

***Report to the
Low Pay Commission
on the impact of the
National Minimum Wage***

***A research report by
Incomes Data Services***

September 2004



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IDS Report to the Low Pay Commission on the impact of the National Minimum Wage in 2003 and 2004

Introduction

This report looks at the impact of the NMW increases in 2003 and 2004 in a number of low-paying sectors: private nurseries, hotels, leisure, pubs and restaurants and retail. It looks in particular at how employers responded to the 2003 NMW increase, its impact on differentials and grading structures, the changing use of age-related pay, and the impact of the forthcoming increase in the NMW to £4.85 from October 2004.

This reports follows on from IDS's Report to the Low Pay Commission in March 2004 and confirms many of our earlier findings. We have conducted a number of surveys of low-paying sectors specifically for this report, as well as expanding on our ongoing monitoring of pay developments to assess the impact of the NMW.

Summary of findings

1. The NMW is having an increasing impact on companies and pay rates, with more having to make moves to meet the 2003 NMW increase than previously.

Nearly two thirds (64 per cent) of nurseries in our 2004 survey needed to raise their pay rates in order to comply with the October 2003 increase in the NMW. This was significantly up on the 46 per cent of organisations who reported that they had been directly affected by the October 2001 increase in the NMW. In the bulk of these organisations it was reported that more than half of employees were directly affected by the increase.

The uplift in the NMW to £4.50 in October 2003 affected nearly half of respondents to the survey of hotels and hotel chains, compared to one third of hotels in our previous survey who needed to raise rates to meet the 2001 increase.

A higher proportion of firms in the leisure industry also told us that they had needed to increase some rates of pay in order to comply with the October 2003 NMW uplift to £4.50 an hour than for previous upratings.

2. Even more companies will have to make moves to meet the 2004 increase in the NMW than in 2003.

Some three-quarters of nurseries said that they would be affected by the next NMW rise in October 2004, a higher proportion than were directly affected by the October 2003 increase. Similarly, the 2004 increase will affect close to

three quarters of hotels, compared to half for the 2003 increase.

Many retailers still have minimum rates below £4.85 an hour following their 2004 pay review. This includes companies such as Waitrose that have hitherto not been affected directly by the NMW. The impact of the coming increase in the NMW is evident by the fact that a majority of the companies we contacted that have already carried out their 2004 pay review will need to hold a further review by 1 October 2004 to bring some of the pay rates into line with the new NMW.

3. The NMW is increasingly the key determinant of pay rates, with starting rates typically at £4.50, across low-paying sectors.

For example, the median starting rate for a nursery assistant is now £4.50, equivalent to the current adult NMW level. In the previous IDS survey of the nursery sector, in December 2001, the median starting rate for nursery assistants was £4.10 an hour – exactly equivalent to the then adult NMW.

Similarly, at over half of the hotels we surveyed, the lowest rate of pay for an adult permanent employee is £4.50 an hour.

Recent upratings have also established the NMW as the lowest rate within pay structures at an increasing number of companies in the leisure industry. This marks a distinct shift from a few years ago, when many firms preferred to keep their rates well ahead of the NMW zone wherever possible. At UCI cinemas, for example, only one

or two of the group's forty cinemas in the UK were affected when the minimum wage was first introduced. Following recent increases, this figure has risen to nearer 18 out of 40.

The NMW has also had an increasing effect on company pay structures in the pubs and restaurants sector, with almost three-quarters of companies setting their new starter rate at the level of the adult NMW.

4. Pay settlements in the economy generally are running behind NMW increases.

Pay settlements in the economy have been running at around 3 per cent since the beginning of 2003, some way behind increases in the NMW of 7.1 and 7.8 per cent in 2003 and 2004.

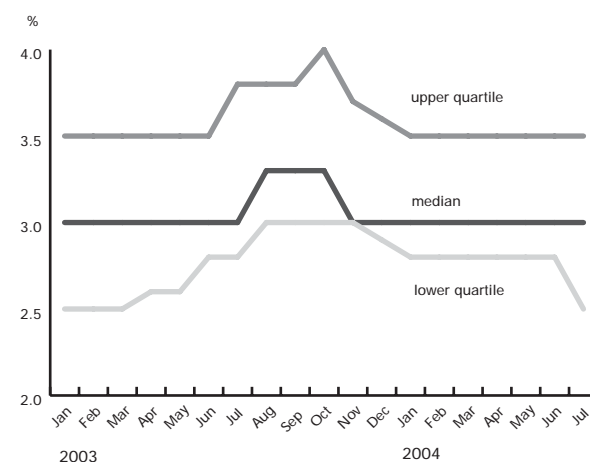
The coming increase will push the pay floor up to the level of, or overtake, the minimum pay rates at a number of retail companies who in previous pay reviews have awarded large increases to their bottom rates to take them beyond the national minimum. For example, Gap awarded an 8 per cent increase to its lowest rate at its 2003 pay review to take it up to £4.75 an hour. The 2.6 per cent increase the company awarded at its review in July 2004 set the minimum rate at £4.85 an hour, placing it back among the ranks of minimum wage paying companies. And in 2002, department store chain James Beattie awarded a 9.2 per cent increase to its minimum rate, setting it at £4.50 an hour, as it said it was getting too close to the NMW. The 2.5 per cent increase awarded at the company's review in April 2004 set a minimum rate of £4.74 an hour.

5. The NMW is the main determinant of pay increases for large groups of employees at the bottom end of pay structures.

The latest survey of nurseries found that median levels of starting pay for nursery assistants and nursery nurses were 10 to 11 per cent higher than those in the December 2001 survey, which equates closely to the percentage increase in the NMW over this period (9.8 per cent). The median pay increase at the last pay review among nurseries was 5 per cent. This is significantly higher than the level of pay increases across the rest of the economy (which is currently running at around 3 per cent). Around a third of the nurseries that gave information had paid an average pay rise of 7 per cent or higher.

There is some evidence that pay increases to meet the NMW in 2003 were widespread enough to affect pay increases in the economy generally. Coupled with the impact of civil service pay

Median pay settlement level whole economy, 2003 to 2004



reviews, the upper quartile of all pay settlements reached 4 per cent in October 2003, its highest for some time.

6. Companies remain divided over the need to increase pay rates further up pay structures to maintain differentials over the lowest paid. Some make moves to restore differentials, while others are prepared to live with narrower pay gaps between jobs.

Just under half (45 per cent) of nurseries had taken action to restore differentials for other grades following the October 2003 NMW increase. Nurseries typically said that this was to maintain differentials between qualified and unqualified staff. However, several nurseries commented that differentials between the lowest paid, unqualified staff and more senior or qualified staff had been narrowed.

One third of the hotels reported that they increased pay rates for more experienced or supervisory staff in order to maintain differentials after October 2003.

In the leisure sector, a number of companies made moves to restore pay differentials, such as UCI, Ladbrokes and Fitness Express. In the retail sector, it seems that some companies are prepared to live with narrower pay differentials, such as TK Maxx and B&Q, which increased its starter rate to £4.85 in February, reducing the differential between starter and established rates from 27p to 7p.

7. In some cases, narrowed pay differentials have led to major changes in pay structures, especially in companies making moves to meet the 2004 NMW.

Rosebys, for example, will replace its current three-stage pay structure (starter, intermediate and final) with a move to a single spot rate for

sales staff when the NMW increases to £4.85 an hour. Argos ended the payment of induction rates as part of its pay review in April 2004. These had been fixed at 95 per cent of the established rate of £4.71 and applied generally for the first eight weeks of employment. Both new starters and established staff are paid £4.84 an hour.

The Co-op will merge its grades A to D, which include all sub-supervisory roles in the shops (such as shelf fillers, checkout assistants and senior assistants), to form a single multi-skilled position of customer service assistant at £5.00 an hour from 1 October 2004. Rates currently range from £4.53 to £4.85 an hour.

Halfords has moved in the other direction. It re-introduced a starter rate of pay for under-18s of £4.20 this year, having previously ended the payment of junior rates in 1997. The company said that introducing the lower rate would release more funding which could be put into bonuses for sales staff.

The 2003 increase in the NMW also closed pay differentials in companies with location-based pay systems, such as KFC. Prior to its pay review in February 2004, KFC operated a pay structure in which pay rates were separated into three locational groups. The company said that the increase in the NMW to £4.50 an hour had wiped out the differentials between these groups in most levels in the performance-related pay scales and it therefore decided to merge the three pay bands into one.

8. Among companies making moves to meet the 2004 NMW, many have decided to increase their lowest rate straight to £5 an hour.

This is particularly the case in the retail sector. For example, Booker Cash & Carry will increase its two lowest rates of pay of £4.65 and £4.93 an hour (for cash & carry assistants) straight to £5.00 an hour from 1 October 2004. Similarly, Iceland will increase its lowest rate from £4.65 to £5.00 an hour from October. The company said it had decided to raise the minimum to £5.00 as it wanted to be above the level of the NMW. Tesco and Taskers DIY have also moved to minimum rates of £5.00 an hour this year.

9. Some companies are operating explicit policies to keep their lowest pay rates above the NMW.

As well as those retail companies moving to a rate of £5.00, a number of leisure companies told us that their strategy was to remain above NMW level. One example is David Lloyd Leisure, where the lowest salary paid – for a hospitality team

member – is £10,271 a year, the equivalent of about £5 an hour. Another is the William Hill organisation, where the company policy is ‘to stay well ahead of NMW rates’. In the March 2004 pay review, one key pay level was increased to bring it 20 pence ahead of the new NMW, and rates higher up the pay structure were raised to maintain differentials.

At JD Wetherspoon, the company policy is to retain a differential of 10 pence an hour above the NMW – currently the lowest starting rate for a company ‘associate’ is £4.60 an hour, although a youth rate of £3.85 an hour is also in operation. At Castle Leisure, the bingo hall operator, the policy is to maintain a 25 to 30 pence differential above the NMW – currently the lowest starting rate is £4.75 an hour for an ‘operative’, rising to £5.25 an hour for an advanced operative after six months.

In the finance sector there have been some significant increases to lowest rates. HSBC amalgamated its two lowest clerical grades increasing the minimum rate for clerks in the middle regional pay band by 22 per cent from £10,000 to £12,250. Barclays raised its minimum cashier rate by 15 per cent from £9,100 to £10,500 this year.

10. There is evidence that the NMW has led to an increasing number of employers using age-related pay.

The use of differing pay rates explicitly linked to the age of the employee is fairly widespread in the nursery sector, and its use appears to be increasing. In our previous survey of pay in the independent nursery sector in 2001, we found that about a third of nurseries operated some form of differentiation in rates of pay based on age. In our latest survey, just under half the respondents did so.

Most of the organisations that used differing rates linked to age said that they had changed their practices on age-related pay specifically as a result of the NMW legislation. One nursery with just under a quarter of its staff aged under 22 commented that ‘younger staff were previously given more than the NMW, but now they just get the [youth] NMW’. Another commented that ‘higher wage costs means that age-related pay is now essential’.

One of the leading cinema chains told us that the latest increases to the minimum wage were beginning to test the company’s commitment to retaining the same rates of pay for all employees,

regardless of age, and that this policy might be about to reach 'creaking point' when the adult NMW rate moves to £4.85 an hour.

An increasing number of pub and restaurant chains are taking advantage of the lower NMW rates for under-22 year-olds. Five of the 16 companies we contacted now pay adult rates from age 22, although in some of the businesses this policy is relaxed in harder-to-recruit locations. At many of these companies age differentiation did not exist in the pay structure prior to the introduction of a statutory minimum pay rate. Counterbalancing the pressure to keep wage costs down through the use of age-related pay is a concern to ensure that staff recruitment is not put in jeopardy. Over half of the 16 companies we contacted said that they paid adult rates from age 18 and three paid them regardless of age.

In the retail sector, companies are moving in different directions. The trend for companies to lower the age at which the full adult rates are paid has continued in some quarters. For example, William Morrison ended the payment of age-related rates for students from August 2004, paying its lowest adult rate from age 18. And Kwik Save is phasing out its junior rates as stores convert to a new format.

However, some companies that had ended the use of age-related pay have subsequently reversed that policy. In September 2003 WH Smith decided to freeze its starter rate for under 18 year-olds at £4.20 an hour as it said this was already higher than many of its competitors. At its previous review it had increased the under 18 year-old trainee rate by 19.3 per cent to bring it up to 96 per cent of the adult rate in line with its policy of phasing out junior rates of pay. And Halfords has re-introduced a new starter rate for under 18s.

Home furnishings retailer Dunelm said that it had been considering closing the gap between its junior and adult pay rates or even ending age-related pay, but the introduction of the NMW and its subsequent increases had caused a re-think due to costs. And the Early Learning Centre, which has a policy of paying adult rates from age 19, told us that from 1 October 2004 the new statutory minimum of £4.85 an hour will apply only to its employees aged 22 and over, thereby introducing greater age differentiation into its pay structure.

11. There is a trend for employers to move their pay review dates to October to coincide with NMW increases

Over four-fifths of the pub and restaurant companies we spoke to now hold their pay reviews

in or close to October. A minority still hold their main review earlier in the year and have an additional review close to October to decide how to respond to the uplift in the NMW. A two-stage pay increase under the Agricultural Wages Board also brought the review of pay rates into alignment with the increase in the NMW in October each year.

In the retail sector, Iceland, Somerfield and the Retail Co-op Societies are among the latest retailers to move their review dates to October. In 1999 we recorded 38 retail pay settlements in April – the key month for pay reviews in the sector – and just three in October. By contrast, in 2003 we monitored 22 pay increases in April and 14 in October.

12. The NMW increases have had a limited impact on the employment mix or on employment levels in companies.

Eleven of the 100 nurseries in our survey said that the NMW had impacted on skill mix within their organisation, saying that they were now employing more unqualified staff, and in one case younger staff. By contrast, at Urbium, which operates city bars, some increases to bar staff pay had been required in order to restore differentials and the company now tended to 'look for more experienced people, at a higher level', presumably to justify these higher rates of pay.

Nine nurseries said that the NMW had impacted negatively on staffing levels. However few of these gave any detail. One nursery said that they could not afford to replace an employee that left, and another that they had reduced the number of nursery assistant posts. However a number of nurseries pointed out that they had no flexibility over staffing levels because they were already operating at the minimum legally required ratios for the numbers of staff to children.

13. There were few reported problems with compliance with NMW rates.

This suggests that employers find the NMW straightforward to understand and comply with. Interestingly, there was no reported use of the adult development rate (set at the level of the youth NMW) which suggests that either employers do not understand the criteria for this, or are unable to meet it.

There was only was possible area where employers may not have been complying with the NMW, and this was in the use of the accommodation offset. It may be the case that some hotels are paying a basic wage above the NMW, but then offsetting accommodation charges which take the pay rate below that allowed under NMW legislation (see page 18).