.50
Office based employee	1	£6.75
Driver	1	£6.80
Specialist operative	3	£6.55 - £9.20
Skilled and semi-skilled facilities management staff	2	£9.50 - £11.00

Hairdressing

Eight companies in Kent, Leicestershire, London, Norfolk, Wiltshire and Yorkshire, employing 140 staff in total, were interviewed.

Employee numbers ranged between five and 38. Reported gross hourly pay (where information was provided, across all ages) ranged from £1.75 to £8.64 (including commission). Where reported, wages as a percentage of costs were estimated as between 15 per cent and 60 per cent.

The following organisations took part in the research:

- A hairdresser in the South East employing 38 members of staff. The business was established in 1992.
- A hairdresser in the East Midlands established just two years ago in 2002, employing 13 people.
- A family owned, London based, hairdressers employing 17 people. The business was established in 2001.
- An East of England hairdresser employing 14 people. The company was established in 1996.

- A Yorkshire-based hairdresser employing 5 people.
- A Kent-based hairdresser established 20 years ago. The company employs 11 people.
- A South West hairdresser employing 10 people. The business was established almost 40 years ago.
- A Hairdresser in London employing 32 members of staff over two sites. The company was established in 1992.

Selected pay rates for hairdressing organisations

Generic job title	No. of companies	Rate
Junior	3	£1.75 - £3.80
Nail technician	1	£4.50
Junior stylist	3	£4.50 - £5.10
Stylist	4	£4.68 - £6.50
Senior stylist	3	£5.00 - £8.64

Hotels

Eight companies in Fife, Lancashire, Leicestershire, Norfolk, Northern Ireland, Tyneside and West Glamorgan, employing 515 staff in total, were interviewed. The number of employees ranged between 12 and 100. Reported gross hourly pay (where information was provided, across all ages) ranged from £3.75 to £10.00. Where reported, wages as a percentage of costs were estimated as between 25 per cent and 40 per cent.

The following firms were interviewed.

- A family owned hotel in Wales employing 100 people (43 permanent and 57 on a temporary basis). The business was originally established more than 40 years ago.
- A recently established (2002) hotel in the Midlands employing 23 – five permanent and 18 temporary – members of staff.
- A Northern Ireland hotels business employing approximately 100 people across two sites. The business unit was part of a conglomerate but was largely autonomous.

- An East of England hotel employing 100 members of staff. The company was originally established in 1997.
- A Lancashire-based hotel that formed an autonomous unit within a company originally incorporated in 1984. The business employed 45 people.
- A North East hotel employing 80 people. The business was originally established in 1988.
- A West Glamorgan hotel employing 100 people. The hotel was established over 40 years ago.
- A Scottish hotel established employing 12 people.

Selected pay rates for hotels

Generic job title	No. of companies	Rate
Employee under 18	2	£3.75 - £4.50
Basic grade staff	7	£4.50 - £5.00
Chef de Partie	1	£5.64
Supervisor	3	£5.64 - £9.00
Manager	1	£10.00

Packing

Six companies in Cambridgeshire, Leicestershire, Northamptonshire, West Glamorgan and Yorkshire, employing 322 staff in total, were interviewed. The number of employees ranged from 12 to 150.

Reported gross hourly pay (where information was provided, across all ages) ranged from £4.70 to £6.75.

The following firms were interviewed:

- A Welsh packing company employed 16 permanent members of staff. The company was incorporated in 2002.
- An East Midlands packing company established in 1993. The company employs 12 people.
- A Packing company based in the East of England employing 150 people. The company was established in 1999.

- A Yorkshire packing company employing 14 people. The company was established in 1997.
- An East Midlands packing company with 110 employees. The company was established in 2000.
- A Yorkshire-based company employing 14 people established in 2000.

Generic job title	No. of companies	Rate
Packer	4	£4.70 - £5.50
Supervisor	2	£5.50 - £6.75

Security

Five companies in County Durham, Derbyshire, the West Midlands and Worcestershire, employing 349 staff in total, were interviewed. Companies primarily provided manned guarding services. The number of employees was ranged widely between 3 and 170. Reported gross hourly pay (where information was provided, across all ages) ranged from £4.50 to £6.15. Where reported, wages as a percentage of costs were estimated as between 50 per cent and 80 per cent.

The following firms took part in the research:

- A North East based company employing just three people – down from 22 employees three years ago. The company was established in 2001.
- A West Midlands based security company with 19 employees.
- A security company based in the West Midlands with 52 members of staff – all but two of those permanent. The company was established in 1999.
- An East Midlands security company employing 105 people. The company was originally established 30 years ago.
- A West Midlands security company employing 170 people.

Selected pay rates for security organisations

Generic job title	No. of companies	Rate
Driver	1	£5.65
Security guard	7	£4.65 - £5.00
Supervisor	2	£5.25 - £6.00
Control room operator	1	£6.15

Office-based companies

Five companies in Lanarkshire, Norfolk, Northern Ireland and Tyneside, employing 429 staff in total, were interviewed. The number of employees ranged between 16 and 240. Reported gross hourly pay (where information was provided, across all ages) ranged from £2.50 to £8.65. Where reported, wages as a percentage of costs were estimated as between 10 per cent and 65 per cent.

The following companies were interviewed:

- A North East travel company employing 25 permanent members of staff. The company deals with both business and retail customers. The business was originally established over 30 years ago.
- A Northern Ireland retail travel agents with 16 employees across several businesses. The company was started in 1990.
- An East of England travel agents with 42 members of staff. The business was originally established more than 40 years ago.
- A North East travel company with 240 members of staff. The company was originally established more than 40 years ago
- A Scottish recruitment, training and travel business employing 106 members of staff. The holding company was incorporated more than 10 years ago.

Selected pay rates for travel and other office based organisations

Generic job title	No. of companies	Rate
Office junior	3	£2.50 - £4.50
Courier	1	£4.50
Recruitment consultant	1	£7.25
Clerical officer	1	£8.65
Travel agent	5	£4.85 - £15.00

4. EMPLOYERS' VIEWS OF THE NMW AND ITS IMPACT

This section, based on interviews with 53 businesses across the UK, presents the views of employers of the NMW, as well as the impact of the rate on their business and covers:

- General views of the NMW
- Knowledge of rates
- Finding out about the NMW
- Notice of NMW upratings
- Working Tax Credits.

General views of the NMW

The employers interviewed for this project were positive about the introduction and need for a national minimum wage. Respondents spoke of it being fair that people should receive a 'decent wage' and a small proportion remarked that it had helped to deal with 'rogue' employers.

A number of employers noted that the NMW had formalised the employment arrangements and wages in their locality and sector. Some respondents reported that the practice of paying 'cash-in-hand' had decreased since the introduction of the NMW, as employees expected to receive the Minimum Wage (NMW) for the work they were doing. As a result, some employers remarked that it had formalised some wage arrangements locally and, as they were less likely to be undercut by employers paying low wages, was of benefit to them in terms of fair competition.

However, while the vast majority of employers interviewed were supportive of the NMW in principle, some – even among those that supported it – were critical of the government's intervention in the labour market by setting wage levels. Those employers that were critical of the minimum wage – as well as some that were not – felt that they should be allowed the freedom to set wages that were commensurate to their employees' 'worth'.

A café owner in the East Midlands employing 65 staff across two sites reported that he was paying wages in excess of the NMW when it was introduced and has continued to pay his staff that way. However, this employer did think that he should not be told how much his staff should be paid. "I resent it because...it assumes that everybody is a bad employer, so it is a very blunt instrument and it hammers everyone down to the same common denominator. It assumes that we are all out to, pardon the expression, shaft our employees."

"The fact that it has kept creeping up and up has meant it has brought a lot more people into the workplace that would not be able to command a wage that their abilities would [normally] allow them to [do]." Packing company employing 100 in the East of England.

"It's unfair because I think it should be up to the employer to decide what his employees are worth." Hotel, bar and restaurant in Scotland employing 12 staff.

Those employers critical of the NMW also complained that it was too blunt an instrument and did not take into account regional, sub-regional or even sectoral factors. For example, respondents gave examples of the same jobs in the same types of establishments elsewhere in their region – and in some cases in the next town – where prices for comparable services, as well as wage rates for comparable jobs, were considerably higher. As a result, those employers operating in higher-wage and higher-price areas of the local economy were unlikely to be affected as much by the NMW or increases to it.

"Unfortunately, it came in across the board, whereas it should have come in per sector...[It should be] based on where they are [the company's location], their size, on [the] availability of staff". Hotel in Wales, paying in excess of the NMW and employing 55 staff.

"We charge, on average, for a cut and blow dry that takes about an hour, about £19 or £20...Canterbury's only 12 miles away [and] the same service is probably about £40 to £45 and yet the minimum wage is the same in Canterbury as it is [here]." Hairdresser in the South East, employing 11 staff.

An employer in the hotel sector operating in the North West and employing 45 staff believed that the minimum wage was too inflexible for its sector. This respondent felt that the minimum wage should reflect the different types of job within the sector – for example, service staff (such as waiters, bar staff etc) were able to supplement their wages with tips, while those working in other areas, such as kitchen staff, could not. When the sector's wage guidelines were set by the wages councils, these differences had been taken into consideration.

Knowledge of rates

Researchers asked interviewees about their knowledge of the various minimum wage rates in operation. Overall, the vast majority of employers were aware of the current adult rate, as well as the planned increase in October 2004.

With the exception of those in the hairdressing sector, few employers appeared to be aware of development or training rates and as a result were not using them. In some of the areas investigated – such as packing jobs, kitchen work, and café, bar and restaurant serving – firms tended to rely on what they called 'unskilled labour'. This 'unskilled labour' was typically categorised as such by employers where they stated that staff did not require any formal training to do the job, or could quickly and easily be shown how to do their job and be 'up to speed' in a very short space of time.

Employers' knowledge of the youth rate (covering 18- to 21-year-olds) and the adult development rate (those aged 22 and over in an accredited training programme) was also mixed. Five employers outside the hairdressing sector reported using the youth rate – in two hotels, one cleaning company, one food processing organisation and one travel organisation. Only one company, a recruitment, travel and training company that unusually had a specific human resource function, reported using the adult development rate. Elsewhere, some employers were knowledgeable about the rate while others either lacked knowledge or were confused as to how these rates could be used.

Of the eight hairdressers interviewed, only one was not aware that the youth rate could be used after the apprenticeship exemption from the

NMW had expired. Only four employers in this sector were fully aware of the details of the forthcoming 16- to 17-year-old rate.

However, the majority of employers did not use the youth or adult development rate and there was some evidence that employers were not using this rate because they did not know it existed. In other cases, employers reported that the nature of the work and what was expected of employees in their organisations was the same for everyone, regardless of an employee's age. As a result, these employers tended to use the adult rate for all staff.

*“Younger staff get paid exactly the same as everyone else. My theory on this is, if they're doing the same as the bloke next to them, then they deserve the same money.”
Food processor in Scotland employing 42 staff.*

“The fact that they're young shouldn't mean that they're paid less. They're doing the same job. They should have the same money.” Cleaning company in the North West employing 53 staff

Finding out about the national minimum wage

Employers received information on the minimum wage and a range of other employment issues (such as changes to maternity and paternity rights, and entitlement to paid holidays) from a number of sources.

Employers reported that they were seeking out information about the NMW for themselves or receiving it from third-party sources. Typically, these were professional and trade bodies such as the National Association of Master Bakers, the Federation of Small Businesses and the National Hairdressers' Federation. Other employers found out about the NMW from the Inland Revenue website, the national press, sector-specific publications or their accountant or bank.

There was confusion among some respondents about the NMW's various rates and their application, as well as the new rates planned for October 2004. Furthermore, some employers were unsure where to turn to for good, relevant and specific advice. However, one respondent praised the information provided by the Inland Revenue. This employer had contacted the Agency via its website with a specific query relative to his business. The enquiry was answered quickly and the advice provided fully answered this particular employer's query.

Increases to the NMW

Despite the largely positive view taken by employers of the NMW, a large proportion were unhappy with what they saw as arbitrary and substantial upgrades to the rate in 2003, as well as that due in October 2004. Respondents remarked that these upgrades represented increases well in excess of inflation and average earnings, and well in excess of the upgrades made in previous years.

Furthermore, employers mentioned that the increase to the rate outstripped the increases they could make to the prices they charged for their products and services and, as a result, these employers reported that this was impacting on the profitability of their business. These employers were also concerned that another increase in 2005 similar to the one planned for October 2004 (ie of 35p per hour) would be more difficult to accommodate.

When researchers pressed employers as to how they would cope with further rises, they tended to talk about how the NMW, if it were to continue to rise, would impact on their profits and levels of employment.

An employer operating in London spoke of his organisation's plans to open a plant overseas in order to overcome the rising cost of the minimum wage. However, this option was not available to most employers, who were operating in sectors where they needed to be close to their customers (for example, on high streets).

Notice of national minimum wage upratings

Employers were generally happy with the amount of notice they received of planned increases to the minimum wage. The advance notice they received of upratings were considered useful, as it allowed businesses to plan budgets and prices well in advance of the changes in pay rates.

The overall view was that the amount of notice employers were given of changes was adequate. However, a hotelier in the North West, whose financial year ran from January to December, would have preferred to receive more notice of any increases – ideally 18 months

– to allow it to plan budgets and its wage bill to take into account the new NMW.

The employers in this study are receiving information about NMW rates from a range of third parties – typically their accountants, banks, business associations and from industry and/or national press. It was suggested that employers would benefit from notification of changes to the NMW rates from an official government source, such as the Inland Revenue. This notification would allow employers to plan any coping strategies to deal with increases to the minimum wage.

“[It would be best] if we got told officially [about upratings] from a government source...The Inland Revenue....do write to us a lot and ask us for money! It would be great if they [sent a letter explaining when the new rates have been decided] so at least we are prepared for it a bit more. It would give us more time to go to clients and say that: ‘Do you realise, in 2005 [the NMW] is going to increase; should we start thinking now what we are going to be doing in 2005?’ It would help with our planning [as] a lot of [our clients] now have budgeted for 2005.” Cleaning company in the North East employing 110 staff.

Working Tax Credits

The LPC has some anecdotal evidence that the interaction between the minimum wage and the WTC may be impacting on the number of hours that employees are prepared to work. The majority of employers in this research relied very heavily on part-time staff to run their business; therefore it was likely that some employers may experience staff refusing to work more hours as it would affect their benefits or tax credits.

Ten employers mentioned encountering problems with the WTC. Where this occurred, staff were often refusing to work extra hours. However, the extent to which this was a WTC issue, or a work–life balance or care issue, was difficult for employers to ascertain. In one company, some staff were prepared to work extra hours only if the employer paid ‘cash-in-hand’.

In another organisation, the owner suspects that the WTC is the reason behind one employee on the sales side keeping down his level of sales (and hence take-home pay) since he is financially better off if he is still eligible for various benefits/credits.

5. EMPLOYERS' COPING STRATEGIES

The following section details employers' coping strategies in dealing with the NMW and covers the following:

- General coping strategies
- Changing wages and pay structures
- Changing hours
- Increasing prices
- Reducing profits
- Reducing employment levels.

General coping strategies

Employers reported using a variety of ways to cope with the increases to the national minimum wage and other changes to employment legislation that had impacted on their businesses.

Overall, 14 employers reported that they had increased prices and 20 had seen the profitability of their business decline in the past two to three years. While others had changed pay structures and rates to cope with the minimum wage and other changes to employment law, these strategies were less common.

However, employers were unable categorically to state that their actions or 'coping strategies' were as a direct result of the NMW. Employers found it difficult to take the NMW in isolation, given that legal changes in the past five years – such as entitlement to paid holidays, improved maternity and paternity rights and increases to NI contributions – had also impacted on their businesses at the same time. As a result, very few employers were able to state that the NMW in isolation was causing them problems or had acted as a catalyst for changes as to how their businesses were managed or operated or where they had introduced new practices.

However, changes in employment legislation have now settled-in and are unlikely to change in the same regular way that the NMW has and will do. While the introduction of holiday pay, for example, did impact

on small businesses when it was introduced, it is no longer causing the same level of concern as it did when it was introduced. In contrast, future increases to the NMW will, and have, caused concern among the small businesses interviewed. Indeed, all the employers interviewed for this study expected that the NMW would continue to increase in the future and that it was important future upratings did not follow the same percentage increases as seen in 2003 and 2004.

Some employers had tried a number of different ways of dealing with the NMW and reducing their costs by looking at productivity, changing suppliers or diversifying into new areas. However, the employers in this study in the main spoke of operating with the minimum number of staff they possibly could or said that the nature of the work their staff was doing could not be changed by investing in new machinery or changing working practices.

A hairdresser in the South West employing 10 staff was now offering beauty treatments and nail extensions in order to find more profitable sources of income.

A security company in the North East was also offering a CCTV installation service.

A travel agent in Northern Ireland employing 16 staff across two sites is considering closing one shop. The shop is currently running on a skeleton staff and its profit margins are low. This follows the closure of another of the company's offices.

A hairdresser in the South West employing 10 staff in reported that it now employed fewer staff but had just as many clients. In the past, staff were not always busy, but now they were always fully booked.

"We'll try and reduce overheads or increase turnover which you can argue...is what you have to do anyway to be a good businessman but the thing is I shouldn't be forced to do it by legislation."

"Training's an absolute necessity. The quality of training is better now [in the hotel industry] than 20 years ago. The minimum wage has helped us focus on things: if you train, you become more efficient. The way we recruit is going to change: we have just recently made a decision to outsource our recruitment. [We are going to] use an agency to sort out job descriptions and interviews and not

rely on cards in windows [or] advertise in local papers [to notify vacant positions]. It costs, but the quality [of staff they hire] will be worth it.” Hotelier in Wales employing 100 staff.

A hotel reported that one-quarter of its domestic staff were from eastern Europe, as these staff were prepared to work at the level of the NMW. The employer was particularly happy to use these staff not only because they were prepared to work at this rate, while local staff were not, but that the quality of these staff, from a work, service and educational perspective, was considerably higher than that offered by local staff. This employer reported that should the NMW continue to rise, he was likely to increase the number of eastern European nationals working at his organisation.

A food distribution company in Northern Ireland previously employing 40 staff was downsized dramatically (to 17 staff) and refocused its operations, which has delivered a level of profitability that is acceptable to the owner.

A packing company in London is looking to open a plant nearer its product markets in order to better control its wages and transport costs.

Changing wages and pay structures

The introduction of the NMW impacted on all but six businesses interviewed for this research – a construction company in the South East, a specialist cleaning company in the North West, a business travel agency in the North East, a high street travel agency in the North East, a recruitment and training company in Scotland and a food processing company in Wales.

Although many of the employers affected were unable to give an accurate assessment of the increases in wage costs and how they had impacted on their profits, they pointed out that the NMW had increased by 90 pence per hour – or one-quarter – since 1999. In addition, the increase in the NMW from £4.20 in 2002 to its current level of £4.50 – an increase of more than 7 per cent – and the

increase planned for October 2004 that will take the NMW to £4.85 per hour, represents an increase of 15 per cent in two years. Of the 33 businesses that gave specific information on the proportion that wages were of their total businesses costs, wages in these organisations accounted, on average, for just over two-fifths of all costs (44.3 %). As a result, any significant increases to the level of the minimum wage results in increases in businesses' costs.

Ten employers reported paying in excess of the NMW for all staff when it was introduced and 17 currently pay in excess of the current rate to all staff. Where this was occurring, these employers were typically using wages as a means of tackling staff shortages or of attracting what they described as 'better-quality' staff.

*"We are already putting rates in place to attract people before anyone else. We have to pre-empt the market price. This year we have significantly increased rates over the minimum wage: [we are] paying chefs London rates, minimum starting rates in the kitchen is £14,500 per year – in [neighbouring city] it would be £5,000 less."
Hotel in Wales employing 100 staff.*

Although some employers gave examples of competitors in their sector and locality that were charging staff for uniforms or transport in order to recoup recent increases to the NMW – in effect, perhaps, illegally denying staff the increase to the NMW – none of the employers interviewed for this research reported doing this.

Pay rates and scales

The pay scales used by employers in this study varied widely within and between each sector and region. Some employers were using the minimum wage as the only wage rate either for some or all their jobs, while in others the rate was used for starting rates from which staff could advance once they gained experience or new skills.

In hotels, bars, restaurants and cafes, employers said they used staff in different ways. These organisations would typically employ a 'core' of senior or experienced staff, while younger people – typically school or university students – would cover peak periods, evenings or weekends. The more experienced staff – cooks, chefs, managers, supervisors and so on – were paid in excess of the minimum wage, while the younger staff would be paid at or just above the adult NMW.

For some positions – typically those jobs that did not, in the employer’s view, require formal training, such as cleaning, packing and in some cases bar work, waiting positions and hotel domestic and kitchen work – many employers were using the minimum wage as the only rate for the jobs.

In hairdressing salons, staff were typically paid an hourly rate – for qualified senior staff, this was in excess of the NMW – as well as a commission based on the number of clients they had in a week. However, those undertaking formal training in the sector were paid below the adult rate and the development rate¹⁹ but could still earn bonuses and tips. As discussed later, hairdressing salons prefer to employ young trainees – ideally aged 16 or 17 – so that they can be paid outside the adult and development rates. Although apprentices are exempt until the age of 19, once non-apprentices reach the age of 18, they are entitled to £3.80 per hour that would give a salary in excess of £150 for a 40 hour week.

Changes to pay scales and pay rates

Six employers in this study had made changes to their pay scales as a result of the NMW and other employment legislation that has impacted on labour costs. This included, for example, consolidating bonuses into hourly rates, reducing the number of pay scales or introducing a flat rate for all staff of a certain type.

A cleaning company in the West Midlands reported that its higher-paid staff were expecting the same increases in their wages as those enjoyed by staff on the NMW.

A packing company in London and a hotel in the North West had consolidated pay packages as a result of the minimum wage and now this was impacting on differentials and the total wage bill.

A cleaning company in the North West is finding it difficult to maintain pay grades and differentials. As a result, this organisation is considering scrapping the grading system for new staff joining the company.

A food processing company in London employing 90 people previously paid different rates for different types of

¹⁹ Three employers gave figures of £60 per week for 16- to 17-year-old hairdressing trainees, which they considered was the average for the sector.

staff, as well as bonuses. The company now has only one rate of pay for these staff and continues to pay bonuses.

As already mentioned, some employers were found to be using the NMW as a floor, and in some cases a ceiling for their wages. The introduction of the NMW did, overall, see staff receive increased hourly rates.

Impact on pay differentials

The introduction of the NMW in 1999 was not reported as greatly affecting pay differentials in the organisations involved in this study. While employers mentioned that the impact on pay differentials was an issue, few mentioned that they had to increase the wages of their staff to answer these concerns. However, a number of employers spoke of having to deal with higher-paid staff's concerns about the pay rises – via the upgrades to the NMW – being given to lower-paid employees.

Twelve employers reported that the NMW had impacted on their organisation's pay differentials in recent years. These organisations, from different regions and sectors, tended to employ relatively large numbers of staff. The use of pay bands is most likely to exist in larger organisations, where employers tend to use divisions of labour and hierarchies to run their operations. For example, larger employers are more likely to use staff for particular jobs or tasks (for example, as packers, machine operators, supervisors etc) while those employed in smaller businesses tend to have flatter hierarchies and fewer levels of supervision or job specialisation. As a result, the impact on differentials on smaller firms, where all staff tend to be paid at the same rate, was less likely to have occurred or did not exist at all.

Employers reported that staff being paid well above the minimum wage when it was introduced in 1999 were now beginning to see their differentials eroded either by lower-skilled or less experienced staff. Worried about the scale of increases in 2003 and those planned for 2004, one employer complained that the inconsistent and large rises ones too made it difficult to plan ahead.

“What the minimum wage has done has raised the floor so you have to raise the ceiling to maintain [pay] differentials.” Café in East Midlands, employing 65 staff.

In order to maintain the integrity of their pay scales and bonus schemes, a cleaning company in the North West employing 53, is forced to increase the wage rates of higher-paid staff when the new NMW rates come into effect in order to maintain the differentials.

A processed food manufacturer in London employing 90 people prior to the introduction of the NMW previously had “significant” pay differentials between its packers (who would take around 60 minutes to train) and those operating machinery (who would require weeks of training in how to set-up, operate and monitor the machines). This difference in pay – around £20 per week – now no longer exists between those staff.

*“The problem that we have is because the national minimum wage will go up again in October to £4.85, we then have people who are on £5 an hour saying, ‘Well hang on, he was on £4.75, you’ve put his wages up to £4.90, surely our wages need to go up in proportion.’”
Security company in the West Midlands.*

Changing hours

Some employers reported that they had cut the number of hours their staff were working in order to cope with the minimum wage. This typically involved employers in the hospitality sector letting staff leave early if there was no work for them to do during ‘slack’ times.

In other cases, employers used measures specifically designed to cope with the national minimum wage. These measures usually involved either using staff more efficiently, reducing their numbers or by cutting training.

A manager in a cafe in the South West had taken the step of closing the business on a Sunday as there was insufficient trade to warrant it being open. By doing this, the employer was protecting his profit levels by removing costs from an unprofitable trading day.

“Our efficiencies have massively increased our output, for example, the number of sandwiches we make has increased by about 355 [per day] in the last 6 years and

the number of people making them has reduced, well we have gone from 9 people to about 6." Catering company in the North West employing ten staff.

"We have put systems in by which we...can use less staff. We have a policy of sending people home as quickly as possible [if there is no work for them to do]. Hotel in the North East employing 80 staff.

"We are finding that companies are not spending more, we are just doing less [work for them]. [Clients are asking:] "What can we do to keep the prices the same? "We know the minimum wage is coming. What can we do to keep the budgets the same? Unfortunately, it is coming back on the cleaners: they are getting less work for the same amount of money." Cleaning company in the North East employing 110 staff.

"What we've noticed is that in those cases where we're dealing with contracts with clients, is that they don't object to a minimum wage but what they do is to ask us to observe the increase while it reduces the number of hours that we're putting into their contract." South West cleaning/facilities company employing 123 staff.

Increasing prices

The ability of businesses in this study to increase their prices to offset the introduction of, and increases to, the NMW was limited by some sectoral, regional or competitive factors. Fourteen employers had increased their prices over the past two to three years, but this was not a 'coping strategy' in dealing with the NMW or other business pressures; it was an annual activity to cover the increase in other input costs to the businesses.

Employers reported that, where they were able to increase prices, this did not cover the full costs of increases caused by the NMW and other legislation. These employers reported that local competition, as well as understanding what the market 'could take' in terms of price increases, hampered their ability to recoup the full costs imposed by the NMW and other legislation.

However, in two contract cleaning companies, employers were able to recover the costs of the NMW from many of their customers by renegotiating contracts or increasing prices.

A contract cleaning company in Yorkshire employing 31 staff had, on receiving notice of the minimum wage as well as future increases and the introduction of paid holidays for all staff, written to their customers explaining the situation. In most cases, this employer was successful in renegotiating contracts to take the higher rate into account. This organisation now renews its contracts during the summer of every year to take into account any changes to the NMW and therefore is able to recoup costs.

Another contract cleaning company, based in the North West and employing 50 staff, said that it coped with increases to the NMW by increasing the hourly rates it charged its customers. The company commented that many of its clients were private households that were able to afford to pay these increased costs, although some clients did ask if the extra money was being passed on to the cleaners. However, although costs were currently being at least partially recouped in this way, the company reported that it could not pass on all the costs. Furthermore, it was concerned that customers would not indefinitely agree to these increased rates in the future and may look elsewhere for a cheaper service from another company.

A small number of employers were not able to pass on any increased costs – be they wage or other input costs, such as raw materials – to their customers. These organisations operated in a range of different markets and sectors – though firms operating in business-to-business markets were less likely to report being able to increase prices.

A London-based packing company employing 65 staff, who supplied and packed produce on behalf of famous UK food brands (that was then sold onto supermarkets) were unable to pass on NMW, or indeed any other price increases to their customers. This company recently experienced a dramatic increase in the prices of fruit due to poor harvests. Despite their customers being aware of this situation, as well as increases to the NMW, they

were unable to accept any price increases from the company for its products.

“The downside [of the NMW] is that the customers don’t want to pay for the increase...as a result, they are downsizing the number of cleaners that they have got or shortening their hours...so where we have had two cleaners in for two hours, we have two cleaners in for one and three-quarter hours. Where we are going for new accounts, where there is usually four cleaners they [customers] are actually saying: ‘Can you schedule it for three?’, knowing that the minimum wage is going up in October.” North East cleaning company, employing 110 staff.

A travel company employing 42 staff in the East of England remarked that although it had some flexibility with the prices it charged, it was, to some extent, set by its suppliers.

A security company in the North East, remarked that the standard industry hourly rate for a security guard has not changed for around three years. This organisation’s customers were not prepared to pay above that rate despite the fact that the minimum wage had increased by almost 20 per cent in the same period. As a result, this firm now subcontracts out work it has won to other organisations, leaving this employer with the problem of dealing with lower margins or lower wage levels.

“There’s only so much the customers will pay, because we also charge VAT, so with the VAT and everything else, we’re more or less pricing ourselves out of what’s already becoming a very competitive market.” Cleaning company in the North West employing 50 staff.

A Scottish hotel/bar employer remarked: “If I put my prices up here, my customers will just go and drink down the road.”

Reducing profits

The increases to labour costs as a result of changes in the NMW and other employment legislation, as well as the inability of employers to recover the full costs of the increases, gave employers only a few other options to cope with the NMW.

The firms in this study spoke of not being able to mechanise their business any further and spoke of operating with the minimum of staff that they could. For example, it required a set number of people to clean a building, or pack, or to serve staff in restaurants or bars, and these positions could not be replaced with machinery or different working practices.

A number of firms reported that their turnover had not increased in the past two to three years and that the increases in the national minimum wage, were affecting their costs and therefore profitability.

Twenty employers spoke of the direct impact the NMW has had on their organisation's profits. These firms tended to be larger employers – typically employing 40 or more staff.

“The fact of the matter is, if you are a small business – and particularly a small business with high costs as we are in this industry – the impact of the NMW has a real impact on your own personal income...All we can do is budget to make less profit as there are no other savings that we can make.” Hotel in the East of England employing 100 staff.

“Believe it or not my profits in the last six years have actually decreased... The turnover is going up, but the actual differential between what it is costing us and what we are taking in is actually [less]. I mean, you think every year [that profit] would go up but it doesn't...just because the prices go up it doesn't mean you make more profit....because you have got more [overheads].” Scottish bar/restaurant employing 12 staff.

A food processing company in London that sells to the major UK supermarkets and chains has made losses in the past two years. The company, which employs 90 staff, blamed recent ‘significant’ increases in its wage bill and increases in other input costs.

"All we can do is budget to make less profit, as there are no other savings that we can make...I'd like to upgrade all my bedrooms but my ability to upgrade all of my bedrooms is hampered because every month I'm forking out vast amounts of costs that is imposed on us." Hotel in the East of England employing 100 staff.

However, firms' expectations of profitability and turnover over the next 12 months were largely positive, despite the new October 2004 NMW rate of £4.85 per hour. The table below details the results of a supplementary questionnaire.

Expectations of current year turnover and profit, compared with the previous year, for selected organisations

Sector	Turnover			Profits		
	Decrease	Remain the same	Increase	Decrease	Remain the same	Increase
Cafés and catering	1	4	1	2	2	2
Cleaning/facilities management	0	4	1	0	3	1
Food distribution and food processing	0	1	3	1	0	3
Hairdressing	0	2	4	0	5	1
Hotel	2	1	2	4	0	1
Packing	0	0	1	1	0	1
Security	2	1	2	2	0	3
Travel	0	2	2	0	1	3
Total	5	15	16	10	11	15

Reducing employment levels

Ten organisations had reduced staffing levels as a result of the NMW and other changes to employment law. Where employers were operating with fewer staff, this typically occurred where staff who left the employer were not replaced.

The extent to which increases in wages and other business costs impact on employment levels in UK businesses is difficult to assess. The UK economy and labour market has continued to grow throughout the recent slowdown the attacks on the United States on

11 September 2001 and the end of the 'dotcom' boom. In previous economic cycles in the 1980s and 1990s, the UK economy had the tendency to cut jobs in response to falling economic growth rates. However, despite the recent economic slowdown, the UK has continued to employ more people – with a record number of people in employment in the UK in 2004.

"When somebody leaves, you try to share their hours around, even if it is just for the short-term, to avoid taking someone else on." Cleaning company in the North West.

A company in the North East employing five staff reported that the industry rate for 'a person hour' in the sector had not changed in the past three years. However, in the same period, the employer had to raise the wages of his staff as a result of the NMW. As a result, this employer has cut the number of staff he employed from in excess of 100 to five. This employer now subcontracts work to other suppliers in order to remain profitable.

A travel agency employing 16 staff across two sites in Northern Ireland reported that the business had experienced quiet periods earlier in the year. The company was unwilling to shed staff during those times, as the larger travel agents tended to do.

"You can't lay people off any more. It doesn't happen any more. If you do, the customer suffers. The last thing you do these days is lay people off in this industry [as] you invest a huge amount in them [in hygiene health and safety training]." Hotel in Wales employing 100 staff.

In an attempt to mitigate the impact of the NMW, a café owner in the East Midlands employing 65 staff reluctantly stated that he would "...consider reducing my work force and investing in equipment because I don't want to employ people."

Employment of young people and inexperienced staff

Employers were using young people in a range of different ways – either as trainees, as full members of staff, or to cover busy periods at the weekends.

There was evidence that the NMW is affecting the employment of young staff and trainees in a number of different ways. In some sectors, such as hotels, bars and cafes, employers were tending to use younger workers in entry-level positions – such as domestic help, bar work, waiting and other work. These young people did not tend to be a part of a recognised industry or professional training programme. Rather, they were filling in during busy or peak times – such as at weekends, during holidays and so on.

In addition, some respondents spoke of only receiving applications from younger members of staff for their positions. In one hotel in the East Midlands, the respondent mentioned that while the company used younger workers, it did not take apprentices training to work in that sector. Instead, they were using students from local FE or HE institutions that were working to supplement their incomes while studying.

In addition, employers considered it was unfair that different trainees could be paid different rates of pay depending on their age, rather than on their skills, experience or ability to contribute to the business's earnings.

“I feel...the NMW has meant that we are less inclined to take starters on because we have to pay them too much. We would probably look at more qualified people who...we would [have to] pay more. So if you like, it's a deterrent to take younger people and train them.” Travel company in the East of England employing 42 staff.

A travel agent in Northern Ireland employing 16 staff asserted that a great deal of training (two- to three-years) was required before an employee could do the job of selling holidays properly. However, the NMW means that they can't be paid a far lower rate until they become productive. The owner had recently declined to employ someone who was inexperienced on the basis that she wasn't worth the minimum wage. In another instance, an undergraduate studying travel and tourism had recently approached the owner looking for a year's work experience. The owner stated that they also were not worth the minimum wage and would be a liability due to the likelihood of making mistakes. The owner had considered recruiting someone young (around 16 years of age) so that they could get experience while not demanding significant wages.

"We encourage the employment of more mature people if we can get them...We don't look to hire young people. In fact, quite the reverse given the opportunity." Hotel in the East of England employing 100 staff.

In one sector in particular, hairdressing, respondents were either reluctant to hire young staff or trainees overall, or had cut down on the numbers of trainees they had taken on in recent years. Some employers said that they were tending to focus on 16-year-olds so that they can get them through training and use pay rates outside the NMW. Employers spoke of the two- to three-year training programme for hairdressers and that this was impacting on trainees' ability to contribute to the profits of the organisation. Even after qualification, the vast majority of newly qualified trainees were still unlikely to be able to be fully productive and contribute to the profits of the organisation.

Employers noted that 16- to 17-year-old trainee hairdressers were unlikely to be able to make any financial contribution to the salon during their training period and that salons were often 'losing money' on these young staff. Furthermore, employers highlighted that an 18-year-old or a 21-year-old starting as a trainee was unlikely to be more productive as a result of their age than a 16- or 17-year-old. However, employers were obliged to pay these trainees considerably more than they would 16- or 17-year-olds. As a result, employers in the sector were unlikely to hire trainees over the age of 16 or 17.

" I have no problem with the NMW. What is difficult is when we get girls who are older coming into hairdressing. We can get 16-year-old girls for £60 per week, but maybe we'd prefer the 22-year-old. But they [older trainees] are being alienated because of the minimum wage: they are desperate to get into the salon but if we can get one [a trainee] for £60, what's the point in paying £140 [per week]?" Hairdresser in the East of England employing 14 staff.

"I wouldn't pay a 16-year-old £120 per week straight from school - no way." Hairdresser in the East Midlands employing 13 staff.

"We don't employ so many trainees [now]. It is as simple as that...[We have had older people aged over 18 wanting to train, but] it's not cost effective to take them on." Hairdresser in the South East employing 38 staff.

However, firms' recent levels of employment over the past three years showed that a high proportion of employers had increased their staffing levels. The table below details the results of a supplementary questionnaire on staffing.

Sector	Number of employees		
	3 years ago	1 year ago	Now
Café	16	10	10
Café	17	17	17
Café	62	63	64
Café	-	-	10
Café	15	15	12
Catering	40	40	65
Catering	23	21	20
Cleaning/facilities management	-	40	40
Cleaning/facilities management	25	60	75
Cleaning/facilities management	60	60	46
Cleaning/facilities management	40	53	53
Cleaning/facilities management	-	-	14
Cleaning/facilities management	205	123	123
Cleaning/facilities management	43	33	31
Construction	40	45	48
Food distribution	36	38	42
Food distribution	42		17
Food processing	30	30	35
Food processing	42	32	38
Hairdressing	31	40	38
Hairdressing	10	8	9
Hairdressing	18	26	32
Hairdressing	10	20	17
Hairdressing	-	-	13
Hairdressing	4	5	5
Hotel	-	10	12
Hotel	20	20	23
Hotel	-	-	100
Hotel	48	45	45
Hotel	55	55	55
Hotel	60	-	80
Hotel	-	80	100
Packing	80	100	110
Packing	-	10	16
Security	20	40	52
Security	65	85	105
Security	24	21	19
Security	-	220	170
Security	22	12	3
Office based	50	99	106
Office based	220	220	220
Office based	53	51	42
Office based	-	-	16
Office based	30	21	25

6. CONCLUSIONS

The sampling strategy adopted for this research saw the fieldwork concentrate on region, sector and organisation size. While there was some evidence that sectoral factors affected employers' views and coping strategies when dealing with the NMW in the hairdressing sector (by reducing the amount and age of trainees it was employing), there were no other common sectoral coping strategies used by the employers in this study.

Organisation variables, such as ownership structure or size did not impact on employers' coping strategies or their ability to deal with the NMW or increases to its rates in this study. In addition, regional factors had little impact on employers' coping strategies. While there were no discernable differences in coping strategies between firms across different regions, employers in each region tended to talk about sub-regional factors, particularly the extent to which firms in urban and/or metropolitan areas were better placed to deal with the NMW. In these cases, employers felt that businesses in metropolitan and urban areas were better able to deal with the NMW and upratings to the rates as their price and wage levels were considerably higher than those in more rural areas.

The majority of firms in this study that were encountering difficulties with the NMW and had made changes to how their business operated revealed that they could not adequately function with fewer staff or introduce any mechanisation that could further improve productivity in their business. For example, in food packing, food processing, cleaning, hospitality and security, the work being undertaken by these firms could only be done using labour and could not be replaced by machinery. Therefore, the coping options available to these firms when dealing with the NMW were to increase prices to recoup some of the costs of the NMW or to accept reductions in their organisation's levels of profitability.

It is noticeable that the hairdressing sector is reacting to the NMW by reducing the number of trainees it is prepared to hire, as well as limiting these training opportunities typically to 16- and 17-year-olds. The sector continues to train staff over a two- to three-year period and the NMW is clearly affecting these businesses. IRS Research reported back these findings early in its fieldwork and the LPC then requested that the fieldworkers ask hairdressers if an 18-month

exemption from the NMW for younger people would help the sector. All the hairdressers that were asked this question answered in the affirmative, though some said that even a newly qualified trainee was not always able to contribute to the profitability of their salon

Knowledge of NMW rates and upratings

There was confusion among some respondents about the NMW's various rates and their application, as well as the new rates planned for October 2004. Furthermore, some employers were unsure where to turn to for good, relevant and specific advice.

The employers in this study are receiving information about NMW rates from a range of third parties – typically their accounts, banks, business associations and from industry and/or national press.

While employers can access information from the Department of Trade and Industry, Low Pay Commission and the Inland Revenue about NMW rates and where they can be applied, the organisations interviewed as part of this research were not proactively seeking out this information when it was released. Furthermore, it is likely that the organisations interviewed are unaware of which government department websites they can obtain information from and these websites are also quite difficult to navigate. While the Low Pay Commission's website is an exception to this (the front page of the website has a link to current NMW rates), none of the employers interviewed for this research mentioned using the LPC website as a source of information on the NMW.

It is likely that employers would benefit from official, written notification of changes to the NMW rates, as well as when the different rates could be used, as soon as decisions have been reached. Employers would expect to receive official written notification from the Inland Revenue, for example, if there were changes made to employee tax rates or national insurance contribution rates. Therefore, providing clear, concise information on any changes to the NMW from an official government source would allow employers to plan coping strategies to deal with any changes.

Staffing levels

Firms reported that there was little or no room to cut staffing levels further in order to cope with future increases to the rate. Although

employers could continue to increase prices and accept lower profit margins, firms did not say to what level the NMW would have to rise to seriously impact on their businesses. Therefore, the extent to which the firms in this study can cope with future upratings to the NMW was difficult to assess. Firms were generally reporting that their sector and geographic locations were performing well and that in a number of cases, employers were expecting profits and or turnover to either remain the same or increase over the next 12 months.

Future increases to the NMW

The employers interviewed for this study expected that the NMW will continue to increase year on year. While two employers believed that the NMW should continue to increase at the same rate as it did in 2003, these were very much in the minority.

Many employers reported that increases to the NMW should now level-off, and suggested that future increases to the rate should be linked to inflation. Given that a high proportion of employers were increasing their prices year on year to cover inflation, it is likely that future increases to the NMW at the same rate is less likely to harm these employers' profitability in the future.

The environment into which the NMW has been introduced is important. Since 1999, the UK economy has continued to perform well. Economic growth has ranged between 1.8 per cent and 3.9 per cent of GDP per year (1999 - 2003) despite the significant changes seen globally in that same time period. This performance is all the more impressive when measured against many of the UK's international competitors. Employment has also held up well in the UK. The unemployment rate now stands at 4.7 per cent - down from 6.1 per cent in 1999. This rate of unemployment is low by the standards of the preceding two decades.

This is perhaps particularly relevant to the low-paying sectors chosen for this study. It is likely that the majority of the firms interviewed for this research were, prior to the introduction of the NMW, operating low-cost low-wage business models (prior to the introduction of the NMW, only ten employers reported that they were paying above the NMW in 1999). While some commentators suggest it is important that the UK economy is based on high-wage high-skill jobs, and that the NMW could be increased in order to force low-skill low-pay organisations into higher-paid higher-skilled sectors out of businesses, the sudden removal of low-paying occupations and sectors could have

a dramatic effect on the low-skilled, deprived communities and ultimately the tax and benefits system.

APPENDIX 1 – FINDINGS FROM THE EMPLOYERS’ SURVEY

IRS requested a random sample of named managerial-level contacts in 4,000 UK organisations, based on the sampling criteria detailed previously from Yell.co.uk – the business-listing service formally called ‘Yellow Pages’ and now part of ‘Experian’.

Each of the 4,000 organisations received a letter explaining the purpose of the research project and a short self-completion screening questionnaire (see Appendix 3).

The screening questionnaire asked seven questions that enabled IRS to categorise each respondent into:

- Business sector;
- Company size (number of employees);
- Government office region the company was operating in; and
- Date the business was established.

Additionally, recipients were asked to indicate “Yes”, “No” or “Don’t know” to the following questions:

- Has the Minimum Wage led to a change in your rates of pay?
- Has the Minimum Wage affected your firm’s profits?
- Has the Minimum Wage caused a change in the number of people you employ?
- Has the Minimum Wage affected the amount of training you give employees?

Respondents were also given the opportunity to give their comments on their firm’s experience of the national minimum wage. Finally, they were asked whether they would be willing to be interviewed as part of this project.

Responses to the initial contact survey were then entered into SPSS and employee numbers, region and sector re-coded. This enabled IRS Research to obtain a summary of initial findings and to generate a shortlist of prospective organisations to interview for the main phase of the research.

The number of organisations responding in the affirmative (ie answering 'Yes' is presented in the tables below:

Table 1 – Responses by sector

Sector	Responses		Has the NMW affected your firm's:			
	(num'r)	(%)	Pay (%)	Profits (%)	Employ -m't (%)	Training (%)
Cafes, snack bar, tearoom	16	6.0	93.8	87.5	31.3	25.0
Caterers	14	5.3	57.1	64.3	14.3	0.0
Cleaning services/facilities maintenance	24	9.1	66.7	50.0	29.2	12.5
Construction	18	6.8	16.7	5.6	5.6	11.1
Hairdressers	36	13.6	83.3	77.8	75.0	33.3
Hotels	48	18.1	62.5	60.4	33.3	22.9
Packers/distributors	22	8.3	68.2	68.2	45.5	31.8
Security services	27	10.2	70.4	66.7	51.9	29.6
Shoe shops	9	3.4	55.6	55.6	33.3	44.4
Travel agents	15	5.7	20.0	20.0	26.7	26.7
Insurance/finance	21	7.9	14.3	9.5	14.3	4.8
Other	15	5.7	53.3	53.3	20.0	26.7
Total	265	100.0	58.5	54.3	35.8	22.6

Note: Totals vary between tables due to exclusion of unclassified organisations.

The insurance/finance and construction sectors included within this survey were excluded from the main research programme due to the very low levels of NMW impact reported. Additionally, shoe shops were discounted as almost all respondents were part of large high-street multiples. Travel agents were included within the sampling schedule owing to the specific comments indicating relevant NMW issues within the sector offered by respondents.

Table 2 – Responses by size of organisation

Number of Employees	Responses		Has the NMW affected your firm's:			
	(num'r)	(%)	Pay (%)	Profits (%)	Employ -m't (%)	Training (%)
Less than 10	37	14.3	62.2	62.2	48.6	27.0
10 – 19	54	20.8	63.0	63.0	48.1	33.3
20 – 49	82	31.7	47.6	46.3	24.4	17.1
50 – 74	42	16.2	61.9	54.8	38.1	21.4
75 – 100	20	7.7	70.0	60.0	35.0	20.0
More than 100	24	9.3	75.0	54.2	29.2	16.7
Total	259	100.0	59.5	55.2	36.3	22.8

Note: Totals vary between tables due to exclusion of unclassified organisations.

Table 3 – Responses by region

Sector	Responses		Has the NMW affected your firm's:			
	(num'r)	(%)	Pay (%)	Profits (%)	Employment (%)	Training (%)
South West	19	7.2	36.8	36.8	31.6	31.6
South East	39	14.7	51.3	46.2	33.3	17.9
London	34	12.8	35.3	38.2	26.5	14.7
East of England	17	6.4	52.9	58.8	41.2	17.6
East Midlands	30	11.3	60.0	53.3	20.0	16.7
West Midlands	20	7.5	65.0	65.0	60.0	35.0
Yorkshire & Humber	29	10.9	75.9	62.1	44.8	31.0
North West	28	10.6	71.4	57.1	35.7	25.0
North East	19	7.2	68.4	63.2	36.8	10.5
Scotland	16	6.0	68.8	62.5	31.3	6.3
Wales	4	1.5	100.0	100.0	50.0	75.0
Northern Ireland	10	3.8	60.0	70.0	50.0	50.0
Total	265	100.0	58.5	54.3	35.8	22.6

Note: Totals vary between tables due to exclusion of unclassified organisations.

When assessed overall, the results from the preliminary questionnaire related closely to those from the ONS estimates of low pay distribution from 2002. The survey results followed the general north-south distribution of wealth within the UK. Although figures are given for Wales, the small number of survey returns from the region should be treated with caution.

Although not included within the sampling criteria, companies were also asked when their business was established. The table below is presented for information purposes only, since the age of a company played no role in its inclusion or exclusion from the further stages of research.

Table 4 – Responses by date of establishment

Date of establishment	Responses		Has the NMW affected your firm's:			
	(num'r)	(%)	Pay (%)	Profits (%)	Employment (%)	Training (%)
Before 1950	17	6.9	47.1	47.1	29.4	17.6
1950 – 1959	8	3.2	62.5	37.5	12.5	12.5
1960 – 1969	24	9.7	50.0	41.7	37.5	37.5
1970 – 1979	33	13.3	45.5	45.5	36.4	12.1
1980 – 1989	54	21.8	55.6	44.4	33.3	16.7
1990 – 1999	86	34.7	65.1	64.0	41.9	27.9
After 2000	26	10.5	76.9	80.8	34.6	30.8
Total	248	100.0	58.9	54.8	36.3	23.4

Note: Totals vary between tables due to exclusion of unclassified organisations.

More than 45 per cent of organisations surveyed were established within the past 14 years. Interestingly, it was these younger companies that tended to report the NMW as having had an impact on their business. This result was particularly stark for those organisation established since 1999 – the year that the NMW was introduced.

The results of this exploratory questionnaire are not robust findings in themselves. Their main purpose was to provide the research team with a simple snapshot of the level, distribution and nature of NMW-related issues facing the sectors included within the original sampling schedule. Additionally, the returns received were fed back into the main research exercise and used, for the most part, as a basis for approaching companies for interviews.

Sector summary of questionnaire responses

As the above tables illustrate, the reported impact of the national minimum wage on pay levels, profits, employment and training varies across the main independent variables – organisation size, sector and region. Overall, just under three-fifths (58.5 per cent) of organisations reported that the NMW had affected their pay levels, with a slightly lower figure (54.3 per cent) reporting it had affected profits.

The results of the survey become even more pronounced when sectors not included within the final sampling schedule are excluded from the analysis (ie construction, insurance, shoe shops and others). More than two-thirds (68 per cent) of included respondents reported that the NMW had caused a change in their rates of pay; a similar proportion (64 per cent) reported that profits had been affected; and just over two-fifths (42.5 per cent) stated that the numbers of staff they employ had altered as a result of the NMW. Those respondents reporting that training provision had been affected by the NMW remained relatively unchanged at 25 per cent.

Overall, it was companies in non-consumer product markets (cleaning, security and packing) that reported the NMW as having the most impact. However, the hotel and hairdressing industries, in customer facing product markets, also reported significant changes as a result of the NMW. The office-based sectors covered by this short survey reported few NMW related problems except that of having to pay trainees more than they felt they were worth.

An overview of comments received is presented below.

Cafes, snack bars and tea rooms

Respondents in the sector appeared to be attempting to stay marginally ahead of the national minimum wage rate but cited declining margins, taxation factors and customer price increases as issues. This group was the most likely to indicate that rates of pay (94 per cent of respondents) and profits (87.5 per cent), but not training and employment levels, had been affected by the NMW.

Respondents within this sector mentioned a particularly broad variety of issues within their comments including: wage compression, reduced scope for rewarding employees, a reduction in hours and an unwillingness to employ younger staff.

Caterers

Respondents frequently stated that they pay more than the minimum wage. Several reported cases of cost increase being passed onto customers. Excluding the construction sector, this group is the least likely to report that the NMW had caused a change in company employment or training.

Respondents within this sector also mentioned a broad variety of issues within their comments. These included: staff above the NMW requesting corresponding increases and one company having to reconsider continuing to employ a member of staff with learning difficulties. Two companies also directly stated that customer prices would have to be increased to cover wage increases caused by the NMW. While 64 per cent of caterers reported the NMW as impacting their profits, and 57 per cent their wages, these figures were significantly lower than those for cafes, snack bars and tea rooms.

Cleaning services

Respondents within this sector generally commented that increased wages have forced companies to pass on price rises to customers (if possible) or have eroded their profit margins. Other respondents commented that clients were reducing the hours or staff they require.

Respondents more frequently made a link between rising wages caused by the NMW (almost 67 per cent of respondents reported that

wages had changed because of the NMW) and declining profit margins that in other sectors. However, many respondents reported that they paid above the minimum wage and so it had little impact on their business. This fact was reflected in that only 50 per cent of respondents reported profits having been impacted compared with almost 94 per cent of cafes, snack bars and tea rooms.

Construction

Few respondents. Generally, no reported problems with the NMW.

Hairdressers

A consistent theme of responses was the impracticality of offering apprenticeships to those aged 17 and over. This has reportedly led to a shedding of training positions and non-productive roles. There was evidence of coping strategies in the form of varying employment arrangements. For example, respondents reported changes in workplace roles and the use of self-employed contractors. A predominant theme was a reluctance to provide training, given the pressures of the NMW.

This group constituted the second largest group of respondents and indicated (very consistently) that they had been negatively affected by the NMW. A large proportion indicated that they had been affected by the NMW in all of the questions asked on the questionnaire: pay (83 per cent), profits (78 per cent) and training (33 per cent). Most significantly, 75 per cent of companies claimed that the number of people they employ had changed as a result of the NMW – the largest proportion in any sector.

Hotels

The single largest group of respondents. Overall responses to the questions suggest that the effects of the minimum wage are comparatively diverse. Comments offered included the difficulty in continuing to offer employment opportunities to those with learning disabilities; importance of regional variations; impact on costs of attempting to maintain differentials; and increased pressure where fewer employees are asked to do more. The proportions of respondents indicating that the NMW had impacted on their pay rates

and profits were nearly identical at 62.5 and 60.4 per cent respectively.

Packers

The comments on the NMW by respondents in the packing industry were almost entirely negative. Price sensitivity of the product market and reduced margins were mentioned as reasons why, for example, staff had had to be laid-off or recruitment of untrained people reduced. Additionally, several respondents mentioned foreign competition as a factor. Overall, 68 per cent of companies reported wages and profits being impacted by the NMW.

Security services

Over 70 per cent of respondents reported the NMW as impacting on wages and a similar proportion for profits (66.7 per cent). This was the only group of respondents to mention that the NMW may have caused a greater reliance on the 'black economy' with two respondents commenting to that effect.

Additionally, when faced with increased prices, customers were reported to have reduced their security requirements. A small number of comments received presented a different view – that, for example, the increased costs caused by the NMW had been accepted by clients – but these were a small minority.

Shoe shops

This sector appears to comprise a large number of retail multiples which were not included within the sampling framework owing to their overall organisational size. Approximately half of respondents reported the NMW as impacting their pay and profits. More significantly, respondents in this sector were most likely to report the NMW as having impacted training (44.4 per cent).

Travel agents

While only a minority of respondents reported the NMW as having impacted their pay or profits (20 per cent) a slightly higher number reported issues with employment and training (27 per cent). From the

comments received on the questionnaires, it would appear that a fair proportion of the respondents in this sector are now unwilling to take on trainees. It was reported that the NMW paid to a trainee was not justified relative to his or her 'usefulness'.

Insurance brokers

Respondents from this sector overwhelmingly reported paying above the NMW and that it had had no effect. Only 14 per cent reported the minimum wage as having an impact on wages and 9.5 per cent on profits. Where respondents did mention problems with the NMW, it was either a general objection to the policy, a fear that it was driving business to low wage economies overseas or (in one instance) its impact on recruiting trainees.

APPENDIX 2 – EMPLOYERS’ ASSOCIATIONS’ INTERVIEW PROFORMA

General information

- Brief explanation of the organisation
 - Size of membership
 - Regional/national
 - Role of the organisation
- How would you describe the structure of your industry?
 - Size of companies
 - Regional disposition
 - Ownership structure
 - Sex/ethnic makeup
- How is your industry performing in general?
- Any particular issues your members are facing at the moment?

Views and impact of the national minimum wage

- What is your organisation’s view of the NMW?
- Describe your members’ knowledge of the NMW and its requirements?
- Are there any particular issues that the introduction of the NMW raised for your members?
- Are there any particular issues that the recent increases to the NMW have raised for your members?
- Probe on the following
 - Staffing costs/differentials
 - Employment levels
 - Productivity
 - Prices
 - Profit margins
 - Employee hours
- Are the issues you cite specific to your industry?
- Are they compounded by particular factors?

Coping strategies

- How are your members dealing with the issues mentioned above?
- Has your organisation provided any specific help/guidance regarding the NMW?

-
- Take-up of this?
 - Success?
 - Any specific examples of members accommodating the NMW?
 - When did those changes occur?
 - What were the outcomes?
 - Could things have been done better/differently
 - What are your members' future expectations of the national minimum wage?
 - Do they have any plans to deal with this?
 - Does your organisation have any plans to assist them?

Closing

- What could have been done better (or worse) by:
 - Government
 - Pressure groups
 - By employer/trade organisations?
 - By individual businesses?
- Future expectations and issues for the sector

Any other issues/comments

APPENDIX 3 – SHORT POSTAL SURVEY OF EMPLOYERS

1 Do you expect your PROFIT to decrease, remain the same or increase THIS YEAR?

Yes No Don't know

2 Has the Minimum Wage led to a change in your rates of pay?

Yes No Don't know

3 Has the Minimum Wage affected your firm's profits?

Yes No Don't know

4 Has the Minimum Wage caused a change in the number of people you employ?

Yes No Don't know

5 Has the Minimum Wage affected the amount of training you give employees?

Yes No Don't know

Please use this space to record any other comments of your experience of the national minimum wage.

APPENDIX 4 – FACE-TO-FACE INTERVIEW PROFORMA

General information

- Brief explanation of the organisation
 - When established
 - Number of employees
 - Sex/age profile of employees
 - Main product markets
 - Customer base
 - Ownership of your organisation
 - Staff involvement
- How is your industry/local economy performing in general?
- Any particular issues your organisation/industry is facing at the moment?

Views and impact of the national minimum wage

- What is your view of the NMW?
- Probe on knowledge of different rates and forthcoming changes (18-21/development rate, 22+, and 16-17 from October 2004)
- (If pre-1997 organisation) Were there any particular issues that the introduction of the NMW raised for your organisation?
- Were there any particular issues that the up-ratings of the NMW raised for your organisation?
- Probe on the following
 - Staffing costs/differentials
 - Employment levels
 - Productivity
 - Prices
 - Profit margins
 - Employee hours
- Are the issues you cite specific to your industry/local economy?
- Are they compounded by particular factors?

Coping strategies

- How are you dealing with the issues mentioned above?
- Has your organisation taken any specific help/guidance regarding the NMW from employer organisations etc?
 - Take-up of this?
 - Success?
- Any specific examples of accommodating the NMW?
- When did those changes occur?
- What were the outcomes?
- Could things have been done better/differently
- What are your future expectations of the national minimum wage?
- Have any plans to deal with this?

Closing

- What could have been done better (or worse) by:
 - Government
 - Pressure groups
 - By employer/trade organisations?
 - By individual businesses?
- Future expectations and issues for the industry/local economy

Any other issues/comments

APPENDIX 5 – POST-INTERVIEW SURVEY

This is an optional questionnaire for you to fill in prior to your interview with one of our colleagues. We appreciate that some of the information requested is sensitive. HOWEVER, YOUR RESPONSES WILL BE TREATED CONFIDENTIALLY AND WILL NOT BE SHARED WITH ANY OTHER PERSON OR ORGANISATION.

The information collected from this questionnaire will be used during the analysis stage of the project and is designed to further assist us in exploring the impact of the minimum wage. It is also intended to reduce the length of the interviews in order to make the research as convenient as possible.

Should you have any questions, please contact Ed Cronin on 020 8662 2042 or ed.cronin@irsresearch.co.uk.

Thank you for your help.

Please check these details and make changes if necessary:

Name:

Company:

Postcode:

Business sector:

No of Employees:

1. What type of company is your organisation?

Partnership Sole trader Limited company

Other (please state): _____

2. Is this a family-owned business? ¹ Yes ² No

3. How many PERMANENT members of staff did you employ

3 years ago: ____ 12 months ago: ____ Employ now: ____

4. How many TEMPORARY members of staff did you employ

3 years ago: ____ 12 months ago: ____ Employ now: ____

5. How many of your employees are from the following ethnic backgrounds?

White: ____ Black: ____ Asian: ____ Other: ____

6. What basic hourly rate do you pay your staff? Please tell us the rates you pay different workers – ie full-time, part-time, permanent/temporary, fully- or partly-qualified, weekday/weekend, males/females etc

Type of worker _____ £ _____ per hour

Type of worker _____ £ _____ per hour

Type of worker _____ £ _____ per hour

7. Do you pay overtime to your staff? ¹ Yes ² No

Please detail the hourly rates below

Saturday _____ Sunday _____ Nights _____

Shifts _____ Call-out _____ Bank holiday _____

Other (please state): _____

Other (please state): _____

8. If you pay any bonuses to your staff, please detail how they are paid below. For example, Christmas bonus, bonuses paid on meeting sales/profit targets etc.

9. Thinking about the TOTAL COSTS your business faces THIS YEAR, approximately what percentage COSTS are made up from the following:

Business rates _____ %

Heating, lighting, telephone and water rates _____ %

Rent/mortgage _____ %

Wages _____ %

Other significant costs, please state:

_____ %

Other significant costs, please state:

_____ %

10. What was the approximate TURNOVER of your business 3 YEARS AGO?

Please write in here or tick one of the boxes below: £ _____

- Up to £49,999
- £100,000 to £199,999
- £500,000 to £999,999
- £50,000 to £99,999
- £200,000 to £499,999
- More than £1million

11. What was the approximate TURNOVER of your business LAST YEAR?

Please write in here or tick one of the boxes below: £ _____

- Up to £49,999
- £100,000 to £199,999
- £500,000 to £999,999
- £50,000 to £99,999
- £200,000 to £499,999
- More than £1million

12. Do you expect your TURNOVER to decrease, remain the same or increase THIS YEAR?

- Increase Remain the same Decrease
-

13. What was the approximate PROFIT LEVEL of your business 3 YEARS AGO?

Please write in here as a percentage of turnover _____ %
or as a total £ _____

14. What was the approximate PROFIT LEVEL of your business LAST YEAR?

Please write in here as a percentage of turnover _____ %
or as a total £ _____

15. Do you expect your PROFIT to decrease, remain the same or increase THIS YEAR?

- Increase Remain the same Decrease

APPENDIX 6 – INTERVIEWS CONDUCTED

Business Sector	Government Office Region	Employees	Date established
Café	North West	Less than 19	1990
Café	South West	Less than 19	1990
Café	South West	Less than 19	1985
Café	South East	Less than 19	1996
Café	South West	20 to 49	1987
Café	East Midlands	50 to 74	1937
Catering	Scotland	50 to 74	1994
Catering	London	More than 74	1974
Cleaning	North West	Less than 19	1975
Cleaning	Yorkshire and the Humber	20 to 49	1974
Cleaning	North West	20 to 49	1984
Cleaning	East of England	20 to 49	1994
Cleaning	North West	50 to 74	-
Cleaning	East Midlands	More than 74	1950
Cleaning	South West	More than 74	1988
Construction	South East	20 to 49	-
Food distribution	Northern Ireland	Less than 19	-
Food distribution	Scotland	20 to 49	-
Food processing	Wales	20 to 49	-
Food processing	West Midlands	20 to 49	-
Food processing	London	50 to 74	1985
Hairdressing	Yorkshire and the Humber	Less than 19	-
Hairdressing	South West	Less than 19	1966
Hairdressing	South East	Less than 19	1983
Hairdressing	East Midlands	Less than 19	2002
Hairdressing	East of England	Less than 19	1986
Hairdressing	London	Less than 19	2001
Hairdressing	London	20 to 49	1992
Hairdressing	South East	20 to 49	1992
Hotel	Scotland	Less than 19	-
Hotel	East Midlands	20 to 49	2002
Hotel	North West	20 to 49	-
Hotel	Wales	50 to 74	-
Hotel	North East	More than 74	1988
Hotel	East of England	More than 74	1997
Hotel	Northern Ireland	More than 74	-
Hotel	Wales	More than 74	1959
Hotel	East Midlands	Less than 19	1993
Packing	Yorkshire and the Humber	Less than 19	2000
Packing	Wales	Less than 19	-
Packing	Yorkshire and the Humber	20 to 49	1997
Packing	East Midlands	More than 74	2000
Packing	East of England	More than 74	1999
Security	North East	Less than 19	2001
Security	West Midlands	Less than 19	-
Security	West Midlands	50 to 74	1999
Security	East Midlands	More than 74	1974
Security	West Midlands	More than 74	-
Travel	Northern Ireland	Less than 19	1990
Travel	North East	20 to 49	-
Travel	East of England	20 to 49	1961
Travel	North East	More than 74	-
Recruitment, travel and training	Scotland	More than 74	-

Note: in some cases the date of establishment has been omitted to preserve respondents' anonymity.

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